



Asian Development Bank

Promoting Regional Cooperation in the
Development of Insolvency Reform

RETA 5975

Draft Country Report for Singapore Conference
Cross-Border Insolvency – Indonesia, Korea,
Philippines and Thailand

Indonesia

A. The provisions

The provisions of the existing insolvency laws of the participating countries as well as any proposed reforms

Question: Please advise as to the extent to which the materials in Section I, J, K, L, O, P and Q of the Report and Sections B, G, H, J and L of the Addendum to that Report continue to be accurate. If those sections of the Report and the Addendum to that Report require amendment or modification, please advise of the amendments or modifications.

Report on Indonesia – produced under Asian Development Bank Technical Assistance No. 5795-REG

Answer: See below.



Section I – Insolvency Law Regime

1. Underlying Philosophy:

- (a) **Question:** *What is the underlying philosophy of the insolvency law of this country? (For example is it distributive, rehabilitative or penal?)*

Answer: The underlying philosophies of the insolvency law are judicial, distributive and rehabilitative. The Indonesian bankruptcy law allows the concept of corporate reorganisation with the approval of a required number of unsecured creditors, failing which the company will be liquidated and its assets will be distributed to the creditors.

- (b) **Question:** *Are there elements of more than one philosophy present in the insolvency law of this country?*

Answer: In addition to the underlying philosophies of Indonesian Bankruptcy Law, there are at least two other elements that can be mentioned: (i) elements relating to the credit presupposes trust; and (ii) elements relating to the purposes of the Bankruptcy Law.

- (c) **Question:** *Briefly describe the relevant elements, and if applicable, any penal sanctions available.*

Answer: Regarding the Credit Presupposes Trust:

This element relates to the issue on how the creditors can trust that the debtor will service his debts on time. In the situation where a debtor is not able to meet his obligations, it is imperative that a well functioning bankruptcy regime is in place.

Regarding the Purposes of Bankruptcy Law, which are as follows:

- (i) *Maximise asset recovery*
This means that all assets of the debtor should belong to the pool that is available to pay creditors' claims.
- (ii) *Provide for equitable and predictable treatment of creditors*
This purpose states that creditors are paid pari passu – creditors will receive pro rata part distribution from the pool according to the size of their claims.
- (iii) *Provide practical opportunities for re-organisation*
This means that Bankruptcy Law provides practical opportunities for ailing but viable businesses where the interests of creditors and social needs are better served by maintaining the debtor in business.

2. Jurisdiction in Insolvency Matters:

- (a) **Question:** *In which judicial category is insolvency law classified in the legal system of Indonesia? (For example civil, commercial or administrative.)*

Answer: As stated in the Article 280, paragraph 1 of the Law No.4/1998: "the petition for adjudication of Bankruptcy and suspension of obligations for payment of debt as intended in the 1st and 2nd Chapter, shall be heard and decided by the Commercial Courts within the frame work of the Courts of General Jurisdiction." Insolvency law is classified as part of the Indonesian Commercial Law.

- (b) **Question:** *Which courts, tribunals or administrative bodies in this country are competent to exercise jurisdiction in insolvency matters?*

Answer: The insolvency cases shall be submitted and decided only by the Commercial Court, a part of the civil court jurisdiction.

- (c) **Question:** *Are any limitations placed on the jurisdiction of any of these bodies?*

Answer: The first Commercial Court was established at the Central Jakarta District Court to deal with the bankruptcy matters, as stated in Article 281, paragraph 1 of the Law No.4/1998. Prior to the establishment of other Commercial Courts in cities outside Jakarta, the Jakarta Commercial Court's jurisdiction covered all of the Indonesian territory.

However, since the establishment of other Commercial Courts in a number of cities outside of Jakarta, which are (i) Surabaya; (ii) Medan; (iii) Ujung Pandang; and (iv) Semarang: Presidential Decree of Republic of Indonesia No.97 of 1999 dated 18 August 1999 concerning the Establishment of the Commercial Court, Article 2 paragraph 1 of Law No.4/1998, the competent court for certain particular cases is the Commercial Court having jurisdiction over the debtors' domicile.

3. Types of Insolvency Procedures

- (a) **Question:** *What types of insolvency procedure are available in the legal system of this country for the administration of corporate debtors in financial difficulty? (For example bankruptcy, liquidation (winding up), receivership, restructuring or other forms of administration.)*

Answer: Indonesian Bankruptcy Law provides for 2 types of law procedures for insolvency cases: (i) bankruptcy petition (liquidation procedure); and (ii) suspension of payment procedures (re-organisation procedure).

The bankruptcy petition may be filed by the: (i) debtor; (ii) creditor(s); and/or (iii) public prosecutor representing the public interest. On the other hand, suspension of payment procedures can only be submitted by the debtor.

A petition for bankruptcy procedure can only be filed by Bank Indonesia. For the security company debtor, a petition for a declaration of bankruptcy may only be filed by the Capital Market Supervisory Agency (“Badan Pengawas Pasar Modal” – “Bapepam”).

Under the proposed Amendments to the Bankruptcy Law, special provisions are to be incorporated which include Self Regulated Organisations (“SRO”) (such as the Jakarta Stock Exchange, Surabaya Stock Exchange and Clearing and Depository Company), and issuer companies and insurance companies in the list of companies with special regulations. It is stated that a declaration of bankruptcy for a SRO Company and an issuer company can be filed by Bapepam, while a declaration of bankruptcy for an insurance company can be filed only by the Minister of Finance.

(b) Question: Briefly describe the main features of each type of insolvency procedure for corporate debtors: including, for example, the manner in which each procedure is initiated and administered, and the aims of each procedure.

Answer: Pursuant to Article 1 of the Law No.4/1998, a debtor with two or more creditors, who does not pay at least one of the loans which are due and payable, may be deemed bankrupt at the petition of the debtor, by one or more of the creditors, or in certain circumstances, by the public prosecutor.

By its nature, a bankruptcy petition is a collective procedure. As such, it is a procedure that has to endeavour to accommodate all those who are affected by, or who have an interest in the insolvent debtor. From the creditors’ side, the bankruptcy procedure can be used as an alternative, in addition to the court filing procedure, to obtain payment from the debtor. From the debtor’s side, the bankruptcy procedure is an alternative way to settle the payment obligations of the debtor to the creditors.

Suspension of payment proceedings can only be commenced and filed by a debtor. The said proceedings may be taken as counter action to certain bankruptcy petitions filed by the creditor(s), or to voluntary action by the debtor with the main goal being to provide for the continuation, not the liquidation, of an insolvent debtor.

Suspension of payment proceedings will facilitate and encourage debtors to address their financial difficulties at an early stage, and to propose a composition plan or re-organisation plan to the creditors, including an offer of payment for all or part of the debts to the unsecured creditors.

A debtor who cannot predict that he will be unable to continue to pay his debts, which are due and payable, may apply for a suspension of obligation to pay such debts: Articles 212 up to 248 of the Law No.4/1998.

(c) Question: Identify the relevant legislation governing each type of insolvency procedure available for corporate debtors.

Answer: The relevant legislation governing each type of insolvency procedure for corporate debtor(s) is as follows:

- (i) Law No.4/1998;
- (ii) Law No.1/1995, concerning the Limited Liability Company (“Law No.1/1995”);
- (iii) the Faillissements-Verordening or the Bankruptcy as set forth in the Statsblad of 1905 No.217 Jo Statsblad of 1906 No.348;
- (iv) Law No.8/1995, if dealing with a public company (“Law No.8/1995”);
- (v) Law No.10/1998 jo. Law No.7/1992, if the insolvency proceedings involve the banking sectors; and
- (vi) Law No.14/1969, regarding the Basic Provisions Respecting Man Power jo. Decree of Minister of Manpower No.:KEP-150/MEN/2000, regarding the Settlement of Labor Dismissal and Termination, and the Stipulation of Severance Pay, Gratuity and Compensations in Companies.

4. Commencement of Insolvency Procedures

(a) Question: Is it usual or customary in respect of a corporate debtor which is insolvent to attempt to negotiate an informal administration before formal insolvency procedures are commenced?

Answer: As stated in the Article 1, paragraph 1 of the Law No.4/1998, where a debtor has two or more creditors, and at least one of the said debts has become due and payable, then the debtor may be declared bankrupt by the Commercial Court as a result of a bankruptcy petition filled by the debtor itself, or by its creditors. However, in practice an amicable settlement or an out of court

settlement will be initiated prior to the filing of the bankruptcy petition.

(b) Question: *In relation to each type of insolvency procedure available in the legal system of Indonesia, who may commence the procedure? (For example the corporate debtor, secured creditors, unsecured creditors, directors, shareholders, the State.)*

Answer: A company can be declared bankrupt at the request of the: (i) debtor, (ii) one or more creditors; (iii) public prosecutor representing the public interest: Article 1, paragraph 1 of the Law No.4/1998.

A petition for a declaration of bankruptcy with respect to a bank debtor, may only be submitted by Bank Indonesia, and for the securities company, it may only be submitted by Bapepam: Article 1, paragraph 2, 3 of the Law No.4/1998. The draft Amendment to Law No.4/1998 proposed new provisions which were concerned with those companies engaging businesses in the capital market industry and in the insurance business.

To be more specific, SRO and issuers may be filed bankrupt only by Bapepam, and an insurance company may be declared as bankrupt only at the request of the Minister of Finance.

(c) Question: *On what basis may each type of insolvency procedure be commenced, or what requirements must be satisfied before the procedure may be commenced? (For example non-payment of debts, balance sheet/cash flow insolvency, trading losses, resolutions by directors to enter insolvency procedure.)*

Answer: It will be necessary to confirm whether or not there is only one type of insolvency procedure in Indonesia which applies to both individual debtors and corporate debtors. The only required conditions for filing a bankruptcy petition are: (i) the debtor has two creditors or more; (ii) the debts have become mature debts, and as such have become due and payable; and (iii) the debtor failed to pay at least one mature debt.

The insolvency proceedings are therefore commenced due to non-payment of debt.

(d) Question: *How is each type of insolvency procedure commenced? (For example by application to the Court, by administrative act, by written notice to the business organisation.)*

Answer: A petition for bankruptcy shall be filed at the competent Commercial Court i.e. the Commercial Court at the debtor's domicile: Article

2 paragraph 1 of the Law No.4/1998. Indonesia has five commercial courts, namely, Jakarta Commercial Court, Semarang Commercial Court, Surabaya Commercial Court, Medan Commercial Court and Ujung Pandang Commercial Court.

(e) Question: *What is the usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor?*

Answer: The decision on a petition for a declaration of bankruptcy must, at the latest, be rendered in 30 days, starting from the date the petition for a declaration of bankruptcy is registered: Article 6, paragraph 4 of the Law No.4/1998. It is arguable whether such 30 days shall be counted based on calendar days or working days. The calculation will be important given that counting on the basis working days may result in a different number of days when you consider the nature of business activities (e.g. telecommunication, hospital, tourism, banking or capital market), and cities where business activities take place (e.g. Jakarta, Aceh, Jayapura, or Ambon).

(f) Question: *How effective is the judicial or court system (or administrative system) in relation to the handling of formal insolvency proceedings?*

Answer: The Commercial Court was initially established in Jakarta on 21 August 1998. Subsequently, in 1999 four other Commercial Courts were established in Semarang, Surabaya, Medan and Ujung Pandang.

Although there is some argument that it is still too early to say whether such Commercial Courts are effective in their performance, most are of the view that the performance of the said Commercial Courts is still far from effective.

5. Effect of Insolvency Procedure:

(a) Question: *In relation to each type of insolvency procedure available in the legal system of Indonesia, what is the effect on the corporate debtor, its constituent parts and its business relationships of initiation of the relevant insolvency procedure?*

(For example how does initiation of the insolvency procedure affect:

- *the powers of management of the debtor;*
- *the interests of owners/shareholders of the debtor;*
- *contracts to which the debtor is a party;*

- *legal proceedings to which the debtor is a party;*
- *remedies available to persons in contractual (non-debt) relationships with the debtor.*

Answer: No answer provided

(b) Question: *If another insolvency procedure has already been initiated in relation to the corporate debtor, how does the initiation of a second procedure affect the first?*

Answer: Under Indonesian Bankruptcy Law, there is only one set of proceedings, namely bankruptcy proceedings. This may be implemented in two alternative proceedings, i.e., a suspension of payment proceedings (in effect a re-organisation), or the bankruptcy proceeding of the debtor's estate.

It should be noted that a bankruptcy declaration to a debtor does not mean that the debtor is insolvent.

Once the debtor is declared bankrupt, the debtor may propose a reconciliation plan ("rencana perdamaian"). If this plan is accepted by the creditors, then insolvency does not occur. On the other hand, if no reconciliation plan is being offered at the creditors' meeting on the verification of claims, or if the offered reconciliation plan is rejected, or if the ratification of the reconciliation plan is rejected by the Supervisory Judge, or by the Supreme Court: Article 117 of the proposed Amendment to Company Law, Law No.1/1995, then the bankrupt estate of the debtor is deemed insolvent. Under Indonesian laws and regulations, bankruptcy declaration comes first, and it may then be followed by possible insolvency.

The following are the effects of bankruptcy proceedings on the corporate debtor, its constituent parts and its business relationships:

- (i) After the application for bankruptcy is made but before the bankruptcy declaration is issued, any creditor or the Attorney General may request the court to seize all or part of the debtor's assets or to appoint a temporary Receiver to supervise the management of the debtor's businesses, payments to creditors, transfers or encumbrances of the debtor's assets. The Receiver's approval is required for the above acts.
- (ii) The following are some of the specific effects on the debtor after the Bankruptcy Declaration is issued:

- (a) forfeiture of the debtor's right to manage its assets;
- (b) all assets of the debtor are subject to the jurisdiction of the Commercial Court and to bankruptcy proceedings, including those assets acquired during the bankruptcy stage;
- (c) any contract entered into by the bankrupt debtor after the issuance of the bankruptcy declaration cannot be paid from the bankrupt estate, unless there is a benefit to the bankrupt estate to be derived from such contract;
- (d) a lawsuit concerning the rights and obligations of the bankrupt debtor on his assets shall be filed against or by the Orphans Chamber "Balai Harta Peninggalan" ("BHP"): Article 24 paragraph 1 of the Law No.4/1998;
- (e) the bankruptcy declaration will cause any court decision which is in effect against any part of the assets of the debtor prior to the bankruptcy declaration to be immediately suspended, and no decision may be executed against the bankrupt debtor;
- (f) any decision of confiscation, whether or not executed, is nullified by law; and
- (g) employees of the bankrupt debtor may resign or the Receiver may dismiss them subject to employment periods stipulated in employment contracts or company regulations (as the case may be), and/or subject to the terms stated in the Manpower laws and regulations. Six weeks termination notice must be given. As from the effective date of the bankruptcy declaration, remuneration to employees is a debt of the bankrupt estate.

Pursuant to Article 102 of the Law No.4/1998, the provisions of Articles 84 through 88 of the Law No.4/1998 apply to the board of management of a limited liability company, a mutual insurance company, a securities company, a cooperative, or other business entity which has the status of a legal entity or an association or a foundation, and Article 101 paragraph 1 of the Law No.4/1998 applies to the board of management and the board of supervisors.

Article 3 paragraph 1 of the Law No.1/1995 provides that shareholders of a limited liability company are not individually responsible for agreements made on behalf of the company, and that they are not responsible for a

company's losses where they exceed the nominal value of the shares subscribed.

In certain cases, it is possible for the shareholders to lose their limited liability. These cases are:

- (i) the company's requirements as a legal entity have not been or are not fulfilled;
- (ii) the relevant shareholders either directly or indirectly with bad faith take advantage of the company solely for their personal interest;
- (iii) the relevant shareholders are involved in unlawful acts conducted by the company; or
- (iv) the relevant shareholders either directly or indirectly unlawfully use the company's assets, causing the company's assets to be inadequate to settle the company's debts.

Pursuant to Article 79 paragraph 3 of the Law No.1/1995, those persons who may be appointed as members of the board of directors are individuals who have never been declared bankrupt, who were not the members of a board of directors or the commissioners responsible for the bankruptcy of another company, or who have never been punished due to criminal acts causing a loss to the state within five years prior to their nomination.

Similar provisions also apply to the board of management, board of supervisors and board of "pembina" in foundation with legal status. See Articles 28 to 30 of Law No.16/2001 concerning the Foundation ("Yayasan").

Article 90 paragraph 2 of the Law No.4/1998 provides that in case the bankruptcy occurs due to the mistake or negligence of the board of directors and the company's assets are inadequate to cover the losses caused by such bankruptcy, each member of the board of directors is jointly responsible for such losses. However, if a member of the board of directors can prove that the bankruptcy was not due to his or her mistake or negligence, he or she is not jointly responsible for the losses. Under Article 39 paragraphs 1 and 2 of the Law No.16/2001, similar provisions apply to the board of management of the Foundation.

Section J – Case Management of Insolvent Enterprises

1. Administration of Insolvency Procedures Generally:

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of Indonesia, what are the administrative organs/entities involved in the implementation and management of that procedure? (For example a trustee, liquidator, receiver, government official).*

Answer: In connection with Indonesia's bankruptcy procedure, the administrative organs involved in the implementation and management of such procedures are as follows: (i) Commercial Courts; (ii) the Supervisory Judge; and (iii) the Receiver.

- (b) **Question:** *What qualifications must each type of administrator of insolvency procedures possess? Is there a system of regulation of insolvency administrators in Indonesia?*

Answer:

Commercial Court and Supervisory Judge:

The Bankruptcy Law does not specify the qualifications which ought to be imposed on Judges of the Commercial Court, or on Supervisory Judges. However, a short training course and a number of workshop programs have been designed and provided to the Judges who have been designated as Commercial Court Judges, and those who have been nominated for a Commercial Judge. The purpose of this is to familiarise those persons with matters related to bankruptcy law.

Another interesting development is that a number of judges of the Commercial Court have joined the Post Graduate Program on Law conducted by prominent Law Schools in this country on their own initiative.

Receivers:

There are two types of Receivers, namely: (i) Orphans Chamber/ BHP, which is a special agency of the Department of Justice; and (ii) private Receiver (Article 67A of the Law No.4/1998). Pursuant to Article 67B of the Law No.4/1998, the private Receiver must be either an individual or a private partnership, and must possess specific expertise in respect to the management and/or settlement of the bankrupt estate, have domicile in Indonesia, and be registered in the Department of Justice. The appointed Receiver must also be independent and have no conflict of interest with either the debtor or the creditor.

- (c) **Question:** *Are the creditors of a corporate debtor permitted to participate in the administration of the relevant insolvency procedure, and if so, how? (For example are the creditors permitted to assist the administrator, or supervise or dictate the conduct of the administration?)*

Answer: Pursuant to the Article 7, paragraph 1 of the Law No.4/1998, as long as a decision on a petition for a declaration of bankruptcy has not been rendered, a creditor or the public

prosecutor may submit a petition to the Commercial Court to: (i) impose a conservatory attachment on part or all of the assets of the debtor; and (ii) appoint an interim Receiver to supervise the management of the debtors business, to supervise the payment to creditors and to transfer encumbrances of any assets of the debtor which under the framework of bankruptcy require approval from the Receiver.

2. Powers of The Administrator

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of Indonesia, what are the powers given to each type of administrator by statute, at general law or pursuant to the terms of the appointment? (For example power to carry on the business of the organisation, to pay creditors, to compromise claims of or against the debtor, to issue or defend legal proceedings, to obtain credit, to sell property, to execute documents on behalf of the debtor.)*

Answer: Below is the outline of powers given by Indonesian Bankruptcy Law to each type of administrators.

Supervisory Judges:

Supervisory Judges are appointed from Judges of the Commercial Courts (Article 13, paragraph 1 of the Law No.4/1998). Articles 63 and 64 of the Law No.4/1998, states that the duty, among others, is to control the management and settlement of the bankrupt estate.

Supervisory Judges shall be responsible for the management of the assets, and to make the completion of the assets. They also have the power to obtain information and clarification from both witnesses and experts: Article 63 and 64 of the Law No.4/1998.

The Supervisory Judges are authorised to hear witnesses, and to order an investigation by experts for the purpose of obtaining the necessary information related to certain bankruptcy proceedings. In this regard, the Commercial Court is obliged to hear the advice of the Supervisory Judge prior to the rendering of their decision on matters related to the management and settlement of the bankrupt estate.

Receivers:

The Receiver shall manage and settle the bankrupt estate, and shall be entitled to obtain loan facilities from a third party creditor to the extent that the use of such a loan facility will increase the value of the bankrupt estate.

With the consent of the Supervisory Judge, the Receiver shall be authorised to transfer the assets of the bankrupt debtor in order to avoid the unnecessary losses of such assets, and the costs and expenses of bankruptcy proceedings.

With the approval of the Creditors' Committee, the Receiver may continue the business of the bankrupt debtor, notwithstanding the fact that an appeal to the Supreme Court has been made, or that a judicial review has been filed against the bankruptcy declaration.

The Receiver appointed for a specific task under the decision of a bankruptcy declaration is authorised to act independently within the scope of its assignment.

The Receiver shall not be required to obtain the approval of, or to give prior notice to, the debtor concerned, notwithstanding that under other circumstances such approval or notice would be required.

Creditors Committee:

The Committee is entitled at any time to make a request to the Receiver for the inspection of books and documents relating to the bankruptcy proceedings.

The Receiver shall have the advice of the Committee before initiating a lawsuit, continuing a pending lawsuit, or defending itself against a lawsuit, unless the lawsuit deals with the verification of debt claims. The Receiver must also request the advice of the Creditors Committee as to whether or not to continue the management of the company, and all matters set forth in Articles 36, 38, 39, 57(2), 97, 98, 170 paragraph 3 and 172 of the Law No.4/1998. The Receiver must also request the advice of the Creditors Committee generally with regard to the settlement and sale of the bankrupt estate, and the time and the amount of allocations of the bankrupt estate to be made to creditors.

(b) **Question:** *To what extent and in what circumstances may each type of insolvency administrator seek assistance, advice or direction in the conduct of the administration, and from what sources? (For example the Court, his appointor, the creditors of the debtor, a solicitor, accountant or other relevant person.)*

Answer: Receivers:

The Receiver may obtain advice and assistance from private parties, such as an attorney, an accountant appraisal firm, a financial adviser or another relevant professional. Specific instances where such advice or assistance is obtained includes:

- (i) If in obtaining a loan from a third party creditor(s), the Receiver is required to encumber the bankrupt estate with a security right, pledge or collateral right on other property, and that the prior approval of the Supervisory Judge must be obtained for such a loan.
- (ii) If in order to appear before the Court, the Receiver must first obtain the approval of the Supervisory Judge.

The Receiver may at any time arrange a meeting with the Creditors Committee in order to obtain its advice, if necessary.

Creditors Committee:

The Creditors Committee is entitled at any time to request an inspection of the books and documents relating to the bankruptcy. The Receiver is obligated to provide all information requested by the Creditors' Committee.

3. Duties of The Administrator

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of Indonesia, what are the duties imposed upon each type of administrator by statute and at general law? (For example a duty to take possession of assets of the debtor, to realise those assets, to discharge the debt owed to his appointer, to call for proof of debts owed to creditors, to adjudicate upon claims of creditors, to apply available assets in discharge of those claims, to report on the conduct of the debtor by the proprietors.)*

Answer:

Supervisory Judge:

The Supervisory Judge is required to supervise the management and settlement of the bankrupt debtor: Articles 67 up to 70b of the Law No.4/1998.

Receiver:

The Receiver is required to perform the following duties:

- (i) to manage and or settle the bankrupt debtor;
- (ii) to appear before the Commercial Court. The Receiver must obtain approval from the Supervisory Judge, except in respect of disputes regarding the verification of claims, or for the matters set out in Articles 36, 38, 39, and 57 paragraph 2 of the Law No.4/1998;

- (iii) to be responsible for any faults and/or negligence in performing its duties which cause loss to the bankrupt debtor;
- (iv) to submit quarterly reports to the Supervisory Judge concerning the condition of the bankrupt debtor and the implementation of the Receiver's duties; and
- (v) to obtain the prior approval of the Supervisory Judge to encumber the bankrupt debtor with a security right, pledge or other type of collateral security on the assets of the bankrupt debtor.

Creditor's Committee:

The Creditor's Committee is required to perform the following duties: (i) to meet with the Receiver; and (ii) to give advice to the Receiver.

4. Breach of Duty and Liability of Administrators:

- (a) **Question:** *What remedies and/or sanctions are available in the legal system of Indonesia in respect of breaches of duty or transgressions committed by each type of insolvency administrator?*

Answer: Article 98 paragraph 1 of Law No. 4/1998 only addresses the breach of duty of a Receiver. It does not stipulate the sanctions for such a breach. Under the Indonesian Bankruptcy Law, the Receiver is responsible for any faults or negligence in performing its duties of managing and/or settling the bankrupt debtor which causes loss.

- (b) **Question:** *Have there been actual instances of breach of duty or transgressions committed by insolvency administrators?*

Answer: Yes. In the Manulife Case in 2002.

- (c) **Question:** *If so, given details of any major cases and a summary of the action taken and the results.*

[Details of the case are provided in the Second Report].

Section K – Assets Available to Creditors

1. Assets Available to Creditors Generally

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what assets of the corporate debtor are available to its administrator to satisfy the claims of its creditors?*

Answer: Pursuant to Article 19 of the Law No.4/1998, the bankruptcy estate will include all the wealth of the debtor at the time of the bankruptcy declaration, including that wealth acquired during the bankruptcy proceedings. Pursuant to this provision, the bankruptcy estate of the debtor also covers the assets of the debtor located outside of Indonesia, although in practice the existence of this provision is meaningless. Moreover, the bankruptcy estate also comprises any inheritance of the debtor that is obtained during the bankruptcy proceedings. Therefore any property or wealth that is inherited by the debtor during the bankruptcy proceedings is subject to the rights of creditors. However, Article 40 of the Law No.4/1998 stipulates that any inheritance of the debtor that is obtained during the bankruptcy proceedings should not be automatically included as part of the bankruptcy estate, except by a special right to register it as part of the bankruptcy estate.

In summary, all assets owned and possessed by the debtor are included within the bankruptcy estate, and are available to the Receiver to satisfy the claims of the unsecured creditors. Exceptions to the foregoing are assets that have been encumbered as collateral to secured creditors, including the holder of security rights (“hak tanggungan”), the holder of fiduciary transfer of security rights (“jaminan fidusia”), mortgages and pledges.

2. Avoidance of Past Transactions Affecting the Assets of a Corporate Debtor

(a) **Question:** *To what extent and in what circumstances may the administrator of a corporate debtor take steps to recover assets of the debtor by overturning past transactions involving property of the debtor? (For example preferences given to certain creditors over others, invalid charges granted by the debtor, uncommercial transactions entered into by the debtor, profits on sales to and from the debtor at an undervalue or overvalue).*

Answer: Transactions made by a debtor prior to a declaration of bankruptcy can be overturned if detrimental to the creditors. The right of annulment of past transactions is regulated by Articles 41 up to 44 of the Law No.4/1998. The act of annulling past transactions is sometimes referred to in Indonesia by its Latin phrase, “actio pauliana”.

Article 41 of the Law No.4/1998 stipulates the general rule that an annulment of past transactions can only be granted if it can be

proven that at the time of the transaction both the debtor and the party concerned (i.e. the transferee of the asset) were aware or should be deemed to have been aware that such action would cause losses to the creditors. Based on the foregoing, a Receiver is empowered to annul such transactions only if it can establish that both parties to the transaction were aware or should be deemed to have been aware that the transaction was detrimental to the creditors. The burden of proof lies with the Receiver and there is no time limit on past transactions that can be annulled.

On the other hand, Article 42 of the Law No.4/1998 states that for legal acts causing losses to the creditors which were undertaken within one year of the declaration of bankruptcy, and which were not actually required to be undertaken by the debtor, unless it can be proven to the contrary, then the debtor and the party with which such actions were undertaken are deemed to have been aware, or should have been aware, that such actions would cause a loss to the creditors, if such actions:

- were obligations in which the debtor’s liability substantially exceeded the obligation of the party with which such commitment was entered into;
- constitute a payment for, or a guarantee for, a debt, which has not yet reached maturity or which is not yet payable; and
- were undertaken by a debtor with certain specified relatives or affiliates.

In conclusion, if a transaction meets one of the foregoing criteria, a Receiver could take action to annul the transaction without having to prove that the debtor and the third party were aware or should have been aware that such actions would cause losses to the creditor. This annulment process under Article 42 of the Law No.4/1998 is limited to transactions undertaken within one year of the bankruptcy proceedings.

(b) **Question:** *What powers or mechanisms are available to each type of administrator for investigation of the affairs of the corporate debtor, for examination of persons formerly involved in the management or control of the debtor, and for the discovery of assets of the debtor?*

Answer: If the bankrupt debtor is summoned for such a purpose, then Article 101(1) of the Law No.4/1998 states that the bankrupt debtor is obliged to appear before the Supervisory Judge, the Receiver or the Creditor’s Committee to provide any relevant information. If the

debtor is a corporate debtor, its representative shall be the person(s) or the party that should answer the summons. Therefore, this provision applies to members of the Board of Directors and Board of Commissioners of the corporate debtor, or their authorised proxy(ies).

(c) **Question:** *What procedures may be employed by each type of administrator for the recovery of assets of the corporate debtor which are available for distribution to creditors? (For example initiation of legal proceedings, compensation from directors.)*

Answer: Please see Section K, 2(a).

Section L – Claims of Creditors

1. Claims admissible for payment

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what types of claims of creditors are properly admissible for payment in the context of the procedure? (for example liquidated debts, future debts, contingent claims, secured claims, unliquidated claims for damages, interest claims, costs of administration or of legal proceedings, periodical payments, debts owed by guarantors of the business organisation.)*

Answer: The Bankruptcy Law does not specifically mention the types of claims of creditors that are admissible for payment. However, Articles 1131 and 1132 of the ICC provide in general that a creditor is entitled to recourse against the general assets of a debtor for non-payment of its debts, and that the proceeds of any sale of such general assets are to be divided amongst all of the creditors on a pro-rata basis based on the respective amounts owing to each creditor. Article 1131 of the ICC stipulates in full that: “Any and all movable and immovable properties of a debtor, whether those are present or future debts, shall account for his personal obligations”. Article 1132 of the ICC states in full that: “The debtor’s goods will serve as a joint guarantee for his creditors; their proceeds shall be divided pro rata among them, in proportion to the debt of each, unless a legal priority among the creditors exists”.

While the Indonesian Bankruptcy Law and the ICC do not directly address what types of claims might be admitted in bankruptcy proceedings, we believe that all types of claims can be admitted. The court would need to determine whether a particular claim should be admitted as

an unsecured claim against the bankruptcy estate, and the amount of such claim.

(b) **Question:** *At what date are the amounts of admissible debts computed?*

Answer: The amount of the admissible debts is computed as of the date of the declaration of the bankruptcy.

(c) **Question:** *By what method are claims of creditors proven by those creditors in the context of each type of insolvency procedure?*

Answer: Based on Article 106 of the Bankruptcy Law, the filing of claims by the creditors is conducted by providing an account statement, letters or any other written statement, indicating the nature and the amount of the claim. Evidence or copies stating whether the creditor has a pledge, a mortgage, a harvest security or other right over particular goods must accompany the statements. The creditors are entitled to demand a receipt for the delivery of the statements. The statements shall be delivered to the private receiver or to BHP.

Further, pursuant to Article 107 of the Bankruptcy Law, the receiver or BHP will then examine the accuracy and verify the claims submitted against the information provided by the debtor. In addition, the receiver or BHP will be involved in consultation with the creditors if there is any objection to their claims, and shall be authorised to demand from any of the creditors concerned any documents not yet submitted, as well as the originals of such documents.

(d) **Question:** *How are disputed claims made by creditors adjudicated upon? (for example by the administrator, or by a Court.)*

Disputed claims are adjudicated by the Supervisory Judge, who is appointed by the Commercial Court.

2. Priority and Payment of Creditors' Claims:

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what principles apply to the division of available assets of the corporate debtor among those of its creditors entitled to payment? Is there a basic principle of equality of payment, or are rights of priority of payment enjoyed by secured creditors, or by certain classes of creditors over others? (For example costs of the administration, claims for taxes owed by the debtor, amounts owed to employees of the organisation).*

Answer: We note that not all claims are treated equally under the ICC. Certain privileges under the Indonesian law are created pursuant to Articles 1139 and 1149 of the ICC. These provisions will be further discussed below.

While a privilege under these Articles does not create a security interest in a particular asset of the debtor, the holder of a privilege will be entitled to a preferential distribution of certain assets of the debtor over unsecured creditors that do not hold a privilege if the proceeds of the sale do not cover all creditors' claims. A secured creditor's rights to its collateral will rank ahead of such privileges, but behind the legal costs of foreclosure and taxes.

Pledges, mortgages, security rights ("hak tanggungan") and fiduciary transfer security ("Fidusia") are the only devices recognised by statutory law for creating security interests in movable and immovable property: Article 1134 of the ICC, Law No.4/1996 regarding Mortgage on Land and land Related Object (the "Law No.4/1996"), and Law No.42/1999 regarding Fiduciary Transfer respectively. Security and creditors who hold pledges and mortgages are categorised as secured creditors.

If bankruptcy proceedings are commenced against a debtor, secured creditors must exercise their rights within two months after the bankrupt estate is determined or deemed to be insolvent. This state of insolvency will occur after a final declaration of bankruptcy is issued, and after the verification meeting is held to reconcile claims.

Article 1134 of the ICC also provides that secured creditor's claims based on pledges and mortgages have priority over all unsecured claims "except where otherwise specifically provided by law". Article 1139 paragraph 1 of the ICC provides that foreclosure court costs have priority over secured creditor's liens. These expenses must thus be paid out of the proceeds of the sale of assets prior to payment to the secured creditors.

Article 21 of Law No.9 of 1994 Regarding the Amendment to Law 6 of 1983 on General Tax Provisions and Procedures (9 November, 1994) provides that the State has a preferential right and priority over all other rights, except for court costs incurred in the auction of assets, expenses incurred to safeguard goods, and court costs incurred with regard to inheritance. Accordingly, the proceeds from the sale of both secured and unsecured assets must be used for the payment of the debtor's taxes prior to any other claims, except those noted for court costs and auction expenses.

Article 110 of Law No.25 of 1997 Regarding the Labor Code, effective as of 1 October, 1998, provides that in the event that an employer is declared bankrupt or is liquidated, the employee's wages are given a priority based on the "prevailing regulations". This ambiguity has not yet been clarified by government regulation.

As mentioned above, under Indonesian Law certain creditors are given privileges over specific assets under Article 1139 of the ICC, and over the entire property of a debtor under Article 1149 of the ICC.

Pursuant to Article 1138 of the ICC, the privileges conferred by Article 1139 of ICC rank above those created under Article 1149 of ICC. These specific priorities rank ahead of general priorities. As noted above, claims for national and local taxes take priority over either type of privilege.

Article 1139 of the ICC provides that certain specific assets of the debtor are subject to the priority claims of certain categories of creditors, and that such claimants are entitled to the proceeds of the sale of these specific assets prior to the claims of general unsecured creditors. The privileges created by Article 1139 of the ICC are as follows:

- (i) claims for court costs arising solely from the auction of movable or immovable property (these claims also have an expressly stated priority over claims based on a pledge or mortgage);
- (ii) claims relating to leases of real property attached to the property concerned;
- (iii) claims of unpaid sellers of movable goods for the sale price of those goods attached to such goods;
- (iv) claims for costs incurred in connection with the storage or conservation of goods attached to such goods (e.g the claims of an unpaid warehouseman or conservator);

- (v) claims of workmen for work performed upon movable goods attached to such goods, regardless of the location of the goods;
- (vi) claims of an innkeeper attached to goods of the debtor in the custody of the innkeeper;
- (vii) claims with respect to freight costs and related expenses attached to the goods carried;
- (viii) claims of workmen, such as carpenters, for work performed in connection with the construction and repair of immovable property attached to the property, provided that the claims are not more than three years old and the debtor still owns the property; and
- (ix) certain claims against public servants as a result of a breach of their obligations.

Article 1149 of the ICC sets out general priorities as follows:

- (i) legal fees, exclusively arising from auction and the safeguarding of estates (these costs have priority over pledges, mortgages, security rights and fiduciary transfer security);
- (ii) reasonable claims for burial costs;
- (iii) claims for medical and hospital expenses in connection with a terminal illness;
- (iv) employee wage claims for the current and preceding year;
- (v) claims for the supply of basic necessities to the debtor and his family for the preceding six months;
- (vi) claims of boarding schools; and
- (vii) claims relating to debts of minors and persons under guardianship and claims relating to expenses incurred in the maintenance and education of minors.

In summary, the assets of the bankrupt estate will be applied to the creditors' claims in the following order of priority:

- (i) court and auction costs;
 - (ii) taxes;
 - (iii) claims of secured creditors;
 - (iv) privileged creditors;
 - (v) unsecured creditors.
- (b) **Question:** Give a brief account of the order of priorities, if any, of payment of creditors prescribed by the legal system of this country.

Answer: For the order of priorities of creditors' payments pursuant to the Indonesian law, see point (a) above.

Section O – Connection Between Debtor and Forum

(a) **Question:** In relation to each type of insolvency procedure available in the legal system of this country, what connection must there be between the debtor organisation and the law of the forum? (For example which of the following requirements, if any, must be satisfied in order for an insolvency procedure in relation to a corporate debtor in your country:

- principal residence of debtor;
- domicile of the debtor;
- nationality of the debtor;
- personal whereabouts at the material time;
- location of a place of business, branch or agency;
- location of assets of debtor;
- place where transaction or event took place which gave rise to liability;
- place where payment, discharge or performance of liability is due to take place.)

Answer:

Question: Are any other requirements imposed in relation to a connection between the debtor and the forum before an insolvency procedure may be initiated? If so, briefly describe these requirements.

Pursuant to Article 2 of Law No.4/1998 it is stated that:

- (i) A decision on a bankruptcy petition and other related issues as intended by this law, shall be rendered by the court having jurisdiction over the region in which the domicile of the debtor is located.
- (ii) Where the debtor has left the territory of the Republic of Indonesia, the competent court to render a decision on a bankruptcy petition is the court having jurisdiction over the region where the last domicile of the debtor was located.
- (iii) Where the debtor is a partner of a firm, the court having jurisdiction over the region where the domicile of the partnership is located shall also be competent to decide.

(iv) Where the debtor does not have a domicile within the territory of the Republic of Indonesia but conducts his profession or business in the territory of the Republic of Indonesia, the competent court to decide is the court having jurisdiction over the region where the domicile of the office from which the debtor conducts his profession or business is located.

(v) Where the debtor is a legal entity, then its domicile shall be as intended by its Articles of Association.

(b) **Question:** *Are any particular rules or conditions imposed in the legal system of Indonesia regarding the opening or commencement of an insolvency procedure in cases where the connection between the debtor and the forum is limited to only one of the factors mentioned in (a) above?*

Answer: There are no particular rules, as mentioned above, since the domicile of the debtor is sufficient to commence an insolvency procedure.

Section P – Foreign/Cross Border Elements

1. Claims of foreign creditors

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, to what extent are the claims of foreign creditors recognised in the context of administration of that procedure?*

Answer: There is no distinction between claims submitted by foreign creditors and claims submitted by local creditors. All claims will be treated equally in the commercial court. The claims of foreign creditors are fully recognised in the administration of the bankruptcy procedure, provided that the transaction documents are legally valid and binding on the foreign creditors and the debtor.

(b) **Question:** *What principle or rules apply to the recognition and admission of claims by foreign creditors? (for example):*

(i) *Are claims by foreign creditors subject to particular rules in relation to priority of payment?*

Answer: The priority for payments to all creditors is governed under the ICC, the Bankruptcy Law, and the Indonesian Income Tax Law, as provided in Section L2. Claims by foreign creditors are not subject to any specific rules in relation to payment priority.

(ii) *Do foreign creditors have to satisfy special or additional requirements, in order for their claims to be admitted?*

Answer: As stated in the previous answer, there are no special or additional requirements in order for the claims of foreign creditors to be admitted. As long as foreign creditors follow the provisions of the Bankruptcy Law their claims will be admitted as local creditors.

(c) **Question:** *What law is applied to establish the validity of foreign claims?*

Answer: The validity of foreign claims is determined by the governing law provided in the transaction document. In other cases, foreign claims secured with debtor's assets which are located in Indonesia shall apply Indonesian law for security document/agreements, but the underlying transaction document does not have to be governed by Indonesian law unless the parties (debtor and foreign creditor) wish this to be the case.

Foreign claims also need to be submitted properly in compliance with the requirements and procedures governed by the Bankruptcy Law.

2. Jurisdiction over Foreign Assets

(a) **Question:** *To what extent does the insolvency law of this country claim jurisdiction over assets of a corporate debtor situated abroad?*

Answer: Article 19 of the Indonesian Bankruptcy Law regulates that bankruptcy includes the total property of the debtor at the time of the bankruptcy statement, together with that which the debtor acquires during the bankruptcy. Further, Article 202 of the Bankruptcy Law provides that such property includes property situated abroad. In practice, the enforceability and effectiveness of this provision will not automatically be recognised by other countries. However, the Indonesian Commercial Court may order the debtor to sign a power of attorney to the bankruptcy receiver or administrator to include the debtor's assets situated abroad in the bankruptcy assets.

3. Foreign Insolvency Procedures

(a) **Question:** *To what extent do the rules of private international law of the legal system of this country recognise insolvency procedures commenced in a foreign jurisdiction?*

Answer: The rules of private international law in Indonesia do not recognise bankruptcy procedures commenced in a foreign jurisdiction, except where the countries of the concerned debtor and creditors have a bilateral agreement

or are bound to regional or international conventions that admit and recognise such bankruptcy proceedings in foreign jurisdictions and the decisions thereof.

(b) **Question:** *Under what circumstances, if any, may orders or judgements resulting from foreign insolvency procedures or administrations be recognised or enforced in the legal system of this country?*

Answer: Orders or judgments resulting from foreign bankruptcy procedures are not recognised and enforced in the Indonesian legal system as judicial orders. They are only recognised as supporting evidence in Indonesian bankruptcy proceedings.

4. Foreign Insolvency Administrators

(a) **Question:** *What recognition is accorded in the legal system of this country to the status and capacity of insolvency administrators (for example trustees, liquidators, receivers) appointed in foreign insolvency procedures?*

Answer: As a consequence of the non-recognition and non-enforceability of foreign bankruptcy orders or judgments, the Indonesian legal system does not recognise bankruptcy administrators appointed in foreign bankruptcy procedures.

Article 67A of the Bankruptcy Law expressly states that the receiver shall be the BHP or other receiver, which is defined as an individual or partnership domiciled in Indonesia and possessing the special expertise required in the framework of managing and/or settling the bankruptcy estate and registered at the Department of Justice. In view of the above, foreign receivers are not recognised under the Indonesian Bankruptcy Law.

(b) **Question:** *To what extent are foreign insolvency administrators entitled to claim, take control of, and realise or deal with property of the corporate debtor situated within the jurisdiction of the legal system of this country?*

Answer: Foreign bankruptcy administrators are not entitled to claim, take control of, realise, or deal with the property of foreign corporate debtors situated within the territory of Indonesia. However, where a foreign debtor's assets are granted as security for the loans of a foreign debtor with its creditors, foreign bankruptcy administrators are able to settle and claim the debtor's assets located in Indonesia, provided they comply with the provisions in the

security documents, which must be governed by Indonesian law.

5. Foreign Security Holders

(a) **Question:** *To what extent does the legal system of this country recognise the validity of rights of security asserted by foreign creditors over assets of the corporate debtor?*

Answer: The Indonesian legal system does not distinguish the validity and enforcement of security rights asserted by foreign and Indonesian security holders, as long as the security documents are legally valid and binding and governed under the Indonesian law.

(b) **Question:** *Are any special rules applicable to determine the validity, extent and ranking of such security rights?*

Answer: Please see our answer in Section L, 2 above.

6. International conventions

(a) **Question:** *To which international conventions having some application in insolvency matters is this country a party?*

Answer: We are not aware of any international conventions applying to insolvency matters in Indonesia which Indonesia is a party to.

(b) **Question:** *When were these conventions entered into, and what other states are parties?*

Answer: Please see our answer to P6(a).

(c) **Question:** *What observations can be made about the practical results achieved under these international instruments?*

Answer: Please see our answer to Section P, 6(a).

7. Cross-border insolvency

(a) **Question:** *Are there any other particular issues or special problems in the field of cross-border insolvency, not included in the answer supplied above, which have presented themselves before the courts of the legal system of this country?*

Answer: Yes. It would be advisable and perhaps necessary to regulate a clear pattern for the participation of foreign creditors who would like to join up with local creditors, and to regulate the possibility of accepting foreign receivers as representatives in the Indonesian Commercial Court.

8. UNCITRAL Model Law on Cross-Border Insolvency

(a) **Question:** *Is the GOI aware of the UNCITRAL Model Law on Cross-Border Insolvency, approved by the United Nations in June 1997?*

Answer: The GOI is aware of the UNCITRAL Model Law on Cross-Border Insolvency.

(b) **Question:** *If so, are you aware of whether the GOI has any proposals to enact the terms of the model law?*

Answer: There are no proposals of the GOI of which we are aware to adopt the UNCITRAL Model Law on Cross-Border Insolvency.

Section Q – New Developments

Question: *Are there any recent, imminent or proposed legislative, administrative, or practical reforms or developments or proposals in the legal system of this country which impact upon the matters mentioned above?*

Answer: Draft Amendments to the Law No.4/1998, the Law No.8/1995 on Capital Market and the Law No.1/1995 have been prepared and submitted to the House of Parliament. However, issues relating to cross-border insolvency have not yet been discussed.

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Answer: See below.

B. Insolvency Reforms

1. **Question:** *Provide details of any reforms that have occurred in relation to insolvency law and practice and related areas (such as corporate governance, secured transactions and so forth) since January 1999.*

Answer: Certain amendments to laws and regulations concerning insolvency law and practice, and other related areas have been prepared. These include the New Draft Law on Bankruptcy, which is to replace Law No.4/1998; draft Amendment to Law No.1/1995 on Corporation law and draft Amendment to Law No.8/1995 on Capital Markets. The new draft on Bankruptcy Law has been submitted to the House of Parliament. However, it has not yet been discussed. The other two draft amendments, i.e. draft Amendment to Law No.1/1995 and draft Amendment to Law No.8/1995 are in the hands of the Secretary Cabinet, but have not yet been submitted to the House of Parliament for discussion purposes.

The improvements which have been proposed and incorporated into those draft New Law and draft Amendments mentioned aim to minimise problems which arise in practice. This includes matters related to the issue of definition, the unrealistic time limit, the unclear law of procedure, the less proper provisions on certain matters, and unclear legal concepts of certain

matters regulated in the law. However, not one of the draft laws or draft Amendments has touched upon issues of cross-border insolvency.

The submission of the draft Amendment to Law No.8/1995 on Capital Markets faced uncertainty due to the issuance of the New Draft Law on Financial Services Authority. This New Draft Law on Financial Services Authority intended to cover not only banking services and financial services, but also pension plans, and the insurance and capital market industry.

2. **Question:** *Provide details of any proposed reforms as above.*

Answer: In May 1998 the Department of Justice formed a Law Reform Team whose duty is to advise the Minister of Justice on legal policy, covering three elements: legal structure, legal substance and legal culture.

Legal structure reform is the restructuring of legal institutions which are no longer relevant, and the establishment of new legal institutions such as the Commercial Court, IBRA and the Investigation Committee on Business Competition and AntiMonopoly Law.

Legal substance reform is the restructuring of legal materials which are no longer relevant to legal developments in society, for example, proposed revisions to the Indonesian Civil Code (the "ICC") and the Indonesian Criminal Code.

Legal culture reform is legal education through several programs to disseminate information to the public, for example, the training of

Commercial Court Judges by international organisations and the registration of Fiduciary Transfer Rights at the Department of Justice

G. Insolvency Law

1. **Question:** *What are the major substantive weaknesses in the corporate insolvency law viewed from the respective positions of:*

- (a) *banks/financial providers*
- (b) *secured creditors*
- (c) *unsecured creditors*
- (d) *employees*
- (e) *corporations*
- (f) *directors*
- (g) *shareholders?*

Answer: *Generally:*

- (i) The definition of debt is still disputable. Areas of dispute include whether a debt is limited only where a loan facility is provided by a commercial bank and lenders in general, or whether it includes any type of contract or arrangement that may create payment obligations on the part of the debtor company, such as payment obligations due to the supply of goods, rendering services, leasing and hire purchase arrangements and dividends for shareholders.
- (ii) The requirement of two creditors sometime becomes meaningless, in particular if the bankruptcy proceedings deal with fictitious creditor(s).
- (iii) The requirement that a debtor has failed to pay at least one debt (of at least two creditors) which is due and payable may create a problem. This is because it may be interpreted simply as the non payment by such debtor, without considering that the debtor is a sound healthy company (i.e that does not have any cash flow problems, and is able to service its current obligations), and without considering whether or not there are any excess liabilities over assets (balance sheet criteria).
- (iv) The time frame work as currently stated in the Bankruptcy Law is in practice unrealistic:
 - a. 20 days for the Commercial Court to commence hearing (Article 4 paragraph 5 of the Law No.4/1998);
 - b. 7 days to summon the debtor (Article 6 paragraph 2 of the law No.4/1998);

- c. 30 days to issue the decision of the Commercial Court (Article 6 paragraph 4 of the Law No.4/1998);
- d. 8 days to submit petition for cessation (Article 8 paragraph 2 of the Law No.4/1998);
- f. 20 days for the Supreme Court to proceed the cessation petition (Article 10 paragraph 2 of the Law No.4/1998); and
- g. 30 days for the Supreme Court to issue decision (Article 10 paragraph 3 of the Law No.4/1998).

At the level of the Commercial Court, this timetable not only means that the debtor respondent and their counsel will be hard pressed for time, but also that the panel of judges presiding over the bankruptcy case will be as well. Given the fact that the Commercial Court is still in the process of adjusting and becoming accustomed to the demands of the new bankruptcy law regime, the 30 day period of time (out of which there will be at least 4 Sundays) within which the panel of three judges must conduct hearings, review documents, briefs and evidences, resolve arguments and decide the matter, is often inadequately short. Moreover, if the case involves loan documentations and supporting documents which have New York law or English law as the governing law, then the documents would be of substantial length and complexity.

Specifically:

(i) Creditors

Creditors may face problems when dealing with loan syndication questions, such as whether the syndicated loan should be considered as one creditor, or as two or more creditors. In a true loan syndication, every bank is a creditor and as such shall have its own claim on the borrower. On the other hand, a syndicate may also be called a "participation syndicate", whereby one lead bank enters into a bilateral loan agreement with the borrower, and then sells its participation in the loan to the other bank(s). In this case, the borrower has only one creditor. The participant in the loan only has a claim against the lead bank.

The provisions relating to the requirement of at least more than two creditors, as referred to in Article 1 paragraph 1 of Law No.4/1998, does not clearly define the matter. Uncertainty resulting from differences in opinion will always arise.

(ii) Secured Creditors

Pursuant to Article 56 of the Law No.4/1998, a secured creditor ("kreditur separatis") is entitled to enforce its rights as if no bankruptcy has

occurred. A secured creditor, on the other hand, does not have the right to cast votes at meetings in bankruptcy proceedings. As a consequence, a secured creditor intending to submit a bankruptcy petition against a particular debtor should waive its rights as a creditor (“kreditur separatis”) and become an unsecured creditor (“kreditur konkuren”) prior to the submission of the petition. Problems arise when the said bankruptcy petition is for some reason rejected by the court, and the former secured creditor with its privilege then becomes only an unsecured creditor of a debtor.

(iii) Unsecured creditor

The major difficulty which may be faced by an unsecured creditor is in dealing with a debtor which has a big cash flow problem, and no fixed assets or assets which are not being encumbered. Although a bankruptcy petition has been filed, and they may have won the case, his winning of the petition will probably only be on paper as in reality he will get nothing.

(iv) Employees

Pursuant to Article 39 of the Law No.4/1998, once a bankruptcy has been declared, the employment relationship will be terminated. The termination may be implemented at the request of either the Receiver or the employee himself. The downside from the employees side is that on the distribution of assets of the bankrupt estate, employee wages are ranked within the component of unsecured creditors, under the following order of priority:

- a. court and auction costs;
- b. taxes;
- c. claims of secured creditors;
- d. privileged creditors; and
- f. unsecured creditors.

(v) *Directors.*

Under the Law No.1/1995, the board of directors shall represent the company and shall act for and on behalf of the company. Indonesian Company Law does not make a clear distinction between the responsibilities of an active director and a silent director. Unless it can be proved otherwise, members of the board of directors may be regarded as personally liable where the occurrence of bankruptcy is due to the mistake and/or the negligence of the board of directors.

The delegation of power by the board of directors to a certain individual grantee shall not waive the possible personal responsibility of each member of the board of directors towards third party(ies).

2. **Question:** *What are the major practical weaknesses in the application of the insolvency law viewed from the respective positions of:*

- (a) *corporations; and*
- (b) *creditors?*

Answer: The Bankruptcy Law only requires simple evidence to prove that the company has two or more creditors, one of whose debt is due. The major weakness in the application of the insolvency law for both the debtor and creditor are the incomplete rules for judicial proceedings, and the fact that the presiding judge is incapable of handling the complicated loan arrangements amongst creditors and debtors.

See Section H 4 for a more detailed discussion.

H. Judicial System

1. **Question:** *Has there been any discernable improvement or change in the operation of the judicial system in relation to the conduct of:*

- (a) *debt collection/recovery processes;*
- (b) *enforcement processes in respect of secured property rights;*
- (c) *recovery or enforcement processes in respect of leased property; and*
- (d) *formal corporate insolvency processes?*

If possible, provide some detail of cases in which any such change or improvement has been made apparent.

Answer:

- (a) The Indonesian Bank Restructuring Agencies (“IBRA”) has been quite successful in recent times in obtaining collection from its debtors. This has been through a number of means, including direct cash payment made by major shareholders of the IBRA’s debtors, selling the fixed assets under the control of IBRA and selling the port-folio assets as a result of the restructuring process being completed.
- (b) No. Please see our comments under Section L.
- (c) No. However, since 1988 the Supreme Court has opined that a lease agreement cannot be cancelled unilaterally, except where the lessee is unwilling to fulfill its obligations under the lease agreement: Decision of Supreme Court No. 1724.K/Pdt/1988. August 31, 1988.

- (d) Yes. The improvements are as follows:
- (i) Under the amended Bankruptcy Law, there are two types of insolvency proceedings, bankruptcy and the suspension of debt payments. The insolvency of a corporate can now be determined by a more simple method, namely that the corporate must have at least two creditors, one of whose debt is due.
 - (ii) Bankruptcy proceedings now have a speedier time frame of 30 days from the date of the filing of the petition at the Commercial Court, and from the date of the filing of the appeal petition at the Supreme Court.
 - (iii) Any objection to the Commercial Court's decision can now be appealed directly to the Supreme Court and will be decided within 30 days as of the date of the filing.
 - (iv) The Bankruptcy Law offers a simple authentication procedure requiring only written evidence of the (due and payable) debts.
 - (v) Also, the hearing process and the announcement of the bankruptcy decision are now open to the public, and copies of the decisions are also publicly available.

Notwithstanding the above, the enactment of the amended Bankruptcy Law has not brought much satisfaction to creditors. However, with the passage of time and the benefit of additional resources, the judiciary is likely to become more consistent in its decision making, and therefore earn the confidence of creditors and investors. A recent Supreme Court case involving PT Dharmala Agrifood is an early but important step in this direction. Most of the problems in the judiciary arise at the first stage of a trial in the Commercial Court. Details of this particular case are provided separately.

2. Question: *What reforms, if any, have been made to improve the operation of the judicial system in relation to the above 4 areas?*

Answer: The only improvements made to the judicial system are in relation to the formal corporate insolvency process. Details follow:

- (i) Following the enactment of the Bankruptcy Law, there was only one Commercial Court established within the domain of the Central Jakarta District Court. This Court tentatively operated for the whole territory of the

Republic of Indonesia until 18 August, 1999 when 4 additional commercial courts were established by the issuance of Presidential Decree No. 97 of 1999. The Commercial Court is the court in charge of hearing and deciding on petitions for bankruptcy adjudication.

In addition to hearing and deciding petitions for both the adjudication of bankruptcy and suspension of debt payments, the Commercial Court should also have jurisdiction to hear and decide other cases in commercial fields. This jurisdiction should be stipulated by a government regulation.

- (ii) Law No. 30 of 1999 on Arbitration and Dispute Settlement Alternatives was enacted on 12 August, 1999 ("Law No. 30"). With the development of national and International business and commercial traffic, as well as the development of law in general, the regulations that were used as arbitration guidelines and contained in the old civil procedure law (Reglement op de Rechtsverding or RV) are no longer applicable. The RV does not stipulate on international contracts and their implementation. This no longer conforms to the reality of the Indonesian business world, especially since the signing of the GATT treaty and given Indonesia's involvement in APEC.

Arbitration as regulated in Law No. 30 is a means of settlement outside the general judicial court system based on the written agreement of the disputing parties. However, not all disputes may be settled through arbitration. The disputes which can be settled through arbitration are those regarding rights which, according to law, are held by the disputing parties on the basis of their agreement.

Law No. 30 has now set forth the procedures for case submissions before the arbitration committee, and creates the possibility of arbitrators issuing provisional decisions, stipulation impounds, ordering the safekeeping of goods or the sale of damaged goods, as well as hearing witnesses and expert witnesses.

In general terms, the arbitration body holds certain advantages over the judicial body. The arbitration body:

- a. guarantees the confidentiality of the parties;
- b. may avoid delays due to procedural and administrative matters;

- c. allows the parties to select those arbitrators they deem as honest and fair, and as having sufficient knowledge, experience and background regarding the matter being disputed;
- d. allows the parties to select which law to use to settle the matter as well as the process and place of arbitration;
- e. makes the decision of the arbitrator binding on the parties through simple procedures or direct implementation.

Therefore, as mentioned above, the option for any party to resolve its dispute through arbitration may improve the operation of the judicial system.

(iii) The establishment of the Steering Committee under the management of the Indonesian Supreme Court. This Steering Committee has made improvements, such as appointing ad hoc judges and determining the court fee for bankruptcy proceedings. However, the functions, authorities, and administration of ad hoc judges are unclear.

3. **Question:** *Are there any identifiable proposals for reforms in these areas?*

Answer: Yes, there are some proposals for such reforms. These are as follows:

The Bankruptcy Law is to be revised, among other things to accommodate a proposed broader definition of "debt" than currently exists; and

Law No. 14 of 1970 on the principles of Judicial Authority is to be reviewed.

Both of these proposed laws will be submitted to the new House of Representatives for approval.

4. **Question:** *What are the main problems or difficulties regarding the operation and application of the corporate insolvency law through the court system?*

Answer: The main problems are as follows:

- (i) Lack of fairness in the trials, due to the questionable credibility of the presiding judges. It is common knowledge that corruption is rampant in the courts. Judges, prosecutors, and lawyers are all involved in such dirty games.
- (ii) Many of the bankruptcy petitions submitted involve modern and sophisticated transactions of derivatives, swaps, commercial paper, etc. In many cases, the Panel of Judges presiding over the hearing

does not quite understand the transactions. This leads to misinterpretation or a narrow interpretation of the documents provided by the parties.

Some problems have arisen in practice due to the unclear provisions in the Bankruptcy Law, particularly on procedural matters. In practice, the procedural law used in bankruptcy trials still refers to the Indonesian Civil Procedural Law. The definition of debt in the Bankruptcy Law has been interpreted in two different ways. One side argues that the legal term "debts" in the Bankruptcy Law refers to the law of obligations in the ICC. Under Article 1233 of the ICC, obligations or debts can arise either out of contract or out of law. There are obligations to provide something, and obligations to do or not to do something: Article 1234 of the ICC. A creditor is entitled to expect the performance of the obligation by the debtor, which obligation the debtor is obliged to perform. In contrast, the Supreme Court has a totally different opinion about the meaning of the legal term "debts". The Supreme Court effectively narrowed the meaning of this term in its judgement in the Modemland Realty case: Decision No. 03/K/N/1998. In this case, the Supreme Court decided that debt consists of the principal debt plus interest. Consequently, only loans would then qualify as debts under the Bankruptcy Law.

5. **Question:** *What practical improvements might be made to overcome these problems?*

Answer: The following are some practical solutions to those problems:

- (i) Improving the salaries of judges and other government law enforcement officials; and
- (ii) Providing the judges who are in charge of the Commercial Court with more training concerning modern business transactions.

Such improvements would be more effective if the Supreme Court decides that the judges are bound by jurisprudence with respect to commercial cases, including bankruptcy cases.

J. Insolvency Administration System

1. **Question:** *Comment on the extent of development, expertise and efficiency regarding both public and private sector administration of formal cases of:*

- (a) corporate liquidation; and
- (b) corporate re-organisation.

Answer:

(a) Bankruptcy proceedings are becoming less and less popular to businessmen and investors. For some reason, the result of certain proceedings is far from what is expected. An example of this is the Manulife case.

On the other hand, the re-organisation process, through the suspension of payment route, is somewhat effective, efficient and successful. This is reflected in the re-organisations involving BCA Group, Bakrie Group, Sinar Mas, Barito Group and Lippo.

(b) Please see our answer to J1(a).

2. **Question:** *Is it considered that education and training in these areas would be valuable and, if so, in what areas?*

Answer: Yes. Training and education should particularly cover the restructuring and re-capitalisation of the banking, insurance, corporate finance and capital market sectors and other relevant issues. Considering their powers and duties under the Bankruptcy Law, independent receivers, officials if the state receiver and Supervisory Judges (including all Commercial Court judges), should be given more training and education to improve their skills and knowledge on current business and legal practices so that they can make the corporate liquidation and re-organisation process more efficient and effective.

3. **Question:** *Is it considered desirable to introduce more formal structures of both public and private sector administration of insolvency cases?*

Answer: No, because we believe the Bankruptcy Law has sufficiently addressed most of the formal structures required in the insolvency proceedings. Instead of setting up new formal structures for the insolvency proceedings, there should be encouragement to improve transparency within the judicial system, to improve generally poorly trained and accountable judges and receivers and to employ judges from professional fields with a solid background in business. We would also recommend optimising the function of ad hoc (expert) judges appointed for insolvency proceedings.

L. General Insolvency Information and Developments

1. **Question:** *Provide details of any other relevant information or developments since January 1999 in regard to such issues as the effect of insolvency law policies on areas such as employment, fiscal revenue debts, detection and recovery of corporate fraud, domestic and foreign investment etc.*

Answer: Apart from the Draft Amendment to the Bankruptcy Law, the Government has already prepared a Draft Law on Debt and Limited Liability Company Restructuring ("Draft Restructuring Law"), as an extensive amendment to the provisions on suspension of debt payment provided in the Bankruptcy Law.

This Draft Restructuring Law was prepared considering that a bankruptcy decision issued by the Commercial Court may have a wide-ranging impact on the termination of employees, suppliers, distributors distributing products and services produced by the bankrupt company, as well as on the consumers of the products and services produced by the bankrupt company. Accordingly, insofar as a corporate debtor and its debt can feasibly undergo re-organisation and restructuring, efforts undertaken in such a context should benefit debtors and creditors, and unsecured creditors respectively. Therefore, in order to guarantee the protection of creditors and debtors, shareholders and related parties, the Draft Restructuring Law should be immediately enacted to protect employees and to support the recovery and collection of debts, as well as for foreign and domestic investments.

2. **Question:** *Is there any evidence of a change in attitudes (such as social/commercial stigma, aversion to strict legal processes, fear of loss of control) toward the use of:*
- (a) *formal insolvency processes; and*
- (b) *informal insolvency processes*
- in respect of corporations in financial difficulty or insolvent corporations? If possible, provide details of any specific cases reflecting evidence of change.*

Answer:

- (a) Despite the slowness of improvements in the implementation of the Bankruptcy Law, there has been some change in attitudes toward the use of formal insolvency processes. The Bankruptcy Law has at least acted as a tool to encourage corporate debtors to negotiate the settlement of their debts. The shareholders of corporate debtors prefer to settle their debts outside formal bankruptcy proceedings in order to avoid the risk of losing control of the Company.
- (b) Many creditors seem as yet unwilling to accept that there is little likelihood of any meaningful recovery of their debts. While most appear willing to accept some loss, they have not accepted the likelihood of substantial write-downs. Nevertheless, with mutual cooperation and good faith, certain methods of debt restructuring and rescheduling may lead to a more significant and valuable recovery.

B. The efficiency of the administration of justice in the participating countries

Question: *Some of the sections in the Report and the Addendum to that Report referred to in A above also address the administration of justice in Indonesia. Please advise as to the extent to which the Report and the Addendum to that Report are accurate in this respect and also advise of any amendments or modifications which should be made to those aspects of the Report or the Addendum to that Report.*

Answer: No answers provided

C. Treaty

1. **Question:** *To what regional treaties providing for economic cooperation or designed for the facilitation of trade is Indonesia a party?*
2. **Question:** *What are the terms of those treaties?*
3. **Question:** *What are the mechanisms for amending those treaties?*
4. **Question:** *Can a signatory to those treaties reserve its position in respect of any amendment with a right to "opt in" either generally or with a prescribed period of time?*
5. **Question:** *Do those treaties provide for resolution of trade or other disputes?*
6. **Question:** *Do those treaties otherwise provide for a collaborative approach to addressing issues of mutual interest?*
7. **Question:** *Do those treaties provide for an exchange of information on issues of mutual interest?*
8. **Question:** *Do any of those treaties address the harmonisation of laws which may effect economic relations between member countries? If so, what are the relevant treaties and stipulations contained in them?*

Answer: No answers provided.

D. Actual outbound cross-border cases

1. **Question:** *In the course of the last five years, are you aware of there having been any companies which were incorporated in Indonesia which have been placed under some formal insolvency administration and which have had assets and/or liabilities in countries other than Indonesia? If so, please identify those companies.*

Answer: Due to developments in law and business, there are a number of Indonesian companies doing investment in countries outside Indonesia. We do not have much knowledge of the companies that have been placed under formal insolvency administration. However, we have been informed by IBRA that there are two insolvency cases in Singapore involving Indonesian shareholders, which involve assets in both Singapore and Indonesia. There is also an insolvency case in Honolulu, United State of America, involving IBRA as debtor, and other insolvency cases which have been filed in Chicago, involving IBRA as creditor.

2. **Question:** *In the case of each of those companies, are you aware of how those non-Indonesian assets and liabilities were administered? If so, in each case, please provide a general description of the process of administration*

Answer: More detailed information will be provided by IBRA

3. **Question:** *In the case each of those companies and so far as you are aware, were Indonesian creditors permitted to file their claims in the formal insolvency administration being conducted in Indonesia? In any case, were any those non-Indonesian creditors required to obtain a judgment in the courts of Indonesia or otherwise undertake any formal procedure in Indonesia as pre-requisite to filling their claims?*

Answer: Non-Indonesian creditors are entitled to file their claims in the formal insolvency administration being conducted in Indonesia. For this purpose, no prior Indonesian court decision should be obtained prior to the filing of the proceedings. There are no special formal procedures required for the filing of such proceedings, except that the said non-Indonesian creditors must appoint a qualified Indonesian lawyer with a special power of attorney to their interest in the court proceedings.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Indonesian creditors exercise their rights by pursuing claims against the non-Indonesian assets of the company? If so was there any procedure or process either available to or invoked by the insolvency administrator of those companies in Indonesia to restrain them from doing so?*

Answer: Yes, they did submit their case to the competent Indonesian commercial court; and such filing was accepted by the respective court. The facts that the Commercial Court decision may not have been in their favour is a different issue.

E. Actual inbound cross-border cases

1. **Question:** *In the course of the last five years, are you aware of there having been any cases of companies which were incorporated other than in Indonesia which have been placed under some form of insolvency administration and which have had assets and/or liabilities in Indonesia? If so, please identify those companies.*

Answer: We have no knowledge of companies under this situation.

2. **Question:** *In the case of each of those companies, are you aware of how its assets and liabilities in Indonesia were administered? If so, in each case, please provide a general description of the process of administration.*

Answer: We have no information with regard to the above matters.

3. **Question:** *In each case and so far as you are aware, in the case of Indonesian creditors, were they permitted to file their claims in the formal insolvency administration of the company being conducted in its place of incorporation?*

Answer: Yes, Indonesian creditors are permitted to file their claims in the formal insolvency administration which is being conducted in Indonesia. Non-Indonesian creditors may also file their claims in formal insolvency administrations by appointing a qualified Indonesia lawyer to represent and protect their interest.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Indonesian creditors exercise their rights by pursuing claims against the non-Indonesian assets of the company? If so was there any procedure or process either available to or invoked by the insolvency administrator of the company in its place of incorporation to restrain those creditors from doing so?*

Answer: No answer provided

F. Hypothetical inbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in Singapore and trades through a branch in Indonesia with the result that it has assets and liabilities there. ABC is ordered to be wound up by order of the Singaporean Courts and liquidator is appointed to administer its affairs. The liquidator wishes to take control of and administer the assets of ABC in Indonesia or

alternatively, arrange for their administration. She also wishes to arrange for all creditors of ABC, whether resident in Singapore, in Indonesia or else where, to file their claims in Singapore so that those claims can be dealt with equitably and consistently.

Assuming that there is presently no procedure in Indonesia for recognising the liquidation of ABC in Singapore.

1. **Question:** *What procedures can be invoked in Indonesia for placing ABC under a formal insolvency administration?*

Answer: As stated in Article 4 of Law No.4/1998, a new bankruptcy petition may be submitted. Such petition shall be submitted by qualified legal counsel.

2. **Question:** *In the case of each of those procedures, does the Singaporean appointed liquidator have standing to initiate the necessary application? If not, then in the case of each procedure in which the Singaporean appointed liquidator does not have that standing, who does have standing?*

Answer: This relates to the issue of sovereignty, which basically states that any country shall have the right to independently regulate anything within the boundary of their country. From this point of view, the Indonesian court should acknowledge whatever has been decided in that country, and as a result that appointed liquidator shall be deemed to be the authorised party to represent the insolvent company. Not all judges of the Commercial Court will agree to this opinion. In looking at sovereignty from the Indonesian legal side, and the fact that there is no treaty between Singapore and Indonesia concerning this issue, it is also possible that Indonesian judges will ignore the decision and the appointment of the liquidator made by the Singaporean court. In this case, those people under the terms of the articles of association of the insolvent company will be the authorised representative of such a company. A more detailed study is required in order to clarify this matter.

3. **Question:** *In the case of each procedure, to whom is the necessary application made for an order or direction establishing a formal insolvency administration?*

Answer: The making of an application for insolvency administration shall be submitted to the Commercial Court having jurisdiction in the particular case.

4. **Question:** *In the case of each procedure, how long does it typically take to obtain an order or other direction establishing a formal insolvency administration?*

Answer: Pursuant to Article 6, paragraph 4 of the Law No.4/1998, the decision on a petition of bankruptcy must be rendered within the time period of 30 days, to be counted as of the date of registration of the petition of bankruptcy.

Given the nature and complexity of the transactions involved, this 30 day time period becomes unrealistic at times.

5. **Question:** *In the case of each procedure, is it possible to obtain some interim or other like order or direction which secures the independent control of the assets of ABC in Indonesia pending the final determination of the application for an order or other direction establishing a formal insolvency administration?*

Answer: Pursuant to Article 7 of Law No.4/1998, to the extent that no decision on petition of bankruptcy has not been rendered, each of the creditors, or the public prosecutor (as the case may be), shall be entitled to submit a petition to the court asking it to:

- impose a conservatory attachment on part or all of the assets of the debtor; or
- appoint an interim receiver to:
 - supervise the management of the debtor's business, and
 - supervise payments made to creditors, the transfer or encumbrance of any assets of the debtor which, under the frame-work of the bankruptcy law, require approval from the receiver.

6. **Question:** *In the case of each procedure, what does it typically cost to obtain a final order or direction establishing a formal insolvency administration?*

Answer: In the case of bankruptcy procedures, there are not any detailed rules relating to the costs and expenses for obtaining final orders or directions establishing a formal insolvency administration. The fees for lawyers and expert witnesses are negotiable. Receiver fees will be in accordance with the direction issued by the Minister of Justice. There are no clear rules on the fees for supervisory judges.

7. **Question:** *In the case of each procedure, to what extent do the Indonesian creditors enjoy priority to or precedence over non-Indonesian creditors in the context of that procedure?*

Answer: Indonesian Bankruptcy Law does not make any distinction between foreign and local creditors. A distinction is made between secured and unsecured creditors. Article 56 of the Bankruptcy Law states that any creditor holding a mortgage, pledge or any other security right in rem may enforce its rights as if there were no bankruptcy.

8. **Question:** *In the case of each procedure, may the Singaporean and other non-Indonesian creditors of ABC file their claims in the formal insolvency administration established under that procedure? If so, what formal procedures or other pre-requisites have to be satisfied by those creditor prior to them filing their claims?*

Answer: Under the general rules, Singaporean creditors and other non-Indonesian creditors may file their claims in the formal insolvency administration under the same rules and procedures as those which apply to Indonesian creditors. Those foreign creditors shall be represented by a qualified Indonesian lawyer.

G. Hypothetical outbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in Indonesia and trades through a branch in Singapore with the result that it has assets and liabilities in Singapore. ABC is placed under a formal administration in Indonesia and an independent trustee is appointed to administer its affairs.

1. **Question:** *Is there any procedure available in Indonesia which will facilitate an application to the courts in Singapore for the establishment of an independent insolvency administration of ABC?*
2. **Question:** *If so, please describe that procedure.*
3. **Question:** *Does the fact that the principal insolvency administration of ABC is initiated in Indonesia as distinct from the insolvency administration of a company's branch affect the answers to F7 or F8?*

Answer: No answers provided.

Supplementary Questions

1. **Question:** *To what regional inter-governmental arrangements relating to economic corporation, facilitation of trade, investment protection, or mutual recognition of administrative or judicial process is the subject country a party? (Such arrangements might include regional treaties, non-treaty agreements, cooperative schemes, or regular forums at the ministerial or official level.)*

Answer: The Government of the Republic of Indonesia is a member of Association of Southeast Asian Nations (the "ASEAN"). As a regional inter-governmental association, ASEAN binds its members in several arrangements relating to economic cooperation, investment protection, judicial process and mutual recognition, including:

- Framework Agreement on Enhancing ASEAN

Economic Cooperation, Singapore, 1992, as amended by the Protocol to amend the Framework Agreement on Enhancing ASEAN Economic Cooperation, 1995;

- Agreement for the Promotion and Protection of Investment, 15 December 1987, Manila, as amended by the Protocol to Amend the Agreement for the Promotion and Protection of Investment. Which (if any) are the other countries that are party to any such arrangements;
- Framework Agreement on Mutual Recognition Arrangements; and

With regards to judicial process, the last regular forum held was the 5th Meeting of ASEAN Law Ministers. It issued the Joint Communiqué of The 5th Meeting of ASEAN Law Ministers 17th-18th June 2002, Bangkok.

2. **Question:** *Which (if any) are the other countries that are party to such arrangements.*

Answer: The members of the ASEAN, which are as follows:

- The Government of Brunei Darussalam;
- The Government of the Republic Indonesia;
- The Government of the Lao People's Democratic Republic;
- The Government of Malaysia;
- The Government of the Union of Myanmar;
- The Government of Republic of Singapore;
- The Government of Kingdom of Thailand; and
- The Government of Socialist Republic of Vietnam.

Please be informed that Until the Framework Agreement on Enhancing ASEAN Economic Cooperation and the Agreement for the Promotion and Protection of Investment Protection of Investment are issued, the Government of the Lao People's Democratic Republic and the Government of the Union of Myanmar are not parties to those Agreements.

3. **Question:** *Does any such arrangement refer to and deal with insolvency, either specifically or within the generality its terms?*

Answer: Yes it does in generality. See for example number 8 and 9 of the Joint Communiqué of The 5th Meeting of ASEAN Law Ministers.

4. **Question:** *Which ministry or agency has or would have responsibility for negotiating and administering arrangements on mutual recognition in the field of insolvency?*

Answer: In Indonesia, the Ministry of Justice of Republic of Indonesia shall be responsible for the negotiation and administration of arrangements on mutual recognition in the field of insolvency, with assistance and guidance from legal counsel, judges of the Commercial Court, Receivers; Supervisory Judge(s), notaries, and the House of Parliament ("Dewan Perwakilan Rakyat").



Asian Development Bank

Promoting Regional Cooperation in the Development of Insolvency Reform

RETA 5975

Draft Country Report for Singapore Conference Cross-Border Insolvency

Korea

A. The provisions

The provisions of the existing insolvency laws of the participating countries as well as any proposed reforms

- (a) **Question:** Please advise as to the extent to which the materials in Section I, J, K, L, O, P and Q of the Report and Sections B, G, H, J and L of the Addendum to that Report continue to be accurate. If those sections of the Report and the Addendum to that Report require amendment or modification, please advise of the amendments or modifications.

Report on Korea – produced under Asian Development Bank Technical Assistance No. 5795 – REG

Answer: See below.

Section I - Insolvency Law Regime

1. Underlying philosophy

- (a) **Question:** What is the underlying philosophy of the insolvency law of this country? (For example is it distributive, rehabilitative or penal?)

Answer: For bankruptcy, the underlying philosophy is distributive. With respect to re-organisation and composition, the underlying philosophy is rehabilitative.



(b) **Question:** *Are there elements of more than one philosophy present in the insolvency law of this country?*

Answer: The principle of equal treatment for equal classes of creditors underlies insolvency law.

(c) **Question:** *Briefly describe the relevant elements, and if applicable, any penal sanctions available.*

Answer: Penal sanctions are in part - fraudulent re-organisation: Articles 289-290, Re-organisation Act; bribery: Articles 291-292, Re-organisation Act and Articles 372-373 *Bankruptcy Act*; prohibition on participation in management: Articles 292-2, Re-organisation Act; unpermitted acts: Articles 292-3, *Re-organisation Act*; refusal of report and inspection: Article 293, *Re-organisation Act*; fraudulent bankruptcy: Article 369, *Bankruptcy Act*; violation of supervision of flight from domicile: Articles 366-367, 369-370 *Bankruptcy Act*; violation of duty to explain: Article 374, *Bankruptcy Act*.

2. Jurisdiction in insolvency matters

(a) **Question:** *In which judicial category is insolvency law classified in the legal system of this country? (For example civil, commercial or administrative.)*

Answer: Civil.

(b) **Question:** *Which Courts, tribunals or administrative bodies in this country are competent to exercise jurisdiction in insolvency matters?*

Answer: The District Court, which has jurisdiction over the main office of the debtor company, is the competent Court to exercise jurisdiction in insolvency matters: Article 96 of the *Bankruptcy Act*, Article 6 of the *Corporate Re-organisation Act*, Article 3 of the *Composition Act*.

(c) **Question:** *Are any limitations placed on the jurisdiction of any of these bodies?*

Answer: No.

3. Types of insolvency procedures

(a) **Question:** *What types of insolvency procedures are available in the legal system of this country for the administration of corporate debtors in financial difficulty? (For example bankruptcy, liquidation (winding up), receivership, restructuring or other forms of administration.)*

Answer: The types of insolvency procedures available under the law are bankruptcy, re-organisation and composition.

(b) **Question:** *Briefly describe the main features of each type of insolvency procedure for corporate debtors: including, for example the manner in which each procedure is initiated and administered, and the aims of each procedure.*

Answer:

Bankruptcy: bankruptcy proceedings may be initiated by the insolvent debtor, creditors or other interested parties. Once the application is filed and accepted, the Court may issue an order to preserve the assets of the debtor. In practice however, such a preservation order is seldom issued because the Court decides on whether the bankruptcy proceedings will commence or not within a month of filing and acceptance. With the adjudication of bankruptcy, the bankruptcy administrator is appointed to oversee the bankruptcy process. The aim of the *Bankruptcy Act* is to liquidate and distribute the remaining assets to the creditors in an equitable manner: Articles 122-125 and 132 of the *Bankruptcy Act*.

Re-organisation: re-organization proceedings may be initiated by the insolvent debtor, creditors or shareholders. Once the application is filed and accepted, the Court may issue an order to preserve the assets of the debtor. With the commencement order, the receiver is appointed to oversee the re-organisation process. The aim of the *Corporate Re-organisation Act* is to restructure the debt and fix a re-organisation plan that would promote the rehabilitation of the debtor: Articles 30, 39 and 46 of the *Corporate Re-organisation Act*.

Composition: composition proceedings may be initiated by the insolvent debtor only. Once the application is filed and accepted, the Court may issue an order to preserve the assets of the debtor. With the commencement order, the composition administrator (trustee) is appointed to oversee the important matters in the composition process. The aim of the *Composition Act* is to protect the insolvent

debtor company from liquidation. Intervention by the Court in composition proceedings occurs much less than in the case of re-organisation, except in the early stages of the composition: Articles 12, 20 and 27 of the *Composition Act*.

In addition, the *Bankruptcy Act* also provides the Compulsory Composition proceedings. However, in practice, Composition under the *Composition Act* is more frequently used than *Compulsory Composition under the Bankruptcy Act*. Moreover, the proposed *Initial Draft of the Unified Insolvency Act* ("IDUIA"), released in early November 2002, suggests that both the Composition, and Compulsory Composition procedures shall be eliminated, and that Re-organisation shall be the only formal procedure for the rehabilitation of an insolvent company.

(c) **Question:** *Identify the relevant legislation governing each type of insolvency procedure available for corporate debtors*

Answer: The relevant laws are the *Bankruptcy Act*, the *Corporate Re-organisation Act* and the *Composition Act*.

4. Commencement of insolvency procedures

(a) **Question:** *Is it usual or customary in respect of a corporate debtor which is insolvent to attempt to negotiate an informal administration before formal insolvency procedures are commenced?*

Answer: Although it will depend on the case, a corporate debtor may seek an informal administration before formal insolvency procedures are commenced.

(b) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, who may commence the procedure? (For example, the corporate debtor, secured creditors, unsecured creditors, shareholders, the State.)*

Answer: Under Korean insolvency law, the mere petition or application for insolvency proceedings shall not be considered as the formal commencement of insolvency proceedings. In order for insolvency proceedings to be formally commenced, an official commencement order (including bankruptcy adjudication) should be rendered by the Court. This being the case, then strictly speaking, only the Court may commence the insolvency procedures. In this regard, the following parties may file an application for the commencement of the procedures with the relevant Courts.

Bankruptcy: debtor, director(s) or the equivalent of a debtor company and creditors: Articles 122-125 of the *Bankruptcy Act*.

Re-organisation: debtor, creditors and shareholders: Article 30 of the *Corporate Re-organisation Act*.

Composition: debtor: Article 12 of *Composition Act*.

(c) **Question:** *On what basis may each type of insolvency procedure be commenced, or what requirements must be satisfied before the procedure may be commenced? (For example, non-payment of debts; balance sheet/cash flow insolvency; trading losses; resolution by directors to enter insolvency procedure.)*

Answer: In principle, a Bankruptcy petition may be filed if a debtor cannot fully repay its debts when they are due. In February 1998, the *Bankruptcy Act* was amended, such that a Bankruptcy petition may also be filed if the company is a joint stock company (chusik hoesa) or a limited liability company (yuhan hoesa), and the company's total debts exceed total assets: Articles 116-117 of *Bankruptcy Act*.

Re-organisation: a Re-organisation petition may be filed if there is a material detriment to the continuation of business or there are reasons to believe that the debtor may go into bankruptcy. Although excess debt can be a cause for filing the petition, this factor is not a necessary requirement.

Composition: a Composition petition may be filed if there are causes for bankruptcy (including excess debt) that exist, or if there are reasons to believe that the debtor may go into bankruptcy.

(d) **Question:** *How is each type of insolvency procedure commenced? (For example, by application to the Court, by administrative act, by written notice to the business organisation.)*

Answer: All types of insolvency proceedings are commenced by filing an application to the competent Court. In the case of bankruptcy, the Court also has the power to decide the initiation of bankruptcy proceeding on its own.

(e) **Question:** *What is the usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor?*

Answer: Re-organisation and Composition: The *Corporate Re-organisation Act* and *Composition Act* were amended in December

1999 (effective as of April 2000), and in January 2000 (also effective as of April 2000), respectively, such that the Court's decision on the commencement of the proceedings shall be made within one month of the application date. This decision is made without exception and regardless of the company's size.

(f) **Question:** *How effective is the judicial or Court system (or administrative system) in relation to the handling of formal insolvency proceedings?*

Answer: Previously, there was not a separate Court which solely heard insolvency cases, and the court system was not effective in relation to the handling of formal insolvency proceedings. However, the bankruptcy department was established within the Seoul District Court in March 1999, and thereafter other major district courts also established bankruptcy departments. Since then, the judges of bankruptcy departments have exclusively handled insolvency proceedings. As a result, the effectiveness of the court system in the insolvency proceedings has considerably improved.

5. Effect of insolvency procedures

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what is the effect on the corporate debtor, its constituent parts and its business relationships on the initiation of the relevant insolvency procedure? (For example, how does initiation of the insolvency procedure affect:*

- (i) *the powers of management of the debtor*
- (ii) *the interests of owners/shareholders of the debtor*
- (iii) *contracts to which the debtor is a party*
- (iv) *legal proceedings to which the debtor is a party*
- (v) *remedies available to persons in contractual (non-debt) relationships with the debtor*

Answer: Unless otherwise expressly indicated, the answers below will be correct only when the Court's commencement orders (including bankruptcy adjudication) for the relevant proceedings have been rendered.

Bankruptcy:

Powers of management: The management no longer has power of management.

Shareholders' interest: The shareholders have the right to the assets remaining after distribution to creditors and interested parties with priority over the shareholders.

Contracts to which the debtor is a party: Creditors under contracts with the debtor company will form part of bankruptcy claimants. Executory bilateral contracts can be terminated by the bankruptcy administrator: Article 14 and Article 50 of the *Bankruptcy Act*.

Legal proceedings: All present legal proceedings will temporarily cease. However, the legal proceedings relating to the bankruptcy estate may be resumed by the bankruptcy administrator or the opponent party. New compulsory execution will not be permitted and all present compulsory execution proceedings will no longer be valid: Articles 60-61 of the *Bankruptcy Act*.

Remedies: Where the contract is terminated by the bankruptcy administrator, damages incurred to persons in contractual relationships with the debtor company will form part of unsecured bankruptcy claims, and the consideration received by the debtor company will form part of the priority (bankruptcy estate) claims: Article 51 of *Bankruptcy Act*.

Re-organisation:

Powers of management: The management no longer has power of management.

Shareholders' interest: The shareholders usually cease to have shareholders' rights.

Contracts to which the debtor is a party: Creditors under contracts with the corporate debtor will form part of a re-organisation claim. Executory bilateral contracts can be terminated by the receiver, subject to the Court's approval: Articles 102-103 and 54 of *Corporate Reorganisation Act*.

Legal proceedings: All present legal proceedings will temporarily cease. However, the legal proceedings, which are not related to secured claims or unsecured claims, may be resumed by the receiver or the opponent party. New compulsory execution will not be permitted and all compulsory execution proceedings currently in progress will cease. During the period between the filing of an application for the re-organisation proceedings, and the Court's commencement order, all compulsory execution proceeding currently in progress will cease after the Court's order: Articles 67-69 and 37 of the *Corporate Reorganisation Act*.

Remedies: In the case that the contract is terminated by the re-organisation receiver, damages incurred to the persons in contractual relationships with the debtor company will form part of unsecured claims, and the consideration received by the debtor company will form part of priority (common benefit) claims: Article 104 of *Corporate Reorganisation Act*.

Composition:

Powers of management: The management continues to have the power of management, subject to the composition administrator's consent for the matters other than in the ordinary course of business.

Shareholders' interest: In principle, the shareholders' rights will not be affected by the commencement of the composition proceedings.

Contracts to which the debtor is a party: Creditors under contracts with the corporate debtor will form part of unsecured composition claimants. Contracts within the ordinary course of business will be effective: Article 32 and Article 42 of the *Composition Act*.

Legal proceedings: In principle, legal proceedings will not be affected with the commencement of the composition proceedings. New compulsory execution will not be permitted and all compulsory execution proceedings currently in progress will cease: Article 40 of *Composition Act*.

Remedies: Contracts cannot be terminated.

(b) Question: *If another insolvency procedure has already been initiated in relation to the corporate debtor, how does the initiation of a second procedure affect the first?*

Answer: In the case where a debtor company is already in bankruptcy proceedings:

- (i) If an application is filed for composition proceedings during the period between the filing of an application for bankruptcy proceedings, and the Court's adjudication for bankruptcy, the bankruptcy proceedings will cease. Also, if the Court authorises the composition plan, then the bankruptcy proceedings will be invalidated. However, if the Court has made an adjudication regarding bankruptcy, then the filing of an application for the commencement of the composition shall not be permitted: Articles 16-17 and 62 of the *Composition Act*.

- (ii) If the Court makes a commencement order for re-organisation, or an order to cease bankruptcy proceedings after the filing of an application for the commencement of the re-organisation, then the bankruptcy proceedings will cease. Also, if the Court authorises the reorganisation plan, then the bankruptcy proceedings will be invalidated. However, the Court may reject the application for the commencement of the reorganisation when it considers that the bankruptcy proceedings currently in progress will be more appropriate for the general interest of the creditors: Articles 37-38, 67 and 246 of the *Corporate Reorganisation Act*.

In the case where a debtor company is already in composition proceedings:

- (i) Once there has been a commencement order for the composition proceedings, the filing of an application for the bankruptcy shall not be permitted unless composition proceedings have been discontinued: Article 9 and Article 15 of the *Composition Act*.
- (ii) If the Court makes a commencement order for re-organisation, or an order to cease composition proceedings after the filing application for the commencement of the re-organisation, the composition proceedings will cease. Also, if the Court renders the commencement order for re-organisation, then the composition proceedings will be invalidated. Theoretically, the Court may reject the application for the commencement of the re-organisation where it considers that the composition proceedings currently in progress will be more appropriate for the general interest of the creditors. In practice, however, the Court usually renders an order to cease such composition proceedings: Articles 37-38, 67 and 246 of the *Corporate Re-organisation Act*.

In the case where a debtor company is already in re-organisation proceedings:

- (i) The filing of an application for bankruptcy shall not be permitted unless re-organisation proceedings have been discontinued: Articles 23, 37 and 67 of *Corporate Re-organisation Act*.
- (ii) The filing of an application for the composition shall not be permitted unless re-organisation proceedings have been discontinued: Articles 23, 27, 37 and 67 of the *Corporate Re-organisation Act*.

Section J – Case Management of Insolvent Enterprises

1. Administration of insolvency procedures generally

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what are the administrative organs/entities involved in the implementation and management of that procedure? (For example a trustee, liquidator, receiver, government official.)*

Answer: Please see Section I, 3.

- (b) **Question:** *What qualifications must each type of administrator of insolvency procedures possess? Is there a system of regulation of insolvency administrators in this country?*

Answer: There is no special qualification requirement. The Court appoints an appropriate person to serve as re-organisation receiver, composition administrator or bankruptcy administrator.

- (c) **Question:** *Are the creditors of a corporate debtor permitted to participate in the administration of the relevant insolvency procedure, and if so, how? (For example are the creditors permitted to assist the administrator, or supervise or dictate the conduct of the administration?)*

Answer: In re-organisation and composition proceedings, creditors form a creditors meeting. The creditors can, through the creditors meeting, express their opinion to the Court. Although the Court is not bound by such an opinion as expressed, it is nevertheless persuasive to the Court.

2. Powers of the administrator

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what are the powers given to each type of administrator by statute, at general law or pursuant to the terms of the appointment? (For example, power to carry on the business of the organisation, to pay creditors, to compromise claims of or against the debtor, to issue or defend legal proceedings, to obtain credit, to sell property, to execute documents on behalf of the debtor.)*

Answer: See below where 2 and 3 are combined.

- (b) **Question:** *To what extent and in what circumstances may each type of insolvency administrator seek assistance, advice or direction in the conduct of the administration, and from what sources? (For example, the Court, his appointor, the creditors of the debtor, a solicitor, accountant or other relevant person.)*

Answer: See below where 2 and 3 are combined.

3. Duties of the administrator:

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what are the duties imposed upon each type of administrator by statute and at general law? (For example, a duty to take possession of assets of the debtor, to realise those assets, to discharge the debt owed to his appointor, to call for proofs of debts owed to creditors, to adjudicate upon claims of creditors, to apply available assets in discharge of those claims, to report on the conduct of the debtor by the proprietors.)*

Answer: See below where 2 and 3 are combined.

Answer: 2 and J combined.

- The administrator in the Composition procedure:
 - (1) consents to the debtor's act not in the ordinary course of business;
 - (2) inspects the assets owned by debtor;
 - (3) examines the vote of Composition creditors and has the right to exercise an objection; and
 - (4) reports the result of the creditor's meeting to the Court and expresses his or her opinion regarding the meeting.
- The administrator in the Corporate Re-organisation procedure:
 - (1) represents the corporation;
 - (2) manages and disposes the assets of debtor;
 - (3) reports the management of the business and the asset status of the debtor to the Court;
 - (4) prepares a list of the assets and balance sheet;
 - (5) exercises objection against claims;
 - (6) prepares and executes Re-organisation plan; and
 - (7) carries out the Re-organisation plan.

- The administrator in the Bankruptcy procedure:
 - (1) manages and disposes of the assets of the bankrupt corporation;
 - (2) prepares the asset list and balance sheet;
 - (3) examines bankruptcy claims;
 - (4) reports the results of bankruptcy claims at the creditor's meeting;
 - (5) exercises objection rights against claims in bankruptcy;
 - (6) exercises avoidance rights; and
 - (7) disposes of bankrupt estates and distributes the proceeds thereof.

4. Breach of duty and liabilities of administrators

- (a) **Question:** *What remedies and/or sanctions are available in the legal system of this country in respect of breaches of duty or transgressions committed by each type of insolvency administrator?*

Answer: If the administrator breaches his fiduciary duty, the Court may remove the administrator and the administrator may be ordered to compensate the creditors for any injury he or she may have caused. Also, where an administrator commits a crime under the insolvency laws, then they will be subject to penal sanctions as set forth in insolvency laws.

- (b) **Question:** *Have there been actual instances of breach of duty or transgressions committed by insolvency administrators?*

Answer: Yes

- (c) **Question:** *If so, give details of any major cases and a summary of the action taken and the results.*

Answer: In May 2000, public prosecutors indicted a few insolvency administrators of debtor companies under bankruptcy, re-organisation and composition for bribery, conversion etc. It was reported that most of them were sentenced to imprisonment, or received fines.

Section K – Assets Available to Creditors

1. Assets available to creditors generally

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what assets of the corporate debtor are available to its administrator to satisfy the claims of its creditors?*

Answer: In each type of insolvency procedure, all transferable assets of the business which may have economic value are available to satisfy the claims of the creditors.

In the cases of composition and re-organisation, the insolvent debtor will repay its debts in accordance with the terms and conditions of the composition plan or re-organisation plan, where relevant, as approved by the Court. Therefore, the composition plan and re-organisation plan effectively changes the terms and conditions of the original debt and the debtor repays its debts in any manner it chooses as long as the manner of repayment is in accordance with the terms and conditions under the respective plans. However, under composition, creditors with security rights over specific assets may exercise this security right to satisfy their claims regardless of the terms and conditions of the composition plan.

Under bankruptcy, except for assets that are not transferable or assets that are required by the debtor to maintain his or her minimum standard of living, all transferable assets of the business which may have economic value are available to satisfy the claims of the creditors. However, creditors with security rights over specific assets will have priority rights of repayment from their respective security.

2. Avoidance of past transaction affecting the assets of a corporate debtor

- (a) **Question:** *To what extent and in what circumstances may the administrator of a corporate debtor take steps to recover assets of the organisation by overturning past transactions involving property of the organisation? (For example, preferences given to certain creditors over others, invalid charges granted by the organisation, uncommercial transactions entered into by the organisation, profits on sales to and from the organisation at an undervalue or overvalue.)*

Answer: Under the *Bankruptcy Act* and the *Corporate Re-organisation Act*, it is the administrator that has the right to take legal action to avoid or nullify transactions deemed prejudicial to creditors, except, generally, for situations where the beneficiary of the transaction(s) concerned was unaware of any prejudice to the insolvency creditors. To avoid or nullify transactions deemed prejudicial to creditors, a creditor would file a litigation claim or request a simplified adjudication proceeding to the Court. However, upon the application of the creditors (creditors or shareholders in re-organisation) the Court may order the administrator to exercise such a right. The *Composition Act* does not specifically provide for the avoidance or nullification of transactions deemed prejudicial to creditors, but the creditor may take legal action to avoid or nullify transactions that are in violation of certain provisions of the *Composition Act*, except in situations where the beneficiary of the transaction(s) concerned was unaware of such violations: Article 64 and Article 68 of the *Bankruptcy Act*, Article 78 and Article 82 of the *Corporate Re-organisation Act*, and Article 33 of the *Composition Act*.

For reference, the relevant articles of the *Bankruptcy Act* and the *Corporate Re-organisation Act* which state the circumstances in which transactions may be avoided or nullified are provided below.

Article 64 of the *Bankruptcy Act* – Avoidable Acts

The following acts may be avoided for the benefit of the bankrupt estate:

1. *Any act done by the bankrupt with the knowledge that it would prejudice creditors in bankruptcy; provided however, that this shall not apply in cases where the person benefited by the act did not know, at the time of the act, the fact that it would prejudice creditors in bankruptcy;*
2. *Any act relative to furnishing of securities or extinction of obligations, and any other act prejudicial to creditors in bankruptcy, done by the bankrupt subsequent to suspension of payment or after petition for bankruptcy has been filed; provided however, that this shall apply only in cases where the person benefited by the act knew at the time of the act that there had been suspension of payment or that petition for bankruptcy had been filed;*
3. *Any of the acts mentioned under the preceding item, of which the other party is a relative of the bankrupt or a person sharing a*

livelihood with the bankrupt; provided however, that this shall not apply in cases where the other party did not know at the time of the act there had been suspension of payment or that petition for bankruptcy had been filed;

4. *Any act relative to furnishing of securities or extinction of obligations done by the bankrupt subsequent to suspension of payment or after petition for bankruptcy has been filed, or within thirty days prior thereto, which does not appertain to the duties of the bankrupt; provided however, that this shall not apply in cases where creditors did not know at the time of the act the facts that there had been*

suspension of payment or that petition for bankruptcy had been filed, or that it would prejudice creditors in bankruptcy; and

5. *Any gratuitous act, or non-gratuitous act which should nevertheless be deemed to be the same as a gratuitous act, done by the bankrupt subsequent to suspension of payment or filing of petition for bankruptcy, or within six months prior thereto.*

Article 78 of *Corporate Re-organisation Act* – Right of Avoidance

Any of the acts set forth below may be avoided in favour of the company assets subsequent to the commencement of re-organisation proceedings:

1. *Any act done by the company with the knowledge that it would prejudice re-organisation creditors or re-organisation security holders (hereinafter in the present article to be referred to as the “re-organisation creditors, etc.”); provided however, that this shall not apply where the person benefited by the act did not know at the time of the act the fact that it would be prejudicial to re-organisation creditors, etc.;*
2. *Any act prejudicial to re-organisation creditors, etc., done by the company after suspension of payment, or after applications for bankruptcy, commencement of composition procedures, or commencement of re-organisation procedures, (hereinafter in the present article to be referred to as “suspension of payment, etc.”) and acts connected with furnishing of securities or extinction of obligations; provided, however, that this shall apply only where the person benefited by the act knew at the time of the act that there has been suspension of payment, etc., or the fact that it is prejudicial to re-organisation creditors, etc.;*

3. Any act concerning furnishing of securities or extinction of obligations done by the company subsequent to suspension of payment, etc., or within thirty days prior thereto, which does not appertain to the duties of the company or which in its method or timing does not appertain to the duties of the company; provided, however, that this shall not apply where the creditor(s) did not know at the time of the act the fact that the company did it knowing that it would prejudice equality with respect to other re-organisation creditors, etc., or, when such act is subsequent to suspension of payment, etc., where the creditor(s) did not know of the fact [of the suspension];

4. Any gratuitous act, or non-gratuitous act which should nevertheless be deemed to be the same as a gratuitous act, which the company has done subsequent to suspension of payment, etc., or within six months prior thereto.

(b) Question: What powers or mechanisms are available to each type of administrator for investigation of the affairs of the corporate debtor, for examination of persons formerly involved in the management or control of the organisation, and for the discovery of assets of the debtor?

Answer: See Section M.

(c) Question: What procedures may be employed by each type of administrator for the recovery of assets of the business organisation which are available for distribution to creditors? (For example, initiation of legal proceedings, compensation from directors.)

Answer: See Section K, 2(a).

Section L – Claims of Creditors

1. Claims admissible for payments

(a) Question: In relation to each type of insolvency procedure available in the legal system of this country, what types of claims of creditors are properly admissible for payment in the context of the procedure? (For example liquidated debts, future debts, contingent claims, secured claims, unliquidated claims for damages, interest claims, costs of administration or of legal proceedings, periodical payments, debts owed by guarantors of the business organisation.)

Answer: Under all insolvency procedures, all types of claims with financial value may be admissible for payment. Please note, under

composition and bankruptcy, the secured creditor maintains its right to be paid by the enforcement of its security interest.

(b) Question: At what date are the amounts of admissible debts computed?

Answer: At the date of approval for commencement of the composition or re-organisation proceedings or at the date of bankruptcy declaration, the amounts of admissible debt shall be appraised and computed.

(c) Question: By what method are claims of creditors proven by those creditors in the context of each type of insolvency procedure?

Answer: See below where 1(c) and 1(d) are combined.

(d) Question: How are disputed claims made by creditors adjudicated upon? (For example by the administrator, or by a Court.)

Answer: See below where 1(c) and 1(d) are combined.

Answer: 1(c) and 1(d) combined. In all procedures, the creditors shall report their claims in accordance with the reporting method as provided. The reporting procedure is administrative in nature. The reported claim is then reviewed and may be disputed or denied as set out below.

Composition Procedure: Other creditors, debtors or the administrator may give an objection against other claims. Creditors may prove their claims by any proofs of evidence.

Re-organisation Procedure: The administrator or creditors may give an objection against other claims reported by other creditors, who bring a lawsuit to the Court against the administrator or the creditors in opposition.

Bankruptcy Procedure: Creditors may give an objection against other claims reported by another creditor, and the Court shall judge the disputed claims. The method to prove the claims may be made by any proof or evidence.

2. Priority and payment of creditors' claims

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what principles apply to the division of available assets of the corporate debtor among those of its creditors entitled to payment? Is there a basic principle of equality of payment, or are rights or priority of payment enjoyed by secured creditors, or by certain classes of creditors over others? (For example, costs of the administration, claims for taxes owed by the debtor, amounts owed to employees of the organisation.)*

Answer: See below where 2(a) and 2(b) are combined.

(b) **Question:** *Give a brief account of the order of priorities, if any, of payment of creditors prescribed by the legal system of this country.*

Answer: See below where 2(a) and 2(b) are combined.

Answer: 2 (a) and (b) combined. In Bankruptcy and Composition, the priority of creditor's claims is: (i) secured claims; (ii) priority claims (claims for bankruptcy estate in bankruptcy and general priority claims in composition); and (iii) unsecured claims (bankruptcy claims in bankruptcy and composition claims in composition): Articles 14-15, 38, 40-41 and 84 of the *Bankruptcy Act*, and Articles 42-44 and 60 of the *Composition Act*.

In Re-organisation, the priority claims (i.e. the common benefit claims) generally have priority over secured claims, though there may be exceptions depending on the cases. For example, there was a decision of the Korean Supreme Court that secured claims shall be prior to the common benefit claims with respect to the proceeds from the sale of the specific property secured for the secured creditor: Articles 102, 112, 123-124 and 208-209 of the *Corporate Re-organisation Act*.

In all insolvency procedures, creditors holding the same class of claims shall be treated and paid equally.

Section O – Connection between Debtor and Forum

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what connection must there be between the debtor organisation and the law of the forum? (For example which of the following requirements, if any, must be satisfied in order for an insolvency procedure to be initiated in relation to a corporate debtor in your country:*

- *principal residence of debtor*
- *domicile of the debtor*
- *nationality of the debtor*
- *personal whereabouts at the material time*
- *location of principal place of business*
- *location of place of business, branch or agency*
- *locations of assets of debtor*
- *place where transactions of event took place which gave rise to liability*
- *place where payment, discharge or performance of liability is due to take place.*

Answer: Under Korean law, whether the debtor is a Korean citizen, a legal entity (established in Korea under Korean law and the business is located in Korea), a foreign citizen or a foreign legal entity (established in a foreign country under the law of a foreign country and the business is located outside of Korea), all debtors may ask for the Composition, Re-organisation (corporations only) or Bankruptcy proceedings in Korea. However, the foreigner or the foreign legal entity may ask for the insolvency procedure in Korea if and only if the foreigner's country also allows a Korean citizen or Korean legal entity incorporated in Korea to ask for the insolvency procedure in that foreign country.

Section P – Foreign/Cross-Border Elements

1. Claims of foreign creditors:

- (a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, to what extent are the claims of foreign creditors recognised in the context of administration of that procedure?*

Answer: See below where 1(a), (b) and (c) are combined.

- (b) **Question:** *What principles or rules apply to the recognition and admission of claims by foreign creditors? (for example)*

- (i) *Are claims by foreign creditors subject to particular rules in relation to priority of payment?*
- (ii) *Do foreign creditors have to satisfy special or additional requirements in order for their claims to be admitted?*

Answer: See below where 1(a), (b) and (c) are combined.

- (c) **Question:** *What law is applied to establish the validity of foreign claims?*

Answer: See below where 1(a), (b) and (c) are combined.

Answer: 1(a), (b) and (c) combined. Under the Korean law, the foreign creditors have the same rights as Korean creditors and the foreign creditors are treated equally as the Korean creditors in the Composition, Re-organisation and Bankruptcy proceedings. However, the foreign creditor shall receive such treatment only if the foreign creditor's nation would also provide the same treatment and protection to the Korean creditors in the foreign nation in its Composition, Re-organisation or Bankruptcy proceedings.

We further note that just because the creditor is a foreigner, it does not mean that the foreign creditor will receive any type of preference over the Korean creditors. Both Korean and foreign creditors are treated equally and have equal rights in the insolvency proceedings mentioned above.

2. Jurisdiction over foreign assets:

- (a) **Question:** *To what extent does the insolvency law of this country claim jurisdiction over assets of a corporate debtor situated abroad?*

Answer: If the Composition, Re-organisation or Bankruptcy proceeding is held in Korean Courts in the republic of Korea, only the debtor's assets in Korea may be contemplated by the Court and the debtor's assets located outside of Korea may not be contemplated.

3. Foreign insolvency procedures:

- (a) **Question:** *To what extent do the rules of private international law of the legal system of this country recognise insolvency procedures commenced in foreign jurisdiction?*

Answer: See below where 3 (a) and (b) are combined.

- (b) **Question:** *Under what circumstances, if any, may orders or judgments resulting from foreign insolvency procedures or administrations be recognised or enforced in the legal system of this country?*

Answer: See below where 3 (a) and (b) are combined.

Answer: 3 (a) and (b) combined. If the Composition, Re-organisation or Bankruptcy proceedings have been initiated in a foreign country, the judgement obtained for the foreign Court has no effect on the assets located in Korea. Thus, Insolvency proceedings in a foreign Court may not have any effect on the assets located in Korea.

The IDUIA provides the procedures for the recognition of foreign insolvency procedures. The representative of a foreign insolvency procedure may file an application for recognition with the relevant Korean court. The Korean court shall make a decision on recognition within one month of the date of filing such an application. In this case, the Korean court may render a preservation order prohibiting creditors from enforcing their rights in order to protect creditors' interests and to keep the assets of the debtor company. Upon the decision for the recognition of a foreign insolvency procedure, the representative of the foreign insolvency procedure may participate in, or file a petition for the commencement of, the insolvency procedure in Korea.

4. Foreign insolvency administrators

- (a) **Question:** *What recognition is accorded in the legal system of this country to the status and capacity of insolvency administrators (for example trustees, liquidators, receivers) appointed in foreign insolvency procedures?*

Answer: See below where 4 (a) and (b) are combined.

(b) **Question:** *To what extent are foreign insolvency administrators entitled to claim, take control of, and realise or deal with property of the corporate debtor situated within the jurisdiction of the legal system of this country?*

Answer: See below where 4 (a) and (b) are combined.

Answer: 4 (a) and (b) combined. The capacity of insolvency administrators appointed in foreign insolvency procedures depends on the question of whether, under Korean insolvency laws, the administrator has the authority to administer the assets located in Korea on behalf of the corporate debtor of the foreign insolvency proceedings. The capacity of the insolvency administrator depends on the law of Korea, not the insolvency administrator's country. Therefore, even if the law of the insolvency administrator allows the administrator to administer the assets in Korea, the administrator is not deemed to exercise its authority in Korea on behalf of the corporate debtor unless he or she obtains approval from the competent Korean Court: Article 3 of the *Bankruptcy Act*, Article 11 of the *Composition Act*, and Article 4 of the *Corporate Re-organisation Act*.

Nonetheless, under the IDUIA, after the recognition of a foreign insolvency procedure, the Korean court may render a decision for the support, including the stay of enforcement rights, in order to protect creditors' interests and to keep the assets of the debtor company. Moreover, the Korean court may appoint the foreign insolvency administrator who has the authority to manage the debtor company's assets in Korea.

5. Foreign Security Holders

(a) **Question:** *To what extent does the legal system of this country recognise the validity of rights of security asserted by foreign creditors over assets of the corporate debtor?*

Answer: See Section P, 2.

(b) **Question:** *Are any special rules applicable to determine the validity, extent and ranking of such security rights?*

Answer: See Section P, 2.

6. International conventions

(a) **Question:** *To which international conventions having some application in insolvency matters is this country a party?*

Answer: None.

(b) **Question:** *When were these conventions entered into, and what other states are parties?*

Answer: N/A.

(c) **Question:** *What observations can be made about the practical results achieved under these international instruments?*

Answer: N/A.

7. Cross-border insolvency

(a) **Question:** *Are there any other particular issues or special problems in the field of cross-border insolvency, not included in the answer supplied above, which have presented themselves before the Courts of the legal system of this country.*

Answer: No.

8. UNCITRAL Model Law on Cross-Border Insolvency

(a) **Question:** *Is the government of this country aware of the UNCITRAL Model Law on cross-border insolvency, approved by the United Nations in June 1997?*

Answer: Yes.

Section Q – New Developments

(a) **Question:** *Are there any recent, imminent or proposed legislative, administrative, or practical reforms or developments or proposals in the legal system of this country which impact upon the matters mentioned above?*

Answer: Recently, the Korean government announced the IDUIA, which consolidates the *Bankruptcy Act*, the *Corporate Re-organisation Act* and the *Composition Act*. There was a public hearing about the IDUIA on November 6, 2002. It is reported that the Ministry of Justice of the Korean government will finalise the final draft of the Unified Insolvency Act after gathering comments and opinions on the IDUIA, and submitting the bill to the Korean National Assembly.

Addendum to Report on Korea

Addendum to Report on Korea – produced under Asian Development Bank Technical Assistance No. 5795 – REG

B. Insolvency Reforms

1. **Question:** Provide details of any reforms that have occurred in relation to insolvency law and practice and related areas (such as corporate governance, secured transactions and so forth) since January 1999.

Answer: The *Corporate Re-organisation Act* was amended in December 1999 (effective since April 2000). The *Bankruptcy Act* and the *Composition Act* were amended in January, 2000. These amendments are purported to expedite and enhance the efficiency of the insolvency procedures.

In April 2001, the *Corporate Re-organisation Act* was amended again with the introduction of the pre-packaged re-organisation plan scheme. As explained above, the Ministry of Justice recently announced the IDUIA.

2. **Question:** Provide details of any proposed reforms as above.

Answer: The main aspects of the IDUIA are summarised and set out below.

With respect to the rehabilitation procedures:

- Elimination of Composition proceedings and consolidation with Re-organisation into Rehabilitation proceedings.
- Introduction of the Comprehensive Temporary Stay - (Under current law, during the period between the filing of a petition for the Re-organisation proceedings and the commencement decision, the debtor company is allowed to file an application for a temporary stay on a specific creditors' enforcement right. Under the IDUIA, the Court may render a decision for the Comprehensive Temporary Stay, which will apply to all creditors' enforcement rights).
- More protection for creditors' rights, such as providing broader roles for the Creditors' Council and guaranteeing liquidation value for creditors.
- More expeditious proceedings by reducing the period for the decision of preservation order and the period for the resolution for the creditor's approval of the Rehabilitation Plan.

- In principle, there is to be no replacement of the management of the debtor company, i.e. the Court is supposed to appoint the existing management as the receiver/administrator of the Re-organisation proceedings.

With respect to the introduction of cross-border insolvency:

- See also Section P, 3 and Section P, 4.

G. Insolvency law

1. **Question:** What are the major substantive defects in the corporate insolvency law viewed from the respective positions of:

- (a) banks/financial providers;
- (b) secured creditors;
- (c) unsecured creditors;
- (d) employees;
- (e) corporations;
- (f) directors; and
- (g) shareholders?

Answer: In re-organisation, the priority between secured claims and common benefit claims is not clear.

In bankruptcy, it is generally the view of unsecured creditors that the limitless priority of tax claims, including the delinquent amount, over unsecured claims is excessive.

In re-organisation, the Court's cease order for stays of execution proceedings is not comprehensive, but rather is rendered with respect to individual cases only.

In re-organisation, existing management, i.e. the representative director, is afraid that he or she would not be appointed as one of the receivers, and could thereby lose the opportunity to contribute to the company's rehabilitation.

2. **Question:** What are the major practical defects in the application of the insolvency law viewed from the respective positions of:

- (a) corporations; and
- (b) creditors?

Answer: Debt researching conditions are too strict and too deep. The process for recovery, especially the preservative measure aspect of the process, is too slow. It is also necessary to prevent corporations from using insolvency laws to cover up faltering or shrinking liabilities. This could be done by preventing them from applying more strict processes of rejection in any one process.

H. Judicial System

- Question:** *Has there been any discernible improvement or change in the operation of the judicial system in relation to the conduct of:*
 - debt collection/ debt recovery processes;*
 - enforcement processes in respect of secured property rights;*
 - recovery or enforcement processes in respect of leased property; and*
 - formal corporate insolvency processes?*

If possible, provide some detail of cases in which any such change or improvement has been made apparent.

Answer: See Section B of Addendum.

- Question:** *What reforms, if any, have been made to improve the operation of the judicial system in relation to the above 4 areas?*

Answer: See Section B of Addendum.

- Question:** *Are there any identifiable proposals for reforms in these areas?*

Answer: There are proposals for a unified insolvency law in the form of IDUIA.

- Question:** *What are the main problems or difficulties regarding the operation and application of the corporate insolvency law through the Court system?*

Answer: Although judges' expertise has been substantially improved, there is still an insufficient number of expert judges.

- Question:** *What practical improvements might be made to overcome these problems/ difficulties?*

Answer: Specialisation of the Court.

J. Insolvency Administration System

- Question:** *Comment on the extent of development, expertise and efficiency regarding both public and private sector administration of formal cases of:*
 - corporate liquidation; and*
 - corporate re-organisation*

Answer: There are a lack of specialists in the field of insolvency. There will be a loss of efficiency and flexibility since the people who manage insolvent companies are a small number of judges responsible for the insolvency cases, as well as other burdensome cases.

- Question:** *Is it considered that education and training in these areas would be valuable and, if so, in what areas?*

Answer: There must be an increase in the number of lawyers and relevant government officials. There is also a need to utilise experts by expanding the pool of bankruptcy trustees and receivers.

- Question:** *Is it considered desirable to introduce more formal structures of both public and private sector administration of insolvency cases?*

Answer: It is necessary to maintain the relevant legislation and the Court's relevant organisation, but there seems no necessity for the installation of a separate apparatus.

L. General Insolvency Information and Developments

- Question:** *Provide details of any other relevant information or developments since January 1999 in regard to such issues as the effect of insolvency law policies on areas such as employment, fiscal/revenue debts, detection and recovery of corporate fraud, domestic and foreign investment and etc.*

Answer: In order to facilitate mergers and acquisition/s of the companies in re-organisation, the Seoul District Court enacted the Guidelines on mergers and acquisition/s of the Companies under Re-organisation. These guidelines were introduced on 31 January 2000, and amended on 9 October 2001. They provide procedures and requirements for and mergers and acquisition/s of re-organisation companies. In 2002, most District Courts enacted such guidelines similar to that of Seoul District Court.

2. **Question:** *Is there any evidence of a change in attitudes (such as social commercial stigma, aversion to strict legal processes, fear of loss of control) toward the use of:*

- (a) formal insolvency processes; and
- (b) informal insolvency processes

in respect of corporations in financial difficulty or insolvent corporations? If possible, provide details of any specific cases which might reflect evidence of change.

Answer: From our experiences and observation, if possible, debtor companies and the management generally prefer informal work-out processes rather than formal Court receivership (re-organisation), mainly because existing management have been replaced with a Court appointed receiver in re-organisation, whereas existing management have not been so frequently changed in informal work-outs. For the past four years, the insolvent companies usually tried to go to informal - first. They eventually went to re-organisation or composition proceedings, but only after such efforts failed.

B. The efficiency of the administration of justice in the participating countries

Question: *Some of the sections in the Report and the Addendum to that Report referred to in A above also address the administration of justice in Korea. Please advise as to the extent to which the Report and the Addendum to that Report are accurate in this respect and also advise of any amendments or modifications which should be made to those aspects of the Report or the Addendum to that Report.*

Answer: Among the issues raised in the 5795 Report, the problem of the lack of specialists in the field of insolvency and the heavy work loads of judges have been significantly resolved as compared to the circumstances of a few years ago.

C. Treaty

1. **Question:** *To what regional treaties providing for economic cooperation or designed for the facilitation of trade is Korea a party?*

Answer: As far as we understand "regional treaty" is a treaty entered into by and among three or more countries within a certain region.

Excluding a bi-lateral treaty and a multilateral treaty like the Agreement of the World Trade Organisation, Korea has not been a party to a regional treaty for the economic cooperation or facilitation of trade.

Therefore, questions 2 through to 8 (listed below for reference purposes) are not applicable.

- 2. **Question:** *What are the terms of those treaties?*
- 3. **Question:** *What are the mechanisms for amending those treaties?*
- 4. **Question:** *Can a signatory to those treaties reserve its position in respect of any amendment with a right to "opt in" either generally or with a prescribed period of time?*
- 5. **Question:** *Do those treaties provide for resolution of trade or other disputes?*
- 6. **Question:** *Do those treaties otherwise provide for a collaborative approach to addressing issues of mutual interest?*
- 7. **Question:** *Do those treaties provide for an exchange of information on issues of mutual interest?*
- 8. **Question:** *Do any of those treaties address the harmonisation of laws which may effect economic relations between member countries? If so, what are the relevant treaties and stipulations contained in them?*

D. Actual outbound cross-border cases

1. **Question:** *In the course of the last five years, are you aware of there having been any companies which were incorporated in Korea which have been placed under some formal insolvency administration and which have had assets and/or liabilities in countries other than Korea? If so, please identify those companies.*

Answer: There are a few insolvent companies which have had assets/liabilities in countries other than Korea. Typical examples are Daewoo Motors, Kia Motors, Jinro, Dong-Ah Constructions, Korea Express, SKM, and Medison.

2. **Question:** *In the case of each of those companies, are you aware of how those non-Korean assets and liabilities were administered? If so, in each case, please provide a general description of the process of administration*

Answer: Assets in foreign countries are excluded from Korea's insolvency procedures. In other words, the assets in foreign countries are not included in the insolvent company's assets. Liabilities to foreign creditors have been treated equally with domestic liabilities, while the liabilities of foreign subsidiaries of Korean insolvent companies have also been excluded from the insolvent procedures in Korea.

See also Section P of the 5795 Report.

In this regard, there were a few exceptional cases with respect to the administration of Korean companies' foreign assets and liabilities. For example, Daewoo Motors had assets in the form of a research institute, as well as liabilities in the UK. The Korean receiver (administrator) of Daewoo Motors, appointed by the Korean Court, requested the relevant Court of the UK to commence the bankruptcy procedures against the research institute in the UK, and thereby distribute the proceedings from the procedure to the Korean receiver. The Court of the UK commenced the bankruptcy proceedings on the condition that the Korean Court would accord UK creditors treatment that was no less favourable than that which it accorded to Korean creditors. The UK liquidator currently holds the proceeds of the sales of the assets in the amount of US\$4 million. The Korean receiver would like to proportionally distribute the proceeds to the UK creditors, but the UK liquidator will not transfer the money to the Korean receiver without the UK Court's approval to do so.

3. **Question:** *In the case each of those companies and so far as you are aware, were Korean creditors permitted to file their claims in the formal insolvency administration being conducted in Korea? In any case, were any those non-Korean creditors required to obtain a judgment in the Courts of Korea or otherwise undertake any formal procedure in Korea as pre-requisite to filling their claims?*

Answer: Non-Korean creditors have been permitted to file their claims in the formal insolvency administration conducted in Korea. No additional procedure or judgments are required as a pre-requisite for foreign creditors to file their claims.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Korean creditors exercise their rights by pursuing claims against the non-Korean assets of the company? If so was there any procedure or process*

either available to or invoked by the insolvency administrator of those companies in Korea to restrain them from doing so?

Answer: Non-Korean creditors may exercise their rights by pursuing claims against the non-Korean assets of the insolvent company. In general, under the current Korean insolvency laws, there is no procedure available to the insolvency administrator of a Korean insolvent company to restrain the foreign creditors from enforcing their rights. Nevertheless, we were told that there was a case in which a Korean insolvency administrator sought the cooperation of the Japanese Court for the resolution of Korean company vessels detained by Japanese creditors, and that such efforts were successful.

E. Actual inbound cross-border cases

1. **Question:** *In the course of the last five years, are you aware of there having been any cases of companies which were incorporated other than in Korea which have been placed under some form of insolvency administration and which have had assets and/or liabilities in Korea? If so, please identify those companies.*

Answer: In L&H, Korea's bankruptcy case, L&H, incorporated in Belgium and the mother company of L&H Korea and its US branch were in bankruptcy proceedings in their respective jurisdictions.

2. **Question:** *In the case of each of those companies, are you aware of how its assets and liabilities in Korea were administered? If so, in each case, please provide a general description of the process of administration*

Answer: L&H filed a petition for the bankruptcy procedure against L&H Korea with the Korean Court, and L&H Korea was liquidated under Korean Bankruptcy Act.

3. **Question:** *In each case and so far as you are aware, in the case of Korean creditors, were they permitted to file their claims in the formal insolvency administration of the company being conducted in its place of incorporation?*

Answer: Yes.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Korean creditors exercise their rights by pursuing claims against the non-Korean assets of the company? If so was there any procedure or process either available to or invoked by the insolvency administrator of the company in its place of incorporation to restrain those creditors from doing so?*

Answer: Korean creditors may exercise their rights by pursuing claims against the Korean assets of the assets of foreign company's branch or its Korean subsidiary. Under Korean law, there is no procedure available to the insolvency administrator of the foreign company to restrain the Korean creditors from enforcing their rights.

F. Hypothetical inbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in Singapore and trades through a branch in Korea with the result that it has assets and liabilities there. ABC is ordered to be wound up by order of the Singaporean Courts and liquidator is appointed to administer its affairs. The liquidator wishes to take control of and administer the assets of ABC in Korea or alternatively, arrange for their administration. She also wishes to arrange for all creditors of ABC, whether resident in Singapore, in Korea or else where, to file their claims in Singapore so that those claims can be dealt with equitably and consistently.

Assuming that there is presently no procedure in Korea for recognising the liquidation of ABC in Singapore.

1. **Question:** *What procedures can be invoked in Korea for placing ABC under a formal insolvency administration?*

Answer: There are no procedures in Korea that may be invoked to place ABC under a formal insolvency administration. However, Bankruptcy and Composition proceedings may be invoked in order to place the ABC's branch, as well as ABC's subsidiary in Korea under formal insolvency administration. If ABC's Korean subsidiary is a joint stock company (Chusik Hoesa), then it may also be subject to the Re-organisation proceedings in Korea.

2. **Question:** *In the case of each of those procedures, does the Singaporean appointed liquidator have standing to initiate the necessary application? If not, then in the case of each procedure in which the Singaporean appointed liquidator does not have that standing, who does have standing?*

Answer: No.

3. **Question:** *In the case of each procedure, to whom is the necessary application made for an order or direction establishing a formal insolvency administration?*

Answer: The necessary application is made to the District Court having jurisdiction over the main office of the debtor company's Korean subsidiary or branch.

4. **Question:** *In the case of each procedure, how long does it typically take to obtain an order or other direction establishing a formal insolvency administration?*

Answer: An order or other direction will be obtained within one month of the filing of the petition for the commencement of respective procedure.

5. **Question:** *In the case of each procedure, is it possible to obtain some interim or other like order or direction which secures the independent control of the assets of ABC in Korea pending the final determination of the application for an order or other direction establishing a formal insolvency administration?*

Answer: Yes. The Court may, upon the debtor company's application or in its discretion, render a preservation order and/or the order of temporary stay on the creditors' specific rights.

6. **Question:** *In the case of each procedure, what does it typically cost to obtain a final order or direction establishing a formal insolvency administration?*

Answer: There are variations depending on the size of the debtor company. However, the cost will normally be between US\$ 30,000 and US\$ 100,000, including legal fees.

7. **Question:** *In the case of each procedure, to what extent do the Korean creditors enjoy priority to or precedence over non-Korean creditors in the context of that procedure?*

Answer: Korean creditors and foreign creditors are treated equally, and therefore have equal rights in the insolvency proceedings.

8. **Question:** *In the case of each procedure, may the Singaporean and other non-Korean creditors of ABC file their claims in the formal insolvency administration established under that procedure? If so, what formal procedures or other pre-requisites have to be satisfied by those creditor prior to them filing their claims?*

Answer: Yes. There is no pre-requisite required for the filing of claims by non-Korean creditors.

G. Hypothetical outbound cross-border insolvency case

Assume that ABC Limited (“ABC”) is incorporated in Korea and trades through a branch in Singapore with the result that it has assets and liabilities in Singapore. ABC is placed under a formal administration in Korea and an independent trustee is appointed to administer its affairs.

1. **Question:** *Is there any procedure available in Korea which will facilitate an application to the Courts in Singapore for the establishment of an independent insolvency administration of ABC?*

Answer: No.

2. **Question:** *If so, please describe that procedure.*

Answer: N/A

3. **Question:** *Does the fact that the principal insolvency administration of ABC is initiated in Korea as distinct from the insolvency administration of a company's branch affect the answers to F7 or F8?*

Answer: No.

Supplementary Questions

1. **Question:** *To what regional inter-governmental arrangements relating to economic corporation, facilitation of trade, investment protection, or mutual recognition of administrative or judicial process is the subject country a party? (Such arrangements might include regional treaties, non-treaty agreements, cooperative schemes, or regular forums at the ministerial or official level.)*

Answer: Korea is a member to the Asia-Pacific Economy Cooperation (APEC).

2. **Question:** *Which (if any) are the other countries that are party to such arrangements.*

Answer: Australia, Brunei, Darussalam, Canada, Chile, People's Republic of China, Hong Kong, China, Indonesia, Japan, Republic of Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, Chinese Taipei, Thailand, United States, Viet Nam

3. **Question:** *Does any such arrangement refer to and deal with insolvency, either specifically or within the generality its terms?*

Answer: As far as we are aware, insolvency issues have not been significantly discussed in APEC thus far.

4. **Question:** *Which ministry or agency has or would have responsibility for negotiating and administering arrangements on mutual recognition in the field of insolvency?*

Answer: The Ministry of Justice



Asian Development Bank

Promoting Regional Cooperation in the Development of Insolvency Reform

RETA 5975

Draft Country Report for Singapore Conference Cross-Border Insolvency

Philippines

A. The provisions

The provisions of the existing insolvency laws of the participating countries as well as any proposed reforms.

1 **Question:** Please advise as to the extent to which the materials in Section I, J, K, L, O, P and Q of the Report and Sections B, G, H, J and L of the Addendum to that Report continue to be accurate. If those sections of the Report and the Addendum to that Report require amendment or modification, please advise of the amendments or modifications.

Report on Philippines – produced under Asian Development Bank Technical Assistance No. 5795 – REG

Answer: See below.

Section I – Insolvency Law Regime

Introduction

There are two principal laws available to a corporation seeking debt relief. These are:

- the Insolvency Law, and
- Presidential Decree No. 902, as amended.



1. The Insolvency Law

The Insolvency Law deals with three (3) principal subjects, namely: suspension of payments; voluntary insolvency; and involuntary insolvency. In accordance with the provisions of the Insolvency Law: "every insolvent debtor may be permitted to suspend payments or be discharged from his debts and liabilities". Corporate debtors however are not given a discharge.

The venue for all proceedings under the Insolvency Law since its enactment in 1909 have been vested exclusively in the regular courts. The economic turmoil in the Philippines that began to brew in 1979 due to anomalies and irregularities which caused the collapse of many corporations, created the need for an agency that would be able to handle proceedings under the Insolvency Law with more efficiency and dispatch. At the same time, a rehabilitation procedure for corporations was needed. It was felt that the logical agency to handle this was the Securities and Exchange Commission (the "SEC"), and once it is given quasi-judicial powers, it could probably act faster than the regular courts.

2. Presidential Decree No. 902-A, as amended ("PD 902-A")

In 1981, a Presidential Decree was issued (PD No. 1758, amending P.D. 902-A). This Presidential Decree vested in the SEC, the administrative agency charged with implementing the laws affecting corporations and partnerships, jurisdiction over petitions for suspension of payments. In addition, the SEC was vested with the power to appoint, upon petition or *motu proprio*, a rehabilitation receiver, or a management committee, for partnerships, corporations and associations in distress. Upon the appointment of such, all actions for claims against the said partnerships, corporations or association would be suspended. The SEC was further granted authority to evaluate the feasibility of continuing operations and of restructuring and rehabilitating such entities. Jurisdiction over petitions for voluntary and involuntary insolvency is still lodged with the courts and has not been transferred to the SEC.

For the past two decades, corporations filed their debt relief petitions with the SEC, either by way of:

- a petition for suspension of payments where the debtor possesses sufficient assets to cover all its debts, but foresees the impossibility of meeting them, with a request for the appointment of a management committee or rehabilitation receiver; or
- a petition for suspension of payments where the corporation does not have sufficient assets

to cover its liabilities, accompanied with a request for the appointment of a management committee or rehabilitation receiver.

The petition for suspension of payments, coupled with the appointment of a rehabilitation receiver or management committee, is what is generally referred to as rehabilitation proceedings in the Philippines. The SEC approved the Rules of Procedure on Corporate Recovery which took effect on 15 January 2000. The Rules were intended to rationalise the procedure on corporate rehabilitation and suspension of payments, and explicitly provide for an independent action for rehabilitation i.e. separate from a proceeding for suspension of payments.

However, on 19 July 2000, Congress enacted the Securities Regulation Code ("SRC"). In Article 5.2, the SRC transferred jurisdiction from the SEC to the regular courts over cases enumerated in Section 5 of PD 902-A (including suspension of payments and rehabilitation cases), and allowed the Supreme Court to designate branches of the Regional Trial Courts ("RTC") to hear and decide cases of such nature. Pursuant to the SRC, the Philippine Supreme Court, under designated certain branches of the RTC, is able to hear and decide cases that used to be under the jurisdiction of the SEC. The Supreme Court also promulgated the Interim Rules of Procedure on Corporate Rehabilitation (the "Interim Rules") to govern the procedure for rehabilitation cases filed with the RTC. The Interim Rules took effect in December 2000. Unlike the SEC Rules on Corporate Recovery, the Interim Rules do not contain provisions for simple suspension of payments. It is believed that the rules of procedure for suspension of payments provided under the Insolvency Law will apply to corporations.

1. Underlying philosophy:

(a) **Question:** *What is the underlying philosophy of the insolvency law of this country? (For example is it distributive, rehabilitative or penal?)*

Answer: The Insolvency Law is both distributive and rehabilitative. In the case of *In Re: Estate of Mindanao Motor Line, Inc.* [57 SCRA 103], the Supreme Court declared: "...the purpose of the filing of the petition was other than the purpose for which the Insolvency Law was enacted, which is to effect an equitable distribution of the bankrupt's properties among his creditors and to benefit the debtor by discharging him to start afresh with the property set apart for him as exempt."

Under the Insolvency Law, discharge is available to an individual insolvent, but not to a corporation. The provisions of the Insolvency Law on the classification and preference of credits, which has since been amended by the Civil Code and the Labour Code, provides a scheme for a fair distribution of the assets of the insolvent to its creditors.

The underlying philosophy of PD 902-A, especially as implemented by the SEC and the Supreme Court, is rehabilitative.

(b) Question: *Are there elements of more than one philosophy present in the insolvency law of this country?*

Answer: Yes.

(c) Question: *Briefly describe the relevant elements, and if applicable, any penal sanctions available.*

Answer: In the Philippines, no person shall be imprisoned for debt: Section 20, Article III, Constitution. The penal provisions of the Insolvency Law (Section 70 to 71), and the Revised Penal Code (Article 314), punish the commission of fraud by the insolvent and not the non-payment of the debt. For a more detailed discussion of the acts punished under these laws, see Section K2 (a).

2. Jurisdiction in insolvency matters:

(a) Question: *In which judicial category is insolvency law classified in the legal system of this country? (For example civil, commercial or administrative.)*

Answer: The insolvency law may be classified as part of the civil and commercial laws of the Philippines. Under Article 2237 of the Civil Code, "insolvency shall be governed by special laws insofar as they are not inconsistent with this Code." The special law is Act No. 1956, as amended, also known as the Insolvency Law.

The SRC which transferred the jurisdiction over debt relief cases involving corporations from the SEC to the regular courts, being a law passed by Congress, is more in the nature of civil or commercial law.

(b) Question: *Which Courts, tribunals or administrative bodies in this country are competent to exercise jurisdiction in insolvency matters?*

Answer: The regular courts have original and exclusive jurisdiction over all petitions for voluntary and involuntary insolvency for all debtors. The SRC transferred jurisdiction over petitions for rehabilitation and suspension of payments filed by corporations to the regular courts, specifically, the RTC.

(c) Question: *Are any limitations placed on the jurisdiction of any of these bodies?*

Answer: While the SRC transferred jurisdiction over rehabilitation/suspension of payments cases to the RTC, the same law expressly provides that the SEC retains jurisdiction over pending suspension of payments/rehabilitation cases pending therewith as of 30 June 2000 until they are finally disposed of.

3. Types of insolvency procedures

(a) Question: *What types of insolvency procedure are available in the legal system of this country for the administration of corporate debtors in financial difficulty? (For example bankruptcy, liquidation (winding up), receivership, restructuring or other forms of administration.)*

Answer: There are three types of actions available under the Insolvency Law. These are:

- suspension of payment where the debtor possesses sufficient property to cover all his debts;
- voluntary insolvency; and
- involuntary insolvency.

Under PD 902-A, as implemented by the Interim Rules, any debtor who foresees the impossibility of meeting its debts when they respectively fall due, or any creditor or creditors holding at least 25% of the debtor's total liabilities, may petition the proper RTC to have the debtor placed under rehabilitation.

(b) Question: *Briefly describe the main features of each type of insolvency procedure for corporate debtors, including, for example the manner in which each procedure is initiated and administered, and the aims of each procedure.*

Answer: Suspension of Payments:

A suspension of payments suspends or delays the payment of debts, the amount of which is not affected, although a postponement is declared. The basis is the probability of the debtor's inability to meet his obligations when they respectively fall due, despite the fact that he has sufficient assets to cover all his liabilities. Under the Insolvency Law (note that all references to Sections are to the Insolvency Law), the steps in the suspension of payments are:

- Filing of the petition by the debtor (Section 2);
- Issuance by the court of an order calling a meeting of creditors (Section 3);

- Publication of the order and service of summons (Section 4);
- Meeting of creditors for the consideration of the debtor's proposition (Ibid);
- Approval by majority of the creditors of the debtor's proposition where it is necessary that:
 - (a) two-thirds of the creditors voting unite upon the same proposition; and
 - (b) the claims represented by said majority vote amount to at least three-fifths of the total liabilities of the debtor mentioned in the petition;
- Objections, if any, to the decision which must be made within ten (10) days following the meeting (Section 11);
- Issuance of order by the court directing that the agreement be carried out in case the decision is declared valid, or, when no objection to said decision has been presented (Ibid); and
- If the decision of the meeting be negative, the proceedings shall be terminated and the creditors shall be at liberty to enforce the rights which may correspond to them¹.

There is an unresolved issue of whether the procedure set forth in the Insolvency Law for suspension of payments as aforesaid will apply to simple suspension of payments cases filed by corporations. It is believed that the same should apply as the Interim Rules did not provide for rules of procedure to govern proceedings for suspension of payments for said entities.

Voluntary Insolvency:

The following steps constitute the proceedings for voluntary insolvency (note that all references to Sections are to the Insolvency Law):

- Filing of the petition by the debtor praying for the declaration of insolvency (Section 14);
- Issuance of an order of adjudication declaring the petitioner insolvent (Section 18);
- Publication and service of the order (Section 19);
- Meeting of the creditors to elect the assignee in insolvency (Section 30);
- Conveyance of the debtor's property by the clerk of court to the assignee (Section 32);
- Liquidation of the debtor's assets and payment of his debts (Section 33); and
- Composition, if agreed upon (Section 63).

Involuntary Insolvency:

The following steps constitute the proceedings

for involuntary insolvency (note that all references to Sections are to the Insolvency Law):

- Filing of the petition by three or more creditors (Section 20);
- Issuance of order requiring the debtor to show cause why he should not be adjudged insolvent (Section 21);
- Service of order to show cause (Section 22);
- Filing of answer or motion to dismiss (Section 23);
- Hearing of the case (Section 24);
- Issuance of order or decision adjudging debtor insolvent (Ibid.);
- Publication and service of order (Section 7);
- Meeting of creditors for election of an assignee in insolvency (Section 30);
- Conveyance of debtor's property by clerk of court to the assignee (Section 32);
- Liquidation of assets and payments of debts (Section 33); and
- Composition, if agreed upon (Section 63).

Rehabilitation under the Interim Rules:

The general procedure for rehabilitation proceedings under the Interim Rules is as follows:

- Filing of the petition with the appropriate RTC;
- If the court finds the petition sufficient in form and substance, it will issue a stay order not later than 5 days from the filing of the petition which, among others, shall also appoint a rehabilitation receiver for the petitioning debtor; stay all actions for claims against the debtor, set an initial hearing for the petitioners and direct the creditors and other interested parties to file their verified comment on or opposition to the petition not later than 10 days before the initial hearing and putting them on notice that their failure to do so would bar them from participating in the proceedings;
- Publication of the stay order in a newspaper of general circulation in the Philippines once a week for two consecutive weeks;
- Initial hearing on the petition not earlier than 45 days but not later than 60 days from the filing of the petition;
- If the court finds merit in the petition, it will refer the rehabilitation plan to the rehabilitation receiver who shall submit his recommendations thereon to the court not later than 120 days from the initial hearing of the petition;

¹ De Leon, Credit Transactions (1999) at p476.

- Meeting/s between the debtor and/or the rehabilitation receiver with the creditors and other interested parties, which should take place before the final version of the plan prior to its final submission to the court for approval;
- Modification or revision (if necessary) by the debtor of the rehabilitation plan in the light of the comments, opposition or discussion with the rehabilitation receiver, creditors and other interested parties;
- Submission of a final rehabilitation plan to the court for its approval; and
- Approval/disapproval of the rehabilitation plan by the court.

(c) Question: *Identify the relevant legislation governing each type of insolvency procedure available for corporate debtors.*

Answer: The relevant legislation governing each type of insolvency procedure available for corporate debtors are the following:

- Suspension of Payments – the Insolvency Law and PD 902-A.
- Voluntary Insolvency – primarily covered by Sections 14 to 19 of the Insolvency Law. Other provisions of the Insolvency Law are also applicable, particularly those on the appointment, powers and duties of the assignee.
- Involuntary Insolvency – primarily covered by Section 20 to 28 of the Insolvency Law. Other provisions of the Insolvency are also applicable, particularly those on the appointment, powers and duties of the assignee.
- Petition for Rehabilitation – PD 902-A as implemented by the Interim Rules.

4. Commencement of insolvency procedure:

(a) Question: *Is it usual or customary in respect of a corporate debtor which is insolvent to attempt to negotiate an informal administration before formal insolvency procedures are commenced?*

Answer: Yes. It is usual or customary in respect of an insolvent corporate debtor to attempt to negotiate an informal administration before formal insolvency procedures are commenced.

(b) Question: *In relation to each type of insolvency procedure available in the legal system of this country, who may commence the procedure? (For example the corporate debtor, secured creditors, unsecured creditors, shareholders, the State.)*

Answer:

- For Suspension of Payments: by the debtor (Section 2, Insolvency Law).
- For Voluntary Insolvency: by the debtor (Section 14, Ibid.).
- For Involuntary Insolvency - by three or more creditors, residents of the Philippines, whose credits or demands are accrued in the Philippines, and the amount of which credits or demands are in the aggregate not less than one thousand pesos, provided that none of the said creditors has become a creditor by assignment, however made, within 30 days prior to the filing of the petition. (Section 20, Ibid.).
- For Petitions for Rehabilitation – by any debtor who foresees the impossibility of meeting its debts when they respectively fall due, or any creditor or creditors holding at least 25% of the debtor's total liabilities (Section 1, Rule 4 of the Interim Rules).

(c) Question: *On what basis may each type of insolvency procedure be commenced, or what requirements must be satisfied before the procedure may be commenced? (For example non-payment of debts; balance sheet/cash flow insolvency; trading losses; resolution by directors to enter insolvency procedure.)*

Answer: The following insolvency procedures may be commenced by:

- Suspension of Payments – under the Insolvency Law, this is commenced by the filing of a petition, which shall annex a schedule of the corporation's assets and liabilities, and the proposed agreement it requests of its creditors.
- Voluntary Insolvency – commenced by the filing of a petition which shall be accompanied by a verified schedule and inventory by a duly authorised officer of the Corporation. Liabilities must exceed P1,000. The officer of the corporation must be duly authorised by the vote of the board of directors, at a meeting specially called for that purpose, or by the assent in writing of a majority of the directors, as the case may be (Section 56, Insolvency Law).

- Involuntary Insolvency – commenced by the filing of a petition by three or more qualified creditors. The petition must allege that the debtor is guilty of at least one of the following acts of insolvency:
 - that such person is about to depart or has departed from the Philippines, with intent to defraud his creditors;
 - that being absent from the Philippines, with intent to defraud his creditors, he remains absent;
 - that he conceals himself to avoid the service of legal process for the purpose of hindering or delaying or defrauding his creditors;
 - that he conceals, or is removing, any of his property to avoid its being attached or taken on legal process;
 - that he has suffered his property to remain under attachment or legal process for three days for the purpose of hindering or delaying or defrauding his creditors;
 - that he has confessed or offered to allow judgment in favour of any creditor or claimant for the purpose of hindering or delaying or defrauding any creditor or claimant;
 - that he has wilfully suffered judgment to be taken against him by default for the purpose of hindering or delaying or defrauding his creditors;
 - that he has suffered or procured his property to be taken on legal process with intent to give a preference to one or more of his creditors and thereby hinder, delay or defraud any one of his creditors;
 - that he has made any assignment, gift, sale, conveyance, or transfer of his estate, property, rights, or credits with intent to delay, defraud, or hinder his creditors;
 - that he has, in contemplation of insolvency, made any payment, gift, grant, sale, conveyance, or transfer of his estate, property, rights, or credits;
 - that being a merchant or tradesman he has generally defaulted in the payment of his current obligations for a period of thirty days;
 - that for a period of thirty days he has failed after demand, to pay any moneys deposited with him or received by him in a fiduciary capacity; and
 - that an execution having been issued against him on final judgment for money, he shall have been found to be without sufficient property subject to execution to satisfy the judgment. (Section 20, Insolvency Law).
 - Petition for Rehabilitation – The petition filed by the debtor must be verified and must set forth with sufficient particularity all the following material facts:
 - the name and business of the debtor;
 - the nature of the business of the debtor;
 - the history of the debtor;
 - the cause of its inability to pay its debts;
 - all the pending actions or proceedings known to the debtor and the courts or tribunals where they are pending;
 - threats or demands to enforce claims or liens against the debtor; and
 - the manner by which the debtor may be rehabilitated and how such rehabilitation may benefit the general body of creditors, employees and stockholders.
 - The petition shall also be accompanied by the following documents:
 - audited financial statements and interim financial statements;
 - schedule of debts and liabilities;
 - inventory of assets;
 - rehabilitation plan;
 - schedule of payments and disposition of assets;
 - schedule of cash flow;
 - statement of possible claims;
 - affidavit of general financial condition;
 - at least 3 nominees for the position of rehabilitation receiver;
 - certificate attesting to the fact that the filing of the petition has been approved, among others; and
 - verification from the debtor that the aforementioned documents contain full, correct and true statements, among others.
- If the petition is filed by a creditor or creditors, it is sufficient that the petition is accompanied by a rehabilitation plan, and a list of nominees to the position of rehabilitation receiver, and verified by a sworn statement that the affiant has read the petition and that its contents are true and correct of his personal knowledge, or based on authentic records obtained from the debtor.

(d) **Question:** *How is each type of insolvency procedure commenced? (For example by application to the Court, by administrative act, by written notice to the business organisation.)*

Answer: See Section 14(c).

(e) **Question:** *What is the usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor?*

Answer: The usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor is usually as follows:

- Suspension of Payments – there is no period in the Insolvency Law for the termination of suspension of payments proceedings. Based on our experience, such proceedings on average take around 2 to 3 years until finally resolved. Note, however, that Section 6 of the Insolvency Law provides for a period of 3 months by which the debtor shall force an agreement with the creditors, otherwise the suspension order is automatically lifted.
- Voluntary Insolvency/Involuntary Insolvency – the Insolvency Law provides that a debtor may apply for a discharge at any time after the expiration of 3 months from the adjudication of insolvency, but not later than one year from such adjudication, unless the property of the insolvent has not been converted into money without his fault. However, in actual practice, petitions for insolvency, whether voluntary or involuntary, usually exceed the one year period provided under the Insolvency Law.
- Rehabilitation – Under the Interim Rules, the petition shall be dismissed if no rehabilitation plan is approved by the court upon the lapse of 180 days from the date of initial hearing. It is likewise provided that in no instance shall the period for approving or disapproving a rehabilitation plan exceed 18 months from the date of filing of the petition.

(f) **Question:** *How effective is the judicial or court system (or administrative system) in relation to the handling of formal insolvency proceedings?*

Answer: There are still complaints on how the regular courts are handling insolvency proceedings, but the special training seminars and workshops given by the Philippine Judicial Academy to judges are starting to bear fruit.

5. Effect of insolvency procedures:

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this country, what is the effect on the corporate debtor, its constituent parts and its business relationships of the initiation of the relevant insolvency procedure?*

For example: how does initiation of the insolvency procedure affect:

(i) *the powers of management of the debtor:*

Answer:

- Suspension of Payments – the corporation will continue to be managed by its directors and officers. The Insolvency Law does not provide for the appointment of a receiver for simple suspension of payments proceedings.
- Voluntary Insolvency – the corporation will continue to be managed by its directors and officers until the appointment of a receiver or an assignee.
- Involuntary Insolvency – the petitioning creditors will most likely request to the court that the present management be changed immediately upon the filing of the petition for the protection of the creditors' interest.
- Rehabilitation – assuming the court finds the petition to be sufficient in form and substance, the court will appoint a rehabilitation receiver not later than 5 days from the filing of the petition. The rehabilitation receiver shall closely oversee and monitor the operations of the debtor during the pendency of the proceedings, primarily to ensure that the value of the debtor's property is reasonably maintained pending the determination of whether or not the debtor should be rehabilitated.

The rehabilitation receiver will not take over the management of the company under rehabilitation. The RTC may, however, appoint a management committee for the company under rehabilitation in appropriate cases, such as when there is dissipation, loss, wastage or destruction of assets of the company under rehabilitation. The rehabilitation receiver has the power to recommend the appointment of a management committee for the corporation. In case the court appoints a management committee, the committee will replace the management and board of directors of the company under rehabilitation.

(ii) *the interests of owners/shareholders of the debtor*

Answer:

- Suspension of Payments – the shareholders remain the owners of their shares in the debtor corporation.
- Voluntary Insolvency and Involuntary Insolvency – the shareholders remain the owners of their shares in the debtor corporation.
- Rehabilitation – the shareholders remain the owner of their shares in the debtor corporation.

(iii) *contracts to which the debtor is a party*

Answer: The stay order prescribed by the Interim Rules for rehabilitation cases prohibits the debtor's suppliers of goods and services from withholding the supply of goods and services in the ordinary course of business for as long as the debtor makes payment for goods and services supplied after the issuance of the stay order. There are no similar provisions in the Insolvency Law. Under the Insolvency Law, the declaration of insolvency is a ground for default upon which the contracting parties may rescind any existing contractual arrangement.

(iv) *legal proceedings to which the organisation is a party*

Answer: In suspension of payments, no creditor (other than those having claims for personal labour and persons having legal or contractual mortgages), shall sue or institute proceedings to collect its claim from the debtor from the moment that suspension of payments is applied for, and while the proceedings are pending.

In both voluntary and involuntary insolvency, once the court issues an order declaring the debtor insolvent, all civil proceedings pending against the debtor are stayed. However, mortgages, pledges, attachments or executions on the property of the debtor duly recorded in the Register of Deeds are not affected.

In rehabilitation proceedings, if the court finds the petition sufficient in form and substance, it will issue a stay order suspending enforcement of all claims, whether for money or otherwise, and whether such enforcement is by court action or otherwise, against the debtor, its guarantors and sureties that are not liable with the debtor.

(v) *remedies available to persons in contractual (non-debt) relationships with the debtor*

Answer: The stay order issued in rehabilitation proceedings suspends enforcement of all claims, which includes all claims or demands of whatever nature or character against the debtor or its property, whether for money or otherwise. However, under the Interim Rules, any creditor may ask for relief from the effects of the stay order upon showing appropriate grounds.

(b) Question: *If another insolvency procedure has already been initiated in relation to the corporate debtor, how does the initiation of a second procedure affect the first?*

Answer: There is a view that the second proceeding should be dismissed. This is due to the nature of insolvency proceedings which is in rem. Once proper publication is made, the proceedings will affect and cover not only the petitioner, but all creditors of the corporate debtor. Thus, there can be no filing of a separate (second) case against the same corporate debtor, and if there is, the same should be dismissed because the proper remedy of the second petitioner is to file his claims in the original insolvency proceedings. There is, however, a view that the two proceedings should be consolidated.

Section J – Case Management of Insolvent Enterprises

1. Administration of insolvency procedures generally

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what are the administrative organs/entities involved in the implementation and management of that procedure? (For example a trustee, liquidator, receiver, government official.)*

Answer: In suspension of payments proceedings, the RTC is the organ involved in the management and implementation of the procedure.

In insolvency proceedings, the RTC, the assignee, the receiver and the sheriff are the organs and entities involved in the management and implementation of the insolvency procedure.

In rehabilitation proceedings, the RTC and the rehabilitation receiver are the organs and entities involved in the implementation and management of the procedure.

(b) Question: *What qualifications must each type of administrator of insolvency procedures possess? Is there a system of regulation of insolvency administrators in this country?*

Answer: The Insolvency Law does not provide for the qualifications of insolvency administrators, nor is there a system of regulation of insolvency administrators in the Philippines.

For rehabilitation proceedings, Section 13 of Rule 4 of the Interim Rules specifies the qualifications for rehabilitation receivers as follows:

- expertise and acumen to manage and operate a business similar in size and complexity to that of the debtor;
- knowledge in management, finance, and rehabilitation of distressed company;
- general familiarity with the rights of creditors in suspension of payments or rehabilitation, and general understanding of the duties and obligations of a rehabilitation receiver;
- good moral character, independence and integrity;
- lack of a conflict of interest; and
- willingness and ability to file a bond in such amount as may be determined by the court.

(c) Question: *Are the creditors of a corporate debtor permitted to participate in the administration of the relevant insolvency procedure, and if so, how? (For example, are the creditors permitted to assist the administrator, or supervise or dictate the conduct of the administration?)*

Answer: Under the Insolvency Law, the creditors elect the assignee to whom an insolvent debtor makes an assignment of all his property for the benefit of his creditors. This is due to the nature of insolvency proceedings which is in rem. Once proper publication is made, the proceedings will affect and cover not only the petitioner but all creditors of the corporate debtor. Thus, some people believe that there can be no filing of a separate (second) case against the same corporate debtor, and if there is, the same should be dismissed because the proper remedy of the second petitioner is to file his claims in the original insolvency proceedings.

In rehabilitation proceedings, the creditors may oppose the nominees for rehabilitation receiver given by the debtor. In practice, the creditors are

often consulted by the receiver in matters relating to the rehabilitation plan proposed by the debtor. In addition, a rehabilitation plan is subject to the approval of the creditors. However, the court may approve a rehabilitation plan even over the opposition of creditors holding a majority of the total liabilities of the debtor, if, in its judgment, the rehabilitation of the debtor is feasible and the opposition of the creditors is manifestly unreasonable.

2. Powers of the administrator

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what are the powers given to each type of administrator by statute, at general law or pursuant to the terms of the appointment? (for example power to carry on the business of the organisation, to pay creditors, to compromise claims of or against the debtor, to issue or defend legal proceedings, to obtain credit, to sell property, to execute documents on behalf of the debtor.)*

Answer: Under PD 902-A, the rehabilitation receiver shall have the powers of a regular receiver under the Rules of Court which are as follows:

“Section 6. General powers of receiver - Subject to the control of the court in which the action or proceeding is pending, a receiver shall have the power to bring and defend, in such property in controversy; to receive rents; to collect debts due to himself as receiver or to the fund, property, estate, person, or corporation of which he is the receiver; to compound for and compromise the same; to make transfers; to pay outstanding debts; to divide the money and other property that shall remain among the persons legally entitled to receive the same; and generally to do such acts respecting the property as the court may authorise. However, funds in the hands of a receiver may be invested only by order of the court upon the written consent of all the parties to the action.”

No action may be filed by or against a receiver without leave of the court which appointed him (Rule 59, Rules of Court).

The management committee rehabilitation receiver shall have the following powers under PD 902-A:

- to take custody of, and control over, all the existing assets and property of such entities under management;

- to evaluate the existing assets and liabilities, earnings and operations of such corporations, partnerships or other associations;
- to determine the best way to salvage and protect the interest of the investors and creditors;
- to study, review and evaluate the feasibility of continuing operations, and restructure and rehabilitate such entities if determined to be feasible by the SEC;
- to report and be responsible to the SEC until dissolved by the Commission; and
- it may overrule or revoke the actions of the previous management and board of directors of the entity or entities under the management, notwithstanding any provision of law, articles of incorporation or by-laws to the contrary (Section 6 (c) & (d), PD 902-A).

The assignee under the Insolvency Law shall have the power to:

- sue and recover all the estate, debts and claims belonging to or due to the debtor;
- take into his possession all the estate of the debtor except property exempt from execution;
- in the case of a non-resident or absconding or concealed debtor, to demand and receive of every sheriff all the property and moneys in his possession belonging to the debtor;
- sell, upon order of the court, any estate of the debtor which has come into his possession;
- redeem all mortgages and pledges and to satisfy any judgment which may be an encumbrance on any property sold by him;
- settle all accounts between the debtor and his debtors, subject to the approval of the court;
- compound, under the order of the court, with any person indebted to such debtor; and
- recover any property fraudulently conveyed by the debtor.²

The aforementioned powers, duties and functions of a receiver under PD 902-A and the Rules of Court are also granted to a Rehabilitation Receiver under the Interim Rules. The Interim Rules detail the powers and functions of the Rehabilitation Receiver as follows:

- to verify the accuracy of the petition, including its annexes such as the Schedule of Debts and Liabilities and the Inventory of Assets submitted in support of the petition;
- to accept and incorporate, when justified, amendments to the Schedule of Debts and Liabilities;

- to recommend to the court disallowance of claims and rejection of amendments to the Schedule of Debts and Liabilities that lack sufficient proof and justification;
- to submit to the court and make available for review by the creditors, a revised Schedule of Debts and Liabilities;
- to investigate the acts, conduct, properties, liabilities, and financial condition of the debtor, the operation of its business and desirability of the continuance thereof; and, any other matter relevant to the proceedings or to the formulation of a rehabilitation plan;
- to examine under oath the directors and officers of the debtor and any other witnesses that he may deem appropriate;
- to make available to the creditors documents and notices necessary for them to follow and participate in the proceedings;
- to report to the court any fact ascertained by him pertaining to the causes of the debtor's problems, fraud, preferences, dispositions, encumbrances, misconduct, mismanagement, and irregularities committed by the stockholders, directors, management, or any other person against the debtor;
- to employ such person or persons such as lawyers, accountants, appraisers, and staff as are necessary in performing his functions and duties as Rehabilitation Receiver;
- to monitor the operations of the debtor and to immediately report to the court any material adverse change in the debtor's business;
- to evaluate the existing assets and liabilities, earnings and operations of the debtor;
- to determine and recommend to the court the best way to salvage and protect the interests of the creditors, stockholders, and the general public;
- to study the rehabilitation plan proposed by the debtor, or any rehabilitation plan submitted during the proceedings; together with any comment made thereon;
- to prohibit and report to the court any payments outside of the ordinary course of business;
- to have unlimited access to the debtor's employees, premises, books, records, and financial documents during business hours;
- to inspect, copy, photocopy, or photograph any document, paper, book, account, or letter, whether in the possession of the debtor or other persons;

² De Leon, *Supra* at 517.

- to gain entry into any property for the purpose of inspecting, measuring, surveying, or photographing it or any designated relevant object or operation thereon;
- to take possession, control and custody of the debtor's assets;
- to notify counter-parties and the court as to contracts that the debtor has decided to continue to perform or breach;
- to be notified of, and to attend all meetings of the board of directors and stockholders of the debtor;
- to recommend any modification of an approved rehabilitation plan as he may deem appropriate;
- to bring to the attention of the court any material change affecting the debtor's ability to meet the obligation under the rehabilitation plan;
- to recommend the appointment of a management committee in the cases provided for under Presidential Decree No. 902-A, as amended;
- to recommend the termination of the proceedings and the dissolution of the debtor if he determines that the continuance in business of such entity is no longer feasible or profitable, or no longer works to the best interest of the stockholders, parties, litigants, creditors, or the general public;
- to apply to the court for any order or directive that he may deem necessary or desirable to aid him in the exercise of his powers and performance of his duties and functions; and
- to exercise such other powers as may from time to time be conferred upon him by the court.

(b) Question: *To what extent and in what circumstances may each type of insolvency administrator seek assistance, advice or direction in the conduct of the administration, and from what sources? (For example the Court, his appointor, the creditors of the debtor, a solicitor, accountant or other relevant person.)*

Answer: Under the Interim Rules, the Rehabilitation Receiver may apply to the court for any order or directive that he may deem necessary or desirable to aid him in the exercise of his powers and performance of his duties and functions. Under Section 62 of the Insolvency Law, in determining the assets, the court may, upon the application of the assignee or any creditor, or without application, examine the debtor under oath in relation to his property, and may also examine other persons tending or

making proof of claims, and may subpoena witnesses to give evidence relating to such matters.

3. Duties of the administrator

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what are the duties imposed upon each type of administrator by statute and at general law? (For example, a duty to take possession of assets of the debtor, to realise those assets, to discharge the debt owed to his appointor, to call for proofs of debts owed to creditors, to adjudicate upon claims of creditors, to apply available assets in discharge of those claims, to report on the conduct of the debtor by the proprietors.)*

Answer: Note that all references to following Sections are to the Insolvency Law. The assignee in insolvency shall have the duty to:

- register the assignment to him of the real estate of the debtor (Section 34);
- file the schedule and inventory of the property of the debtor (Ibid.);
- convert, as speedily as possible, the estate, real and personal, into money (Section 39);
- to keep a regular account of all moneys received by him as assignee (Ibid.);
- petition the court to allow the private sale of the debtor's property if it appears that it is for the best interest of the estate (Ibid.);
- file a just and true account of all receipts and payments (Section 42);
- file accounts upon order of the court on motion of two or more creditors (Section 44);
- distribute such dividends as may be required (Ibid.); and
- file his final account within one year from the date of order of adjudication, or the receiver's bond is found to be insufficient (Section 43).³

In respect of the Rehabilitation Receiver, please see Section J2.

4. Breach of duty and liability of administrators

(a) Question: *What remedies and/or sanctions are available in the legal system of this country in respect of breaches of duty or transgressions committed by each type of insolvency administrator?*

Answer: They may be sued for damages. Insofar as Rehabilitation Receivers are

³ De Leon, *Supra* at 518, all references to Sections are to the Insolvency Law.

concerned, the Interim Rules provide that the rehabilitation receiver shall not be subject to any action, claim, or demand in connection with any act done or omitted by him in good faith in the exercise of his functions and powers herein conferred.

The Interim Rules expressly provide that a rehabilitation receiver may be dismissed by the court, upon motion or *motu proprio*, on account of conflict of interest, or on any of the grounds for removing a trustee under the general principles of trusts.

An action for estafa for breach of fiduciary duty under the Revised Penal Code is also available, as well as forfeiture of the bond that is supposed to have been put up.

Section K – Assets Available to Creditors

1. Assets available to creditors generally

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what assets of the business organisation are available to its administrator to satisfy the claims of its creditors?*

Answer: For voluntary and involuntary insolvency, the properties of the insolvent that pass to the assignee are the following:

- all real and personal property, estate and effects of the debtor including all deeds, books and papers in relation thereto (Section 32);
- properties fraudulently conveyed (Sections 33, 36);
- right of action for damages to real property; and
- the undivided share or interest of the insolvent debtor in property held under co-ownership (Article 2239, Civil Code).⁴

A secured creditor may maintain his right under his security or lien, and may enforce his lien thereon, or he may waive his right under the security or lien, and thereby share in the distribution of the assets of the debtor (Section 59).

For rehabilitation proceedings, the Interim Rules require that an inventory of all the assets of the debtor, including those subject to encumbrances, liens or claims, must be submitted together with the petition. It appears that all the properties of the debtor are available to satisfy the claims of its creditors.

2. Avoidance of past transactions affecting the assets of a corporate debtor

(a) Question: *To what extent and in what circumstances may the administrator of a business organisation take steps to recover assets of the organisation by overturning past transactions involving property of the organisation? (For example, preferences given to certain creditors over others, invalid charges granted by the organisation, uncommercial transactions entered into by the organisation, profits on sales to and from the organisation at an undervalue or overvalue.)*

Answer: Under the Insolvency law, the assignee may recover the property or the value of assets which have been fraudulently conveyed. Section 70 of the Insolvency Law reads:

“Section 70. If any debtor, being insolvent, or in contemplation of insolvency, within thirty days before the filing of a petition by or against him, with a view to giving a preference to any creditor or person having a claim against him or who is under any liability for him procures any part of his property to be attached, sequestered, or seized on execution, or makes any payment, pledge, mortgage, assignment, transfer, sale, or conveyance of any part of his property, either directly or indirectly, absolutely or conditionally, to anyone, the person receiving such payment, pledge, mortgage, assignment, transfer, sale or conveyance, or to be benefited thereby, or by such attachment, sequestration, seizure, payment, pledge, mortgage, conveyance, transfer, sale or assignment is made with a view to prevent his property from coming to his assignee in insolvency or to prevent the same from being distributed rateably among his creditors, or to defeat the object of, or in any way hinder, impede or delay the operation of or to evade the provisions of this Act, such attachment, sequestration, seizure, payment, pledge, mortgage, transfer, sale, assignment, or conveyance is void, and the assignee, or the receiver, may recover the property or the value thereof, as assets of such insolvent debtor. If such payment, pledge, mortgage, conveyance, sale assignment, or transfer is not made in the usual and ordinary course of business of the debtor, or if such seizure is made under a judgment which the debtor has confessed or offered to allow, that fact shall be prima facie evidence of fraud. Any payment, pledge, mortgage, conveyance, sale, assignment, or transfer of property of whatever character

4 De Leon, *Supra* at 516, all references to Sections are to the Insolvency Law.

made by the insolvent within one month before the filing of a petition in insolvency by or against him, except for a valuable pecuniary consideration made in good faith, shall be void. All assignments, transfers, conveyances, mortgages, or encumbrances of real estate shall be deemed, under this section, to have been made at the time the instrument conveying or affecting such realty was filed for record in the office of the Register of Deeds of the province or city where the same is situated."

The SEC has opined that Section 70 of the Insolvency Law should also apply to proceedings filed before it pursuant to PD 902-A. It is believed that this SEC opinion may have some persuasive effect on the RTCs under whose jurisdiction new rehabilitation cases must be filed.

Under Section 71 of the Insolvency Law, the following acts of the debtor shall be punishable by imprisonment:

- If he shall, after the commencement of proceedings in insolvency, secrete or conceal any property belonging to his estate or part with, conceal, destroy, alter, mutilate, or falsify or cause to be concealed, destroyed, altered, mutilated, or falsified, any book, deed, document, or writing relating thereto, or remove, or cause to be removed, the same or any part thereof, with the intent to prevent if from coming into the possession of the assignee in insolvency, or to hinder, impede, or delay his assignee in recovering or receiving the same, or if he shall make any payment, gift, sale assignment, transfer, or conveyance of any property belonging to his estate, with like intent, or shall spend any part thereof in gambling; or if he shall, with intent to defraud, wilfully and fraudulently conceal from his assignee, or fraudulently or designedly omit from his schedule any property or effects whatsoever, or if, in case of any person having, to his knowledge or belief, proved a false or fictitious debt against his estate he shall fail to disclose the same to his assignee within one month after coming to the knowledge or belief thereof; or if he shall attempt to account for any of his property by fictitious losses or expenses.
- If he shall, within three months before commencement of proceedings in insolvency, under the false pretence of carrying on business and dealing in the ordinary course of trade, obtain on credit from any person any goods or chattels [with intent to defraud], or shall, [with intent to defraud his creditors,]

pawn, pledge, or dispose of, otherwise than by bona fide transactions in the ordinary course of his trade, any of his goods and chattels which have been obtained or credit and remain unpaid for, or shall have suffered loss in any kind of gaming when such loss is one of the causes determining the commencement of proceedings in insolvency, or shall have sold at a loss or for less than the current price any goods bought on credit and still unpaid for, or shall have advanced payments to the prejudice of his creditors.

- If he shall, from and after the taking effect of the Act, during the proceedings for the suspension of payments, secrete or conceal, or destroy, or cause to be destroyed or secreted any property belonging to his estate; or if he shall secrete, destroy, alter, mutilate, or falsify or cause to be secreted, destroyed, altered, mutilated, or falsified, any book, deed, document, or writing relating thereto, or if he shall, with intent to defraud his creditors, make any payment, sale, assignment, transfer, or conveyance of any property belonging to his estate; or if he shall spend any part thereof in gaming; or if he shall falsely swear to the schedule and inventory exacted by paragraph two of Section 2 as required by Sections 15, 16, and 17 of the Act, with intent to defraud his creditors; or if he shall violate or break in any manner whatsoever the injunction issued by the court under Section 3 of the Act.

Section 37 of the Insolvency Law also imposes a liability on the persons, who, before the assignment is made, having notice of the commencement of the proceedings in insolvency, or having reason to believe that insolvency proceedings are about to be commenced, embezzles or disposes of any of the moneys, goods, chattels, or effects of the insolvent, he is chargeable therewith, and liable to an action by the assignee for double the value of the property so embezzled or disposed of, to be received for the benefit of the insolvent's estate.

The above provisions are seldom enforced in insolvency proceedings in the country.

For rehabilitation proceedings, the court is given the power under Section 7 of Rule 4 of the Interim Rules, upon motion or motu proprio, to declare void any transfer of property or any other conveyance, sale, payment, or agreement made in violation of its stay order or in violation of the Interim Rules. In this connection, the rehabilitation receiver is given the authority and duty to prohibit and report to the court any encumbrance, transfer, or disposition of the

debtor's property outside of the ordinary course of business or what is allowed by the court and to prohibit and report to the court any payments outside of the ordinary course of business.

(b) Question: *What powers or mechanism are available to each type of administrator for investigation of the affairs of the business organisation, for examination of persons formerly involved in the management or control of the organisation, and for the discovery of assets of the organisation?*

Answer: See Section K1 (a) for insolvency cases. For rehabilitation cases, see powers of the rehabilitation receiver under Section J2 (a).

(c) Question: *What procedures may be employed by each type of administrator for the recovery of assets of the business organisation which are available for distribution to creditors? (For example, initiation of legal proceedings, compensation from directors.)*

Answer: See Section K1 (a) above for insolvency cases. For rehabilitation cases, please see powers of the rehabilitation receiver Section J2 (a).

Section L – Claims of Creditors

1. Claims admissible for payment

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what types of claims of creditors are properly admissible for payment in the context of that procedure? (For example liquidated debts, future debts, contingent claims, secured claims, unliquidated claims for damages, interest claims, costs of administration or of legal proceedings, periodical payments, debts owed by guarantors of the business organisation.)*

Answer: Under the Insolvency Law, different classes of debts may be proved against the estate of the debtor in insolvency proceedings (Sections 53 to 59 of the Insolvency Law). Under Section 53 of the Insolvency Law, all debts due and payable from the debtor at the time of the adjudication of insolvency, and all debts then existing but not payable until a future time, may be proved against the estate of the debtor. Contingent debts as well as those based on commercial papers where the debtor is bound as endorser, surety, bail or guarantor may also be proved against the estate of the debtor after such liability shall have become fixed and before the final dividend shall have been declared.

The following claims shall not be allowed or proved against the estate of the insolvent debtor:

- claims barred by the statute of limitation;
- claims of creditors who have received any preference made or given by debtors in violation of the insolvency law;
- claims of creditors who hold a mortgage or pledge on real or personal property of the debtor, or a lien thereon for receiving payment of a debt owing to them from the debtor, unless the security is surrendered to the sheriff, receiver or assignee, and
- claims of creditors who hold an attachment or execution on property of the debtor duly recorded and not dissolved under the Insolvency Law, unless the security is surrendered to the receiver, sheriff or assignee, as the case may be. A claim is disallowed when the court determines that a creditor has not duly established his claim.

The Interim Rules do not have provisions relating to what debts may be proved and what claims are properly admissible in rehabilitation proceedings. What is required is for a Schedule of Debts and Liabilities which lists all the creditors of the debtor, indicating the name and address of each creditor, the amount of each claim as to principal, interest, or penalties due as of the date of filing, the nature of the claim, and any pledge, lien, mortgage, judgment, or other security given for the payment thereof, to be submitted together with the petition. The rehabilitation receiver may, however, recommend to the court the disallowance of claims and rejection of amendments to the Schedule of Debts and Liabilities.

(b) Question: *At what date are the amounts of admissible debts computed?*

Answer: See Section L1 (a)

(c) Question: *By what method are claims of creditors proven by those creditors in the context of each type of insolvency procedure?*

Answer: See Section L1 (a). Section 62 of the Insolvency Law provides that the court may, upon the application of the assignee, or of any creditor, or without any application, before or after adjudication in insolvency, examine upon oath the debtor in relation to his property, and his estate and may examine any other person tending or making proof of claims, and may subpoena witnesses to give evidence relating to such matters.

In rehabilitation proceedings, the Interim Rules allow every creditor of the debtor to file a

verified opposition or comment to the petition for rehabilitation. If the Schedule of Debts and Liabilities attached to the petition omit a claim or liability, the creditor concerned shall attach a verified statement of the obligations allegedly due to it to its comment or opposition.

(d) Question: *How are disputed claims made by creditors adjudicated upon? (For example by the administrator, or by a Court.)*

Answer: Under the Insolvency Law, the assignee decides whether or not a claim is admissible.

2 Priority and payment of creditor's claims:

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this country, what principles apply to the division of available assets of the corporate debtor among these of its creditors entitled to payment? Is there a basic principle of equality of payment, or are rights or priority of payment enjoyed by secured creditors, or by certain classes of creditors over others? (For example costs of the administration, claims for taxes owed by the debtor, amounts owed to employees of the organisation.)*

Answer: Only taxes enjoy absolute preference under the Civil Code. Under the Labour Code of the Philippines (P.D. No. 422, as amended), unpaid wages and other monetary claims of workers enjoy preference over taxes due the Government:

“Article 110. Worker preference in case of bankruptcy - In the event of bankruptcy or liquidation of an employer's business, his workers shall enjoy first preference as regards their wages and other monetary claims, any provisions of law to the contrary notwithstanding. Such unpaid wages and monetary claims shall be paid in full before claims of the government and other creditors may be paid.”

Note, however, that the Supreme Court has held that the provision of the Labor Code giving preference to claims of employees cannot be viewed in isolation, and must be read in relation to the Civil Code⁵. The mortgage lien of a secured creditor over particular properties of the insolvent employer cannot be overcome by the preference of unpaid workers who must actually seek their preference on the unencumbered properties of the employer.

All the remaining classes of preferred credits with respect to specific immovable property, or

the remaining classes with respect to specific movable property enjoy no priority among themselves but must be paid pro rata.

In order that this pro-rating may be fully effected, the preferred creditors must necessarily be convened and the import of their claims ascertained. It is thus apparent that given the full application of the Civil Code, provisions on concurrence and preference of credit demands, there must be first some proceeding where the claims of all the preferred creditors may be adjudicated with binding effect, such as insolvency or other liquidation proceedings of similar import.

(b) Question: *Give a brief account of the order of priorities, if any, of payment of creditors prescribed by the legal system of this country.*

The pertinent provisions of the Civil Code are as follows:

“Article 2241. With reference to specific movable property of the debtor, the following claims or the liens shall be preferred.

- (1) Duties, taxes and fees due thereon to the State or any subdivision thereof;
- (2) Claims arising from misappropriation, breach of trust, or malfeasance by public officials committed in the performance of their duties, on the movables, money or securities obtained by them;
- (3) Claims for the unpaid price of movables sold, on said movables, so long as they are in the possession of the debtor, up to the value of the same; and if the movable has been resold by the debtor and the price is still unpaid, the lien may be enforced on the price, this right is not lost by the immobilisation of the thing by destination, provided it has not lost its form, substance and identity, neither is the right lost by the sale of the thing together with other property for a lump sum, when the price thereof can be determined proportionally;
- (4) Credits guaranteed with a pledge so long as the things pledged are in the hands of the creditor, or those guaranteed by a chattel mortgage, upon the things pledged or mortgaged, up to the value thereof;
- (5) Credits for the making, repair, safekeeping or preservation of personal property, on the movable thus made, repaired, kept or possessed;

⁵ *Development Bank of the Philippines vs. National Labor Relations Commission*, 183 SCRA 328 (1990) and *Batong Buhay Gold Mines, Inc. vs. Dela Serna*, 312 SCRA 22 (1999).

- (6) Claims for labourers' wages, on the goods manufactured or the work done;
- (7) For expenses of salvage, upon the goods manufactured or the work done;
- (8) Credits between the landlord and the tenant, arising from the contract of tenancy on shares, on the share of each in the fruits or harvest;
- (9) Credits for transportation, upon the goods carried, for the price of the contract and incidental expenses, until their delivery and for thirty days thereafter;
- (10) Credits for loading and supplies usually furnished to travellers by hotel keepers, on the movables belonging to the guest as long as such movables are in the hotel, but not for money loaned to the guests;
- (11) Credits for seeds and expenses for cultivation and harvest advanced to the debtor, upon the fruits harvested;
- (12) Credits for rent for one year, upon the personal property of the lessee existing on the immovable leased and on the fruits of the same, but not on money or instruments of credit;
- (13) Claims in favour of the depositor if the depositary has wrongfully sold the thing deposited, upon the price of the sale.

In the foregoing cases, if the movables to which the lien or preference attaches have been wrongfully taken the creditor may demand them from any possessor, within thirty days from the unlawful seizure."

"Article 2242. With reference to specific immovable property and real rights of the debtor, the following claims, mortgages and liens shall be preferred, and shall constitute an encumbrance on the immovable or real right:

- (1) Taxes due upon the land or building;
- (2) For the unpaid price of real property sold, upon the immovable sold;
- (3) Claims of labourers, masons, mechanics and other workmen, as well as of architects, engineers, and contractors, engaged in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works;
- (4) Claims of furnishers of materials used in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works;

- (5) Mortgage credits recorded in the Registry of Property, upon the real estate mortgaged;
- (6) Expenses for the preservation or improvement of real property when the law authorises reimbursement, upon the immovable preserved or improved;
- (7) Credits annotated in the Registry of Property, in virtue of a judicial order, by attachments or executions, upon the property affected, and only as to later credits;
- (8) Claims of co-heirs for warranty in the partition of an immovable among them, upon the real property thus divide;
- (9) Claims of donors of real property for pecuniary charges or other conditions imposed upon the donee, upon the immovable donated;
- (10) Credits of insurers, upon the property insured, for the insurance premium for two years."

"Article 2243. The claims or credits enumerated in the two preceding articles shall be considered as mortgages or pledges of real or personal property, or liens within the purview of legal provisions governing insolvency. Taxes mentioned in No. 1, Article 2241, and No. 1, Article 2242, shall first be satisfied."

"Article 2244. With reference to other property, real and personal, of the debtor, the following claims or credits shall be preferred in the order named:

- (1) Proper funeral expenses for the debtor, or children under this or her parental authority who have no property of their own, when approved by the court;
- (2) Credits for services rendered the insolvent by employees, labourers, or household helpers for one year preceding the commencement of the proceedings in insolvency;
- (3) Expenses during the last illness of the debtor or of his or her spouse and children under his or her parental authority, if they have no property of their own;
- (4) Compensation due to the labourers or their dependents under laws providing for indemnity for damages in cases of labour accident, or illness resulting from the nature of the employment;

- (5) Credits and advancements made to the debtor for support of himself or herself, and family, during the last year preceding the insolvency;
 - (6) Support during the insolvency proceedings, and for three months thereafter;
 - (7) Fines and civil indemnification arising from a criminal offence;
 - (8) Legal expenses, and expenses incurred in the administration of the insolvent's estate for the common interest of the creditors, when properly authorised and approved by the court;
 - (9) Taxes and assessments due the national government, other than those mentioned in Articles 2241, No. 1, and 2242, No. 1;
 - (10) Taxes and assessments due any province, other than those referred to in Articles 2241, No. 1, and 2242, No. 1;
 - (11) Taxes and assessments due any city or municipality, other than those indicated in Articles 2241, No. 1, and 2242, No. 1;
 - (12) Damages for death or personal injuries caused by a quasi-delict;
 - (13) Gifts due to public and private institutions or charity or beneficence;
 - (14) Credits which, without special privilege, appear in (a) a public instrument; or (b) in a final judgment, if they have been the subject of litigation. These credits shall have preference among themselves in the order of priority of the dates of the instruments and of the judgments, respectively."
- nationality of the debtor;
 - personal whereabouts at the material time;
 - location of principal place of business;
 - location of place of business, branch or agency;
 - locations of assets of debtor;
 - place where transactions of event took place which gave rise to liability;
 - place where payment, discharge or performance of liability is due to take place.)

Answer:

- In the case of a petition for suspension of payments, Section 2 of the Insolvency Law provides that the debtor "may petition that he be declared in the state of suspension of payments by the court, or the judge thereof in vacation, of the province or city in which he has resided for six months next preceding the filing of this petition".
- In the case of voluntary petitions for insolvency, the Insolvency Law provides that an insolvent debtor "may apply to be discharged from his debts and liabilities by petition to the Court of first Instance [now the Regional Trial Court] of the province or city in which he has resided for six months next preceding the filing of such petition."
- In the case of involuntary insolvency proceedings, Section 20 of the Insolvency Law contains the following requirements:
 - the petition must be filed by three or more creditors, residents of the Philippine Islands, whose credits or demands accrued in the Philippine Islands" and
 - "[s]uch petition must be filed in the Court of First Instance [now Regional Trial Court] of the province or city in which the debtor resides or has his principal place of business."

It appears that the principal connection required is the location of the principal place of business of the debtor. For involuntary insolvency proceedings, however, it is also required that the creditors be residents of the Philippines, and that their claims accrued in the Philippines. There is not any Philippine jurisprudence available on what "accrued" means in connection with a petition for insolvency. We assume that it will be understood in the context in which it is ordinarily used, i.e., to arise; to become due. This would necessitate some form of substantial connection with the Philippines, such as the place of performance of the obligation, governing law, place of execution of the contract, source of payment and other similar factors.

The aforementioned preference and concurrence of credits apply only when the debtor has been declared insolvent.

Section O. Connection Between Debtor and Forum

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this economy, what connection must there be between the debtor organisation and the law of the forum?*

(For example, which of the following requirements, if any, must be satisfied in order for an insolvency procedure to be initiated in relation to a corporate debtor in your economy:

- principal residence of debtor;
- domicile of the debtor;

Under the Interim Rules, a petition for rehabilitation shall be filed with the RTC having jurisdiction over the territory where the debtor's principal office is located.

Section P – Foreign/Cross-Border Elements

1. Claims of foreign creditors

(a) Question: *In relation to each type of insolvency procedure available in the legal system of this economy, to what extent are the claims of foreign creditors recognised in the context of administration of that procedure?*

Answer: In the case of both suspension of payments and voluntary insolvency proceedings, Section 15 of the Insolvency Law provides that the debtor is obliged to annex to his petition a schedule which “must contain a full and true statement of all his debts and liabilities, together with a list of all those to whom, to the best of his knowledge and belief, said debts or liabilities are due, the place of residence of his creditors and the sum due each.” Section 15 does not distinguish between creditors who are residents of the Philippines and those who are residents of some other country. The reference to “all his debts” in Section 15 provides a basis for the position that the claims of foreign creditors should also be included in the Schedule annexed to the petition, and that the claims of foreign creditors would be recognised in the proceedings.

Under the Insolvency Law, a petition for involuntary insolvency may be initiated only upon the petition of at least three creditors who are residents of the Philippines. A foreign corporation licensed to engage in business in the Philippines would qualify as a resident creditor. Thus, the Philippine Supreme Court in *State Investment House vs Citibank*,⁶ declared that “what effectively makes such a foreign corporation a resident corporation in the Philippines is its actually being in the Philippines and licitly doing business here.”

In the case of involuntary insolvency proceedings, Section 29 of the Insolvency Law allows creditors who are not the petitioners, to file their claims in the office of the clerk of court in which the proceedings are pending. Section 29 does not distinguish between resident and non-resident creditors. We therefore believe that both resident and non-resident creditors may file their claims with the local court and that the interests of both would be protected.

Similarly, the Interim Rules do not distinguish as

to the claims of the creditors that would have to be included in the Schedule of Debts and Liabilities that should be attached to the petition. There does not appear to be any restriction on including claims of foreign creditors.

(b) Question: *What principles or rules apply to the recognition and admission of claims by foreign creditors? (For example, see (i) and (ii) below).*

Answer: Neither the Insolvency Law nor the Interim Rules distinguish as to the application of the rules and principles therein. We believe that the relevant provisions apply to claims of all creditors, whether foreign or not.

(i) Question: *Are claims by foreign creditors subject to particular rules in relation to priority of payment?*

Answer: Claims of foreign creditors would not be subject to any different rules as are applicable to claims of resident creditors, even in respect of priority of payment. They would also be governed by Articles 2241, 2242 and 2244 of the New Civil Code of the Philippines which lays down the rules in respect of priority of payment of the obligations of an insolvent debtor.

(ii) Question: *Do foreign creditors have to satisfy special or additional requirements in order for their claims to be admitted?*

Answer: There are no special or additional requirements in order for claims of foreign creditors to be admitted, which are not applicable to local creditors. As above mentioned, what is required for petitions for involuntary insolvency is that the claims must have accrued in the Philippines.

If the claim of a foreign creditors stems from a foreign judgment in its favour, the following are the conditions and requisites before such foreign judgments may be recognised and enforced in the Philippines:

- There must be proof of the foreign judgment;
- The judgment must be on a civil or commercial matter; and
- There must be no lack of jurisdiction, no want of notice, no collusion, no fraud, no clear mistake of law or fact.

(c) Question: *What law is applied to establish the validity of foreign claims?*

Answer: The applicable law would depend on the nature of the claim. The following are the “Conflicts” rules covering real and personal properties:

6 203 SCRA 9 (1991).

- If the conflict concerns real property, the governing law is the place where the property is situated. The exceptions to this rule are:
 - contracts involving real property but which do not deal with title to such real property shall not necessarily be governed by the law where the property is situated, but may be governed by the law voluntarily agreed upon by the parties or the law intended by them expressly or implicitly; and
 - in contracts where real property is given by way of security, the principal contract is governed by the proper law of the contract, while the accessory contract of mortgage is governed by the laws of the state where the real property mortgage is situated.
- For tangible personal property, in general, the law to be applied shall be the law where the property is situated. Vessels, in view of their inherent movability, are governed by the law of the flag.
- For intangible personal property, the following are the conflicts rules:
 - For the recovery of debts or for the involuntary assignment of debts (garnishment), the proper point of contract is the place where the debtor may be effectively served with summons;
 - The validity and effectiveness of a voluntary assignment of a debt would depend on the proper law of the contract;
 - For the purpose of administering debts the site is the place where the assets of the debtor are actually located;
 - The validity of the transfer, delivery, or negotiation of the instrument is in general governed by the law of the suits of the instrument at the time of transfer, delivery, or negotiation.

2. Jurisdiction over foreign assets

(a) Question: *To what extent does the insolvency law of this economy claim jurisdiction over assets of a corporate debtor situated abroad?*

Answer: There is good basis for the view that Philippine courts or administrative agencies have no effective jurisdiction over assets of a corporate debtor that are situated abroad if the corporate debtor has no control over those assets abroad. This is also consistent with the principle of *lex situs* which the Philippines follows. Article 16 of the Civil Code provides that “real property as well as personal property is subject to the law of the country where it is situated.”

3. Foreign insolvency procedures

(a) Question: *To what extent do the rules of private international law of the legal system of this economy recognise insolvency procedures commenced in foreign jurisdiction?*

Answer: If the property of an insolvent is situated abroad, then Philippine courts should recognise insolvency procedures commenced in a foreign country in respect of property of a debtor located in that country, in the same manner that Philippine courts would not recognise insolvency proceedings instituted abroad involving assets of a debtor located in the Philippines.

(b) Question: *Under what circumstances, if any, may orders or judgments resulting from foreign insolvency procedures or administrations be recognised or enforced in the legal system of this economy?*

Answer: If the property of the debtor is located abroad, we believe that there would be no reason or need to have the foreign insolvency procedure or administration recognised or enforced in the Philippines. If, however, the foreign insolvency proceedings involve property of the debtor that is located in the Philippines, we believe that there would be difficulty having a judgment or order in the foreign insolvency proceedings enforced in the Philippines, because a Philippine court would take the position that the foreign administrator, body, court or tribunal would have no jurisdiction over assets located in the Philippines.

4. Foreign insolvency administrators

(a) Question: *What recognition is accorded in the legal system of this economy to the status and capacity of insolvency administrators (For example, trustees, liquidators, receivers) appointed in foreign insolvency procedures?*

Answer: Although there are no decisions by local courts on the matter, we believe that the Philippines would recognise the capacity of these trustees and liquidators, provided that the assets they administer are located abroad.

(b) Question: *To what extent are foreign insolvency administrators entitled to claim, take control of, and realise or deal with property of the corporate debtor situated within the jurisdiction of the legal system of this economy?*

Answer: We do not believe that foreign insolvency administrators would have jurisdiction to claim, take control of, and realise or deal with

property of the corporate debtor situated within the jurisdiction of the legal system of the Philippines.

5. Foreign security holders

(a) **Question:** *To what extent does the legal system of this economy recognise the validity of rights of security asserted by foreign creditors over assets of the corporate debtor?*

Answer: They are treated on an equal footing as local creditors with similar security, with the exception that in the case of mortgages over land, the foreign creditors may not bid in any foreclosure sale of the mortgaged land because of the prohibition in the Philippine Constitution against alien landholding.

(b) **Question:** *Are any special rules applicable to determine the validity, extent and ranking of such security rights?*

Answer: No. The same rules would apply as are applicable to local secured creditors.

6. International conventions

(a) **Question:** *To which international conventions having some application in insolvency matters is this economy a party?*

Answer: None that we are aware of.

(b) **Question:** *When were these conventions entered into, and what other states are parties?*

Answer: N/A

(c) **Question:** *What observations can be made about the practical results achieved under these international instruments?*

Answer: N/A

7. Cross-border insolvency

(a) **Question:** *Are there any other particular issues or special problems in the field of cross-border insolvency, not included in the answers supplied above, which have presented themselves before the courts of the legal system of this economy.*

Answer: None that we are aware of.

8. UNCITRAL Model Law on Cross-Border Insolvency

(a) **Question:** *Is the government of this economy aware of the UNCITRAL model law on cross-border insolvency, approved by the United Nations in June 1997?*

Answer: Yes, the government is aware of this. However, no law has been passed by the Philippine Congress based on this model law.

Section Q – New Development

(a) **Question:** *Are there any recent, imminent or proposed legislative, administrative, or practical reforms or developments or proposals in the legal system of this country which impact upon the matters mentioned above?*

Answer: There is now pending in Congress a proposed bill on Corporate Recovery (“CRA”), encompassing provisions on corporate insolvency, rehabilitation and suspension of payments. The bill, if passed, is expected to change the landscape of Philippine corporate law on insolvency and rehabilitation. The CRA incorporates, to a limited extent, some concepts of the UNCITRAL Model Law on cross-border insolvency.

Addendum to Report on Philippines

Addendum to Report on Philippines produced under Asian Development Bank Technical Assistance No. 5795 – REG

B. Insolvency Reforms

1. **Question:** *Provide details of any reforms that have occurred in relation to insolvency law and practice and related areas (such as corporate governance, secured transaction and so forth) since January 1999.*

Answer: On 15 January 2000, the Securities and Exchange Commission (“SEC”), pursuant to a grant of technical assistance from the World Bank, approved the Rules of Procedure for Corporate Recovery. These rules, for the first time since jurisdiction over suspension of payments and rehabilitation cases was vested in the SEC, provide detailed rules of procedure for handling suspension of payments and rehabilitation cases.

However, in July 2000, Congress passed the SRC which, among other things, transferred jurisdiction over rehabilitation cases filed after 30 June 2000 from the SEC to regular courts specially designated by the Supreme Court to hear and decide them. Following the said transfer, the Supreme Court promulgated the Interim Rules setting forth the rules of procedure to be followed by the specialised courts in handling rehabilitation cases.

On 23 December 2002, Congress passed the *Special Purpose Vehicles Act* (R.A. 9182), which is envisioned to solve the problem of non-performing assets of the financial industry.

In addition, there are pending bills in Congress on corporate rehabilitation, known as the *Corporate Recovery Act*, which are envisioned to form the comprehensive legislation that will streamline the outdated insolvency regime of the country and clarify the rights and obligations of debtors and creditors who will undergo rehabilitation or find themselves insolvent.

2. **Question:** *Provide details of any proposed reforms as above.*

Answer:

- *The Special Purpose Vehicles Act*

The *Special Purpose Vehicle Act* of 2001 (“SPV Act” or the “Act”) attempts to encourage

investment, both local and foreign, in the non-performing loans and acquired assets (“NPAs”) of the financial sector by providing time-bound tax exemptions and privileges in the acquisition of non-performing loans and acquired assets of the banking industry and some government-owned corporations.

The following are the main features of the Act:

1. The Special Purpose Vehicle – The Special Purpose Vehicle (“SPV”) for the acquisition of NPAs must be in the form of a stock corporation. If the SPV acquires land, at least 60% of its outstanding capital stock must be owned by Philippine nationals pursuant to the Foreign Investments Act (R.A. 7042). The SPV shall have a minimum authorised capital stock of P500 million, subscribed capital stock of P125 million, and a paid-up capital stock of P31.25 million.
2. Investment Unit Instruments – SPVs may issue Investment Unit Instruments (“IUIs”) for the purpose of raising funds to acquire NPAs. Any person, including non-Filipino citizens or entities, may acquire or hold IUIs in the minimum amount of P10 million.⁷
3. True Sale – The transfer of the NPAs from a Financial Institution (“FI”) to a SPV must be in the concept of a true sale. “True sale” refers to a sale wherein the selling Financial Institution transfers or sells its NPAs without recourse for cash or property to a SPV with the following results: (a) the transferor relinquishes effective control over the transferred NPAs; (b) the transferred NPAs are legally isolated and put beyond the reach of the transferor and its creditors; (c) the transferor FI shall not have direct or indirect management over the transferee SPV; and (d) the selling FI does not possess a claim of beneficial ownership of more than 5 % in the transferee SPV.⁸
4. Prior Notice to borrowers – The transfers of NPLs require prior notice to the borrowers and to the persons holding prior encumbrances upon the assets mortgaged or pledged. The borrower and transferring FI are given a period of at most 90 days to restructure or renegotiate the loan.⁹

⁷ Section 11, R.A. 9182.

⁸ Section 3 (l), R.A. 9182.

⁹ Section 12, R.A. 9182.

5. Certificate of Eligibility Certification – The transfer of a NPA from an FI to a SPV requires a prior certification of eligibility (“COE”) from the appropriate regulatory authority having jurisdiction over the operations of the FI to the effect that the asset is really non-performing.

6. Assumption of Rights and Obligations - After the transfer to the SPV, the SPV assumes all rights and obligations of the transferring FI, including the right to enforce contractual obligations, and the obligation to recognise the rights of the borrowers, as well as to prosecute and defend suits relating to the acquired assets.¹⁰

7. Tax Incentives and Privileges – The transfer of the NPAs from a FI to a SPV, and from a SPV to a third party or dation in payment by the borrower in favour of the FI or in favour of the SPVs shall be exempt of the following taxes:

- Documentary stamp taxes;
- Capital gains taxes imposed on the transfer of land/buildings treated as capital assets;
- Creditable withholding taxes imposed on the transfer of land/buildings treated as ordinary assets;
- Value added taxes.

The above transfers shall be subject to the following reduced fees:

- 50% of the applicable mortgage registration and transfer fees;
- 50% of the foreclosure filing fees; and
- 50% of the land registration fees.¹¹

All sales or transfers of NPAs from FIs to SPVs, or transfers by way of dation in payment by the borrower to the FIs or to the SPVs shall be entitled to the aforesaid exemptions for a period not exceeding two years from implementing Rules of the Act. All transfers from SPVs to a third party of NPAs acquired by the SPV within such two year period shall enjoy the tax exemptions from a period of not more than five years from the date of acquisition by the SPV.¹²

The SPV shall also be exempt from income taxes on net interest income, documentary stamp tax and mortgage registration fees on new loans in excess of existing loans granted to borrowers with NPLs that have been acquired by the SPV.

The SPV is also exempt from documentary stamp taxes in the event of capital infusion to the borrower by the SPV. These additional exemptions apply for a period of not exceeding five years from the date of implementation of the Rules of the Act.¹³

8. NOLCO – Any loss incurred by the FI as a result of the transfer of the NPAs shall be treated as an ordinary loss. The loss may be carried over for a period of 5 consecutive taxable years immediately following the year of such loss.¹⁴

9. Penalties – Abuse of the tax exemptions granted under the Act is punishable by imprisonment and/or fine. In addition, the offender shall be made to refund double the amount of the tax exemptions and privileges availed of, plus an interest of 12% per annum.¹⁵

10. Applicability – The provisions of the Act apply to assets which have become non-performing as of 30 June 2002.¹⁶

The following are the salient features of the Corporate Recovery Act:

- Initiation of Proceedings:
 - Voluntary – the proposed law will provide specific and different sets of requisites for each remedy (i.e. suspension of payments, court-supervised rehabilitation, pre-negotiated rehabilitation and liquidation).
 - Involuntary – at least 3 creditors with total claims of either P1 million, or at least 25% of the total paid-in capital of the debtor, whichever is higher; or any creditor, if another creditor (other than the petitioner) has initiated foreclosure proceedings against the debtor that will prevent the latter from paying its debts as they fall due or will render it insolvent.
- Effect of commencement of proceedings:
 - vests in the conservation the right to review and obtain all records;
 - suspend all legal proceedings for the enforcement of claims and all actions to enforce any judgment against the debtor;
 - prohibits the sale, encumbering, transfer or disposition of debtor’s properties and payment of outstanding liabilities;

10 Section 14, R.A. 9182.

11 Section 15, R.A. 9182.

12 Section 15, R.A. 9182.

13 Section 16, , R.A. 9182.

14 Section 17, , R.A. 9182.

15 Section 18, , R.A. 9182.

16 Section 25 of the Act.

- consolidates the resolution of all legal proceedings by and against the debtor before the court;
- serves as legal basis for rendering null and void (i) the results of any extra-judicial activity or process to seize property, sell encumbered property, or otherwise attempt to collect on or enforce a claim against the debtor; (ii) any set-off after the commencement date of any debt owed to the debtor by any of the creditors; and (iii) the perfection of any lien against the debtor's property after the commencement date.
- Non-applicability of suspension order to appeals and specialised proceedings: the suspension order will not apply to appeals cases filed with the Court of Appeals or the Supreme Court prior to the commencement date. However, the execution of any judgment resulting from such appeal or remand for further proceedings shall be directed to the court.
- Application of suspension to government financial institutions: the suspension of rights to foreclose or otherwise pursue legal remedies applies to government financial institutions, notwithstanding provisions in their charters or special laws to the contrary.
- Rescission of transfer/encumbrance of property: the court may rescind any transfer or encumbering of the debtor's unencumbered property that occurs after the commencement of the proceedings and is outside the ordinary course of business. However, the following transactions may be implemented upon a decision of the court, after notice and hearing:
 - payments made to meet administrative expenses of the proceedings as they arise;
 - payments to victims of quasi-delicts upon a showing that the claim is valid and the debtor has insurance to indemnify the debtor for the payment made;
 - sales of the debtor's unencumbered property if such is in the interest of administering the debtor and facilitating the preparation and implementation of a rehabilitation plan;
 - mortgages or pledges of property in order to provide a substitute lien under this Act;
 - payments made to repurchase property of the debtor that is auctioned off in a judicial or extra-judicial sale under this Act; or
 - payments made to reclaim property of the debtor pursuant to a possessory lien.
- Rescission of pre-commencement transactions: the court may rescind transactions that have occurred prior to the commencement date on grounds that they were executed with an intent to defraud creditors.
- Post-commencement interest: Interest on unsecured claims shall not accrue after the commencement date. Interest on secured claims owed by the debtor as of the commencement date shall accrue at the pre-default rates established by law or the debtor's contracts.
- Post-commencement credit: With the written concurrence of a majority in number of the committee of general unsecured creditors, the debtor may:
 - enter into credit arrangements on behalf of the debtor, the payments under which shall be considered an administrative expense; or
 - enter into creditor arrangements on behalf of the debtor, secured by mortgages of its unencumbered property or secondary mortgages of encumbered property with the approval of senior parties with regard to the encumbered property.
- Establishment of claims: a creditor must submit evidence of his claim within 45 days from the commencement date, otherwise, the claim is extinguished. The difference between the claimed and realised value of sold encumbered property of secured creditor becomes a subordinated claim, not an unsecured claim. The court is allowed to estimate a disputed, challenged or unliquidated claim for the purpose of determining a creditor's voting right in collective decision-making.
- The receiver: a receiver may be appointed by the court if the relief sought is suspension of payments, court-supervised rehabilitation, or pre-negotiated rehabilitation. The court shall appoint as receiver any qualified individual whose nomination is supported by more than 50% of the secured creditors and general unsecured creditors.
- General unsecured creditors committee: the court, within 30 days of the commencement date, on the basis of information provided by the conservator, shall appoint a committee of not more than 9 general unsecured creditors that have the largest such claims against the debtor, and that are willing to serve in such capacity. The members of the committee shall act with a view towards protecting the interests of the general unsecured creditors as a whole. The general unsecured creditors' committee shall have the right to:

- veto petitions for post-commencement financing requested by the conservator or liquidator;
 - authorise the conservator’s assumption of control of the debtor;
 - review the conservator’s or liquidator’s records in connection with the administration of the debtor;
 - remove the conservator or liquidator from his position; and
 - participate in a decision to extend the deadline for the submission of a rehabilitation plan.
- Remedies available:
 - Suspension of payments – this limited remedy provides a company with a moratorium on debt payments while it negotiates an out-of-court arrangement with its creditors. To prevent abuse, the moratorium is limited to only three months under the watch of a conservator. Further, if a debtor chooses this remedy, it is precluded from obtaining relief under court-supervised rehabilitation or pre-negotiated rehabilitation for an entire year thereafter. This “election of remedies” provision is designed to prevent debtors first trying suspension of payments, and then seeking rehabilitation (in effect, unnecessarily delaying the proceedings).
 - Court-supervised rehabilitation - this remedy contemplates the formulation of a plan under supervision of the court. The remedy may be availed of (a) by voluntary petition, or (b) upon conversion from liquidation petitioned involuntarily. The legislation establishes minimum standards for the plan to maintain transparency and fairness. The creditors vote on the plan according to specific classes (secured creditors, for instance would usually be a separate class). If the majority of each of the creditor classes (voting on the basis of size of claim) support the plan, the debtor submits the plan and evidence of such support to the court for final approval.
 - Pre-negotiated rehabilitation: the provision allows for accelerated judicial proceedings for debtors seeking ratification of a rehabilitation that was approved by a majority of the creditors before the debtor goes to court. While out-of-court debt restructuring is quite common, they suffer from the need of near unanimity amongst the creditors. Pre-negotiated rehabilitation allows a debtor to establish a comprehensive plan without needing to obtain unanimity, so long as the minimal standards in the legislation are met, and a majority of the creditors support the plan.
 - Liquidation: this is the final resort under the legislation. The liquidation provisions ensure that the debtor’s assets are sold quickly. The proceeds from the sale of mortgaged properties are distributed to the secured creditors. Proceeds remaining from such sales, and from sales of non-mortgaged properties are distributed as follows:
 - first, to meet unpaid administrative expenses;
 - second, to workers for back wages;
 - third, to the government for back taxes;
 - fourth, to all creditors not specifically mentioned; and
 - fifth, to creditors whose claims are subordinated by law or agreement.

If the court approves the plan it becomes binding on all creditors, even those who voted against it. If support from all the voting creditor classes is not obtained, the court may nevertheless approve the plan if evidence is shown that 80% of all the voting creditors support it. If this is not the case, the debtor comes under liquidation.

The proceedings are converted to liquidation in case of (a) late submission of plan (b) court failure to approve plan, and (c) debtor’s breach of plan.

G. Insolvency Law

1. **Question:** *What are the major substantive defects in the corporate insolvency law viewed from the respective positions of:*

(a) *banks/financial providers*

Answer: The banks and financial providers will not be able to enforce their claims, whether secured or unsecured, pending rehabilitation proceedings if a stay order is issued by the court.

(b) *secured creditors*

Answer: Under the Interim Rules, secured creditors will not be able to enforce their security pending rehabilitation proceedings as this is suspended by the stay order issued by the court.

(c) *unsecured creditors*

Answer: In addition to the suspension of their claims, there is great uncertainty as to whether unsecured creditors will be paid at all.

(d) *employees*

Answer: Claims of employees are also suspended during rehabilitation proceedings. They, however, enjoy preference in the event of liquidation if rehabilitation proves unfeasible.

(e) corporations

Answer: There is no discharge for corporations under the Insolvency Law.

(f) directors

Answer: In the event that a management committee is appointed for a company undergoing rehabilitation, such management committee takes the place of the board of directors of the corporate debtor.

(g) shareholders

Answer: In case a management committee is appointed for a company under rehabilitation, the board of directors elected by the shareholders becomes *functus officio*.

2. **Question:** *What are the major practical defects in the application of the insolvency law viewed from the respective positions of:*

(a) corporations

Answer: The rehabilitation receiver monitors the operations of the corporation.

(b) creditors

Answer: Delay in the enforcement of their claims.

H. Judicial System

1. **Question:** *Has there been any discernible improvement or change in the operation of the judicial system in relation to the conduct of:*

(a) debt collection/recovery processes

Answer: Under the Interim Rules, the stay order is time-bound, and shall in no case exceed 18 months from the filing of the rehabilitation case. This substantially limits the delay for the enforcement of creditors' claims.

(b) enforcement processes in respect of secured property rights

Answer: See Section H1 (a).

(c) recovery or enforcement processes in respect of leased property

Answer: See Section H1 (a).

(d) formal corporate insolvency processes?

Answer: Under the Interim Rules, a rehabilitation case must be dismissed if no rehabilitation plan is approved within 18 months from the filing of the case. This maximum period was the Supreme Court's response to the oft-repeated complaint that a rehabilitation case could virtually take place forever.

2. **Question:** *What reforms, if any, have been made to improve the operation of the judicial system in relation to the above 4 areas?*

Answer: See Section B of Addendum.

3. **Question:** *Are there any identifiable proposals for reforms in these areas?*

Answer: See Section B of Addendum.

4. **Question:** *What are the main problems or difficulties regarding the operation and application of the corporate insolvency law through the court system?*

Answer: See Section B of Addendum.

5. **Question:** *What practical improvements might be made to overcome these problems/difficulties?*

Answer: The enactment of definitive and time bound insolvency rules or laws which provide adequate protection to all concerned.

J. Insolvency Administration System

1. **Question:** *Comment on the extent of development, expertise and efficiency regarding both public and private sector administration of formal case of:*

(a) corporate liquidation

Answer: The RTC judges who exercise jurisdiction over debt relief cases cannot as of yet be considered specialists in insolvency and rehabilitation proceedings, in terms of mastery of the applicable law/procedure or experience in handling these types of cases. The RTCs are courts of general jurisdiction. While the Insolvency Law was enacted way back in 1909, there have been relatively few petitions for insolvency filed since then. As for rehabilitation, jurisdiction was transferred to the RTCs only in August 2000, and the Interim Rules were promulgated only in December 2000. In this sense, the experience of the court in handling these cases is limited.

There is also a perception that it is difficult to appoint private individuals to act as liquidators, either because of lack of training, or because of inadequate compensation for serving as such. At present, there is no institutionalised system of accreditation for these private individuals, so that it becomes more difficult for the courts and other interested parties to identify who can be appointed as liquidators. There is also no system of training for court-appointed liquidators, nor is there a Code of Conduct governing them. These are believed to be important components in improving the administration of corporate liquidation.

(b) corporate reorganisation

Answer: The SEC is generally not involved in corporate reorganisation. There is however a procedure known as quasi-reorganisation where a corporation's assets are written up following an appraisal indicating an appraisal surplus which is utilised to wipe-out a deficit in the equity account. Quasi-reorganisations require the approval of the SEC.

2. **Question:** *Is it considered that education and training in these areas would be valuable and, if so, in what areas?*

Answer: We are aware of several seminars for judges dealing with or intended to train judges in handling rehabilitation cases. Included in the training modules are financial issues and other aspects related to insolvency/rehabilitation cases. It may be helpful to train these judges to seminars/workshops in other jurisdictions so that they will learn how similar cases or situations are handled in other jurisdictions.

3. **Question:** *Is it considered desirable to introduce more formal structures of both public and private sector administration of insolvency cases?*

Answer: For insolvency law reform to be completed, a new law should be enacted providing not only a new insolvency regime but also the upgrading of skills of both public and private sector participants in the administration of insolvency cases.

L. General Insolvency Information and Developments

1. **Question:** *Provide details of any other relevant information or developments since January 1999 in regard to such issues as the effect of insolvency law policies on areas such as employment, fiscal/revenue debts, detection and recovery of corporate fraud, domestic and foreign investment and etc.*

Answer: More than a few have expressed the view that one reason for the continuing reluctance of banks to lend is the unclear insolvency regime existing in the country at present. They point out that banks would not want to lend as they are not certain if they can recover payment and enforce their security. However, we are not aware of any formal study that has been conducted recently to validate this view. There have also been reports that due to the difficulties being encountered by export credit agencies in the debt-relief petition of Philippine Airlines, export credit agencies are not

inclined to extend credit to Philippine companies for fear that recovery of machinery and equipment, the object of the credit, may be difficult to recover once a petition for suspension of payments or other similar proceedings is filed before the courts.

2. **Question:** *Is there any evidence of a change in attitudes (such as social/commercial stigma, aversion to strict legal processes, fear of loss of control) toward the use of:*

(a) formal insolvency processes; and

(b) informal insolvency processes

in respect of corporations in financial difficulty or insolvent corporations? If possible, provide details of any specific cases which might reflect evidence of change.

Answer: The fear of social stigma attached to insolvency cases is no longer as pronounced as before. While it is still a concern, it hardly plays a key role in deciding whether or not to seek debt relief under the formal, much less the informal, insolvency process.

B. The efficiency of the administration of justice in the participating countries

Question: *Some of the sections in the Report and the Addendum to that Report referred to in A above also address the administration of justice in the Philippines. Please advise as to the extent to which the Report and the Addendum to that Report are accurate in this respect and also advise of any amendments or modifications which should be made to those aspects of the Report or the Addendum to that Report.*

Answer: See Part A of this Report, where we have indicated the amendments/ changes.

C. Treaty

1. **Question:** *To what regional treaties providing for economic cooperation or designed for the facilitation of trade is the Philippines a party?*

Answer: The Philippines is a member of the Association for Southeast Asian Nations ("ASEAN") which was created through the Bangkok Declaration in 1967. The members of the ASEAN through the Singapore Declaration of 1992 entered into an agreement creating the ASEAN Free Trade Area ("AFTA"), which is also being implemented through the Framework Agreement on Enhancing ASEAN Economic Cooperation (the "Framework Agreement") and the Agreement on the Common Effective Preferential Tariff ("CEPT") Scheme for the AFTA (the "CEPT Agreement").

2. **Question:** *What are the terms of those treaties?*

Answer: The creation of AFTA and its implementation through the Framework Agreement and the CEPT Agreement were intended principally to increase trade among the members through the reduction of tariff and non-tariff barriers, creation of a CEPT, harmonisation of standards, reciprocal recognition of tests and certifications, removal of barriers to foreign investments, macroeconomic consultations, rules of fair competition and promotion of venture capital. Under the CEPT Scheme, the tariff for pre-identified manufactured products originating from a member State will be progressively reduced, if not totally eliminated within a period of 15 years or until 2008 (later moved to 2003). Agricultural products are, however, excluded from the CEPT Scheme.

3. **Question:** *What are the mechanisms for amending those treaties?*

Answer: The CEPT Agreement provides that any amendment to such agreement shall be made by consensus, and shall become effective upon acceptance by all Member States. Amendments are generally done by the adoption by the Members of protocols which will set forth the particular modifications agreed upon by the parties. Moreover, it is not settled under Philippine law whether an agreement such as this, including its amendment, will need the concurrence of the Philippine Senate to become valid and effective. Under the Philippine Constitution "no treaty or international agreement shall be valid unless concurred in by at least two-thirds of all the members of the Senate."

4. **Question:** *Can a signatory to those treaties reserve its position in respect of any amendment with a right to "opt in" either generally or with a prescribed period of time?*

Answer: The CEPT Agreement provides that no reservation shall be made with respect to any provisions of the agreement. We believe that since amendments may only be done by consensus, no reservation is likewise allowed for amendments.

5. **Question:** *Do those treaties provide for resolution of trade or other disputes?*

Answer: Although the Singapore Declaration and the CEPT Agreement provided for the establishment of a ministerial-level Council to supervise, coordinate and review the implementation of the agreement, it has not provided for a judicial or even quasi-judicial mechanism to settle trade or other disputes. The CEPT Agreement, however, provides that "any difference between the Member States concerning the interpretation or application of this Agreement shall, as far as possible, be settled amicably between the parties." If the parties fail to settle amicably, it shall be submitted to the aforementioned council and, if necessary, to the ASEAN Economic Ministers ("AEM"). The agreement does not provide for a formal dispute resolution process or a statement relating to the binding nature of the decisions of the council or of the AEM.

6. **Question:** *Do those treaties otherwise provide for a collaborative approach to addressing issues of mutual interest?*

Answer: The CEPT Agreement encourages the Member States to accord adequate opportunity for consultations regarding any representations made by other Member States with respect to

any matter affecting the implementation of the agreement.

7. Question: *Do those treaties provide for an exchange of information on issues of mutual interest?*

Answer: The CEPT Agreement does not contain a specific provision on exchange of information.

8. Question: *Do any of those treaties address the harmonisation of laws which may effect economic relations between the member countries? If so, what are the relevant treaties and stipulations contained in them?*

Answer: No, although they aim to remove barriers to foreign investments and promote macroeconomic consultations.

D. Actual Outbound cross-border cases

1. Question: *In the course of the last five years, are you aware of there having been any companies which were incorporated in the Philippines which have been placed under some formal insolvency administration and which have had assets and/or liabilities in countries other than the Philippines? If so, please identify those companies.*

Answer: The Philippine Airlines, Inc. ("PAL"), which is the Philippine flag carrier, was placed under rehabilitation proceedings, by the SEC. This is, to our best knowledge, the only Philippine company with assets and/or liabilities outside the Philippines, that have been placed under some formal insolvency administration in the last 5 years.

2. Question: *In the case of each of those companies, are you aware of how those non-Philippine assets and liabilities were administered? If so, in each case, please provide a general description of the process of administration.*

Answer: As far as we know, the SEC included the non-Philippine assets and liabilities of PAL in the rehabilitation proceedings.

3. Question: *In the case of each of those companies and so far as you are aware, were non-Philippine creditors permitted to file their claims in the formal insolvency administration being conducted in the Philippines? In any case, were any of those non-Philippine creditors required to obtain a judgment in the courts of the Philippines or otherwise undertake a formal procedure in the Philippines as a pre-requisite to filing their claims?*

Answer: As far as we are aware, PAL's non-Philippine creditors were permitted to file their claims in the rehabilitation proceedings without being required to obtain a judgment in any Philippine court.

4. Question: *In the case of each company and so far as you are aware, did any of the non-Philippine creditors exercise their rights by pursuing claims against the non-Philippine assets of the company? If so, was there any procedure or process either available to or invoked by the insolvency administrator of those companies in the Philippines to restrain the form doing so?*

Question: Some foreign creditors of PAL attempted to take possession of aircrafts in the United States. To our knowledge, PAL was able to get an injunction on the basis of the rehabilitation proceedings that was then taking place in the Philippines.

E. Actual in-bound cross-border cases

1. Question: *In the course of the last five years are you aware of there having been cases of companies which were incorporated other than in the Philippines which have been placed under some form of insolvency administration and which have had assets and/or liabilities in the Philippines? If so, please identify those companies.*

Answer: Yes. In the 14 June 2002 issue of the Business World¹⁷, a notice was published requiring creditors to prove their claims against the HSBC Investment Bank Asia Limited, a company incorporated in Hong Kong, which is undergoing liquidation proceedings in Hong Kong.

2. **Question:** *In the case of each of those companies, are you aware of how its assets and liabilities in the Philippines were administered? If so, in each case, please provide a general description of the process of administration.*

Answer: N/A

3. **Question:** *In each case and so far as you are aware, in the case of Philippine creditors, were they permitted to file their claims in the formal insolvency administration of the company being conducted in its place of incorporation?*

Answer: Yes. As a matter of fact, the notice regarding HSBC Investment Bank Asia Limited requires creditors to submit proof of their claims to the liquidator on or before 28 January 2003.

4. **Question:** *In the case of each of those companies and so far as you are aware, did any of the Philippine creditors exercise their rights by pursuing claims against the Philippine assets of the company? If so, was there any procedure or process either available to or invoked by the insolvency administrator of the company in its place of incorporation to restrain those creditors from doing so?*

Answer: N/A

F. Hypothetical inbound cross-border insolvency case

Assume that ABC Limited (“ABC”) is incorporated in Singapore and trades through a branch in the Philippines with the result that it has assets and liabilities there. ABC is ordered to be wound up by order of the Singaporean Courts and a liquidator is appointed to administer its affairs. The liquidator wishes to take control of and administer the assets of ABC in the Philippines or, alternatively, arrange for their administration. She also wishes to arrange for all creditors of ABC, whether resident in Singapore, in the Philippines or elsewhere, to file their claims in Singapore so that those claims can be dealt with equitably and consistently.

Assuming that there is presently no procedure in the Philippines for recognising the liquidation of ABC in Singapore:

1. **Question:** *What procedures can be invoked in the Philippines for placing ABC under a formal insolvency administration?*

Answer: The procedure provided under Act. No. 1956, otherwise known as the Insolvency Law, can be invoked. Under this law, an insolvent debtor who owes debts exceeding one

thousand pesos, may file a petition for voluntary insolvency.¹⁸ An adjudication of insolvency may also be made on the petition of three or more creditors, residents of the Philippines, whose credits accrued in the Philippines, totalling not less than P1,000 (involuntary insolvency).¹⁹ Corporations, however, are not entitled to discharge; its properties, both present and future, are answerable for its past obligations.

The general procedure for voluntary insolvency proceedings is as follows:

- Filing of the petition with the appropriate RTC by a debtor who owes at least P1,000. The following must be attached to the petition.
 - Schedule – an enumeration of his debts, names of creditors, how much he or she owes to each, and the nature of each debt, whether secured or not secured.
 - Inventory – an accurate description of all his or her real and personal properties not exempt from attachment or execution, excluding the family home.
- On the same day that the petition is filed, and if the petition is in order, the court shall issue an order of adjudication (i.e. that the debtor is declared insolvent).
- Publication of the order declaring the debtor insolvent, as many times as the court may deem proper.
- Meeting of creditors for the election of an assignee in insolvency.
- Conveyance of debtor’s property to assignee in insolvency.
- Liquidation of assets and payment of debts.

The general procedure for involuntary insolvency proceedings is as follows:

- Filing of the petition with the appropriate RTC by three or more creditors, residents of the Philippines, whose credits amount to at least P1,000 and accrued in the Philippines.
- The court issues an order directing the debtor to file its answer or a motion to dismiss, and to show cause why it should not be declared insolvent; in the same order, or subsequently, upon good cause shown, the court may also prohibit payments to the debtor of any debts due him, delivery to the debtor of any property belonging to him, and the transfer of any property by the debtor.
- A copy of the order directing the debtor to file his answer, together with a copy of the petition, will be served by personal service on the debtor at least 5 days before the time fixed for the hearing.

¹⁸ Section 14, Insolvency Law.

¹⁹ Section 20, Insolvency Law.

- Trial/Hearing
- If, after trial, the issues are found in favour of the petitioning creditors, the court will issue an order declaring the debtor insolvent as of the time of the filing of the petition and will direct him or her to file a schedule of its debts and liabilities and an inventory of its assets within a period not exceeding three days. In the same order, the court will:
 - direct the sheriff to take possession of, and safely keep, all the real and personal property of the debtor, including deeds, vouchers, books of account, bonds, bills, and securities, except those which are exempt from execution;
 - prohibit payments to the debtor of any debts due him, delivery to the debtor of any property belonging to him, and the transfer of any property by the debtor;
 - call a meeting of the creditors for the election of the assignee of the estate of the debtor and setting the date, place, and time of said the meeting, which date shall not be less than two nor more than eight weeks from the date of the order; and
 - direct the publication of the order for the number of times the judge may deem proper; and designate the newspaper where the order should be published, which newspaper must be of general circulation in the province or city in which the petition is filed or, if there is none, a newspaper which, in the opinion of the judge, will best give notice to the creditors.

If the decision is in favour of the debtor, the petition will be dismissed.

- If the debtor is declared insolvent, the clerk of court will immediately cause the publication of the order in the newspaper and for the number of times prescribed by the judge. If the debtor files the required schedule before the date set for the meeting of the creditors, the clerk of the court will also furnish the creditors appearing in the schedule with a copy of the order, either by personal delivery or by registered mail. If the schedule is not filed before the date set for the meeting of the creditors, the publication of the order constitutes sufficient notice to the creditors of the date and place of the meeting.
- Meeting of the creditors to elect an assignee. The creditors will elect the assignee in open court. The majority of the creditors who have proven their claims, majority being in terms of number and amount, must concur in the election of an assignee.

- The clerk of court will assign and convey to the assignee all the property of the insolvent.
- Liquidation of assets and payment of debtor's obligations.

2. **Question:** *In the case of each of those procedures, does the Singaporean appointed liquidator have standing to initiate the necessary application? If not, then in the case of each procedure in which the Singaporean appointed liquidator does not have that standing, who does have standing?*

Answer: Section 14 of the Insolvency Law states that "(a)n insolvent debtor, owing debts exceeding one thousand pesos, may file a petition for insolvency." Thus, if the Singaporean appointed liquidator is authorised or deemed authorised by ABC to institute insolvency proceedings in the Philippines, he has standing to file the petition. However, if the order of liquidation in Singapore is in the nature of an involuntary liquidation, and the Singaporean appointed liquidator is not authorised by ABC to initiate insolvency proceedings in the Philippines, he may not have the personality or standing to do so.

Involuntary insolvency proceedings may be initiated by three or more creditors, residents of the Philippines, whose credits amounting to at least P1,000 accrued in the Philippines.

3. **Question:** *In the case of each procedure, to whom is the necessary application made for an order directing the establishment of a formal insolvency administration?*

Answer: A petition for voluntary insolvency must be filed in the RTC of the city or province where the petitioning debtor has resided for 6 months next preceding the filing of the petition. In the case of corporations, the place of residence is the place where the principal office of the corporation is located in the Philippines.

A petition for involuntary insolvency must be filed in the RTC of the city or province where the debtor resides or has its principal place of business.

4. **Question:** *In the case of each procedure, how long does it typically take to obtain an order or other direction establishing a formal insolvency administration?*

Answer: In voluntary insolvency, upon the filing of the petition, the court will immediately issue an order declaring the petitioning debtor insolvent. In practice, this may take from a day to a week. In involuntary insolvency, a trial is

held to determine whether or not the allegations in the petition are true. It is only after trial, and a determination by the court that the allegations in the petition are true, that it issues an order declaring the debtor insolvent. This may take up to a year, or even more.

5. **Question:** *In the case of each procedure, is it possible to obtain some interim or the like order or direction which secures the independent control of the assets of ABC in the Philippines pending the final determination of the application for an order or other direction establishing formal insolvency administration?*

Answer: In voluntary insolvency, the order declaring the petitioning debtor insolvent is issued almost immediately upon the filing of the petition. In the same order, the sheriff is directed to "take possession of, and safely keep, all the real and personal property of the debtor, including deeds, vouchers, books of account, bonds, bills, and securities, except those which are exempt from execution." Upon the appointment of the assignee, the sheriff conveys all of the debtor's assets to him.

In voluntary insolvency, upon the filing of the petition, and pending the issuance of the order of insolvency, the judge will issue an order directing the debtor to file an answer at the time and place fixed in the order, and show cause why he should not be declared insolvent. In the same order, or subsequently, upon good cause being shown, the court may also prohibit payments to the debtor of any debts due him, delivery to the debtor of any property belonging to him, and the transfer of any property by the debtor.

6. **Question:** *In the case of each procedure, what does it typically cost to obtain a final order or direction establishing a formal insolvency administration?*

Answer: It is difficult to make an estimate of the cost to prosecute an insolvency proceeding. Law firms and lawyers in the Philippines have different billing practices and rates. In addition to lawyers, it is almost always necessary to also engage the services of accountants.

7. **Question:** *In the case of each procedure, to what extent do the Philippine creditors enjoy priority to or preference over non-Philippine creditors in the context of that procedure?*

Answer: The Insolvency Law makes no distinction between creditors solely on the basis of nationality or place of incorporation.

8. **Question:** *In the case of each procedure, may the Singaporean and other non-Philippine creditors of ABC file their claims in the formal insolvency administration established under the procedure? If so, what formal procedures or pre-requisites have to be satisfied by those creditors prior to them filing their claims?*

Answer: Singaporean and other non-Philippine creditors of ABC may file their claims in the insolvency proceedings by filing a verified notice of claim before the insolvency court at least 2 days before the date of the meeting of the creditors for the election of the assignee. This is the same procedure for Philippine creditors.

G. Hypothetical outbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in the Philippines and trades through a branch in Singapore with the result that it has assets and liabilities in Singapore. ABC is placed under a formal administration in the Philippines and an independent trustee is appointed to administer its affairs.

1. **Question:** *Is there any procedure available in the Philippines which will facilitate an application to the courts in Singapore for the establishment of an independent insolvency administration of ABC?*

Answer: None.

2. **Question:** *If so, please describe that procedure.*

Answer: N/A

3. **Question:** *Does the fact that the principal insolvency administration of ABC is initiated in the Philippines as distinct from the insolvency administration of a company's branch affect the answers to F7 or F8?*

Answer: No.

Supplementary Questions

1. **Question:** *To what regional inter-governmental arrangements relating to economic corporation, facilitation of trade, investment protection, or mutual recognition of administrative or judicial process is the subject country a party? (Such arrangements might include regional treaties, non-treaty agreements, cooperative schemes, or regular forums at the ministerial or official level.)*

Answer: No answer provided.

2. **Question:** *Which (if any) are the other countries that are party to such arrangements.*

Answer: No answer provided.

3. **Question:** *Does any such arrangement refer to and deal with insolvency, either specifically or within the generality its terms?*

Answer: No answer provided.

4. **Question:** *Which ministry or agency has or would have responsibility for negotiating and administering arrangements on mutual recognition in the field of insolvency?*

Answer: No answer provided.



Asian Development Bank

Promoting Regional Cooperation in the
Development of Insolvency Reform

RETA 5975

Draft Country Report for Singapore Conference
Cross-Border Insolvency – Indonesia, Korea,
Philippines and Thailand

Thailand

A. The provisions

The provisions of the existing insolvency laws of the participating countries as well as any proposed reforms

Question: Please advise as to the extent to which the materials in Section I, J, K, L, O, P and Q of the Report and Sections B, G, H, J and L of the Addendum to that Report continue to be accurate. If those sections of the Report and the Addendum to that Report require amendment or modification, please advise of the amendments or modifications.

Report on Thailand – produced under Asian Development Bank Technical Assistance No. 5795 – REG

Answer: Sections I, J, K, L, O, P and Q of the Original Report continue to be accurate. These sections are reproduced below.



Section I – Insolvency Law Regime

[Note: It would be helpful in this section if, where it is relevant to the answer, the relevant sections or articles of the insolvency law were identified]

1. Underlying philosophy

a) **Question:** *What is the underlying philosophy of the insolvency law of this economy? (For example is it distributive, rehabilitative or penal?)*

Answer: Bankruptcy law in Thailand is part of the body of commercial law. It is designed both to help a debtor to rehabilitate, if possible, through the reorganization provisions, as well as distribute the debtor's property between debtors. It attempts to achieve fairness for both debtor and creditors.

b) **Question:** *Are there elements of more than one philosophy present in the insolvency law of this economy?*

Answer: Except for the concept in clause (a), Thai bankruptcy law also wants to give a debtor a chance of release from their debt by compromise or cancellation and allowing the debtor to continue their business through re-organization proceedings for debtors in financial difficulties.

c) **Question:** *Briefly describe the relevant elements, and if applicable, any penal sanctions available.*

Answer: Advantages for creditor:

- Equality for all creditors of equal rank;
- Convenience and low expense for creditors;
- For following the properties better than in Civil case.

Advantages for debtor:

- Helps an honest debtor overcome bankruptcy through use of the compromise rule, deposition from bankruptcy or cancellation of bankruptcy;
- Having criminal sanctions for dishonest debtors.
- Limited rights and duties of the debtor such as the debtor must do business in a manner that is transparent for the receiver.

Advantages for public:

- Protection for the public from further damage from a debtor by having a declaration in a newspaper and gazette that the debtor is in receivership.

Criminal sanctions of a fine or imprisonment are applicable if:

- The debtor leaves the Kingdom, unless with the written permission of the court or the receiver, and, if he changes his address, he must report the new address within a reasonable time in writing to the receiver.
- The debtor does not go to meetings of the creditors.
- The debtor does not assist to the utmost of his capacity in the realization of his asset.
- The debtor objects to the receiver entering into any place of residence or business of the debtor to examine assets, seals, accounting ledgers, or documents of the debtor.
- The debtor does not deliver all the assets, seals, accounting ledgers, and documents relating to his asset and business to the receiver.
- The debtor does not explain his business and assets to the receiver.
- The debtor removes, conceals, destroys, causes damage to or alter seals, accounting ledgers, or documents relating to his business or assets.

2. Jurisdiction in insolvency matters

a) **Question:** *In which judicial category of insolvency law classified in the legal system of this economy? (For example civil, commercial or administrative.)*

Answer: Insolvency law comes under the Civil law classification in Thailand.

b) **Question:** *Which Courts, tribunals or administrative bodies in this economy are competent to exercise jurisdiction in insolvency matters?*

Answer: The Civil Courts and the Provincial Courts are competent to exercise jurisdiction in insolvency matters.

c) **Question:** *Are any limitations placed on the jurisdiction of any of these bodies?*

Answer: The only limitations placed on the jurisdiction of the Court of Justice of Thailand is with regard to the execution of a judgment. Thai judgments are not recognized in other countries, nor will foreign judgments be recognized in Thailand. Although foreign judgments may be used in evidence, cases must be reinstigated in a court of justice in Thailand.

3. Types of insolvency procedures

a) **Question:** *What types of insolvency procedure are available in the legal system of this economy for the administration of corporate debtors in financial difficulty? (For example bankruptcy, liquidation (winding up), receivership, restructuring or other forms of administration.)*

Answer: There are three types of insolvency procedures available in the legal system of Thailand for the administration of corporate debtors in financial difficulty. The first type is the "straight" bankruptcy procedure. The receiver will administrate the debtor's business. The second type is the restructuring procedure under the bankruptcy legislation. The planner or the plan administrator will administrate the debtor's business. The third type is liquidation. During the liquidation process, the liquidator, once he has

found that the company's assets shall not cover its liabilities, must file a petition to the court to order a bankruptcy. The law generally stipulates that liquidation shall be in accordance with applicable bankruptcy laws, as permissible. However, a person may not enter into a liquidation voluntarily under the CCC as the Bankruptcy law stipulates its procedures otherwise. In short, a debtor under a bankruptcy case must comply with the procedures under the Bankruptcy Act. Liquidation is managed by a corporate liquidator

1 Comparison Between CCC & Bankruptcy Act

| Liquidation under CCC | Bankruptcy Act |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> Initiated by an authorized liquidator. | <ul style="list-style-type: none"> Initiated by a creditor. |
| <ul style="list-style-type: none"> Case entered by a one-sided petition. | <ul style="list-style-type: none"> Relevant parties shall be officially informed and involved. |
| <ul style="list-style-type: none"> Liquidator must file a petition as soon as it becomes known that the assets will not cover liabilities. | <ul style="list-style-type: none"> Timing depends on the petitioner(s). |
| <ul style="list-style-type: none"> Liquidator must prove that the company's assets do not cover liabilities. Court's consideration is largely based on finance and account documents and the liquidator's persuasion. | <ul style="list-style-type: none"> Petitioner must prove that the debtor is insolvent; and there are no reasonable grounds that the debtor might be able to repay its debts or other grounds that the debtor should not be placed under receivership. Debtor's situation, actions and other related circumstances will be taken into consideration. |
| <ul style="list-style-type: none"> Debtor voluntarily consents to be placed in bankruptcy. | <ul style="list-style-type: none"> Exposure to the disputes. |
| <ul style="list-style-type: none"> Procedures and legal steps not specifically detailed. | <ul style="list-style-type: none"> Procedures and legal steps are stipulated under the law. |
| <ul style="list-style-type: none"> Liquidation managed by the corporate liquidator. | <ul style="list-style-type: none"> Under Court control and if the debtor is placed under receivership, their business is controlled by receiver. |

b) Question: Briefly describe the main features of each type of insolvency procedure for corporate debtors: including, for example the manner in which each procedure is initiated and administered, and the aims of each procedure.

Answer: The main features for straight bankruptcy procedure is to place the debtor under absolute receivership in order to end the business operation of the debtor and to divide the debtor's assets.

The main feature of the rehabilitation procedure is to help a debtor who faces a liquidity problem by affording an opportunity to rehabilitate his business before being bankrupted.

The main feature for the liquidation procedure is that a debtor voluntarily consents to be placed in liquidation.

c) Question: Identify the relevant legislation governing each type of insolvency procedure available for corporate debtors.

Answer: The legislation governing both types of bankruptcy proceedings available for corporate debtors is the *Bankruptcy Act*. The legislation governing the liquidation process is contained in the Civil & Commercial Code sections 1247 - 1273.

4. Commencement of insolvency procedures

a) Question: Is it usual or customary in respect of a corporate debtor which is insolvent to attempt to negotiate an informal administration before formal insolvency procedures are commenced?

Answer: It is usual in respect of an insolvent corporate debtor to attempt to negotiate with its creditors for an extension period for repayment of the debt if it is considered that there is no other choice. Where negotiations fail, the formal insolvency procedure may be commenced.

b) Question: In relation to each type of insolvency procedure available in the legal system of this economy, who may commence the procedure? (For example the corporate debtor, secured creditors, unsecured creditors, directors, shareholders, the State.)

Answer: The Plaintiff of the straight bankruptcy procedure may be the secured or unsecured creditors or the liquidator of the corporate debtor after the liquidation process.

The persons who may commence the rehabilitation procedure are as follows:

- (1) A creditor or several creditors whose debts in aggregate total an amount that exceeds Baht 10 million.
- (2) A debtor having the following qualifications:
 - is a limited company or any juristic person as provided in the Ministerial Regulations;
 - is insolvent;
 - one or several creditors whose debts in aggregate total an amount exceeding Baht 10 million, regardless of whether or not such debts are immediately due or become due in the future;
 - no order issued against it by the Court to place the assets in absolute custody;
 - no order from the Court or Registrar issued against it or from any other causes to dissolve or revoke its registration or has not yet registered to dissolve it.
- (3) The Bank of Thailand, in case where the debtor is a commercial bank, finance company, finance and securities company or a credit financing company.
- (4) The Office of the Securities and Exchange Commission, in cases where the debtor is a securities company.
- (5) An insurance company, where the debtor under (2) above is a life or accident insurance company.
- (6) The government agencies empowered to oversee the debtor's business for debtors under (2) above.

(Bankruptcy Act (No.4) B.E. 2541, Article 90/4).

For the liquidation procedure, a resolution from the shareholders of the corporate to wind up the company is required. A liquidator will then be appointed. As soon as the appointment is made, the liquidator is the sole manager of the corporate business.

c) Question: On what basis may each type of insolvency procedure be commenced, or what requirements must be satisfied before the procedure may be commenced? (For example non-payment of debts; balance sheet/cash flow insolvency; trading losses; resolution by directors to enter insolvency procedure.)

Answer: Legal prerequisites and requirements for a formal insolvency procedure to be commenced are:-

- (1) The debtor is insolvent;

- (2) The debtor who is an ordinary person is indebted to one or several entities amounting to not less than Baht fifty thousand, or the debtor who is a juristic person is indebted to one or several plaintiffs amounting to not less than Baht five hundred thousand; and
- (3) The said debt may be determined in a definite amount irrespective of whether it becomes due for payment immediately or at a future date.

(Bankruptcy Act B.E. 2483, Section 9).

Where the petition is filed by a secured creditor, the following conditions also apply:

- (1) The creditor is not prohibited from the enforcement for the settlement of debts from the debtor's assets in excess of that placed as a security; and
- (2) The creditor must state in the complaint that if the debtor becomes bankrupt, he is willing to waive the security for the benefit of all creditors, or make an appraisal of the security in the complaint which, after deduction of the obligation due to him, is still in the deficit for the debtor who is an ordinary person in the amount not less than Baht 50 thousand or for a debtor who is a juristic person in the amount not less than Baht 500 thousand.

(Bankruptcy Act B.E. 2483, Section 10).

In general, the creditor is required to establish that the debtor is insolvent i.e. his assets do not cover his liabilities. In this matter, if there is undisclosed information about the assets and liabilities not known to the creditor, the debtor will be able to raise its defense based on one-sided information which cannot be properly verified by the creditor. Therefore, to avoid any difficulties during the Court inquiries in this matter, the presumptions as specified by law (see below) should be taken into consideration in order to expedite the initial proceedings and proceed with the details of the complaint. Normally, a petitioning creditor would conduct a search on the debtor or take formal action against the debtor to be in compliance with at least one of the prescribed legal presumptions. In most cases, issuance of formal notices under the highlighted clause 9 below is selected as it is the safest and least difficult way. Other alternatives may be selected upon an assessment of sufficient grounds but the formal notice method may be conducted concurrently. Please note the following available presumptions of insolvency:

- (1) If the debtor transfers assets or rights in management of his assets to other persons for the benefit of all his creditors whether such an act is done within or outside the Kingdom.
- (2) If the debtor transfers or delivers his assets with dishonest or fraudulent intent whether such act is done within or outside the Kingdom.
- (3) If the debtor transfers his assets or creates any right over such asset which, if the debtor were a bankrupt, would be deemed as an act of preference whether such act is done within or outside the Kingdom.
- (4) If the debtor does any of the following acts in order to delay payment of his debt, or in order to prevent a creditor from receiving payment of the debt:
 - a. leaves the Kingdom, or, having previously left, remains outside the Kingdom;
 - b. leaves the premises in which he has resided, or conceals himself in any premises, or absconds or leaves by other means, or closes his place of business;
 - c. removes assets out of the jurisdiction of the court;
 - d. consents to judgment ordering the payment of money which he should not pay.
- (5) If the debtor has had his assets attached under a writ of execution, or there is no asset of any kind capable for attachment for payment of the debt.
- (6) If the debtor declares to the court in any action that he cannot pay his debts.
- (7) If the debtor informs any of his creditors that he cannot pay his debts.
- (8) If the debtor submits to any two or more of his creditors a proposal for composition of his debts.
- (9) If the debtor receives demand letters from his creditor not less than twice, at intervals of not less than 30 days, and the debtor does not pay the debt.

(Bankruptcy Act B.E. 2483, Section 8).

The legal prerequisites and requirements for filing a rehabilitation petition are:-

- a debtor whose debts in aggregate to one or more creditors total an amount exceeding Baht 10 million, regardless of whether or not such debts are immediately due or become due in the future.
- the name(s) and address(es) of the creditor(s)

to whom the debtor owes in aggregate at least Baht 10 million;

- reasonable grounds and methods for reorganizing business operations;
- the name and qualifications of the proposed planner;
- the consent of the planner;
- a list of assets and liabilities (if the petitioner is the debtor).
- consent of the authorities where applicable as follows:

1. The Bank of Thailand, where the debtor is a commercial bank, finance company, finance and securities company or a credit financing company.
2. The Office of the Securities and Exchange Commission, where the debtor is a securities company.
3. The Insurance Department, where the debtor is a casualty insurance company or a fire insurance company.
4. The government agencies empowered to oversee the debtor's business government agency and in such case the debtor shall be in compliance with the provisions stipulated in the Ministerial Regulations.

(Bankruptcy Act (No.4) B.E. 2541, Articles 90/4, 90/6).

The liquidator will commence the case with the court on the above bankruptcy grounds for such corporate as soon as it becomes known to the liquidator that the assets will not cover liabilities. The liquidator must prove that the company's assets do not cover liabilities. The Court's consideration is largely based on balance sheets and accounting documents, and the liquidator's powers of persuasion.

(d) Question: *How is each type of insolvency procedure commenced? (For example by application to the Court, by administrative act, by written notice to the business organization.)*

Answer: The straight bankruptcy procedure is commenced by a creditor filing a complaint with the civil court or provincial court.

Rehabilitation procedures are commenced by the eligible petitioner filing a petition with a civil or provincial court in accordance with the debtor's domicile.

The liquidation procedure is commenced by a corporate's liquidator filing a case with the court requesting the court to order the corporate debtor bankrupt.

e) Question: *What is the usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor?*

Answer: The usual time period between the commencement of formal insolvency proceedings and the declaration or imposition of a formal administration on the corporate debtor will be dependent on whether or not a defence is mounted. If the Defendant does not defend itself in Court, it will take approximately 3-4 months for an absolute receivership order to be made against the Defendant. If the Defendant offers no defence, it will take approximately 1 year for the issuance of a final order.

f) Question: *How effective is the judicial or court system (or administrative system) in relation to the handling of formal insolvency proceedings?*

Answer: The court system in relation to the handling of formal insolvency proceedings is quite effective except for the procedural delays involved with the hearing of cases.

5. Effect of insolvency procedures

a) Question: *In relation to each type of insolvency procedure available in the legal system of this economy, what is the effect on the corporate debtor, its constituent parts and its business relationships of initiation of the relevant insolvency procedure?*

(For example, how does initiation of the insolvency procedure affect:

- the powers of management of the debtor;
- the interests of owners/shareholders of the debtor;
- contracts to which the debtor is a party;
- legal proceedings to which the organization is a party;
- remedies available to persons in contractual (non-debt) relationships with the debtor).

Answer: The "Straight" Bankruptcy Procedure

There is an effect on the corporate debtor only when the court orders the debtor to be placed in receivership. In such a situation, the Receiver solely has the following powers:

1. to manage and dispose of the assets of the debtor, or do any necessary act to complete any pending business of the debtor;
2. to collect and receive money or asset that belong to the debtor, or which the debtor is entitled to receive from others;

3. to compromise, come to a settlement, file actions, or defend actions, relating to the assets of the debtor.

(Bankruptcy Act B.E. 2483, Sections 141-148).

When the court has ordered the debtor to be placed under receivership, it is prohibited for the debtor to do any act relating to its assets or business except by order or approval of the court, the Receiver, the administrator of the assets, or of a creditors' meeting. When a temporary receivership order is made, the receiver, with the assistance of the petitioning creditor, will have the power to manage the debtor's business.

The Receiver, once appointed, is required to join in all civil actions relating to the assets of the debtor that may be pending in court at the time when the court orders the debtor to be placed under receivership, and when the receiver applies by motion, the court is empowered to order the cessation of the hearing of civil actions, or make any other order it may deem appropriate. Where the Receiver joins a pending action on behalf of the debtor and such a case is lost, the judgment creditor is entitled to file a claim for repayment of debt within 2 months from the date of final judgment for the action.

Any person who has suffered a loss because of the attachment of his assets which are in the possession of the debtor at the time the receivership order is made, because of the cancellation of any transfer of asset or any other act during the three months prior and subsequent to an application to adjudicate him as bankrupt, or because of the refusal to accept any asset or any right under a contract is subject to terms more onerous than the benefits receivable thereunder made by the Receiver, is entitled to file a claim for repayment of debt for the price of the goods, the original debt, or for any loss, as the case may be, within 2 months but such period shall be calculated starting from the date when such right to claim repayment accrued. If the dispute has been taken to court, the calculation shall be as from the date of final judgment for such action (Sections 91, 92 of Bankruptcy Act).

Rehabilitation Procedure

Where the court has accepted a petition for business reorganization under Article 90 of the Bankruptcy Act and the planner is appointed, the planner will have the power and duties in managing the business and assets of the debtor. If there is no planner first nominated, the power and duties of the debtor executive in managing the business and assets ceases. The court will

appoint one or more persons or the debtor's executive in the interim to manage the business and assets of the debtor under the supervision of the receiver until a planner is appointed. For the period it is not possible to issue an order to appoint an interim executive, the receiver shall have the temporary power to manage the business and assets of the debtor. In respect of the supervision, the receiver determines the powers and duties including ordering the interim executives to prepare an explanation of the accounts, finance or any matters relating to the management of the business and assets, or he may give orders to do or not to do any act he thinks fit. Upon deeming it proper or upon a motion made by the receiver, the court shall be empowered to relieve the interim executive from his powers and duties. In such a case, the court may appoint a new interim executive to assume the office. If the court does not do so, the receiver shall have the temporary power to manage the business and assets of the debtor (Section 90/20 of *Bankruptcy Act*).

Where the court orders a business reorganization but has not yet appointed a planner, all legal rights of the debtor's shareholders are suspended except the right to receive dividends, and the said rights shall be vested in the interim with the executive or the receiver, as the case may be, until a planner is appointed (Section 90/21 of *Bankruptcy Act*).

Upon acknowledgment of the order for a business reorganization, the debtor's executive shall deliver the assets, seal, accounting ledgers and documents relating to the assets, liabilities and business of the debtor to the interim executive or the receiver, as the case may be, as soon as possible. For this purpose, the interim executive or the receiver shall be empowered to call upon the possessor to deliver the assets, seal, accounting ledgers and documents mentioned above to him. The interim executive who is relieved, by order of the court, from his office, shall have the said duties (Section 90/21 paragraphs 3,4 of *Bankruptcy Act*).

b) Question: *If another insolvency procedure has already been initiated in relation to the corporate debtor, how does the initiation of a second procedure affect the first?*

Answer: If no absolute receivership order has been made against that debtor prior to the initiation of a second insolvency procedure, the second procedure will not affect the first, and vice versa. Hence, it is possible to have concurrent insolvency proceedings.

Addendum to Report on Thailand

Addendum to Report on Thailand produced under Asian Development Bank Technical Assistance No. 5795 - REG

Answer: Sections G, J and L of the Addendum to that Report are still accurate. Section B of the Addendum should be updated to reflect the amendments to the Bankruptcy Act. There is another amendment to the Act, which is referred to as the Bankruptcy Act No.6, B.E.2543. The amendment revoked paragraph 3 of Section 139, which stated, "The official receiver shall be deemed as an official of the court."

There are proposed amendments to the rehabilitation and insolvency parts of the Bankruptcy Act. These two draft amendments are currently awaiting review by the Council of State.

The original sections B, G, H, J and L of the Addendum to the Report are produced below.

Section J – Case Management of Insolvent Enterprises

1. Administration of insolvency procedures generally

a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this economy, what are the administrative organs/entities involved in the implementation and management of that procedure? (For example a trustee, liquidator, receiver, government official.)*

Answer: When the court has ordered a debtor to be placed under receivership, only the receiver shall have the power to manage and dispose of the assets of the debtor, or do any necessary act to complete any pending business of the debtor.

In the case of a business reorganisation under Article 90 of the Bankruptcy Act, the planner will have the power and duties to manage the business and assets of the debtor. If the court orders a business reorganisation but has not yet appointed a planner, the power and duties of the debtor's executive in managing the business and assets shall cease. The court will appoint one or more persons or the debtor's executive to be the interim executive with the power and duties in managing the business and assets of the debtor under the supervision of the receiver until a planner is appointed. During the time in which it is not possible to issue an order to appoint an interim executive, the receiver shall have the temporary power to manage the

business and assets of the debtor (Section 90/20 of the Bankruptcy Act).

b) **Question:** *What qualifications must each type of administrator of insolvency procedures possess? Is there a system of regulation of insolvency administrators in this economy?*

There is no regulation specifying the qualifications of the administrator. There are only specified qualifications for the receiver, namely:

1. Thai nationality;
2. LL.B. degree;
3. Passed the execution officer's examination.

c) **Question:** *Are the creditors of a corporate debtor permitted to participate in the administration of the relevant insolvency procedure, and if so, how? (For example are the creditors permitted to assist the administrator, or supervise or dictate the conduct of the administration?)*

Answer: The creditors of a corporate debtor are permitted to participate in the administration of the relevant insolvency procedure, as follows:

1. Attending the creditors' meeting to consider what business, if any, the creditors would allow the debtor to proceed with;
2. Considering whether to give consent to any requests/applications made by the debtor; and
3. Voting on whether to accept a planner appointed by the debtor or whether to approve or amend the plan prepared by the planner (in the case of a reorganisation).

2. Powers of the administrator

a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this economy, what are the powers given to each type of administrator by statute, at general law or pursuant to the terms of the appointment? (For example power to carry on the business of the organisation, to pay creditors, to compromise claims of or against the debtor, to issue or defend legal proceedings, to obtain credit, to sell property, to execute documents on behalf of the debtor.)*

Answer: Under the Bankruptcy Act, B.E.2541, when the court orders the debtor to be placed in

receivership, the receiver shall have the following powers:

1. Manage and dispose of the assets of the debtor, or do any necessary act to complete any pending business of the debtor;
2. Collect and receive money or assets belonging to the debtor, or which the debtor is entitled to receive from others;
3. to compromise, come to a settlement, file actions or defend actions relating to the assets of the debtor.

When the court has ordered the debtor to be placed under receivership, it is prohibited for the debtor to do any act relating to its assets or his business (including executing any document), except with the approval of the court, the receiver, the administrator of the assets, or a creditors' meeting.

In the case of the court ordering a business reorganisation, the planner will have the power and duty to manage and carry on the business of the organisation, to pay creditors, to issue or defend legal proceedings, to obtain credit, to sell property and to execute documents on behalf of the debtor.

b) Question: *To what extent and in what circumstances may each type of insolvency administrator seek assistance, advice or direction in the conduct of the administration, and from what sources? (For example the Court, his appointor, the creditors of the debtor, a solicitor, accountant or other relevant person.)*

Answer: At a creditors' meeting, a resolution may be passed appointing a committee of creditors to represent all creditors in matters relating to the management of the debtor's assets. The receiver may apply to the court for orders and under sections 141-145 of the Bankruptcy Act, the official receiver is empowered to employ counsel to act on his behalf.

3. Duties of the administrator

a) Question: *In relation to each type of insolvency procedure available in the legal system of this economy, what are the duties imposed upon each type of administrator by statute and at general law? (For example a duty to take possession of assets of the debtor, to realise those assets, to discharge the debt owed to his appointor, to call for proofs of debts owed to creditors, to adjudicate upon claims of creditors, to apply available assets in discharge of those claims, to report on the conduct of the debtor by the proprietors.)*

Answer: The official receiver's duties include reporting on matters relating to the business, property or conduct of the debtor, assisting in examining the debtor or other persons as required by the court and to borrow money for the benefit of the management of the debtor's property (if necessary). On approval from the Creditors' Committee, the official receiver may withdraw the attachment of property, transfer property other than by public auction, surrender a right, file or withdraw a civil action or (other) bankruptcy case, and effect a compromise or submit a matter to arbitration.

Other duties and powers include the following:

- Under Section 19 of the Bankruptcy Act, if the court orders to place the debtor under a receivership order, the receiver is empowered to attach seals, accounting ledgers, and documents belonging to the debtor, and all assets in the possession of the debtor, or in the possession of other persons, which may be distributable in the bankruptcy action. In attaching such assets, the receiver is empowered to enter into any premises belonging to the debtor, or of which he is in possession, and is empowered to make a forcible entry into any such place, including to open any safe, cupboard or other place for the keeping of things, as may be necessary.
- Under Section 21 of the Bankruptcy Act, on the application of the receiver, the court is empowered to order post and telegraph officials to send to the receiver telegrams, postal mail, letters, or other papers addressed to the debtor, for a period not exceeding 6 months from the date that the debtor's assets are under receivership.
- The receiver can file a motion to the court for an order to cancel fraudulent acts under the Civil and Commercial Code (Section 113).
- Transfers of asset or any acts concerning the debtor's assets, done or permitted to be done

by the debtor during the three years prior and subsequent to the application to adjudicate him or her as bankrupt, may be cancelled by order of the court upon the filing of a motion by the receiver, except where the transferee or the beneficiary can prove to the satisfaction of the court that such transfer or act was made in good faith and for consideration (Section 114).

- Upon the filing of a motion by the receiver, the court is empowered to cancel any transfer of assets or any act done or permitted to be done by the debtor during the three months prior and subsequent to an application to adjudicate him as bankrupt, and with the intention to give undue preference to a creditor (Section 115).
- Upon the application of the receiver, the court is empowered to compel persons who admit to being indebted to the debtor, or who admit to possessing an asset belonging to the debtor, to pay money or deliver the asset to the receiver within such period as the court may deem proper. If the order of enforcement is not complied with, the receiver may apply to the court for a writ of execution as if such persons were judgment debtors (Section 118).
- When it appears that the debtor is entitled to claim for repayment of money from another person, or demand that such other person deliver assets to the debtor, the receiver shall inform such a person in writing to repay the money or deliver the asset as is stated in the notice, and shall inform the person that if liability is disclaimed, he or she shall show cause for a disclaimer in writing to the receiver within 14 days from the date of receipt of the above notice. Otherwise, it shall be deemed that the person is indebted to the bankrupt estate in the amount stated.
- If the person receiving such a notice disclaims liability to the receiver within the time prescribed in the previous paragraph, the receiver is required to conduct an investigation, and if the receiver finds that such a person is not indebted to the debtor, he or she shall delete the person's name from the list of debtors and inform the person accordingly. If it is found that the person is indebted to any extent, the receiver shall inform the person in writing, confirming the amount of liability. The receiver must also inform the person that if he has any objections to make they must be filed with the court within 14 days from the date of receipt of the confirmation of his or her indebtedness.
- If the person receiving the confirmation of indebtedness objects to the court by filing a motion within the time stated in the previous paragraph, the court shall consider the matter. If the court is satisfied that he or she has indebtedness, there shall be an order directing the person to pay the money or deliver the asset to the receiver. If it is found that there is no indebtedness, there shall be an order directing the deletion of the person from the list of debtors.
- If any person who receives a notice from the receiver does not make a disclaimer to the receiver, or does not file any objection with the court within the period prescribed above, the receiver may apply to the court to compel the person to repay the debt within the period the court deems appropriate.
- If the person does not comply with such an order, the receiver may apply to the court to issue of a writ of execution as if the person were a judgment debtor.
- Where a person against whom a demand for repayment of debt has been made files an objection to the court, the receiver may file a motion to the court for an order of temporary attachment or temporary injunction against the asset of the objecting party before a court order regarding such a debt is issued (Section 119).
- Within three months from the date on which the receiver learns that assets of the debtor or rights under a contract are subject to terms more onerous than the benefits receivable thereunder, the receiver is empowered to refuse such s or rights under the contact (Section 122).
- Under the reorganisation procedure, upon a motion being submitted by the planner, plan administrator, or receiver, the court has the power to compel those persons who admit that they are indebted to the debtor or who admit that they have assets of the debtor in their possession. to pay the debt or turn over those assets to the planner, plan administrator or receiver within the time period deemed appropriate by the court. If the person fails to comply with the order, the planner, plan administrator, or receiver can ask the court to issue a writ of execution treating that person as if he or she were a judgment debtor (Section 90/38).
- When it appears that the debtor has the right to demand that any person repay debts or deliver assets to the debtor and the person does not admit that he or she is indebted to the debtor or that he or she has in his or her possession assets belonging to the debtor, the planner or plan administrator shall notify the receiver for further procedures.

- The receiver shall give a written notice to the person to repay debts or deliver assets, as stated in the notice. Where the debts are disputed, a letter giving the reasons why must be sent to the receiver within 14 days of the date of receipt of the notice. Otherwise, it shall be deemed that the person is conclusively indebted to the debtor for the amount stated in the notice.
- If the person receiving the notice disputes the indebtedness in writing to the receiver within the time stipulated in paragraph 2, the receiver is required to conduct an investigation, after which the receiver shall notify the planner or plan administrator and the person of the result. There is a right of objection if filed with the court within 14 days of the date of receipt of the receiver's notification.
- If an objection is filed by motion with the court within the time stipulated above, the court shall consider the matter. If the court is satisfied that the person has indebtedness, the court shall issue an enforcement order that the person pay the debt or deliver assets to the planner or plan administrator. If the court sees that such person is not indebted to the debtor, the court shall issue an order to strike such person's name from the list of debtors.
- If the person does not comply with the court's order, the receiver may make a request that the court issue a writ of execution as if the person has been adjudged a judgment debtor.
- Where the person subject to demand for repayment of debts files an objection with the court, the receiver may make a request in the form of a motion to the court for an order of temporary seizure or attachment of the assets of the person filing the objection before an order regarding such debts is issued (Section 90/39).
- The planner, plan administrator, or receiver may ask the court to cancel a fraudulent act pursuant to the Civil and Commercial Code by filing a motion (Section 90/40).
- When it appears that there has been a transfer of assets or any other act which the debtor had committed or had allowed to be committed within the period of three months before and after the filing of the motion, with the intent to place any creditor in an advantageous position over the other creditors, the planner or plan administrator or receiver may submit a request to the court in the form of a motion. In this regard, the court has the power to order the cancellation of the transfer or such act (Section 90/41).

4. Breach of duty and liability of administrators

a) **Question:** *What remedies and/or sanctions are available in the legal system of this economy in respect of breaches of duty or transgressions committed by each type of insolvency administrator?*

Answer: If an interim executive, planner, plan administrator, or interim plan administrator dishonestly carries out or omits to carry out his duties or if he violates or fails to comply with the duties under the rehabilitation procedure, the person is liable to a fine not exceeding Baht 500,000 or imprisonment not exceeding 5 years, or both.

In carrying out his duties, the receiver shall have no personal liability, except when he has acted with bad intent or gross negligence (Section.147).

b) **Question:** *Have there been actual instances of breach of duty or transgressions committed by insolvency administrators?*

Answer: There have not been actual instances of breach of duty or transgressions committed by insolvency administrators.

c) **Question:** *If so, give details of any major cases and a summary of the action taken and the results.*

Section K – Assets Available to Creditors

1. Assets available to creditors generally

(a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this economy, what assets of the business organisation are available to its administrator to satisfy the claims of its creditors?*

Answer: The assets of the business organisation that are available to its administrator for the creditors' claims are as follows:

- (1) All assets belonging to the debtor as from the beginning of the bankruptcy, including all rights over any asset of third parties, except:
 - (a) Personal and necessary effects that the debtor, his wife, and his minor children reasonably require in accordance with their status, and
 - (b) Livestock, seeds, and instruments for use in the debtor's livelihood, of a total value not exceeding Baht 3,000.

- (2) Assets accruing to the debtor subsequent to the institution of the bankruptcy preceding and up to the date of his discharge from bankruptcy.
- (3) Things in the possession or disposition of the debtor in the court of trade or business of the debtor by the consent of the true owner under circumstances which create the impression that the debtor is the owner at the time of the filing of the application for adjudication of bankruptcy of the debtor (Section 109, Bankruptcy Act).

2. Avoidance of past transactions affecting the assets of a corporate debtor

- a) **Question:** *To what extent and in what circumstances may the administrator of a business organisation take steps to recover assets of the organisation by overturning past transactions involving property of the organisation? (For example preferences given to certain creditors over others, invalid charges granted by the organisation, uncommercial transactions entered into by the organisation, profits on sales to and from the organisation at an undervalue or overvalue.)*

Answer: Transfers of assets or any acts concerning the debtor's assets, made or permitted to be made by the debtor during the three years prior and subsequent to the application to adjudge him bankrupt, may be cancelled by order of the court upon the filing of a motion by the receiver, except where the transferee or the beneficiary can prove to the satisfaction of the court that such transfer or act was made in good faith and for consideration (Section 114, Bankruptcy Act)

Upon the filing of a motion by the receiver, the court is empowered to cancel any transfer of assets or any act done or permitted to be done by the debtor during the three months prior and subsequent to an application to adjudge him bankrupt, and with the intention to give undue preference to a creditor (Section 115, Bankruptcy Act)

- b) **Question:** *What powers or mechanisms are available to each type of administrator for investigation of the affairs of the business organisation, for examination of persons formerly involved in the management or control of the organisation, and for the discovery of assets of the organisation?*

Answer: The receiver is empowered to issue a summons to the debtor or any person who has

been ascertained to, or is suspected of, having the debtor's assets in his or her possession, or who is believed to be indebted to the debtor, or is considered to be capable of giving information regarding the business or assets of the debtor, to appear for examination or investigation, and is empowered to order that the person produce documents or evidence that is in the person's possession or control, which relate to the business or assets of the debtor. If the person intentionally defies the summons or order, the court is empowered to issue a warrant for the arrest of the person and to detain him or her until he or she complies with the order of the court or receiver.

- c) **Question:** *What procedures may be employed by each type of administrator for the recovery of assets of the business organisation which are available for distribution to creditors? (For example initiation of legal proceedings, compensation from directors.)*

Answer: Assets realised by the receiver on the debtor's bankruptcy may be sold by the receiver in the manner which is most convenient and beneficial. However, sale other than by public auction must receive the approval of the creditors' committee, except when the assets are perishable or would deteriorate if kept for any length of time, or the expense would be disproportionate to the value of the asset(s) (Section 123.)

Section L – Claims of Creditors

1. Claims admissible for payment

- a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this economy, what types of claims of creditors are properly admissible for payment in the context of the procedure? (For example liquidated debts, future debts, contingent claims, secured claims, unliquidated claims for damages, interest claims, costs of administration or of legal proceedings, periodical payments, debts owed by guarantors of the business organisation.)*

Answer: Unsecured creditors may file a claim for repayment of debt if the cause of the indebtedness arose before the date on which the court ordered receivership of the asset, even if such debt may not yet be due or is subject to conditions (Section 94, Bankruptcy Act). Therefore, liquidated debts, future debts for a liquidated amount, secured claims, costs of administration or of legal proceedings, interest claims and debts owed by guarantors of the

business organisation, are admissible for payment in the context of the procedure.

b) Question: *At what date are the amounts of admissible debts computed?*

Answer: The amounts of admissible debts are computed as of the date on which the court ordered receivership of the asset.

c) Question: *By what method are claims of creditors proven by those creditors in the context of each type of insolvency procedure?*

Answer: Upon the expiry of the two months following the date of publication of the order of absolute receivership, the receiver must fix a date for a meeting of the debtor and all creditors to examine the claims for repayment of debts, by giving notice thereof not less than 7 days in advance (Section 104). In examining the claims for repayment of debts, whether such debts are judgment debts or not, the receiver has the power to issue summons to creditors, or other persons to appear for questioning as to the debts, and to report his or her opinion and send the case file of such claims for repayment of debts to the court, together with a report as to whether any of the claims are contested or not (Section 105). The court will then decide in accordance with the official receiver's findings.

d) Question: *How are disputed claims made by creditors adjudicated upon? (For example by the administrator, or by a Court.)*

Answer: For disputed claims made by creditors, the court will conduct a review and issue any of the following orders (Section 108):

1. Dismiss the claim for repayment of debt;
2. Approve repayment of the whole debt;
3. Approve repayment of part of the debt.

2. Priority and payment of creditors' claims

a) Question: *In relation to each type of insolvency procedure available in the legal system of this economy, what principles apply to the division of available assets of the corporate debtor among those of its creditors entitled to payment? Is there a basic principle of equality of payment, or are rights of priority of payment enjoyed by secured creditors, or by certain classes of creditors over others? (For example costs of the administration, claims for taxes owed by the debtor, amounts owed to employees of the organisation.)*

Answer: In bankruptcy cases, the available assets of the corporate debtor are sold in order that the money received from the sale will be shared among the creditors.

Secured creditors naturally have rights over the secured assets which is security afforded to the creditor by the debtor prior to the order of receivership of the debtor's assets. Secured creditors need not file a claim for repayment of the debt. However, the secured creditor must allow the receiver to inspect secured assets.

A secured creditor may file a claim for repayment of the debt on the following conditions:

1. When he or she agrees to surrender the asset afforded as security for the benefit of all creditors, he or she may claim for the full amount of the debt.
2. After he or she has already enforced the claim against the asset given as security, he or she can claim for the balance of the debt remaining unpaid.
3. When he or she has asked the receiver to sell by public auction the asset given as security, he or she can claim for the balance of the debt remaining unpaid.
4. When he or she has appraised the asset given as security, he or she can claim for the unpaid balance. In such a case, the receiver is authorised to redeem the asset at valuation. If the valuation is considered incorrect, the receiver is authorised to sell the asset by such method as the receiver and the creditor may agree. However, if no agreement is reached, the asset may be sold by public auction but not at a loss to the creditor.

Any creditor filing a claim in bankruptcy, whether or not the creditor is a petitioning creditor, shall file the claim with the receiver within two months following the date of

publication of the order of absolute receivership. However, if the creditor resides outside of the Kingdom, the receiver may extend this period by up to an additional two months. The claim must be made in accordance with the standard printed form, with a statement showing details of the debt, evidence of such debt, and any assets the debtor holds as security or which may be in the creditor's possession.

An unsecured creditor may file a claim for repayment of debt if the cause of indebtedness arose before the date on which the court ordered receivership of the asset, even if the debt may not yet be due.

In the event that the court orders the debtor to be under absolute receivership, creditors with the right to receive repayment of debts for business reorganisation and the creditors of other debts eligible to apply for payment from the obligations arising from the time the court issues an order of reorganisation, a business is required to file an application for repayment with the receiver. The debts incurred by the receiver, planner, plan administrator, or interim plan administrator, in accordance with the plan for the benefit of the reorganisation of business operation of the debtor, shall have the same rank as the expenses incurred by the receiver in the administration of the debtor's assets, which shall have the priority payment over other creditors

Secured creditors may enforce payment of debt from assets used as collateral without having to file an application for repayment of debts for the business reorganisation. However, they must allow the receiver or planner to examine the assets.

b) Question: Give a brief account of the order of priorities, if any, of payment of creditors prescribed by the legal system of this economy.

Answer: Expenses shall be deducted prior to distribution of proceeds in the following order:

- 1) Expenses of administration of a deceased debtor's estate;
- 2) Expenses of the receiver in managing the debtor's assets;
- 3) Funeral expenses of a deceased debtor proper to his status;
- 4) Fees for collecting the assets;
- 5) Taxes due for payment within 6 months preceding the order for control of the property;
- 6) Wages, salaries for 2 months prior to the order for control of the property;

- 7) Debt in any series (secured, unsecured) (Section 130).

Section O – Connection Between Debt or and Forum

a) Question: In relation to each type of insolvency procedure available in the legal system of this economy, what connection must there be between the debtor organisation and the law of the forum? (For example which of the following requirements, if any, must be satisfied in order for an insolvency procedure to be initiated in relation to a corporate debtor in your economy:

- principal residence of debtor;
- domicile of the debtor;
- nationality of the debtor;
- personal whereabouts at the material time;
- location of principal place of business;
- location of a place of business, branch or agency;
- location of assets of debtor;
- place where transaction or event took place which gave rise to liability;
- place where payment, discharge or performance of liability is due to take place.)

Answer: An insolvent debtor may be adjudged bankrupt by a court, if the debtor is domiciled in the Kingdom, or operates business therein, whether by himself or by representative, at the time an application is made to adjudge the debtor a bankrupt, or within a period of one year previously.

a) Question: Are any other requirements imposed in relation to a connection between the debtor and the forum before an insolvency procedure may be initiated? If so, briefly describe these requirements.

Answer: No.

b) Question: Are any particular rules or conditions imposed in the legal system of this economy regarding the opening or commencement of an insolvency procedure in cases where the connection between the debtor and the forum is limited to only one of the factors mentioned in (a) above?

Answer: There are no other rules or conditions imposed in the legal system of Thailand

regarding the opening or commencement of an insolvency procedure in cases where the connection between the debtor and the forum is limited to only one of the factors mentioned in (a) above. The factors mentioned in (a) above are required by the insolvency law of Thailand to instigate a bankruptcy case.

Section P – Foreign/Cross-Border Elements

1. Claims of foreign creditors

a) **Question:** *In relation to each type of insolvency procedure available in the legal system of this economy, to what extent are the claims of foreign creditors recognised in the context of administration of that procedure?*

Answer: Foreign creditors' claims are recognised according to Section 91 of the Bankruptcy Act, B.E.2541.

b) **Question:** *What principles or rules apply to the recognition and admission of claims by foreign creditors?*

Answer: If a creditor resides outside of the Kingdom, the creditor is required to submit a claim with the receiver within two months (extendable by not more than another two months) following the date of publication of the order of absolute receivership.

(i) **Question:** *Are claims by foreign creditors subject to particular rules in relation to priority of payment?*

Answer: No, they are not.

(ii) **Question:** *Do foreign creditors have to satisfy special or additional requirements in order for their claims to be admitted?*

Answer: Section 178 requires proof that creditors in the Kingdom are similarly entitled to claim under the laws of the country in which the foreign creditors reside. Also, on showing the amount that the foreign creditor is entitled to receive, or has received in a distribution from the same debtor's property outside the Kingdom, if any, the foreign creditor must agree to deliver such portion of the debtor's property to be added to the debtor's property in the Kingdom.

c) **Question:** *What law is applied to establish the validity of foreign claims?*

Answer: The Conflict of Law Act and the Bankruptcy Act, B.E.2541.

2. Jurisdiction over foreign assets

a) **Question:** *To what extent does the insolvency law of this economy claim jurisdiction over assets of a corporate debtor situated abroad?*

Answer: There are no instances where the insolvency law of Thailand claims jurisdiction over assets of a corporate debtor situated abroad. Section 177 states that the Act only applies to property of the debtor within the Kingdom.

3. Foreign insolvency procedures

a) **Question:** *To what extent do the rules of private international law of the legal system of this economy recognise insolvency procedures commenced in foreign jurisdictions?*

Answer: There are no rules of private international law of the legal system of Thailand that recognise insolvency procedures commenced in foreign jurisdictions.

b) **Question:** *Under what circumstances, if any, may orders or judgments resulting from foreign insolvency procedures or administrations be recognised or enforced in the legal system of this economy?*

Answer: No orders or judgments resulting from foreign insolvency procedures or administrations will be recognised or enforced in Thailand.

4. Foreign insolvency administrators

a) **Question:** *What recognition is accorded in the legal system of this economy to the status and capacity of insolvency administrators (for example trustees, liquidators, receivers) appointed in foreign insolvency procedures?*

Answer: There is no recognition of insolvency administrators appointed in foreign insolvency procedures in Thailand.

b) **Question:** *To what extent are foreign insolvency administrators entitled to claim, take control of, and realise or deal with property of the corporate debtor situated within the jurisdiction of the legal system of this economy?*

Answer: They have to instigate their claims against the corporate debtor in Thailand in order to claim for repayment. Section 177 stipulates that the control of property and the bankruptcy law of other countries has no effect on property in the Kingdom.

5. Foreign security holders

- a) **Question:** *To what extent does the legal system of this economy recognise the validity of rights of security asserted by foreign creditors over assets of the corporate debtor?*

Answer: The validity of rights of security asserted by foreign creditors over assets of the corporate debtor is recognised only when such security has been registered or complies with Thai law.

- b) **Question:** *Are any special rules applicable to determine the validity, extent and ranking of such security rights?*

Answer: Section 177 states that the Act only applies to property of the debtor within the Kingdom, and that the control of property and the bankruptcy law of other countries has no effect on property in the Kingdom.

6. International conventions

- a) **Question:** *To which international conventions having some application in insolvency matters is this country a party?*

Answer: Thailand is not a party to any international conventions concerning insolvency matters. Thailand has just become a member of the International Association of Insolvency Regulators. Additionally, Thailand, represented by the Ministry of Justice, has also appointed its representatives to attend the Working Group on Insolvency Law undertaken by the United Nations Commission on International Trade Law to prepare the instrument, tentatively entitled the draft UNCITRAL Model Legislative Provision on Cross-Border Insolvency.

- b) **Question:** *When were these conventions entered into, and what other states are parties?*

Answer: N/A

- c) **Question:** *What observations can be made about the practical results achieved under these international instruments?*

Answer: The working group on cross-border insolvency are still preparing the instrument based on the draft UNCITRAL Model Legislative Provision on Cross-Border Insolvency. The Thai government is tentatively considering amending the law on cross-border insolvency in order to comply with the UNCITRAL Model Legislative Provisions.

7. Cross-border insolvency

- a) **Question:** *Are there any other particular issues or special problems in the field of cross-border insolvency, not included in the answers supplied above, which have presented themselves before the courts of the legal system of this economy?*

Answer: No Answer/s provided

8. UNCITRAL Model Law on Cross-Border Insolvency

- a) **Question:** *Is the government of this economy aware of the UNCITRAL model law on cross-border insolvency, approved by the United Nations in June 1997?*

Answer: Yes, the government of Thailand is aware of the UNCITRAL model Law on cross-border insolvency (see P6 above).

- b) **Question:** *If so, are you aware of whether the government has any proposals to enact the terms of the model law?*

Answer: There are no firm proposals from the government to enact the terms of the model law at this moment, but the Ministry of Justice has appointed its representatives to attend the Working Group on Insolvency Law undertaken by the United Nations Commission on International Trade Law to prepare the instrument, entitled the draft UNCITRAL Model Legislative Provision on Cross-Border Insolvency.

Addendum to Report on Thailand

Addendum to Report on Thailand – produced under Asian Development Bank Technical Assistance No. 5795 - REG

B. Insolvency Reforms

1. **Question:** *Provide details of any reforms that have occurred in relation to insolvency law and practice and related areas (such as corporate governance, secured transactions and so forth) since January 1999.*

Answer: Two enactments concerning insolvency have come into effect this year. The Establishment of and the Procedure for the Bankruptcy Court, and Amendment to the Bankruptcy Act (No. 5) B.E.2542. The amendments are with respect to both the straight bankruptcy and rehabilitation procedures.

Establishment of and Procedure for the Bankruptcy Court

1. The Jurisdiction of the Bankruptcy Court

The Bankruptcy Courts have jurisdiction over bankruptcy cases. Once regional Bankruptcy Courts are inaugurated, no other courts of first instance may accept a case that falls within the jurisdiction. However any bankruptcy cases arising outside the jurisdiction of the Central Bankruptcy Court may be filed with the Central Bankruptcy Court.

2. The Procedure of Bankruptcy Cases

The Bankruptcy Court is required to proceed with the hearing without adjournment until the case is over, save in the case of unavoidable necessity.

Where any party fails to appear on any day appointed whether with or without permission of the court, that party is deemed to acknowledge the proceeding of the hearing on that appointed date.

The court may direct that another court or court officer examine the evidence or part of it on its behalf.

The Bankruptcy Court may call any knowledgeable persons or experts to appear and give opinions for its consideration.

Parties or interested persons in the case may appoint any person domiciled in the jurisdiction of the bankruptcy court to receive pleadings or documents on its behalf, by submitting a request to the competent court.

After the approval of the court, such pleadings or documents may be served on the appointed person.

3. The Appeal

Appeals of judgments or orders of the Bankruptcy Court in respect of a business reorganisation must be lodged with the Supreme Court within one month from the date the Court renders the judgment or order.

Amendment to the Bankruptcy Act, (No. 5) B.E.2542:

Effective April 22, 1999.

The key issues of the amendment are:

1. Minimum Claim Amounts

The amount of claim for an unsecured creditor to institute bankruptcy proceedings against the debtor under section 9 of the Bankruptcy Act is raised from Baht 50,000 for an individual person to Baht 1.5 million, and from Baht 500,000 for a juristic person to Baht 2 million. Secured creditors may set up a bankruptcy charge only when the Creditor states that if the debtor becomes bankrupt, he or she is willing to waive the security in the claim which, after deduction of the obligation due to him, is still in the deficit for the debtor who is an ordinary person in the amount not less than Baht 1 million or for a debtor who is a juristic person in the amount not less than Baht 2 million.

2. Discharge from Bankruptcy

A bankrupted individual whose debt was not procured through dishonest means will be discharged from bankruptcy within 3 years from the date the court orders the individual bankrupt.

3. Classification of Creditors

The amendment to the Bankruptcy Act has classified creditors as follows (Section 90/42 bis):

1. Each secured creditor whose debt is not less than 15% of total debts for business reorganisation shall be placed in each group.
2. Secured creditors who have not been grouped under (1) shall be set in another group.
3. Unsecured creditors may be placed in many groups. The unsecured creditors who have

the same type of claims or benefits are to be placed in the same group.

4. The creditors under Section 130 bis shall be in one group.

Any creditor who believes that the grouping of creditors is not in accordance with these provisions may submit an application to the court within 7 days from the date of knowledge of the groupings. The court may issue an order for re-grouping. The order of the court is final.

The rights of creditors who are in the same group must be treated equally, unless the creditors who are not treated equally consent in writing.

4. Resolution to Approve the Plan

The resolution approving the plan must be a special resolution passed at:

1. every creditor's meeting of each group of creditors; or
2. at least one group of creditors' meetings and at the time of counting the debts of the creditors who accept the plan in each group of creditor's meeting, the amount of such creditors' debt is not less than 50% of the outstanding debt of the creditors who attend the meeting in person or by proxy and pass the resolution on that vote.

5. Other Changes

- 2.1 The amendment specifies that the conversion of foreign currency denominated debts into Baht is for the sole purpose of calculating votes to be attributed to the various creditors' claims at creditors' meeting.
- 2.2 The discretionary power of the court under Section 90/58 to approve or reject the plan is replaced by objective criteria for approval by the court, including a requirement that upon completion of implementation of the plan, creditors will have received debt repayments not less than the amounts they would have received on liquidation.
- 2.3 The plan administrator has the power to disclaim the debtor's assets or rights under contracts made by the debtor where the terms are more onerous than the benefits receivable by the debtor as prescribed by the plan. This extends the existing provision in the Bankruptcy Act that applies to bankruptcies in rehabilitation proceedings.
- 2.4 Section 94(2) which provides that a creditor may not file a claim in the

bankruptcy of the debtor in respect of a debt which the creditor allowed the debtor to create knowing that the debtor was insolvent at the time, is amended to permit a claim to be filed by a creditor in these circumstances provided it is created for the purpose of enabling the debtor's business to continue.

The above changes represent important substantive changes that have by and large received a positive reaction.

2. **Question:** *Provide details of any proposed reforms as above.*

Answer: A proposed amendment to the Bankruptcy Act, No. 6/2542 was made but is now no longer under consideration.

G. Insolvency Law

1. **Question:** *What are the major substantive defects in the corporate insolvency law viewed from the respective positions of:*

- (a) *banks/financial providers*
- (b) *secured creditors*
- (c) *unsecured creditors*
- (d) *employees*
- (e) *corporations*
- (f) *directors*
- (g) *shareholders?*

Answer:

- a) *Banks/financial providers*

The reason for promulgating Bankruptcy Act (No. 4) B.E. 2541, which introduced the reorganisation process (Article 90) is because it was deemed that certain articles of the Bankruptcy Act B.E. 2483 were not suitable for the current economic and social condition. Particularly in the case where a corporate debtor (including a bank) faces a temporary financial liquidity problem and should receive financial aid from any person wishing to give such financial aid to the debtor to provide opportunity to rehabilitate the debtor's business operation. Article 94(2) of the Bankruptcy Act, however, provided that a creditor who allowed the debtor to incur debt knowing full well that the said debtor is insolvent shall not be entitled to receive payment or debt in a bankruptcy case with the result that no financial institutions or private enterprises agreed to grant financial aid to a debtor facing temporary financial liquidity

problem. The debtor therefore became a bankrupt person albeit its business operations were in a condition to be rehabilitated if the debtor were to be the receiver of financial aid. It was therefore deemed appropriate to prescribe provisions to protect the granting of financial aid to a debtor facing temporary financial difficulties to allow the debtor to rehabilitate its business operations.

The new bankruptcy law designated that the Bank of Thailand is entitled to file a motion for rehabilitation if the debtor is a commercial bank or financial company.

(b) *secured creditors*

Realisation of secured property is slow and requires a court order.

Under Section 90/12 of the Bankruptcy Act, a moratorium or automatic stay will come into effect from the time a petition is accepted for reorganisation. This will prevent secured creditors from pursuing their debts, enforcing their civil judgment or filing a straight bankruptcy petition against the debtor. The only option is to participate in the reorganisation proceeding.

(c) *unsecured creditors*

Unsecured creditors share the problems of slow court proceedings with secured creditors, but also face subordination to secured creditors. Enforcement practices are hampered by the unavailability of complete information concerning a debtor's financial position.

Under Article 90 of the Bankruptcy Act, unsecured creditors are divided into several groups. The rights of creditors who are in the same group must be treated equally, unless the creditors who are not treated equally consent in writing. Additional finance given to a company under the plan enjoys a priority right over existing unsecured debts – the opposite effect of Article 94(2).

(d) *employees*

The existing legislation can generally be regarded as favourable for employees. They are possessed of a preferential right under Section 253 of the Civil and Commercial Code. Consideration of the effects of a proposed Plan under a reorganisation petition on employment should be indicated. This adds a new dimension to the bankruptcy law.

(e) *corporations*

Section 90 of the Bankruptcy Act has not attracted many cases. More reorganisations

have been through the Bank of Thailand initiated CDRAC procedure, which does not enjoy the benefits of the moratorium/automatic stay under Section 90, but has the benefit of speed, the coercive powers of the Bank of Thailand and a mechanism to ensure that creditors agree amongst themselves – one of the biggest problems with reorganisations. There also appears to be some stigma attached to filing an application under the Bankruptcy Act. There is a perception that doing so will adversely affect the perception of the company, and its share value. However, most corporations have conducted their reorganisations independently. The corporate preference in Thailand is still to avoid the courts and government assisted approaches.

(f) *directors*

A director's authority upon plan acceptance will depend upon the Plan, but for most directors their role will be suspended.

(g) *shareholders*

Under Article 90, the interests of shareholders seems to be very much limited. All the powers relating to the decision making on the future of the company shifts to the creditors. This includes the power to decide to reduce and increase the capital. Conversion of debts into equity is also allowed.

But with the concept of appointing someone as a planner, the law has to balance the interest of the shareholders and creditors reasonably.

2. Question: *What are the major practical benefits in the application of the insolvency law viewed from the respective positions of:*

Answer:

(a) *corporations*

Reorganisation is provided for companies both private and public.

The new law stipulates "automatic stay", which has a very wide scope and comes into effect at the beginning of the process (i.e. upon acceptance of the petition by the court).

During the stay, but before the reorganisation order is issued, existing management can still have the control of the company subject to limitation that it can only conduct the ordinary business of the company. To do something further than the ordinary course of business, the manager needs leave of the court.

In addition, under section 90, the rights of shareholders are very limited. The power

relating to the decision-making on the future of the company shifts to creditors. This includes the power to decide to reduce and increase the capital and conversion of debt to equity (securitisation).

(b) *creditors*

Upon filing the petition (reorganisation process), the moratorium or automatic stay under section 90/12 will come into effect and will prevent secured and unsecured creditors from pursuing their claims, enforcement, civil judgments and the filing of "straight" bankruptcy proceedings by the debtor. The only option left to creditors to advance their claims is to participate in the reorganisation proceeding.

The reorganisation order must be put to a vote by creditors within 3 months of the appointment order and be approved by a special resolution of creditors representing 75% of the claimable debt. Only the creditors who have lodged their proof of claim with the official receiver of the business reorganisation within one month from the date of the publication of the appointment of a Planner have the right to vote.

A Bill has recently been proposed by the Ministry of Justice to adopt principles of classification of creditors and voting by classes. This [will enable the Planner and the court to divide creditors into classes and voting will represent the real needs of each class better. It may also make arriving at a special resolution more difficult.

H. Judicial System

1. **Question:** *Has there been any discernible improvement or change in the operation of the judicial system in relation to the conduct of:*

- (a) *debt collection/recovery processes;*
- (b) *enforcement processes in respect of secured property rights;*
- (c) *recovery or enforcement processes in respect of leased property;*
- (d) *formal corporate insolvency processes?*

Answer: There has been no discernible improvement or change in the operation of the judicial system except in respect of the formal corporate insolvency process under Article 90 of the Bankruptcy Act, which has attracted very few cases considering the number of insolvent companies and in comparison with the CDRAC procedure (see an independent restructurings).

2. **Question:** *What reforms, if any, have been made to improve the operation of the judicial system in relation to the above 4 areas?*

Answer: A Central Bankruptcy Court has been established. This is a positive move, as "specialist" judges and court officers can better implement the legislation and the proceedings should proceed more rapidly.

3. **Question:** *Are there any identifiable proposals for reforms in these areas?*

Answer: There is a proposed amendment to the Civil Procedure Code related to debt recovery and enforcement. The foreclosure laws are the subject of review, as is the reorganisation process under the Bankruptcy Act.

4. **Question:** *What are the main problems or difficulties regarding the operation and application of the corporate insolvency law through the court system?*

Answer: There are no significant problems or difficulties regarding the operation and application of the corporate insolvency law through the court system since the Central Bankruptcy Court has been established, but as it has only been in existence a few months, it is perhaps too early to comment.

5. **Question:** *What practical improvements might be made to overcome these problems/difficulties?*

Answer: No answer provided.

J. Insolvency Administration System

1. **Question:** *Comment on the extent of development, expertise and efficiency regarding both public and private sector administration of formal cases of:*

Answer:

- (a) *corporate liquidation; and*

The corporate liquidation is exercised by the appointed liquidator. The liquidator's power is stipulated in accordance with Section 1259 of the Civil & Commercial Code. There has been no amendment to the law, even though the Bankruptcy Act has been amended several times. In practice there are few cases filed with the Court by the liquidator on such grounds. There is also no specific qualification for liquidators under the corporate law. Anybody can be a liquidator if he or she is appointed by the shareholders of the company at an extraordinary meeting of shareholders to dissolve the company, or if he or she is appointed by the Court. Therefore, liquidators have no special expertise.

(b) *corporate reorganisation*

As the reorganisation law has just been implemented, not many cases have been filed with the Court. No comments can properly be made at this stage. From the records available at the Bankruptcy and Civil Courts, Planners for corporate reorganisation have come from the major accounting firms. Such firms are probably best equipped for the role.

2. **Question:** *Is it considered that education and training in these areas would be valuable and, if so, in what areas?*

Answer: Education and training in substantive insolvency law and procedure would be valuable. The judges who deal with insolvency cases and business reorganisation cases should also be trained in business matters, not purely legal so that they can understand the cases well.

3. **Question:** *Is it considered desirable to introduce more formal structures of both public and private sector administration of insolvency cases?*

Answer: Yes, so that cases can go more smoothly.

L. General Insolvency Information and Developments

1. **Question:** *Provide details of any other relevant information or developments since January 1999 in regard to such issues as the effect of insolvency law policies on areas such as employment, fiscal/revenue debts, detection and recovery of corporate fraud, domestic and foreign investment and etc.*

Answer: Although economic growth is now occurring (estimated 3-5% for 1999), unemployment is at ...% and NPLs stood at 46% of total outstanding credit at the end of June. It appears that while the economic recession has already troughed, the clean-up in its aftermath will take years.

2. **Question:** *Is there any evidence of a change in attitudes (such as social/commercial stigma, aversion to strict legal processes, fear of loss of control) toward the use of:*

- (a) *formal insolvency processes; and*
- (b) *Informal insolvency processes*

in respect of corporations in financial difficulty or insolvent corporations? If possible, provide details of any specific cases which might reflect

evidence of change.

Answer: In our own assessment and judging from the statistics, we can find no evidence of a discernible change in attitudes towards the insolvency processes.

B. The efficiency of the administration of justice in the participating countries

Question: *Some of the sections in the Report and the Addendum to that Report referred to in A above also address the administration of justice in Thailand. Please advise as to the extent to which the Report and the Addendum to that Report are accurate in this respect and also advise of any amendments or modifications which should be made to those aspects of the Report or the Addendum to that Report.*

Answer: The administration of justice in Thailand is better than it has been in the past. The procedures at the Bankruptcy Court are much faster. There is a good computerised system to record and search cases at the Bankruptcy Court and at the Legal Execution Department. This system is regarded as efficient.

C. Treaty

1. **Question:** *To what regional treaties providing for economic cooperation or designed for the facilitation of trade is Thailand a party?*

Answer: An important treaty providing for regional cooperation to which Thailand is a party is the Association of South-East Asian Nations (ASEAN). The substantial treaties for economic cooperation or facilitation of trade for ASEAN Countries (Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam) are as follows:

- Agreement on the common effective preferential tariff scheme for the ASEAN free trade area (AFTA);
- Framework Agreement on the ASEAN Investment Area (AIA);
- ASEAN Industrial Cooperation Scheme (AICO);
- ASEAN Framework Agreement on Services (AFAS);
- e-ASEAN Framework Agreement (e-ASEAN); and
- ASEAN Framework Agreement on the Facilitation of Goods in Transit (AFGT).

Note: For some ASEAN countries, the terms of these Agreements are different from those applicable to other ASEAN countries.

2. Question: What are the terms of those treaties?

Answer:

(AFTA): This Agreement aims to further the economic growth of the region by accelerating the liberalisation of intra-ASEAN trade and investment with the objective of creating the ASEAN Free Trade Area using the Common Effective Preferential Tariff (CEPT) Scheme. The CEPT is an agreed effective tariff, preferential to ASEAN, to be applied to goods originating from ASEAN Member States. Member States agree to follow a schedule of effective preferential tariff reductions. Member States agree to eliminate all quantitative restrictions in respect of products under the CEPT Scheme, and agree to eliminate other non-tariff barriers. Moreover, Member States shall make exception to their foreign exchange restrictions relating to payments for products under the CEPT Scheme.

(AIA): The AIA aims to make ASEAN a competitive, conducive and liberal investment area through several measures. The AIA will have important implications for investment strategies and production activities in the region. The ASEAN investor will benefit from the AIA arrangement in the following ways:

- Greater investment access to industries and economic sectors as a result of the opening up of industries under the AIA arrangements;
- National treatment;
- Greater transparency, information and awareness of investment opportunities in the region;
- More liberal and competitive investment regimes; and
- Lower transaction costs for business operations across the region.

The privileges offered by the AIA in investment market access and the granting of national treatment take immediate effect for ASEAN investors, with the exception of those sectors in the list of exclusions. There are three categories of exclusions, the Temporary Exclusion List (TEL), the Sensitive List (SL), and the General Exception List, for national security, public morals, public health or environmental protection.

(AICO): This Scheme is designed to provide the guidelines and institutional framework within which the ASEAN private sector may collaborate on the basis of mutual and equitable benefits for

the ASEAN Member States, and increased industrial production for the region as a whole. The process is that a minimum of two companies of two different ASEAN countries will participate, and form an AICO Arrangement which specifies the products which shall receive the privileges under the arrangement. This arrangement is not a legal entity but is a type of umbrella association under the scheme, whereby the output of the participating companies will enjoy a preferential tariff rate in the range of 0-5 (percent) % and other privileges.

(AFAS): This Framework seeks to enhance cooperation in service amongst Member States, eliminate restrictions to trade in service amongst Member States and liberalise trade in services by expanding the depth and scope of liberalisation beyond those undertaken by Member States under the General Agreement on Trade in Services ("GATS") of the World Trade Organisation ("WTO"). Members States shall accord preferential treatment to one another on a Most-Favoured Nations basis. Member States who are WTO Members shall continue to extend their specific commitments under GATS to ASEAN Member States who are not WTO Members. Member States shall identify sectors for cooperation, and formulate Action Plans which provide details on the cooperation. Member States shall also enter into negotiations on measures affecting trade in specific service sectors, and such negotiations shall be directed towards achieving commitments.

(e-ASEAN): This Agreement covers measures to:

- facilitate the establishment of the ASEAN Information Technology infrastructure;
- adopt electronic commerce regulatory and legislative frameworks;
- promote and facilitate the liberalisation of trade in ICT products and the provision of ICT services. Member States shall eliminate duties and non-tariff barriers on intra-ASEAN trade in ASEAN ICT products in three tranches (2003, 2004 and 2005);
- develop an e-Society in ASEAN and capacity building to reduce the digital divide within individual ASEAN Member States and amongst ASEAN Member States;
- promote the use of ICT applications in the delivery of government services (e-Government);

"ICT" means Information and Communication Technology. "ICT products" means the products in the WTO Information Technology Agreement and related products which Member States may

agree to add later. "ICT services" means the Information and Communications-related services listed in the Central Product Classification (CPC) and any additional related services which Member States may agree to add later.

(AFGT): This Agreement provides an arrangement for the facilitation of inter-State traffic and transit transport among ASEAN countries. The principles under this Agreement which the Contracting Parties must follow are:

- Contracting Parties shall accord transit transport to or from the territory of any other Contracting Party treatment no less favourable than the treatment accorded to transit transport to or from any other country;
- Contracting Parties shall accord products which have been in transit through the territory of any other Contracting Party treatment no less favourable than that which would have been accorded to such products had they been transported from their place of origin to their destination without going through the territory of such other Contracting Party;
- Contracting Parties shall ensure the consistent application of the relevant laws and regulations, procedures, and administration guidelines and other rulings within each Contracting Party;
- Contracting Parties shall endeavour to ensure the simplification of all transit transport procedures and requirements in ASEAN;
- Contracting Parties shall make all laws, regulations, procedures and administrative notifications pertaining to the relevant authorities publicly available in a prompt, transparent and a readily accessible manner;
- Contracting Parties shall ensure the efficient and effective administration of transit transport to facilitate movement of goods in transit;
- Contracting Parties shall ensure that an effective mechanism for the review of the decisions by the relevant authorities of Contracting Parties is made available and accessible to users and providers of transit transport within ASEAN; and
- Contracting Parties shall provide their utmost cooperation and mutual assistance between the concerned agencies involved in the facilitation of goods in transit in ASEAN.

3. Question: *What are the mechanisms for amending those treaties?*

Answer:

(AFTA): Any amendments to this Agreement shall be made by consensus and shall become effective upon acceptance by all Member States.

(AIA): Any amendment to this Agreement shall be made by consensus and shall become effective upon the deposit of instruments of ratification or acceptance by all signatory governments with the Secretary-General of ASEAN.

(AICO): Any amendment of this Agreement shall be made by consensus and shall become effective upon acceptance by all Member States.

(AFAS): The provisions of this Agreement may be amended through the consent of all the Member States and such amendments shall become effective upon acceptance by all Member States.

(e-ASEAN): Any amendments to this Agreement shall be made by consensus and shall become effective upon the deposit of instruments of ratification or acceptance by all signatory governments with the Secretary-General of ASEAN.

(AFGT): Any amendments to the provisions of this Agreement shall be effected by the consent of all Contracting Parties.

4. Question: *Can a signatory to those treaties reserve its position in respect of any amendment with a right to "opt in" either generally or with a prescribed period of time?*

Answer:

(AFTA): No reservations can be made with respect to any of the provisions of this agreement. However, Member States are entitled to take action and adopt measures which they consider necessary for the protection of their national security, public morals, human, animal or plant life and health, and the protection of articles of artistic, historic and archaeological value.

(AIA): There are no reservation clauses in the Agreement. However, the privileges offered by the AIA in investment market access and the granting of national treatment take immediate effect for ASEAN investors, with the exception of those sectors in the list of exclusions.

(AICO): There are no reservations to any of the provisions of this agreement.

(AFAS): A Member State cannot reserve its position in this Agreement. However, Member States are not required to accept or enter into

any mutual recognition agreements or arrangements which arise from this Agreement.

(e-ASEAN): There are no provisions which entitle Member States to reserve their position under this Agreement.

(AFGT): No reservations may be made to this Agreement either at the time of signature or ratification.

5. Question: Do those treaties provide for resolution of trade or other disputes?

Answer:

(AFTA): The Agreement provides dispute resolution of any matter affecting the implementation of the Agreement only. Member States shall accord adequate opportunity for consultation regarding any representations made by other Member States with respect to any dispute. In respect of any matter for which it has not been possible to find a satisfactory solution during previous consultations, the matter shall be submitted to the Council which is established by the ASEAN Economic Ministers (AEM), and if necessary, to the AEM itself.

(AIA): The Agreement provides dispute resolution for any matter affecting the interpretation or application of this Agreement only. The Protocol on Dispute Settlement Mechanism for ASEAN shall apply in relation to any dispute arising from, or any differences between Member States concerning the interpretation or application of this Agreement, or any arrangement arising from it. However, if necessary, a specific dispute settlement mechanism may be established for the purpose of this Agreement which shall form an integral part of this Agreement.

(AICO): The Agreement provides dispute resolution for any matter affecting the interpretation or application of this Agreement only. Any differences between the ASEAN Member Countries are to be settled amicably between the parties, but if such differences cannot be settled amicably, they shall be submitted to the Dispute Settlement Mechanism for ASEAN.

(AFAS): The Agreement provides dispute resolution for any matter affecting the implementation of the Agreement only. The Protocol on Dispute Settlement Mechanism for ASEAN is applied for such disputes.

(e-ASEAN): The Agreement provides dispute resolution for any matter affecting the interpretation or application of this Agreement only. The disputes are to be settled by

consultation between the Member States concerned. If a settlement cannot be reached, the dispute shall be a "default" in accordance with the Protocol on Dispute Settlement Mechanism for ASEAN.

(AFGT): The Agreement provides dispute resolution for any dispute under this Agreement only. The provisions of the ASEAN Protocol on Dispute Settlement Mechanism shall apply to the consultation and settlement of such disputes.

Note: The dispute resolution procedure under the Protocol on Dispute Settlement Mechanism for ASEAN are as follows:

- A Member State is entitled to seek recourse to another forum for the settlement of disputes involving other Member States. A Member State involved in a dispute can resort to another forum at any stage before the Senior Economic Officials Meeting ("SEOM") has made a ruling on the panel report;
- When the dispute arises, Member States shall accord adequate opportunity for consultation regarding any representation made by other Member States;
- Member States which are parties to a dispute may at any time agree to conciliation or mediation. This may begin at any time, and be terminated at any time. Once procedures for conciliation or mediation are terminated, a complaining party may then proceed to raise the matter to SEOM. The SEOM shall establish a panel to make an assessment of the dispute, examine the facts of the case and the applicability of and conformity with the sections of the disputed Agreement or any covered agreement, and make such other findings as will assist the SEOM in making the rulings;
- The SEOM shall consider the report of the panel in its deliberations and make a ruling.
- Member States, who are parties to the dispute, may appeal the ruling by the SEOM to the ASEAN Economic Ministers ("AEM"). AEM shall make a decision based on simple majority. The decision of the AEM on the appeal shall be final and binding on all parties to the dispute.
- If the Member State concerned fails to comply with SEOM's rulings or AEM's decisions within a reasonable period of time, then that Member State shall, if requested, and within the reasonable period of time, enter into negotiations with any party having invoked the dispute regarding the mutually acceptable compensation. If no satisfactory

compensation has been agreed, any party having invoked the dispute settlement may request authorisation from the AEM to suspend the application to the Member State concerned of concessions or other obligations in the disputed Agreement and/or covered agreements.

6. Question: *Do those treaties otherwise provide for a collaborative approach to addressing issues of mutual interest?*

Answer:

(AFTA): No.

(AIA): No.

(AICO): No.

(AFAS): No.

(e-ASEAN): No.

(AFGT): No.

7. Question: *Do those treaties provide for an exchange of information on issues of mutual interest?*

Answer:

(AFTA): No.

(AIA): No.

(AICO): No.

(AFAS): No.

(e-ASEAN): No.

(AFGT): No.

8. Question: *Do any of those treaties address the harmonisation of laws which may effect economic relations between member countries? If so, what are the relevant treaties and stipulations contained in them?*

Answer:

(AFTA): No.

(AIA): This Agreement specifies in the General Obligations that the Member States shall take appropriate measures to ensure transparency and consistency in the application and interpretation of their investment laws, regulations and administrative procedures, in order to create and maintain a predictable investment regime in ASEAN.

(AICO): No.

(AFAS): No.

(e-ASEAN): This Agreement provides that Member States shall adopt an electronic commerce regulation and legislative frameworks

as follows:

expeditiously put in place national laws and policies relating to electronic commerce transactions based on international norms;

facilitate the establishment of mutual recognition of digital signature frameworks;

facilitate secure regional electronic transactions, payments and settlements, through mechanisms such as electronic payment gateways;

adopt measures to protect intellectual property rights arising from e-commerce. Member States should consider adoption of the WIPO Copyright Treaty 1996" and the WIPO Performances and Phonograms Treaty 1996;

take measures to promote personal data protection and consumer privacy; and

encourage the use of alternative dispute resolution mechanisms for on-line transaction.

(AFGT): The Agreement provides the main principle that Contracting Parties shall ensure the consistent application of the relevant laws and regulations, procedures, and administration guidelines and other rulings within each Contracting Party.

D. Actual outbound cross-border cases

1. Question: *In the course of the last five years, are you aware of there having been any companies which were incorporated in Thailand which have been placed under some formal insolvency administration and which have had assets and/or liabilities in countries other than Thailand? If so, please identify those companies.*

Answer: We are aware that most of the companies in Thailand which have been placed under some formal insolvency administration, and which have had assets and/or liabilities in countries other than Thailand are the companies which are under rehabilitation. However, we are not able to disclose the names of those companies because of professional conduct requirements. We are also aware of one company with assets which was placed under absolute receivership, and under the administration of the receiver.

2. Question: *In the case of each of those companies, are you aware of how those non-Thai assets and liabilities were administered? If so, in each case, please provide a general description of the process of administration*

Answer: In the rehabilitation process, once the court approves and appoints the planner or the plan-administrator (as the case may be), the planner or the plan-administrator will administer the debtor's business and prepare or implement the rehabilitation plan, while the official receiver will have the authority to deal with all creditors' claims for repayment of debt. The planner or plan-administrator will oversee all the debtor's assets and liabilities, whether or not they are Thai or non-Thai assets and liabilities. The plan-administrator will implement and administer the assets and liabilities of the debtor according to the plan. In summary, the planner or plan-administrator will administer those non-Thai assets and liabilities as specified by the business plan. For the bankruptcy process, the official receiver is not entitled to administer non-Thai assets and liabilities in countries other than Thailand.

3. **Question:** *In the case each of those companies and so far as you are aware, were Thailand creditors permitted to file their claims in the formal insolvency administration being conducted in Thailand? In any case, were any those non-Thai creditors required to obtain a judgment in the Courts of Thailand or otherwise undertake any formal procedure in Thailand as pre-requisite to filling their claims?*

Answer: Non-Thai creditors are permitted to file their claims in the formal insolvency administration being conducted in Thailand. If such creditors file their claims with the official receiver under the bankruptcy process, such creditors must prove to the official receiver that Thai creditors are also entitled to file their claims for repayment within the creditor's country. Non-Thai creditors are not required to first obtain a judgment in the courts of Thailand. If such creditors file their claim with the official receiver under the rehabilitation process, then they just present evidence of the debt to the receiver in the bankruptcy case. Non-Thai creditors are not required to obtain a judgment in the courts of Thailand or otherwise undertake any formal procedure in Thailand as a pre-requisite to filing their claims.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Thai creditors exercise their rights by pursuing claims against the non-Thai assets of the company? If so was there any procedure or process either available to or invoked by the insolvency administrator of those companies in Thailand to restrain them from doing so?*

Answer: We are not aware of any non-Thai creditors exercising their rights by pursuing claims against the non-Thai assets of the company.

E. Actual inbound cross-border cases

1. **Question:** *In the course of the last five years, are you aware of there having been any cases of companies which were incorporated other than in Thailand which have been placed under some form of insolvency administration and which have had assets and/or liabilities in Thailand? If so, please identify those companies.*

Answer: We are aware of two cases of companies which were incorporated in countries other than Thailand, which have been placed under receivership, and which have had assets and/or liabilities in Thailand. One case was administered by a Singaporean liquidator, the other by a Japanese administrator. However, we can not reveal the names of the debtor companies as it is against rules of professional conduct.

2. **Question:** *In the case of each of those companies, are you aware of how its assets and liabilities in Thailand were administered? If so, in each case, please provide a general description of the process of administration*

Answer: As far as we are aware, the insolvency administrators in those cases had to file a complaint with the Thai court in order to enforce the assets and liabilities in Thailand.

3. **Question:** *In each case and so far as you are aware, in the case of Thailand creditors, were they permitted to file their claims in the formal insolvency administration of the company being conducted in its place of incorporation?*

Answer: As far as we are aware, the Singaporean liquidator and the Japanese administrator permitted Thai creditors to file their claims against the company in the place of incorporation of the debtor company.

4. **Question:** *In the case of each company and so far as you are aware, did any of the non-Thai creditors exercise their rights by pursuing claims against the non-Thai assets of the company? If so was there any procedure or process either available to or invoked by the insolvency administrator of the company in its place of incorporation to restrain those creditors from doing so?*

Answer: We are not aware of Thai creditors exercising their rights by pursuing claims against Thai assets of the company.

F. Hypothetical inbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in Singapore and trades through a branch in Thailand with the result that it has assets and liabilities there. ABC is ordered to be wound up by order of the Singaporean Courts and liquidator is appointed to administer its affairs. The liquidator wishes to take control of and administer the assets of ABC in Thailand or alternatively, arrange for their administration. She also wishes to arrange for all creditors of ABC, whether resident in Singapore, in Thailand or else where, to file their claims in Singapore so that those claims can be dealt with equitably and consistently.

Assuming that there is presently no procedure in Thailand for recognising the liquidation of ABC in Singapore.

1. **Question:** *What procedures can be invoked in Thailand for placing ABC under a formal insolvency administration?*

Answer: Under the Thai Foreign Business Act, BE.2542, the branch office is the same judicial person as ABC in Singapore. The Branch operation license shall cease if its head office is placed under a bankruptcy order. However, the foreign bankruptcy order is not recognised in Thailand. Therefore, the appointed liquidator of ABC in Singapore must either come to Thailand to proceed with the cancellation of its branch office operation license, or instruct and authorise the branch office manager to cancel or return the operation license to the Foreign Business Department or the Ministry of Commerce, and to appoint a liquidator in Thailand to liquidate the office. All assets in Thailand have to be sold and the money received from such sales and liabilities shall be the property of the head office in Singapore. All Thai creditors have to file their claims for repayment of debts with the liquidator in Singapore.

2. **Question:** *In the case of each of those procedures, does the Singaporean appointed liquidator have standing to initiate the necessary application? If not, then in the case of each procedure in which the Singaporean appointed liquidator does not have that standing, who does have standing?*

Answer: The Singaporean appointed liquidator will initiate the necessary process by giving instruction to ABC's branch office manager in Thailand to appoint a private liquidator or, if ABC's branch office manager is no longer present, the Singaporean appointed liquidator has to come to Thailand to appoint the liquidator to liquidate the branch office. After liquidation, the liquidator in Thailand will sell the assets in Thailand, and since the money and liabilities are those of ABC in Singapore, will deal with such assets and liabilities according to ABC's Singaporean liquidator's instructions.

3. **Question:** *In the case of each procedure, to whom is the necessary application made for an order or direction establishing a formal insolvency administration?*

Answer: See F2. The process is the appointment of a private liquidator for the branch office in Thailand.

4. **Question:** *In the case of each procedure, how long does it typically take to obtain an order or other direction establishing a formal insolvency administration?*

Answer: It may only take one week to appoint a liquidator in Thailand. It may take approximately two to four months or longer to liquidate the office and sell the assets of the company, depending on the type and the amount of the assets. It only takes one day to cancel or return the operating license of the branch office.

5. **Question:** *In the case of each procedure, is it possible to obtain some interim or other like order or direction which secures the independent control of the assets of ABC in Thailand pending the final determination of the application for an order or other direction establishing a formal insolvency administration?*

Answer: It is not necessary to obtain any interim or other like order which secures the independent control of the assets of ABC in Thailand. This is because it is the appointed private liquidator in Thailand who deals with the

assets of the ABC branch office in Thailand under the control or direction of the Singaporean appointed liquidator.

6. Question: *In the case of each procedure, what does it typically cost to obtain a final order or direction establishing a formal insolvency administration?*

Answer: The fees of liquidators in Thailand are negotiable.

7. Question: *In the case of each procedure, to what extent do the Thailand creditors enjoy priority to or precedence over non-Thai creditors in the context of that procedure?*

Answer: Thai creditors could not enjoy priority to or precedence over non-Thai creditors. The liquidator in Thailand has no authority to distribute any assets or money of the branch office to creditors in Thailand, except as authorised by the Singaporean liquidator. All creditors must file their claims for repayment of debt with the liquidator in Singapore.

8. Question: *In the case of each procedure, may the Singaporean and other non-Thai creditors of ABC file their claims in the formal insolvency administration established under that procedure? If so, what formal procedures or other pre-requisites have to be satisfied by those creditor prior to them filing their claims?*

Answer: Thailand does not recognise the liquidation of ABC in Singapore. The liquidation in Thailand is just to follow the instruction of the Singaporean appointed liquidator in order to acquire and deal with all assets and liabilities of the branch office in Thailand. Therefore, there is no procedure for filing claims for the repayment of debt in Thailand. All creditors, including Thai creditors must file their claims in Singapore.

G. Hypothetical outbound cross-border insolvency case

Assume that ABC Limited ("ABC") is incorporated in Thailand and trades through a branch in Singapore with the result that it has assets and liabilities in Singapore. ABC is placed under a formal administration in Thailand and an independent trustee is appointed to administer its affairs.

1. Question: *Is there any procedure available in Thailand which will facilitate an application to the Courts in Singapore for the establishment of an independent insolvency administration of ABC?*

Answer: If ABC in Thailand is placed under a formal administration, the official receiver as appointed by the court shall have sole authority to manage and dispose of the property of the debtor, or do any necessary act to complete any pending business of the debtor, and to collect and receive money or property belonging to the debtor, or which the debtor is entitled to receive from others. There are no procedures available in Thailand which will facilitate an application to the courts in Singapore for the establishment of an independent insolvency administration of ABC.

2. Question: *If so, please describe that procedure.*

Answer: See G1.

3. Question: *Does the fact that the principal insolvency administration of ABC is initiated in Thailand as distinct from the insolvency administration of a company's branch affect the answers to A7 or A8?*

Answer: See A7. i.e. there are no special priorities for their creditors. However, under Section 178 of the Thai Bankruptcy Act, foreign creditors who are resident outside the Kingdom can claim repayment of debts in the bankruptcy only when they comply with the following conditions:

Proof that creditors in the Kingdom of Thailand are similarly entitled to claim for payment of debts in bankruptcy actions under the laws and before the courts of the countries of which the foreign creditors are nationals; and

They must report the amount of the asset or distribution that they have received or are entitled to receive from the same debtor's estate located outside the Kingdom, if any. If so, they must agree to deliver the asset or distributor from the debtor's said estate to be added to the debtor's estate in the Kingdom.

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