A GLOBAL APPROACH FOR MULTI-CREDITOR OUT-OF-COURT RESTRUCTURINGS - A MAJOR STEP FORWARD FOR THOSE INVOLVED IN INFORMAL WORKOUTS

Workouts, turnarounds, informal or out-of-court restructurings, whatever term used to describe them, they have now been around for some years in many countries of the world. Initially inspired by the London Approach, set up through the Bank of England in London, the practice of lenders working informally together to help rescue a company in trouble has become standard practice in those countries, albeit in somewhat different forms allowing for differing legal systems.

Two things have led to a desire to establish a set of basic Principles by which all such restructurings are carried out. Firstly, restructuring itself becomes ever more difficult. Whilst initially such arrangements mainly concerned banks, increasingly it is necessary also to involve bondholders, derivative counterparties, major trade creditors and so on. There are less people familiar with the informal practices, and more pressure on those trying to lead such restructurings.

Secondly, as has been so well proven in the economic crisis in South East Asia, in many developing countries of the world, there is no history or experience of out-of-court restructuring at all.

The Insol Lenders Group (a sub group of Insol the International Federation of Insolvency Practitioners) has been working on a set of basic Principles to be used in such restructurings. This became part of an initiative set up by the World Bank in 1999. After considerable work and worldwide consultation, involving 150 different bodies, Insol has now formally launched the Principles, which have been distributed to all its members worldwide.

It is the hope that over time, these Principles will become widely accepted as the framework used by those involved in informal restructurings, providing a basis for inter-creditor negotiations. This should provide more certainty, and reduce the number of inter-creditor disputes that can so easily become a feature of such endeavours. The Principles will certainly not resolve all the difficulties that can arise in such negotiations, but the acceptance of basic Principles will allow those involved to focus more on the actual rescue of the company.

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The published document comprises two parts. Firstly, there are eight Principles, which it is intended should be adopted internationally, and form the basis of restructurings in the future. These eight Principles are listed at the end of this article.

Secondly, attached to each of the Principles is a commentary which consists of a discussion of the salient features and problems within each Principle, and also discusses best practice, gleaned from the handling of previous situations. It is hoped that such practice may be helpful when there are difficulties but it is acknowledged that local laws and practice may not always permit some methods.

The intent of these Principles is to provide a sound basis against which the lenders and other major creditors involved in restructuring can seek to reach agreement. This will particularly apply to the larger cross-border or international multi-banked situations, but there is no reason why they should not also be applied on a domestic basis in multi-banked deals. They will provide a number of advantages for those using them.

a. The learning curve will be reduced. Instead of groups of creditors in each new restructuring sitting around and determining the rules by which they will play, there will be a basic set of Principles from which to start, which means that they can move much more swiftly onto the key issues. The real focus of attention should be the business to be restructured, assessing its viability and determining by what method value may be preserved. All too often huge amounts of time are spent resolving inter-creditor disputes, time which could be better spent in helping save the business.
b. Time and costs are saved. Cost is an important ingredient. The longer that is spent on inter-creditor disputes, the longer likely involvement of professionals, especially lawyers, and the higher the overall cost will be, almost invariably to the account of the company.

c. Distrust and suspicion can be reduced. There will always be anxiety and the risk of distrust between the various creditor groups, who by their very nature are in competition with each other. Such suspicion is particularly the case when there are banks and other creditors from different countries, unaccustomed to local practice. The existence of a set of Principles which is widely accepted and practiced, should increasingly help to remove some of this distrust, lead to greater co-operation, and ultimately a swifter and hopefully better resolution of situations.

d. The Principles are not intended to vary the legal position of any creditors, nor to alter their rights. They specifically acknowledge the initial starting positions of each creditor, and one of the key cornerstones of the Principles is that the starting position of any creditor should not, during the process, be prejudiced, vis a vis the positions of other creditors.

A key factor in achieving successful out-of-court restructurings is that there should be an effective, reliable and predictable set of insolvency laws in the country concerned. Whilst the lack of such laws does not mean that informal processes cannot work, they are likely to be much more effective if the formal process is there to fall back upon. Indeed, the out-of-court restructuring process has often been described as operating in the "shadow of the law". The Principles acknowledge the importance of applicable local law, and clearly they have to be made to work against the differing backgrounds. Where local law is less than helpful, it is the hope that the value of effective out-of-court restructuring will, in due course, lead to adjustment to local laws so as better to assist the working of the Principles. This in fact is another key purpose of the Principles. They are likely to be of particular value to developing countries, and will be of special use where such countries are revising or bringing in new insolvency laws. It would clearly be beneficial if those drafting those laws were to do so in such a way that took account of the Principles, and thus made for a more effective and efficient informal or out-of-court restructuring process in the countries concerned. Indeed, one of the comments within the World Bank Initiative is that the formal process may work better if it enables the use of informal techniques.

So why have the Principles? There is a much over-used expression "win, win", but potentially that actually applies to the use of the Principles. The more effectively that they are used, the quicker restructurings will be achieved, and the greater the chance of preservation and indeed maximisation of value. There should be less inter-creditor disputes, more certainty for those running the business, better prospects for finding a solution and thus for other stakeholders, including employees, less damage overall to other companies trading with the business and, perhaps ultimately, a benefit to the economy of the country concerned as a whole. Last but not least, the less time that is lost, the better the likelihood of an improved return to the creditors around the table.

So what next? The Principles have been endorsed by organisations such as the World Bank and the Bank of England, have the support of the IMF and are approved by a large number of organisations around the world. The next stage is to see them brought into use. This will happen in several ways.

Firstly, those who are involved in restructuring who approve and support the Principles will start ensuring that they are used in practice. This is already happening, and in a number of recent restructurings and workouts, the Lead Bank or co-ordinator has asked that the Principles be used as the basis for negotiation, which has been accepted by the lender groups involved.
Next there has to be a wide promotion of the Principles, especially in those parts of the world where they are likely to be least known, and therefore ultimately most useful. This will mean presentations at conferences and seminars, but more particularly creating opportunities to discuss them with central banks, regulators, judiciary, professional organisations, lenders and so on in those countries.

Finally, there is likely to be the need to set up training, the Principles will best work if there are people who understand how they can apply in different situations, and have a good understanding of how the different Principles are put into practice.

This is a daunting task, and will require much effort. Insol has accepted this as a challenge, and will be giving it every support. The success of this initiative should be of particular importance to lenders, particularly banks, and Barclays Bank Plc has determined it to be sufficiently important that it is prepared to put resource behind it to see it promoted successfully. To achieve this, Barclays has agreed to allow Terry Bond, the author of this article, to dedicate a considerable part of his time over the next few months in developing this work. This reflects the importance which Barclays attaches to this venture. As says Ivan Armstrong, Head of Corporate Support and Recoveries "We had no hesitation in making Terry Bond available for this important stage of the embedding of the Principles. The Principles will provide a means of stakeholders working together to retain value in business which could be lost through insolvency. Barclays is committed to this aim both in the UK and internationally".

There is much to be done, but, after some years in development, with the combination of a tremendous drive to see this initiative work, coupled with an obvious desire already being exhibited around the world to learn more about the Principles, the prospect is looking good.

As says Neil Cooper, President of Insol, "It is essential that out of court systems work against a backdrop of efficient modern systems that deliver fairness and certainty to all the stakeholders. With this proviso, we believe that the INSOL Principles make a major contribution to the preservation of ultimately viable businesses, employment and the other factors that in sum are termed "the Rescue Culture". They deserve support from all stakeholders, including governments and central banks, in the common good of our economies".