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Draft UNCITRAL Legislative Guide on Insolvency Law

Note by the Secretariat

Compilation of comments by international organizations

Contents

		Page
I.	Introduction	2
II.	Compilation of comments	2
	International organizations	2
	European Commission—Directorate-General Justice and Home Affairs	2
	European Bank for Reconstruction and Development (EBRD)	4
	International Labour Organization (ILO)	5
	International Monetary Fund (IMF) Legal Department	7

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I. Introduction

1. In preparation for the thirty-seventh session of the Commission, the text of the draft Legislative Guide on Insolvency Law, as approved in principle by the Commission at its thirty-sixth session in 2003 and by the Working Group in September 2003 was circulated to all governments and to interested international organizations for comment. The comments received as of 26 March 2004 that relate specifically to the content of the draft Guide are reproduced below.

II. Compilation of comments

International organizations

European Commission

Directorate-General Justice and Home Affairs

[Original: English]

First, the draft Guide says that it would be used as a reference for law making but it does not provide a single set of solutions. Instead, there is some attempt in the Recommendations presented at the end of each section to strike a balance between the different objectives of insolvency law—e.g. between universal proceedings and territorial proceedings, liquidation and re-organization, creditor-friendly and debtor-friendly regimes, secured and ordinary claims. As a result, such an approach seems to argue against any need for harmonization e.g. through a binding international instrument. Where the recommendations address specific issues of substantive insolvency law, it is possible that such legislative guidelines would constitute a pragmatic solution, given the difficulty in finding a common approach on matters that were developed in different ways by national judicial systems. However, where jurisdictional rules and conflict of law rules may apply to cross-border insolvencies, there is a need to ensure their compatibility between countries.

Therefore the draft Guide refers to existing instruments of private international law such as the UNCITRAL Model Law on Cross-Border Insolvency and the EC Regulation No 1346/2000 of 29 May 2000 on Insolvency Proceedings. In particular, the definitions of the centre of main interests of the debtor and of an establishment for the opening of proceedings are also mentioned in the draft Guide. However, there is some inconsistency between paragraph 99—"especially where the parties are from a foreign country, it should be made clear in the law which courts have jurisdiction for which functions"—and footnote No 8—"this recommendation is intended to indicate minimum and non-exclusive grounds for commencing insolvency proceedings. Other grounds, such as the presence of assets, are used in some jurisdictions". We find no particular justification for the continued use of the assets criterion. This is not to say that one may not exist—but, if it does, it should be inserted in the Recommendation. If it does not, or if it is weak—see paragraph 98 which states: "the test of presence of assets may therefore raise multi-jurisdictional issues, including the possibility of multiple proceedings and questions of coordination and cooperation"—we are not clear what recommendation is being made.

Second, under Recommendation (18) on page 69, paragraph 583 on page 219 and Recommendation (158) on page 228 about formalities for submission of foreign claims, it is worth mentioning the specific provisions of Articles 40 to 42 of EC Regulation No 1346/2000 concerning the information of creditors.

Page 72, under paragraph 161 beginning "other insolvency laws provide that the security right is unaffected by insolvency proceedings and secured creditors may proceed to enforce their legal and contractual rights", it should be highlighted that such a principle is provided in a cross-border context by Article 5 of EC Regulation No 1346/2000.

Page 73, under paragraph 166, it would be useful to make a reference to the solution adopted in the Regulation which relies on the principle of proceedings with universal scope, while retaining the possibility of opening secondary proceedings whose effects are limited to the territory of the Member State concerned. There is automatic recognition of foreign decisions and special rules for coordination between liquidators.

Paragraphs 324-325 and Recommendation (74) on page 136 about "Security interests": it is worth mentioning the Hague Convention on the law applicable to certain rights in respect of securities held with an intermediary, adopted on 13 December 2002, Article 8.

As to the consideration of priority claims, paragraph 632 on page 234 states that this issue may be of particular concern in transnational cases. Besides the reference to the UNCITRAL Model Law, it is possible to describe briefly the balanced approach followed by the European Union through Article 4.2 (i) of Regulation No 1346/2000 –i.e. the ranking of claims is determined by the law of the State of the opening of (main or secondary) proceedings.

Turning to the crucial issue of group insolvencies, Section C on pages 238-241 favours an extensive approach of insolvency including groups of companies, while highlighting the disadvantages of such an approach. In the European Union, both the "companies group" approach (based on economic criteria) and the "incorporation" approach (based on the head office jurisdiction) were represented. Basically, the new Regulation does not provide for "consolidated" treatment of group companies. However, there are some contradictory cases by national courts that show the difficulty of applying common criteria in practice.

European Bank for Reconstruction and Development[1]

[Original: English]

General comments

In submitting the comments included below, the EBRD noted the importance of insolvency for the transition economies of eastern Europe and Central Asia and that as part of its continuing work in this area, the EBRD will be conducting its New Legal Indicator Survey (NLIS) this year in the area of insolvency. The NLIS will involve measuring the practical effectiveness of the insolvency law regimes in the EBRD's countries of operations to assist in determining where the main strengths and weaknesses of insolvency law regimes in those countries lie. The EBRD also noted the complementary nature of the work of EBRD and UNCITRAL, with the Bank's main emphasis being on the economic benefits to be derived from the enactment of effective, efficient and transparent insolvency law regimes. Based upon their review of the Guide, they expressed that view that it furthers these goals and provides clear policy recommendations that will be of use to civil and common law countries with developed or developing economies.

Specific comments

Paragraph 126 provides that there is no general consensus as to whether re-organisation proceedings can be initiated by a creditor as well as a debtor. We are of the view that the ability of a creditor to initiate such proceedings is critical. This is not simply because management of the debtor corporation may have resigned but, also, because of the inherent desire that creditors are likely to feel to exert some control over the insolvency process. As you point out, in most regimes creditors may institute liquidation proceedings. If instituting restructuring proceedings is also an option to creditors, in other words if they can effect restructuring while still "driving" the process, we are of the view that creditors are more likely to support reorganisation. This is particularly true in the case of regimes in which the party commencing the proceeding is likely to be able to select the insolvency administrator. Creditors are far more likely to support a reorganisation if they are able to ensure that "their" insolvency administrator is at the helm.

Paragraph 142 speaks to the issue of notice to be given upon an application to commence proceedings. It is suggested in the guide that, in some circumstances, the debtor may not need to give notice of the application to commence proceedings to creditors. While there may be circumstances where this is appropriate, this has to be balanced with concerns arising from some insolvency regimes which allow the costs of the insolvency administrator to be put ahead of the interests of secured creditors. Where the law has such provisions, we are of the view that secured creditors should be entitled to notice of applications made to commence proceedings and that, if no such notice is provided, the costs of the insolvency administrator cannot be placed ahead of the interest of such creditors. If notice provisions are not practical in a specific legal regime, we would suggest a provision mandating that court orders initiating the insolvency process be served upon all secured creditors by the insolvency administrator, within a reasonable period of time, and that such secured

[1] The comments provided are noted as not having been reviewed by the EBRD's management.

creditors be explicitly authorised to apply for a variation of the cost provisions of these orders.

Paragraph 143 deals with notice to be given by creditors to the debtor when commencing proceedings but is silent on what notice, if any, need be given by creditors to other creditors. It is not clear whether this omission is intentional. For the reasons described in the preceding paragraph, other than when exceptional time-driven circumstances make it impractical, notice should be given to all known secured creditors by other creditors seeking to commence an insolvency proceeding.

Paragraph 324 suggests that security granted to secured creditors that is not in consideration of "new funds being advanced" may be avoidable under insolvency legislation. The presumption here is that where there are "new funds" advanced, the transaction will not be avoidable. We suggest that the Working Group may wish to amplify this point to be clear that it is not just the advancement of "new funds" that will protect the transaction but, rather, the advancement of any new consideration under the relevant legal system. This distinction is important in the context of, for example, lender forbearance arrangements. Where a lender agrees to forbear from enforcing its rights under a given loan agreement, such forbearance under many legal systems may be a valid consideration and should thus protect any new security given in exchange for that forbearance. As a result, while new cash may not be injected by the lender, valid consideration for new security has been provided.

Paragraph 402 suggests that the insolvency law should specify the degree of relationship between the debtor and the insolvency administrator which may give rise to conflicts of interest. We wholeheartedly endorse this position as such provisions promote greater transparency in the insolvency process. We suggest that the Working Group may wish to give consideration to going much further than this and recommending an outright prohibition against certain relationships. For example, where the insolvency administrator (often a public accounting f=) has, in the past, been the auditor of the debtor corporation, it may be inappropriate to have them act as insolvency administrator. Such proximate relationship poses numerous potential conflicts including, but not limited to, the obvious "Enron Situation" where prior accounting practices of the company and its auditor in fact precipitated the debtor's insolvency. In this situation, an independent insolvency administrator may have the responsibility of pursuing those responsible on behalf of the creditors and would obviously be in conflict if the responsible parties included its own firm.

International Labour Organization (ILO)

[Original: English]

The International Labour Office has followed with interest the work of UNCITRAL's Working Group V on insolvency law and wishes to present the following comments on Doc. A/CN.9/WG.V/WP.70(Part I) and Doc. A/CN.9/WG.V/WP.70 (Part II) in view of the forthcoming finalization and adoption of the Legislative Guide on Insolvency Law.

Concerning the key objectives of an effective and efficient insolvency law as listed in Part One of the Legislative Guide, the ILO cannot agree with the formulation of key objective No. 8 in para.21 (page 14) of the draft text, which declares that "to the greatest extent possible, those priorities should be based upon commercial bargains and not reflect social and political concerns that have the potential to distort the outcome of insolvency" and accordingly suggests that "priority to claims that are not based on commercial bargains

should be avoided". In the ILO's view, this is an ideologically biased manner to express the objective of establishing clear rules for ranking of priority claims. It clearly advocates for priority to be given to money lenders or institutional creditors, thus prejudicing essentially workers whose work is, however, indispensable for any enterprise to be credit-worthy.

Money lenders charge interest on the loans they accord to debtors, in which the risk factor is implied. The risk of not being paid for a loan is normally a business risk for any money lender. As a matter of fact, money lenders charge different rates of interest, depending on the different level of risk each client represents for them. If despite the risk they accept the business, they should be expected also to accept the losses when their client becomes insolvent. By contrast, it is a basic principle in labour law that the workers do not share the employer's business risk. It follows that the approach adopted in the draft legislative guide means no less and no more than to shift the business risk of money lenders and contractors onto the workers' shoulders. Despite what might be the opinion of the drafters of the Guide, the fact remains that most countries in the world have taken the decision to privilege workers' claims in the event of the insolvency of their employer. As 95 countries are to date parties to the ILO's Protection of Wages Convention, 1949 (No. 95), Article 11 of which requires Members to treat workers as privileged creditors in the event of judicial liquidation or bankruptcy, the ILO feels that these countries cannot go along with UNCITRAL's proposal unless they repudiate the international obligations by which they are bound.

With regard to Part Two of the Legislative Guide dealing with core provisions for an effective and efficient insolvency law, the ILO objects to the position taken in para. 629 to the effect that "some priorities are based on social concerns that may more readily be addressed by other law, such as social welfare legislation, than by designing an insolvency law to achieve social objectives which are only indirectly related to questions of debt and insolvency" since "providing a priority in the insolvency law may at best afford an incomplete and inadequate remedy for the social problem, while at the same time rendering the insolvency process less effective". The danger is that, in the interest of facilitating the viability of an insolvent business and rendering the insolvency process less cumbersome for secured creditors and insolvency professionals, the guide not only pays little attention to the social parameters of insolvency and liquidation but openly suggests that any consideration concerning the social protection of workers in the event of an employer's insolvency should be kept outside the ambit of insolvency law. The ILO has serious doubts as to the soundness of the view reflected in the draft Guide to the effect that insolvency law should not seek to respond to social concerns. The Guide in its current reading gives the disquieting impression that the real intention is to dismantle the system of privileged protection in respect of workers' claims, despite its nearly universal application, in order to better protect the interests of institutional creditors. All the more so as the Guide does not appear to propose a valid and readily applicable alternative to the privilege system, since the wage guarantee institutions, which are summarily referred to in the Guide, are admittedly "rich-country arrangements" and are very difficult to put in place and operate in the developing world.

In addition, the ILO considers that paras. 633 and 634 (page 235) reflect poorly international state practice, which overwhelmingly recognizes the need for special protection to be afforded to employee claims and grants such claims a ranking of priority higher than most other privileged claims. It is indicative that the draft text does not mention the case of those jurisdictions in which workers' claims enjoy a "super-privilege" ranking ahead of all other claims, including secured claims (in this connection, the definition of the term "superpriority" in the introductory part of the Guide is incorrect and

has to be reworded). The ILO has had the opportunity to submit alternative language with respect to these two paragraphs which described more faithfully the state of law and practice in most countries, but none of its suggested wording seems to have been retained. The ILO wishes to make a new reference to the 2003 General Survey on the Application of the Protection of Wages Convention, 1949 (No. 95) prepared by the ILO Committee of Experts on the Application of Conventions and Recommendations, which contains in paras. 298-353 a lengthy analysis of national laws in matters of protection of employees' service-related claims. [copy forwarded with comments]

Moreover, recommendation 174 (page 238) as it is currently drafted seems to imply that workers' claims are to be grouped together with all other privileged claims in a single class of priority claims and that they may be satisfied proportionately (and not fully) in the event of insufficient assets. This view reflects the practice in a limited number of countries of common law tradition but is far from being widely accepted. In fact, in the great majority of countries, workers' claims constitute a class of privileged claims on their own and are granted a higher rank of priority that that of the State and the social security system. Besides, this prevailing view has found expression in Article 8(1) of the ILO's Protection of Workers' Claims (Employer's Insolvency) Convention, 1992 (No. 173), which requires Member States to accord to workers' claims a higher rank of privilege than most other privileged claims, and in particular those of the State and the social security system.

Overall, the ILO believes that the ongoing work of UNCITRAL's Working Group V on insolvency law is extremely relevant to its own Decent Work Agenda, indeed in certain respects directly challenging the policy objectives and priorities of the Organization. The ILO intends to keep a watchful eye on the discussions of the Working Group so as to ensure that basic concepts and principles of existing ILO instruments in the field of bankruptcy/ insolvency law are not uncritically undermined. As the ILO Committee of Experts has stated in para. 505 (p. 298) of the above-mentioned General Survey, "the process of making insolvency laws more effective should in no event result in such laws becoming socially insensitive. The designation of employees' wages and entitlements as a preferential debt is a keystone of labour legislation in practically every nation and the Committee would firmly advise against any attempt to question such a principle without proposing in its place an equally protective arrangement, such as a wage guarantee fund or an insurance scheme providing a separate source of assets to ensure the settlement of employees' claims".

International Monetary Fund Legal Department

[Original: English]

1. Overview

The IMF Legal Department has some remaining comments on key aspects of the Guide's discussion of reorganization issues, as well as on other sections of the Guide. This note first addresses reorganization, then provides comments on other chapters in the order that they appear in the Guide.

2. Reorganization proceedings

As noted in previous comments, our primary concerns relate to the provisions governing creditor voting on and approval of reorganization plans. It should be emphasized that these comments are not intended to change the policy direction of the Guide but, rather, are intended to address ways in which the Guide could be more specific and analytical about the policy choices in this critical area.

First, the Commentary and Recommendations need to state explicitly that, if the rights of secured creditors or other priority creditors can be affected by a reorganization plan, then these creditors must in all cases vote in a separate classes from unsecured creditors and from each other. As currently drafted, the Guide does not preclude applicability of a plan to priority creditors, but it also does not expressly state that such creditors must in all cases vote in separate classes. As such, the Guide could be read as allowing arrangements under which secured and other priority creditors may be forced to vote with unsecured creditors. This in turn could cause significant dilution – if not outright deprivation – of the rights of priority creditors and consequential effects, inter alia, on the availability, cost and other terms of credit in jurisdictions with such arrangements. To address this concern, language regarding the need for secured and priority creditors to vote in all cases in separate classes could be added to Rec. 130 and 133, as well as to the third sentence of para. 515 of the Commentary.[2]

Second, the Guide needs to clarify and discuss more systematically the minimum protections that a law should provide to dissenting creditors that are subjected to a restructuring plan (including both minority members of an approving class, and members of a rejecting class on whom the plan is being "crammed down"). The Commentary mentions in passing various kinds of protections (minimum liquidation value rule, absolute priority rule, etc.), but there is no systematic discussion of the issue and no clarification of the minimum protections that must be observed vis-à-vis dissenting creditors in order for a plan to be acceptable. To the contrary, the existing discussions seem limited and discontinuous.[3]

Third, while the issue is discussed well in the Commentary, the Recommendations do not seem to address the approach of subdividing unsecured creditors into classes for voting purposes.[4] As discussed in the Commentary, despite its potential complexity, subdividing of unsecured creditors can in some cases be a crucial means of assuring creditor approval of a reorganization plan. Accordingly, the Recommendations could very usefully be revised to specify that the law should also provide the option for subdividing unsecured creditors into further classes.

Fourth, beyond the voting and plan approval issues discussed above, a separate concern on the reorganization chapter relates to the discussion (para. 535 and 538)

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[2] Para. 515 could be revised to read as follows (additions underlined): "Adopting an approach that allows for secured and priority creditors to vote as a separate class provides a minimum safeguard for the adequate protection of such creditors, and recognizes that the respective rights and interests of secured and priority creditors differ from those of unsecured creditors."

[3] For example, para. 508 first sentence states only that there "may be a need" to ensure protection of dissenting creditors; and para. 532 states only that laws with cram down provisions "generally" include conditions aimed at protecting creditors (with neither discussion shedding light on what are provisions are appropriate in what circumstances). Similarly, Rec. 134 simply notes that the law should address "the treatment" of dissenting classes where approval by all classes is not necessary; Rec. 137 provides for broad continued use of encumbered assets against the secured creditor's wishes without discussing specific protections; and Rec. 138 does not explain what constitutes "fair and equitable" treatment of creditors for plan confirmation purposes (notwithstanding that very few readers outside of the U.S. are likely to be aware of the "gloss" associated with this term under U.S. law).

[4] The current language (Rec. 130) states only that the law should address "whether or not creditors should vote in classes according to their respective rights"; this does not seem to contemplate subdividing *unsecured* creditors into further classes.

of the court's ability to reject or fail to confirm a plan on grounds of lack of economic "feasibility". The one example of such feasibility given in these paragraphs (i.e., lack of arrangements for dealing with secured claims) is appropriate, but the general feasibility point is much broader and could be used to reject a plan in many other, less appropriate, circumstances. Given the complexity of these kinds of economic decisions and the fact that creditors ultimately are the ones best placed to make them, we are of the view that laws generally should either not give courts power to reject a creditor-approved plan on feasibility grounds, or should define very narrowly the circumstances under which this power may be exercised. Language to this effect could usefully be added not only to the Commentary (e.g., para. 539), but also to the Recommendations.

Other comments on reorganization:

- To avoid unlimited court discretion (and, inter alia, the extensive delays that oftentimes go with it), Recommendations 123 and 125 should clarify the circumstances under which the plan filing period and exclusivity period may be extended, or at least should state that the law should identify specific and limited grounds on which such extensions can be granted.
- We would delete the brackets—and retain without revision the relevant statements—in Rec. 128(b)(i), 128(c)(v)-(vii), and 138(e) and (f).
- The references to recommendations "142" and "144" in Rec. 139(a) and 139(b), respectively, should probably read instead recommendations 138 and 140.
- Concerning expedited reorganization proceedings, the bracketed material in Recommendation 146(b) could very usefully be deleted, as such vote solicitation procedures are not likely to be well developed in many emerging markets.
- The significance is unclear of the requirement in Rec. 150 that notice of the commencement of expedited proceedings be given to creditors "individually." We would note, however, that expedited proceedings are increasingly being used not only with respect to banks and other easily identifiable creditors, but also to enable reorganizations involving debt held by bondholders. As such, it is important that the expedited proceedings not require individual notice by the insolvency representative to such widely dispersed creditors, but rather allow notice through the trustee or other arrangement contemplated under the terms of the bonds.
- In Recommendation 153, the first bracketed clause seems more appropriate, as it would simply allow reversion to original rights in the event of failure of an expedited plan. The second bracketed clause, calling for conversion to liquidation upon failure to implement a confirmed expedited plan, may have the effect of discouraging debtors from using expedited proceedings in the first place, thereby possibly delaying the stage at which debtors begin to address their financial difficulties.

3. **Glossary**

We continue to have the following concerns on the Glossary, which were noted in earlier comments on the Guide:

References to "Court"—Glossary para. 5 should include a nuance to the effect that alternatives to court involvement may be an option, *if such an alternative is permissible under the legal system of a country*. The point is that there are often *constitutional* limits under most legal systems on the extent to which the courts may be avoided entirely and replaced with administrative mechanisms. Consequently, even where administrative agencies are used, parties in these countries always retain a right ultimately to have their disputes heard by a *court*.

"Protection of the Value of Encumbered Assets"—This definition could very usefully be deleted, in light of the complexity of the subject; the alternative approaches possible (including protecting the value of a secured claim), which are not discussed in the Glossary; and the more detailed and clear discussion of the issue in Part II of the Guide.

"Secured debt"—The first bracketed definition (aggregate amount of secured claims) is more appropriate than the second (claims pertaining to secured creditors), although neither definition is entirely clear. The main point, recognized elsewhere in the Guide (and the contrary of what is stated in the second definition), is that the extent to which a claim is secured should depend on the *lesser* of the value of the secured creditors' claim or the value of the collateral security. It would thus be useful to clarify in the Glossary that a secured creditor's claim should be considered "secured debt" only up to the value of the collateral, as any other approach would give such a creditor a larger benefit than it has bargained for.

"Security interest"—The first sentence of the definition is not accurate, and could usefully be deleted. First (and as noted in the second sentence), a security interest need not be granted by a party, it can also be established involuntarily. Second, a security interest in itself does not "commit" a debtor to pay or perform its obligation; the commitment to pay/perform is established *in the underlying contract*, and the security interest simply gives the creditor certain rights in the event of non-fulfillment by a debtor of its obligation to pay/perform.

"Stay of proceedings"—In addition to actions concerning the debtor's rights, obligations and liabilities, it would seem that this definition should also cover *actions against the debtor*.

"Unsecured creditor"—Related to the comment under "secured debt" above, this definition could usefully clarify that unsecured creditor can include an otherwise secured creditor, to the extent that the value of its claim exceeds the value of the collateral.

4. **Institutional framework**

Related to the comment above concerning the definition of "court", para. 75 should clarify that even if the insolvency representative or other third party is given broad responsibility as a means of limiting the court's role, court involvement would still be necessary under most legal systems *once there is disagreement regarding a matter assigned to the insolvency representative*. This in turn further demonstrates the necessity of strengthening judicial capacity in jurisdictions where such capacity is weak. The current discussion could be misread to give the impression that courts can be avoided (and thus that capacity building can be postponed), which is not correct.

5. **Assets constituting the insolvency estate**

While we realize that the issue is discussed in greater detail elsewhere in the Guide, this section (in particular para. 160) could make clearer the point that adequate protection will need to be provided in all cases where encumbered assets are included in the estate. For example, the first sentence of para. 160 could note that where encumbered assets are included, they ***should*** (not just "may") be subject to certain protections. The last sentence of the paragraph should similarly add the point that an insolvency law *should specifically ensure the protection of the property rights of secured creditors in encumbered assets*.

The Commentary (para. 173) appropriately notes that there are differences among jurisdictions as to whether the time of constitution of the estate is set by reference to the date of commencement, application or some other event. However, the "purposes" clause of this section needs to be revised to reflect these alternatives, as the current draft refers only to assets included in the estate on *commencement* of proceedings).

6. **Protection and preservation of the insolvency estate**

This section concludes that an exception from the stay is appropriate where this is necessary to preserve a claim against the debtor (e.g., Rec. 35 and para. 182, 184. We do not disagree with the substance, but query whether the same result could not be achieved, without the complexity of an exception, simply by defining the stay so as to "toll" the running of the statute of limitations with respect to claims against the debtor. If there is no running of the statute of limitations, then a creditor's rights to bring a claim against the debtor should be the same on the day the stay is lifted as it was on the day the stay became effective. If tolling of the statute of limitations is in fact already included under the Guide's current concept of the stay, then the more general question is why an exception to "preserve a claim" against the debtor is necessary.

In discussing the technique of protecting the value of the secured portion of the claim, para. 215 could very usefully note that this approach involves far less complexities than the alternative approach of protecting the value of the encumbered asset, particularly since the former approach eliminates the need for the complex and ongoing valuation judgments associated with the latter. Indeed, while discussed very little in the Guide, this approach may well be the most appropriate one for most emerging market jurisdictions that lack the institutional framework necessary for ongoing complicated calculations of collateral value.

Other comments on preserving the estate:

- The bracketed clause in Rec. 38(b) should probably be deleted, as this concept would further complicate the determination by raising additional valuation issues.
- As parties other than the debtor can also be affected by an order for provisional measures, para. 199 should discuss notice requirements for *interested parties generally* (and not only for the debtor).
- A subheading ("*(ii) Liquidation*") seems to be missing immediately before the discussion beginning in para. 188.

7. **Use and disposal of assets**

Para. 237 indicates that any "benefits" conferred on the estate by the continued use of third party assets should be paid for by the estate as an administrative expense. Rather than the narrow and subjective focus on "benefits" to the estate, it would seem that *all* claims due to a third party for the continued use of its assets should be to treat as an administrative expense. Para. 237 could usefully be revised to include the latter concept.

In the last sentence in para. 220, the phrase "In particular" should probably be replaced with "*For example*".

8. **Treatment of Contracts**

The current discussion of ipso facto clauses focuses exclusively on ipso facto *termination* clauses. The Guide could also usefully address the approach among jurisdictions towards the nullification or acceptance of other kinds of ipso factor clauses (e.g., clauses calling for penalty interest and other special charges upon insolvency or certain other events indicative of insolvency).

Similar to the point made above under use and disposal of assets, the reference in para. 270 to treatment as an administrative expense of "benefits received" under a subsequently rejected contract should be revised to note instead that administrative expense treatment will be provided for any *payments falling due* in connection with such contracts in the period until they are rejected.

We agree fully that claims relating to the rejection of a long-term contract may be limited by the law (Rec. 68). The Commentary, however, seems to discuss this only as an issue for long-term *leases* (para. 285) and needs to be expanded in this regard. More generally, it would seem that the overall discussion of damages for rejection (para. 281, 282) could very usefully be expanded to sanction leeway for the law to limit damages in appropriate circumstances (e.g., not only for long-term contracts, but also in cases where the imposition of penalty interest and other kinds of default-related charges results in a much larger claim against the debtor than the original claim before calculation of these charges). The current statement that calculation of damages might be determined in accordance with applicable general law is not adequate, as it is unlikely that the general law will limit otherwise permissible damages simply to avoid overwhelming the claims of other creditors in an insolvency.

9. **Avoidance proceedings**

It remains unclear why "potential creditors" are included in the definition of "transactions intended to defeat, delay or hinder the ability of creditors to collect claims" (Rec. 73 and para. 314), particularly given that a key reason for avoidance provisions is to overturn transactions that upset the principle of equitable treatment of *actual creditors*. Notably, this seems to be the only category of avoidable transactions that is defined by reference to a group other than actual creditors. It would be useful to clarify in the Guide the basis for this special rule (as well as perhaps to note that that the problems of proof noted in the Guide are likely to exacerbated where the finding relates to intent vis-à-vis a "potential creditor"). If there is no particular basis for the language regarding potential creditors, then this language should probably be deleted to avoid confusion.

The category of transactions that may be used as a defense to avoidance (Rec. 82) seems unduly limited, as it does not include (a) transactions entered into pursuant to voluntary workout or even expedited reorganization proceedings, or (b) transactions entered into pursuant to reorganization (or expedited reorganization) proceedings that are not subsequently converted to liquidation.[5] These transactions could very usefully be included among those that constitute a defense to avoidance (or an explanation added as to why such inclusion would not be appropriate).

Finally, we would delete the brackets (and retain the relevant sentence) in Rec. 81.

10. **The Participants**

To avoid the inference that all insolvency representatives have such a role, the brackets in Rec. 95(c) could be removed and the currently bracketed phrase revised to read "where an insolvency representative is appointed *for such purposes*. . . "

11. **Treatment of Creditor Claims**

A key premise of this section, namely, that claims excluded from the insolvency proceedings are legally uncollectible (see, in particular, para. 571), is not necessarily correct. Rather, in a number of insolvency laws, recovery of certain claims that are not provable within the insolvency proceeding (e.g., secured claims or government tax claims) can be pursued outside and in parallel with the insolvency proceeding. As such, the discussion could very usefully distinguish between the alternative effects of: (i) extinguishing claims that are excluded from insolvency proceedings; and (ii) preserving alternative recourse for claims that are excluded from insolvency proceedings. For similar reasons, the discussion on failure to submit claims should explicitly state that it is dealing with the consequences of failure to submit claims that are required to be submitted in insolvency, and not dealing with those claims that can or must be enforced outside of insolvency.

12. **Priorities and Distribution**

In para. 631, we found curious the reference to the "need to give effect to international obligations" as a relevant consideration for according privileged status to debt owed by corporate or individual debtors. It would be very useful to explain the motivation behind this provision, particularly since the reference may otherwise be read as relating to international obligations of *sovereign debtors* (thereby leading to a misunderstanding that the Guide also provides guidance for sovereign insolvency issues).

13. **Discharge**

The Commentary discusses discharge of legal persons in reorganization proceedings, but this is not addressed in the Recommendations. This important issue should be dealt with in the Recommendations.

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[5] For its part, the Commentary (para. 329) identifies, as an avoidance defence, payments under both expedited reorganization proceedings or voluntary restructuring agreements, but it still limits the defence to cases in which liquidation proceedings are subsequently commenced.