CREDIT CONTROL JOURNAL and ASSET & RISK REVIEW is published by House of Words Media Limited.

The current issue and full text archive of this journal is available at **https://www.creditcontrol.co.uk/**

Analysis

Trade May Be Globalized, But Insolvency Regimes Are Not

Nick Hood

Nick Hood
Senior Business Advisor
Opus Business Advisory Group

Biography

Nick Hood is the Senior Business Adviser at the Opus Business Advisory Group (https://www.opusllp.com), the largest independent advisory, restructuring and insolvency firm in the UK.

Nick was a licensed Insolvency Practitioner, working in the business rescue market for 25 years. He is a committed internationalist, having created the largest global network of independent business rescue firms and having also worked overseas in Canada, Milan and Bahrain.

In his earlier career and after qualifying as a Chartered Accountant in 1970, Nick held senior executive positions in major companies in the construction, engineering and media sectors, as well as working for a boutique investment bank.

Nick's thought leadership and opinion blogs for Opus can be found at https://opusllp.com/resources/.

Keywords Insolvency, Restructuring, Harmonization, Insolvency Practitioners (IPs), Debt, Global, International, Cross-border, Business culture
Paper type Opinion

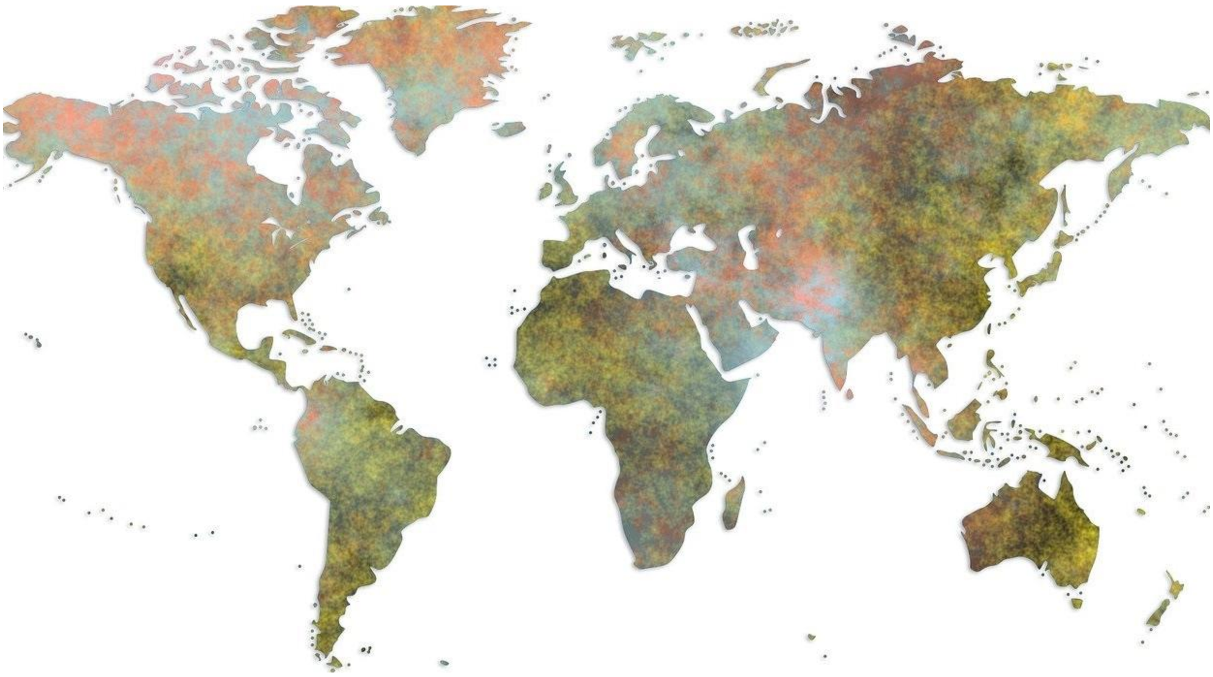
Abstract

The bewildering array of insolvency systems worldwide is little known in commercial circles but can be a potentially problematical inconvenience when issues raise their heads in foreign jurisdictions. In this article, the author analyses why these regimes have developed into such contrasting and confusing worlds in which to enforce debts and settle disputes.

Introduction

Trade has become ever more global in recent decades, much of it dominated by more and more powerful multinationals with bewilderingly complex corporate structures. This is generating increasing volumes of cross-border issues on debt recovery and fraud investigation, some of which need resolving through some form of restructuring or insolvency process. Unfortunately, very few of these disputes can be settled on a consensual basis or within one jurisdiction.

The more one delves into the world of international insolvency, the reality becomes clear. Insolvency regimes are like human fingerprints: no two are exactly alike and the differences can be not just stark, but sometimes completely incomprehensible and almost always deeply inconvenient for the parties involved.



The question is, why do insolvency frameworks vary so much around the globe?

The development of insolvency systems

Debt and debt relief processes are as old as civilization itself. In Ancient Greece, insolvent debtors and their families had to work off unpaid amounts through physical labour under a system of 'debt slavery'.

In Judaism, the Torah requires that every seventh year is decreed by Mosaic Law as a Sabbatical year, during which all debts owed by members of and within the Jewish community are forgiven. In Islamic teaching, according to the Quran, an insolvent person was deemed to be allowed time to be able to pay off their debt.

In mediaeval times, English canon law perhaps surprisingly included provisions to mitigate the harshness of debtor punishment. By contrast, in East Asia the law under Genghis Khan mandated the death penalty for anyone who became bankrupt three times.

In the late Middle Ages, England's first recognized piece of debt-related legislation was the Statute of Bankrupts Act 1542. The rapid development of commerce prompted by the industrial revolution led to a series of bankruptcy laws in the first half of the 19th century, culminating in the Bankruptcy Law Consolidation Act 1849 and eventually, the Bankruptcy Act 1869 which determined debt enforcement and debtor punishment right up to the introduction for the first comprehensive UK insolvency regime through the Insolvency Act 1986.

America was quicker off the mark with its own Bankruptcy Act 1800 but its modern debt resolution system there has its origins way back in the later Bankruptcy Act 1898.

CREDIT CONTROL JOURNAL and ASSET & RISK REVIEW is published by House of Words Media Limited.

The current issue and full text archive of this journal is available at **https://www.creditcontrol.co.uk/**

In Europe, a bankruptcy statute issued in Sienna in 1272 created a tradition of debt resolution leading through the French Ordonnance sur le Commerce of 1673, via the French commercial code of 1807 and on into modern times. But all around the Continent systems were evolving, each one with very distinct characteristics and often producing wildly differing financial outcomes for the various stakeholders from apparently similar circumstances.

Recent financial crises

Major economic events, whether they are local, regional or global tend to drive significant changes to insolvency regimes, stemming from the urgent need to remedy the pre-existing systemic flaws so brutally exposed by each crisis.

1. ***Asian financial crisis 1997 –*** Prompted by the collapse of the Thai currency in July 1997 in what was known as the Tom Yum Kung crisis, the contagion spread throughout East and South East Asia. Apart from the broadscale economic damage caused, the crisis highlighted a critical lack of effective insolvency processes right across the region.

   In some jurisdictions there wasn't even an accepted definition of insolvency and certainly not either the judicial or professional capacity to deal with the huge numbers of insolvent businesses that needed to be wound up. Fast track mass liquidation procedures had to be designed and implemented at breakneck speed, while restructuring and business rescue methods were invented where they were absent.

2. ***Global Financial Crisis 2008/9 –*** The Global Financial Crisis in 2008/9 differed from previous post-WW2 worldwide economic shocks by originating in the financial systems of countries, cutting off access to urgently needed rescue funding while those systems were stabilized.

CREDIT CONTROL JOURNAL and ASSET & RISK REVIEW is published by House of Words Media Limited.

The current issue and full text archive of this journal is available at **https://www.creditcontrol.co.uk/**

The failure of systemically critical global entities such as Lehman Brothers and Bear Stearns threatened to trigger the collapse of huge numbers of counter parties to the highly complex financial transactions in which they specialized. Even more challenging were the cross-border insolvency difficulties their demise caused, especially in jurisdictions whose insolvency systems had not kept pace with modern banking practice.

Innovative solutions had to be found through the ingenuity of insolvency professionals and the creativity of specialist insolvency judges in adapting existing insolvency legislation to meet the new scenarios for which they were never designed. The lessons learnt have changed insolvency practice in many jurisdictions and should make it less hard to deal with the next global crisis.

3. ***Coronavirus Pandemic 2019-2022*** – This was potentially the greatest commercial and financial disruption for nearly a century since the Wall Street Crash of 1929 and the Great Depression that followed it. The pandemic started out with what turned out to be misplaced hopes of a short duration and generated a near universal emphasis on preserving businesses as going concerns rather than seeing them perish unnecessarily. Globally, it caused the wholesale redesign of business rescue procedures or the introduction of them where they didn't exist, plus the imposition of significant constraints on creditor enforcement rights on a temporary basis.

Major influences on global insolvency regimes

In broad terms, a wide range of factors will determine the character and the financial or legal 'red lines' in any insolvency system:

- Local business culture and practice.
- Broader cultural issues – the more employee-friendly procedures in France, for example.
- Legal systems – for example, the different principles of common law as compared to civil law.

- Degree of judicial involvement – light touch supervision rather than a direct and proactive role
- Legal precedents – judicial decisions constantly adapt laws to reflect changing commercial conditions or to remedy errors left by poor legislative drafting.
- Professional leadership – accountants in charge in some countries, lawyers in others.

What hope is there of future harmonization?

The concept of harmonizing insolvency systems worldwide has long been an aspiration of the business rescue world and the academics, professionals and judges servicing it. Sadly, it has turned out to be more of a will of the wisp, to be chased endlessly but never quite caught. It has been broadly accepted that any satisfactory outcome could only ever be achieved on a strictly limited basis.

Even within an apparently coherent trading bloc like the European Union, the job of bringing the very different business cultures and practices across its 27 member nations within one all-embracing regime has proved to be extremely difficult. The degree of compromise needed is too vulnerable to attack by the powerful vested interests in each country's business and political communities.

In 2022, the European Commission published a draft directive harmonizing certain aspects of insolvency law with the aim of facilitating distressed Mergers & Acquisitions (M&A) and reducing legal uncertainties for investors in cross-border companies. The proposal is now going through the legislative process, but the limited objective of this initiative is to restrict creditor avoidance tactics deployed by unscrupulous corporate entities by harmonising law on this specific aspect across the European Union.

Implications of differing insolvency systems

Insolvency professionals thrive on uncertainty, but not generally as regards the laws governing their activities. Finding themselves dealing with other workout regimes with completely different triggers, processes and philosophies is an intimidating experience. Fortunately, insolvency practitioners are also deeply pragmatic and have demonstrated an extraordinary ability to work successfully cross-border despite facing apparently incompatible insolvency regimes.