

# CHILEAN LAW'S NEW DEBTOR REORGANIZATION SYSTEM

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## I. INTRODUCTION

Since obtaining its independence from Spain, Chile has passed several insolvency laws. Immediately after independence, the Spanish insolvency laws remained in effect. Nevertheless, the new State of Chile quickly started to enact its own laws. The first Chilean legislation that regulated some aspects of insolvency was the so-called “Leyes Marianas” of 1837.<sup>1</sup> However, the first law that contained a complete bankruptcy regulation was the Commercial Code of 1865 (Book IV, articles 1.325-1.533, applicable only to merchant debtor), which came into force on January 1, 1867.<sup>2</sup> Law Number 4.558 of 1929—which regulated the insolvency of all debtors rather than just the merchant debtor—repealed that law.<sup>3</sup> After that, Law Number 18.175 of 1982 ruled the insolvency

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<sup>1</sup> See RICARDO ANGUITA, LEYES PROMULGADAS EN CHILE DESDE 1810 HASTA EL 1° DE JUNIO DE 1913 285 (Vol. I 1913).

<sup>2</sup> See Chile’s original commercial code. CÓDIGO DE COMERCIO (CÓD COM.), BOOK IV, 1865, <http://www.leychile.cl/Navegar?idNorma=1974&tipoVersion=0>.

<sup>3</sup> See Law No. 4.558, April 1, 1929, Diario Oficial [D.O.] (Chile), <http://www.leychile.cl/Navegar?idNorma=1974&tipoVersion=0>.

of all debtors, thereby repealing Law Number 4.558. Law Number 18.175 was modified a number of times, including a return of insolvency law back to Book IV of the Commercial Code under Law Number 20.080 of 2005.<sup>4</sup> Finally, Law Number 20.720, which came into force on October 10, 2014,<sup>5</sup> repealed Book IV of the Commercial Code and became the only Chilean regulation of bankruptcy.

In practice, the bankruptcy system of Book IV of the Commercial Code<sup>6</sup> was not good enough. First, many companies solved their insolvency issues informally.<sup>7</sup> Second, when companies submitted to in-court insolvency proceedings, many of them preferred liquidation to reorganization.<sup>8</sup> Third, the recovery rate was very low<sup>9</sup> in comparison with developed countries.<sup>10</sup> Finally,

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leychile.cl/Navegar?idNorma=17474&idVersion=.

<sup>4</sup> See Chile's most recent commercial code. CÓDIGO DE COMERCIO (CÓD COM.), BOOK IV, 2014, <http://www.leychile.cl/Navegar?idNorma=1974&idVersion=2014-09-04> [hereinafter Cód COM. IV].

<sup>5</sup> Law No. 20.720, Octubre 10, 2014, Diario Oficial [D.O.] (Chile), <http://www.leychile.cl/Navegar?idNorma=1058072>. Law No. 20.720 was published in the Chilean Official Journal on January 9, 2014, but came into force on October 10, 2014.

<sup>6</sup> Cód. COM. IV. Book IV of the Commercial Code regulated two insolvency proceedings: liquidation and reorganization. In turn, there were two kinds of reorganization: one judicial and one non-judicial. Judicial reorganization plans could be approved in order to prevent bankruptcy or to lift bankruptcy. Non-judicial reorganization plans could be entered into by the debtor and its creditors in order to prevent bankruptcy.

<sup>7</sup> In the bill submitted to Congress, the President expressed that for every one insolvency solved in-court, there were 12 solved in an informal manner. See BIBLIOTECA DEL CONGRESO NACIONAL DE LA REPÚBLICA DE CHILE, HISTORIA DE LA LEY 20.720 11 (2014) <http://www.bcn.cl/historiadelay> (enter 20.720 in the search box (*buscador*)) [hereinafter BIBLIOTECA DEL CONGRESO].

<sup>8</sup> According to figures published by Superintendence of Insolvency and Re-entrepreneurship, in 2013 (the last entire year in which the prior law was in force) 142 liquidations were published and ten reorganization plans were approved and came into operation. In 2012, 128 liquidations were published and ten reorganization plans were approved and came into operation. See SUPERINTENDENCIA DE INSOLVENCIA Y REEMPREDIMIENTO, BOLETÍN ESTADÍSTICO: LIBRO IV DEL CÓDIGO DE COMERCIO, LEY NO. 18.175 (2015), [http://www.superir.gob.cl/wp-content/document/estadisticas/generales/Cifras\\_30.09.2015.pdf](http://www.superir.gob.cl/wp-content/document/estadisticas/generales/Cifras_30.09.2015.pdf) [hereinafter BOLETIN ESTADÍSTICO]. This situation can be explained because the prior legislation itself expressed preference for liquidation over reorganization. That perspective was founded on the historical circumstances in which Law Number 18.175 was enacted in 1982: in a critical financial crisis context, that law had to provide for a quick liquidation system of insolvent companies, leaving rehabilitation procedures in a secondary stage. See BIBLIOTECA DEL CONGRESO, *supra* note 7, at 8; NELSON CONTADOR ROSALES & CRISTIÁN PALACIOS VERGARA, PROCEDIMIENTOS CONCURSALES 1-4 (2015) [hereinafter CONTADOR ROSALES].

<sup>9</sup> The low recovery rate under prior law is related to the foresaid in the previous footnote: if there is not a satisfactory reorganization system and insolvency law is applied only during the last stages of the insolvency process, companies usually cannot already be rehabilitated, but they must be liquidated in an extreme financial situation. Then, liquidation results in low levels of satisfaction for creditors, employees, and the State.

the insolvency proceedings were too long.<sup>11</sup> Some of these problems were detected by the World Bank in a 2004 report on insolvency and creditor rights in Chile.<sup>12</sup> This situation induced a reflex in insolvency international rankings, where Chile had a poor performance under prior insolvency system.<sup>13</sup>

The solution to the foresaid problems and the necessity to harmonize Chilean insolvency Law with international standards were taken by the Chilean Government as relevant goals to enact Law Number 20.720.<sup>14</sup> Therefore, it is important to determine whether or not the Chilean State has reached its aim of passing an insolvency law according to recognized international standards that can contribute to harmonize insolvency law in an international context, and could contribute to eliminate or mitigate the problems detected under prior Chilean

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<sup>10</sup> According to the Doing Business Report 2015 (the most recent to provide information about the prior law), Chile had on average a recovery rate of 30%, which is low if it is compared with developed countries like Japan (92.9%), Finland (90.2%), the U.K. (88.6%), Canada (87.3%), Germany (83.4%), Korea (83.1%), the United States (80.4%), or France (77.2%). However, in this matter Chile was average in the Latin American context if its figures are compared with Venezuela (6.7%), Ecuador (17.9%), Paraguay (20.8%), Brazil (25.8%), Peru (28.5%), Argentina (28.6%), Bolivia (38.9%), Uruguay (44.2%), México (68.1%), and Colombia (72%). WORLD BANK GROUP, Doing Business 2015: Going Beyond Efficiency (2014) <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB15-Full-Report.pdf> [hereinafter Doing Business 2015].

<sup>11</sup> The average duration of liquidation proceedings in Chile was 24-36 months. WORLD BANK, Report on Observance of Standards & Codes: Chile 12 (2004) [hereinafter WORLD BANK 2004]. Likewise, Doing Business Report 2015 states that the average duration of insolvency proceedings in Chile was 3.2 years. That figure appears high if it is compared with developed countries (Japan, 0.6 years; Canada, 0.8 years; Finland, 0.9 years; the U.K., 1 year; Germany, 1.2 years; the United States, 1.5 years; Korea, 1.5 years; and France, 1.9 years), but was average in Latin America (Ecuador, 5.3 years; Venezuela, 4 years; Brazil, 4 years; Paraguay, 3.9 years; Peru, 3.1 years; Argentina, 2.8 years; Bolivia, 1.8 years; Uruguay, 1.8 years; México, 1.8 years; and Colombia, 1.7 years). Doing Business 2015, *supra* note 10. Notwithstanding, Puga Vial thinks that the diagnosis given by Doing Business Report is wrong because, according to him, most of bankruptcy proceedings under prior law lasted not more than one year to 18 months, and reorganization proceedings had a duration that was shorter than OECD countries. JUAN ESTABAN PUGA VIAL, DERECHO CONCURSAL: EL ACUERDO DE REORGANIZACIÓN 96 (4th ed. 2014) [hereinafter PUGA VIAL].

<sup>12</sup> WORLD BANK 2004, *supra* note 11, at 13-15. There the World Bank made some policy recommendations to enhance the Chilean insolvency legislation.

<sup>13</sup> According to Doing Business Report 2015 Chile was ranked 73rd among 189 countries measured. Doing Business 2015, *supra* note 10, at 178. This situation seems to have changed since the Law No. 20.720 came into force. In fact, the next edition of Doing Business report ranks Chile in 58th place among 189 countries measured. See WORLD BANK GROUP, Doing Business 2016: Measuring Regulatory Quality and Efficiency (2016) <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB16-Full-Report.pdf> at 194.

<sup>14</sup> These ideas were expressed in the Bill submitted by the President of Chile to the National Congress. See BIBLIOTECA DEL CONGRESO, *supra* note 7, at 7-10.

insolvency law.<sup>1516</sup> This is especially important in the matter of reorganization of companies because, unlike former legislation, Law Number 20.720 prefers reorganization to liquidation.<sup>17</sup> This Article compares Law Number 20.720's company reorganization system with instruments drafted by three main international institutions, namely, the World Bank,<sup>18</sup> UNCITRAL,<sup>19</sup> and the European Commission,<sup>20</sup> to verify that the new Chilean insolvency Law comports with the main aspects of an effective reorganization system of debtor.

<sup>15</sup> Figure 1.7 in the World Bank Group's report records the impact of the quality of insolvency Law (in concordance with international standards) on the recovery rate. *Doing Business 2015*, *supra* note 10, at 10.

<sup>16</sup> Cód. COM. IV. At this moment of the implementation of Law Number 20.720 we can only make a text comparison. By now it is not possible to determine whether or not the problems detected under prior Law have been eliminated or mitigated by the new Law. This matter must be object of empirical study after some years of implementation of the Law. Notwithstanding, it is interesting to note that having past only one year from the implementation of the Law No. 20.720, the Chilean figures seem to be enhancing in general, at least in *Doing Business* ranks. *See supra* note 13.

<sup>17</sup> This preference was announced in the bill submitted by President to the Congress. *See BIBLIOTECA DEL CONGRESO*, *supra* note 7, at 7, 12. *See also* CONTADOR ROSALES, *supra* note 8, at 53-4.

This preference is a basis for criticisms of Law Number 20.720. PUGA VIAL, *supra* note 11, at 10, 96. Puga Vial argues that neutrality is the best option. In fact, he states that reorganization plans agreed in the context of insolvency are rarely successful. Likewise, he considers that reorganization of viable businesses are generally out-of-court, because the insolvency procedure gives publicity to insolvency, aspect that causes damage to the debtor (because suppliers could suspend provisions and clients could look for more reliable commercial alternatives) and to the creditors (because their credits will depreciate). *Id.* In other respects, Vial writes that when a debtor initiates a reorganization proceeding, the debtor typically does not pursue a real rehabilitation, but rather sells deficient commercial units. *Id.* Apart from that, he states that under the prior law, the re-entrepreneurship was hindered by factors typically present in the Chilean credit market, not by the insolvency Law. *Id.*

Notwithstanding the foresaid legal preference, it must be observed that companies and legal practitioners seem to prefer liquidation procedures even under the new legislation. In fact, from October 9, 2014 to July 31, 2015, 52 applications for reorganization of companies and 315 applications for liquidation of companies have been submitted. *See SUPERINTENDENCIA DE INSOLVENCIA Y REEMPENDIMIENTO: BOLETÍN ESTADÍSTICO LEY 20.720 (9 de octubre de 2014 al 31 de julio de 2015)*, <http://www.superir.gob.cl/wp-content/document/estadisticas/ley20720/BOL-EST-201507.pdf> [hereinafter *BOLETÍN ESTADÍSTICO LEY 20.720*].

<sup>18</sup> WORLD BANK, *Principles for Effective Insolvency and Creditor Right Systems* (2005) <http://www.worldbank.org/ifa/FINAL-ICRPrinciples-March2009.pdf> [hereinafter *WORLD BANK 2005*].

<sup>19</sup> UNCITRAL, *LEGISLATIVE GUIDE ON INSOLVENCY LAW* (2005) [http://www.uncitral.org/pdf/english/texts/insolven/05-80722\\_Ebook.pdf](http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf) [hereinafter *LGIL*].

<sup>20</sup> European Commission, *Commission Recommendation of 12 March 2014 on a New Approach to Business Failure and Insolvency*, 57 O.J. EUR. UNION 65 (Mar. 14, 2014) [hereinafter *ECR*].

## II. GENERAL ASPECTS OF THE LAW NUMBER 20.720

Law Number 20.720 also regulates the two basic insolvency proceedings. But unlike former legislation, Law Number 20.720 contains different regulations depending on whether the debtor is a natural person or a company.<sup>21</sup> Thus, the new law regulates four insolvency proceedings: reorganization of companies, liquidation of companies, renegotiation (reorganization) of natural persons, and liquidation of a natural person's assets.

The law provides for four kinds of reorganization of companies: (1) A judicial reorganization proceeding, occurring before the commencement of liquidation process; (2) Non-judicial or simplified reorganization agreement in the same orientation;<sup>22</sup> (3) A judicial reorganization proceeding to terminate the liquidation process; and (4) Informal agreements reached between the debtor and one or more creditors, governed by general rules of contracts in the Civil Code.<sup>23</sup>

## III. INTERNATIONAL STANDARDS IN THE FIELD OF REORGANIZATION AND THE NEW CHILEAN LAW

### A. The Preference for Reorganization

Law Number 20.720's preference for reorganization is consistent with documents drafted by European Institutions,<sup>24</sup> but it cannot be said that the law followed the ECR because the publication of the former preceded the latter.<sup>25</sup>

On the other hand, UNCITRAL's Legislative Guide on Insolvency Law (LGIL) and the World Bank display no preference between liquidation and

<sup>21</sup> The legal definition of company includes some natural persons that offer professional services. Law No. 20.720, art. 2 No. 13.

<sup>22</sup> These are agreements reached between the debtor and a legal amount of creditors under some formalities and subject to court confirmation. Law No. 20.720, arts. 102-14.

<sup>23</sup> PUGA VIAL, *supra* note 11, at 441-55.

<sup>24</sup> ECR *supra* note 20; *see also, e.g.*, European Parliament Resolution of November 15, 2011 with Recommendations to the Commission on Insolvency Proceedings in the Context of EU Company Law (2011/2006 (INI)); Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, COM (2012) 573 final (Oct. 3 2012) (where the Commission undertook as a key action to "modernize EU insolvency rules to facilitate the survival of businesses and present a second chance for entrepreneurs"); Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee: A New European Approach to Business Failure and Insolvency, COM (2012) 742 final (Dec. 12 2012); Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Entrepreneurship 2020 Action Plan, COM (2012) 795 final (Jan. 9 2013).

<sup>25</sup> ECR was published on March 14, 2014. Although Law Number 20.720 was published on January 9, 2014, it came into force on October 10, 2014.

reorganization.<sup>26</sup> This neutrality does not involve an inconsistency between Law 20.720 and the mentioned instruments, because even though they do not prefer any of them, they recommend a balance between liquidation and reorganization,<sup>27</sup> which is present in Law Number 20.720.

This balance implies that reorganization should be applicable to viable companies and liquidation should be applicable to unviable companies.<sup>28</sup> Law Number 20.720 is aligned with this criterion because it does not require any express commencement standard for reorganization; an application for reorganization can be submitted in any stage of the company's insolvency when the company is still viable.<sup>29</sup> However, liquidation is subject to commencement standards that involve an advanced stage of insolvency.<sup>30</sup>

Likewise, the foresaid balance between reorganization and liquidation implies that there must be allowed the conversion of proceedings from one to another in appropriate circumstances.<sup>31</sup> Law Number 20.720 also meets this criterion because it states those conversions.<sup>32</sup>

In sum, even though Law 20.720 does not share the neutrality criterion given by the LGIL and World Bank, it follows their rules of balance between liquidation and reorganization.

### **B. Persons Permitted to Make an Application for Commencement of Reorganization Proceeding**

The LGIL<sup>33</sup> and the World Bank<sup>34</sup> recommend that an insolvency law should specify the persons permitted to make an application for commencement of

<sup>26</sup> UNCITRAL, *supra* note 19, at Recommendation 1, Recommendation 2, Part One.II, para. 22; WORLD BANK 2005, *supra* note 18, at, C.1.iii, C.1.iv.

<sup>27</sup> WORLD BANK 2005, *supra* note 18, at C.1.iv; LGIL, *supra* note 19, at Part One.I, paras. 5 and 6.

<sup>28</sup> WORLD BANK 2005, *supra* note 18, at C.1.iii; LGIL, *supra* note 19, at Part One.I, paras. 4, 18, 22.

<sup>29</sup> See PUGA VIAL, *supra* note 11, at 216 (arguing that the commencement standard for reorganization must be real a situation of insolvency, but not a simple restructuring of the debtor's liabilities).

<sup>30</sup> Article 117 provides the following commencement standards for liquidation: (a) Cessation of payment of one mercantile obligation evidenced in an executory instrument; (b) Existence of two or more executory instruments against the debtor and at least two execution proceedings initiated, in which the debtor has not offered assets enough to pay the debt; (c) Fleeing of debtor. Law No. 20.720 art. 117.

<sup>31</sup> WORLD BANK 2005, *supra* note 18, at C.1.iv; LGIL, *supra* note 19, at Part One.I, paras. 6, 22-24.

<sup>32</sup> Law Number 20.720 permits the conversion from reorganization to liquidation (see arts. 57 Nos. 4, 81, 88, 96, 100) and conversion from liquidation to reorganization (arts. 257-59). All these cases are mentioned bellow. See sections III.C, III.I, and III.J.

<sup>33</sup> LGIL, *supra* note 19, at Recommendation 14.

<sup>34</sup> WORLD BANK 2005, *supra* note 18, at C4.1.

insolvency proceedings, which should include the debtor and any of its creditors. Law Number 20.720 is at least partially aligned with this recommendation. It states that the debtor alone is entitled to apply for judicial reorganization proceeding<sup>35</sup> and judicial reorganization proceeding to terminate the liquidation process.<sup>36</sup> But, in the case of a simplified reorganization agreement or an informal agreement, there are no specific rules. The formation of these agreements is governed by the general rules of contracts, so either a debtor or a creditor can propose them.

### **C. General Features of Reorganization Proceedings**

According to both the LGIL and the World Bank, an effective insolvency proceeding should provide for timely, efficient, and impartial resolution of insolvency.<sup>37</sup> Likewise, the ECR states that the restructuring procedure should not be lengthy and costly, and it should be flexible so that more steps can be taken out-of-court.<sup>38</sup> Law Number 20.720 also contains procedural rules for a fast reorganization of a debtor. Judicial reorganization under Law Number 20.720 proceeds as follows:

- (1) The proceeding starts with debtor's application for commencement before a competent court.<sup>39</sup>
- (2) A copy of that application is sent to the Superintendence of Insolvency and Re-entrepreneurship, which nominates an insolvency representative and a substitute one and communicates the nomination to the court.<sup>40</sup>
- (3) Then the court pronounces the *reorganization sentence*, which designates the insolvency representative and his/her substitute. The sentence also rules on the following matters, among others: The beginning of the stay of individual enforcement actions (financial protection period); the implementation of provisional measures; the date, hour, and place in which the first creditors' meeting must take place;

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<sup>35</sup> Law No. 20.720 art. 54, ¶ 2.

<sup>36</sup> *Id.* art. 257.

<sup>37</sup> LGIL, *supra* note 19, at Recommendation No. 1; WORLD BANK 2005, *supra* note 18, at C1.(vi).

<sup>38</sup> ECR, *supra* note 20, at 68 ¶ 7.

<sup>39</sup> Law No. 20.720 art. 54. It must be mentioned that in large cities the insolvency proceedings must be preferentially assigned to judges with specialized insolvency expertise. *Id.* art. 3.

<sup>40</sup> *Id.* arts. 55, 22. Insolvency representatives must be professionals who need to prove knowledge in bankruptcy law. They are subject to periodical examinations and legal responsibility. *See id.* arts. 13-29.

- and the order to the debtor to submit to the court and publish the reorganization plan in the Insolvency Bulletin.<sup>41</sup>
- (4) Within eight days from publication of the reorganization sentence, creditors have to submit their claims to the court.<sup>42</sup> Creditors, the debtor, and the insolvency representative can then object to credits or priorities claimed. The court rules all the objections in an oral audience. Finally, the insolvency representative must publish in the Insolvency Bulletin the list of admitted credits before the creditors' meeting take place.<sup>43</sup>
  - (5) The reorganization plan must be submitted to the court and published in the Insolvency Bulletin at least ten days before the creditors' meeting. If the debtor does not submit the plan, the court must order liquidation.<sup>44</sup>
  - (6) The creditors' meeting must take place the day in which the period of "financial protection" ends.<sup>45</sup> In that meeting, only creditors whose credits have been admitted are entitled to vote.<sup>46</sup> Creditors qualified by law as related to the debtor cannot vote.<sup>47</sup> The plan must be approved by the debtor,<sup>48</sup> and by at least two thirds of the attending creditors that represent at least two thirds of debtor liabilities.<sup>49</sup> Creditors may vote out-of-meeting.<sup>50</sup> If the plan is not approved, the court must order liquidation.<sup>51</sup>

In the case of non-judicial or simplified reorganization proceedings, the process is:

- (1) The simplified reorganization agreement must be entered into before a certifying officer.<sup>52</sup> It must be signed by the

<sup>41</sup> *Id.* art. 57. See THE INSOLVENCY BULLETIN, <http://www.boletinconcursal.cl/boletin/procedimientos> (last visited Jan. 19, 2016). The Insolvency Bulletin is a free electronic platform in charge of Superintendence of Insolvency and Re-entrepreneurship. Publication in this platform is the main form of notification during the proceeding.

<sup>42</sup> This formality can be omitted if creditor finds that its credit is correctly described in the documents submitted by the debtor. Law No. 20.720 art. 70 ¶ 1.

<sup>43</sup> *Id.* arts. 70, 71.

<sup>44</sup> *Id.* art. 57 No. 4.

<sup>45</sup> *Id.* art. 57 No. 5.

<sup>46</sup> *Id.* art. 78.

<sup>47</sup> Law No. 20.720 art. 79 ¶ 3.

<sup>48</sup> If the debtor does not attend the meeting, the court must order liquidation. *Id.* art. 81.

<sup>49</sup> *Id.* art. 79 ¶ 2.

<sup>50</sup> *Id.* art. 80. Creditors are permitted to vote by signing a document before a certifying officer or sending their votes in electronic documents signed through electronic signature.

<sup>51</sup> *Id.* art. 96.

<sup>52</sup> Law No. 20.720 art. 104.



- debtor and two or more creditors that represent at least three fourth of debtor liabilities. Creditors qualified by law as related to the debtor cannot sign this kind of agreement.<sup>53</sup>
- (2) The court must confirm the simplified reorganization agreement in order for it to become binding.<sup>54</sup> This confirmation is made through a very simple procedure.<sup>55</sup> Dissident and excluded creditors are entitled to object the draft agreement.<sup>56</sup> Once the court rules on proffered objections, or the term to object without objections submitted expires, the court must confirm the simplified reorganization agreement so long as the legal requirements are fulfilled. The insolvency representative must publish the sentence in the Insolvency Bulletin.<sup>57</sup>

In the case of judicial reorganization proceeding to terminate the liquidation process, the procedures are summarized by the following:

- (1) Once notified of the list of credits admitted in the liquidation process, the debtor can submit to the court a draft agreement of reorganization that must be published in the Insolvency Bulletin. Then the Court must state the date, hour, and place in which the creditors' meeting shall take place.<sup>58</sup>
- (2) The plan must be approved by the debtor and at least two thirds of the attending creditors that represent three fourth of debtor liabilities. Creditors qualified by law as related to the debtor cannot vote.<sup>59</sup> If the plan is approved, the court must declare the end of the liquidation procedure.<sup>60</sup>

Finally, informal agreements reached between the debtor and one or more creditors are governed by general rules of contracts set out in the Civil Code and they are not the object of procedural rules.

After this brief description of reorganization procedures under the new Chilean Law, it can be said that Law 20.720 is generally coherent with international standards. Examples of its consistency include the role the court must play,<sup>61</sup> approval of the plan under majority vote, respect for the legal rules

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<sup>53</sup> *Id.* art. 109.

<sup>54</sup> *Id.* art. 102.

<sup>55</sup> *Id.* arts. 107, 110.

<sup>56</sup> *Id.* art. 111.

<sup>57</sup> Law No. 20.720 art. 112.

<sup>58</sup> *Id.* art. 257.

<sup>59</sup> *Id.* art. 258.

<sup>60</sup> *Id.* art. 259.

<sup>61</sup> WORLD BANK 2005, *supra* note 18, at D1; ECR, *supra* note 20, at 68 ¶ 7.

and fairness among creditors,<sup>62</sup> qualification and role of the insolvency administrator,<sup>63</sup> creditors' rights,<sup>64</sup> voting mechanism,<sup>65</sup> conversion to liquidation process,<sup>66</sup> submission of claims, objections, and effects of admission of claims.<sup>67</sup>

#### **D. Legal Requirements of Reorganization Plan**

In this matter, international texts recommend minimum contents of reorganization plan,<sup>68</sup> or giving a general rule of flexibility.<sup>69</sup> According to the latter criterion, Law Number 20.720 contains a flexible rule stating that the draft reorganization plan may cover any matter with the aim to restructure assets and liabilities of the debtor.<sup>70</sup>

The LGIL, World Bank, and ECR also recommend that the reorganization plan be able to set diverse effects for different categories of creditors, who are classified according to their particular rights.<sup>71</sup> Law Number 20.720 provides for this. It requires that each class of creditors vote separately and that all creditors of the same class be offered the same treatment, unless creditors of that class agree otherwise.<sup>72</sup>

#### **E. Stay of Individual Enforcement and Provisional Measures**

The LGIL, World Bank, and ECR all recommend that commencement of a reorganization proceeding should suspend the commencement or continuation of actions by creditors to enforce their rights against the debtor. Further, those three authorities believe that this stay should be limited to a specified duration in order to strike a proper balance between creditor protection and insolvency proceeding

<sup>62</sup> WORLD BANK 2005, *supra* note 18, at C14.3; LGIL, *supra* note 19, at Recommendation 152; ECR, *supra* note 20, at 68-69 ¶¶ 15, 18, 21, 22.

<sup>63</sup> WORLD BANK 2005, *supra* note 18, at C6.2 and D8; LGIL, *supra* note 19, Recommendations 115-25.

<sup>64</sup> WORLD BANK 2005, *supra* note 18, at C2.1; LGIL, *supra* note 19, Recommendations 24, 126-30, 137; ECR, *supra* note 20, at 69 ¶ 24.

<sup>65</sup> LGIL, *supra* note 19, Recommendations 145, 149; ECR, *supra* note 20, at 69 ¶ 19.

<sup>66</sup> WORLD BANK 2005, *supra* note 18, at C14.3; LGIL, *supra* note 19, Recommendation 158.

<sup>67</sup> WORLD BANK 2005, *supra* note 18, at C13; LGIL, *supra* note 19, Recommendations 169-84.

<sup>68</sup> LGIL, *supra* note 19, Recommendation 144; ECR, *supra* note 20, at 68 ¶ 15.

<sup>69</sup> WORLD BANK 2005, *supra* note 18, at C14.2.

<sup>70</sup> Law No. 20.720 art. 60.

<sup>71</sup> WORLD BANK 2005, *supra* note 18, at C14.3; LGIL, *supra* note 19, Recommendations 148-51; ECR, *supra* note 20, at 68 ¶ 17.

<sup>72</sup> Law No. 20.720 arts. 61-64, 79.

objectives.<sup>73</sup> Finally, the World Bank and LGIL also recommend regulation of provisional measures.<sup>74</sup>

Law Number 20.720 follows suit. Its stay of individual enforcement is called the “financial protection period.” The financial protection period includes the suspension and prohibition of liquidation, individual execution, restitution, anticipatory avoidance of contract, enforcement of contract, and enforcement of collaterals proceedings, with some exceptions. This protection lasts 30 days from notice of the reorganization sentence and can be extended if the debtor has support from a legal quorum of creditors. Creditors deemed related to the debtor are not considered support.<sup>75</sup> A similar protection is given to the debtor applying to non-judicial or simplified reorganization proceeding.<sup>76</sup>

Provisional measures are also an automatic effect of the reorganization sentence, and they last the same time as the financial protection period. During this period: (1) the administration of a debtor's business is entrusted to an insolvency representative; (2) a debtor's right to transfer or encumber its assets is suspended unless the operation is proper to its activity or it is necessary for its business; and (3) if the debtor is a legal entity, its articles of association cannot be modified.<sup>77</sup>

#### **F. Creditors Bound by Reorganization Plan**

The World Bank suggests that a plan approved by majority should bind all creditors, including dissenting minorities.<sup>78</sup> LGIL recommends that creditors or equity holders whose rights are modified or affected by the plan should not be bound to the terms of the plan unless they have had an opportunity to vote on the plan.<sup>79</sup> Finally, the ECR contains three recommendations: (1) a plan adopted pursuant to national law should be binding on all creditors, provided that a court confirms the plan; (2) a plan that all affected creditors unanimously adopt should bind those creditors; and (3) a plan that a court confirms should be binding on each affected and identified creditor.<sup>80</sup>

Law Number 20.720 states that the plan is binding to the debtor and all creditors of each category, whether or not they attended the creditors' meeting at which it was approved.<sup>81</sup> But, the reorganization agreement affects only credits

<sup>73</sup> WORLD BANK 2005, *supra* note 18, at C5.2 and C5.3; LGIL, *supra* note 19, Recommendations 46-49; ECR, *supra* note 20, at 67-68 ¶¶ 6(c), 10-14.

<sup>74</sup> WORLD BANK 2005, *supra* note 18, at C5.1; LGIL, *supra* note 19, Recommendations 39-45.

<sup>75</sup> Law No. 20.720 arts. 57 No. 1, 58.

<sup>76</sup> *Id.* art. 108.

<sup>77</sup> *Id.* art. 57 No. 2.

<sup>78</sup> WORLD BANK 2005, *supra* note 18, at C14.5.

<sup>79</sup> LGIL, *supra* note 19, Recommendation 146.

<sup>80</sup> ECR, *supra* note 20, at 67, 69 ¶¶ 6(d), 25, 26.

<sup>81</sup> Law No. 20.720 art. 91. This rule is also applicable to simplified reorganization

that originated before the reorganization sentence.<sup>82</sup> These rules fit in with the World Bank, LGIL, and ECR because in all the reorganization proceedings ruled by Law Number 20.720 creditors are notified of the commencement of the process, and all of them are entitled to vote (except those related to the debtor) in the context of proceedings overseen by an independent court.

### **G. Supervision of Implementation**

International standards suggest that implementation of the plan should be independently supervised.<sup>83</sup> Accordingly, Law Number 20.720 provides for supervision by insolvency representative or by a creditors' committee.<sup>84</sup>

### **H. Modification of Reorganization Plan**

International standards also recommend permitting amendments of the reorganization plan and establishing a mechanism for approval of amendments that gives guaranties to affected parties.<sup>85</sup> Law Number 20.720 also permits plan modification as long as creditors approve the modification under legal quorum.<sup>86</sup>

### **I. Legal Challenges of Reorganization Plan**

The World Bank and LGIL recommend that an insolvency law should permit a confirmed plan to be legally challenged on the basis of fraud. The latter states that the law should specify a time limit for bringing such a challenge as calculated by reference to the time the fraud is discovered, the party who may bring such a challenge, and that the challenge should be heard by the court.<sup>87</sup>

Law Number 20.720 contains specific causes of action to challenge the plan: procedural mistakes, fraud, or illegal contents of the reorganization plan.<sup>88</sup> The law gives five days from the publication of the reorganization plan agreement

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proceeding (art.113) and to reorganization plan to terminate the liquidation process (art. 257).

<sup>82</sup> *Id.* art. 66.

<sup>83</sup> WORLD BANK 2005, *supra* note 18, at C14.4; LGIL, *supra* note 19, Recommendation 157.

<sup>84</sup> Law No. 20.720 art. 69.

<sup>85</sup> WORLD BANK 2005, *supra* note 18, at C14.4; LGIL, *supra* note 19, Recommendations 155-56.

<sup>86</sup> Law No. 20.720 art. 83.

<sup>87</sup> WORLD BANK 2005, *supra* note 18, at C14.6; LGIL, *supra* note 19, Recommendation 154.

<sup>88</sup> Law No. 20.720 art. 85.

in the Insolvency Bulletin to submit such a claim.<sup>89</sup> A court must rule on each challenge orally before an audience.<sup>90</sup> In some cases, the court's ruling obliges the debtor to submit a new draft reorganization plan.<sup>91</sup> But if the plan is invalidated because of fraud the court must order liquidation.<sup>92</sup> The law also permits nullifying the reorganization agreement based on fraud if the interested party discovered the fraud after the challenge term.<sup>93</sup> The application for nullity is subject to the same procedural rules as breach of the reorganization plan.

#### **J. Breach of the Reorganization Plan**

Finally, international standards suggest that a court should be able to convert a reorganization proceeding to liquidation upon the debtor's substantial breach of the terms of the plan.<sup>94</sup> According to this recommendation, Law Number 20.720 states that a court can declare a breach of the reorganization agreement if any affected creditor claims a specific breach, or if the debtor's financial situation becomes so imperiled as to make creditors afraid of damage.<sup>95</sup> This proceeding is subject to a summary procedure.<sup>96</sup> When the court declares a breach, the reorganization agreement becomes invalid and the court must pronounce the liquidation sentence.<sup>97</sup>

### **IV. CONCLUSION**

One of the goals of the Chilean Government in enacting Law Number 20.720 was passing an insolvency law consistent with international standards that could contribute to solving the problems detected under the prior legislation. Law Number 20.720 reasonably achieved that goal through its coherence with the standards of insolvency law drafted by the World Bank, UNCITRAL, and the European Commission.

In most cases, the coherence is given with the LGIL and World Bank. In the vast majority of cases, this coherence is total or nearly total with both of them, taking into account the differences among the standards themselves,<sup>98</sup> but in

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<sup>89</sup> *Id.* art. 86.

<sup>90</sup> *Id.* art. 87.

<sup>91</sup> If the debtor fails to submit a new draft, the court must order liquidation.

<sup>92</sup> Law No. 20.720 art 88.

<sup>93</sup> *Id.* art. 97.

<sup>94</sup> WORLD BANK 2005, *supra* note 18, at C14.4; LGIL, *supra* note 19, Recommendations 158, 159.

<sup>95</sup> Law No. 20.720 art. 98.

<sup>96</sup> *Id.* art. 99.

<sup>97</sup> *Id.* art. 100.

<sup>98</sup> This happens in the regulation of the following issues under Law Number 20.720: balance between liquidation and reorganization; qualification and role of the insolvency

another case the coherence is partial with each of them.<sup>99</sup> Finally, there are some cases in which there is coincidence with only one of the aforementioned instruments. This situation appears when an issue is not explicitly addressed by one of them<sup>100</sup> and when the LGIL and World Bank have different recommendations for the same issue.<sup>101</sup>

On the other hand, it cannot be said that Law 20.720 followed ERC because the publication of the former was prior to the latter's publication. However, in many cases the ERC's criteria coincide with rules of Law Number 20.720.<sup>102</sup> That coincidence confirms that Law Number 20.720 fits international standards and recognized good practices in the field of reorganization.




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administrator; creditors' rights during the process; submission of claims, objections and effects of admission of claims; regulation of diverse effects for different categories of creditors; stay of individual enforcement; regulation of provisional measures; creditors bound by the reorganization plan; supervision of implementation of the plan; modification of the plan; legal challenge of the plan; and breach of the plan.

<sup>99</sup> This is the case of the regulation of persons permitted to make an application for commencement of reorganization under Law Number 20.720.

<sup>100</sup> This is the case of the regulation of the voting mechanism, which is regulated by LGIL but not by the World Bank.

<sup>101</sup> This is the case of the regulation of legal requirements of reorganization plan, matter in which Law Number 20.720 follows the World Bank's recommendation instead of LGIL's.

<sup>102</sup> This happens in the regulation of the following issues under Law Number 20.720: the role of the court in reorganization, creditors' rights, voting mechanism, regulation of diverse effects for different categories of creditors, stay of individual enforcement, and creditors bound by the reorganization plan.