

# Toward Universalism In International Bankruptcy Law: Foundations For Strategy Formulation In Selected Countries<sup>1</sup>

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## Abstract

*Two major impacts of globalization have been the dramatic increase in the number of multinational corporations that now exist and the wave of international bankruptcy law reform now taking place. Multinational corporations are widening their search for new strategic opportunities and are venturing into new countries, cultures, and geographic markets in this pursuit. As a result of the reform movement, bankruptcy laws in various countries are becoming more similar, are providing documentation that the Universalism Model is a pragmatic vehicle for resolving multinational bankruptcies, and are indirectly generating increased strategic opportunities for multinational corporations.*

*This paper comprises 1) a brief summary of globalization and its impact on the creation of multinational corporations; 2) a brief summary of the Territorial Model and the Universalism Model of international bankruptcy law; 3) a general discussion and comparison of bankruptcy laws in selected Latin American countries; 4) a discussion of the strategic implications of these countries' bankruptcy laws; and 5) general conclusions regarding the strategic significance of global bankruptcy reform and Universalism.*

## 1.0 Introduction

**G**lobalization may be defined as a progression away from a world in which national economies were isolated from each other by barriers to cross-border trade and investment, distance, time zones, language, culture, government regulation, and differences in business systems and toward a world in which national economies are merging into a single interdependent global economic system (Hill, 2001). The globalization movement has two main components: globalization of markets and globalization of production. Globalization of markets suggests that the boundaries of national markets are breaking down and a single huge market place is emerging. The globalization of production has to do with locating production facilities in optimal world locations.

## 2.0 Inputs and Outcomes of Globalization

Declining trade barriers and dramatic increases in technology of several types underlie the globalization movement. Lowered trade barriers have produced freer flows of goods, services, and capital investment, while the development of new technology in telecommunications, information processing, and transportation has enabled firms to achieve tight coordination of operations both domestic and in foreign locations (Hill, 2001).

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<sup>1</sup> Much of the information on the selected countries in this paper was gleaned from translated materials. The translators use a certain amount of discretion when translating terms used in these various legal systems that may not have precise equivalents in the U.S. system.

Globalization of markets and globalization of production have led business executives all over the world to increasingly view the world as a single market. Consequently, a number of dramatic changes in the profile of international business have occurred. By the last decade of the twentieth century, the U.S. share of world output had been reduced by 50% and the U.S. share of worldwide foreign direct investment had fallen by approximately 67% (Hill, 2001). Major shares of world output were being attributed to Western European and Southeast Asian economies, and a large number of Japanese and European multinationals emerged. Put in more general terms, globalization of markets and production has accelerated world trade growth, elevated foreign direct investment, and produced more intense competitive pressures in many industries. Additionally, the number of multinational firms is proliferating geometrically as more and more firms are positioned to exploit the opportunities for growth, profit, and market share that globalization seems to promise. With more and more multinational companies seeking shares in the emerging global market, competitive pressures are intensifying and multinational corporations are widening their search for new strategic opportunities with ventures into new countries, cultures, and geographic markets. These new ventures into unfamiliar strategic environments combined with the large increase in the sheer number of multinational companies have resulted in a dramatic increase in the numbers of international company insolvencies and have brought attention to the question of how to deal with transnational bankruptcies. The attention and accompanying debate have to date occurred mainly within the community of legal scholars and the ramifications that these debates hold for business strategists are only now beginning to be recognized as scholars evaluate the strategy implications of this development (Brewerton and LeMaster, 2002).

### **3.0 Emerging Issues**

Two related issues have emerged: (1) the increased necessity for a multinational company to systematically develop contingency strategies in the event that its primary strategy fails and the company becomes insolvent; and (2) the increased need for a uniform bankruptcy law and court system for resolving international business insolvencies. In regards to the first issue, no company ever intentionally pursues a strategic goal culminating in bankruptcy. Companies ordinarily pursue strategies designed to achieve long term goals of profitability market share, growth, or other similar accomplishments. When strategies for achieving these goals fail, multinational companies may find themselves scrambling to minimize the effects of an insolvency that has completely escaped strategic consideration. Ideally, in the event of insolvency and bankruptcy, multinational company strategists will have already determined what bankruptcy law, court, and actions are optimal, and which countries' bankruptcy laws and court system minimize the negative impact of the insolvency as a contingency plan or strategy. There is little in the strategy literature that suggests that multinational company strategists are devoting much attention to the formulation of bankruptcy contingency strategy.

The second emerging issue – the need for a more standardized bankruptcy law and uniform court system for adjudicating transnational insolvencies – is being fueled by debates within the community of legal scholars that center on the determination of the optimal legal solution for resolving international defaults. Guzman (2000) concludes that there are two polar approaches to the adjudication of international insolvencies. These include the “territorialism” model and the “universalism” model. A brief summary of each model follows.

### **4.0 The Territorial Model of Bankruptcy Law**

Territoriality is the idea that each country has the exclusive right to govern within its own borders and as such a basic principle of international law that it is simply accepted as a given or even overlooked. It is the default rule in every substantive area of law including constitutional law, taxation, trademarks, industrial regulation, debt collection and bankruptcy (LoPucki, 2000). In applications of bankruptcy law to multinational companies, territoriality or territorialism means that the bankruptcy courts of a country have jurisdiction over those portions of the company that are within its borders (only) and not those portions that are outside them (LoPucki 2000). Unless there are treaties or other binding conventions to the contrary, countries can only enforce their laws against assets or persons within their own borders. Currently, such treaties or conventions are virtually non-existent and consequently territoriality or territorialism is the international law of bankruptcy today.

If the multinational firm's financial problems are confined to its entities in a single country, the troubled entity or entities either liquidate or reorganize in that country and the multinational's other foreign entities are unaffected. The situation is even simpler in the case of non-multinationals with assets and operations confined entirely to a single country. In this simplest case the company would be liquidated or reorganized under the bankruptcy law provisions of the country in which it resides.

When a multinational company's financial difficulties extend across borders, each financially distressed entity files for bankruptcy in each country in which it has significant assets. The effect is to create at least one bankruptcy estate in each country in which significant assets are held. Ideally, in a territorial system the necessary international cooperation takes place in each case. That is, "parallel" bankruptcy proceedings are initiated in each country, and each court appoints a representative for the estate of each entity filing bankruptcy in its jurisdiction. The appointed representatives then negotiate a court-approved solution to the debtor's financial problems that may involve cooperation across international borders. If the estates are worth more in combination than they are separately it will be in the interests of the representatives to combine them. Should the negotiators not reach an agreement the assets in each country would be reorganized or liquidated and the proceeds distributed in accordance with the priority rules of each respective country.

### **5.0 The Universalism Model of Bankruptcy Law**

Universalism in its purest form involves the administration of multinational insolvencies by a court applying a single bankruptcy law within the debtor's home country. The two strongest proponents of universalism are Westbrook (2000) and Guzman (2000). The concept of universalism as a pragmatic vehicle for resolving multinational bankruptcies is itself complex and is predicated on numerous assumed conditions about the real world.

Westbrook (2000) concludes that there are two elements necessary to a universalism convention for international bankruptcy. These include a single bankruptcy law and a single forum (court and/or court system) to govern each multinational case. A single international bankruptcy law would create a single set of priorities and method of distribution (of assets) thus ensuring equality for all stakeholders with similar legal rights everywhere in the world. Further, a single law would provide a single consistent set of transfer-avoidance rules that protect all creditors against strategic behavior by debtors and other creditors (Westbrook, 2000).

Similar benefits derive from a single international system of bankruptcy courts. Among other benefits, a single court system applying a single bankruptcy law could reasonably be expected to produce a more consistent set of bankruptcy outcomes with an accompanying high level of predictability. If there were but a single international bankruptcy court (as contrasted to a unified court system), an even higher degree of uniformity, consistency, and predictability would likely be possible. A single court would provide a unified approach to assembly and sale of assets, could more effectively protect those assets prior to sale, and would make prevention or reversal of debtor fraud easier and more certain. This is a particularly urgent need in a world of electronic funds transfer, asset protection trusts, and other devices currently being used to accomplish debtor fraud.

For Universalism to function there must be symmetry between the law and the market in which it operates. This condition requires that the law be capable of covering all or nearly all transactions and stakeholders in the market with respect to the legal rights and duties embraced by the system. Beyond symmetry between the law and the market, universalism also suggests that there must be convergence of other laws governing creditors' priority, setoff, security interests, debt collection and other related concepts. The primary objection to universalism as a workable solution to international bankruptcy is political in nature; therefore Universalism is unlikely to be achievable in the foreseeable future (Westbrook, 2000). But Westbrook (2000) also argues that the linking mechanism that brings about symmetry and convergence of related laws is the emergence of the global market, citing initiatives from the International Monetary Fund and the World Bank; recently rewritten bankruptcy laws in Germany, Argentina, Australia, Canada, Japan, Russia, China, and most of Eastern Europe; the emergence of new bankruptcy laws in Singapore, Indonesia, and Thailand; additional ongoing bankruptcy reform efforts in Japan, Great Britain, and Mexico; the promulgation of a Model Law on Cross Border Insolvency by the United Nations Commission on International Trade Laws (UNITRAL); and initiatives within the European Union and NAFTA countries that provide for closer

coordination of transnational bankruptcy procedures. The revisions, changes, and initiatives cited above are all based on extensive examinations and analyses of other countries' bankruptcy laws and reform proposals (Westbrook, 2000).

## **6.0 Bankruptcy Laws in Latin American Countries**

Most of Westbrook's (2000) citations of bankruptcy reform are in Eastern and Western European Countries, North America, and Asian countries. The only country in South America that was mentioned was Argentina, and no Central American Country was cited. This paper examines the extent to which bankruptcy laws are converging in seven Latin American countries by examining basic bankruptcy law provisions for comparability. A brief summary of bankruptcy law features contained each country's law follows.

### **6.1 Mexico**

Mexico does not have a Chapter 11 type of bankruptcy provision. As a matter of fact, "[u]nder the 1943 bankruptcy law, business owners...[were] actively encouraged to suspend payments to creditors for years" (The Economist Intelligence Unit, November 29, 1999) and under the 1943 law, few companies ever actually reached bankruptcy; "they simply declared themselves in 'suspension of payments' indefinitely" (The Economist Intelligence Unit, November 29, 1999). Mexico is one of the countries that distinguish between commercial/trade laws and civil laws, and finally, in May 2000, Mexico enacted a new law on commercial insolvency. A comment made by one of the Supreme Court Judges when the members of the newly created Directive Board of the Federal Institute of Specialists in Commercial Concursos (IFEECM) were installed was that "Mexico has passed from a protectionist economy to a market oriented economy. Today Mexico experiences socio-economic conditions that are radically different from the decade of the forties. Today Mexico has a different way of doing business and a new form of resolving its commercial disputes." (Inter-American Trade Report, July 31, 2000, p.1839).

The extensive abuse and misapplication of the Law on Bankruptcy and Suspension of Payments (LQSP) in Mexico required a fundamental change in the law. The law was actually theoretically sound, but in reality it simply could not work because of the suspension of payments (SOPP) aspect of the law. The purpose of the SOPP was to provide for renegotiation between the debtor and his creditors. Because the provisions of the law were so imprecise and uncertain delaying tactics were the norm. Once a petition was filed, results would include: a prolonged period of time to resolution (as long as 10 years), any interest on the debts ceased accruing during this time, the moment the process was put into place, all debts were converted to peso denominations suffering the consequences of inflation or deflation. It was an untenable situation described as at best to be: "a radically reduced recovery...that would have to be worked out with a debtor..." and at worst to be: "the complete loss of value of the credit over time..." (Inter-American Trade Report, July 31, 2000, p.1840).

The new law provides for an initial conciliation period of 180 days with provision for extensions up to 360 calendar days. If no agreement can be reached within this maximum period then the entity is declared bankrupt with the purpose to sell off the assets as quickly as possible and pay the creditors. "The bankruptcy may be terminated by (i) payment, (ii) lack of sufficient assets to be sold, and (iii) agreement between the debtor and his or her creditors" (Inter-American Trade Report, July 31, 2000, p.1843). There are provisions in the new law for criminal conduct, or for international cooperation.

### **6.2 Venezuela**

The commercial code in Venezuela provides for 3 types of bankruptcy. *Fortuitous* bankruptcy results from some event that requires cessation of payments to creditors and the inability to continue the business. *Guilty* bankruptcy is the result of negligence, and *fraudulent* bankruptcy provides for willful misconduct. The date a company stops payments cannot be more than 2 years after the court makes its decision regarding the outcomes of the cessation of payment. This is an important concern since any gratuitous or onerous acts that have taken place within 2 years and 10 days prior to declaring bankruptcy become null and void.

In Venezuela, bankruptcy is required when a firm loses two thirds of its capital stock. At the point where the firm has lost one third of its capital stock, the shareholders must meet and decide if the company will “continue operations by reimbursing the capital, reduce it to the existing amount or liquidate the company” (<http://natlaw.com/pubs/spvegal.htm>) and ultimately, the shareholders will decide whether to continue or not to continue the operations of the company. Additionally, managers of a company that has losses up to two thirds of capital stock who have not called a meeting of the stockholders can be held criminally liable.

As in the case of Mexico, Venezuela provides for a “conciliatory-like” period before bankruptcy is filed that is referred to as a moratorium. Moratoriums can be granted for one year, which is most common, with a possible extension of one additional year. Clearly, the purpose is to allow for recovery or for a friendly liquidation of the assets of the firm.

### **6.3 Panama**

Panama allows for dissolution, insolvency, and bankruptcy. These actions are provided for under the Commercial Code of the country including bilateral contracts. Unlike Venezuela, Panama allows for dissolution of an entity when fifty percent of the capital is lost rather than the two thirds requirement in Venezuela. At this time the partners may elect to restore the loss or to file for dissolution of the company. Once dissolution has been filed, the proceedings begin. There does not appear to be a grace period, or a period for conciliation, or reorganization. A company, however, that goes into dissolution is given 3 years to “settle its affairs, but in no case may it continue the business for which it was organized” (<http://natlaw.com/pubs/sppngal.htm>).

If the board members of a company call for dissolution of a company a meeting of all shareholders must be called within 10 days of the decision to dissolve. Interestingly, “if all the shareholders ... state in writing their consent to the dissolution, neither the meeting of the board of directors nor the meeting of the shareholders shall be necessary...” (<http://natlaw.com/pubs/sppngal.htm>). In any case, consent to dissolve must be “protooled, recorded in the Mercantile Registry and published at least once in a local newspaper as well as in the Official Gazette” (<http://natlaw.com/pubs/sppngal.htm>).

In Panama, bankruptcy is appropriate when “any individual or company is incapable of meeting one or more of their liquid assets and certain obligations resulting from acts of commerce...” (<http://natlaw.com/pubs/sppngal.htm>). The individual(s) who determine bankruptcy is necessary and consequently suspends payments, must file a declaration of bankruptcy within 2 days of the decision. This seems relatively constrained when comparing with other countries’ laws. It seems that for Panama, once the decision is made, it is then full speed ahead with the proceedings. Additionally, for up to a period of 15 years, debtors remain responsible and liable for any unsettled debts. In the case of partnerships all partners share personal liability, while in the case of corporations shareholders are not personally liable. There does not appear to be a provision for criminal conduct.

### **6.4 Ecuador**

Civil Code, Commercial Code, and Code of Civil Procedure regulate bankruptcy and insolvency in Ecuador. In Ecuador, as in other countries, bankruptcy assumes insolvency of the debtor. A debtor can seek bankruptcy through voluntary relinquishment to the creditors of all assets, or a creditor can petition bankruptcy of a debtor. Interestingly, in a case where registered traders are involved, the law is a little different. In this case, bankruptcy can be declared “if a creditor presents an unsettled writ for payment, or the debtor does not fulfill his obligations to three or more different persons...” (<http://natlaw.com/pubs/specgal.htm>).

It does seem that Ecuador is much less tolerant of bankruptcy than other countries. Once a creditor has filed a petition a Judge will declare bankruptcy. The creditors seem able to wield quite a bit of power directly over the debtor. The consequences of insolvency are that the creditor can demand the sale of property, can subrogate the rights of the debtor to someone else, and can demand rescission of contracts. In addition, the debtor can be interdicted from managing property or from doing business at all. “All of the acts executed by the debtor are null and void”, and only a Judge can give the debtor permission to leave his home. A Judge can even order criminal proceed-

ings against the debtor, with a penalty of from 8 days to 6 years imprisonment, if there is an indication of mismanagement.

### **6.5 Chile**

Unlike the bankruptcy law in the European countries of Italy, France and Germany, Chile's bankruptcy law applies to every type of debtor entity. In 1982 Chile created a bankruptcy law that replaced the previous law enacted in 1931. "The Bankruptcy Law is inspired by the market economy as an instrument to reassign productive resources and permit the transfer of the assets of a failed debtor for reintegration into the economy" (<http://natlaw.com/pubs/spchbr1.htm>). The law is designed to provide first for reorganization so that the company does not have to declare bankruptcy, and second to provide for an orderly liquidation of assets. But, there are certain designations to be qualified for bankruptcy under Chile's law. A debtor must be determined as "qualified" or "not qualified". Qualification in this sense is a function of the type of entity and a "qualified" designation includes commercial, manufacturing, mining, or agricultural businesses while "not qualified" refers to businesses engaged in all other activities. As is the case in Ecuador, Chile's law provides for special criminal proceedings if a debtor is found to be negligent or fraudulent in the course of operating the company.

There are four common elements to bankruptcy law in Chile: the active party, the passive, qualified debtor, the judicial action, and the judicial declaration. The active party is the one initiating the bankruptcy and can consist of the debtor, any of the creditors, or the court. The passive, qualified debtor is a part of the business entity and can be classified as either "qualified" or "not qualified". The judicial action represents the specific action being petitioned and the judicial declaration represents the grounds for an adjudication of the bankruptcy.

In Chile, "a business will be deemed bankrupt when it is found to be insolvent...[or as a result of] the inability to meet ongoing obligations" (<http://natlaw.com/pubs/spchbr1.htm>). But, there are 4 other grounds under which a business can file for bankruptcy: *default* (cessation of payments), *pending executions* (a minimum number of expired or unfulfilled executions being initiated), *fugitive debtor* (leaving Chile or not leaving someone in charge), or a *voided nonjudicial workout agreement* (there has been no amenable solution). These all apply to the "qualified" debtor who has stopped making payments to the creditors. For the "not qualified" debtor there are three additional alternatives. Interestingly, "generally an adjudication of bankruptcy results in a prompt liquidation of assets, although a business may be permitted to continue operating in the ordinary course in order to preserve its integrity and to permit a prompt sale of the business as one unit..." (<http://natlaw.com/pubs/spchbr1.htm>). There does not appear to be a designated or required period of time for conciliation, or any type of grace period, or moratorium.

### **6.6 Bolivia**

In Bolivia, as in Chile and other countries, a company that cannot make its payments is declared insolvent. The Commercial Code of Bolivia manages bankruptcy issues. Similar to Panama, Bolivia allows for a loss in capital stock up to 50% before the company must consider liquidation. Prior to being declared bankrupt, the shareholders have the opportunity to reduce the capital to the appropriate level and if a firm files for bankruptcy voluntarily the filing must be done within 10 days of suspended payments to the creditors. If any agreements relating to any type of reorganizing effort are not complied with either the debtor or any of the creditors can request the commencement of bankruptcy proceedings, which must then be declared by a Judge. Interesting in the case of Bolivia is that "foreign companies [are] not required to guarantee their debts in the original registration [of the business]" (<http://natlaw.com/pubs/spboga1.htm>). Also, "there are no special provisions for reorganization of a business under dissolution. This is in concert with the requirement that all disputes must be arbitrated. The provisions that apply in this circumstance are the ones of voluntary bankruptcy" (<http://natlaw.com/pubs/spboga1.htm>). A debtor, once bankruptcy is filed, can be ordered detained by a Judge which could be interpreted as a form of criminal conduct.

### **6.7 Argentina**

Argentina has undergone a very long period of modification of bankruptcy laws as part of their efforts to overcome the economic crisis in Argentina and as part of the recommendations of the IMF. The most recent modification in the bankruptcy law was introduced in May 2002. A big difference in this law from the previous laws is that it “limits the broad scope of protection from creditors granted to bankrupt companies” (Inter-American Trade Report July-August 2002). The IMF noted the previous law had made it very difficult for foreign investors in Argentina. The new law now allows creditors or other third parties to purchase the bankrupt firm. This was not possible under the previous law. Other changes that took place in the new bankruptcy law in Argentina concerned the repeal of the Economic Subversion Law and changes to the Criminal Code. Regarding criminal action, if there is a presumption of fraud in a liquidation case, a Judge will give notice to a criminal court. It is not known how such an action might proceed with regard to fines, incarceration, or other liabilities.

While other countries tend to have a minimum capital stock reduction to trigger an insolvency or bankruptcy proceeding, Argentina defines the start of reorganization as a “cessation of payments”. It seems that reorganization is the beginning of a process that ends in adjudication by a bankruptcy judge.

Another interesting change in the May 2002 law was a reduction in the grace period allowed for insolvent companies to make alternative arrangements. “Alternative arrangements” refers to one of the four articles of the new law on “reorganization” that is comparable to Chapter 11 in the United States. In the previous law, the grace period was 30 days with a possible extension up to 60 days. The new law grace period is 90 days with a possible extension up to 30 days. What is interesting here is that there was an “interim” law between the 1995 and 2002 modifications that provided for a grace of 180 days with a possible 180-day extension.

## 7.0 Strategic Implications

Table 1 summarizes the discussion of basic bankruptcy law provisions in the seven Latin American countries’ bankruptcy laws. The summary data contained in Table 1 have strategic implications for multinational companies, particularly if the company is attempting to place new operations or relocate existing ones in a Latin American country.

**Table 1: Comparison of Selected Latin American Country Bankruptcy Law Provisions**

	<b>Reorganization</b>	<b>Conciliation</b>	<b>Criminal Conduct</b>	<b>Trigger Condition</b>
<b>Argentina</b>	Yes	Yes; 90 – 120 days	Yes	Cessation of payments
<b>Bolivia</b>	No	No	Yes (Detention can be ordered)	Unpaid accounts; ½ loss of capital
<b>Chile</b>	Yes	No	Yes	Insolvency and 4 others
<b>Ecuador</b>	No	No	Yes	Unpaid accounts; ½ loss of capital
<b>Mexico</b>	No	Yes; 130-360 days	Yes	Yes, if no agreement
<b>Panama</b>	No	No	No	½ loss of capital
<b>Venezuela</b>	Yes	Yes; 1 –2 years	Yes	2/3 loss of capital

## 7.1 Reorganization

Should a multinational company experience bankruptcy, reorganization would normally be preferred to liquidation, all other things being equal. Four of the countries included in this study – Bolivia, Ecuador, Mexico, and Panama – do not have a Chapter 11 type of reorganization provision. Consequently, strategists should prefer Argentina, Chile, and Venezuela as alternative locations for the placement of new operations. Should a multinational company already have operations in two or more of the Latin American countries included in this study, the company would prefer to adjudicate its insolvency in a country that provides for or favors reorganization. This view is confirmed by Guzman (2000) who argues that territorialism has a harsher effect on the ability of the bankrupt firm to reorganize, and that large multinational bankrupt firms are much more likely to pursue reorganization than liqui-

dition. Under territorialism, reorganization depends on the decisions of all relevant jurisdictions and may be impossible if important assets are located in a jurisdiction that does not favor reorganization, believes reorganization is inappropriate in this particular case, or feels its local creditors can be satisfied out of local assets.

## **7.2 Conciliation Period**

The provision for a conciliation period in a country's bankruptcy law would ordinarily be preferred over the absence of such a provision. The conciliation period concept is often linked to the existence of a provision for possible reorganization. The summary data in Table 1 generally confirm this linkage. Three of the four countries with no reorganization provision also have no provision for a conciliation period. Mexico has no provision for reorganization but does offer a conciliation period in which debtors and creditors might resolve the conditions causing the impending bankruptcy proceedings. Strategists would normally prefer a conciliation period to provide additional time for negotiating a resolution of insolvency, to provide a "cooling off" period for all parties, or to provide additional time to divest the operations and achieve a more favorable outcome than liquidation promises. In general, conciliation periods are viewed as providing greater strategic flexibility, particularly if the host country's bankruptcy law also contains a provision for reorganization. Two of the three countries that offer reorganization also offer a conciliatory period. Chile has a reorganization feature, but does not offer a conciliatory period. This combination is not as attractive as having both a reorganization opportunity and a conciliatory period, but it is more attractive than having no reorganization opportunity along with a conciliatory period as in the case of Mexico.

## **7.3 Trigger Conditions**

The term "trigger condition" refers to that circumstance or condition described in the bankruptcy law that triggers the bankruptcy process and procedures. Each country's bankruptcy law incorporates some type of triggering condition, so the presence of a triggering device is a "given" in formulating a bankruptcy contingency strategy. Of much greater importance is the nature of the triggering condition. Six of the seven Latin American countries included in this study have one or more provisions in their bankruptcy law that trigger bankruptcy proceedings because of unpaid accounts, loss of capital, or a combination of these conditions. In the case of Mexico, it is unclear whether or not there is an absolute condition that initiates the process. The implied condition of financial insolvency resulting in nonpayment of one or more creditors seems to be the basis for Mexico's 130-360 day conciliation period during which debtors and creditors might attempt to negotiate a solution to the problem in the form of an agreement between them. In the event that no agreement is forthcoming, bankruptcy proceedings begin after the completion of this conciliation period.

When considering strategists' preferences between unpaid accounts and loss of capital as triggering mechanisms for bankruptcy in the countries included in this study, strategists should generally prefer loss of capital as a triggering mechanism. The preference for this type of triggering mechanism derives from the more precise nature of the loss of capital provision in comparison with the much less precise concept of unpaid accounts. In Bolivia, Ecuador and Panama, the loss of one half of the company's capital triggers bankruptcy; in Venezuela, the loss of two-thirds of the company's capital initiates the proceedings. In Bolivia and Ecuador, failure to pay accounts is an alternative trigger for initiating bankruptcy proceedings along with the loss of capital criterion. Venezuela's only triggering criterion is the loss of 2/3 of the company's capital.

Strategists should prefer Venezuela first because of the greater loss of capital (2/3) required to initiate bankruptcy, allowing the company a greater amount of time (all other things being equal) to search for other alternatives. Strategists should prefer Panama second because of its single but precise criterion of loss of one-half of the company's capital. Bolivia and Ecuador should be preferred third because of the loss of capital criterion (1/2) coupled with the unpaid accounts criterion. These countries' bankruptcy laws would be less preferred than those of Venezuela and Panama because the unpaid accounts criterion represents a trigger that can potentially initiate bankruptcy much quicker than the loss of capital criterion. Additionally, these countries' laws are unclear regarding the number of unpaid accounts required to initiate bankruptcy, with the number of unpaid accounts required to trigger bankruptcy conceivably being as little as a single unpaid account. Argentina's and Chile's laws would be next in the order of preference because of their single criterion of unpaid accounts (cessation of payments in Argentina's case).



Finally, Mexico's trigger condition would be the least preferable among strategists because of its limited options, high degree of uncertainty, and absence of structured outcomes.

#### **7.4 Criminal Conduct**

Six of the seven Latin American countries' bankruptcy laws include a provision for criminal conduct penalties that vary in severity from country to country. Only Panama's bankruptcy law has no provision for criminal conduct penalties. Of the seven countries, Ecuador seems the most hostile to the bankruptcy concept. Ecuador's law includes no provision for reorganization and no conciliation period, but does include a quick trigger (unpaid accounts) as well as the possibility of harsh penalties (up to six years in prison) for mismanagement. To the extent that individual strategists are risk averse in regard to the possibility of being held criminally liable for their actions as strategists, they should all prefer Panama's law that has no such provision, and then those laws which provide for criminal penalties ranked in decreasing order according to the increasing severity of the penalty provisions. Under this scenario, Panama would be ranked first, Ecuador last, and the other five countries would be ranked second through sixth according to the increasing severity of their criminal penalties.

The provisions for criminal conduct penalties in bankruptcy laws must also be considered from a general and personal ethics point of view. Generally, ethical strategists as a group might well favor and embrace such provisions as a necessary and desirable deterrent to unethical actions by strategists from competing organizations. In this scenario, the rankings discussed above would be exactly reversed, with Ecuador topping the preference list and Panama being the least preferred.

Individual strategists' preferences may be expected to vary widely in regard to this provision, depending on the strength of the individual's sense of right and wrong and the strategist's sense of compassion and retribution. The most unethical strategists should prefer Panama's law above all of the others because it has no provision for criminal penalties and should least prefer Ecuador's law because of its severe criminal penalties. However, even the most ethical strategists might have the same ordered preferences regarding this provision simply because of an unwillingness to assume even the smallest of risks that he/she could be judged to have been involved in activities that result in criminal penalties.

#### **7.5 General Territoriality Implications**

As explained earlier, territorialism is based on the concept that each country has the exclusive right to govern within its borders. Applied to bankruptcy of a multinational company it means that the bankruptcy courts of each country have jurisdiction over those portions of the company (assets) that are within its borders. This results in the failed multinational company being subject to multiple laws administered by multiple courts in multiple countries. From the point of view of multinational company strategists, territoriality poses major, almost nightmarish complications to both primary and contingency strategy formulation. If bankruptcy were considered a contingency possibility for each primary strategic alternative then it would behoove the strategist to be knowledgeable regarding at least the general nature of the bankruptcy regime – the bankruptcy law and the bankruptcy court and court system – for each of the countries in which the multinational firm has assets and operations. For firms with multiple and far flung divisions, the strategic implications are almost limitless if these firms' strategists attempt to incorporate or otherwise systematically include bankruptcy ramifications into strategic contingency plans. Exceptionally well resourced firms may not be dissuaded from pursuing a primary strategy with high probability of success such as market development or concentric diversification because of unfavorable bankruptcy laws and/or courts in foreign countries, but smaller, less well-resourced firms might well be influenced to pursue different strategies with lower probabilities of success when confronted with hostile bankruptcy laws and courts when considering expanding into foreign countries where they do not currently have assets and operations (Brewerton and LeMaster, 2002).

#### **7.6 General Implications of Universalism**

From the point of view of multinational company strategists, universalism offers important dimensions to strategy formulation. If universalism were the bankruptcy regime of the land, strategy formulation could be some-

what simpler, particularly in regards to assessing the outcome of a failed strategy resulting in bankruptcy. Regardless of whether the bankruptcy resulted in liquidation or reorganization, the treatment by the law and the courts would be uniform across all countries and would eliminate concerns and deliberations regarding which country's laws would take precedence. In short, because the outcome of a failed strategy would be identical regardless of the country or countries in which the multinational firm operates, the consequences of bankruptcy would be a "given" or a factor common to selection of any and all strategies and therefore could not affect the choice of strategic alternative. Strategists could then focus all of their attention to the optimum selection of a specific strategic alternative without any concern regarding contingencies associated with failed strategy resulting in bankruptcy. In short, the outcome of bankruptcy would be completely predictable (Brewerton and LeMaster, 2002).

## 8.0 Summary and Conclusions

The purpose of this paper has been to (1) examine the degree of convergence of bankruptcy laws in seven Latin American countries regarding four basic provisions, and (2) to assess the implications that differences in basic bankruptcy law provisions in these countries pose for strategists.

Although at least two of the seven Latin American Countries' bankruptcy laws have undergone major changes in recent years (Mexico, 2000; Argentina, 2002), the bankruptcy laws of the seven countries have not yet converged into a common set of provisions. The results of this study suggest that Westbrook's (2000) arguments that convergence is already occurring as a result of globalization can only be described as generally true. The movement toward Universalism predicted by Westbrook (2000) and supported by the Universalism school within the community of legal scholars may be best described as "creeping universalism". Nevertheless, from the strategist's point of view, universalism still permits the greatest degree of simplicity and ease in the formulation of contingency plans that might involve bankruptcy and should be preferred by all strategists. This simplicity derives from the uniform outcome that universalism produces in the event of bankruptcy irrespective of which specific strategic alternative is pursued. Universalism also produces the highest predictability of outcome (perfect predictability, theoretically), the lowest information requirements, the lowest costs, and the simplest and most reliable enforcement.

Compared to Universalism, the Territorial model of bankruptcy law is less attractive when formulating contingency strategies. The territorial model makes contingency planning extremely difficult to accomplish, requires inordinate amounts of information and analysis, and carries higher costs with it because of these characteristics. Furthermore, bankruptcy outcomes are not as predictable as they are under Universalism and enforcement is difficult because of the multiplicity of laws and court systems involved. This very limited study clearly confirms these arguments. Comparison and analysis of four basic provisions across seven Latin American countries' bankruptcy laws is tedious and produces varied preferences among strategists for the countries' laws in which these provisions are present or absent. Furthermore, this study has made no attempt to weigh the relative importance of these provisions, a factor that further complicates the formulation of contingency strategy in the event that a multinational firm would be forced into bankruptcy. Nevertheless, this study suggests that multinational company strategists' first preference for a country's bankruptcy law and subsequent adjudication would be Venezuela because of its provisions for reorganization, its relatively long conciliation period, and its two-thirds capital loss bankruptcy trigger. Venezuela's provisions for criminal conduct would affect strategists' preferences only if all other countries' laws contained common provisions for reorganization, conciliation, and trigger conditions. A precise ordering of strategists' preferences for the remaining six countries' laws is difficult to assess but Ecuador's bankruptcy law is probably the least preferable because of its early triggering provisions, its lack of a reorganization provision and a conciliation provision, and its harsh provision for criminal penalties associated with mismanagement. 📖

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