

Exclusive Q&A on Bankruptcy & Restructuring

With Mary Fernandez - Headrick Rizik Alvarez & Fernández



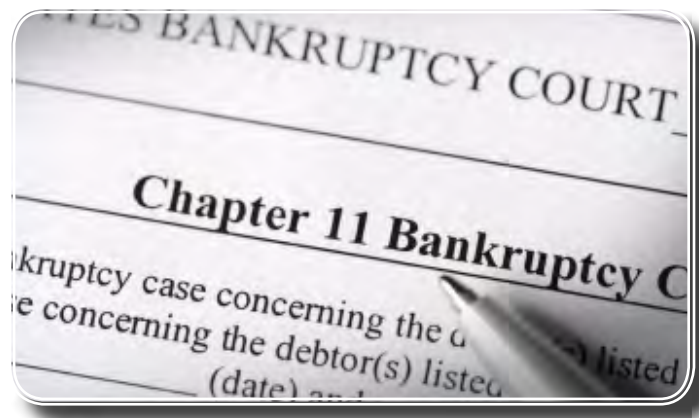
Mary Fernandez is a founding partner of Headrick Rizik Alvarez & Fernández, Dominican Republic. She specialises in corporate and business law, banking law, foreign investment, intellectual property, arbitration, and trusts and estates. Serves as the Chair of the Legal Committee of the American Chamber of Commerce and is a member of the Board of the Center for Resolution of Controversies (CRC) of the Chamber of Commerce and Production of Santo Domingo (CCPSD). Mary is also member of the editorial committee of Gaceta Judicial, the only legal periodical in the country. Her professional practice has been recognised and ranked in Band 1 by Chambers Global 2013 and Chambers Latin America 2014 in Corporate/Commercial and Intellectual Property.

What are the main challenges currently facing bankruptcy and restructuring lawyers?

Challenges vary across jurisdictions. The absence of reorganisation procedures appears to be at the single greatest problem in emerging economies. Out of Court Workouts

(“OOCW”) are extremely useful for corporations with the capability of restructuring their debts.

As the *Doing Business*(1) report rightly provides: “*a well-balanced bankruptcy system distinguishes companies that are financially distressed but economically viable from inefficient companies that should be liquidated. But in some insolvency systems even viable businesses are liquidated*”. This is common in the Dominican Republic, where reorganizations are not contemplated by the law.



Excessive time in concluding insolvency procedures and low recovery rate is another common problem(2). In the Dominican Republic, a bankruptcy procedure – which can only take the form of a liquidation – takes approximately 3 ½ years to complete, on average costs 38% of the bankruptcy estate,

and the recovery rate for claimants (creditors, tax authorities, and employees) is about 8.7 cents on the dollar(3). And even OOCW, which are currently carried out in the country, lack adequate legal protection.

Lastly, and possibly the most challenging problem faced by lawyers, is dealing with cross-border insolvencies due to increased globalisation of commercial activity.

Have there been any regulatory changes or interesting developments over the past twelve months?

In the Dominican Republic, a bill was introduced to Congress to specifically address bankruptcy issues, including – most importantly – the creation of the concept of bankruptcy reorganisations, but the bill expired prior to congressional approval. The bill was first introduced in 2007 and has been reintroduced periodically, but has not gained sufficient approval to get converted into law.

Internationally, the development by the American Law Institute (ALI) and the International Insolvency

Institute (III) of the Global Principles for Cooperation in International Insolvency Cases to be applied to international insolvency cases is a major breakthrough, which is not so much aimed at the harmonisation of individual legal systems but at providing guidelines and alternative solutions for cross-border cases.

Although these principles are not binding, they will certainly serve as viable options and clear guidelines whenever a national rule is not available.

Which industries are in most need of bankruptcy and restructuring expertise?

Banking and financial institutions in general are probably in the most need of insolvency regulation. It is no secret that investors are more prone to invest where the rules for exiting investments cases where things don't go as planned are clear.

Organised insolvency for non-merchants is also necessary in jurisdictions like the Dominican Republic.

Can you outline the due diligence process during preparation for debt and company restructuring?

With respect to in-court restructurings or pre-packaged bankruptcies, we are unable to comment on this topic since restructuring does not exist in the Dominican Republic. Regarding OOCW, typically these are carried out by lenders after carrying out due diligence on the debtor's assets and operations in order to ascertain the status of such given what is presumably a difficult time for the debtor.

How would you assist a company on the verge of declaring bankruptcy?

Our advice to a company on the verge of declaring bankruptcy in a jurisdiction other than the Dominican Republic is to pursue an OOCW pursuant to the procedure contemplated in the jurisdiction where the company is located.

Locally, however, our first recommendation would be to attempt a voluntary reorganisation (such as closing down unprofitable stores or lines of business, or

attempting other commercial strategies to improve business) and/or OOCW of the business prior to initiating formal legal proceedings since reorganisation is not formally contemplated by the law.

Is there an increasing reluctance from banks to accept an application for bankruptcy in your jurisdiction?

Banks are extremely reluctant to provide prior acceptance of any insolvency or bankruptcy procedure initiated by one of its debtors, principally because such a declaration will exclusively result in the liquidation of the business and will require time to sort out. Although bankruptcy declaration presently has no effect for secured creditors (banks are typically secured creditors), banks prefer to control the processes through informal reorganisation processes (such as an OOCW) conducted and directed by them.

As for the insolvency or bankruptcy of the banks themselves, the Dominican Republic has special insolvency rules for financial institutions, which involve

intervention by the Superintendence of Banks and a fund with which to support a bank in the interest of its depositors. Even if banks were reluctant to accept an application for bankruptcy, the special bankruptcy procedures embody public policy and the same is ultimately decided and directed by the Superintendence of Banks. It consists in a purely administrative procedure under the supervision of the Monetary Board, without any participation by judges or courts. The domestic legal system was significantly enhanced after the financial crisis of year 2003; this has played an important role in the strengthening of the economic and financial system of the Dominican Republic.

What methods are creditors using to assert their claims against insolvent debtors and recover as much value as possible?

Aiding debtors to engage in a voluntary reorganisation and/or OOCW is becoming more common every day. The process is less expensive and can have a greater return than pursuing the formal insolvency procedure against the debtor. The alternative is to have

the debtor initiate liquidation proceedings – which no party benefits from.

In the Dominican Republic, unsecured creditors, before commencing any other action or at any time during such proceedings, can seek from the judge, in an ex parte proceeding, an order attaching personal property owned by his or her debtor. To attach real property, the creditor requests judge authorisation for a provisional judicial lien, which is filed at the Land Registrar's Office, and then notifies the debtor. The provisional judicial lien is converted into a definitive judicial lien, through a judicial decision, which the plaintiff can then foreclose, in a separate proceeding. Another method creditors may use to assert their claims is the garnishment of a debt owed to his debtor by a third party. This possibility is known as an *embargo retentivo*.

Do you believe that “Amend and Extend” is a possible solution or is it merely papering over the cracks?

I believe “amend and extend” is an exceptional solution to be considered in certain specific situations for

struggling debtors that although may be facing momentary insolvency, are capable of surviving and will not have to face bankruptcy, which otherwise would not benefit any of the parties involved. Ultimately, the “amend and extend” is many times not only granted in the best interest of the debtor but also turns out to be the best solution for the lender itself, which avoids having to engage in a lengthy and complicated insolvency process and can be a helpful part of any OOCW.

Does your jurisdiction offer any restructuring schemes to aid insolvent organizations?

The Dominican legislation does not contemplate reorganisations or pre-packaged bankruptcies (as previously mentioned, the legislation only contemplates liquidations), although a debt restructuring can be agreed upon at the compulsory preliminary conciliation proceeding. Commercial banks and other financial institutions tend to promote informal reorganisation processes for debtors in lieu of initiating a lengthy and costly judicial insolvency process.

A proposed bill to modernise the bankruptcy legislation in the country, but which recently expired in Congress, contemplates an out-of-court reorganisation procedure to be conducted by the Chambers of Commerce.

Are you witnessing an increase in out of court or pre-packaged insolvencies? What other strategies of resolution are currently proving popular?

Although no general provisions are currently available in the Dominican Republic governing reorganisation of failed businesses, amicable out-of-court settlements and reorganisations are being pursued and supervised by banking institutions which profit more from an operating company than from a bankrupt one. Therefore, companies facing financial difficulties and which have bank loans or commitments are being assisted in conducting out-of-court reorganisation processes by the same creditors.

Pre-packaged plans for reorganisation are gaining momentum in other jurisdictions, such as the United States, France and

Germany, but are not contemplated by local law.

Can you talk us through the process of acquiring an insolvent business in your jurisdiction?

Typically, an insolvent business is acquired prior to the initiation of any formal bankruptcy process. Therefore, the acquisition process, although entails significantly more due diligence work than it would in other cases, and requires more detailed legal provisions to protect the acquirer, the acquisition does not contemplate additional legal formalities. Pre-pack agreements for the sale of an insolvent company’s asset are generally entered into prior to the company entering into a formal insolvency procedure.

The scenario where a business is already involved in a liquidation process is different. The sale of specific assets out of the ordinary course of business is allowed during a liquidation procedure when such assets are perishable and when abstaining from their sale would be harmful to the creditors of the bankrupt debtor. Therefore, such assets would be passed ‘free and

clear’ to the purchaser.

Upon entry of a bankruptcy order, the following transfers of property by the debtor are defined by the Code of Commerce as null and void: (a) payments made within 10 days of the insolvency date or after the insolvency date for obligations not yet due and payable, or obligations due and payable but made other than in cash; and (b) any transfers of cash or property made without consideration.

How has the rise in cross-border activity changed the complexity and sophistication of bankruptcy and restructuring?

Cross border activity has changed the way of conducting business and of bankruptcy and restructuring, as well. Nowadays, there are fewer instances where you are able to conduct a bankruptcy or restructuring proceeding where no cross border activity exists.

The Dominican Republic has not entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries, nor have they

communicated or held joint hearings with courts in other countries in cross-border cases, cross-border activity has had no effect on the improvement or sophistication of bankruptcy in the Dominican Republic.

Under the current regime, there is no relief available concerning an insolvency proceeding in another country, except in the benefit of signatory countries of the International Private Law Convention signed in Havana in 1928 (the Bustamante Code). This provides for extraterritorial effects within the signatory countries of the bankruptcy declaration of a debtor, and remedies pursued by appointed receivers or liquidation administrators. It also provides rules for the enforcement of foreign judgments within the signatory countries. Therefore, outside these cases, there are no provisions regarding cooperation actions between domestic and foreign courts or administrators (even though the Dominican Code of Commerce contains provisions for a reserve for the payment of foreign claims).

Foreign judgments or awards

are made enforceable in the Dominican Republic upon issuance of an exequatur by a local judge, authorising the validity of the foreign judgment. Dominican courts will ratify such judgment if it: (a) complies with all formalities required for the enforceability thereof under the laws of the foreign country; (b) has been translated into Spanish, together with related documents and satisfies the authentication requirements of Dominican law; (c) was issued by a competent court after valid service of process upon the parties to the action; (d) was issued after an opportunity was given to the defendant to present its defense; (e) is not subject to further appeal; and (f) is not against Dominican public policy.

Is an international network a prerequisite to dealing effectively with cross-border matters?

Dealing effectively with cross-border matters requires the existence of an international network. Interrelationship between different territorial regimes where a bankruptcy proceeding must take place, cannot be efficient without the

guidance of general international principles.

What key trends do you expect to see over the coming year and in an ideal world what would you like to see implemented or changed?

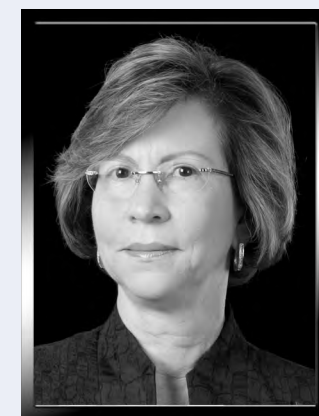
We would like to see implemented guidelines that would be applicable at the local or international arena aimed at achieving the successful recovery of struggling companies, or failing that, an efficient and predictable sale and distribution of the assets in favour of the creditors.

Locally, we would very much like to see the legislative proposal passed by Congress to grant the Dominican Republic a modern system that would contemplate out-of-court reorganisation and an expedited judicial proceeding for cases where liquidation is necessary. The new law would make possible the transition from one procedure to the other, providing an equal treatment to similar creditors, including foreigners, respecting their priority rights. The new law would also provide a legal framework for the regulation of cross-border insolvencies.

The implementation of a modern and effective insolvency regime would act as a balance between the need to quickly and efficiently assist the debtor's facing financial difficulties and the need to protect the rights of the creditors, especially those holding secured claims.

For more information please visit www.hrafdom.com

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(1)DOING BUSINESS, *Doing Business 2013*, World Bank, Palgrave MacMillan and IFC, Washington, D.C, 2012.

(2) Other challenges in the Dominican jurisdiction include the following:

- a. There is no organised insolvency for non-merchants, no debt relief systems and no protection against over-indebtedness.
- b. Legal provisions on bankruptcy do not contemplate reorganisation, although a debt restructuring can be agreed upon a compulsory preliminary conciliation proceeding before the Chamber of Commerce[2], prior to a creditor being able to institute a bankruptcy proceeding against its debtor.
- c. The criterion to determine if a debtor could be made subject to bankruptcy proceedings revolves around the concept of “cessation on payments” rather than considering a state of insolvency. Nonetheless, the number and importance of the debts owed are not established by law.
- d. Arbitration is not available for insolvency proceedings.
- e. The legislation does not contemplate the possibility of expedited reorganizations.
- f. There are no provisions regarding cooperation actions between domestic and foreign courts or administrators. Nonetheless, the Dominican Code of Commerce contains provisions for a reserve for the payment of foreign claims.

(3)DOING BUSINESS, *Doing Business 2013*, World Bank, Palgrave MacMillan and IFC, Washington, D.C, 2012, p. V.