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**UNCITRAL Working Group V and a Simplified Insolvency Regime for MSEs**

*Dr Jennifer L. L. Gant, INSOL Europe Delegate to UNCITRAL WGV;   
Email: <jenniferl.l.gant@gmail.com>.*

*Introduction*

The last year has laid bare the weaknesses of many modern market economies to guard against the financial and social costs of a health crisis that has driven the global marketplace nearly to a standstill. Emergency measures covering everything from furlough schemes for workers unable to perform their job due to workplace closures to adjustments to some of the more draconian aspects of insolvency procedures, such as filing obligations, were introduced and have been steadily extended through the now extensive period of the pandemic.

Some of the hardest hit businesses have been those of small and micro sizes (MSEs) – consider the local pubs, cafes, and bars that have had to shut their doors for months on end, relying only on government loans, grants, and schemes to see them through to the reintroduction of normal circumstances. In addition, the many shared responses to the crisis such as the isolation of populations, travel bans, and limits placed on indoor and outdoor gatherings have potentially changed the perspective of individuals going forward.[[1]](#footnote-1) Who knows what long-term impact this crisis will have on the behaviours of consumers in particular within the global marketplace?

There was a sense of urgency in the proceedings of Working Group V due to the potential consequences that the eventual withdrawal of SME protection provided during the COVID 19 pandemic may have in the near future. The tenor of the discussions and debate highlighted the need for an imminently, if not immediately useable instrument to help SMEs deal with the fall out of pandemic related lockdowns. The impact of the pandemic on the efficiency of discussions fed into that concern further, which inspired the convening of several informal sessions hosted on Zoom, during which many of the issues were acknowledged and at least to some extent ironed out before the formal meetings convened.

**A Simplified Insolvency Regime for MSEs**

Although UNCITRAL’s Working Group V on insolvency has been discussing the need for providing a model for a simplified insolvency regime aimed at micro and small enterprises since a preliminary examination of this idea was made at the 45th session of Working Group V in 2013 (mandated by the Commission at its 47th session in 2014), it has taken some time for the concept to find form in a soft-law instrument that would be useable by its target group. At the 55th session in New York 2019, the Working Group commenced detailed deliberations on the features that should be included in a simplified insolvency regime.

The first full draft of the simplified insolvency regime was considered at the 56th session in Vienna in 2019 and which was discussed and revised by the secretariat several times over the sessions that followed in 2020. It is only this year during the height of the COVID 19 pandemic that a draft text has been agreed in principle for the recommendations that should be included with this new model law on a simplified insolvency regime for MSEs. Given the economic challenges of the last year, this progress is particularly timely.[[2]](#footnote-2)

Working Group V met for its 58th session from 4-7 May in a virtual space, instead of in the bustling metropolis of New York City, much to the regret of the majority of the delegates. The meetings were hosted in Vienna where delegates from across the world united morning, noon, and night (depending on the time zone) to discuss the remaining open questions within the 107 recommendations and 389 commentary paragraphs of the draft text on a simplified insolvency regime.[[3]](#footnote-3)

The draft instrument itself is based largely on similar concepts and provisions included in the UNCITRAL Legislative Guide on Insolvency Law, which was designed with the aim of providing “a comprehensive statement of the key objectives and principles that should be reflected in a State’s insolvency laws.”[[4]](#footnote-4) The key objectives of the simplified insolvency law are to provide an expeditious, simple, flexible and low-cost insolvency proceeding targeted and easily accessible by MSEs. The regime also aims to promote the opportunity for a “fresh start” and a discharge of debt obligations through the agreement and implementation of a debt restructuring plan with creditors.[[5]](#footnote-5)

The simplified insolvency regime shares a number of key concepts with the Legislative Guide, such as the need for efficiency, though this characteristic should be enhanced in the context of MSE insolvency. The simplified regime also focuses on debtor in possession procedures and reduced formalities as far as possible, and provides for a stay of enforcement actions, while also ensuring fair treatment of creditors and a protection of pre-insolvency entitlements as far as possible.

The main issues arising during the discussions often revolved around how to word some of these key provisions in order to encourage close implementation as well as ensuring a balance between the need for the regime to be “simplified”, while avoiding the moral hazards that could lead to the abuse of a process that is perhaps too easily accessible.

**Soft-law Instruments – Woulda, coulda, shoulda?**

Like all of the model laws and legislative guides produced by UNCITRAL, the World Bank, and other international organisations, the simplified insolvency regime will, of course, be a soft-law instrument that is fully optional as to the scope of its implementation. It does not provide any kind of obligatory harmonising instrument that could “level the playing field”, as the Preventive Restructuring Directive has been categorised (perhaps overzealously given the scope for implementation). It is, like the Legislative Guide, aimed at fostering and encouraging “the adoption of effective national corporate insolvency regimes”.[[6]](#footnote-6) It provides recommendations – 107 of them – and 389 paragraphs of commentary that adds clarity and explanation to those recommendations, which implementing countries can take or leave as they see fit.

Given the nature of such soft-law instruments, it struck this observer as particularly odd that there were a few significant arguments over whether the words “may” or “should” ought to be used in the context of these recommendations. Some observers, including from international bodies, opined that “may” is not a very strong word and queried why such recommendations should give an option between these two words at all given the nature of soft-law. Both “may” and “should” are essentially optional, so why the need to choose between the two?

Conversations with other delegates during the proceedings (on a WhatsApp group as that is what is done in the time of COVID) provided an interesting perspective, given their longer involvement in the development of soft-law within Working Group V. There are certain nuances between these two words. The effect of the degrees of power between “may” and “should” could have an influence on *indirect* harmonisation of insolvency law on a global level. The use of the stronger “should” for those provisions that the Working Group felt particularly strongly about, may well result in a higher implementation rate simply due to the psychological effect of “may” being fully permissive as opposed to “should” having a more moralistic implication. The influence of verb-choice on the implementation of soft-law recommendations may well be a very interesting psycho-legal area of research for the future!

**Tension: Balancing Simplification and Ease of Access with Moral Hazard**

During the session, a clear contentiousness was apparent between the influence of the similar policy positions of both the World Bank and the International Monetary Fund and the general consensus of the experts within Working Group V. This became particularly acute during a discussion revolving around the concept of deemed consent of non-voting creditors. Essentially, the confirmation and approval process within the simplified insolvency regime is set up to encourage simplicity, efficiency, and accessibility, which includes being able to circumvent creditors who appear to be apathetic about their participation rights.

The issue between the World Bank and IMF in opposition to the Working Group consensus was that there was no *requirement* *per se* to hold a full vote among the creditors on the approval of the reorganisation plan and that any failure to vote by a creditor would be deemed as consent to the plan. The opponents to this position were primarily concerned that there was a positive expectation placed on creditors to oppose or object to a plan rather than a right to vote on it. This could be perceived as creating a potential moral hazard for debtors not to try so very hard to ensure all creditors are informed. With that being said, adding additional obligations to inform, consult, and hold creditors’ meetings would clearly also detract from the “simplified” nature of the regime that Working Group V has been trying to create.

One clear message from Working Group V experts was that the simplified insolvency regime is aimed at SMALL business enterprises, many of which, being in severe financial difficulties, require expedited relief. While there is clearly still a need to balance the rights of creditors with the need for expeditiousness, the text itself provides that notice must go to all creditors affected by the plan with a time period within which to object or oppose. A voting process would cause a potentially excessive delay, during which time the MSE may well fall into full financial failure, unable to survive during that period and exhausting the last reserves that may have been available to repay a proportion of what was owed to the creditors waiting to vote!

In any event, as a soft-law instrument, the bottom line is that the states choosing to implement the recommendations in some fashion still have the ability to determine whether it is appropriate for their jurisdiction to provide for deemed approval in this way, particularly given the number of specific protections that have already been provided within the text to mitigate the potential moral hazard of such a flexible and easily accessible regime.

This issue had come up a number of times in previous negotiations and discussions on this topic. The underlying question perhaps boils down to whether all international organisations that create model laws and soft-law guidelines should fully align in their views on best practices? Perhaps the provision of multiple instruments underpinned by different policy perspectives would actually create a higher number of successful implementations of at least some kind of framework that has a similar aim of providing easily accessible, efficient and simplified procedures for MSEs, even if those defining characteristics are on a spectrum limited by national legal cultures, social and economic policies. Arguably, frameworks underpinned by a range of policies along a spectrum would cater more fully to a global rehabilitation framework.

**Conclusion**

Despite issues of efficiency due to the virtual format and the challenges of interpretation over poor connections, Working Group V succeeded in finalising the 107 recommendations and most of the commentary, agreeing in the end to submit the recommendations to the Commission to approve in principle. The commentary was to be included in the submission to the Commission, but with the caveat that they could be revisited at the next session should that be necessary. This followed the precedent of the UNCITRAL Legislative Guide, which was also done in stages with the Commission.

One of the key reasons for adopting what is essentially a staged approval approach was to ensure that the Working Group is as efficient as possible at getting this instrument out so that it can be used when it is most needed. This approach will allow for the recommendations for a simplified insolvency regime to be circulated and utilised at an earlier date than would otherwise have been possible upon approval of the full instrument. The instrument will hopefully be available as a resource for MSEs by the time the economic fallout of withdrawn safety nets proffered during the pandemic come home to roost.

In the time of COVID and the impact that the lockdowns will have upon smaller businesses in particular when the safety nets are taken away, it is clear that a means of resolving the financial distress or at least providing less painful exits from a failing business is vital to the continued health the global economy. It is a relief to report that the recommendations and its associated commentary, though the latter has not yet been fully discussed, will be with the Commission during their next session in July, leading hopefully to the availability of the recommendations at least for consideration by states who need better provisions for MSEs facing imminent insolvency. The rest of the commentary will then be the topic of discussion for the next Working Group V session in December.

1. For a comparative discussion on European responses to the pandemic, see Emilie Ghio *et al*., “Harmonising Insolvency Law in the EU: New Thoughts on Old Ideas in the Wake of the COVID-19 Pandemic” (2021) 30(3) *International Insolvency Review* (forthcoming). [↑](#footnote-ref-1)
2. Working Group V work and papers can be accessed here:

   <<https://uncitral.un.org/en/working_groups/5/insolvency_law>>. [↑](#footnote-ref-2)
3. The draft text on a simplified insolvency regime discussed during the 58th session of Working Group V can be found here: <<https://undocs.org/en/A/CN.9/WG.V/WP.172>> (Draft simplified insolvency regime). [↑](#footnote-ref-3)
4. The UNCITRAL Legislative Guide on Insolvency Law can be found at:

   <<https://uncitral.un.org/en/texts/insolvency/legislativeguides/insolvency_law>> (Legislative Guide). [↑](#footnote-ref-4)
5. Draft simplified insolvency regime, Recommendation 1. [↑](#footnote-ref-5)
6. Legislative Guide, iii. [↑](#footnote-ref-6)