CHAPTER FIVE

INFORMAL WORKOUTS AND RESTRUCTURING\textsuperscript{1}

5.0. Introduction

There seems to be a consensus in most commercial cultures that informal procedures that solve problems are preferable to litigation with its much added expense and time. By definition, such procedures are not enshrined in law, although background legal rules may shape them in important ways. Thus in this chapter we seek to provide a discussion that enables the reader to evaluate informal approaches in various legal situations and as to debtors in various circumstances.

An informally agreed solution may enhance the trust and goodwill that are often vital to the future commercial relationships among the parties. This is particularly true where the issues concern the attempt to rescue an insolvent debtor with potential for survival and where continuing support for the debtor from existing customers or clients will be an important factor in the survival. Furthermore, an informal procedure can enjoy secrecy, something that might be of special value in circumstances where adverse publicity might have a further detrimental effect on the weakening debtor.

An informal procedure would in appropriate circumstances provide something more flexible and less rigid than the process available under formal rescue regimes. Many cases of corporate financial difficulty require an earlier and more active response from key bank and financial institution creditors, which is normally not possible under formal rescue regimes. It is less confrontational and so provides a better environment for market negotiations, both between creditors and the debtor and among creditors themselves. It is perceived to carry a lesser stigma than the formal process.

\textsuperscript{1} For instructive and entertaining descriptions of the workout process, see Michael Mortitz & Barrett Seaman, \textit{Going for Broke: The Chrysler Story} (1981); Tom Wolfe, \textit{A Man in Full}, Chapter 2 (1998).
Some countervailing considerations are heard. It may be thought that informal arrangements are not sufficiently transparent and may advantage large and sophisticated creditors. They may also be employed, as they were said to be in the United States during the Great Depression, as a device by which certain groups of corporate stakeholders could “squeeze” other groups, taking more of the enterprise’s value for themselves.\(^2\) On the other hand, when informal procedures are used to affect primarily the interests of lenders and other sophisticated creditors, those concerns are largely avoided and the benefits of the informal approach are more difficult to deny.

An informal workout probably would not be attempted unless a number of well-defined conditions were present; for example, a significant amount of debt should be owned by a number of bank or financial institution creditors, the debtor should be unable to service that debt, and it should be possible to carry out all the arrangements without the need for a formal moratorium. Further, it almost goes without saying, there should be agreement to carry out such discussions not only between the debtor and the creditors but also among creditors.

INSOL International, in a document endorsed by the World Bank, the Bank of England, and the British Bankers’ Association, expressed considerable support for informal workout procedures in the following terms:\(^3\)

During the last thirty years there has been a growing recognition amongst the world’s financial institutions that, as creditors, they can achieve better returns through supporting an orderly and expeditious rescue or workout of a business in financial difficulty than by forcing it into formal insolvency. This realization has coincided with efforts by certain regulatory and official authorities to encourage financial institutions to co-operate with each other when dealing with debtors to whom they are collectively exposed, particularly in cases of large exposures.

In their document, INSOL International identified eight principles to ensure the best practice in multi-creditor workouts. In brief, these principles would require that all relevant creditors should be prepared to

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\(^3\) See e.g., Statement of Principles for a Global Approach to Multi Creditor Workouts, INSOL International 2000 at p. 4.