GETTING THE DEAL THROUGH

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Philippines

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1 Legislation

What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The applicable law is Republic Act No. 10142, known as the Financial Rehabilitation and Insolvency Act of 2010 (FRIA). The FRIA took effect on 18 July 2010.

A debtor is considered insolvent if it is unable to pay its liabilities as they fall due in the ordinary course of business or has liabilities that are greater than its assets (FRIA, section 4(p)).

2 Courts

What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Pursuant to the Financial Rehabilitation Rules of Procedure (2013) (the FR Rules), regional trial courts with jurisdiction over the city or municipality in which the principal office of the alleged debtor is located were designated to hear and determine petitions involving rehabilitation plans, suspension of payments, liquidation, and recognition of foreign proceedings. The FR Rules also allow the Court of Appeals to review the regional trial court's approval or disapproval of the rehabilitation plan, orders issued after the approval of the rehabilitation plan, or the judgment in any action involving out-of-court or informal restructurings or workout agreements (OCRA) or rehabilitation plans. The Court of Appeals' decision may be taken to the Supreme Court for review.

3 Excluded entities and excluded assets

What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Banks, insurance companies and pre-need companies are not covered by the FRIA. The rehabilitation of banks, insurance companies and pre-need companies is governed by Republic Act No. 7653 (the New Central Bank Act), Presidential Decree No. 612 (Insurance Code of the Philippines) and Republic Act No. 9829 (Pre-Need Code of the Philippines), respectively (FRIA, section 5).

The following assets are excluded from insolvency proceedings and are exempt from execution:

- the insolvent debtor's family home as provided by law, or the homestead in which he or she resides, and land necessarily used in connection therewith;
- ordinary tools and implements personally used by him or her in his or her trade, employment or livelihood;
- three horses, or three cows, or three carabaos or other beasts of burden at the option of the judgment obligor as may be necessary in his or her ordinary occupation;
- his or her necessary clothing and articles for ordinary personal use, excluding jewellery;
- household furniture and utensils necessary for housekeeping, and used for that purpose by the judgment obligor and his or her family, such as the judgment obligor may select, of a value not exceeding 100,000 Philippine pesos;
- provisions for individual or family use sufficient for four months;
- the professional libraries and equipment of judges, lawyers, physicians, pharmacists, dentists, engineers, surveyors, clergymen, teachers and other professionals, not exceeding 300,000 Philippine pesos in value;
- one fishing boat and accessories not exceeding the total value of 100,000 Philippine pesos owned by a fisherman and by the lawful use of which he or she earns his livelihood;
- as much of the salaries, wages or earnings of the insolvent debtor for his or her personal services within the four months preceding the levy as are necessary for the support of his or her family;
- lettered gravestones;
- monies, benefits, privileges or annuities accruing or in any manner growing out of any life insurance;
- the right to receive legal support, or money or property obtained as such support, or any pension or gratuity from the government; and
- properties specially exempt by law (Rules of Court rule 39 section 13; FRIA section 130).

4 Protection for large financial institutions

Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No. However, the following laws provide a government guarantee in favor of certain institutions:

- The Social Security Act of 1954 guarantees the solvency of the Social Security System;
- Presidential Decree No. 1080 (1977) guarantees the obligations of the Trade & Investment Development Corporation of the Philippines, also known as the Philippine Export-Import Credit Agency;
- Presidential Decree No. 690 (1975) guarantees the payment of bonds, debentures, collaterals, notes or such other obligations incurred by the Southern Philippines Development Administration; and
- Presidential Decree No. 1770 (1981) guarantees the obligations of the National Food Authority upon approval of the President.

5 Secured lending and credit (immoveables)

What principal types of security are taken on immoveable (real) property?

The principal type of security taken over immoveable property is the real estate mortgage.

6 Secured lending and credit (moveables)

What principal types of security are taken on moveable (personal) property?

The principal types of security taken over personal property are the chattel mortgage and the pledge.

7 Unsecured credit

What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor must file a civil action in court for collection of the debt. At the commencement of the action, or at any time prior to the judgment, the creditor may apply for the issuance of a writ of preliminary attachment on the debtor's assets, but only on limited specified grounds (eg, if the debtor is about to leave the Philippines with the intent to defraud creditors, or is guilty of fraud in contracting or performing the obligation in regards to which the action is brought).

Debt-collection suits are often protracted and expensive. It may take several years before a judgment is rendered, and the judgment of the trial court can be appealed all the way to the Supreme Court.

Foreign corporations doing business here are required to obtain the appropriate licence. Otherwise, they will not be allowed to initiate or intervene in any judicial action in the Philippines. However, a foreign corporation is allowed to sue even without a licence on an isolated transaction.

8 Voluntary liquidations

What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Voluntary liquidation is initiated by an insolvent debtor via a verified petition, or a verified motion in a court-supervised or pre-negotiated rehabilitation proceedings (FRIA, section 90).

If the petition or motion is meritorious, the court will issue a liquidation order, which shall, among other things:

- declare the debtor insolvent;
- order the liquidation of the debtor and, in the case of a juridical debtor, declare it as dissolved;
- order the sheriff to take possession and control of all the property of the debtor, except those that may be exempt from execution;
- direct payments of any claims and conveyance of any property due the debtor to the liquidator;
- prohibit payments by the debtor and the transfer of any property by the debtor;
- direct all creditors to file their claims with the liquidator within the period set by the rules of procedure; and
- set the case for hearing for the election and appointment of the liquidator (FRIA, section 112).

9 Involuntary liquidations

What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Three or more creditors with an aggregate claim of at least 1 million Philippine pesos or at least 25 per cent of the subscribed capital stock or partners' contributions, whichever is higher, may initiate liquidation proceedings against an insolvent debtor by filing a verified petition for liquidation with the court, or a verified motion in a court-supervised or pre-negotiated rehabilitation proceeding. The petition or motion must show that:

- there is no genuine issue of fact or law in the claim of the petitioner, and that the due and demandable payments thereon have not been made for at least 180 days or that the debtor has failed generally to meet its liabilities as they fall due; and
- there is no substantial likelihood that the debtor may be rehabilitated (FRIA, section 91).

Rehabilitation proceedings may also be converted into liquidation proceedings:

- when the rehabilitation court finds that the debtor is insolvent and there is no substantial likelihood for the debtor to be successfully rehabilitated;
- when the rehabilitation plan is not confirmed by the rehabilitation court within one year from filing of the petition;
- when the rehabilitation proceedings is terminated due to failure of rehabilitation or dismissal of the rehabilitation petition for reasons other than technical grounds;
- at any time during the pendency of or after court-supervised or pre-negotiated rehabilitation proceedings, upon motion of the debtor or of three or more creditors whose claims are at least either 1 million Philippine pesos or at least 25 per cent of the subscribed capital stock or of the debtor's contribution in the partnership, whichever is higher; or
- if the court determines that the debtor or creditors supporting the pre-negotiated rehabilitation plan acted in bad faith, or that the objection to the petition or rehabilitation plan is not curable. (FRIA, section 91; FR Rules rule 2, sections 17(C), 70, 73, 74, and rule 3, section 7).

As in cases of voluntary liquidations, the court will issue a liquidation order if the petition or motion is meritorious (FRIA, section 112).

10 Voluntary reorganisations

What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Court-supervised rehabilitation

An insolvent debtor may file a verified petition for rehabilitation when approved by the owner in the case of a sole proprietorship, or by a majority of the partners in the case of a partnership or, in the case of a corporation, by a majority vote of the board of directors or trustees and authorised by the vote of the stockholders representing at least two-thirds of the outstanding capital stock, or of the members, in a stockholders' or members' meeting duly called for the purpose. The petition must establish the insolvency of the debtor and the viability of its rehabilitation (FRIA, section 12, FR Rules rule 2, section 1).

The verified petition should contain the following:

- the name, business and principal address and other addresses of the debtor;
- the nature of the business and principal activities of the debtor, and the addresses where these activities are conducted;
- the history of the debtor;
- the fact and the cause of the debtor's insolvency;

- the specific relief sought;
- the grounds upon which the petition is based;
- all pending actions or proceedings by or against the debtors and the courts or tribunals where they are pending;
- the threats or demands to enforce claims or liens against the debtors;
- the manner by which the debtor may be rehabilitated and how such rehabilitation may benefit the general body of creditors, employees and stockholders; and
- the exact addresses at which documents regarding the debtor and the proceedings may be reviewed and copied (FR Rules, rule 2 section 2(A)).

The petition must also be accompanied by financial statements and schedules, inventory of assets, rehabilitation plan, responses to questions on the debtor's financial condition, a list of at least three nominees for rehabilitation receiver, and other supporting documents, under FR Rules rule 2, section 2(B).

If the court finds the petition to be sufficient in form and substance, it will issue a commencement order, which shall, among other things:
- appoint a rehabilitation receiver;
- summarise the requirements and deadlines for creditors to establish their claims against the debtor;
- prohibit suppliers of goods or services from withholding supply for as long as the debtor makes prompt payments;
- prohibit the debtor from making any payment of its outstanding liabilities; and
- issue a stay or suspension order (FRIA, section 16, FR Rules rule 2, section 7).

The commencement order also:
- prohibits and renders null and void extrajudicial process or activity to seize property, sell encumbered property or otherwise attempt to collect on or enforce a claim against the debtor, after the commencement date, unless otherwise allowed under the FRIA;
- renders null and void any set-off, after the commencement date, of any debt owed to the debtor by any of the debtor's creditors; and
- renders null and void the perfection, after the commencement date, of any lien against the debtor's properties (FRIA, section 17, FR Rules rule 2, section 9).

Imposition of national and local taxes and fees, penalties and surcharges are also waived from issuance of the commencement order until approval of the rehabilitation plan or dismissal of the petition (FRIA, section 19).

Pre-negotiated rehabilitation

An insolvent debtor, by itself or jointly with any of its creditors, may file a verified petition with the court for the approval of a pre-negotiated rehabilitation plan, together with an affidavit showing the written endorsement or approval by creditors holding at least two-thirds of the total liabilities of the debtor, including secured creditors holding more than 50 per cent of the total secured claims and unsecured creditors holding more than 50 per cent of the total unsecured claims (FRIA, section 76; FR Rules rule 3, section 1).

The petition must contain the statements required in a petition for rehabilitation under court-supervised rehabilitation proceedings and include the following documents:
- a schedule of debts and liabilities which lists all the creditors of the debtor;
- an inventory of assets.
- a summary of disputed claims against the debtor and a report on the provisioning of funds to account for appropriate payments should any such claims be ruled valid or their amounts adjusted;
- an affidavit of general financial condition containing answers to the questions or matters prescribed in Annex A of the FR; and
- the pre-negotiated rehabilitation plan, including the names of at least three qualified nominees for rehabilitation receiver (FR Rules rule 3, section 1).

If the court finds the petition to be sufficient in form and substance, it will issue an order, which shall, among other things:
- declare that the debtor is under rehabilitation;
- appoint a rehabilitation receiver, if provided under the plan; and
- issue a stay or suspension order (FRIA, section 77; FR Rules rule 3, section 2).

Out-of-court or informal restructuring or workout agreement or rehabilitation plan

This may be done if:
- the debtor agrees to the out-of-court or informal restructuring or workout agreement or rehabilitation plan (OCRA); and
- the agreement or plan is approved by:
  - creditors representing at least 67 per cent of the secured obligations;
  - creditors representing at least 75 per cent of the unsecured obligations; and
  - creditors holding at least 85 per cent of the total liabilities, secured and unsecured (FRIA, section 84, FR Rules rule 4, section 1(A)).

The OCRA must be published once a week for at least three consecutive weeks in a newspaper of general circulation in the Philippines (FR Rules rule 3, section 1(B)).

11 Involuntary reorganisations

What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Any creditor or group of creditors with a claim of, or the aggregate of whose claims is, at least 1 million Philippine pesos or at least 25 per cent of the subscribed capital stock or partners' contributions, whichever is higher, may initiate involuntary rehabilitation proceedings against the debtor by filing a verified petition for rehabilitation with the court if:
- there is no genuine issue of fact or law in the claim of the petitioner and that the due and demandable payments thereon have not been made for at least 60 days;
- the debtor has failed generally to meet its liabilities as they fall due; or
- a creditor, other than the petitioner, has initiated foreclosure proceedings against the debtor that will prevent the debtor from paying its debts as they become due or will render it insolvent (FRIA, section 13, FR Rules rule 2, sections 4 and 5).

The verified petition must contain the following:
- the name, business, and principal address and other known addresses of the debtor;
- the nature of the business and the principal activities of the debtor;
- the circumstances sufficient to support a petition to initiate involuntary rehabilitation proceedings under this Rule;
- the specific relief sought under this rule;
- a rehabilitation plan;
- the names of at least three nominees to the position of rehabilitation receiver, as well as their qualifications, office and email addresses;
- the exact addresses at which documents regarding the debtor and the proceedings may be reviewed and copied, if known to the petitioners; and

- documents showing that there is substantial likelihood that the debtor may be rehabilitated (FR Rules rule 2, section 6).

Similarly to a court-supervised voluntary rehabilitation, the court will issue a commencement order if the petition is sufficient in form and substance (FRIA, section 15).

12 Mandatory commencement of insolvency proceedings

Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result?

There are no instances where companies are required to commence insolvency proceedings under the FRIA.

13 Doing business in reorganisations

Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities?

The debtor may carry on its ordinary business during the rehabilitation, and suppliers of goods or services are prohibited from withholding supply to the debtor for as long as the debtor makes prompt payments (FRIA, section 16). For purposes of continuing the business, the management of the debtor shall remain with the existing management, subject to applicable laws and agreements, if any, on the election or appointment of directors, managers or managing partner. However, all disbursements, payments or sale, disposal, assignment, transfer or encumbrance of property, or any other act affecting title or interest in property, will be subject to the approval of the rehabilitation receiver and/or the court (see discussion in question 16 on sale of assets) (FRIA, section 47).

The court may, upon motion of any interested party, appoint and direct the rehabilitation receiver or a management committee to assume the powers of management of the debtor if:

- there is actual or imminent danger of dissipation, loss, wastage or destruction of the debtor's assets or other properties;
- business operations of the debtor are paralysed; or
- there is gross mismanagement of the debtor, or fraud or other wrongful conduct on the part of, or gross or wilful violation of the FRIA by, existing management of the debtor or the owner, partner, director, officer or representative in management of the debtor (FRIA, section 36; FR Rules rule 2, section 31).

14 Stays of proceedings and moratoria

What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The commencement order in rehabilitation proceedings includes a stay or suspension order that suspends all actions or proceedings, in court or otherwise, for the enforcement of claims against the debtor and suspends all actions to enforce any judgment, attachment or other provisional remedies against the debtor (FRIA, section 16(q); FR Rules rule 2, section 8(v)). Attempts to seek legal or other recourse against the debtor outside the rehabilitation proceedings shall be sufficient to support a finding of indirect contempt of court (FRIA, section 17, FR Rules rule 2, section 9).

The court, upon motion or recommendation of the rehabilitation receiver, may allow a secured creditor to enforce his security or lien, or foreclose upon property of the debtor securing its claim, if the said property is not necessary for the rehabilitation of the debtor (FRIA, section 60; FR Rules rule 2, section 59). The court, on motion or motu proprio (ie, on its own), may also terminate, modify or set conditions for the continuance of suspension of payment, or relieve a claim from the coverage thereof, upon showing that:

- a creditor does not have adequate protection over property securing its claim; or
- the value of a claim secured by a lien, on property which is not necessary for rehabilitation of the debtor, exceeds the fair market value of the said property (FRIA, section 61; FR Rules rule 2, section 60).

In liquidation proceedings, no separate action for the collection of an unsecured claim is allowed after the issuance of the liquidation order. Pending actions will be transferred to the liquidator for him to accept and settle or contest. If the liquidator contests or disputes the claim, the court will allow, hear and resolve such contest except when the case is already on appeal. In such a case, the suit may proceed to judgment, and any final and executory judgment therein for a claim against the debtor shall be filed and allowed in the court. Furthermore, no foreclosure proceeding is allowed for a period of 180 days from issuance of the liquidation order (FRIA, section 113).

The FRIA provides that the liquidation order shall not affect the right of a secured creditor to enforce his lien in accordance with the applicable contract or law (FRIA, section 114).

15 Post-filing credit

May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

As regards liquidation, there is no specific provision in the FRIA permitting or prohibiting the debtor from obtaining secured or unsecured loans or credit. However, sections 113 (on effects of the liquidation order) and 119 (on the powers, duties and responsibilities of the liquidator) of the FRIA appear to imply that a debtor in liquidation may not obtain such loans or credit. According to section 113, the juridical debtor shall be deemed dissolved upon the issuance of the liquidation order. Furthermore, the section states that legal title to and control of all the assets of the debtor, except those that may be exempt from execution, shall be deemed vested in the liquidator or, pending his election or appointment, with the court. Section 119 does not expressly authorise the liquidator to obtain such loans or credit.

With respect to rehabilitation, section 55 of the FRIA and rule 2, section 54 of the FR Rules provide that a debtor may perform the following acts in order to enhance its rehabilitation:

- enter into credit arrangements;
- enter into credit arrangements, secured by mortgages of its unencumbered property or secondary mortgages of encumbered property with the approval of senior secured parties with regard to the encumbered property; or
- incur other obligations as may be essential to rehabilitation.

The debtor may do these with the approval of the court and upon the recommendation of the rehabilitation receiver.

Section 55 of the FRIA and rule 2, section 54 of the FR Rules further state that the payment of the foregoing obligations shall be considered administrative expenses. On the other hand, section 16(l) of the FRIA and rule 2, section 8(p) of the FR Rules state that the commencement order shall authorise the payment of administrative expenses as they become due. Consequently, the credit arrangements or obligations obtained by the debtor under section 55 of the FRIA may be said to be given priority to the extent that they are to be paid as they become due.

16 Set-off and netting

To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

With respect to liquidation, the FRIA provides that a debt shall be offset against another debt if the insolvent debtor and a creditor are mutually debtor and creditor of each other (section 124). The liquidation proceedings shall only include the balance, if any, of the set-off.

As regards court-supervised rehabilitation, it appears that the right of set-off may be exercised only prior to the commencement of the rehabilitation proceedings. The issuance by the court of a commencement order shall serve as the legal basis for rendering null and void any set-off after the commencement date of the rehabilitation proceedings (FRIA, section 17(c); FR Rules rule 2, section 9(C)). The commencement date of the rehabilitation proceedings refers to the date on which the court issues the commencement order, which, however, shall be retroactive to the date of the filing of the petition for voluntary or involuntary proceedings (FRIA, section 4(d); FR Rules rule 1, section 5(e)). In this connection, under the old law, the stay order was not expressly given any retroactive effect.

17 Sale of assets

In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In rehabilitation, the debtor may use or dispose of funds or property in the ordinary course of business or if necessary to finance the administrative expenses of the rehabilitation proceedings (FRIA, section 48; FR Rules rule 2, section 47).

Outside the ordinary course of business, unencumbered assets of the debtor may be sold but only with court authorisation, upon application of the rehabilitation receiver. The application must show that the property, by its nature or because of other circumstance, is perishable, costly to maintain, susceptible to devaluation or otherwise in jeopardy (FRIA, section 49; FR Rules rule 2, section 48). The court may also authorise the sale of unencumbered assets:

- if such are in the interest of administering the debtor and facilitating the preparation and implementation of a rehabilitation plan;
- in order to provide a substitute lien, mortgage or pledge of property under the FRIA;
- for payments made to meet administrative expenses as they arise;
- for payments to victims of quasi-delicts (ie, torts) upon a showing that the claim is valid and the debtor has insurance to reimburse the debtor for the payments made;
- for payments made to repurchase property of the debtor that is auctioned off in a judicial or extrajudicial sale under the FRIA; or
- for payments made to reclaim property of the debtor held pursuant to a possessory lien (FRIA, section 52; FR Rules rule 2, section 51).

Meanwhile, sale of encumbered property of the debtor, or property of others held by the debtor, where there is a security interest pertaining to third parties under a financial, credit or other similar transactions may be done with court authorisation, upon application of the rehabilitation receiver, with the consent of the affected owners of the property or secured creditors, and after notice and hearing. The court must determine that:

- such sale, transfer, conveyance or disposal is necessary for the continued operation of the debtor's business; and
- the debtor has made arrangements to provide a substitute lien or ownership right that provides an equal level of security for the counterparty's claim or right (FRIA, section 50; FR Rules rule 2, section 49).

In liquidation, the liquidator may sell the unencumbered assets of the debtor and convert the same into money. The sale shall be made at public auction. However, a private sale may be allowed with the approval of the court if:

- the goods to be sold are of a perishable nature, or are liable to quickly deteriorate in value, or are disproportionately expensive to keep or maintain; or
- the private sale is in the best interests of the debtor and his creditors.

With the approval of the court, unencumbered property of the debtor may also be conveyed to a creditor in satisfaction of his claim or part thereof (FRIA, section 131).

There appears to be no legal prohibition against 'stalking horse' bids or credit bidding in the sale of an insolvent debtor's assets.

18 Intellectual property assets in insolvencies

May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The authority of the IP licensor or owner to terminate the debtor's right to use it when an insolvency case is opened shall depend on the terms and conditions of their contract, subject to the stay order, which, as discussed in question 14 above, retroacts to the date of the filing of the petition for voluntary or involuntary proceedings.

Thus, the contract between the IP licensor or owner and the debtor will be subject to the provisions of the FRIA relating to contracts of the debtor. In rehabilitation proceedings, the debtor may choose to confirm a contract within 90 days following the commencement of the rehabilitation proceedings (FRIA, section 57; FR Rules rule 2, section 8(U)). The contracts which are not confirmed within the said period shall be deemed terminated (FRIA, section 57; FR Rules rule 2, section 8(U). It appears that the debtor may continue using the IP rights only if the licence contract is confirmed. The debtor and the IP licensor or owner shall respect the terms and conditions of the confirmed licence contract (FRIA, section 62(q); FR Rules rule 2, section 61(R)).

In liquidation, all contracts of the debtor shall be deemed terminated and/or breached upon the issuance of a liquidation order, unless the liquidator, within 90 days from the date of his assumption of office, declares otherwise and that the contracting party agrees (FRIA, section 113). As such, the debtor may continue using the IP rights only if the licence contract is declared valid and subsisting by the liquidator within the said 90-day period and the IP licensor or owner agrees.

The right of the debtor to use the IP is based on contract. The termination of the licence contract will thus extinguish the right of the debtor to use the IP.

19 Rejection and disclaimer of contracts in reorganisations

Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party?

Yes, a debtor can reject an unfavourable contract by not confirming the contract in a rehabilitation proceeding. All contracts not confirmed by the debtor, with the consent of the rehabilitation receiver, within 90 days following the commencement of the rehabilitation proceedings, are considered terminated. Claims for actual damages, if any, arising as a result of the election to terminate a contract shall be considered a pre-commencement claim against the debtor (FRIA, section 57; FR Rules rule 2, section 56).

20 Arbitration processes in insolvency cases

How frequently is arbitration used in insolvency proceedings? What limitations are there on the availability of arbitration in insolvency cases? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Under the old law, arbitration was generally not used in insolvency proceedings. Under the FRIA, however, with respect to court-supervised rehabilitation, any dispute involving the rehabilitation plan or the rehabilitation proceedings may be referred by the court to arbitration or other dispute-resolution mechanisms if doing so will help the court resolve the dispute more quickly, fairly and efficiently, and if it will not prejudice the one-year period for the confirmation of the rehabilitation plan (FRIA, section 26; FR Rules rule 2, section 18).

As regards liquidation, the FRIA does not specifically provide for the referral of a dispute involving the liquidation plan or the liquidation proceedings to arbitration or other dispute resolution mechanisms.

Unless the rehabilitation or liquidation court allows arbitration proceedings to continue, the arbitration proceedings shall be subject to the stay or suspension order.

Further, parties may submit disputes that arise in an insolvency case to arbitration even after the case is opened (Arbitration Law, section 2) The court can refer the dispute to arbitration if it is covered by an arbitration agreement and if at least one party requests such referral (but not later than the pretrial conference) or if both parties consent (Alternative Dispute Resolution Act of 2004, section 24).

21 Successful reorganisations

What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Mandatory features of a rehabilitation plan

According to section 62 of the FRIA, a rehabilitation plan must contain the following minimum features:

- specify the underlying assumptions, the financial goals and the procedures proposed to accomplish such goals;
- compare the amounts expected to be received by the creditors under the rehabilitation plan with those that they will receive if liquidation ensues within the next 120 days;
- contain information sufficient to give the various classes of creditors a reasonable basis for determining whether supporting the plan is in their financial interest when compared to the immediate liquidation of the debtor, including any reduction of principal interest and penalties payable to the creditors;
- establish classes of voting creditors;
- establish subclasses of voting creditors if prior approval has been granted by the court;
- indicate how the insolvent debtor will be rehabilitated including, but not limited to, debt forgiveness, debt rescheduling, reorganisation or quasi-reorganisation, *dacion en pago* (ie, payment by assignment of property), debt-equity conversion and sale of the business (or parts of it) as a going concern, or setting-up of a new business entity or other similar arrangements as may be necessary to restore the financial well-being and viability of the insolvent debtor;
- specify the treatment of each class or subclass of voting creditors;
- provide for equal treatment of all claims within the same class or subclass, unless a particular creditor voluntarily agrees to less favourable treatment;
- ensure that the payments made under the plan follow the priority established under the provisions of the Civil Code on concurrence and preference of credits and other applicable laws;
- maintain the security interest of secured creditors and preserve the liquidation value of the security unless such has been waived or modified voluntarily;
- disclose all payments to creditors for pre-commencement debts made during the proceedings and the justifications thereof;
- describe the disputed claims and the provisioning of funds to account for appropriate payments should the claim be ruled valid or its amount adjusted;
- identify the debtor's role in the implementation of the plan;
- state any rehabilitation covenants of the debtor, the breach of which shall be considered a material breach of the plan;
- identify those responsible for the future management of the debtor and the supervision and implementation of the plan, their affiliation with the debtor and their remuneration;
- address the treatment of claims arising after the confirmation of the rehabilitation plan;
- require the debtor and its counterparties to adhere to the terms of all contracts that the debtor has chosen to confirm;
- arrange for the payment of all outstanding administrative expenses as a condition to the plan's approval unless such condition has been waived in writing by the creditors concerned;
- arrange for the payment of all outstanding taxes and assessments, or an adjusted amount pursuant to a compromise settlement with the Bureau of Internal Revenue (BIR) or other applicable tax authorities;
- include a certified copy of a certificate of tax clearance or evidence of a compromise settlement with the BIR;
- include a valid and binding resolution of a meeting of the debtor's stockholders to increase the shares by the required amount in cases where the plan contemplates an additional issuance of shares by the debtor;
- state the compensation and status, if any, of the rehabilitation receiver after the approval of the plan; and
- contain provisions for conciliation and/or mediation as a prerequisite to court assistance or intervention in the event of any disagreement in the interpretation or implementation of the rehabilitation plan.

Additionally, the FR Rules require the following to be included in the rehabilitation plan:

- relevant foreign ownership limits or information, if any;
- material financial undertakings or commitments to support the rehabilitation plan;
- provisions for monitoring the implementation of the rehabilitation plan, including, requiring the rehabilitation receiver and/or debtor to make reports from time to time;
- the manner of its implementation, giving due regard to the interests of secured creditors such as the non-impairment of their security liens or interests; and

- such other relevant information as to enable a reasonable investor to make an informed decision on the feasibility of the rehabilitation plan (FR Rules rule 2, section 61).

Classification of creditors

The FRIA does not expressly provide for the criteria to be utilised in classifying creditors for purposes of the rehabilitation plan. However, section 42 of the FRIA and rule 2, section 39 of the FR Rules recognise several classes of creditors:
- secured creditors;
- unsecured creditors;
- trade creditors and suppliers; and
- employees of the debtor.

The above-mentioned list does not exhaust all possible classification of creditors, and the rehabilitation plan may establish other classes of voting creditors (FRIA, section 62(d); FR Rules rule 2, section 61(D)).

Process for approval of rehabilitation plan

The process for approval of a rehabilitation plan depends on the nature of the rehabilitation proceeding, in particular:
- court-supervised rehabilitation;
- pre-negotiated rehabilitation; and
- out-of-court or informal restructuring agreements or rehabilitation plans.

Court-supervised rehabilitation

Pursuant to section 64 of the FRIA, the rehabilitation receiver shall notify the creditors and stakeholders for the examination of the rehabilitation plan. Within 20 days from notification, the rehabilitation receiver shall convene the creditors for purposes of voting on the approval of the rehabilitation plan (FRIA, section 64; FR Rules rule 2, section 62). The rehabilitation plan must be approved by all classes of creditors whose rights are adversely affected by the said plan. The rehabilitation plan is deemed to have been approved by a class of creditors if members of the class holding more than 50 per cent of the total claims of the class vote for the approval of the rehabilitation plan (FRIA, section 64; FR Rules rule 2, section 62).

If the rehabilitation plan is approved, the plan shall be submitted to the court for confirmation (FRIA, section 65; FR Rules rule 2, section 63). An objection may be filed by a creditor within 20 days from receipt of the court notice regarding the submission of the rehabilitation plan for confirmation (FRIA, section 66; FR Rules rule 2, section 64). The court shall confirm the rehabilitation plan '[i]f no objections are filed within the relevant period or, if objections are filed, the court finds them lacking in merit, or determines that the basis for the objection has been cured, or determines that the debtor has complied with an order to cure the objection' (FRIA, section 68; FR Rules rule 2, section 65).

Pre-negotiated rehabilitation

Upon the determination that the petition for the approval of a pre-negotiated rehabilitation plan is sufficient in form and substance, the court shall issue an order which shall, among other things, state that copies of the petition and the rehabilitation plan are available for examination and copying by any interested party (FRIA, section 77(f); FR Rules rule 3, section 2(F)). The court shall approve the rehabilitation plan within 10 days from the date of the second publication of the order, unless a verified objection is filed by a creditor or other interested party within eight days of the date of the second publication of the order (FRIA, section 78; FR Rules rule 3, section 4). The rehabilitation plan shall be deemed approved upon a court determination that the objection has no substantial merit, or that the same has been fixed (FRIA, section 80; FR Rules rule 3, section 7).

Moreover, the court shall have a maximum period of 120 days from the date of the filing of the petition to approve the rehabilitation plan. The rehabilitation plan shall be deemed approved in the event that the court does not act within the given period (FRIA, section 81; FR Rules rule 3, section 8).

Out-of-court or informal restructuring agreements or rehabilitation plans

Pursuant to section 84 of the FRIA and rule 4, section 1 of the FR Rules, an out-of-court or informal restructuring or workout agreement or rehabilitation plan shall qualify under the FRIA provided the following minimum requirements are satisfied:
- the debtor must agree to the out-of-court or informal restructuring or workout agreement or rehabilitation plan;
- it must be approved by creditors representing at least 67 per cent of the secured obligations of the debtor;
- it must be approved by creditors representing at least 75 per cent of the unsecured obligations of the debtor; and
- it must be approved by creditors holding at least 85 per cent of the total liabilities, secured and unsecured, of the debtor.

Release of non-debtor parties

The FRIA does not expressly provide for the release of non-debtor parties from liability and the circumstances for such release. It must be noted, however, that the rehabilitation plan must aim to restore 'the financial well-being and viability of an insolvent debtor' (FRIA, section 4(ii); FR Rules rule 2, sections 61(f) and 66).

22 Expedited reorganisations

Do procedures exist for expedited reorganisations?

The FRIA does not expressly provide for expedited reorganisations or rehabilitations. It does, however, recognise and permit pre-negotiated rehabilitation plans and allows the court or the rehabilitation receiver to authorise the creditors' committee in a court-supervised rehabilitation to perform such other tasks and functions as may be defined by the procedural rules to facilitate the rehabilitation process (FRIA, section 43; FR Rules rule 2, section 42). The FR Rules also provide that any order of the court is immediately executory (FR Rules rule 1, section 4).

23 Unsuccessful reorganisations

How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

According to section 74 of the FRIA, the following instances constitute failure of rehabilitation:
- dismissal of the petition by the court;
- the debtor fails to submit a rehabilitation plan;
- under the rehabilitation plan submitted by the debtor, there is no substantial likelihood that the debtor can be rehabilitated within a reasonable period;
- the rehabilitation plan or its amendment is approved by the court but in the implementation thereof, the debtor fails to perform its obligations thereunder, or there is a failure to realise the objectives, targets or goals set forth therein, including the timelines and conditions for the settlement of the obligations due to the creditors and other claimants;
- the commission of fraud in securing the approval of the rehabilitation plan or its amendment; and
- other analogous circumstances as may be defined by the rules of procedure.

Additionally, rule 2, section 73 of the FR Rules provide that the following instances shall also constitute failure of rehabilitation:
- a rehabilitation plan is not confirmed by the court;

- a determination that the rehabilitation plan may no longer be implemented in accordance with its terms, conditions, restrictions, or assumptions;
- where, after finding merit in the objections raised against the confirmation of the rehabilitation plan, the defect is not cured within such time as the court may order, or if the court determines that the debtor acted in bad faith, or that it is not feasible to cure the defect; and
- the debtor fails to comply with the FR Rules, the Rules of Court or any order of the court.

Section 74 of the FRIA and rule 2, section 73 of the FR Rules further provide that the court, upon breach or failure of the rehabilitation plan, may perform the following:
- issue an order directing that the breach be cured within a specified period of time, failing which the proceedings may be converted to a liquidation;
- issue an order converting the proceedings to a liquidation;
- allow the debtor or rehabilitation receiver to submit amendments to the rehabilitation plan, the approval of which shall be governed by the same requirements for the approval of a rehabilitation plan;
- issue any other order to remedy the breach consistent with the present regulation, other applicable law and the best interests of the creditors; or
- enforce the applicable provisions of the rehabilitation plan through a writ of execution.

24 Insolvency processes

During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

In the event that a petition or motion for liquidation is sufficient in form and substance, the court shall issue a liquidation order (FRIA, section 112). The liquidation order directs, among others, the publication of the petition or motion for liquidation in a newspaper of general circulation once a week for two consecutive weeks (FRIA, section 112(d)). Furthermore, the liquidation order directs all creditors to file their claims with the liquidator within the period set by the rules of procedure (FRIA, section 112(g)).

The FRIA does not expressly provide for the holding of meetings and the manner of calling meetings during liquidation proceedings.

It is the duty of the liquidator to prepare a registry of claims of secured and unsecured creditors, and to make such registry available for public inspection. The liquidator must also inform, through publication notice, the creditors and stakeholders of the debtor/individual debtor of the place and time for inspection of the registry of claims (FRIA, section 123).

Furthermore, it is the duty of the liquidator to make and keep a record of all monies received and all disbursements made by him or under his authority as liquidator (FRIA, section 121). The liquidator shall also render a quarterly report thereof to the court, which report shall be made available to all interested parties (FRIA, section 121). The liquidator shall also submit such reports as may be required by the court from time to time as well as a final report at the end of the liquidation proceedings (FRIA, section 121). Where a creditors' committee is created to assist the liquidator in the discharge of its functions, there appears to be no limitation on the information that a liquidator can provide the committee (FRIA, section 119). A creditor may, with the consent of the liquidator, initiate and prosecute an action for rescission or declaration of nullity of transactions entered into by the debtor or involving its assets in order to defraud creditors or give undue preference to creditors (FRIA, sections 127 and 128). The action may be instituted with leave of court if the liquidator does not consent to its filing or prosecution (FRIA, section 128). Where the action was initiated by the creditor, any benefit derived from the action belongs to the creditor to the extent of its claim and costs, and the surplus, if any, belongs to the estate (FRIA, section 128).

25 Enforcement of estate's rights

If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Under the FRIA, only the rehabilitation receiver or liquidator is entitled to sue and recover, with approval of the court, properties pertaining to the debtor (sections 31(f) and 119(a); FR Rules rule 2, section 26(F)). An exception is the action for rescission or declaration of nullity of transactions entered into by the debtor or involving its assets in order to defraud creditors or give undue preference to creditors which, as discussed in item 23 above, a creditor may initiate and prosecute, with the consent of the liquidator or with leave of court. Having said that, the Civil Code allows creditors to exercise all the debtor's rights and bring all actions of the latter to satisfy their claims (called accion subrogatoria; article 1177). This is pertinent in liquidation proceedings of an individual debtor who is liable with all property, present and future, for the fulfilment of his or her obligations (Civil Code article 2236) – that is, even after the termination of liquidation proceedings. The fruits of the remedies will belong to the creditors to the extent of their credit.

26 Creditor representation

What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

With respect to rehabilitation, a class of creditors may establish a creditors' committee (FRIA, section 42; FR Rules rule 2 section 39). Furthermore, a creditors' committee may be established by all the creditors acting as a body, and a representative from each class of creditors shall be a member of the creditors' committee (FRIA, section 42; FR Rules rule 2 section 39). The representative from each class shall be elected, and the rehabilitation receiver or his representative shall assist in the said election (FRIA, section 42; FR Rules rule 2, section 39).

It shall be the duty of the creditors' committee to assist the rehabilitation receiver in communicating with the creditors and shall be the principal liaison between the rehabilitation receiver and the creditors (FRIA, section 43; FR Rules rule 2, section 42). However, the creditors' committee does not have the authority to exercise or waive any right or give any consent on behalf of any creditor, unless specifically authorised in writing by such creditor (FRIA, section 43; FR Rules rule 2, section 42). The court or the rehabilitation receiver may assign other tasks to the creditors' committee to facilitate the rehabilitation proceedings (FRIA, section 43; FR Rules rule 2 section 42).

As regards liquidation, the liquidator may recommend to the court the creation of a creditors' committee that will assist him or her in the discharge of his or her functions (FRIA, section 119(g)). The creditors' committee shall have such powers as the court may deem just, reasonable and necessary (FRIA, section 119(g)).

The expenses of the creditors' committee incurred in the performance of its duties may be considered as administrative expenses (FR Rules section 42). Administrative expenses are paid as they become due, pursuant to the commencement order in a rehabilitation proceeding or the liquidation order (FRIA, sections 16(l) and

112(h); FR Rules rule 1, section 5(a) and rule 2, section 8(P)). The FRIA does not expressly provide for the retention of advisers by the creditors' committee.

27 Insolvency of corporate groups

In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

With respect to rehabilitation, a group of debtors may jointly file a petition for rehabilitation (FRIA, section 12; FR Rules rule 2, section 1). Section 4(n) of the FRIA specifically defines a group of debtors as strictly referring to any of the following:
- corporations that are financially related to one another as parent corporations, subsidiaries or affiliates;
- partnerships that are owned more than 50 per cent by the same person; or
- single proprietorships that are owned by the same person.

The petition for rehabilitation may be filed by a group of debtors when one or more of its members foresee the impossibility of meeting debts when they respectively fall due, and the financial distress would be likely to adversely affect the financial condition and/or operations of the other members of the group and/or the participation of the other members of the group is essential under the terms and conditions of the proposed rehabilitation plan (FRIA, section 12; FR Rules rule 2, section 1).

As a general rule, the debtor's assets and liabilities cannot be commingled or aggregated with those of another entity (FRIA, section 7). However, the commingling or aggregation of assets is permitted if the other entity is a related enterprise which is directly or indirectly owned or controlled by the same interests (FRIA, section 7; FR Rules rule 1, section 8). The commingling and aggregation must satisfy the following requisites:
- there was commingling in fact of assets and liabilities of the debtor and the related enterprise prior to the commencement of the proceedings;
- the debtor and the related enterprise have common creditors and it will be more convenient to treat them together rather than separately;
- the related enterprise voluntarily accedes to join the debtor as party petitioner and to commingle its assets and liabilities with the debtor's; and
- the consolidation of assets and liabilities of the debtor and the related enterprise is beneficial to all concerned and promotes the objectives of rehabilitation (FRIA, section 7; FR Rules rule 1, section 8).

The FRIA does not expressly provide for the transfer of assets from an administration in this jurisdiction to an administration in another jurisdiction. It should be noted, however, that the UNCITRAL Model Law on Cross-border Insolvency has been adopted as part of the FRIA (FRIA, section 139). Furthermore, section 141(b) of the FRIA states that the court may issue an order requiring the surrender of property of a foreign entity located in this jurisdiction to its foreign representative, in relation to an insolvency or rehabilitation proceeding in another jurisdiction. Where the court recognises a foreign proceeding, the court may, at the request of the foreign representative, entrust the distribution of all or part of the debtor's assets located in the Philippines to the foreign representative or another person designated by the court, provided that the court is satisfied that the interests of local creditors are adequately protected (rule 5 of the FR Rules).

With respect to liquidation, the FRIA does not expressly provide for the filing of a petition for liquidation by a group of debtors.

28 Claims and appeals

How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditor claims are initially submitted to the court through the petition for rehabilitation or liquidation which contains a schedule of the debtor's liabilities (for an out-of-court restructuring agreement, the claims are normally contained in the agreement itself). For court-supervised rehabilitation or liquidation, the rehabilitation receiver or liquidator is given 20 days from his or her appointment to accept applications for recognition of claims and establish a preliminary registry of claims (FRIA, sections 44, 123 and 125; FR Rules rule 2, section 44). After 30 days from the expiry of such period, interested parties may challenge such claims (FRIA, sections 45 and 125; FR Rules rule 2, section 45). The rehabilitation receiver or liquidator may disallow claims and a creditor may appeal the disallowance to the court (note that, in liquidation, there is no express provision for an appeal for disallowance, but it is still allowed under general procedural law; FRIA sections 46 and 126; the Judiciary Reorganisation Act of 1980 or Batas Pambansa Blg. 129 section 39).

There are no provisions on transfer of creditor claims under the FRIA. There are also no disclosure requirements or restrictions for credit transfer during insolvency under general laws (Civil Code articles 1300 to 1304 and articles 1624 to 1635). Having said that, an assignee of a creditor's claims will necessarily have to disclose the transfer if it wishes to be substituted for the creditor in the insolvency proceedings. Contingent or unliquidated claims can be recognised by the rehabilitation receiver or liquidator (FRIA, section 4(c) in relation to sections 44 and 123). The amounts of such claims are determined based on the evidence given by the creditors in their application for recognition (FRIA, sections 44 and 123).

29 Modifying creditors' rights

May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Generally, the court cannot change the priority of claims in rehabilitation or liquidation. This can only be done through a waiver of preference by the creditor. In rehabilitation cases, however, the priority of claims may be modified through confirmation of a rehabilitation plan which binds the debtor and all participating creditors (FRIA, section 69; FR Rules rule 2, section 67). While generally the rehabilitation plan requires approval of creditors (holding more than 50 per cent of the total claims), the court can nonetheless confirm the rehabilitation plan (despite creditor rejection) if all of the following circumstances are present:
- the rehabilitation plan complies with the requirements specified in the FRIA;
- the rehabilitation receiver recommends the confirmation of the rehabilitation plan;
- the shareholders, owners or partners of the juridical debtor lose at least their controlling interest as a result of the rehabilitation plan; and
- the rehabilitation plan would likely provide the objecting class of creditors with compensation which has a net present value greater than that which they would have received if the debtor were under liquidation (FRIA, section 64; FR Rules rule 2, section 62).

30 Priority claims

Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Philippine law classifies credits into three general categories:
- special preferred credits (Civil Code, articles 2241 and 2242);
- ordinary preferred credits (Civil Code, article 2244); and
- common credits (Civil Code, article 2245).

The special and ordinary credits are the major privileged and priority claims in liquidations and reorganisations (FRIA, section 133). The special preferred credits are the highest priority claims that attach as liens or encumbrances on the specific moveable or immoveable property to which they relate. Moreover, they are considered as 'mortgages or pledges of real or personal property, or liens within the purview of legal provisions governing insolvency' (Civil Code, article 2243). With reference to specific moveable property, they are the following:
- duties, taxes and fees due thereon to the state or any subdivision thereof;
- claims arising from misappropriation, breach of trust, or malfeasance by public officials committed in the performance of their duties, on the moveables, money or securities obtained by them;
- claims for the unpaid price of moveables sold, on said moveables, so long as they are in the possession of the debtor, up to the value of the same; and if the moveable has been resold by the debtor and the price is still unpaid, the lien may be enforced on the price; this right is not lost by the immobilisation of the thing by destination, provided it has not lost its form, substance and identity; neither is the right lost by the sale of the thing together with other property for a lump sum, when the price thereof can be determined proportionally;
- credits guaranteed with a pledge so long as the things pledged are in the hands of the creditor, or those guaranteed by a chattel mortgage, upon the things pledged or mortgaged, up to the value thereof;
- credits for the making, repair, safekeeping or preservation of personal property, on the moveable thus made, repaired, kept or possessed;
- claims for labourers' wages, on the goods manufactured or the work done;
- for expenses of salvage, upon the goods salvaged;
- credits between the landlord and the tenant, arising from the contract of tenancy on shares, on the share of each in the fruits or harvest;
- credits for transport, upon the goods carried, for the price of the contract and incidental expenses, until their delivery and for 30 days thereafter;
- credits for lodging and supplies usually furnished to travellers by hotel keepers, on the moveables belonging to the guest as long as such moveables are in the hotel, but not for money loaned to the guests;
- credits for seeds and expenses for cultivation and harvest advanced to the debtor, upon the fruits harvested;
- credits for rent for one year, upon the personal property of the lessee existing on the immoveable leased and on the fruits of the same, but not on money or instruments of credit; and
- claims in favour of the depositor if the depositary has wrongfully sold the thing deposited, upon the price of the sale (Civil Code, article 2241).

With respect to specific immoveable property and real rights, they are the following:
- taxes due upon the land or building;
- for the unpaid price of real property sold, upon the immoveable sold;
- claims of labourers, masons, mechanics and other workmen, as well as of architects, engineers and contractors, engaged in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works;
- claims of furnishers of materials used in the construction, reconstruction, or repair of buildings, canals or other works, upon said buildings, canals or other works;
- mortgage credits recorded in the registry of property, upon the real estate mortgaged;
- expenses for the preservation or improvement of real property when the law authorises reimbursement, upon the immoveable preserved or improved;
- credits annotated in the registry of property, in virtue of a judicial order, by attachments or executions, upon the property affected, and only as to later credits;
- claims of co-heirs for warranty in the partition of an immoveable among them, upon the real property thus divided;
- claims of donors or real property for pecuniary charges or other conditions imposed upon the donee, upon the immoveable donated; and
- credits of insurers, upon the property insured, for the insurance premium for two years (Civil Code, article 2242).

The enumeration above does not establish an order of preference. Such claims concur and are satisfied on a prorated basis (Civil Code article 2247). For special preferred credits, there is a two-tier order of preference: the first tier includes only taxes, duties and fees due to the Philippine state, and the second tier includes all other special preferred credits which are to be satisfied, pari passu and pro rata, out of any residual value of the specific property (ie, net of the taxes, duties and fees due to the Philippine state) (*Republic v Peralta*, GR No. 56568, 20 May 1987; *Development Bank of the Philippines v National Labor Relations Commission*, GR No. 86227, 19 January 1994). Thus only taxes, duties and fees due to the Philippine state will have priority over secured creditors. As a special case, if the debtor is a securities market participant, trade-related claims of its customers are deemed to have absolute priority over all other claims of whatever nature or kind in so far as trade-related assets are concerned (FRIA, section 136).

Unlike special preferred credits, ordinary preferred credits create no liens that attach to determinate property. Ordinary preferred credits only create rights in favour of certain creditors out of the 'free property' of the insolvent debtor (ie, the residual value of the debtor's assets when the special preferred credits are satisfied) in the order below:
- credits for services rendered the insolvent debtor by employees, labourers or household helpers for one year (as modified by article 110 of the Labour Code or Presidential Decree No. 442; *Republic v Peralta*);
- proper funeral expenses for the debtor, or children under his or her parental authority who have no property of their own, when approved by the court;
- expenses during the last illness of the debtor or of his or her spouse and children under his or her parental authority, if they have no property of their own;
- compensation due the labourers or their dependants under laws providing for indemnity for damages in cases of labour accident, or illness resulting from the nature of the employment;
- credits and advancements made to the debtor for support of himself or herself, and family, during the last year preceding the insolvency;
- support during the insolvency proceedings, and for three months thereafter;
- fines and civil indemnification arising from a criminal offence;
- legal expenses, and expenses incurred in the administration of the insolvent's estate for the common interest of the creditors, when properly authorised and approved by the court;

- taxes and assessments due to the national government, other than those mentioned in the Civil Code articles 2241(1) and 2242(1) (on special preferred credits);
- taxes and assessments due to any province, other than those referred to in the Civil Code articles 2241(1) and 2242(1) (on special preferred credits);
- taxes and assessments due to any city or municipality, other than those indicated in the Civil Code articles 2241(1) and 2242(1) (on special preferred credits);
- damages for death or personal injuries caused by a quasi-delict;
- gifts due to public and private institutions of charity or beneficence; and
- credits that, without special privilege, appear in a public instrument or in a final judgment, if they have been the subject of litigation. These credits shall have preference among themselves in the order of priority of the dates of the instruments and of the judgments, respectively.

Common credits are the ones that do not enjoy preference and are satisfied pro rata regardless of dates (Civil Code, article 2251 in relation to article 2245).

31 Employment-related liabilities in restructurings

What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

When employees are terminated in restructurings that are not due to 'serious business losses or financial reverses', the terminated employees are entitled to separation pay equivalent to one month's pay or at least one-half month's pay for every year of service, whichever is higher (Labor Code, section 283). However, if the termination is due to the employer's insolvency or liquidation (ie, due to serious business losses or financial reverses), the terminated employees are not entitled to separation pay (*Galaxie Steel Workers Union-NAFLU-KMU v. NLRC*, GR No. 165757, 17 October 2006; *Republic v Peralta*; *Cama et al v Joni's Food Services Inc*, GR No. 153021, 10 March 2004). During the employer's bankruptcy or liquidation, employee claims for wages and other monetary claims enjoy the highest priority as an ordinary preferred credit (see question 29; *Republic v Peralta*).

Termination is achieved by serving a written notice both on the workers and the Philippine Department of Labor and Employment at least one month before the intended date of termination.

32 Pension claims

What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

There is no provision in the FRIA or FR Rules that provides a specific treatment for pension-related claims. Further, pension-related claims are not specifically given preference based on the list of priority claims provided under question 30, unless the court considers the claims as credits for employee services rendered to the insolvent debtor, or if the agreement embodying the pension plan between the debtor and its employees appear in a public instrument.

33 Liabilities that survive insolvency proceedings

Do any liabilities of a debtor survive an insolvency or a reorganisation?

For a juridical debtor, no liabilities survive because the insolvent partnership or corporation is automatically dissolved upon liquidation (FRIA, sections 113(a), 134 and 135). Claims that survive in rehabilitation proceedings due to failure of rehabilitation or dismissal of the petition for rehabilitation are automatically carried over to liquidation proceedings and are therefore extinguished upon termination of the liquidation proceedings (FRIA, section 75; FR Rules rule 2, section 74).

34 Distributions

How and when are distributions made to creditors in liquidations and reorganisations?

Distributions are made to creditors pursuant to a rehabilitation or liquidation plan confirmed by the court or a duly approved out-of-court restructuring agreement (approved by the debtor and the creditors). Under the FRIA, the court is given one year from the filing of the petition to confirm a court-supervised rehabilitation plan (section 72) and 120 days for pre-negotiated rehabilitation (section 81); no period is mentioned under the statute for the approval of the liquidation plan. Once the rehabilitation or liquidation plan is confirmed or approved, the distribution may proceed in accordance thereto.

35 Transactions that may be annulled

What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Transactions entered into in fraud of creditors or which constitute undue preference of creditors before rehabilitation or liquidation proceedings are commenced may be rescinded or declared null and void (FRIA, sections 52, 58 and 127; FR Rules rule 2, sections 51 and 57; Civil Code, articles 1177, 1381(3) and 1382). There is a disputable presumption that the transactions were done with intent to defraud creditors if they:

- provide unreasonably inadequate consideration to the debtor and are executed within 90 days prior to the commencement date of the rehabilitation or liquidation;
- involve an accelerated payment of a claim to a creditor within 90 days prior to the commencement date of the rehabilitation or liquidation;
- provide security or additional security executed within the 90 days prior to commencement of the rehabilitation or liquidation;
- involve creditors, where a creditor obtained, or received the benefit of, more than its pro rata share in the assets of the debtor, executed at a time when the debtor was insolvent; or
- are intended to defeat, delay or hinder the ability of the creditors to collect claims where the effect of the transaction is to put assets of the debtor beyond the reach of creditors or to otherwise prejudice the interests of creditors (FRIA, sections 58 and 127; FR Rules rule 2, section 57).

Moreover, in rehabilitation proceedings, the court can rescind transactions entered into after the commencement of the rehabilitation if they are not in the ordinary course of business of the debtor except if made:

- to administer the debtor and facilitate the preparation and implementation of a rehabilitation plan;
- to provide a substitute lien, mortgage or pledge of property under this rule;
- to pay or meet administrative expenses as they arise;
- to pay victims of quasi-delicts upon a showing that the claim is valid and the debtor has insurance to reimburse the debtor for the payments made;
- to repurchase property of the debtor that is auctioned off in a judicial or extrajudicial sale under these Rules; or
- to reclaim or redeem property of the debtor held pursuant to a possessory lien (FRIA, section 52; FR Rules rule 2, section 51).

Rescission creates the obligation to return the things that were the object of the contract, together with their fruits, and the price with its interest. Rescission, however, cannot take place when the things that are the object of the contract are legally in the possession of third persons who did not act in bad faith. In this case, indemnity for damages may be demanded from the person causing the loss (Civil Code, article 1385).

36 Proceedings to annul transactions

Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The suspect period may be said to be 90 days from the commencement of the rehabilitation or liquidation proceedings. Transactions during this period are disputably presumed to have been done in fraud of creditors, or to constitute undue preference of creditors, and thus may be rescinded or declared null and void (see question 33.) The rescissible transactions may be challenged by both the rehabilitation receiver or liquidator and the creditors with the conformity of the rehabilitation receiver or liquidator. If the latter do not consent to the filing of such action, any creditor may seek leave of court to commence the rescissory action (FRIA, sections 59 and 128; FR Rules rule 2, section 58).

37 Directors and officers

Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The general rule is that obligations incurred by the corporation, acting through its directors, officers and employees, are its sole liabilities. However, solidary liability may be incurred under the following exceptional circumstances:

- when directors and trustees or, in appropriate cases, the officers of a corporation: (i) vote for or assent to patently unlawful acts of the corporation; (ii) act in bad faith or with gross negligence in directing the corporate affairs; (iii) are guilty of conflict of interest to the prejudice of the corporation, its stockholders or members, and other persons;
- when a director or officer has consented to the issuance of watered stocks or who, having knowledge thereof, did not forthwith file with the corporate secretary his written objection thereto; and
- when a director, trustee or officer has contractually agreed or stipulated to hold himself personally and solidarily liable with the corporation; or
- when a director, trustee or officer is made, by specific provision of law, personally liable for his corporate action. (*Uy v Villanueva*, GR No. 157851, 29 June 2007; Corporation Code section 31).

Philippine law also recognises the limited liability of corporations subject to the doctrine of piercing the corporate veil. Thus individual directors and officers are generally not liable for their corporation's obligations unless it is proved that they are using the corporate personality 'to defeat public convenience, justify wrong, protect fraud, or defend crime'. This is generally true for pre-bankruptcy actions by the company.

Under the FRIA, directors and officers of a debtor shall be liable if they, having notice of the commencement of the proceedings, or having reason to believe that proceedings are about to be commenced, or in contemplation of the proceedings, wilfully commit the following acts:

- dispose or cause to be disposed of any property of the debtor other than in the ordinary course of business or authorise or approve any transaction in fraud of creditors or in a manner grossly disadvantageous to the debtor or creditors; or
- conceal, or authorise or approve the concealment, from the creditors, or embezzles or misappropriates, any property of the debtor (FRIA, section 10; FR Rules rule 1, section 11).

38 Groups of companies

In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

A parent or affiliated corporation can be responsible for its subsidiaries or affiliates' liabilities when the corporate personality of the latter is used:

- to evade obligations to employees or used as a pretext to dismiss employees;
- to evade lawful obligations or a monetary judgment;
- as a mere alter ego of the parent or affiliated corporation;
- to defeat public convenience;
- to justify a wrong;
- to protect fraud;
- to defend crime;
- to confuse legitimate legal or judicial issues;
- to perpetrate deception or otherwise circumvent the law; or
- so organised and controlled and its affairs are so conducted as to make it merely an instrumentality, agency, conduit or adjunct of another corporation (*Park Hotel, et al v Soriano*, GR No. 171118, 10 September 2012).

For the subsidiary or affiliate to be considered a mere alter ego of the parent or affiliated corporation, all of the following circumstances must exist:

- there must be control – not mere stock control but complete domination – not only of finances, but of policy and business practice with respect to the transaction attacked and must have been such that the corporate entity had at the time no separate mind, will or existence of its own as to this transaction;
- such control must have been used to commit a fraud or wrong to perpetuate the violation of a statutory or other positive legal breach or duty, or a dishonest and an unjust act in contravention of a legal right; and
- said control and breach of duty must have proximately caused the injury or unjust loss complained of (*Times Trans Co Inc v Sotelo et al*, GR No. 163786, 16 February 2005).

39 Insider claims

Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There appears to be no restrictions against claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings under existing laws and regulations.

40 Creditors' enforcement

Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Before rehabilitation or liquidation proceedings, if the debtor's assets are encumbered and the security contract (eg, mortgage) provides for an extrajudicial foreclosure (coupled with a special power of attorney in favour of the creditor for the purpose of foreclosure), the creditor may take physical possession of the encumbered assets and foreclose them without court proceedings. Under Philippine law, the contracting parties can stipulate in their contract that in the case of default or non-payment of the debt the creditor may foreclose by selling the asset at a private sale, without previous advertisement or notice for the purpose of applying the proceeds thereof to the payment of the debt (*Philippine National Bank v Manila Investment & Construction Inc*, GR No. L-27132, 29 April 1971; *Philippine National Bank v De Poli*, GR No. 19026, 3 April 1923).

However, during rehabilitation or liquidation, any extrajudicial activity or process to seize property, sell encumbered property or otherwise attempt to collect or enforce a claim against the debtor, such as foreclosures, are stayed unless lifted by the court in rehabilitation proceedings (FRIA, sections 17(b) and 21; FR Rules rule 2 sections 9(B) and 11) or after the expiry of 180 days from the liquidation order in liquidation proceedings (FRIA, section 113(e)). Once the stay is lifted or has expired, creditors can seize the encumbered assets for the purposes of foreclosure outside of court proceedings.

41 Corporate procedures

Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Yes. Under the Corporation Code, a corporation may be dissolved either voluntarily or involuntarily. A corporation is deemed voluntarily dissolved when:
- the Securities and Exchange Commission (SEC) issues a certificate of dissolution based on the vote of the board of directors or trustees and the stockholders or members, where no creditors are affected;
- by judgment of the SEC after hearing of the petition for voluntary dissolution, where creditors are affected;
- upon SEC approval of the amendment of the articles of incorporation to shorten the corporate term, or the expiration of the corporate term, as the case may be; or
- upon SEC approval of the verified declaration of dissolution for approval in case of a corporation sole (Corporation Code, sections 115, 118–120).

On the other hand, involuntary dissolution may be effected by:
- expiration of the term provided in the original articles of incorporation;
- legislative enactment;
- failure to formally organise and commence the transaction of its business within two years of the date of incorporation; or
- order of the SEC (Corporation Code, sections 11, 22, and 121).

Corporate liquidation may be effected by:
- the corporation itself within three years of dissolution;
- a receiver duly appointed by the SEC upon rendering judgment dissolving the corporation (where creditors are affected) and directing the distribution of assets; and
- a trustee to whom the corporation had conveyed the corporate assets (Corporation Code, sections 119 and 122).

The SEC may order the dissolution of the corporation but the appropriate regional trial court has jurisdiction over the liquidation of the corporation (*Consuelo Metal Corp v Planters Bank Development Bank*, GR No. 152580, 26 June 2008). Unlike corporate dissolution proceedings, bankruptcy proceedings do not affect the existence of the corporation.

42 Conclusion of case

How are liquidation and reorganisation cases formally concluded?

Rehabilitation proceedings are formally concluded through a court order (initiated by motion by any stockholder or the rehabilitation receiver), either declaring a successful implementation of the rehabilitation plan or a failure of rehabilitation (FRIA, section 74; FR Rules rule 2, section 73).

Liquidation proceedings are formally concluded through a court order terminating the proceedings upon:
- determination that the liquidation has been completed according to the FRIA and other applicable laws; and
- evidence showing that the juridical debtor has been removed from the registry of legal entities in the Philippine Securities and Exchange Commission (FRIA, sections 134 to 135).

43 International cases

What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

In cross-border insolvency proceedings, insolvency courts in the Philippines can recognise a foreign proceeding and grant any necessary relief including those granted under the UNCITRAL Model Law on Cross-Border Insolvency and orders:
- suspending any action to enforce claims against the entity or otherwise seize or foreclose on property of the foreign entity located in the Philippines; or
- requiring the surrender of property of the foreign entity to the foreign representative. (FRIA, sections 140 and 141).

If necessary to protect the assets of the debtor or the interests of the creditors, the court may also, upon request of the foreign representative, grant appropriate relief including:
- suspending the right to transfer, encumber or otherwise dispose of any assets of the debtor;
- providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor's assets, affairs, rights, obligations or liabilities;
- entrusting the administration or realisation of all or part of the debtor's assets located in the Philippines to the foreign representative or another person designated by the court; or
- granting any additional relief that may be available to the rehabilitation receiver under the law or FR Rules; FR Rules rule 5, sections 5 and 13).

Subject to the rule of reciprocity and without prejudice to the ranking of claims in a proceeding under relevant laws, foreign creditors have the same rights regarding claims as creditors in the Philippines in cross-border insolvency proceedings (FR Rules rule 5, section 3(a)).

The FRIA expressly adopts the UNCITRAL Model Law, subject only to section 136 of the FRIA (on liquidation of a securities market participant) and the rules of procedure that may be adopted by the Supreme Court (FRIA, section 139). Accordingly, the treatment of foreign creditors in liquidations and reorganisations is based on the model law, which provides them direct access to Philippine courts (UNCITRAL Model Law chapter II).

A foreign court judgment or final order (foreign judgment) may be enforced in the Philippines through a petition to be filed with the appropriate regional trial court with territorial jurisdiction over either the plaintiff or the defendant, at the election of the plaintiff.

The effect of a judgment or final order of a tribunal of a foreign country, having jurisdiction to render the judgment or final order is as follows:
- in the event of a judgment or final order upon a specific object, the judgment or final order is conclusive upon the title to the object; and

Update and trends

The ease of doing business in the Philippines is set to improve with the Supreme Court finally promulgating the rules of procedure to govern proceedings brought under the FRIA, thereby stabilising the country's system of resolving insolvency matters.

- in the event of a judgment or final order against a person, the judgment or final order is presumptive evidence of a right as between the parties and their successors in interest by a subsequent title.

The foreign judgment may be repelled by evidence of lack of jurisdiction, want of notice to the party, collusion, fraud, or clear mistake of law or fact (Rule 39, section 48 of the 1997 Rules of Civil Procedure) In addition, the defendant may claim that the foreign judgment is contrary to morals and public policy.

To date, the Philippines is not signatory to any treaty on international insolvency or on the recognition of foreign judgments. Nonetheless, Philippine case law recognises that while there is no obligatory rule derived from treaties or conventions that require the Philippines to recognise foreign judgments, or allow the enforcement thereof, these are recognised pursuant to generally accepted principles of international law, which under the Constitution form part of Philippine laws (see *Mijares v Javier*, GR No. 139325, 12 April 2005).

44 Cross-border cooperation

Does your country's system allow cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts?

The FRIA expressly provides for the recognition of foreign insolvency or rehabilitation proceedings and the grant of relief in cross-border insolvency proceedings (FRIA, section 139). The court and rehabilitation receiver will cooperate to the maximum extent possible in all court-to-court communications for purposes of information and assistance (FR Rules rule 5; sections 18 and 19). Cooperation may be implemented by any appropriate means, including:

- appointment of a person or body to act at the discretion of the court;
- communication of information by any means considered appropriate by the court;
- coordination of the administration and supervision of the debtor's assets and affairs;
- approval or implementation by courts of agreements concerning the coordination of proceedings;
- coordination of concurrent proceedings regarding the same debtor;
- suspension of proceedings against the debtor;
- limiting the relief to assets that should be administered in a foreign proceeding pending in a jurisdiction other than the location in which the debtor has its principal place of business (foreign non-main proceeding) or information required in that proceeding; and
- implementation of the rehabilitation or reorganisation plan (FR Rules rule 5, section 20).

However, the FRIA (which adopted the UNCITRAL Model Law) was only recently enacted in 2010. Thus, there are no known examples yet of such cooperation under the FRIA.

45 Cross-border insolvency protocols and joint court hearings

In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

We are not aware of any cross-border insolvency protocols or other arrangements that the Philippines may have entered into with other countries. We are also not aware of Philippine courts communicating with or holding joint hearings with courts in other countries in cross-border cases.

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