Doing Business 2016

Legal research findings on business regulation and the law

- The legal research findings relevant to the *Doing Business* indicators cover four main areas: court efficiency and alternative dispute resolution; corporate governance; creditors' rights and collateral laws; and insolvency rules and reorganization procedures.
- Alternative dispute resolution mechanisms tend to have a symbiotic relationship with court efficiency. Where available, these mechanisms tend to be linked with faster dispute resolution in courts.
- The corporate governance literature highlights the need for a clear set of rules on who makes key decisions, who needs to be informed about those decisions and how abuse from different stakeholders can be prevented.
- The creditors' rights literature focuses on analyzing whether the legal framework can help maximize the value of collateral held by small and medium-size companies while giving secured creditors the assurance that their rights will be protected.
- The main objective of insolvency legislation is to ensure the survival of viable businesses, on the one hand, and the most equitable return for stakeholders in businesses that should ultimately be liquidated, on the other.

How laws and regulations affect the life of a local company is a complex question. The *Doing Business* report has endeavored to provide a cross-country comparison of the regulatory environment for local small and medium-size businesses since its inception 13 years ago. Its analysis has traditionally focused on two aspects of the regulatory environment as it applies to the topics covered: the efficiency with which a regulatory goal is achieved and the quality of the rule itself. The data collected for the *Doing Business* indicators over the years have served as a source of information for articles published in peer-reviewed academic journals and for working papers. In reviewing this research, past editions of the *Doing Business* report presented the economic perspective on the findings.[1] But the indicators are also part of a broader discussion on what constitutes "business friendly" rule of law.

This chapter reviews articles that were published in legal journals ranked among the top 70 and that focus on areas covered by four sets of *Doing Business* indicators—including articles whose core analysis centers either on the adequacy of legislation as compared with internationally accepted standards or on the application of the law.[2] The four sets of indicators are those on enforcing contracts, getting credit (legal rights), protecting minority investors and resolving insolvency. While most of these indicators are based primarily on a study of substantive law, some also examine the efficiency of the judiciary in dealing with commercial disputes and insolvencies.

The review reveals four thematic axes (table 12.1). First, a number of articles study the impact of court efficiency and the role of alternative dispute resolution (ADR) in countries' development by analyzing the symbiotic relationship between the two.[3] Second, many articles examine the rights and obligations of different types of shareholders in a company and the rules of corporate governance that can help ensure good corporate management. Third, researchers have looked at how creditors' rights affect access to finance, often focusing on the importance of a modern secured transactions system. Finally, studies have debated the importance of reorganization procedures in an insolvency framework, particularly in the light of the U.S. reorganization model.

COURT EFFICIENCY AND ALTERNATIVE DISPUTE RESOLUTION

The *Doing Business* indicators on enforcing contracts have historically touched on some of the issues of judicial efficiency explored by legal research in recent years, and a new indicator introduced this year—the quality of judicial processes index—broadens their coverage to include several additional aspects. One of these is the availability of arbitration and voluntary mediation as ADR mechanisms. Several studies discuss aspects of ADR and its relationship with court efficiency, including Dakolias (1999), Ryan (2000) and Drahozal and O'Connor (2014).

TABLE 12.1 Four thematic axes in the literature

Court efficiency and ADR	Corporate governance	Creditors' rights and collateral laws	Insolvency rules and reorganization procedures
Performance of judicial administration • Dakolias (1999) ADR mechanisms and procedural safeguards • Ryan (2000) Scope of arbitration clauses • Drahozal and O'Connor (2014) Technology and access to justice • Cabral and others (2012)	Regulatory convergence in shareholder protection and corporate governance • Katelouzou and Siems (2015) • Aytekin, Miles and Esen (2013) Director versus shareholder primacy • Bainbridge (2014) Agency cost in principal-agent relationship • Hill and McDonnell (2015) • Gilson and Gordon (2013) Company form and rights of shareholders • De Jong (forthcoming) Relationship between shareholder and worker protection • Gahan, Ramsay and Welsh (2014)	Importance of secured transactions regimes • Kozolchyk and Furnish (2006) Legal and collateral registry reform in Malawi • Dubovec and Kambili (2013) Secured transactions reform in Ghana • Dubovec and Osei-Tutu (2013) Statutory erosion of creditors' rights and the U.K. example • Walters (2014)	Good insolvency practices • Azar (2008) Deciding between liquidation and reorganization proceedings • Adams (1993) Relationship between reorganization law and the performance of reorganization systems • Eisenberg and Sundgren (1997) • LoPucki and Triantis (1994) Secured creditors' rights in reorganization proceedings • Segal (2007) Voting on reorganization plans • Kordana and Posner (1999)

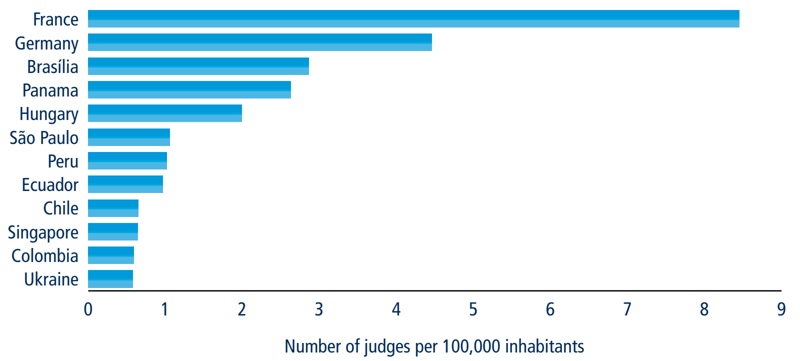
Another aspect measured by the new index is the use of technology in ways that can increase court efficiency and reduce corruption—such as electronic filing, electronic delivery of legal documents to the parties to a case, electronic payment of court fees, random assignment of cases to the judges, publication of judgments and electronic case management systems. As Cabral and others (2012) suggest, technology can also improve access to justice. Beyond these aspects, the index also measures elements of the court structure (such as the availability of a specialized commercial court and a court or simplified procedure for small claims) as well as the case management system (such as the existence of specific rules on adjournments or time limits for key court events like delivery of the final judgment).[4]

Added to the traditional indicators on the time and cost to enforce a contract, the new index provides broader insights into judicial efficiency and the quality of judicial processes and can help policy makers around the world make more informed decisions when undertaking judicial reform. A review of the literature suggests that the enforcing contracts indicators are a unique tool for policy makers, as cross-country data on court efficiency are scarce and no other data set compares judicial efficiency in as many as 189 economies.

Until recently there was also little quantitative research on judicial efficiency. Researchers preferred to focus instead on the qualitative aspect of comparative law. Dakolias (1999) was among the first to carry out a comparative analysis of the performance of judicial administration. Focusing on 11 economies in different regions, the author's analysis was based on data provided by public sources on the following metrics: number of cases filed per year, number of cases disposed per year, number of cases pending at year-end, clearance rate (ratio of cases disposed to cases filed), congestion rate (pending and filed cases over resolved cases), average duration of each case and number of judges per 100,000 inhabitants (figure 12.1).

The results show that in many of these economies the judiciary was able to meet demand at a specific point in time; as time

FIGURE 12.1 The number of judges relative to the population varies widely across economies



Source: Adapted from Dakolias (1999).

passed, however, difficulties arose and reforms were needed to address deficiencies. Some of the solutions proposed by Dakolias involve introducing ADR mechanisms to address backlogs, increasing the number of judges by establishing temporary courts and using information technology to improve productivity—all areas addressed by *Doing Business*.

Researchers have studied some of these solutions more broadly. For example, Cabral and others (2012) analyze how the use of technology by courts and legal aid organizations can help improve access to justice for low-income litigants in the United States. While great strides have been made through the use of web-based delivery models (such as electronic filing and document assembly), accessibility and usability are still far from ideal. Indeed, the authors argue that to avoid penalizing the parties to a case, courts implementing new technologies should consider the barriers that some litigants might face in accessing the technologies—such as self-represented litigants, litigants located in rural areas and persons with disabilities or with limited English proficiency.

In addition, Cabral and his coauthors argue that mobile devices, for example, will become one of the primary means of accessing information and that the legal community needs to adapt accordingly. And they emphasize the need to improve well-accepted technological enhancements such as electronic filing systems. The adoption of open technical standards for electronic filing, the authors contend, could ensure universal access for litigants. They also propose a triage system that would recommend cost-efficient choices for litigants. Finally, the authors analyze different barriers to the adoption of effective technology strategies that could improve access to justice. They identify eight sometimes overlapping barriers (for example, lack of funding, a lack of uniformity or standardization and a perception that using technology is not full justice) as well as potential solutions (such as the adoption of standardized forms or the use of incentives like grants) to foster technology.

ADR mechanisms have long been recognized as an important tool for enhancing court efficiency, either by helping to alleviate court congestion or by providing a faster, less costly and more flexible solution for litigants. Today ADR mechanisms are commonly incorporated into the litigation process (such as through court-annexed arbitration),[5] and even if there is criticism of these mechanisms, models such as contractual arbitration and mediation are undeniably popular in the business community. Ryan (2000) argues that the widespread use of ADR needs to be accompanied by procedural safeguards so as to ensure the rights of the parties involved. The author suggests that among the most important developments in judicial ADR has been the designation of uniform standards of ethics and procedure. The author provides further recommendations in areas relating to confidentiality, evidence, public accountability, ethical issues and quality control.

The relationship between courts and ADR mechanisms can be particularly complex when a contractual relationship is agreed between sophisticated parties. Drahozal and O'Connor (2014) argue that when the parties to a contract choose between courts and arbitration, an ex ante procedural unbundling occurs when they select specific claims and remedies rather than an "a la carte" choice of individual procedures. For example, it is common practice for arbitration clauses to exclude certain claims and remedies or for parties to agree that even when going to court they will still rely on arbitration to resolve particular matters.[6] These practices, referred to as "carve-ins" and "carve-outs," are used to ensure greater performance incentives and lower dispute resolution costs.

The authors gather empirical data on procedural unbundling for different types of contracts (such as franchise agreements, technology contracts and joint venture agreements) and find, among other things, that almost all franchise contracts include "carve-outs" in their arbitration clauses. In addition, the authors argue that where there is mistrust in the courts, parties will rely on arbitration procedures. And they show that contractual value is lost if parties cannot rely on courts to protect the value of their information and innovation.

CORPORATE GOVERNANCE—WHO SHOULD HAVE CONTROL?

The *Doing Business* indicators on protecting minority investors measure the protection of minority shareholders from conflicts of interest as well as shareholders' rights in corporate governance. To construct these indicators, *Doing Business* applies a consistent methodology and case study to assess whether each economy has implemented a set of good practices in litigation and corporate governance that protect minority shareholders. As Aytekin, Miles and Esen (2013) illustrate, economies can benefit from the lessons drawn from comparisons with good practices worldwide. And the authors confirm earlier *Doing Business* findings that developing economies are closing the gap in regulatory frameworks. Indeed, Katelouzou and Siems (2015) suggest that there is a pattern of global convergence toward regulatory good practices as measured by *Doing Business*, regardless of legal origin or tradition.

Hill and McDonnell (2015) concur on the importance of measurements and benchmarks, suggesting that they have contributed to reducing the agency problem in modern company law in the past decade. Gilson and Gordon (2013) also reflect on the agency issue. Nevertheless, as Bainbridge (2014) shows, whether shareholder-centric or board-centric company law is more beneficial depends on myriad characteristics specific to each economy. In line with the updated methodology for the protecting minority investors indicators, De Jong (forthcoming) attempts to shed further light on differences between regulatory frameworks applicable to listed and nonlisted companies and on the consequences for the rights of investors.

Research on company law and corporate governance models has generated three commonly accepted paradigms: First, this area of law may be path-dependent and thus not subject to many significant changes in a given jurisdiction. Second, the influence of the U.S. corporate governance model has led to the dominance of market-oriented company law. And third, an economy's legal origin and stage of economic development are important factors in determining shareholder protection. Yet Katelouzou and Siems (2015), using leximetric data measuring the strength of formal legal protections in 30 countries over a 24-year period, demonstrate the weakening of these paradigms. To do so, they construct a shareholder protection index by measuring 10 aspects of shareholder protection, some of which are also covered by the protecting minority investors indicators. According to the authors' findings, the U.S. model of company law is not the norm. In addition, since the financial crisis, interest in reform has shifted to other areas of law. And countries with similar levels of shareholder protection do not necessarily have the same legal origin or stage of economic development. The authors also suggest that all 30 countries in their study increased shareholder protection over the period covered (figure 12.2).

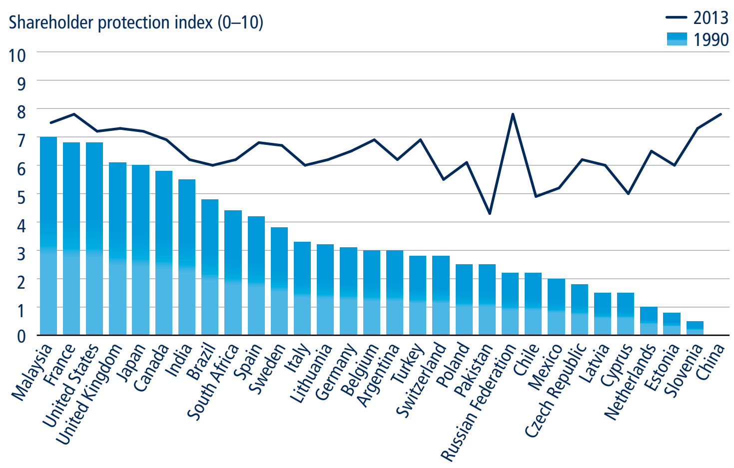
Comparisons of countries with different legal traditions and levels of development can help identify good practices as well as weaknesses in law. Aytekin, Miles and Esen (2013) use a comparative approach to analyze the development of corporate governance in Turkey, particularly after 2006. They use a comparison with Canada to identify strengths and weaknesses in the Turkish system and to determine whether Turkey is making faster progress in corporate governance practices than Canada is. The authors find that Turkey has improved in many aspects of modern corporate governance, though the development of effective and efficient boards remains an area of slower progress. And they provide support for the claim that developing countries are closing the corporate governance gap with high-income countries.

In another important finding, Aytekin, Miles and Esen show that while there was no change in Turkey's positive trend of corporate governance development during the 2008–09 financial crisis, Canada's corporate governance practices and reputation were adversely affected during this period. The authors conclude that researchers and practitioners need to give special attention to the development and functioning of company boards in Canada as well as Turkey, because they find that this element of corporate governance is weaker than others in both these countries.

For a corporation to flourish, a clear set of rules is needed on who makes key decisions, who needs to be informed about those decisions and how abuse from different company stakeholders can be prevented. Bainbridge (2014) discusses whether shareholders or management should ultimately have control in corporate decisions and whose interests should ultimately prevail. The author examines the general assumption that shareholder primacy is a defining characteristic of New Zealand company law and compares the means and ends of corporate governance in that body of law with those in the considerably more board-centric regime of the United States. He finds that New Zealand company law both establishes shareholder wealth maximization as the objective of corporate governance and, despite assigning managerial authority to the board of directors, gives shareholders significant control rights. This contrasts with the separation of ownership and control mandated by the U.S. system. Arguing that this separation of ownership and control has significant efficiency advantages, the author suggests that New Zealand has opted for a more shareholder-centric model because there are only a small number of New Zealand firms for which director primacy would be optimal.

Transparency in the decision-making structure is also imperative to ensure the performance of corporations—especially since performance can be understood in

FIGURE 12.2 Shareholder protection increased between 1990 and 2013 in all 30 countries in a study



Source: Adapted from Katelouzou and Siems (2015, figure 1).
Note: Higher scores on the shareholder protection index (as defined in Katelouzou and Siems 2015) indicate stronger protection of shareholders in the law.

different ways. Hill and McDonnell (2015) illustrate how corporate managers may favor themselves at the cost of corporations or shareholders and thus become bad agents. They argue that the agency cost paradigm, by emphasizing the maximization of shareholder value as the duty of corporate managers, has had some good effects, but also some bad effects and some ugly ones. The good is to provide a benchmark that can make it easy to identify bad management performance. The bad effect extends to actions with ambiguous consequences, such as takeovers aimed primarily at reducing development costs, which may entail results worse even than the self-gain of corporate managers. The ugly effect emerges when managers, by focusing on increasing shareholders' value, boost their own first through questionably defined performance payments.

Gilson and Gordon (2013) analyze the costs of ownership by institutional investment intermediaries—the agency costs of agency capitalism in the United States and other jurisdictions. According to the authors, such costs emerge from a divergence of interests, not only between owners and managers but also between owners of record (institutional investors) and beneficial owners. These costs can be lessened with the aid of shareholder activists, serving as an additional set of specialists who can intervene and challenge institutional investors.

The form of a company is also relevant in corporate governance. De Jong (forthcoming) analyzes the distinction between public and private (limited) companies and its relevance to company law in the Netherlands and the United Kingdom. In both jurisdictions the private company is of more recent origin than the public company and currently the most common company form. The author discusses the motives for choosing the public company form over the more lightly regulated private company one as well as the justifications for the more extensive regulation of the public company. De Jong argues that both British and Dutch law could relax certain mandatory provisions for nonlisted public companies and thus offer more flexibility to shareholders. In contrast with British law, under Dutch law a private company can make public offers of its securities and become listed, though there is no appropriate legislative regime as there is for a public company. The author concludes with a discussion on several areas in which British or Dutch company law distinguishes between public and private companies, including capital protection, resolutions and meetings, rights attached to shares, the board, accounting law and dispute resolution.

Finally, Gahan, Ramsay and Welsh (2014) use leximetric analysis to document changes in the level of worker protection and shareholder protection in six countries over the period 1970–2005. They find that both worker and shareholder protection increased in five of the six countries—France, Germany, India, the United Kingdom and the United States. By contrast, in the sixth country, Australia, shareholder protection increased while the level of worker protection in 2005 was similar to that in 1970. Statistical tests show that greater formal protection for shareholders does not come at the expense of formal protection for workers (figure 12.3).

CREDITORS' RIGHTS AND COLLATERAL LAWS

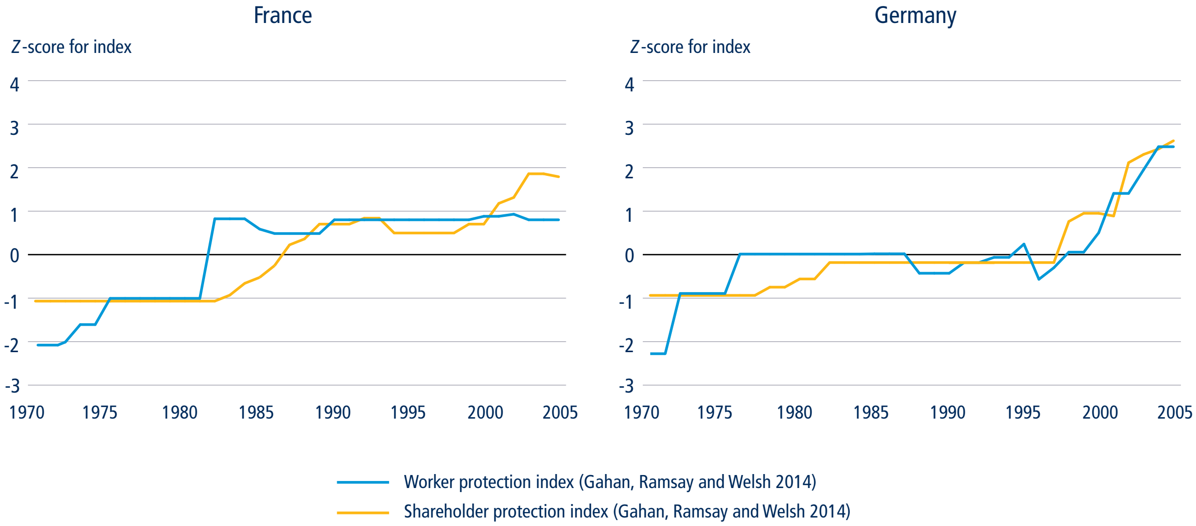
One of the *Doing Business* indicators on getting credit, the strength of legal rights index, centers on the key stages in the life cycle of a security interest in movable property: creation, publicity and enforcement. These are the pillars of a modern secured transactions system. The index also measures aspects of the interactions between collateral law and bankruptcy regimes, providing guidance on good practices according to internationally accepted standards. Recent articles look at closely related issues. Kozolchyk and Furnish (2006) highlight the importance of modern secured transactions systems, while Dubovec and Kambili (2013) and Dubovec and Osei-Tutu (2013) reflect on the experiences of different countries in implementing such systems. Going in another direction, Walters (2014) looks at ways in which lenders are able to adjust to changes in bankruptcy law perceived as affecting their interests.

When thinking about secured transactions reform, policy makers and researchers tackle two main issues: What type of legal framework can help maximize the value of collateral held by small and medium-size companies while giving secured creditors the assurance that their rights will be protected? And how does the secured transactions system in place affect the relative competitiveness of the private sector through its impact on the cost of commercial credit?

Kozolchyk and Furnish (2006) examine these issues through an analysis of the basic principles of modern secured transactions law. They explain that the main reason such laws are essential is that they enable the use of movable assets as collateral, increasing access to affordable credit and thus promoting economic development. The authors review the historical evolution of security interests in Latin America and the development by the Organization of American States of the Model Inter-American Law on Secured Transactions, which can help address shortcomings in the existing legislation of different countries in the region. Finally, the authors compare Mexico's amendments of secured transactions laws in 2000 and 2003 with the model law and the U.S. and Canadian paradigms and provide suggestions on how the country could continue the reform process.

Dubovec and Kambili (2013) examine the ongoing legal and collateral registry reform in Malawi and its potential for creating a modern, efficient secured transactions system. In Malawi, as in Sub-Saharan Africa generally, getting access to credit has been a major challenge for small and

FIGURE 12.3 Greater shareholder protection did not come at the cost of worker protection in France and Germany between 1970 and 2005



Source: Adapted from Gahan, Ramsay and Welsh (2014, figure 1).

Note: Higher scores on the worker and shareholder protection indices (as defined in Gahan, Ramsay and Welsh 2014) indicate stronger worker and shareholder protection in the law. As noted in the source, the figure "graphs the *z*-score for each index, which measures the different indices in a standard (equivalent) way that enables comparison across the indices. The *z*-score represents the distance between the raw score and the population mean in units of the standard deviation and is calculated as $z = (x-\mu)/\sigma$, where x is the raw index value for an individual year, μ is the mean value of the index number of all years, and σ is the standard deviation of the index number over all years for which data are observed. A negative *z*-score means the raw score is below the mean, positive when above" (Gahan, Ramsay and Welsh 2014, footnote 54).

medium-size enterprises. The country's legal framework for secured transactions consists of outdated laws whose application varies depending on many criteria, resulting in greater monitoring costs for lenders, unnecessary formalities and registration deficiencies that lead to the voiding of transactions. These issues led to an inability to improve access to affordable credit for the private sector, prompting the decision to reform the legal framework. The suggested reform is the functional approach to secured transactions, which simplifies the legal framework by bringing all security devices under a single law—in Malawi, the Personal Property Security Act signed by the president in 2013. The authors argue in favor of taking a methodical approach to secured transactions reform by using a model law—such as the New Zealand Personal Property Securities Act, used as a model in Malawi—as well as the recommendations of the *UNCITRAL Legislative Guide on Secured Transactions* (UNCITRAL 2010). The authors also note the need to take into account the local legal and socioeconomic context.

Several other reform initiatives have taken a similar approach. One such initiative was in Ghana. According to Dubovec and Osei-Tutu (2013), the prereform legal framework in Ghana, based on English law, was outdated. Ghana's new secured transactions law—the Borrowers and Lenders Act of 2008—and new collateral registry have the potential to serve as models for other African countries. But these are not typical examples of a modern secured transactions law and collateral registry, as they could still be improved. The authors argue that the reforms did not meet all international standards as set out in the *UNCITRAL Legislative Guide on Secured Transactions* (UNCITRAL 2010) and the *Secured Transactions Systems and Collateral Registries* toolkit (World Bank Group, Investment Climate Advisory Services 2010). A drafting group that includes the authors suggested amendments to the law and steps to modernize the collateral registry. These suggestions led to a redesign of the collateral registry, making it the first modern one in Africa.

Walters (2014) draws on his experience in the jurisdiction of England and Wales to describe two cases of secured lenders successfully adjusting to statutory erosion of their rights. Secured lenders responded to a redistribution of priority rights between secured and unsecured creditors by introducing transactional innovations. And they adjusted to an abolition of administrative receivership aimed at eroding their control rights by exerting their remaining control rights in new ways.[7]

INSOLVENCY RULES AND REORGANIZATION PROCEDURES

The *Doing Business* indicators on resolving insolvency measure the recovery rate for secured creditors and the extent to which domestic law has incorporated certain internationally accepted legal principles on liquidation and reorganization proceedings. The indicators address several themes discussed in the literature. One is key insolvency principles in the law, a question explored by Azar (2008). Another is the availability of reorganization proceedings to enable insolvent but viable businesses to continue operating. Aspects of reorganization proceedings are the focus of an important part of the literature, including Eisenberg and Sundgren (1997), LoPucki and Triantis (1994), Segal (2007) and Kordana and Posner (1999). A related theme is the problem of making the right choice in deciding whether to start liquidation proceedings or reorganization proceedings, discussed by Adams (1993).

The main objective of insolvency legislation is to ensure the survival of viable businesses, on the one hand, and to ensure the most equitable return for stakeholders in businesses that should ultimately be liquidated, on the other. The question of which insolvency practices support this objective has been extensively debated. Azar (2008) looks at this issue through a comparative analysis of seven key bankruptcy themes in 50 countries around the world. The author argues that replacing the management of a company undergoing reorganization provides better protection for creditors but is not without costs—and that the mechanisms for selling a debtor's assets in liquidation should be prompt, efficient, flexible and transparent. Assessing the importance of the stay of individual proceedings in bankruptcy, he argues that without it, recovery rates for creditors are lower.[8] And on the fate of executory contracts, the author argues that if the debtor's value is maximized through the continuous exploitation of its business, bankruptcy should first preserve essential contractual relationships that arose before the start of insolvency proceedings and allow the bankruptcy estate to discard nonbeneficial ones.[9]

Azar also discusses the concept of preference in bankruptcy. He argues that preferences to creditors should be objectively defined to include transactions in the ordinary course of business when these violate the pari passu principle—the principle according to which creditors will be treated equally and creditors within a class will be repaid on a pro rata basis—to allow the trustee to bring important assets back to the estate. In addition, bankruptcy law should provide mechanisms to encourage post-commencement finance and should protect creditors whose claims arose before the start of proceedings without freezing the debtor's access to the new financing.[10]

Finally, turning to the role of the court and creditor participation, Azar argues that the court's role should be limited to guaranteeing the transparency of the collective proceeding and to providing a forum for the parties to negotiate and vote on a viable reorganization plan. Creditors should participate in important decisions through a creditors' committee, a principle promoted by *Doing Business*.

Reorganization procedures have dominated the academic research on insolvency law. Chapter 11 of the U.S. Bankruptcy Code is among the reorganization models most discussed in the comparative law literature. For example, Eisenberg and Sundgren (1997) compare data on reorganizations in the United States and Finland to assess whether differences between the two countries' laws affect the performance of their reorganization systems. The two countries' laws are alike in many important respects. Under both systems, debtors can preserve pending contracts and obtain post-commencement credit on a priority basis, reorganization plans are permitted to affect the rights of secured creditors, and payments under a reorganization plan must be at least equal to what creditors would receive in liquidation.

But the systems also differ in important ways. One main difference is that Finland's system routinely appoints administrators, while the U.S. system uses the debtor-in-possession model.[11] Another difference is that Finland's system provides more substantive early screening of cases, while underlying Chapter 11 is a de facto presumption that nearly all firms should be given a chance to reorganize. The authors find that Finland's more stringent initial screening leads to faster processing of cases; for U.S. firms, proceedings take almost three times as long. In addition, they find that Chapter 11, while perceived as being more pro-debtor, does not lead to reorganization plans that leave creditors with only the liquidation value of the assets while leaving the debtor's owners with the reorganization surplus. The authors also find that unsecured creditors receive more under the U.S. system than they do under the Finnish one.

LoPucki and Triantis (1994) use a "systems" approach to compare the judicial reorganization systems of the United States and Canada. Although U.S. and Canadian lawmakers set out to create very different systems, these systems came to function in very similar ways. The authors suggest that this functional convergence was bound to happen: given the countries' broadly similar objectives for reorganization and shared economic background (market economy), there was a limited range of alternative designs that could result in a functioning system. They speculate that functional imperatives such as these may be the principal determinant of any system that attempts to effect court-supervised reorganization through a coordinated plan.

Many critiques of the Chapter 11 system have focused on firms' attempting reorganization when liquidation is the more efficient solution and the effects this has on the costs of bankruptcy. Adams (1993) proposes a two-part revision to the Chapter 11 system to reduce these costs: First, establishing a bifurcated debtor-in-possession structure in which a bankruptcy trustee makes fundamental bankruptcy decisions and the entity's existing management makes business activity decisions. Second, providing the trustee with a methodology for determining whether reorganization or liquidation is the proper course of action. Under this methodology the trustee would first determine the present value of the future earnings of the reorganized firm and the liquidation value of the firm. Relying on experience, the trustee would then adjust the present value of the future earnings upward to reflect intrinsic values of the reorganization. After making this adjustment the trustee would consider the two values and decide whether to reorganize or liquidate the entity.

Segal (2007) presents a comparative perspective on the rights of secured creditors during reorganization proceedings. The author does so in reference to the operation and effect of both the English (administration) and U.S. (Chapter 11) regimes, without seeking to address the broader topic of secured creditors' treatment in these regimes. He identifies six core areas of comparison: secured creditors' enforcement rights, automatic stay, the after-acquired property clause in bankruptcy proceedings, debtors' power to use and sell the collateral free of security interests, costs that arise after the start of the proceedings and the cram-down of security interests in bankruptcy proceedings.[12] The comparison reveals that the English and U.S. approaches still differ, with secured creditors having stronger rights in reorganization proceedings in the United Kingdom, yet legal evolution has brought the two jurisdictions closer to each other.

Kordana and Posner (1999) address the debate about whether the voting system in U.S. reorganizations is efficient or whether it should be replaced with a system that avoids voting and relies on a more market-driven valuation of the bankruptcy firm, such as an auction system. The authors expand on existing bargaining models to consider bargaining with multiple creditors, paying particular attention to difficulties posed by imperfect information, and analyze the major voting rules in Chapter 11. They find that the bargaining system under Chapter 11 is more flexible within the constraints provided by a supervising judge. Bargaining enables parties to agree to a reorganization when parties have substantial interests arising after the start of bankruptcy proceedings that cannot be the object of a contract. The auction approach does not allow the confirmation of such plans unless parties with interests arising after bankruptcy proceedings can borrow enough to purchase the firm or can buy the claims of other parties.

CONCLUSION

This literature review confirms the interest in the areas of business regulation covered by *Doing Business*. The enforcing contracts, protecting minority investors, getting credit (legal rights) and resolving insolvency indicators address the four thematic axes identified in the literature: court efficiency and the role of ADR; corporate governance rules; creditors' rights and collateral laws ; and insolvency rules and reorganization procedures. *Doing Business* has benefited greatly from academic discussion and has expanded its methodology to keep abreast of developments in academic research.

Doing Business has also expanded its methodology to produce new data sets and indicators that quantify new aspects of regulation. Last year's report introduced new data sets on the rights of shareholders in corporate governance, on the adoption of a functional approach to secured transactions, on additional aspects of collateral registries and extrajudicial enforcement, and on the quality of insolvency legislation. This year's report includes new data sets on the quality of judicial processes. By introducing these changes, *Doing Business* provides empirical evidence to support the testing of existing legal theories and creates new empirical foundations to inform further academic work.

NOTES

This chapter was written by Santiago Croci Downes, Magdalini Konidari and María Antonia Quesada Gámez.

1. See, for example, the chapter on research on the effects of business regulations in *Doing Business 2014* (World Bank 2013).
2. The review relied on the rankings of legal journals produced by the Washington and Lee University School of Law, available at http://lawlib.wlu.edu/LJ/. A few exceptions were made for articles that were published in law journals not in the top 70 but whose content was highly relevant to the areas covered by the indicators.
3. ADR refers to mechanisms for settling disputes without litigation. Such mechanisms include negotiation, mediation and arbitration.
4. Adjournment is the act of a court to dissolve a session, temporarily or permanently, and dismiss the business in hand, temporarily or permanently.
5. In court-annexed arbitration, courts divert certain cases to arbitration rather than trial. The cases are typically heard by experienced lawyers rather than judges, under the general supervision of the courts.
6. An arbitration clause in a contract requires the parties to resolve their disputes through an arbitration process.
7. Administrative receivership is a procedure in which an administrative receiver is appointed in order to facilitate the repayment of creditors through secured debt.
8. Under a stay of individual proceedings in bankruptcy, individual actions by creditors against a debtor (such as lawsuits or foreclosures) must stop at the moment a bankruptcy petition is filed.
9. An executory contract is one that has not been fully performed by all the parties to the contract at the time bankruptcy proceedings are commenced. Bankruptcy estate refers to all interests of the debtor in property at the time of the filing for bankruptcy.
10. Post-commencement finance is new funding provided to an insolvent company after the start of insolvency proceedings. For further discussion of post-commencement finance, see the resolving insolvency case study in this report.
11. A debtor-in-possession in U.S. bankruptcy law is an individual or corporation that has filed for reorganization (under Chapter 11 of the U.S. Bankruptcy Code) and remains in control of the property and retains the power to operate the business while proceedings are ongoing, in lieu of a trustee.
12. An after-acquired property clause defines whether an asset acquired after the commencement of bankruptcy proceedings is considered to be collateral. A cram-down of security interests is an involuntary change or discharge in rights of secured creditors by the reorganization plan without the consent of the affected creditors.