REFGOV

Reflexive Governance in the Public Interest

Corporate Governance

THE PROBLEMATIC OF FINANCIAL DISTRESS OF COMPANIES IN BELGIUM :

A CONTEXTUAL PRAGMATIC APPROACH

By Ibrahim SANHAYI

Working paper series : REFGOV-CG-11

THE PROBLEMATIC OF FINANCIAL DISTRESS OF COMPANIES IN BELGIUM : A CONTEXTUAL PRAGMATIC APPROACH

Ibrahim SANHAYI ♣

INTRODUCTION

In this paper, we suggest a pragmatic approach to financial distress of companies. This implies that we clarify our position with respect to concepts like semantism and pragmatism,[1] as developed by J. Lenoble[2]. First, we will develop the reasons why it does make sense to adopt this pragmatic approach. Then, we will show that the mechanism in place – the Belgian bankruptcy law – has implicitly adopted a semantic approach, which does not allow the stakeholders to have a hold on the context so that they can reach a solution at the same time acceptable by all and effectuable.

This pragmatic posture is the key theoretical option in our doctoral research process. After a brief description of our main research hypothesis – contextual proceduralisation – we will develop the rationales behind adopting a pragmatic approach. The next step of our research will be the tentative construction of better adapted collective mechanism to solve financial distress, based on the empirical material – case studies – that we have already partially gathered.

The structure of this paper is as follows: the first section is a brief description of our problematic and of our research hypothesis, while the second one discusses our positioning vis-à-vis the respective semantic and pragmatic approaches to financial distress of companies in the Belgian context.

♣ Ph.D. student - IAG School of Management –UCL - Belgium

[1] These concepts will be defined and further analyzed later in this paper.

[2] J. Lenoble, « La question de l'application en droit: Au-delà d'une approche herméneutique», Au-delà d'une approche herméneutique", in *Mélanges J. van Compernolle*, Bruxelles, Bruylant, 2004

1. Brief description of our problematic and main research hypothesis

The starting point of the problematic of this research is observing the fact that there is a general dissatisfaction with regard to the new legal procedure of bankruptcy introduced in Belgium in 1997.

The goal of this research is to determine more precisely the causes of the failure –quasi unanimously recognized – of the new procedure as well as to contribute to elaborate new solutions, that would fit better to the specific situations of SMEs. After a first case study, we have been able to reach some provisional conclusions that have oriented our research hypothesis and our methodological options.

Indeed, we identified that during the procedure, there are serious problems of misalignments of point of views among the different stakeholders, regarding the goals to be achieved, the bargaining power of each stakeholder as well as the role and means of action of the "commissaire au sursis"[3], who acts as a mediator between the stakeholders.

To realise our objective, we will mobilize the theoretical hypothesis of "contextual proceduralisation" developed by the UCL's "Center for philosophy of law"[4]. In the following sub-section, we will present our research hypothesis.

1.1. Contextual proceduralisation and financial distress

The contextual proceduralisation hypothesis' objective is to take into consideration the context in which operate multiple actors involved in a situation of action for which they have to elaborate a normative mechanism[5] that constitutes a solution which will be both acceptable and effectuable. For this sake, the individuals base themselves on a cognitive base previously acquired, yet given by the context in which their common action is inscribed, but which consists in a set of representations of the context. The contextual proceduralisation hypothesis claims that, in order to reach an "effectuable" solution, it is indispensable that the stakeholders will collectively construct a "vision of the world" that is common to all of them.

---

[3] Litterally: the 'reprievement officer'. The "commissaire au sursis" is appointed by the court in the beginning of the procedure. His/her role is to assist the debtor during the first stage of the procedure and to monitor him/her during the last stage. It is important to note that the "commissaire au sursis" does not manage the firm during the procedure – contrary to other countries, like the UK, where the administrator appointed by the court controls and manages the company during the CVA procedure – but assists the debtor in elaborating a planning for restructuration .

[4] Voir : Lenoble J. et Maesschalck M. (2003), *Toward a Theory of Governance – The Action of Norms*, Kluwer Law International, The Hague/London/New York; Cobbaut R. et Lenoble J. (eds) (2003), *Corporate Governance: An Institutionalist Approach*, Kluwer Law International, The Hague/London/New York.

[5] In french : dispositif normatif

Therefore, as Boyer puts it, "the contextualisation of a norm is not a simple listing of the actual states of the nature : it is an operation of definition shared by the actors of what poses problem and thanks to which the context appears as something that can be changed and not as an exogenous factor"[6].

However, the individuals have different perceptions of the context, with different priorities regarding actions to be taken – the selection operated among the elements of the context is different among individuals – and therefore, a great many times, the actors will not succeed in building a common world, nor will they be able to elaborate a common and effectuable solution to the problem at hand. It is then necessary to "proceduralise" the contextualisation process.

The financial distress is a typical case of a situation where the actors will select in a particularly divergent manner the elements of the context that they think are the most appropriate and important. In such situations, it appears very clearly that "a specific activity that elaborates a common perception of the context must be organized. This activity will allow to increase the number of possibles on the basis of which the solutions judged the most rational will be selected to meet the insufficiencies of the context"[7].

The condition of possibility of an effectuable solution is the commitment of the parties to find a solution that will adapt the context adequately. Indeed, the "reflexive construction of a common world as a condition of implementation of the action needs the building of a cooperation mechanism in order to operate this integration of necessary transformations of the context in order to insert a form of life deemed pertinent. The issue is then the definition of the procedural conditions that, in such particular conflict, must ensure the actors' reflexive capacity to build in common the solution that appears to them the most justifiable as well as the transformation conditions of the existing contexts that this solutions calls"[8].

A first formulation of our research hypothesis is that the current Belgian mechanism – the bankruptcy law – does not make it possible to build "reflexive incentives that allow the actors to enter into an efficient decisional process"[9] because it does not support the emergence of an interaction process that gathers all the stakeholders of the firm. Regarding this point, a common opinion is that the "commissaire au sursis" plays the central role in the mechanism

---

6 Boyer T. (2005), "Les conditions d'émergence d'une gouvernance réflexive des situations de danger pour l'emploi dans les entreprises : de la procédure du licenciement économique collectif à celle du droit d'alerte", Working paper CPDR-LSF, p.4

7 Lenoble (2003), op. cit.
8 Lenoble (2003), op. cit.
9 Boyer (2005), op. cit., p.14

put into place by the 1997 bankruptcy law. A formalist interpretation of this affirmation could consist in saying that only his sole presence guarantees the implementation of a mechanism adequately contextualised. Before discussing this proposition, we suggest to describe the main characteristics of this central character.

Appointed by the court, the role of the "commissaire au sursis" starts when the procedure begins – when the judge pronounces the "sursis provisoire" (provisional stay of proceedings). His role consists in assisting the debtor during the first stage of the procedure – provisional stay – and to monitor him/her during the last stage – final stay.

The "commissaire au sursis" has clearly a key role in the mechanism, and hence is able to favor the emergence and the development of a collective approach of the context reconstruction in a reflexive process, which will allow a collective decision in which the context is not considered as a purely exogenous element (a pure constraint), but as a given whose elements are modifiable in variable temporal horizons by the voluntarist action of actors that have a common project, or as Lenoble poses it : in "the construction of a cooperation mechanism to do this integration of necessary transformations of the context in order to insert a form of life deemed pertinent"[10].

However, following our preliminary investigation, we believe that there is an important risk that the "commissaire au sursis" has a perception of his own role that is not compatible with contextualisation. He can for example consider his role as the one of an "expert" – whose authority is based both on his competence and experience – who supplies a ready-made solution and monitors its implementation, or as the one of a "traditional mediator" who goes back and forth between the actors in order to make compatible a series of bilateral agreements initially juxtaposed.

2. Our positioning vis-à-vis the concepts of semantism and pragmatism

Before explaining our positioning and elaborating our choice, we suggest a definition of the concepts of semantism and pragmatism.

In the elaboration of a system of norms, the key question consists in considering "the conditions of possibility of the operation by which reason (activity of judgment) produces meaning effects in reality, that is, 'is applied' or 'is effected' in social reality."[11] A semantic approach to this question consists in supposing that "this application is entirely determined by

[10] Lenoble (2003), op. cit

[11] Centre de Philosophie du Droit (UCL), *Theory of the Norm and Democratic Governance*, Overview Report, Louvain-la-Neuve, 2005, p. 19.

the simple formal rules of rational activity. In such a perspective, the operations of application and of justification are ruled *by the same resources* and are therefore in a *symmetrical* relation."[12] In contrast to this "mentalist" view of the operation of application, a pragmatic approach is conceived as "a theory of both reason and action that will therefore privilege problem solving thanks to a constant and cooperative re-elaboration of ends and means and of their connection in social activities".[13]

As reminded above, we believe that the current Belgian bankruptcy law does not allow to solve the problem of financial distress. Our hypothesis is that the Belgian mechanism implicitly adopts and practically favours a semantic approach to the procedure, where a pragmatic approach would be appropriate. Indeed, our field knowledge of the Belgian procedure – acquired through interviews of various stakeholders and through the case study of a firm that has been through the whole financial distress process – makes us think that the Belgian mechanism adopts a semantic approach of the law, which explains – at least partially – its failure. We will show this through a selection of examples taken from our previous work.

First, the Belgian procedure favours an application of the law which is in most of the cases, "stricto sensu", i.e. without taking into consideration the specificities of each case, and most importantly, without allowing a *return on the context*. For example, the CEO of a SME in financial distress explained us – during an interview we conducted – that the O.N.S.S. – the Belgian social security national office – was not willing to forgive the interests due because of late payment, and its argument was : "it's the law". We think that it is very important to enforce the rules strictly to avoid imbalance between individuals and companies; we believe, however, that a too rigid application of the law is an obstacle to *the re-elaboration of the ends and means*.

Second, the procedure does not allow a reflexivity from the actors, that would allow them to act on the context in order to adapt it to their specific situation. On the contrary, the context is considered as an "exogenous element" on which the stakeholders cannot have an action and that they consequently cannot modify. For example, we have been able to collect numerous indications that the procedure is not suited to small companies, mostly because of its high cost. However, more than ninety percent of the bankrupt companies in Belgium in 2005 were SMEs (companies with less than fifty employees). This example shows that the procedure does not allow a reflexive return leading to an adaptation of the context.

---

[12] Ibid., p. 20.

[13] DEWEY, cited by M.C. DORF and C.F. SABEL, "A Constitution of Democratic Experimentalism", *Columbia Law Review*, 98 (1998), p. 286.

Another example is the role of the "commissaire au sursis". We believe that he has in mind *semantic presuppositions*. Indeed, he adopts a semantic approach of the financial distress, i.e. he applies the rules without taking into consideration the context in which the procedures takes place and without a reflexive return on the context. Because of this, he does not favor the interaction of the actors.

Our central thesis is thus – as reminded above – that an adequate regulation of financial distress situations necessitates a pragmatic conception of the law. Hereunder, We propose hereunder a few arguments against the semantic approach adopted by the Belgian bankruptcy law.

Although we believe that the law must be applied with rigor, yet it must allow the reflexivity of the actors on their context of action and hence adopt a pragmatic approach, which leads to an effectuable solution which would be acceptable for all the stakeholders. For example, the US Chapter 11 gives an important interpretive power to the judge, so that he can "force" decisions that are acceptable to all – or to a majority of – the actors and hence avoid situations in which one single actor – pursuing his own interest – can block a decision, situation in which the majority of the actors are worse off.

In addition to this, we consider that the context should not be considered as an "exogenous element" but as an element in which the stakeholders can act and that they can modify in order to adapt it to their specific situation. As a consequence, our further work will consist, starting from the analysis of several cases, in highlighting situations that have been structured in such a way that the interaction of the actors has succeeded in constructing a collective mechanism that, on the condition of an adequate modification of the institutional framework, could have made it possible to reach a common and effectuable solution. The main characteristic of such a mechanism is that it should incorporate reflexive incentives allowing the stakeholders to have a collective action on the context.

CONCLUSION

We have positioned our research theme vis-à-vis the concepts of semantism and pragmatism, and e have showed that it is necessary to adopt a pragmatic approach in order to be able to adapt the context and hence reach an effectuable solution that would be acceptable to all the stakeholders. Moreover, we have showed that the pragmatic approach favors a reflexive return on the context.

Now that we have constructed our theory, the next step of our research will be to show – through case studies and interviews[14] – that it is necessary to build up collective mechanisms that would allow the stakeholders to interact and that such mechanisms must incorporate reflexive incentives in order to favour an adaptation of the context.

This point will be further analyzed in our next paper, in which we will further develop our empirical approach in order to test our hypothesis against the "reality of the field". Our objective will be to show that the collective mechanism must be "institutionalised", i.e. put into place by an organizational structure – for instance, the state – in order to "coordinate intentional actions, and the planning of their agenda, and structure relevant bargaining"[15]

[14] Most of the interviews have been done
[15] Bratman, cited by J. Lenoble (2003), op.cit.