

G20 SME Finance Action Plan  
IMPLEMENTATION FRAMEWORK:  
Credit Infrastructure  
Country Self-Assessment

July 2016

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## Background

Small and medium-sized enterprises (SMEs) play a crucial role for employment, job creation, investment, innovation and economic growth around the world. They account for about 90% of businesses and more than 50% of employment worldwide, and are therefore crucial for the recovery of the world's economy. Considering this important role, it is critical to ensure that viable SMEs around the world have access to the credit they need to expand.

Lack of a sound financial infrastructure is one of the major problems in the credit market for SMEs. Having a solid financial infrastructure will help countries reduce the information asymmetries and legal uncertainties that increase risk to lenders and constrain the supply of finance to SMEs.

By endorsing the G20 Action Plan on SME Financing<sup>1</sup> in 2015, the G20 agreed, and encouraged non G20 countries to fully develop credit infrastructure for SMEs, improve SME financial capability through targeted learning and support interventions and enable competition through an enabling regulatory environment.<sup>2</sup>

The G20 Action Plan on SME Financing provided a framework to (a) facilitate a **dialogue between the relevant international fora and G20 work streams**; (b) **extend, as appropriate, successful G20 endorsed reforms and policy measures** in G20 and willing non G20 countries in order to increase the availability of finance for SMEs to grow and create jobs, action by individual countries in these areas would take into account the status of current regulatory and jurisdictional arrangements, and other reforms which are underway; and (c) **advance the agenda for SME finance across different G20 work streams with a focus on Low Income Developing Countries (LIDCs)**, including additional work from implementing partners and International Organizations (IOs),

The priority reform measures in the action plan are<sup>3</sup>:

- 1. Improvements of the credit reporting framework for SMEs*
- 2. Reforms that allow banks and non-banks to lend to SMEs against movable collateral*
- 3. Insolvency reforms*

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<sup>1</sup> Developed by World Bank Group, as part of the GPFI 2015 work plan, in consultation with GPFI implementing partners.

<sup>2</sup> The G20/OECD High-Level Principles on SME Financing that also were endorsed under Turkish presidency and the G20 Action Plan on SME Financing are complementary and mutually reinforcing.

<sup>3</sup> Implementing partners with expert capacity would be available, as part of their normal development operations, such as World Bank Group and other Development Finance Institutions, to support willing countries, on request.

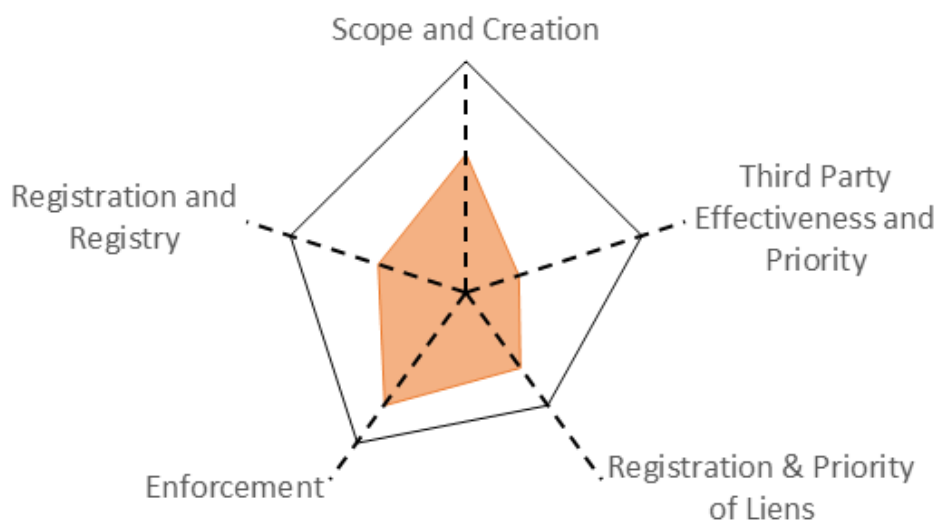
## Framework Description

As recognized by the G20, one of the key recommended actions going forward is to accelerate and replicate successful policy reforms that facilitate the expansion of financial services to SMEs, both on the demand and supply sides. The proposed approach is to use specific, SME-related aspects of recognized standards to prioritize areas of reforms, guided by agreed-on indicators which allow country self-reporting on progress.

Diagnostic assessments against aspects of international good practices are necessary as a first step to inform the selection and sequencing of reforms in the areas of financial market infrastructure. For the development of these assessments, reference to recognized international standards was made. These references are not comprehensive but, rather, draw on selected aspects of the recognized standards most relevant to promoting SME access to finance.

In the area of Insolvency and Creditor/Debtor Rights (“ICR”)<sup>4</sup>, which includes both insolvency and secured transactions, the World Bank ICR Principles (2015), together with the UNCITRAL Legislative Guide on Insolvency (2015) form the unified international standard, as designated by the FSB.

The proposed self-assessment framework is composed of a questionnaire covering three sections – 1) Credit reporting, 2) Secured Transactions & Collateral Registries, and 3) Insolvency. It is proposed that each question is assigned a particular score in the overall matrix, the sum of which adds up to a score of 10 for each of the three sections (**Total score =  $\sum$  1 (Yes) x weight of question**). Following the completion of the questionnaire, respondents may see the calculated total points and a visual radar graph for each of the three areas, which plots country existing practice compared to market development best practice. For illustrative purposes:



<sup>4</sup> The General Principles for credit reporting have been included in the Financial Stability Board (FSB) compendium of standards as relevant standards for financial system soundness. Standards are endorsed by each respective standard-setting body (SSB).

A baseline for each country will be collected in 2017 and progress will be reported in a consolidated report, on a regular basis to be determined by the G20.<sup>5</sup>

## General Instructions

The purpose of the questionnaire is to enable countries to conduct a self-assessment of their respective legal frameworks on the three priority reform areas of the G 20 Action Plan. It is a simplified and independent framework that would allow specialized self-assessments of the legal framework for SMEs at country level in G20 countries. It is not a substitute for full country assessments/ diagnostics and full assessment methodologies exist for all three areas and are the ones used by external assessors (e.g. FSB, IMF/WB through the Observance of Standards and Codes (ROSCs), and Financial Sector Assessment Programs (FSAPs).

Due to the significant disparity among countries regarding the definition of the term “small and medium-sized enterprises” (SMEs), SMEs are not strictly defined in this document and respondents should use their own “national” definition of an SME in completing this questionnaire.

Respondents should carefully read the questions below and answer “yes” or “no”, based on their understanding of the legal framework in question. The answers should reflect the legal environment and system in the country and take into account all available measures and procedures, regardless of differences in terminology.

This effort might require collaboration between different actors from the public sector in order to complete the questionnaire.

One primary authority should be identified in each country to coordinate these efforts and consolidate the responses obtained from the different actors. In addition respondents also need to be familiar with relevant policy, regulatory and oversight aspects.

The questionnaire, for simplicity, is designed to have a list of Yes/No questions, which will potentially require qualitative explanation. Therefore, careful selection of expert respondents is required and opportunity to provide qualitative comments will be provided in the assessment tool itself.

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<sup>5</sup> Prepared by WBG for GPF.

## Credit Reporting

### Introduction

In May 2009, an international task force coordinated by The World Bank with support from the Bank for International Settlement was created with the ultimate goal of producing international standards for credit reporting.<sup>6</sup> As a first result of such work, the General Principles for Credit Reporting were produced, and published in September 2011.

Since then, the international task force has been transformed into an international Committee on Credit Reporting (ICCR) and is working in promoting and facilitating observance and implementation of the standards by providing additional information and guidance<sup>7</sup>.

The G20 Action Plan on SME Financing identified credit infrastructure for SMEs, including improvements of the credit reporting framework for SMEs, as a key priority. In this context, the diagnostic assessment against international standards is recognized as an area of focus including the assessment against the General Principles for Credit Reporting included under the Financial Stability Board FSB non-core compendium of standards in 2013.

Although the ICCR has published an assessment methodology to provide guidance to assessors for evaluating observance of the five (5) principles, six (6) roles for participants and five (5) recommendations for Oversight set forth in the General Principles for Credit Reporting, this is a simplified framework that would allow self-assessments at country level in G20 members<sup>8</sup>. This simplified framework is structured as follows; section 1 includes a description of market development of the Credit Reporting Systems (CRS) covering SMEs related aspects, section 2 includes key considerations and directions on how to respond the questionnaire, section 3 presents a description of the rating scale and its intend and section 4 includes a list of key questions corresponding to each principle, recommendations for oversight and possible actions for SMEs credit reporting systems and finally section 5 including a glossary of terms.

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<sup>6</sup> The task force comprised representatives from central banks and other financial and data privacy regulators, from multilateral organizations involved in credit reporting and from credit reporting service providers, represented through their associations.

<sup>7</sup> As a result of such work the ICCR has produced the report “Facilitating SME Finance through improved Credit Reporting” in 2014 including more detailed guidance for specific credit reporting aspects related to SMEs. . The self-assessment questionnaire is based on the ICCR General Principles and this report.

<sup>8</sup> The simplified framework in no way should be considered a “substitute” to the Assessment Methodology for the General Principles for Credit Reporting published by the World Bank in 2013.

## Instructions

The present framework does not allow for an assessment of existing international standards, however it can show trends and key characteristics of the CRS in each jurisdiction. In order to respond to the questionnaire, the respondent should be aware of existing CRS in the country concerned as well as the products and services offered and the legal and regulatory framework supporting such activities. Some of the questions might be answered using existing public information while others might require private information (e.g. internal CRS policies and procedures, organizational charts and governance aspects, data and statistics).

One primary authority should be identified in each country to coordinate these efforts and consolidate the responses obtained from the different actors.

A balanced set of skills might be required including detailed knowledge of credit reporting and the credit market in general as well as the credit reporting market. In addition respondents also need to be familiar with relevant policy and regulatory and oversight aspects.

A rating system has been developed based on key aspects that should be observed in any G20 jurisdiction taking into consideration the diversity of credit reporting systems with the G20 countries. The rating scale presented here has been built on the basis of identified key criteria for an efficient CRS that would enable the flow of the necessary credit information to assess creditworthiness of SMEs. The rating system would not be used to rank countries in connection with their national credit reporting systems or market.

Context and Oversight	1.5
General Principle 1	2.5
General Principle 2	1
General Principle 3	1.5
General Principle 4	2.5
General Principle 5	1

### **Context and Oversight (SCORE - 1.5)**

This section intends to evaluate the existence of CRS offering products relevant for the evaluation of the creditworthiness of SMEs as well as the existence of a primary authority overseeing the CRS activities. The respondent should respond YES if all the elements included in the question are met in the given jurisdiction, otherwise the respondent should mark NO.

### **Based on General Principle 1 (SCORE - 2.5)**

This group of questions addresses aspects of data accuracy, sufficiency and timeliness. One of the key issues that impacts data accuracy refers to the possibility of uniquely identifying the debtor in the database, other relevant elements are related to the different sources of data not only from the financial sector but also financing from supply chain or other companies as well as it refers to the level of automation and processes in place to mitigate potential errors in the existing CRS. The

respondent should respond YES only in the case all the elements included in each question are present in the given jurisdiction. For example if there is a unique identification number in the country but it is not widely used in the CRS, the respondent should mark NO. Consequently if there are critical datasets or data providers not currently included in the CRS, the response to sufficient data collection should be NO.

#### **Based on General Principle 2 (SCORE - 1)**

The questions below require access to specific detailed information from each CRS operating in the country. Particular aspects regarding governance and policies and procedures might not be available in the public domain. It is necessary though that the respondent has access to this information from all relevant sources. (These applies for questions 2.1 to 3.4)

#### **Based on General Principle 3 (SCORE - 1.5)**

The questions related to this section should reflect the situation of all existing CRS in the country. If there is one CRS that does not comply with the requirements included in the question, respondent should mark NO.

#### **Based on General Principle 4 (SCORE - 2.5)**

Information needed to complete this section is typically available but might entail the need to read each law and/or regulation that relates to CRS (e.g. banking laws, credit bureau laws and others) and they might also require to have access to contractual arrangements between the parties.

#### **Based on General Principle 5 (SCORE - 1)**

Questions related to this section might not be applicable to all existing jurisdictions and therefore the initial question relates to the existing conditions that call for the exchange of information between 2 or more jurisdictions. Even if conditions are not in place the existence of mechanisms to enable the exchange would serve to identify correcting measures. Respondents will need to be knowledgeable of existing international agreements between countries and technical arrangements in each of the existing CRS. If there is at least one critical condition (e.g. EU membership) that call for the exchange of data across borders then respondent should mark YES.

### Market development stages

#### **1. Developed**

In an advanced CRS covering SMEs, the existing systems include all relevant data to develop credit reports and value added services tailored to SMEs. In addition the legal framework in the given jurisdiction covering CRS is clear and predictable and enables the flow of information across different credit reporting systems and users while being subject to adequate regulation and oversight. Moreover, the solutions adopted by the credit reporting systems are efficient and cost effective. Under this scenario, CRS should be able to offer creditors (both financial and commercial) innovative and affordable tools to support their credit risk evaluation based on reliable information transferred



safely through efficient networks. The CRS is supported by adequate legal and regulatory framework and the service providers and other participants are reliable and subject to oversight.

As a result, an advanced CRS covering SMEs contains the majority of the elements in all six sections proposed and scores above 7.5/10 in the questionnaire.

## **2. Developing**

In a developing CRS covering SMEs related aspects some of the critical elements for an efficient safe and reliable CRS are in place but some critical aspects are still not developed or under development. For instance, the legal framework might not be clear or predictable or the current governance might impede the development of adequate value added services or the systems are extremely fragmented impeding the collection of all relevant data necessary to evaluate the creditworthiness of SMEs. In addition the legal framework might not allow the collection of relevant key data items or might lack the adequate privacy protection for individuals regarding the use of their data and mechanisms to correct such data. Other aspects that might be lacking are those related to value added services tailored to the evaluation of SMEs (including their management and shareholders).

As a result, a developing CRS covering SMEs includes some critical elements in the six sections proposed and scores greater than 4 and less than or equal to 7.5 out of 10 in the questionnaire.

## **3. Formative**

A formative CRS can be described as a system that has many deficiencies and lacks many of the basic elements described in the questionnaire. Main elements might refer to the existence of a CRS but not yet collecting sufficient data on a systematic basis and facing severe data quality problems. Additional deficiencies can include (but are not limited to) lack of a CRS collecting relevant data, a CRS focused on consumer credit related information, lack of interoperability of existing systems or lack of adequate measure to protect data from unauthorized access, loss or data corruption or data misuse. In such a context, creditors face difficulties in properly assessing the risk of potential debtors at an affordable cost requesting either collateral to the debtors or conducting highly costly investigations that are transferred to debtors, increasing cost of credit.

As a result, a formative CRS covering SMEs only includes some elements of the proposed framework and therefore scores 4/10 or below in the questionnaire.

## Accessing Questionnaire

	<b>International Best Practices Issue/Subject matter</b>	<b>Yes</b>	<b>No</b>	<b>Score</b>
<b>1.</b>	<b>Existing CRS and role of authorities</b>			<b>1.5</b>
1.1.	Are there commercial credit reporting companies, credit registries and consumer credit bureaus in the country?			0.50
1.2.	Have service providers developed reliable credit scoring models tailored to SMEs that are used by lenders and investors?			0.25
1.3.	Are there mechanisms in place that allow the exchange of data between different CRSPs?			0.50
1.4.	Is there any authority that coordinates and oversees the actions of the various credit reporting systems participants, and provides guidance and leadership inducing changes and reforms when necessary?			0.25
<b>2.</b>	<b>Data- Quality, sufficiency and timeliness</b>			<b>2.5</b>
2.1.	Is there a unique identification number for legal entities and for individuals (e.g. National Identification Number, LEI, Tax identification number) broadly used in the CRS			0.75
2.2.	Do CRSPs collect sufficient relevant data on a systematic basis from different sources (e.g. peer to peer, trade credit, government-held data, and creditors) to effectively develop value added products tailored to SMEs?			0.5
2.3.	Is information from relevant public records easily accessible (e.g. via electronic means) and updated on a timely and systematically basis (e.g. records on key financial and legal aspects of companies, property, shareholders, status)?			0.75
2.4.	Does information on the credit history include a detailed compilation of past and current payment behaviour of individuals and all types of legal entities and is kept for more than three (3) years			0.25
2.5.	Are processes such as normalization, validation and verification in place for each data load in every CRS?			0.25
<b>3</b>	<b>Data Processing; Security and Efficiency</b>			<b>1.0</b>
3.1.	Is data governance a critical part of the CRS and network, data and infrastructure comply with ISO security standards (e.g. 27001, PCI-DSS or other equivalent)?			0.1
3.2.	Does the CRSP promote and/or facilitate the use of standardized formats/templates for data provisioning and in general terms greater levels of automation?			0.25
3.3.	Do all existing CRS have a BCP in place where RTO, secondary site and data loss recovery are also included in the BCP?			0.15
3.4.	Are all types of users' needs regarding data, services and products are taken into consideration by CRSPs when designing their products?			0.5
<b>4</b>	<b>Governance and Risk Management</b>			<b>1.5</b>
4.1.	Are there clear policies and procedures in place to manage conflicts of interest arising from shareholders or managers?			0.25
4.2.	Are all existing CRS in the country audited by an independent and certified auditor?			1.00

4.3	Have business, operational, reputational and legal risks related to CRS been identified and policies are in place to address and mitigate such risks?			0.25
4.4	Is board composition and their roles and responsibilities clear and publicly disclosed in all CRS?			0.25
<b>5</b>	<b>Legal and Regulatory Environment</b>			<b>2.5</b>
5.1	Is the legal framework covering credit reporting systems clear, non-discriminatory and supportive of SMEs' rights?			1
5.2	Are there any conflicts of law or legal vacuums in aspects related to the CRS that impede the development of efficient, safe and reliable CRS?			0.25 (If answer No, then score 0.25)
5.3	Does the legal and regulatory framework underpinning the permissible uses of the government held-data allow CRSPs to collect and exploit information (e.g. property registrar, companies' registrar, judicial courts)?			0.25
5.4	Are sole proprietors and shareholders treated as data subjects in the respective data protection/privacy laws in the country?			0.5 (If answer No, then score 0.25)
5.5	Are data subject's rights recognized by law and exercised in practice by CRSPs including (i) the right to object to their information being collected for certain purposes and/or used for certain purposes, (ii) the right to be informed on the conditions of collection, processing and distribution of data held about them, (iii) the right to access data held about them periodically at little or no cost, and (iv) the right to challenge accuracy of information about them?			0.5
<b>6</b>	<b>Cross-Border Data Flows</b>			<b>1</b>
6.1	Are there market conditions, economic and financial integration requirements and/or any legal and regulatory requirements that call for the exchange of credit information across borders?			0.25
6.2	Are there mechanisms in place to facilitate exchange of credit information between two or more jurisdictions for the evaluation of the creditworthiness of debtors (e.g. law, regulation, bi-lateral agreements)?			0.25
6.3	Does the exchange of information between two different jurisdictions take place through any of the following: (i) direct exchange, (ii) portability model or (iii) right to access model?			0.50

## Glossary of Terms

**Commercial Credit Reporting Companies:** Entities that collect information on businesses, including sole proprietorships, partnerships and corporations for the purpose of credit risk assessment, credit scoring or for other business purposes such as the extension of trade credit.

**Consent:** A data subject's freely informed and specific agreement, written or verbal, to the collection, processing and disclosure of personal data.

**Consumer;** An individual or a business whose data could be collected, processed and disclosed to third parties in a credit reporting system

**Credit Bureau:** Model of credit information exchange whose primary objective is to improve the quality and availability of data for creditors to make better-informed decisions.

**Credit Rating Agency:** An entity that typically assigns a credit grade or rating to issuers of certain types of debt obligations. More recently credit rating agencies assign a credit rating to some financial institutions, despite whether the latter are issuing securities in the marketplace or not, and have even entered into new business lines, including in some cases credit reporting.

**Credit Registry:** Model of credit information exchange whose main objectives are: assisting bank supervision and enabling data access to regulated financial institutions to improve the quality of their credit portfolios.

**Credit Reporting Service Provider (CRSP):** An entity that administers a networked credit information exchange.

**Credit Reporting System (CRS):** Describes the broader institutional framework for credit reporting in an economy, including the following: (1) the public credit registry, if one exists; (2) private credit reporting firms, if they exist, including those run by chambers of commerce, bank associations, and any other organized database on borrower performance available in the economy; (3) the legal framework for credit reporting; (4) the legal framework for privacy, as it relates to credit reporting activities; (5) the regulatory framework for credit reporting, including the institutional capacity in government to enforce laws and regulations; (6) the characteristics of other pertinent borrower data available in the economy, such as data from court records, utility payments, employment status; (7) the use of credit data in the economy by financial intermediaries and others, for example, the use of credit scoring or use of credit data in creating digital signatures; and (8) the cultural context for credit reporting, including, for example, the society's view on privacy and the importance accorded to reputation collateral.

**Credit Reporting System Participant:** Any individual or business that intervenes at one or more points throughout the cycle of collecting, storing, processing, distributing and, finally, using information to support credit-granting decisions and financial supervision.

**Credit Scoring:** A statistical method for evaluating the probability of a prospective borrower fulfilling its financial obligations associated with a loan.

**Creditor:** One to whom a financial obligation is owed. Also, an individual or legal person who is engaged in the business of lending money or selling items for which immediate payment is not demanded but an obligation of repayment exists as of a future date.

**Creditworthiness:** The ability of a borrower to repay current and prospective financial obligations on a timely manner. It is used as an assessment of a borrower's past credit behavior to assist a potential lender to decide whether or not to extend new credit.

**Data Subject:** An individual or a business whose data could be collected, processed and disclosed to third parties in a credit reporting system.

**Financial Infrastructure:** The underlying foundation for a country's financial system. It includes all institutions, information, technologies, rules and standards that enable financial intermediation.

**Hit:** A positive match from an inquiry on a data subject is made by a creditor or other party and the data stored in a credit reporting service provider. Hit rate indicates the percentage of hits per enquiries made to the CRS.

**Late Payment:** Any payment posted after the due date (see arrears). In the credit report is represented by the number of days after the due date.

**Lender:** See Creditor.

**Negative data:** It consists of statements about defaults or arrears and bankruptcies. It may also include statements about lawsuits, liens and judgments that are obtained from courts or other official sources.

**Other Data Sources:** Entities that collect information for purposes different than credit granting decision-making and/or financial supervision. These entities typically do not pro-actively provide the information they collect to credit reporting service providers but rather can be consulted upon request.

**Payment history:** A detailed compilation of past and current payment behavior.

**Positive Data:** Information that covers facts of contractually compliant behavior. It includes detailed statements about outstanding credit, amount of loans, repayment patterns, assets and liabilities, as well as guarantees and/or collateral.

## Secured Transactions & Collateral Registries

### Introduction

According to research, providing legal and institutional structures through which movable assets can be effectively used as collateral significantly improves access to finance by those firms that need it the most. Well-functioning secured transactions systems enable businesses to use their assets as security to generate capital.

Further economic analysis suggests that SMEs in countries that have stronger secured transactions laws and registries have greater access to credit, better ratings of financial system stability, lower rates of non-performing loans. The end result is higher productivity and more growth.

The G20 Action Plan on SME Financing identified the development of credit infrastructure for SMEs including improvements of secured transactions systems as a key priority. The area of secured transactions is where the disparity among G20 countries' performance is the greatest. For example, some G20 jurisdictions still use document registration, which requires delivery and recording of the agreement and possibly other documentation at the registry, instead of a modern notice registration system. Other countries do not have a centralized registry or a single registry for all types of movable assets.

In such context, the diagnostic assessment against SME-related aspects of international standards is recognized as an area of focus including the assessment against the World Bank ICR Principles (2015) and the UNCITRAL Legislative Guide on Secured Transactions (2007).

### Instructions

The purpose of the exercise is to enable countries to conduct a self-assessment of their respective legal and institutional frameworks supporting secured transactions. The questionnaire consists of 5 key pillars which are critical for understanding the extent to which secured transactions frameworks meet international standards of best practice.

Each pillar/category contains several questions which raise the most important aspects related to creation, third party effectiveness, priority, publicity and enforcement of security interests. The objective behind the questionnaire is to reflect key principles of modern secured transactions systems; however, not all aspects were included considering that the goal of the exercise is to conduct a high level assessment with a simplified framework.

Respondents should carefully read the questions below and answer "yes" or "no", based on their understanding of the framework in question. It will be critical to review closely the glossary of terms which is provided to ensure the responses are based on the accurate interpretation of the terms and phrases used in the questionnaire. Responses to the questions will primarily require knowledge of jurisprudence, however in some cases the responses may have to be vetted with entities responsible for registration of security interests.

## Market development stages

### 1. Developed

In an advanced legal framework, secured creditors can effectively create, publicize and enforce their rights over movable assets of debtors. Such rights can be created over all types of movable assets (tangible and intangible, present or future) of all kinds of debtors (legal entities, sole proprietors, individuals). Legislation establishes clear and transparent priority scheme of various creditors and lienholders in case of competing claims and secured creditors can rely on the out of court procedures to enforce their rights or fast and effective judicially supported enforcement procedures. Institutional framework permits all kinds of creditors and lienholders to publicize their rights through on-line notice based registry in an effective and efficient way.

Therefore, an advanced legal framework should satisfy two criteria:

- a. Contain the majority of the elements in sections 1, 2, 4 and 5 described above and as a result score above 7.5/10 in the questionnaire.
- b. Contain all the elements described in questions 1.1 - 1.6; 2.1 - 2.3; 4.1 - 4.3 and 5.1-5.3 since these issues are considered critical for effective and modern framework.

### 2. Developing

In a developing legal framework, even though some aspects of the legal and institutional systems require improvement and further reform is needed, key elements of effective creditors and debtors rights are in place. In this context, the legal system permits creation of enforceable security right over present and future movable assets, allows general description of these assets, contains unambiguous priority scheme; permits secured creditors to enforce their rights out of court. Finally, a registry is in existence that provides creditors means to ensure transparency of their rights vis-à-vis third parties.

As a result, a developing legal framework a) scores greater than 5 and less than or equal to 7.5 out of 10 in the questionnaire and b) contains all the elements described in questions 1.3 – 1.6; 2.3; 4.1; 5.1. A legal framework is also classified as “developing” if it scores above 7.4/10 but lacks one of the elements required of a developed system as specified in (b) above under “Developed” category.

### 3. Formative

A formative legal framework can be described as a framework that has many deficiencies and lacks many of the basic concepts described in the questionnaire. There are gaps in coverage of certain types of assets as potential collateral and in the registration system. Specifically, these deficiencies can include (but are not limited to): no assurance of priority of security interests given lack of uniform treatment of various security interests and liens and lack of efficient publicity mechanisms; fragmented registries according to type of collateral, type of legal interest, type of borrower or geography; use of document registration, resulting in arbitrariness/error in registration, burdensome procedures which can be lengthy, and lead to disclosure of proprietary information; complex and slow enforcement process that requires time-consuming and costly judicial intervention. As a result, a formative legal framework scores 5 or below in the questionnaire.

## Accessing Questionnaire

	<b>International Best Practices Issue/Subject matter</b>	<b>Yes</b>	<b>No</b>	<b>Score</b>
<b>1.</b>	<b>Scope and Creation</b>			<b>2.5</b>
1.1.	Does an integrated or unified legal framework for secured transactions exist and extend to the creation, publicity, priority and enforcement of at least 3 functional equivalents to security interests in movable assets (fiduciary transfers of title; leases; assignments or transfers of receivables; and sales with retention of title)?			0.3
1.2.	Does the legal framework allow for security agreement to become effective and enforceable between the secured party and the grantor upon attachment without the need for registration of the agreement?			0.2
1.3.	Does the law allow businesses to grant a non-possessory security interest in a single category of movable assets, without requiring a specific description of encumbered asset?			0.3
1.4.	Does the law allow businesses to grant a non-possessory security interest in substantially all of its assets, without requiring a specific description of encumbered asset?			0.3
1.5.	May a security interest extend to future or after-acquired assets?			0.3
1.6.	May a security interest extend automatically to the products, proceeds or replacements of the original encumbered assets?			0.3
1.7.	May a security interest attach to and continue in movable assets that becomes affixed to immovable property?			0.2
1.8.	Is a general description of debts and obligations permitted in security agreements?			0.2
1.9.	Can all types of debts and obligations (e.g. monetary or non-monetary, pre-existing, present or future, conditional or unconditional) be secured between parties?			0.2
1.10	Can the security agreement include a maximum amount for which the assets are encumbered (e.g. a line of credit)?			0.2
<b>2.</b>	<b>Third Party Effectiveness and Priority</b>			<b>2.0</b>
2.1.	Does the law permit the following methods for achieving third party effectiveness: (1) registering a notice of the security interest in the registry; (2) secured party taking possession of the asset; (3) secured party taking control of the asset (e.g. a deposit account);			0.6
2.2.	Does the law permit the secured party to pre-file a notice of security interest in the registry before such interest is created with the priority dating back to the time of registration?			0.6
2.3.	Does the law uphold the “first in time – first in right” principle to determine the order of priority in case of competing security interests (subject to established exceptions from this principle)?			0.6
2.4.	Do third parties take free of a security interest that was made effective against third parties when the asset subject to a security interest is sold, leased, licensed or otherwise disposed if such sale, lease, license or disposition was conducted in the ordinary course of grantor’s business?			0.2



<b>3.</b>	<b>Registration &amp; Priority of liens</b>			<b>1.5</b>
3.1.	Does the law permit registration of notices in the Security Interest Registry of various liens created by operation of law such as tax liens, labor liens and judgement liens?			1.0
3.2.	Does the “first in time – first in right” rule of priority also apply to the rights of lienholders such as tax authorities, judgement creditors, etc.?			0.5
<b>4.</b>	<b>Enforcement</b>			<b>2.0</b>
4.1.	Does the law allow parties to agree on out of court enforcement at the time a security interest is created or by a separate agreement before occurrence of an event of default?			0.5
4.2.	Does the law allow the secured party to enforce its rights through expedited judicial or other official enforcement proceedings?			0.5
4.3.	Does the law allow the secured party to sell the encumbered asset through public auction, private tender or any commercially reasonable means?			0.5
4.4.	Does the law allow a secured party to proceed with taking possession and disposition of encumbered asset despite the debtor or grantor filing objection or a lawsuit against such action by the secured parties?			0.5
<b>5.</b>	<b>Registration and registry</b>			<b>2.0</b>
5.1.	Is there a unified, electronic Registry for security interests in all types of movable assets for both individual and legal entity grantors?			0.4
5.2.	Does the law permit registration of security interests, their functional equivalents and interests of lienholders in a Security Interests Registry?			0.4
5.3.	Does a Security Interest Registry exist in which only a notice of existence or potential existence of a security interest is registered with no requirement to provide or attach documentary evidence of existence of a security interest?			0.4
5.4.	Does a Security Interest Registry exist in which registrations, amendments and cancellations can be made by secured parties online?			0.4
5.5.	Does a Security Interest Registry exist in which searches can be performed on-line by any interested third party using grantor’s identifier?			0.4

## Glossary of Terms

**Assignments or Transfers of Receivables:** assignment of receivables is understood here as the creation of a security right in a receivable that secures the performance of an obligation. Although outright transfers of receivables are transfers not intended to secure an obligation, as exception, they are included in the scope of secured transactions law and for convenience of reference the term is included in the assignment of receivables.

**Attachment:** completion of all conditions necessary to make a security interest enforceable against the debtor with respect to the collateral. Attachment occurs when a) a security agreement is signed; b) a secured party provides consideration and c) grantor has alienable right in the collateral.

**Debtor:** a person who owes payment or other performance of a secured obligation, whether or not the person owns or has rights in the collateral, and includes a seller of accounts receivable or secured sales contracts, and a lessee of goods.

**Expedited judicial or other official enforcement proceedings:** enforcement of security interest by a secured party conducted with the support from judiciary (e.g. Judge of Urgent Matters issuing a court order), or other formal authorities (e.g. public notaries issuing a notary writ subject to execution) in an expedited manner without conducting litigation.

**Fiduciary Transfers of Title:** fiduciary transfer is understood here as transfer of ownership for security purposes until the debt is extinguished.

**“First in time – First in right”:** general priority principle which establishes that the priority of secured parties’ competing interests in collateral is determined by the date and time of achieving third party effectiveness. There are also a number of exceptions to this general rule such as for instance: a) “ordinary course of business” exception which allows the transferee to acquire assets subject to a security interest that are transferred in the ordinary course or grantor’s business free from the security right of the secured party; b) “purchase money security interest” exception rule which (under certain circumstances) grants the purchase money security creditor priority over prior security interest in the same category or class of collateral; c) “right of retention” exception which grants the person holding possession of the goods until paid priority as against the secured party holding security interest in these goods.

**Fixture:** goods that are fixed or are intended to become fixed to immovable property in a manner that causes a property right to arise in the goods. Building materials and readily removable factory machines, office machines, and domestic appliances are not fixtures.

**Functional Equivalents of Security Interests:** Any transaction that in substance creates a security interest in favor of secured party over movable property of the grantor. Such transactions cover all rights in movable assets that are created by agreement and secure the payment or other performance of an obligation, regardless of the form of the transaction or the terminology used by the parties (including rights of transferees under a transfer of title to tangible assets for security purposes, rights of an assignee under an assignment of receivables for security purposes,

as well as rights of sellers or financial lessors under various forms of retention-of-title agreement and financial leases, respectively).

**Future or After-Acquired Assets:** assets that do not yet exist or are owned by the debtor.

**Grantor:** a person that creates a security interest to secure either its own obligation or that of another person.

**Grantors' identifier:** name or unique identification number (national ID, taxpayer registration number, etc.) which identifies a person that creates a security interest to secure either its own obligation or that of another person.

**Judgement Creditor:** a party to which a debt is owed that has proved the debt in a legal proceeding and that is entitled to use the judicial process to collect the debt.

**Lien-holder** – a person who obtains a right in collateral by order of a court or other legal authority, or by the authority of an administrator in an insolvency proceeding, or any other person who obtains a right in collateral by operation of law, except a person with a right of retention.

**Lease:** means a lease whether financial or operational where the leased asset is transferred in the possession of the lessee for the period exceeding 12 months.

**Non-Possessory Security Interest:** a security interest created in favor of a secured party where such parties do not hold the possession of the asset subject to security interest.

**Notice:** a record registered in the registry. The term includes an initial notice, amended notice, continuation notice, termination notice and notice of objection.

**Notice-Based Security Interest Registry:** An electronic internet-based registry which permits users to a) file notices directly on-line without scrutiny of the information on the part the Registrar and b) perform searches on-line.

**Ordinary Course of Debtor's Business:** refers to a transfer of movable property by a person who deals in the kind of property transferred.

**Out of Court Enforcement:** enforcement of security interest by a secured party without intervention or support from judicial or other formal authorities of the state.

**Pre-filing of notice:** refers to a registration of a notice in the Security Interests Registry before the attachment of the security interest. In case of pre-filing of a notice, secured party's priority right dates back to the time of the notice registration (as opposed to the date and time of attachment).

**Proceeds:** means identifiable or traceable movable property in any form derived directly or indirectly from any dealing with the collateral or the proceeds therefrom.

**Purchase money security interest** – a security interest taken by a seller of goods to secure their price or by a person who gives value to enable a debtor to acquire goods.

**Right of retention** – the right of a person who provides services or materials to maintain or enhance the value of goods to retain possession of the goods until paid for the services or materials.

**Sales with Retention of Title:** such sale in which title to the goods remains vested with seller until the purchase price has been paid in full by the buyer.

**Security Agreement:** an agreement, regardless of whether the parties have denominated it as a security agreement, between a debtor and a secured party that provides for the creation of a security interest.

**Secured Party:** a person in whose favor a security interest is created under a security agreement.

**Secured Transactions:** Legal and institutional framework which supports the use of movable property as collateral for both business and consumer credit.

**Specific Description:** a description of collateral that relies on individual characteristics of the asset as opposed to generic characteristics where asset can be described as a separate class or a category.

**Third Party Effectiveness:** Effectiveness of a security interest against third parties which is achieved by registration of an interest in the Security Interest Registry or possession by the secured party.

## Insolvency

### Introduction

Effective insolvency regimes have a dual aim: to save viable businesses and to ensure that non-viable businesses can quickly exit the market, allowing the deployment of assets to more productive firms. This is particularly important in liberating productive resources from an unproductive enterprise and in ensuring that creditors and potential investors are protected if a business fails.

A number of studies demonstrate that the positive results of developing effective and efficient insolvency systems can be extended throughout the economy. Insolvency reform, along international best practices, has been linked to lower cost of credit, increased access to credit, improved creditor recovery, strengthened job preservation, promotion of entrepreneurship, and other benefits for small businesses. Countries that implement sound insolvency regimes also manage to increase financial inclusion and thereby promote overall economic stability. A systematic approach to debt resolution and insolvency thus strengthens the investment climate and advances economic growth.

The G20 Action Plan on SME Financing identified the development of credit infrastructure for SMEs, including improvements of insolvency frameworks, as a key priority. Results show that there is significant disparity between G20 countries in terms of efficiency of insolvency regimes and that some countries are far from implementing best international practices. For example, in several G20 countries early restructuring is not possible. In others, secured creditors are not affected by the automatic stay, or it is impossible for debtors to obtain fresh-financing during insolvency proceedings. As a result, viable businesses are channeled into liquidation thereby resulting in a significant loss of value for the economy.

The questionnaire focuses on the most important SME-related aspects of such a framework and its questions are grouped into five major categories: 1) Pre-insolvency procedures: the existence of a framework for preventive restructuring, 2) Automatic stay: the efficiency of the rules relating to the moratorium on creditors' enforcement actions following the commencement of proceedings, 3) Insolvency estate: the rules that regulate the management of the debtor's assets in the course of proceedings, 4) Reorganization plan: the provisions governing the content of a reorganization plan as well as the process of voting and approval and 5) Insolvency Practitioners and SME Insolvency: the framework for the regulation of Insolvency Practitioners and the existence of specialized streamlined procedures for SMEs.

### Instructions

The purpose of this questionnaire is to enable participants to conduct a self-assessment of their respective legal frameworks on the particular issue of SME insolvency. The questionnaire focuses on the most important aspects of such a framework and its questions are grouped into five major categories that are critical for understanding the extent to which insolvency frameworks meet international standards of best practice.

Due to the significant disparity among countries regarding the definition of the term, SMEs are not strictly defined in this document and respondents should use their own "national" definition of an

SME in completing this questionnaire. Respondents should carefully read the questions below and answer “yes” or “no”, based on their understanding of the legal framework in question. The answers should reflect the legal environment of their country and take into account all available measures and procedures, regardless of differences in terminology. Each question is assigned a particular score in the overall matrix, the sum of which adds up to a score of 10.

The present document however is strictly limited to the purpose of providing G20 countries with a framework and a methodology to measure the ability of their legal framework to deal with the specific issue of SME insolvency. As such, it should under no circumstances be viewed as a substitute, an accessory or in any way fully representative of the international standards or assessment methodologies in the field of insolvency law, namely the World Bank Principles on Insolvency and Creditor Rights (the ICR standard) and the Reports on the Observance of Standards and Codes (ROSC). Therefore, more in-depth assessments are encouraged.

## Market development stages

### 1. Developed

In an advanced legal framework, insolvent debtors are given the opportunity to initiate proceedings before formal insolvency and are allowed to remain in control of their business. Furthermore, upon commencement of insolvency proceedings, debtors are afforded protection from creditors’ enforcement actions, with due consideration to the interests of secured creditors. During the course of proceedings, the law facilitates the continued operation of the debtor’s business, maximizes the value of its assets and encourages debtors to achieve reorganization. A developed legal framework also contains provisions on the qualifications and duties of insolvency practitioners, allows debtors to obtain a discharge of their residual debts following a liquidation of their assets and finally provides SMEs with access to special and expedited proceedings for reorganization.

Therefore, an advanced legal framework should satisfy two criteria:

- a. Contain the majority of the elements in all five sections described above and as a result score above 7.5/10 (top quarter) in the questionnaire.
- b. Contain all the elements described in questions 1.1, 2.1, 3.2, 3.3 and 5.1 since these issues are considered crucial and weigh significantly in the scoring system.

### 2. Developing

In a developing legal framework, insolvent debtors face certain difficulties in accessing proceedings and achieving a successful reorganization of their business. These difficulties may refer, among other things, to lack of access of a preventive restructuring framework, inability to obtain post commencement financing or obstacles to discharge. Furthermore, creditors also face a number of challenges such as the inability to obtain relief from the automatic stay or unworkable voting provisions. In general, however, a developing legal system contains many of the elements of a developed framework and works well in practice by facilitating the restructuring of viable businesses despite the obstacles described above.

As a result, a developing legal framework scores greater than 5 and less than or equal to 7.5 out of 10 in the questionnaire. A legal framework is also classified as “developing” if it scores above 7.5/10 but lacks one of the central elements required of a developed system as specified in (b) above.

### **3. Formative**

A formative legal framework can be described as a framework that has many deficiencies and lacks many of the basic concepts described in the questionnaire. These deficiencies can include (but are not limited to) the absence of a system for the regulation of insolvency practitioners, the absence of a mechanism for the management of the estate and the rejection of contracts or even the complete absence of reorganization provisions. In such a context, debtors face many difficulties in achieving reorganization and liquidation is the most prevalent outcome, keeping creditor recoveries low. As a result, a formative legal framework scores 5/10 or below in the questionnaire.

## Accessing Questionnaire

	<b>International Best Practices Issue/Subject matter</b>	<b>Yes</b>	<b>No</b>	<b>Score</b>
<b>1</b>	<b>Pre-Insolvency Procedures</b>			<b>1.5</b>
1.1	In addition to formal, fully court-supervised insolvency procedures, does the insolvency framework provide debtors, both SMEs and larger corporates, with access to a separate procedure that allows them to restructure their business with the objective of preventing insolvency, containing the following elements:			0.8
	a) Is the debtor able to access such procedure at an early stage, as soon as it is apparent that there is a likelihood of insolvency but before defaulting on a particular payment?			0.3/0.8
	b) Does the debtor keep control over the day-to-day operation of its business?			0.2/0.8
	c) Is a restructuring plan adopted by a majority of creditors binding on all creditors, provided that the plan is confirmed by a court?			0.3/0.8
1.2	Does the law require that when directors of the debtor know, or should have reasonably known, that insolvency is imminent or unavoidable, they should take reasonable steps either to avoid insolvency, or where insolvency is unavoidable, to minimize its extent and file for a pre-insolvency or insolvency procedure?			0.3
1.3	In case such an obligation exists, does the obligation include any person formally appointed as a director AS WELL AS any other person exercising factual control and performing the functions of a director?			0.2
1.4	In case of breach of the obligation mentioned in the 2 questions above, does the insolvency law impose liability on the directors of the debtor that may amount up to the loss or damage suffered by creditors as a result of the breach?			0.2
<b>2</b>	<b>Automatic Stay</b>			<b>2.0</b>
2.1	Are enforcement actions by ALL creditors subject to an automatic stay (or an automatic suspension or moratorium) upon commencement of insolvency proceedings?			1.0
2.2	Is there a time limit prescribed by law on the automatic stay imposed on the secured claims? If yes, what is the time limit? If yes, does the law stipulate that secured creditors may request that the stay is lifted (relief) when the collateral is not needed for the reorganization or sale of the business as a going concern OR when the stay poses a great risk to the existence of the collateral (e.g. perishable goods)?			0.5
2.3	Does the law allow insolvency representatives to provide additional or substitute assets to compensate for the diminution of value of the encumbered assets due to the stay?			0.3
2.4	Does the law require payment of interest during the period of stay?			0.2
<b>3</b>	<b>Insolvency Estate</b>			<b>2.5</b>
3.1	Does the insolvency framework allow the continuation of contracts supplying essential goods and services to the debtor (goods and services necessary for the survival of the business), even where the debtor is in breach?			0.5



3.2	Does the insolvency framework allow the rejection by the debtor (or by the insolvency representative or by the court on the debtor's behalf) of overly burdensome contracts (the cost of performance is greater than the benefit to be received), where both parties have not fully performed their obligations?			0.7
3.3	Does the insolvency framework provide for the possibility of the debtor obtaining credit after commencement of insolvency proceedings (post-commencement credit) to finance its on-going needs during the proceedings?			1
3.4	Does the insolvency framework assign priority to post-commencement credit?			0.3
<b>4</b>	<b>Reorganization Plan</b>			<b>2.0</b>
4.1	Does the law allow for the submission of restructuring plans and mandate that such plans contain:			1.0
	a) A clear and complete identification of the creditors who would be affected by the plan, potentially dividing them in classes?			0.3/1.0
	b) The effects of the proposed restructuring on individual debts or categories of debts or classes?			0.3/1.0
	c) Identification of the role of the debtor in the implementation of the plan?			0.2/1.0
	d) Description of the viability of the business and the likelihood that the plan will succeed, once implemented?			0.2/1.0
4.2	Does the insolvency law specify that a creditor whose rights are modified or affected by the plan should not be bound to the plan unless that creditor has been given the opportunity to vote on the plan?			0.2
4.3	Does the insolvency law specify that creditors entitled to vote on the plan should be separately classified according to their respective rights and that each class should vote separately?			0.5
4.4	Does the insolvency law specify that all creditors in identical circumstances must be offered the same treatment?			0.3
<b>5</b>	<b>Insolvency Practitioners and SME Insolvency</b>			<b>2.0</b>
5.1	Does the insolvency framework provide the following?			1.0
	a) The qualifications and qualities required for the appointment of the insolvency representative?			0.4/1.0
	b) That the insolvency representative has an obligation to protect and preserve the assets of the estate?			0.3/1.0
	c) The consequences of the insolvency representative's failure to perform its duties and functions under the law?			0.3/1.0
5.2	Where natural persons are eligible as debtors under the insolvency law, does the law allow a discharge of those debtors from liability for pre-commencement debts?			0.2
5.3	If the insolvency law allows a discharge of natural persons, is that discharge subject to any conditions, like not acting fraudulently and cooperating with the insolvency representative during the insolvency case?			0.2

5.4	Does the law specify that the discharge does not apply until after the expiration of a specified period of time following commencement, during which period the debtor is expected to cooperate with the insolvency representative?			0.2
5.5	Does the insolvency framework specify abbreviated procedures for small cases or SMEs, where certain stages of the insolvency procedure can be streamlined or merged into other phases (e.g. verification of claims, report by the insolvency practitioner, simpler voting mechanisms, etc.)?			0.4

## Glossary of Terms

**Automatic Stay:** A measure that prevents the commencement, or suspends the continuation, of judicial, administrative or other individual actions concerning the debtor's assets, rights, obligations or liabilities, including actions to make security interests effective against third parties or to enforce a security interest; and prevents execution against the assets of the insolvency estate, the termination of a contract with the debtor, and the transfer, encumbrance or other disposition of any assets or rights of the insolvency estate.

**Collateral:** An encumbered asset

**Commencement of proceedings:** The effective date of insolvency proceedings whether established by the law or by a decision of the court.

**Court:** A judicial or other authority competent to control or supervise insolvency proceedings.

**Creditor:** A natural or legal person that has a claim against the debtor that arose on or before the commencement of insolvency proceedings.

**Debtor:** Any natural or legal person in financial difficulties that is the subject of an insolvency or pre-insolvency procedure.

**Discharge:** The release of a debtor from claims that were, or could have been, addressed in the insolvency proceedings.

**Encumbered asset:** An asset in respect of which a creditor has a security interest

**Estate:** Assets of the debtor that are subject to insolvency or pre-insolvency proceedings.

**Insolvency:** A situation, where a debtor is generally unable to pay its debts as they mature and/or where its liabilities exceed the value of its assets.

**Insolvency Procedures:** Collective proceedings, subject to court supervision, either for reorganization or liquidation.

**Insolvency Representative:** A person or body (including one appointed on an interim basis) authorized in insolvency proceedings to administer the reorganization or the liquidation of the insolvency estate.

**Liquidation:** A process through which the assets of the debtor are sold and disposed for the collective distribution of the proceeds among its creditors.

**Pre-insolvency Procedure:** A collective proceeding that enables the debtor to restructure at an early stage with a view of preventing its insolvency.

**Priority:** The right of a claim to rank ahead of another claim where that right is stipulated by the law.

**Reorganization:** A process through which the financial well-being and viability of a debtor's business may be restored so that the business can continue to operate, through means that may include debt

forgiveness, debt rescheduling, debt equity conversions and sale of the business (or parts of it) as a going concern.

**Restructuring plan:** A plan by which the financial well-being and viability of the debtor's business can be restored.

**Sale as a going concern:** The sale or transfer of a business as a whole or in substantial parts, as opposed to the sale of separate assets of the business.

**Secured claims:** A claim assisted by a security interest in an asset taken as a guarantee for a debt enforceable in case of the debtor's default.

**Secured creditor:** A creditor holding a secured claim.

**SME:** The "national" definition of a small and medium sized enterprise according to the legal framework in question