RESOLVING CORPORATE DISTRESS IN A FAST CHANGING GLOBAL ECONOMY

Harvard negotiation as a concept to improve and speed up reorganization proceedings in Poland? A case study from the Netherlands

1. Introduction

Today’s global and technological driven economy asks for companies to be flexible with regard to their business models and strategies. Yesterday’s success easily can be tomorrows’ failure while large traditional and matured companies sometimes seem to be subjected to be swept away “in a minute” by small fairly recently started-up techno-

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driven companies. Corporate bankruptcies being the sad result of it. For that reason it does not seem unwise to state that today’s local business laws should be flexible and as a consequence have the ability – if theoretically possible – to facilitate companies as much as possible in changing business strategies and behavior fast, if needed in a given situation. This specifically seems to apply for reorganization provisions of insolvency laws – in the Netherlands for instance called (translated) Suspension of Payments (art. 213) and in Poland named Preliminary Reorganization Proceedings (art 519) – as these procedures their selves are designed to help firms overcome temporary financial difficulties. Yet research shows that formal reorganization provisions often do not lead to satisfying results. Moreover, evidence exists that failure rates of reorganization procedures in most countries actually do exceed successful ones. For instance, in the Netherlands about 73% of the suspension of payment procedures fail, and in the United States only a minority of companies in distress apply for so-called Chapter 11 and even then most of these are not able to use the provision for its intended form, that is to say providing “breathing space” for company management to turn the company around and work out a deal with relevant creditors. Poland – although incorporating a relatively modern Bankruptcy Act – also does not seem to live up to expectations regarding court-supervised formal reorganization procedures. So, while being in distress for company management in general a court-led reorganization proceeding is not a promising area to enter. In addition, as formal reorganization rules generally require public announcement – to be precise the insolvent company is registered as filing for reorganization protection in newspapers and/or other forums – this in itself will often trigger vendors, financiers and also customers to stop doing business with the company; in fact as a consequence provoking liquidation of the company as necessary working capital then is diminished and sales volumes drop instantly. This so-called self-fulfilling prophecy phenomenon makes formal insolvency procedures largely inefficient and therefore unattractive, also because by entering legal procedures managerial control is lost. Companies in distress in dire need for a quick solution and not willing to be subjected to harsh and unpredictable stakeholder behavior therefore need better ways to resolve risen problems. Harvard negotiation theory seems to provide for an answer.

This article aims at giving ideas and insights to improve reorganization processes respectively entrepreneurship climates in given countries. Based on a case study from The Netherlands it is argued that business communities can and should take control of the insolvency process themselves in order to meet the demanding challenges of the 21st century.

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4 See Lowitzsch 2007, p. 325-326.
Resolving corporate distress in a fast changing global economy

century. It is shown that bottlenecks regarding resolution of financial distress often can be traced back to interrelationships of interested parties. Consequently focusing thereon seems more effective than simply looking for court protection in order to effectively handle (future) obligations.

First the concept of Harvard negotiation is briefly described (paragraph 2) subsequent a case study called “Techno Group” is presented (paragraph 3). In paragraph 4 found bottlenecks and conflicts are given and then further worked out in paragraph 5 using Harvard negotiation theory as an analysis instrument. Paragraph 6 contains a conclusion proposing Harvard negotiation as an instrument for practice in dealing with financial distress.

2. Harvard negotiation

The concept of Harvard’s “principled, problem-solving negotiation theory” is a result of the so-called Harvard Negotiation Project. Developed over the last decades and often referred to as “Harvard negotiation” it is a theory on effective negotiation and conflict resolving. Negotiation can be described as “the process we use to satisfy our needs when someone else controls what we want” and core of the Harvard negotiation concept is to always use a problem-solving approach in this process (as opposed to a “competitive approach”). The approach is based on four principles, to be summed up as follows.

1. [People] Adopting a problem-solving approach and not allowing personality differences to side-track this;
2. [Interests] Avoiding taking and defending positions but rather concentrating on parties’ respective interests;
3. [Options] Before making decisions, generating as many options as possible, particularly those creating mutual benefit;
4. [Criteria] Establishing objective and fair criteria for a resolution, rather than the judgment of either party.

Research has shown that by using this theoretic concept it is in fact possible to create value for all parties involved in any conflict. Yet it then is necessary that all parties involved adopt a “co-operative, problem-solving mode, with pooled information, a flexible and creative approach and an appreciation of one another’s interests and concerns”. Major advantage of using this method is that parties find a solution together. And because it is the parties themselves who determine the outcome, the level of acceptance will be higher. Decisions are not imposed – as is often the case in court-led reorganizations – but found together. This decreases the chance of (further) frustration in this respect. In addition, the pace can be set by the parties themselves and they are in full control thereof. Accordingly, the advantage is increased flexibility. Parties can for example – if necessary – make a joint decision to (partly) deviate from (legal) rights and

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obligations that apply to both, whereby a solution is brought closer, without being imposed on the parties.

3. Case study

As announced, below a description is given of a reorganization process that eventually failed. The case provided was taken from an extensive research project by Leiden University – partly commissioned by the Dutch Ministries of Justice and Economic Affairs – into the relationship between informal reorganization routes and (formal) reorganization legislation. For reasons of privacy all names, products and years were made anonymous. Some parts of the text are encoded (A, B, C...). These parts will be elaborated in the subsequent analysis as specific bottlenecks in which (Harvard) negotiation may play part. First of all a short description of the company profile is given, subsequently the so-called process of insolvency. The case study ends with a description of the events around bankruptcy. Although the case turned out to be exemplary for failed rescue operations it is not the intention to define an exhaustive list of insolvency related conflicts (which probably also is impossible). Obviously most occurring conflicts regarding imminent insolvency are present in the case.

Techno Group

[Company profile] The Techno Group consists of Techno Holding Ltd. which holds a 100% share interest in Techno Ltd. Techno Ltd. has participating interests abroad. The group is owned by a number of investment companies. The group develops technologically high-quality machinery and also coordinates large (international) projects with regard to the installation of the machines. The production and installation in this respect is carried out by external partners, assembly though is (partly) completed in-house. In addition, technological knowledge is exploited by issuing licenses to (international) producers. The company is known to be innovative and is a market leader. In 1998, the company employs around 50 people.

[Insolvency process] At the end of 1994 the company is placed in the Intensive Care Department of its so-called housebank (A). The company suffers from an acute liquidity problem as a result of rising figures in balance sheet items such as stock and accounts payable. In anticipation of a number of orders, parts had already been

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6 See Adriaanse 2005, p. 6 ff. for a detailed description of the research project, including methodology. The case study ranked number 14 out of 35 cases in the project. About the project in relation to Central and Eastern Europe see also J.A.A. Adriaanse, J.G. Kuijl, Resolving financial distress: informal reorganization in The Netherlands as a beacon for policy makers in the CIS and CEE/SEE Regions?, “Review of Central and East European Law”, 2006, nr. 31, pp. 135-154.

7 To be described as the process where the company slips from healthy management into a situation where, without restructuring, a situation of insolvency will arise.

8 A housebank can be described as: bank which is the main provider of risk-avoiding capital to a company and which undertakes an information-intensive long-term relationship with the specific company (in international literature also referred to as Hausbank).
ordered and assembled to prevent problems in view of low staffing levels. However, the orders never materialized.

In 1995, in order to prevent liquidation, a workout agreement with (unsecured) creditors is set up (B) in which the company pays 30% straight away, whilst 40% is provided by the creditors in the form of a subordinated loan – 30% is waived. In addition, the shareholders inject over €2 million of risk-bearing capital. In order to carry out the future plans, lengthy discussions regarding a capital participation of €3.3 million (20% interest) are held with an interested company. These negotiations fail (C), as a result the existing shareholders decide to again introduce risk-bearing capital (to the amount of €1.4 million) in order to meet any liquidity and capital needs in line with the growing business.

Because the business is incapable to self-support any growth, the shareholders decide to sell the company in the beginning of 1999. The price range in that respect is estimated to be €40 – 60 million.

In order to meet the liquidity requirements during the selling process, a subordinated loan of €2.4 million is taken out with a bank, the existing shareholders bring in €0.8 million and the housebank increases the credit limit (from €5.4 to 6.3 million). Some of the group’s financial details are shown below.

<table>
<thead>
<tr>
<th></th>
<th>1997</th>
<th>1998</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover</td>
<td>40</td>
<td>37</td>
<td>38</td>
</tr>
<tr>
<td>Gross profit</td>
<td>3.8</td>
<td>3.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Net profit</td>
<td>-/- 0.389</td>
<td>-/- 0.791</td>
<td>-/- 2</td>
</tr>
<tr>
<td>Solvency [equity/total assets]</td>
<td>34%</td>
<td>27%</td>
<td>20%</td>
</tr>
</tbody>
</table>

Although the turnover of 1999 remains approximately the same compared to that of 1998, a steep drop in the gross margins can be detected (particularly as a result of high development costs), as a result net profits too considerably decrease. Despite the introduction of risk-bearing capital solvency reduces from 34 to 20% in three years. Profits of €0.8 million are forecast for 2000.

The attempted selling process is slow. At a certain moment an interested party tables an offer of €20 million. The shareholders decline this offer; as a result the sale falls through in the spring of 2000 (D). However, discussions with new parties are started straight away. The problem is that a number of deferred claims (project-related) weaken the salability of the group (E). In order to improve the salability, a construction is devised in which the technology is sold to a new company called New Techno Ltd. which is still to be established. This includes the transfer of staff. The new company will be owned by the current shareholders as well as a new investor. The proceeds of this transaction (€3.6 million) will see to the short-term continuity of Techno Holding Ltd. In addition, converting short-term debts into subordinated loans will be pursued as well as converting a subordinated loan into shares. The housebank, despite further deterioration of security (funding deficit is estimated to be €5.2 million), is prepared to transfer part of the overdraft finance facilities to the new company; this does require a minimum deposit of €4 million in risk-bearing capital into the new company. In addition, the bank is prepared to grant a waiver until 1 October 2000 with regard to the required solvency of 30% (as arranged in the credit
agreement). Also, an interim manager is appointed who will improve the internal organization as well as customer contact.

The cooperation of the housebank stems from trust in the relevant product market plus the company’s technological position which can be regarded as strong. In addition, it is believed that a strategic and financially strong partner will be found soon.

Early July 2000 the bank withdraws the credit (F). Reason is the fact that despite many discussions with takeover candidates, no concrete agreements have been reached. In anticipation of the realization of the intended sale, as well as the negative security position, security interests are not enforced. A couple of weeks later the company applies for a suspension of payments procedure, since the only party with which negotiations are held, has pulled out. The suspension is not granted due to a procedural error in the application.

In reaction to that, one of the shareholders submits a business plan with the bank in order to save the company from liquidation. The objective is to ultimately sell assets and activities via an organized restart (either or not via a suspension of payments procedure or a so-called “technical liquidation”). The underlying thought is to prevent loss in value of the intangible assets during an uncontrolled scenario of a suspension of payments and/or liquidation procedure (the loss in value is estimated to be € 10.4 million). Since the bank has confidence in the shareholder who, together with a number of shareholders and interested parties, is prepared to inject € 1.4 million of risk-bearing capital, the bank is willing to re-open its credit facilities for a period of three months. In those three months, the bank is informed, an organized restart will be completed during which full settlement will be made.

In April 2001, the bank concludes that ever since the credit withdrawal was reversed, the company already had to deal with over fifteen requests for liquidation (G). As a result of an open dialogue with the creditors, during which it is made clear that a transfer of assets would be in the interest of all parties, peace has been created in that respect. However, the discussions and negotiations have not resulted in a takeover as yet. A complicating factor is that clients are no longer prepared to pay deposits for (parts of) projects prior to completion (H). This puts further pressure on the liquidity. However, the bank is prepared to temporarily increase the overdraft facility by € 1 million, partly due to new-found confidence in management following the appointment of two interim managing directors.

Also, there is a dispute between another department of the bank and the company. This relates to the invoice for supervising the selling process of the company. In order to facilitate the contact between the Intensive Care Department and the company a compromise is made, meaning that part of the claim will be remitted when risk-bearing capital is introduced in settlement of the debt (I).

[Bankruptcy events] On 12 July 2001 the company yet decides to apply for a suspension of payments procedure. There appears to be a need for € 600/m to pay the salaries; payment is two months in arrears due to on-going losses (J). Since the shareholders are not prepared to inject a minimum of € 280/m this time, the bank refuses (K) to extend credit any further. In addition, a takeover candidate from France whom the company is holding discussions with seems to be aiming for a transfer of assets following liquidation (L).
At the end of July 2001 personnel files for liquidation of the company (M). Subsequently, the appointed trustee starts looking for a takeover candidate. Ultimately, on 12 September 2001, a transfer of assets is completed with an Italian party which, in addition to the assets, takes over half of the number of staff.

4. Description of bottlenecks and conflicts

In the Techno Group case no less than thirteen different bottlenecks and conflicts were found. These are more detailed below (referring to the encodings above) and in a more universal way. Because of this, although still without claiming to be exhaustive, a thorough image arises of where opportunities for private (Harvard) negotiation in reorganization routes could lie. Per conflict/bottleneck a short description is given along with a reproduction of differences in interests at stake.

(A) Intensive care versus full control

A company in (imminent) financial distress is placed under severe supervision – “intensive care” – of its housebank. This action being the result of increased doubts of bankers involved on the prospect of continuity of the company. In fact, by doing this the bankers are actually forcing the company to start reorganizing. As a result management will have or at least experience less autonomy. Main interest of the bank however is to have more direct control of the company in order to be able to force it to become profitable again en with that to (again) continue fulfilling payments with regard to repayment- and interest obligations. The conflict of interest can be described as company management wanting to have as much control on the strategic and operational direction of the company, while bankers want to intervene and (partly) take charge. Not answering this – one way or the other – can lead to withdrawal of credit lines as a result of which insolvency chances increase. Their common interest however: a fast recovery of company health.

(B) Partly versus full writing off

A company in financial distress is not able to fulfill repayment obligations due. As additional cash flow is not available – no external parties can be found at the specific moment – unsecured creditors are asked to write off a part of their claims. Underlying motive is the reasoning that when the company collapses at this specific moment the chance of full payment also is practically zero. So for them, one way or the other it always is a bad choice. Yet for company shareholders debt write-offs obviously lead to (paper) profits as the debt-equity ratio improves also leading to incoming cash flow potentially usable for other operational and financial expenses. In fact by choosing for debt write-offs (unsecured) creditors are forced to take a loss for the better of the (owners of the) company in financial distress. The interest of the company in this situation is to generate sufficient cash flow for the short term in order to prevent the company to become bankrupt. For the creditors a conflicting interest appears as direct payment – as much as possible – obviously is their primary focus. Nonetheless their common interest: a fast recovery of company health in the short term and survival for the long term.
(C) Lots for less or less for lots
A company in financial distress negotiates with third parties in order to invest in its equity, and with that to supply for additional cash flow necessary to make up for losses and inefficiencies that dried up liquidity. Primary interest of company management and its shareholders at that moment is to have as much cash injected into the company as possible, yet against a minimum transfer of ownership rights and consequently minimum loss of control. The interest of a potential investor however is exactly the opposite. Common interests though are to preserve the company from liquidation yet for company management and shareholders this interest obviously is bigger than for any potential investor; the latter simply can allocate its resources differently, and further on has nothing to loose if no agreement is reached.

(D) All or nothing
Shareholders of a company in financial distress are negotiating with a third party to buy the company. The process takes place as it is foreseen that additional risk-bearing capital is necessary in the short term (growth still cannot be financed by positive operational cash flows as losses still occur). However parties involved do not agree on the sales price of the company. The potential investor considers the company less worth than shareholders do. Shareholder’s interest is leaving the company against a price as high as possible, yet for the potential buyer the reasoning is exactly opposite. Their common interest is to preserve the company though for shareholders a bigger incentive is present (see also C) as for them forced liquidation will probably lead to (almost) total evaporation of equity invested. Although, sometimes for a potential investor strategic motives can exist – for example to further strengthen itself against competition – also providing for increased interests to actually close the deal and in that way to benefit from the transaction.

(E) Damage claim paradox
A company in financial distress is confronted with potential damage claims as a result of which salability and with that preservation of the company is jeopardized. The claimants have an interest in granting, that is to say in payment, and implicitly with that continuation of the company. Opposite, shareholders have an interest in payment obligations regarding the claims as small as possible as forced liquidation chances are increased by them. For both parties it is therefore of extreme importance, despite (perceived) opposed interests, to find solutions to preserve the company.

(F) Credit crunch
The housebank of a company in financial distress cancels financing. Its bankers are not convinced (anymore) of the company’s viability and calculate the chances of (bigger) debt write-off losses to be largely present. Company management realizes that with that the end of company existence is near as chances of raising new and additional financing (read: cash) will not be huge in these circumstances (which bank is willing to provide credit to a distressed company just being left by its housebank?). So, for the bank primary interest is to prevent (additional) losses to occur, for company management however the (opposing) interest is to have credit lines to remain open. Nonetheless, their common interest to work out this “credit crunch” is in fact and perhaps strange enough to preserve the company from collapsing. For company
management this apparently is evidently, for the bank it does seem to be more indirectly, that is to say liquidation of the company will lead to losing a client and with that potential future sales.

**(G) Race to collect**

A company in financial distress is being forced by various creditors to pay amounts due by means of (threatening with) filing for liquidation at bankruptcy court. For creditors involved it is in theory a possibility to be paid in advance and to the disadvantage of other creditors. Yet for company management it is of great importance to create some sort of stable situation – “breathing space” – to find a solution which given the circumstances potentially is beneficial for all creditors. However, for individual creditors the only stake seems to be paid in full detrimental to others creditors as – of course – the “pie” is too small. Yet when an uncontrolled race to collect\(^9\) is about to start this will unmistakably lead to forced liquidation of the company. The result of which is that creditors even will receive less as in general value of assets in forced liquidation sales drops enormously.\(^{10}\) Although probably not realizing themselves, all creditors in such situation thus are trapped in a classic prisoner’s dilemma casu quo conflict of interests.

**(H) Self-fulfilling prophecy**

A company in financial distress is looking for a solution yet as the problem is publicly known (all or not due to market rumors) customers refuse to pay in advance anymore and/or to commit to the company (long-term contracts) as a result of which the situation for the company deteriorates (see also paragraph 1). The behavioral pattern is explained by the fact that in a potential subsequent liquidation procedure claims attributable to payment in advance and/or with regard to contracted services or products not delivered most of the times will rank behind other (secured and preferential) claims potentially increasing the chances of non payment (all due to deteriorated liquidation values and new preferred claims as a result of liquidation, for instance related to salaries of court-appointed trustees). This reasoning also applies to guarantee warranties; a bankrupt company can and will not fulfill these obligations which is in fact a potential risk for new customers. Yet for the company it is of vital importance that its customer base stays loyal and keeps on doing business, as well as that (in certain situations as with Techno Group) payment is (still) made in advance. However for customers it is most important to be sure to a certain amount that the company is able to deliver in the future before ordering and/or paying in advance. Common yet apparently conflicting interest therefore seems to be that the company remains in tact.

**(I) Payment now versus sales tomorrow**

A company in financial distress is having a conflict with a vendor regarding payment (at Techno Group the housebank as a commercial advisor). The claim

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\(^{10}\) At Techno Group it was estimated about € 10,4 mln.
potentially threatens survival of the company. Nevertheless the same vendor just as management also has an interest in remaining the status quo – that is to say the company not failing – as future existence of the business is an important condition for the claim to be paid. Next to that both parties also do have an interest in a successful turnaround in order to sustain the customer-vendor relationship, for example concerning specific future goods and/or services. Although perhaps fully justified the individual claim for payment thus conflicts with the common interest of existence in the long run.

(J) Yes or no emergency loan

A company in financial distress is not able to negotiate an “emergency loan”, for instance (as in the Techno Group case) to pay salaries, while at the same time liquidity actually is dried up. Obviously the company has an interest in personnel performing its duties. Yet for the potential provider of the finance there is no interest at all besides perhaps some commercially attractive contractual conditions (due to increased risks associated to the loan). This latter party therefore should be convinced of the potential win-win situation that could occur when an agreement in fact is reached.

(K) Signal of trust disappeared

A company in financial distress – more specifically its management – is confronted with a shareholder or a group of shareholders not willing to provide for additional capital any more, to be injected in the company. As a consequence the company’s principal bank also refuses to extend its credit lines. This being the result of the shareholders signaling that the company definitely is not viable to any further extent (by refusing to inject any cash). Therefore, in this kind of situation rebuilding trust with and among shareholders, as well as bankers by management is of vital importance and should be at the front of the agenda. Apparently paradoxically this is also largely in favor of the shareholders themselves as liquidation of the company most probably will lead to (almost) all invested capital to be vaporized (see also D). Yet for banks less of an interest seems to be present as diminishing losses will be their principle aim, although the aspect of future commercial sales perhaps could be present (see also F).

(L) Yes or no skeletons in the cupboard

A company in financial distress is confronted with an investor having a specific interest in business activities being cleared from “old debts” and so-called “skeletons in the cupboard” (as yet unknown debts, claims or problems at a distressed company). A restart following liquidation for that reason could be an option. However company management, as well as the shareholders only have an interest in keeping the legal entity in tact in order to stay in full or partial control and/or to gain from (future) value enhancement. These interests conflict though and therefore a solution should be found meeting all parties’ expectations. It must also be remembered that investors in these kind of situations sometimes in fact do have a strategic interest (see also D) to preserve the company, that is to say for instance when both companies operate in the same market and by acquiring/merging scale and market positioning can be improved (as in a judicial liquidation procedure it can never be guaranteed that business activities and related assets can be acquired from the trustee; a competing company then has as much chances).
(M) Catch 22 for employees

Employees of a company in financial distress file for liquidation at bankruptcy court. Obviously this is not in the interest of company management, moreover she actually strives for (a group of) personnel to in fact keep on operational in order to help the company survive. Yet personnel as a whole have an interest in (immediate) payment and for that reason they use filing for liquidation as an instrument for “pressure”. Furthermore, as a collective they strive for maintenance of all jobs. Nevertheless due to the filing different interests, perspectives and goals in fact do collide. Moreover, it could be the trigger for liquidation (as in the case of Techno Group) and in that sense employees in such circumstances seem to be caught in a kind of “Catch 22”.

5. Harvard negotiation related to chances of survival

The thirteen conflicts of interest as described above (potentially) lead to harsh complications in a given process of reorganization. To put it differently, when company management is not able in such circumstances to take away some or perhaps all of the bottlenecks raised, chances increase enormously that the company ends up in liquidation (as happened with Techno Group). Therefore it is of utter importance for her to take drastic action and perform measures to resolve the conflicts simultaneously and/or subsequently. Important question then is what the most efficient and sustaining way to realize that is, as it is fascinating to observe that reorganizations so often fail in practice, both in The Netherlands, Poland and beyond (see also earlier). As stated before, by using Harvard negotiation as analysis instrument it must be possible – together with the found bottlenecks above - to find some explanation for that and give guidance for improvement in practice. Therefore below the Harvard model is further detailed now specifically focusing on reorganization. This is done by using the four basic principles of Harvard negotiation as described in paragraph 2: (1) people, (2) interests, (3) options and (4) criteria.

1. People – Separate people from the problem

Rescue operations never only deal with rational businesslike behavior. Taking away frustrations and anger due to not complying with earlier negotiated deals therefore often form a large part of the corporate recovery process. Also, in rescue operations financiers and vendors simply do experience increased risks to have to write-off substantial amounts of uncollectible accounts receivable. Not only does this lead to significant financial damage for the company, it also affects individual employees who clearly internally will be held responsible and as a result also take the “blame”. The imminent insolvency problem thus not only stretches to financial aspects but far beyond. Reputations and careers are at stake. Consequently it is necessary that during negotiation processes enough attention is being paid to these issues, and in that way at first instance people should not be separated from the problem; clearly in the eventual solution process it ought to. In some publications this phenomenon is called stakeholder management meaning that in every rescue operation at all times significant

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consciousness must be present to interaction with and feelings of involved creditors. In conflict situations as described above behavior of creditors was in fact mostly a consequence of fear for large(r) losses and related consequences.

2. Interests – Focus on interests not positions

As indicated above in the “heat” of rescue operations various conflicts arise, at various moments and with various stakeholders. Also, often conflicts do arise between parties not even aware of it themselves. In the race to collect described earlier (see G) creditors for example individually put pressure on the company to be paid at first; yet fulfilling ones obligations to one creditor automatically leads to the other being put in a worsened position. Next to that, at first instance multi-creditor workout sessions12 will most of the time not take place with all (possible) parties involved. Moreover, most of the times negotiations will take place one-on-one and as nearly all operating companies contract on a day-to-day basis everyday new obligations are due also making the group of creditors diverse and dynamic. This in any way further complicates the process of negotiating from the point of view of interests instead of from positions. In the negotiating process with individual creditors it is therefore tremendously important for company management to constantly remain reviewing and stressing the common interest – which is preserving the company as a whole – to individual interests of creditors which basically is to be paid in full, as well as making the right coordination and partitioning of payments.

3. Options – Create various options before deciding

In negotiations with various creditors, from conflicting positions and ideas solutions should be sought for. Yet this often is in fact the heart of the problem. As the company in financial distress operates from a situation in which she no longer can fulfill payments due, this increasingly limits possible options. Settlements in (both business and legal) practice therefore often seem to stem from the idea of having (often unsecured) creditors footing the bill meaning that this group of stakeholders is asked to make the necessary “sacrifice”. For example by having debts for a large part discharged (also called haircuts; see for instance B). But also other alternatives do exist, for instance so-called snacks or waterfalls.13 Core of these options is that earlier payment conditions are revised yet not immediately or entirely leading to debt write-offs. In (Dutch) practice these creative alternatives however are not always fully investigated; sometimes due to ignorance, often more driven by some sort of opportunism (fueled by perceived judicial alternatives). Fact is that creditors in general do prefer options somewhere between discharge and direct payment, rather than discharging


13 A snack can be described as: a benefit which is connected to agreeing to a certain proposal during an (informal) reorganization; a waterfall as: a method where incoming cash flows are distributed among company and creditors according to a pre-established method.
instantaneously. Ignoring this natural creditor tendency too easily may lead to forced liquidation as with that underlying conflicts of interest simply remain in tact.\footnote{See on creditor preferences among others Adriaanse 2005, p. 81 ff.}

4. Criteria – Results must be based on objective criteria

Companies in financial distress in fact negotiate in the shadow of two alternatives: (1) the company survives or (2) the company fails. Clearly, different roles of parties involved largely influence the perception of the outcome of the process. More difficult, in fact their respective behavior fundamentally influences the chances of survival. Consequently it seems impossible for an objective norm to exist regarding the question whether companies will or will not survive in such cases, and nobody will ever be 100% certain to predict that a specific company will become profitable again following (rigorous) turnaround measures. Techno Group actually provides an excellent example to proof this statement. Though for the year 2000 a profit of € 800/k was prognosticated, half way through the year it became evident (implicitly) that expectations were not going to be met. Some time later, the company collapsed.

Reorganization routes contain a high degree of subjectivity and this seems to be big part of the crux. The success or failure of rescue operations is to a great extent dependent on the way management \textit{herself} tries to make the business operations profitable again. Consequently a turnaround plan always needs to be present focusing on restoring the cash generating capacity of the company for the long term, in which the company (again) is able to deliver services and/or goods in an efficient way to targeted customer groups whose expectations are really met. Although that may sound a bit abstract this in reality simply has to do with proper harmonization of activities in the field of \textit{marketing} and \textit{innovation}, the \textit{production process}, \textit{human resources}, as well as \textit{management information} requirements within the organization.\footnote{See for more details on this subject J.A.A. Adriaanse, L.C. Lispet, \textit{Entrepreneurship \\& Financial Distress, A Framework for Business Planning in a Turnaround Context}, 2007, Interdisciplinary Entrepreneurship Conference, Aachen, http://www.g-forum.de, 30.01.2008 and also J. Hagel, M. Singer, \textit{Unbundling the Corporation}, “Harvard Business Review”, 1999, pp. 133-141.} If these aspects are not described and worked out in the turnaround planning process (Techno Group unfortunately was a good example thereof) then a basis for real negotiation in fact does not exist as answers to these issues – and of course follow up \textit{hands on} implementation – are particularly necessary in order to be able to create “objectified subjectivity” regarding the chances of survival. This objectified subjectivity to be the best alternative for the fact that objective criteria never really can be determined in such cases.

Negotiations in the shadow of imminent insolvency therefore always do require this last principle of the Harvard negotiation concept to be present in full. In the sense that company management and its advisors need to work exceptionally hard on finding economic (turnaround) answers next to the other negotiating aspects as described above. Moreover, whenever this 4th aspect is in fact in order, then chances of successful dealing with principles 1-3 and with that chances of survival will increase considerably.
Research from the United States (implicitly) confirms these facts concerning the relationship between business plans and corporate failure.\textsuperscript{16}

6. Conclusion
In a fast changing and more global oriented business world it is important for companies to be tremendously adaptive to change and – if necessary – to find high-speed solutions regarding new strategic and operational challenges, as well as related bottlenecks. This also, or better, particularly regards the subject of financial distress. It is shown in this article that companies in fact can and should be able to truly take charge in such situations themselves. The Harvard negotiation concept – used in this article as an instrument for analysis – could actually serve in turnaround practice as a guidance instrument par excellence to examine (potential) bottlenecks and conflicts, as well as to generate viable options for negotiation, and with that to resolve distress in a given situation. In other words, when company managers and their advisors approach (imminent) financial distress using Harvard negotiation, in combination with harsh turnaround measures (basically principle 4) they do have all ingredients necessary to speed-up and improve the restructuring process taking place. It is for that reason of importance that the business and banking community in any given country – including Poland and The Netherlands – as well as governments and universities start adopting, promoting and encouraging the use of this concept in corporate reorganizations, next to the in general already intense promotion and development of insolvency (rehabilitation) legislation. As entrepreneurship can be described as “pursuing opportunity without regard to resources currently controlled”\textsuperscript{17} this is – with regard to financial distress almost literally – a great chance not to be missed.


\textsuperscript{17} See W.A. Sahlam et al., The Entrepreneurial Venture, Harvard Business School Press, Boston 1999, p. 1 ff.
List of references


Summary

In a fast changing and more global oriented business world it is important for companies to be tremendously adaptive to change and – if necessary – to find high-speed solutions regarding new strategic and operational challenges, as well as related bottlenecks. This too applies to dealing with financial distress. To stay ahead in changing environments company managers always should take charge of insolvency processes themselves. This instead of filing for court-led reorganization procedures that most often lead to unnecessary and passive waiting for third parties (judges, administrators/trustees) to intervene, control and set the pace. For that reason this article proposes “Harvard negotiation” as a concept for company managers to rapidly and effectively deal with financial difficulties in given situations. It is argued that by approaching faced financial distress from a problem-solving negotiation point-of-view chances will rise that quick solutions can and will be found in practice meeting stakeholders’ expectations and needs despite the circumstances. A case study of a failed Dutch reorganization is used to reveal bottlenecks and conflicts in such situations and to analyze the usability of the concept in general.