



# Corporate Debt Restructuring Impacted by the Pandemic Case Study: Indonesian Airline Company

Nasrullah<sup>(✉)</sup>, Sihabuddin, Reka Dewantara, and Hanif Nur Widhiyanti

Law Doctoral Program, Faculty of Law, University of Brawijaya, Malang, Indonesia  
nasrullahnawawi@gmail.com

**Abstract.** The Covid-19 pandemic has been a heavy blow to the business world, including companies engaged in the transportation sector, particularly air transportation. The biggest problem that is constraining is the declining ability of airline companies to maintain the smooth implementation of their obligations to lessors and/or other parties which causes accumulation of corporate debt. The research method used is legal research (normative juridical) with a comparative approach. Legal materials will be interpreted with the Theory of Economic Analysis of Law.

**Keywords:** Covid-19 Pandemic · Debt Restructuring · Aviation Companies

## 1 Introduction

Airline companies have an important role in countries whose territory consists of islands and still has very limited land connections [1]. Even though airlines are only a small part of the industry that plays a role in increasing a country's gross domestic product (GDP), aviation companies are a downstream industry that has an important role in supporting other important economic activities [2]. At least the important role of airlines, especially related to air transportation, is to maintain supply chains that occur non-stop every day, all year round throughout the world.

The Covid-19 pandemic has become a heavy blow to the aviation industry, especially for companies engaged in air transportation. According to notes International Air Transport Association (IATA), passenger air transport has decreased by 90 percent year on year since April 2020 and continues to fall by 75 percent in August 2020. On the other hand, the Covid-19 pandemic has also limited trade, thus affecting transportation cargo which has continued to decline by nearly 30 percent year-over-year since April 2020 [3].

This decline proves that restrictions on interactions and connections between regions and countries during the Covid-19 Pandemic have placed the air transportation business in uncertainty. The Covid-19 pandemic has caused an extraordinary increase in debt for the air transportation business, even though the government has always made various interventions as a rescue measure so that airlines can continue to exist amidst increasingly fierce competition in the aviation industry. In the uncertainty of the Covid-19

Pandemic, many airline companies in the world are experiencing financial distress [4]. Such conditions will seriously endanger the aviation industry, especially in developing countries where generally airlines are companies whose shares or ownership are mostly owned by the state. If so, holistic government intervention is urgently needed, including cutting down airline companies that are inefficient or in other words that are no longer possible to save because various problems had arisen before the pandemic. This choice is not easy, because in general state-owned airlines have a long historical romance, so the airlines in question do not only have economic value but also high historical value. One of them is an airline company in Indonesia.

The problem that arises if the debt problems of airline companies are not immediately resolved with a holistic mechanism is the constraints on support for other economic sectors. This is caused by unresolved legal issues that occur. One consequence that is very likely to occur is the enactment of a ban on operations or unilateral withdrawal from the lessor of the leased aircraft. So that the nature of debt settlement as a going concern cannot be achieved, because it does not provide enough space for the company to continue and maintain its business. This condition will certainly greatly disrupt the conduciveness of the business world.

Previous research on legal efforts to resolve debt problems due to the pandemic experienced by companies including airlines in Indonesia was carried out by Reza Y. Siregar and friends, in a very broad perspective on the problems experienced by companies, especially state-owned companies due to the pandemic Covid-19. However, this research is incomplete because it does not analyze the impact of solving these problems both economically and legally. The research that the authors conducted aims to analyze the legal issues of debt settlement due to the Covid-19 Pandemic in airline companies through a debt restructuring mechanism, with the Suspension of Debt Payment Obligations (PKPU) mechanism which is known in Indonesian bankruptcy institutions.

## **2 Method**

The research method used is legal research (normative juridical) with a comparative approach. Legal materials will be interpreted through an analysis process that uses the Theory of Economic Analysis of Law. The use of this theory aims to see the effectiveness and efficiency of PKPU as a legal mechanism for resolving debt and credit problems. So that the company can avoid bankruptcy, while at the same time it can be organized more efficiently.

## **3 Results and Discussion**

### **3.1 Airline Company Problems**

The increase in the number of debts of airline companies in developing countries during the Covid-19 Pandemic was fundamentally due to the limited ability of these countries to develop local capabilities in the aircraft manufacturing industry. Therefore, airline companies in these countries are very dependent on countries that have mastered aircraft manufacturing technology. The mechanism is that the airline company will lease aircraft either to the private sector or the government of the country in question.

This is why in general airline companies in certain countries already have acute problems related to their ability to maintain smooth payment of their obligations to overseas lessors. Aircraft rental prices are generally high, because they refer to the dollar exchange rate, while the airline's income generally relies on revenues that refer to local currency which generally has a lower exchange rate [1].

The Covid-19 pandemic has caused a very rapid increase in debt to airline companies, due to new loans, bailout funds to increase equity, company operational costs (especially wage subsidies), aircraft maintenance and most significantly delays in aircraft payments to lessors which are increasingly piled up. At the same time, various policies have limited or even prohibited the operation of air transportation.

Therefore, settling the increase in airline debt due to the Covid-19 Pandemic requires a comprehensive strategy. On the one hand it can solve debt and credit problems and on the other hand it must be able to overcome deadlocks and prevent airline companies from being liquidated due to bankruptcy. In addition, specifically for state-owned airlines, interventions are urgently needed which can avoid the side effects of competition and encourage efficiency control [2].

### **3.2 Airline Company Debt Restructuring Through Suspension of Debt Payment Obligations**

The main problem in accounts payable is the orientation of each country regarding the management and management of company assets in relation to their obligations to creditors, in this case, the lessor and various industry providers that can support the operations of airline companies. At the same time, the settlement mechanism can provide an opportunity for the company to maintain and continue its business (going concern). It is in this reality that the settlement of airline debt after the Covid-19 pandemic is not only an economic problem but also creates legal problems [5].

The judge's decision on the request of the creditors plays an important role in determining the fate of the airline in the future. The decision to declare bankruptcy will have consequences for a long settlement and may end with the airline being unable to continue at its intended destination. This is because, airline companies that experience debt and credit problems and have been asked by creditors for settlement to the court indicate that the liquidation of the company's assets is generally no longer able to guarantee the fulfillment of creditor rights.

In the case of bankruptcy institutions in Indonesia, it regulates the steps that can be taken if the company still has prospects to continue its business. Especially for airline companies with the status of state-owned enterprises (BUMN), bailout funds provided by the government in the National Economic Recovery (PEN) program will greatly assist airline companies in maintaining their company's leverage. Therefore, the use of leverage is focused on increasing the company's profitability and solvency. This mechanism is part of the restructuring known by bankruptcy institutions in many countries. In the context of bankruptcy law in Indonesia this mechanism is known as Suspension of Debt Payment Obligations (PKPU).

PKPU is essentially a settlement of debts and receivables that was born from a peace process between the debtor and the creditor, so that the debtor has sufficient time to settle his debts. Therefore, in the PKPU process, the debtor does not lose the right and

authority to manage the company and its assets, so that the debtor really believes that with the PKPU mechanism, the debtor can complete his obligations and develop his business [6].

### 3.3 PKPU PT. Garuda Indonesia Persero

PT. Garuda Indonesia Persero (Garuda Indonesia) during the restrictions due to the Covid-19 Pandemic until September 2021 was in debt up to USD 9.78 billion, equivalent to IDR 140 trillion. With the following description total assets USD: 10, 789, 980, 407.00 2, total liabilities USD (total short term liabilities USD: 4, 294, 797, 755.00 2) total long term liabilities USD: 8, 438, 206, 899.00, so total liabilities USD: 12, 733,004, 654.00. USD equity: (1,943, 024, 247.00). Loss for the Year USD 2, 476, 633, 349.00. Number of Outstanding Shares 25, 886, 576, 254 6. Due to various problems above, Garuda Indonesia's shares were stopped from trading per date. June 18, 2021.

Based on the description above, Garuda Indonesia's debt which is too large when compared to its assets makes the peace proposal submitted in PKPU have the potential to cause various problems. One of them, the potential for the end of PKPU in the bankruptcy mechanism. Based on the peace proposal that has been approved by 97 percent of Garuda Indonesia's lessors and creditors in the PKPU process, in addition to Garuda Indonesia's business plan, Garuda Indonesia's debt payments will be carried out through several procedures, namely: First, for debts under Rp. 225 million. Second, debts of Rp. 225 million and above will be settled through the issuance of new bonds in the form of lessor bonds worth US\$ 825 million and shares worth US\$ 330 million. Third, debts and loans to banks and BUMN will be extended for 22 years with an interest rate of 0.1 percent per year [6]. Considering that the PKPU mechanism is not a procedure that is not limited by time, even though the PKPU mechanism does not recognize any legal remedy for a judge's decision at a commercial court, the time limit and extension of PKPU cannot be more than 270 days from the time the PKPU decision is announced.

The business plan in question is very important in the peace process because this business plan contains the things that the debtor knows best about the company going forward, especially regarding financial ratios concerning the company's potential and operational risks that will hinder the debtor's ability to repay debts and and/or obligations. From a normative juridical perspective, the above description can be used as an analysis of the relevance of debt restructuring through the PKPU mechanism, which can be an important variable in maintaining the conduciveness of the business world. Because, in the process PKPU does not eliminate the debtor's authority in managing his assets and company so that he can continue his business. On a macro level this will have an impact on being able to continue the production process in a sustainable manner because the debtor is the party who understands the most.

In the context of Garuda Indonesia, the ratio of Garuda's main expenses in the form of high prices for aircraft rental to foreign lessors shows inefficiency due to an imbalance between costs and benefits. Theoretically from an economic perspective, the financial distress experienced by Garuda Indonesia when analyzed through the Altman Z Score model according to Stephen A. Ross, the concept of financial accounting, assets and human resources can be concluded. Whereas pressure on profitability, due to financial burdens that are too heavy can occur due to mismanagement, so it has the potential

to lead to inefficiency which is then exacerbated by a decrease in income during the pandemic [7].

Therefore, the business plan formulated in the Garuda Indonesia PKPU process cannot only be analyzed from a legal perspective, but holistically must be analyzed through the economic concepts of profitability, solvency, costs and benefits and efficiency. The goal is to maintain Garuda Indonesia as a national airline which is a symbol of open inter- regional connectivity throughout Indonesia.

In comparison, China's fourth-largest airline, Hainan Airlines, announced the transfer of management of its core business as an aviation service provider to Liaoning Fangda Group Industrial Co Ltd. The transfer was made after Hainan Airlines' parent company, HNA Group, was in the process of bankruptcy and debt restructuring. Hainan in March announced a company loss of 64 billion Yuan or about 144.7 trillion for 2020, which was the largest loss on the list of companies in China. The High Court in January issued a notice notifying its creditors of filing for bankruptcy, the China Daily reported. Since 2010, HNA has aggressively made inroads by increasing its overseas assets so that its total acquisitions have reached more than USD 50 billion (approximately IDR 717.6 trillion). HNA had acquired shares of 40 large companies, including Deutsche Bank AG and Hilton Worldwide Holdings Inc. Recently, the acquisition of HNA has come under scrutiny from Chinese regulators. HNA began to be heavily in debt and started looking for buyers for its assets [8].

The PKPU concept regulated in the Bankruptcy Law in Indonesia is almost the same as that which applies also in the peace plan mechanism as regulated in Chapter 11 of the US Bankruptcy Code. Thought to share the burden of the conciliation plan to creditors or related parties in the process of deferring payments. These two restructuring mechanisms provide freedom of action for debtors to run their business as they should, as a follow-up process to prepare for concealment plans or in PKPU known as business plans [9].

The settlement of debt problems in Chapter 11 of the US Bankruptcy Code holistically also regulates the differences between individuals, corporations and small and medium businesses, as debtors. It is absolutely essential that there is a Creditor Committee institution that is required in deferring payments. Therefore, reorganization under Chapter 11 of the US Bankruptcy Code may provide a more balanced fairness and protection [10].

Therefore, in resolving debt problems with airlines, it is best to refer to the global agreement on post-pandemic recovery efforts. Not only focusing on carrying out the obligations of airline companies, at least this orientation refers to logical efforts to create a new global order for a more universal aviation industry, in which every country remains connected without being burdened by differences in technological mastery, financial capability and discrimination in maintaining the region remains connected with other regions.

## 4 Conclusion

Settlement of corporate debt after the Covid-19 Pandemic, especially for airline companies that have a strategic role in maintaining connectivity between regions and/or countries, requires a mechanism that can guarantee the continuity of the airline company in question. Therefore, debt restructuring through the peace process is the right

mechanism, but it must be accompanied by a holistic and comprehensive analysis of the company's ability to continue its business, while at the same time being able to carry out its obligations to creditors, in this case the dominant one is the lessor.

**Acknowledgments.** Thank you to the Study Program at the Main Campus, Faculty of Law, University of Brawijaya, Jakarta, which has given the author the opportunity to participate in the preparation of the proceedings of the 2022 BcoBL International Seminar until the publication of this manuscript.

## References

1. V. S.: Aviation in a Post-Pandemic World: Challenges and opportunities. 6 min read, November 1–4, 4 (2020).
2. OECD.: COVID-19 and The Aviation Industry: Impact and Policy Responses. Tackling Coronavirus (Covid-19): Contributing To A Global Effort, 2–8, 15 October (2020).
3. IATA.: Economic Performance of the Airline Industry. IATA Economic Terms, (2021).
4. Setyaningrum, K. D.: Analisis Z-Core Dalam Mengukur Kinerja Keuangan Untuk Memprediksi Kebangkrutan Perusahaan Manufaktur Pada Masa Pandemi Covid-19. Riset Akuntansi Politala. 3 (2), 74-87 (2020).
5. Shen, H., Fu, M., Pan, H., Yu, Z., Chen, Y.: The Impact of the COVID-19 Pandemic on Firm Performance. Emerging Markets Finance and Trade. 56 (10), 2213-2230 (2020).
6. Muhammad, F.: Bankruptcy Law in Theory and Practice, Jakarta: PT. Aditya Bhakgti, (2014).
7. Ilyas, W.: Legal Implication of Garuda Indonesia's Financial Distress. Investor.id, August 22, (2021).
8. Ouyang, I.: Chinese airlines resort to short-term debt for lifeline as coronavirus batters global aviation industry. Shout China Morning Post, June 1, (2020).
9. Dodge, D.: International Financial Architecture and the Resolution of Financial Crises. International Journal. 57 (4), 624-630 (2002).
10. Peterson, S.: Debt Restructuring and Notions of Fairness. The Modern Law Review. 80 (4), 600-623 (2017).

**Open Access** This chapter is licensed under the terms of the Creative Commons Attribution-NonCommercial 4.0 International License (<http://creativecommons.org/licenses/by-nc/4.0/>), which permits any noncommercial use, sharing, adaptation, distribution and reproduction in any medium or format, as long as you give appropriate credit to the original author(s) and the source, provide a link to the Creative Commons license and indicate if changes were made.

The images or other third party material in this chapter are included in the chapter's Creative Commons license, unless indicated otherwise in a credit line to the material. If material is not included in the chapter's Creative Commons license and your intended use is not permitted by statutory regulation or exceeds the permitted use, you will need to obtain permission directly from the copyright holder.

