



## **SUMMATIVE (FORMAL) ASSESSMENT: MODULE 4B**

### **BRAZIL**

This is the **summative (formal) assessment** for **Module 4B** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 4B.** In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

## **INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentID.assessment4B]**. An example would be something along the following lines: 202122-336.assessment4B. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentID” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **9 pages**.

## **ANSWER ALL THE QUESTIONS**

### **QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

#### **Question 1.1**

Indicate the **correct answer** regarding bankruptcy legislation in Brazil: [1 mark]

- (a) The Bankruptcy Law regulates the liquidation – but not the reorganisation – of any individual or legal entity with activities in Brazil.
- (b) The former Civil Procedure Code regulates the reorganisation of non-business individuals and legal entities.
- (c) The current Bankruptcy Law contains a section addressing cross-border bankruptcies.**
- (d) The Bankruptcy Law does not allow companies belonging to the same economic group to file for restructuring jointly.

#### **Question 1.2 [1 mark]**

Which of the following statements is **correct** with regards to the Brazilian judiciary?

- (a) Brazil has a single apex court: the Superior Court of Justice, which is in charge of constitutional issues.
- (b) Labour disputes take place at a specialised segment of the judiciary, composed of labour courts, courts of appeal and a superior court.**
- (c) Insolvency proceedings take place at the federal-level judiciary (as opposed to the state-level judiciary).
- (d) The nomination of an individual as a judge of a bankruptcy court is the result of an election by popular vote from residents within that particular judicial district.

#### **Question 1.3**

Select the **false statement** concerning security rights within the Brazilian legal system: [1 mark]

- (a) A pledge is a lien that may be constituted over both movable and immovable assets.**
- (b) Despite being a lien over immovable property, mortgages may also be used to offer aircrafts and vessels as security.

- (c) The *antichresis* is a rarely used type of security, the purpose of which is to assign the income from an immovable property to the guaranteed party.
- (d) Fiduciary titles are increasingly used as a security due to the fact that this guarantee allows for the guaranteed party to take possession of the collateral and sell it outside a bankruptcy proceeding, as long as certain conditions are met.

#### Question 1.4

Which of these parties **is allowed** to file for a judicial recovery case under the terms of the Bankruptcy Law? [ 1mark]

- (a) A *sociedade de economia mista* (a company whose majority equity interest belongs to the Federal, State or local government).
- (b) An accounting firm.
- (c) An individual who carries on a business activity without the use of a legal entity.
- (d) An insurance company.

#### Question 1.5 [ 1 mark]

Concerning corporate liquidation, indicate the **incorrect** statement below:

- (a) The Bankruptcy Law provides the means for the debtor to file a voluntary liquidation proceeding.
- (b) None of the gateways for the involuntary liquidation of a debtor require the creditor to actually prove the balance sheet insolvency of the debtor.
- (c) A debtor has a 10-day period, after service of process, to present his defence against a creditor seeking its liquidation.
- (d) A decision from the bankruptcy court declaring the bankruptcy of a debtor is unappealable.

#### Question 1.6 [ 1 mark]

Which of the following claims has the **highest priority** under a bankruptcy proceeding?

- (a) Fees payable to the judicial administrator and its auxiliaries.
- (b) Tax-related fines.
- (c) Administrative expenses of the estate.
- (d) Unsecured claims.

**Question 1.7 [ 1 mark]**

A debtor under judicial recovery has the following creditors:

- 50 creditors in Class I (workers and labour-related claims)
- 3 creditors in Class II (creditors secured by *in rem* guarantees)
- 300 creditors in Class III (unsecured creditors)
- 200 creditors in class IV (claims held by micro and small enterprises)

The total amount of debt owing in each class is the following:

- BRL 1 million in Class I
- BRL 5 million in Class II
- BRL 50 million in class III
- BRL 30 million in Class IV

Assuming all creditors are present at the debtor's general meeting of creditors, **indicate the only true statement** regarding the approval of the plan:

- (a) The approval of the plan in Class I is solely dependent on its approval by creditors whose claims amount to a quantity in excess of BRL 0.5 million.
- (b) The approval of the plan in Class II is solely dependent on a majority by head count.
- (c) The approval of the plan in Class III depends on a double majority: by head count and by the total amount of claims.
- (d) The approval of the plan in Class IV is solely dependent on favourable votes by creditors whose claims exceed BRL 15 million.

**Question 1.8 [ 1 mark]**

Which of the following documents **needs to be** presented by the debtor at the moment of filing for judicial recovery?

- (a) A full nominal list of creditors.
- (b) Accounting statements for the last financial year for the current administrators of the company.
- (c) A judicial recovery plan.
- (d) A list with a brief description of the contracts entered into by the debtor in the last financial year.

**Question 1.9 [ 1 mark]**

Indicate the **only correct statement** below relating to the cramdown of a judicial recovery plan:

- (a) "Cramdown" is a doctrine that allows for creditors to present their own alternative reorganisation plan.
- (b) There are no statutory provisions on cramdown under the current Bankruptcy Law, it is a judicially-created doctrine.

(c) Among the criteria that must be met for a cramdown to be imposed, the plan needs to receive favourable votes from over half the total amount of claims in each of the classes of creditors that were present at the general meeting.

(d) A cramdown cannot be imposed if the judicial recovery plan entails the discriminatory treatment of creditors within the class that rejected it at the general meeting of creditors.

**Question 1.10 [ 1 mark]**

Select the **correct statement** from the options below regarding extrajudicial recoveries:

(a) Extrajudicial recoveries allow for a larger set of debtors to seek their reorganisation in comparison to the set of debtors that are allowed to file for judicial recovery.

(b) Extrajudicial recoveries do not allow the debtor to restructure labour claims.

(c) Extrajudicial recoveries represent a consensual solution to a financial crisis, as extrajudicial plans may not be imposed on dissenting creditors.

(d) Extrajudicial recoveries do not allow the debtor to dispose of its assets free of any encumbrances, unlike judicial recoveries.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 2 marks] [ 2 marks]**

Cite **two (2) faulty actions** that could lead to the debtor's administration being removed during a judicial recovery case.

Article 64 of the Bankruptcy Law provides the circumstances which could lead to the debtor's administration being removed during a judicial recovery case. Two such circumstances are (i) where the debtor or its managers have acted with malice, simulation or fraud against the interests of its creditors; and (ii) where the debtor or its managers have shown strong signs of having committed a crime provided for in this Article 64

**Question 2.2 [maximum 3 marks] [ 3 marks]**

State the **three (3) manners or ways** by which the assets of the bankrupt estate may be sold by the judicial administrator during a liquidation procedure.

The three manners by which the assets of the bankrupt estate may be sold by the judicial administrator during a liquidation procedure are:

- (i) by electronic, in-person or hybrid auction;
- (ii) by competitive procedure promoted by a specialised agent; or
- (iii) by any other modality, as long as approved under the terms of the Bankruptcy Law

**Question 2.3 [maximum 2 marks] [ 1 mark]**

State **two (2) acts** that may be rendered ineffective towards the bankrupt estate if carried out whilst the "suspect period" of a bankruptcy proceeding was in effect.

Article 129 of the Bankruptcy Law provides various acts that may be rendered ineffective towards the bankrupt estate if carried out during the “suspect period” of a bankruptcy proceeding. Two of those acts are:

- (i) the waiver of an inheritance or a legacy in the two years preceding the decree of bankruptcy; and
- (ii) where the debtor pays debts which have not yet fallen due [only when such payment is made within the suspect term]

**Question 2.4 [maximum 3 marks] [ 3 marks]**

Identify **three (3) changes** introduced to the Brazilian insolvency legal system due to the enactment of Federal Law 14.112/2020.

Three changes introduced to the Brazilian insolvency legal system due to the enactment of Federal Law 14.112/2020 are:

- (i) the creation of a specific incidental procedure for the tax authorities to present their definitive claims against a debtor (Article 7-A);
- (ii) creditors are now able to present an alternative judicial recovery plan in instances where the recovery plan presented by a debtor is rejected at a general meeting of creditors (Article 54); and
- (iii) the provision of an expedited termination of insignificant or ageless assets (Article 114-A)

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1 [maximum 5 marks] [4 marks]**

How is the judicial recovery for micro and small enterprises different from a regular judicial recovery?

Although the processes for judicial recovery and for judicial recovery for micro and small enterprises have some of the same requirements, i.e., in both instances the plan must be presented within 60 days of the filing for judicial recovery, there are some marked differences between the two procedures.

First, in a regular judicial recovery, all existing claims, even those that are not yet due are included in the plan. [does not include tax claims; see also art. 86, II of the Bankruptcy Law] However, in a special judicial recovery for micro and small enterprises, claims which relate to the borrowing of official funds, tax claims and any other legal exception, are not included in the plan.

Secondly, in a regular judicial recovery, a general meeting of the creditors are called and at that meeting, the categories of creditors are broken up into those with labour claims; secured creditors; unsecured claims and those with claims of micro and small enterprises. However, in a special judicial recovery for micro and small enterprises, there is no general meeting of creditors called.

Thirdly, in a regular judicial recovery, there are a number of circumstances which will trigger the conversion to a regular liquidation. These include (i) where the creditors at the general meeting pass a resolution to this effect; (ii) where the debtor fails to produce a recovery plan within the specified legal timeframe; (iii) where the recovery plan is rejected by the creditors and no alternative plan is entertained by the rejecting creditors; (iv) where the recovery plan requires the fulfilment of certain obligations and those obligations are not fulfilled within 2 years

of filing the recovery plan [until the proceeding is terminated]; (v) where a debtor defaults on payment terms on certain negotiated tax instalment payment programmes; (vi) where there is a substantial liquidation of the debtor as a result of depletion of its assets to the detriment of creditors not a part of the judicial recovery procedure. On the other hand, in the case of a special judicial recovery for micro and small enterprises if creditors which hold more than 50% of the claims in each class object to the plan, then the process is converted to bankruptcy and the judicial recovery will be dismissed.

Fourthly, in a regular judicial recovery, when the petition is filed and the judge in charge of the process accepts the processing of the procedure, then a 180 day stay comes into effect. That stay period could then be extended once for an additional 180 days. In the case of a special judicial recovery for micro and small enterprises however, there is no 180 day stay period and the first instalment payment must in fact be paid within 180 days of filing the petition for judicial recovery before the court.

Fifthly, a regular judicial recovery has a duration of 2 years whereas there is a maximum of 36 months by which equal instalment payments are to be paid under a special judicial recovery for micro and small enterprises and such payments must be equal. Such payments will also be restated to include (a) haircuts on claims; and (b) interest at a rate which is equivalent to the Special Settlement and Custody System (Selic) for federal securities, i.e. Taxa Selic.

Sixthly, in a regular judicial recovery, the plan only needs to contain (a) a detailed description of how the debtor will be rescued; (b) a statement regarding the economic feasibility of the plan; and (c) an economic-financial and appraisal report regarding the debtor's assets. However, in a special judicial recovery for micro and small enterprises, the plan must provide for authorisation by a judge for the increase by a debtor of its expenses or in order to be able to hire employees.

Lastly, a regular judicial recovery requires the appointment of a judicial administrator whereas special judicial recoveries for micro and small enterprises, are a much more inexpensive process than regular judicial recovery given that no judicial administrator is required.

### **Question 3.2 [maximum 5 marks] [ 5 marks]**

What is a "claim for restitution" under a bankruptcy procedure? How does it work?

A claim for restitution under a bankruptcy procedure is a claim by which the creditor asserts that the asset which he seeks to recover is in fact his (i.e the creditor's asset) and should therefore not form a part of the bankrupt's estate. It will thus, if the restitution claim is successful, be deemed to have fallen outside of the bankruptcy proceedings and will therefore be paid in priority to all other claims. A restitution claim in this context is therefore a claim for the return to the creditor of his property.

Where bankruptcy proceedings are on foot, a restitution claim must be filed in separate proceedings to the bankruptcy proceedings. A restitution claim may be asserted (in addition to circumstances where the reclaim of property is being pursued as above), where an asset was sold to a debtor on credit, within 15 days of the filing of a bankruptcy petition, provided that the asset in question has not yet been disposed of.

In a restitution claim, assets or the cash value on assets may be returned to a successful claimant as follows:



- (i) where the asset no longer exists at the time of the claim, the cash value of the asset at the time of the filing of the claim, or if the asset has been sold, the cash amount paid for the asset. In both instances, monetary compensation in addition to the claimed amount will be payable to the claimant;
- (ii) the amount delivered to the debtor, in domestic currency, resulting from an advance on an export exchange contract under the relevant Federal Law provision, provided that the full term does not exceed that provided for in the specific rules of the relevant competent authority;
- (iii) any amounts delivered to a debtor by a bona fide purchaser, if the contract by which the payment was made is either revoked or declared ineffective; and
- (iv) taxes due or the amount of withholding taxes other taxes payable and amounts received by collecting agents which amounts have not been paid over to the government.

**Question 3.3 [maximum 5 marks] [ 5 marks]**

Describe the process of proof of claims for a creditor, under a judicial recovery case, who (i) was not listed in the first list of creditors (presented by the debtor) and (ii) for a creditor who was not listed in the second list of creditors (presented by the judicial administrator).

Where a creditor in a judicial recovery case was not listed in the first list of creditors, the affected creditor has 15 days to submit their claim to the judicial administrator. The judicial administrator must, in this context, enable the delivery of the request by an electronic address. This 15-day period is considered the administrative phase and during this phase, the creditor does not incur any costs. This no-costs rule applies even in the instance where the judicial administrator does not accept the creditor's claim. In this phase, there is no requirement for the judicial administrator to justify his decision either way (although he may) nor is there a requirement for him to allow an appeal of any unfavourable decision he makes towards the creditor (although he may).

When the second list of creditors is published, if a creditor has not been listed, if that creditor wishes for its name to be included in the list of creditors, that creditor will need to challenge the second list (prepared by the judicial administrator). That creditor will however lose the benefit of no-costs consequences as in the administrative phase since this phase is considered the judicial phase and requires court involvement. In this phase, the creditor will have 10 days to object to the second list of creditors. As above, since the challenge is heard in court, all associated costs will have to be borne by the creditor if that creditor is unsuccessful in its claim for inclusion in the creditors' list. Once a challenge is submitted, the judicial administrator will issue an opinion on it and the judge presiding over the proceedings will make a final determination. There is scope however for an appeal by the creditor to a higher court against the decision of the lower court.

Where a creditor misses the 15-day period by which to submit its proof of claim in the administrative phase, then the subsequent submission of the claim will be considered late and that creditor will not be able to vote at a meeting of the creditors until a judge accepts its claim during the judicial phase. As above, any claim presented in the judicial phase puts the creditor at risk for costs if its claim is unsuccessful.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

Braz Bank is a Brazilian bank. The financial institution has had considerable success lending to distressed debtors. Nonetheless, a series of risks are associated with this activity. Just recently one of its borrowers, Brazil Empreendimentos Ltda (Empreendimentos), has defaulted on a loan.

**Using the facts above, answer the questions that follow.**

**Question 4.1 [maximum 5 marks] [3 marks]**

The loan Empreendimentos has defaulted on was valued at BRL 1,000,000 (one million reais). Due to Empreendimentos' default, an acceleration clause came into effect and caused the entire value of the contract to mature. Given that the loan agreement met all the criteria for making it an extrajudicial executive title under the Civil Procedure Code, Braz Bank's initial step was to protest the contract before a protest officer, making it public that Empreendimentos had defaulted on it. Despite this measure, Empreendimentos did not cure its breach and the loan remains unpaid.

Does Braz Bank have grounds for filing an involuntary bankruptcy proceeding against Empreendimentos? Is there any defence that may be presented by Empreendimentos in order to ensure that the court will not declare its bankruptcy under any circumstances?

Yes, Braz Bank has grounds for filing an involuntary bankruptcy proceeding against Empreendimentos as the current position fits one of the scenarios which Article 94 of the Bankruptcy Law provides as a scenario in which an involuntary bankruptcy procedure may be commenced in Brazil. That scenario is that the debtor has, without a relevant reason under the law failed to pay a due debt which was valued at BRL 1,000,000 (the debt being certain on its value) and expressed in one extra-judicially enforceable title (given that it is a public document executed by the debtor) was duly protested (given Braz Bank protested the contract before a protest officer) and the sum exceeds 40 minimum wages at the date of the petition for bankruptcy – the sum being BRL 1,000,000.

In this context there is no defence that may be presented by Empreendimentos preventing its bankruptcy. Empreendimentos would have been able to present a defence if Braz Bank did not hold any document that enabled it to directly initiate an enforcement procedure. If Braz Bank did not hold such a document then the bankruptcy process would have been initiated by a cognisance phase which would have allowed for Empreendimentos to present a defence. **[Several arguments could theoretically be raised, see article 96 of the Bankruptcy Law. Besides, the debtor could make a deposit of the amount due.]**

**Question 4.2 [maximum 5 marks] [5 marks]**

Suppose, additionally, that the referred loan agreement between Braz Bank and Empreendimentos was also secured by a mortgage over land valued at BRL 350,000 (three hundred-and-fifty thousand reais). Before Braz Bank took any additional measure against Empreendimentos, the debtor voluntarily filed for a judicial recovery proceeding, the processing of which was accepted by the court. The list of creditors presented by the debtor upon filing for judicial recovery showed the following four (4) creditors in Class II (creditors secured by *in rem* guarantees):

- Braz Bank SA: BRL 350,000;
- Banco Enterprises SA: BRL 125,000;
- Brasil Autoparts SA: BRL 100,000;
- Oil Brasil SA: BRL 100,000.

The complete list of creditors (also portraying Classes I, III and IV) has just been published in the official press. A few rumors have come to Braz Bank's attention concerning the fact that Brasil Autoparts SA and Oil Brasil SA are likely to reject the recovery plan that Empreendimentos has been working on. Should the rumors show themselves to be accurate,

is Empreendimentos still capable of having its recovery plan approved at a general meeting of creditors? Would there be grounds for a cramdown?

Assuming that all four Class II creditors attend the general meeting, and assuming that Brasil Autoparts SA and Oil Brasil SA reject the recovery plan, then the plan will not be approved at the general meeting of the creditors. The reason why there would not be approval at the general meeting is because as secured creditors, the threshold for approval is majority by headcount (which in this case would be 3) and majority in value of claims. In the current scenario, there will only be a majority by the value of the claims.

In order to be eligible for a cramdown in this case, the judge before whom the judicial recovery plan is placed for approval, will have to be satisfied that:

- (i) the recovery plan has received the favourable vote of the majority of creditors represented at the general meeting, independent of the class of each such creditor;
- (ii) there has been approval of three of the classes of creditors; and
- (iii) there is no discrimination to any creditor in the class of creditors that rejected the recovery plan and in that class there is at least a 1/3 percent vote in favour of the recovery plan.

Assuming that of the creditors, the only dissenters are Brasil Autoparts SA and Oil Brasil SA, then each of the criteria above would have been satisfied and there will thus be grounds for a cramdown.

**Question 4.3 [maximum 5 marks] [ 5 marks]**

Suppose Braz Bank's loan agreement with Empreendimentos was not secured by a mortgage but rather by a fiduciary title over land valued at BRL 600,000 (six hundred thousand reais). The referred piece of land corresponds to the site where Empreendimentos' main factory is located. Empreendimentos' judicial recovery proceeding has just begun: the Court issued the decision allowing for the processing of the judicial recovery two (2) days ago. How soon can Braz Bank take possession of the land and sell it outside the recovery proceeding? Could Empreendimentos argue anything in defence of maintaining its possession over the land?

Since Braz Bank's loan with Empreendimentos is secured by a fiduciary title, that security entitles Braz Bank to take immediate possession of the asset without the need to involve the Judiciary. This is because as holder of a fiduciary title, Braz Bank would have had the title in the property transferred into its name at the time that it took security. In this case, if the property is considered a capital good, although Braz Bank is in possession of the title, it may still meet with difficulty in selling since during the 180-day stay period. At the earliest therefore, Braz Bank will be able to sell after the expiry of an additional 178 days.

Although Braz Bank could possibly sell after the 180-day stay period, it might face difficulties if the court considers that the asset is fundamental to the turnaround of the debtor's business. Empreendimentos could therefore argue that the land is where its main factory is located and without that factory Empreendimentos' business could never recover.

**\* End of Assessment \***

**TOTAL MARKS 46 OUT OF 50**