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 [1 mark]

Indicate the **correct answer** regarding bankruptcy legislation in Brazil:

(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 [1 mark]

Select the **false statement** concerning security rights within the Brazilian legal system:

(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 [zero]

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

(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. [correct]

(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 [zero]

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. [correct]

(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 [zero]

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. [correct]

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 states that the manager(s) shall be removed if the debtor or its manager(s) have its dismissal provided for in the judicial recovery plan, if they have shown strong signs of having committed a crime, or, have acted with malice, simulation, or fraud against the interest of its creditors.

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:

1) By electronic, in-person, or hybrid auction;
2) By a competitive procedure dealt with by a specialised agent; or
3) By any other method so long as it is approved under the terms of the Bankruptcy Law.

Question 2.3 [maximum 2 marks] [2 marks]

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.

The following acts may be rendered ineffective towards the bankrupt estate if carried out whilst the "suspect period" of a bankruptcy proceeding was in effect:

1) Acts performed free of charge during the two years preceding the decree of bankruptcy;
2) The waiver of an inheritance or legacy during the two years preceding the decree of bankruptcy;
3) Payment of debts that have become due and enforceable, in a way not provided for under the terms of the contract; and
4) The granting of an in rem guarantee (including a lien) in relation to a debt previously entered into but not secured.

See Article 129 of the Bankruptcy Law for further examples.

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.

Upon the enactment of Federal Law 14.112/2020, the following changes were introduced to the Brazilian insolvency legal system:

1) An expediated termination of insignificant or assetless cases;
2) Groups of companies are eligible for the filing of a restructuring procedure (as a group);
3) Creditors are allowed to present an alternative judicial recovery plan where the one voluntarily presented by the debtor is rejected under a general meeting of creditors;
4) Debtors being able to initiate a mediation or conciliation procedure with the creditors prior to the actual filing of the judicial recovery case;
5) Debtors being able to file for extrajudicial recovery as soon as they have one third of favourable votes from the creditors subject to the proceeding;
6) Providing for the stay period to apply to extrajudicial recoveries;
7) In certain circumstances, creditors can present their won version of a recovery plan for the debtor (thereby resulting in creditors playing a more active role in recovery proceedings); and
8) Health insurance co-operatives being permitted to enter into judicial recovery.

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

Question 3.1 [maximum 5 marks] [3 marks - incomplete answer]

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

Firstly, micro enterprises are those whose gross revenues are less than BRL 360,000 per annum, and small enterprises are those with gross revenues exceeding BRL 360,000 per annum, but that are less than BRL4.8m.

There are differences in remuneration in the judicial recovery for micro and small enterprises and a regular judicial recovery – namely, the total amount paid to the judicial administrator in the case of a micro/small enterprise bankruptcy is a maximum of 2% of the amount payable to the creditors, compared to 5% in a regular judicial recovery.

The recovery procedure for micro and small enterprises provided for in the Bankruptcy Law is very restricted and is often ineffective in allowing for the restructuring of such enterprises experiencing financial crisis.

Question 3.2 [maximum 5 marks] [3 marks - incomplete answer]

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

A claim for restitution relates to a third party (having and) seeking the right to a restitution of assets that belong to it but are in the possession of the bankrupt estate.

Any monies due as a result of a restitution lawsuit have to be paid in priority to all other claims (including super-priority claims).

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).

(i) a creditor was not listed in the first list of creditors (presented by the debtor)

Upon the publication of the first notice in the official press, creditors who are subject to the judicial recovery case have 15 days to submit their claims to the judicial administrator.

If the creditor does not submit a claim within the 15 day window (also known as the "administrative phase"), its claim is then deemed to be a "late claim", meaning that the creditor will not have the right to vote at the general meeting of creditors until such a point where his claim is recognised by the judge – this could leave the creditor at risk of bearing legal fees and judicial costs, in the event that its claim is successfully opposed by the debtor.

ii) a creditor who was not listed in the second list of creditors (presented by the judicial administrator)

Creditors have a 10 day window (also known as the "judicial phase") to object to the (second) list of creditors, or argue that a claim is missing and must be listed.

Objections are run under separate case records and are given their own case numbers. Given that objections to claims take place in court, it is the creditor who bears the risk of the objection being unsuccessful. In the event that the creditor's objection is unsuccessful, it may be ordered to pay the legal fees and judicial costs incurred as a result of its challenge.

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.

<u>Using the facts above, answer the questions that follow</u>.

Question 4.1 [maximum 5 marks] [5 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?

Pursuant to Article 94 of the Bankruptcy Law, there are three situations that allow the commencement of an involuntary bankruptcy procedure in Brazil, which may be requested by *any** creditor.

*If the creditor is an individual entrepreneur or a business legal entity, he/it must prove the regularity of the business by showing a certificate from the Board of Trade. If the creditor is not domiciled in Brazil, he/it must post a pond of sufficient value for the payment of costs and fees of the proceeding, as well as for the payment of the indemnification.

Whilst we note that Braz Bank is a Brazilian bank, we need to determine whether it is actually domiciled in Brazil.

One of the three situations that allow the commencement of an involuntary bankruptcy procedure in Brazil is:

1) The debtor, without a relevant reason under the law, does not pay on the due date a debt that is certain on its value (divida liquida) and expressed in one or more extra-judicially or judicially enforceable titles duly protested, the sum of which exceeds the equivalent of 40 minimum wages on the date of the petition for bankruptcy.

As far as we are aware from the facts of the question, Empreendimentos has, without a relevant reason under the law, failed to pay on the due date a debt that is certain on its value (divida liquida) and expressed in one or more extra-judicially or judicially enforceable titles duly protested, the sum of which exceeds the equivalent of 40 minimum wages on the date of the petition for bankruptcy. As noted above, the loan Empreendimentos has defaulted on was valued at BRL 1,000,000 (one million reais), meaning that Braz Bank does have grounds for filing an involuntary bankruptcy proceeding against Empreendimentos.

After service, Empreedimentos would have 10 days to present its defence against the involuntary bankruptcy petition – Article 96 of the Bankruptcy Law contains a list of facts that can prevent a bankruptcy decree, being:

a) Falsity of the title presented by the creditor;
b) Statute of limitations applies to the case;
c) Nullity of the obligation or its title;
d) The debt has already been paid;
e) Any other face that extinguishes or suspents the obligation, or does not legitimise the collection of the claim presented by the creditor;
f) Defect in the protest or its instrument;
g) Filing of a petition for judicial recovery during the 10-day term that the debtor has to oppose the request for bankruptcy; and

h) Cessation of corporate activities for more than two years prior to the petition in bankruptcy, evidenced by a proper document of the Board of Trade, which must not prevail against evidence that the debtor has, in fact, developed his business activities any time during the referred period.

As a result, anything from the above list may be presented by Empreendimentos in order to ensure that the court will not declare its bankruptcy under any circumstances.

Question 4.2 [maximum 5 marks] [4 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?

For the judicial recovery plan to be approved by creditors secured by in rem guarantees, Empreendimentos will need favourable votes from the majority of such creditors by head count and by value of the claims of the attending creditors.

Should all creditors secured by in rem guarantees attend and vote, Braz Bank SA will hold 52% of the votes, however, for the judicial recovery plan to be approved, Empreendimentos also needs a majority by head count – if Braz Bank SA is the only (secured) creditor to vote in favour, it will not meet the criteria for approval.

NB, the only creditors who are eligible to vote on the judicial recovery plan are those whose claims would be impaired as a result of the same. To this end, unless Brasil Autoparts SA and Oil Brasil SA also have unsecured claims, they could have claims for restitution (i.e. having and seeking the right to a restitution of assets that belong to them but are in the possession of Empreendimentos) – a successful recovery of their assets (and corresponding creditor sum) may result in a full recovery. In this scenario, Brasil Autoparts SA and Oil Brasil SA's claims would not be considered impaired and as a result, they may not be eligible to vote on the judicial recovery plan, meaning Braz Bank SA could carry the vote in Class II. [Argument unrelated to the question]

Side note: any monies due as a result of a restitution lawsuit have to be paid in priority to all other claims (including super-priority claims). [Argument unrelated to the question]

It should be noted that all four classes of claims (labour, secured, unsecured, and those from micro and small enterprises) must approve the plan for it to go ahead. In light of this, even if

the plan was to get a favourable vote by Class II, it still requires approval from the other three classes.

In the event that the other three classes vote in favour of the plan, and Braz Bank SA holds the majority of vote by headcount and value of claim, Empreendimentos is still capable of having its recovery plan approved at a general meeting of creditors.

Article 58 of the Bankruptcy Law details the circumstances in which a cramdown of a judicial recovery plan can occur – this states:

"The requirements of this Law having been met, the judge shall grant the judicial recovery of the debtor whose plan has not been objected to by any creditor pursuant to Article 55 hereof or has been approved by the general meeting of creditors pursuant to Article 45 or 56A hereof.
Paragraph 1. The judge may grant judicial recovery based on a plan that has not been approved pursuant to Article 45 hereof, provided it has obtained, cumulatively, at the same general meeting:
I – the favourable vote of creditors representing over half the amount of all credits represented at the general meeting, independently of classes;
II – the approval of three (3) of the classes of creditors pursuant to Article 45 hereof, or if there are only two (2) classes with voting creditors, the approval of at least one (1);
III – in the c lass that rejected it, the favourable vote of over one third (1/3) of the creditors, computed pursuant to Article 45, paragraphs 1 and 2 hereof.
Paragraph 2. Judicial recovery may only be grated pursuant to Paragraph 2 of this article if the plan does not entail different treatment among the creditors of the class that rejected it."

Given the above, there would be grounds for a cramdown.

Given the above, there would not be grounds for a cramdown.

Question 4.3 [maximum 5 marks] [3 marks – last question not answered]

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?

Braz Bank SA cannot retake possession of the referred piece of land during the stay period if it is essential for Empreendimentos' business activities. NB, the stay period lasts for 180 days and is able to be extended by the court for up to an additional 180 days, should the court consider that the referred piece of land is vital for Empreendimentos' turnaround.

*** End of Assessment ***

TOTAL MARKS 40 OUT OF 50

GOOD WORK!