



39 = 78%

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: 202223-336.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 2023. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2023. 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 8 pages.**



**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total] - 8**

**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**

**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 Bankruptcy Law has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.**
- (d) The Bankruptcy Law allows companies belonging to the same economic group to jointly file for restructuring.**

**Question 1.2 - 1**

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

- (a) Brazil has a single apex court: the Superior Court of Justice, which is in charge of constitutional issues.**
- (b) Tax disputes take place at a specialised segment of the judiciary; composed of tax courts, tax courts of appeal and a superior court.**
- (c) Insolvency proceedings take place at the state-level judiciary (as opposed to the federal-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

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

- (a) A pledge is a lien over movable assets.
- (b) Despite being a lien over immovable property, mortgages may also be used to offer aircraft and vessels as security.
- (c) The *antichresis* is a widely 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 - 1

Which one 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) A big law firm.
- (c) An individual who carries on a business activity without the use of a legal entity.**
- (d) An investment bank.

Question 1.5 - zero

Concerning judicial recovery, indicate the incorrect statement below:

- (a) Failure to present the judicial reorganisation plan within the stipulated period is a case for conversion into bankruptcy.
- (b) The judicial recovery plan must be presented within 60 days from the decision granting the processing of the procedure.
- (c) The special regime of judicial recovery for small or micro enterprises is optional, and the company may opt for the common regime.**

**(d) With no objections to the judicial reorganisation plan, the judge will appoint a general meeting of creditors so that the creditors can deliberate on the judicial reorganisation plan.**

Question 1.6 - 1 (considered right because the options were misleading)

**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 claims, including principal, interest, and fines.**

**(c) Administrative expenses of the estate.**

**(d) Unsecured claims.**

Question 1.7 - zero

**Assume that a debtor under judicial recovery has the following creditors:**

- **700 creditors in class I (workers and labour-related claims);**
- **three creditors in class II (creditors secured by *in rem* guarantees);**
- **150 creditors in class III (unsecured creditors); and**
- **47 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 20 million in class II;**
- **BRL 10 million in class III; and**
- **BRL 200 thousand in class IV.**

**Assuming all creditors are present at the debtor's general meeting of creditors, indicate the only correct 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 an amount 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 100,000.**

Question 1.8 - 1

Select the correct statement from the options below regarding the judicial recovery of small or micro enterprises:

- (a) As it is a simplified regime, there is no stay period.
- (b) There is no discount in the judicial reorganisation plan, but instalments are allowed.
- (c) The remuneration of the judicial administrator is limited to 2% of the amount payable to the creditors.**
- (d) There is no limit in the Bankruptcy Law as to the number of instalments for the payment of the debts.

Question 1.9 - 1

Indicate the correct statement 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 as 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 held by the creditors that were present at the general meeting.**
- (d) A cramdown cannot be imposed if the creditors have presented an alternative recovery plan after rejecting the recovery plan presented by the debtor.

Question 1.10 - 1

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 tax 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 in total]**

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

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

For Judicial recovery the bankruptcy law adopts the of debtor in possession, meaning the debtor continues to manage the business during a judicial recovery but under the supervision of a creditors committee and the judicial administrator, appointed by a judge, creditors and the public prosecutor. Throughout this period the debtor or administrators must continue their business, unless dismissal of the debtor from management is provided for in the recovery plan and in case the debtor(managers) have acted in a faulty manner (change might also be included in the provision of the reorganizatio<sup>s</sup> plan). In terms of Article 64<sup>1</sup>, which reads that the managers shall be removed if the debtor or its managers:

- (a) "have been sentenced finally and conclusively for a crime committed under previous judicial recovery or bankruptcy or for a crime against property, public welfare or economic order provided for by applicable law;*
- (b) shown strong signs of having committed a crime provided for herein;*
- (c) have acted with malice, simulation or fraud against the interests of its creditors;*
- (d) have engaged in any of the following acts:*
  - (i) incurring personal expenditures that are manifestly excessive in relation to his equity condition;*
  - (ii) incurring expenses, the nature and extent of which cannot be justified in view of the capital or type of business, movement of transactions and other similar circumstances;*
  - (iii) unjustifiably decapitalising the company or carrying out transactions that impair its regular functioning;*
  - (iv) simulating or omitting claims on submitting the list referred to in Article 51, main section, III, of the Bankruptcy Law (the complete list of*

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<sup>1</sup> Article 64 of the Bankruptcy Law

creditors) without any relevant reason under the law or being supported by a court decision;

(e) have refused to provide information requested by the judicial administrator or the other Committee members; or

(f) have its dismissal provided for in the judicial recovery plan.”

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

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

Once the judicial administrator has signed the instrument of commitment, he must take the assets and documents of the debtor into his custody.

The administrator must sell the assets either as whole or separately ensuring the best price either:

1. by electronic, in-person or hybrid auction;
2. by a competitive procedure promoted by a specialized agent; or
3. by any other way , as approved under the terms of the Bankruptcy Law.<sup>2</sup>

The sale of assets or guarantee granted by the debtor to a *bona fide* purchaser or lender, and provided that the sale is carried out by express judicial authorization or provided for in an approved judicial or extrajudicial reorganization plan, this may not be rendered ineffective after the consummation of the legal transaction with the receipt of the corresponding funds by the debtor.

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

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

In terms of Article 129 the suspect period may not be retrospective for a period of more than 90 days from the filing of the petition requesting the bankruptcy, or from the time of the first protest by a creditor due to default being<sup>3</sup>:

- (a) “payment by the debtor, within the suspect period, of debts that have not yet fallen due, by any means whereby the claim is extinguished, including advances on a given note payable;
- (b) payment of debts, within the suspect period, that have become due and enforceable, in a way not provided for under the terms of the contract;

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<sup>2</sup> Guidance Text , Brazil , Page 21

<sup>3</sup> Guidance Text , Brazil , Page 39

- (c) *the granting of an in rem guarantee, including a lien, within the suspect period, in relation to a debt previously entered into but not secured. If the assets given in mortgage are the object of other subsequent mortgages, the bankruptcy estate will receive the part of the proceeds that should have applied to the creditor of the revoked mortgage;*
- (d) *acts performed free of charge (for example, a donation or services performed free of charge) during the two years preceding the decree of bankruptcy.” (two years and suspect period are different concepts)*

**Question 2.4 [maximum 3 marks] - 1**

State the requirements that a Brazilian corporation needs to meet to file for judicial recovery.

A petition for judicial recovery must present, in addition to the requirements set forth in the Code of Civil Procedure:<sup>4</sup>

- (a) *“a statement setting out the causes of the economic and financial crisis of the debtor, reasons for financial difficulties;*
- (b) *ALL accounting statements for the last three financial years and for the current year as well as description of the legal entities within the corporate group;*
- (c) *complete list of creditors which will include creditors that are not subject to the judicial recovery proceeding, stating their physical and electronic addresses, as well as the kind, rating and updated amount of their claims;*
- (d) *full list of employees and their functions and salaries;*
- (e) *certificate of regular standing of the debtor with the Board of Trade, updated articles of incorporation and minutes of appointment of current officers;*
- (f) *list of the debtor’s private assets, controlling partners and officers;*
- (g) *updated statements of debtor’s bank accounts and financial applications;*
- (h) *certificates of the protest offices in the judicial district of the debtor’s domicile or headquarters and branches;*
- (i) *list of all legal and arbitral actions to which the debtor is a party, with an estimate of the respective amounts involved;*
- (j) *detailed report on tax liabilities; and*
- (k) *list of assets and rights that integrate the non-current assets in the balance sheet, including the ones that are considered not to be subject to the judicial recovery proceeding due to serving as special types of collateral, along with the respective contracts entered into with the non-subject secured*

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<sup>4</sup> Civil Procedure Code, Art 319

creditors.<sup>5</sup>

If the above-mentioned documents are in order, the judge may grant an order for judicial recovery. Alternatively, the court may order a “pre-inspection”, in terms of which a professional must present a report within 5 days, confirming the correctness of the all the required documents and the actual conditions of the debtor’s establishments.<sup>6</sup>

**(a) the entity must not be bankrupt or, if it has ever been declared bankrupt, the liabilities must be declared to have been extinguished;**

**b) the entity must not have obtained a concession for judicial recovery, or for judicial recovery for micro or small enterprises, within the previous 5 years; and**

**c) the debtor entity, its officers and controlling shareholder must not have been convicted of any offences relating to insolvency procedures.**

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

#### Question 3.1 [maximum 5 marks] - 4

How is a judicial recovery different from an extrajudicial recovery?

The law provides rules on judicial recovery, extra-judicial recovery and bankruptcy proceedings. It further provides provides for extra-judicial recovery, which is a process that enables out-of-court restructuring and is intended to prevent judicial insolvency proceedings.<sup>7</sup> These also provide for specific insolvency rules on:

- civil insolvency proceedings, for individuals and non-business entities regulated by the Civil Code
- insolvency of financial institutions, co-operatives and other entities excluded from the scope of Law 11,101 of 9 February 2005. These are regulated by other specific legislation.

**Judicial recovery proceedings** are requested through a petition to the court by the debtor. This petition should explain the reasons for the economic and financial crisis and must include supporting evidence which consists of:-

- financial statements,
- list of creditors and respective debts,
- list of employees,
- certain certificates relating to debts and enforcement actions,
- corporate documents and agreements,
- list of assets of the controlling shareholders,
- the insolvent company’s administrators,

<sup>5</sup> Guidance Text , Brazil , Page 46

<sup>6</sup> Bankruptcy Law, Art. 51-A.

<sup>7</sup> Law 11,101 of 9 February 2005.

- bank statements,
- investment statements of the insolvent company,
- list of legal actions in which the insolvent company maybe a party to, involves court proceedings.

The insolvent company makes a request to the court for judicial recovery proceedings. Should it be approved, the insolvent company must present a plan to reorganise the business and pay off the debts.

This plan is presented and approved or rejected by the majority of its creditors in a creditors' meeting.

In judicial recovery proceedings, a judicial administrator is appointed to represent the insolvent company, further a creditors' committee can be constituted to represent the creditors.

Should the plan be rejected, the company can be declared bankrupt.

Should the plan be approved by the required majority of creditors in different classes, the company remains in recovery for up to 2 years until it pays off its debts in accordance with the plan<sup>8</sup>.

Under bankruptcy and judicial recovery proceedings, a judicial administrator is appointed to administer the plan, dealing with the creditors and the court. The payment of debts follows a prescribed order of preference.

**Extra-judicial recovery** is not initiated with the Court. The extrajudicial recovery is a hybrid proceeding, which starts as an out-of-court restructuring followed by a court procedure to approve the arrangement.

The debtor negotiates with its creditors to agree a recovery plan, which is then validated with the court.

The insolvent company does not stop its operations.

The insolvent company enters into an agreement with its creditors to settle its debts.

The insolvent company and creditors agree on a plan to reorganize the business and pay off the debts.

This plan, if agreed by the majority of creditors, shall be filed with the court to validate the agreement.<sup>9</sup>

(labour-related claims are not subject to an extrajudicial recovery process automatically because there must be a collective negotiation with the labour union, whereas in judicial recovery such claims are automatically included; in a judicial recovery process, the debtor's assets may be sold free of encumbrances, but this is not possible in an extrajudicial recovery process; and while post-commencement debtor-in-possession (DIP) financing is possible for a debtor in judicial recovery, it is not possible for a debtor in extrajudicial recovery.)

### Question 3.2 [maximum 5 marks] - 4.5

***What is a "claim for restitution" under a bankruptcy procedure, and how does it work?***

<sup>8</sup> Bankruptcy Law, Article 61

<sup>9</sup> <https://cms.law/en/int/expert-guides/cms-expert-guide-to-restructuring-and-insolvency-law/brazil>

Super priority is provided for by law.<sup>10</sup> A claim for restitution in *natura* is not subject to the competition of creditors, [therefore a fiduciary guarantee is advisable.] (?)

The Bankruptcy Law allows certain parties the right to seek restitution of assets or any funds in possession of the insolvent estate. A third party has the right to restitution of assets that belong to him or entity but are in the possession of the insolvent estate. This claim seeks to reclaim property from the estate in order to be returned to the creditor.<sup>11</sup>

Restitution in cash refers to:-

1. Together with the appraised value of the asset and monetary compensation be delivered to a third party if the asset no longer exists at the time of the claim for restitution or, if the asset has been sold, the price it was sold for, as in both cases;
2. the amount delivered to the debtor, in domestic currency, resulting from an advance on an export exchange contract, provided the full term of the transaction,<sup>12</sup> including any extensions, does not exceed the term established in the specific rules of the competent authority;
3. the amounts delivered to the debtor by the *bona fide* contracting party in the event the contract is revoked or declared ineffective; and
4. the amount of withholding taxes, taxes due for subrogation and any amounts received by collecting agents and not transferred to the government.

The amounts due as a result of a restitution, priority payment must be in respect to all other claims, including super-priority claims.

A restitution suit will run under a separate case record. The debtor, the committee of creditors, the creditors and the judicial administrator will be notified about the existence of the request and decide to oppose it or not.

(restitution May also be filed by the seller of an asset sold on credit and delivered to the debtor during the 15 days prior to the petition for bankruptcy, but only if the asset has not yet been disposed of)

### Question 3.3 [maximum 5 marks] - 5

Describe the circumstances in which the creditors may file a recovery plan in a judicial recovery.

In December 2020, the Brazilian Bankruptcy Law went through its first major reform. Federal Law 14.112/2020, which entered in effect as of 23 January 2021, this law introduced provisions on various key matters. For example:-

- the possibility of creditors presenting a judicial recovery plan for the debtor in certain cases,
- the stimulus to the use of alternative dispute resolution procedures such as mediation,
- substantial and procedural consolidation for groups filing for judicial recoveries,
- incentives for the use of DIP financing,

<sup>10</sup> Bankruptcy Law, Article 84

<sup>11</sup> Guidance Text , Brazil , Page 40

<sup>12</sup> Article 75, paragraphs 3 and 4, of Federal Law 4.728/1965

- additional alternatives for the payment of tax debts under a judicial recovery procedure,
- cross-border insolvency,
- improvements to the bankruptcy regime in order to make liquidation cases more efficient.<sup>13</sup>

Since the enactment of Federal Law 14.112/2020, it is possible, if the plan presented by the debtor is not approved by the creditors the creditors can present their own version of a recovery plan for the debtor – a measure that could lead creditors to play a more active role in recovery proceedings, though the presentation of a new plan by the creditors might not be seen so frequently because creditors that support the plan are required to release personal guarantees from third party individuals.<sup>14</sup>

It is possible under these circumstances:

- if the plan presented by the debtor is not approved by the creditors
- the creditors may decide to adjourn the general meeting for a few days in order to negotiate a different recovery plan with the debtor. Where the meeting is adjourned, it must be concluded within 90 days.<sup>15</sup>

The recovery plan is exclusively presented by the debtor in both a judicial or an extrajudicial recovery proceeding, although such plan may be negotiated with the creditors. The creditors who often initiate the bankruptcy proceedings, seeking the involuntary bankruptcy of a company that has defaulted on a given debt. The Federal Law 14.112/2020, creditors are now given the possibility of presenting an alternative judicial recovery plan in case the plan presented by the debtor is rejected at a general meeting of creditors.<sup>16</sup>

In terms of Art 56, para 4, creditors may present an alternative recovery plan if the plan presented by the debtor is rejected at a general meeting of creditors. When the debtor's plan is rejected, the judicial administrator must immediately put to a vote whether the creditors have an interest in presenting an alternative plan – if there are positive votes from creditors owning more than half the claims present at the meeting, the measure will be approved and the alternative plan must be presented within 30 days.

This measure is not likely to become regular practice. Because the creditors that support the plan must forego any personal guarantees provided for by the individuals in relation to their credits that are subject to the proceeding (Bankruptcy Law, Art 56, para 6, V)<sup>17</sup>

(when the term of the stay period has elapsed without deliberation of the judicial recovery plan presented by the debtor)

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

<sup>13</sup> Guidance Text Brazil, Page 5

<sup>14</sup> Guidance Text Brazil, Page 8

<sup>15</sup> Guidance Text Brazil, Page 55

<sup>16</sup> Guidance Text Brazil, Page 23

<sup>17</sup> Guidance Text Brazil, Page 58

**The business company Braz Veículos Ltda (the company) is a subsidiary of a holding company with head offices in Germany. Braz Veículos Ltda produces electrical cars and was incorporated in the city of São Paulo where its board sits, but its operations are conducted from a single plant located in the city of Porto Alegre, where the officers and most of the back office also work. Despite its long history of success, the past few years have been particularly rough for the company, especially as a result of the Covid-19 pandemic. The company has already asked for judicial recovery in the past, and the case was terminated 10 years ago. The company's chief executive officer (CEO) has gathered the board of directors in order to deliberate on a potential filing of a judicial recovery. Several issues have come up during this meeting and your law firm has been hired to advise on the matter.**

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

**(a) Advise why the company should be allowed to file for a second judicial recovery and where the judicial recovery should be filed. (5 marks) - 5**

The company had asked for judicial recovery in the past and the case was terminated 10 years ago. In terms of the Bankruptcy Act the debtor should not have been granted judicial reorganization at least over the past 5 years.<sup>18</sup> Therefore the company should be allowed to file for a second judicial recovery.

Chapter VI-A of the Bankruptcy Law regulates transnational insolvency proceedings. The Brazilian legal system had only adopted the UNCITRAL Model Law on Cross-Border Insolvency when the enactment of Federal Law 14.112/2020, effected on 23 January 2021. This reform of the Bankruptcy Law has given rise to a new legal scenario which impact is not known as yet.

One practical and important aspect that needs to be considered whenever dealing with transnational insolvency, is that any foreign company that wants to set up an agency or a branch to operate in Brazil needs to seek government approval before hand.<sup>19</sup> Therefore in most cases, companies willing to operate in Brazil use an independent corporate form as there is no need to obtain approval to own shares of a corporation or of a limited liability company. As a result, if the parent company is liquidated in a foreign jurisdiction and the administrator of the foreign estate wants to liquidate the subsidiary in Brazil, the Brazilian company, as an independent legal entity, will have to be liquidated in Brazil.

In terms of the forum with jurisdiction to process the judicial recoveries would not necessarily be that of the registered office, but be that of the place where the business activity remains centralised, which forms the vital centre of the main activities of the debtor<sup>20</sup> and where its main assets are.<sup>21</sup>

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<sup>18</sup> Article 48 II

<sup>19</sup> Federal Decree-law 4.657/1942, Art 11, para 1. See also the Civil Code, Art 1.134.

<sup>20</sup> Guidance Text , Brazil , Page 6, STJ, CC 32.988, Reporting Justice Sálvio de Figueiredo Teixeira, decided on November 14<sup>th</sup>, 2001.

<sup>21</sup> Guidance Text , Brazil , Page 6, TJSP, AI 990.09.372608-4, Chamber Reserved for Bankruptcy and Judicial Recovery, Reporting Appellate Judge Elliot Akel, decided on June 1st, 2010; TJSP, AI 642.782-4/0-00, Chamber Reserved for Bankruptcy and Judicial Recovery, Reporting Appellate Judge Elliot Akel, decided on June 30<sup>th</sup>, 2009.



There was a decision where the main establishment should be the place where the debtor has the higher turnover; as the important place from a business perspective.<sup>22</sup>

In a 2017 decision, The Court of Appeals of the State of São Paulo, by its Second Chamber Reserved for Business Matters, in a 2017 decision, ruled that the main establishment was the place where the administrative, financial, commercial and operational decisions were taken and not the place where the industrial plant was located.<sup>23</sup> There are also decisions that used both criteria being :-

1. “centre of activities” and
2. “decision-making centre”

as a basis for establishing the competence, mainly because usually there is a coincidence between them.<sup>24</sup>

Therefore the definition of what the main establishment is dependent on a fact and evidence based investigation.

#### The facts

1. The business company Braz Veículos Ltda (the company) is a subsidiary of a holding company;
2. head offices in Germany;
3. Braz Veículos Ltda produces electrical cars and was incorporated in the city of São Paulo where its board sits;
4. its operations are conducted from a single plant located in the city of Porto Alegre;
5. where the officers and most of the back office also work.
6. No Information is available on the holding company and its operations etc.

From the above facts and notwithstanding any further information that may be available or required, the judicial recovery as stated in the 2017 decision which ruled that the main establishment was the place where the administrative, financial, commercial and operational decisions were taken and not the place where the industrial plant was located, therefore being São Paulo where the board sits. (questionable)

- (b) The company has entered into some preliminary negotiations with key creditors in order to assess whether said creditors would support the recovery of the company. The company currently has five creditors that fall into class II of a judicial recovery: creditors secured by *in rem* guarantees. Through the preliminary negotiations, two secured creditors have signalled that they would vote in favour of a judicial recovery plan, whereas three secured creditors have shown that they are likely to seek the liquidation of the

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<sup>22</sup> Guidance Text , Brazil , Page 6, STJ, AgInt on CC 147.714, Reporting Justice Luis Felipe Salomão, decided on February 22nd, 2017. See also, among others: TJRS, AI 70060247848, Fifth Civil Chamber, Reporting Appellate Judge Jorge Lopes do Canto, decided on June 26th, 2014 (It should be noted that the main establishment is measured by the concentration of the company’s largest turnover, which may or may not coincide with the head offices).

<sup>23</sup> Guidance Text , Brazil , Page 7, TJSP, AI 2230327-51.2016.8.26.0000, Second Chamber Reserved for Business Matters, Reporting Appellate Judge Alexandre Marcondes, decided on April 11th, 2017. See also: TJSP, ED 2062296-73.2013.8.26.0000, Second Chamber Reserved for Business Matters, Reporting Appellate Judge Lígia Araújo Bisogni, decided on October 8th, 2014; TJSP, AI 0080995-49.2013.8.26.0000, First Chamber Reserved for Business Matters, Reporting Appellate Judge Alexandre Marcondes, decided on May 21st, 2013.

<sup>24</sup> Guidance Text , Brazil , Page 7, STJ, Second Joint Panel, CC 37.736, Reporting Justice Nancy Andrichi, decided on June 11th, 2003; TJMG, AI 1.0525.13.017952-2/001, Eighth Civil Chamber, Reporting Appellate Judge Edgard Penna Amorim, decided on December 11th, 2014; TJSP, AI 0124191-69.2013.8.26.0000, First Chamber Reserved for Business Matters, Reporting Appellate Judge Alexandre Marcondes, decided on December 5th, 2013.

company in the event that it initiates a judicial recovery proceeding. The board of directors is aware that the current standing of the class II creditors would not allow for a reorganisation plan to be approved in such class, but doubts have arisen regarding the possibility of a Bankruptcy Court applying a cramdown in order to confirm the plan. Advise the company on whether the current standing of the class II creditors (favourable votes by 40% of the creditors) would, in the future, allow for a judicial recovery plan to be confirmed by a Bankruptcy Court applying the cramdown provisions of the Brazilian Bankruptcy Law (Law Number 11.101/2005). Is further information required in order to offer a more precise legal opinion? **(5 marks) – 2,5**

In terms of Federal Law 14.112/2020 provides an additional tool for the debtor. Because debtors are now allowed to file for extrajudicial recovery as soon as the debtor has one-third of favorable votes from the creditors subject to the proceeding. The debtor has an additional 90 days from the filing to obtain favorable votes in order to reach the 50% required threshold. The measure is especially useful as Federal Law 14.112/2020 also provides for the stay period to apply to extrajudicial recoveries.

The extrajudicial recovery plan can only be rejected by the court if the plan does not comply with the law and, if the plan is not ratified, the debtor may, in the future, file a new petition for the ratification of an out-of-court recovery plan.

When compared to the judicial recovery procedure, the extrajudicial recovery procedure is:

- more flexible,
- simpler,
- faster,
- less expensive and
- less risky.

Due to there is no general meeting of creditors, creditor's committee or judicial administrator and it is easier to approve the plan.

Further, there is no risk of conversion to bankruptcy nor the two-year period in which the proceeding remains running after approval of the plan.<sup>25</sup>

Where a debtor has filed for an extrajudicial recovery seeking immediate protection from the stay period, and not yet meeting the minimum 50% threshold of favorable votes so as to have the plan confirmed, the court will confirm whether the debtor has indeed managed to obtain at least one-third favorable votes – where the debtor has obtained this, the stay period will be confirmed.<sup>26</sup>

Here the company has favourable votes by 40% of the creditors, Class II.

A committee of creditors must be formed by resolution of any of the classes of creditors at a general meeting of creditors.

It should have one representative and two alternates of each one of the classes of creditors, being :-

- (b) labour creditors,
- (c) creditors with *in rem* guarantees or special privileges,
- (d) unsecured creditors and creditors with general privileges, and

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<sup>25</sup> Guidance Text Brazil, Page 60

<sup>26</sup> Bankruptcy Law, Art 163, paras 7 and 8

(e) creditors defined as small or micro enterprises

These creditors have an important role to play at the general meeting of creditors. The general meeting is called to make a decision regarding the judicial recovery plan, and further has other important functions, eg. to decide any matter in the creditors' interest and to approve alternative types of asset settlement in bankruptcy.<sup>27</sup> When a debtor's judicial recovery plan is rejected, creditors also have the opportunity of presenting an alternative plan.

Where the judicial recovery plan is rejected at a general meeting of creditors, the Judicial Administrator will put to a vote the concession of a 30-day period for the creditors to present alternative judicial recovery plan.<sup>28</sup> This could be a possibility for the above company, where the creditors could present a suitable plan for consideration.

The creditors eligible for voting are only those whose claims are impaired by the terms of the recovery plan. Where the plan does not provide any alteration to the original conditions of payment of a given claim, the creditor has no voting rights.<sup>29</sup> In this regard more information will be necessary in respect to whether their claim in order to determine whether they have voting rights or not.

It is not possible for a single class to approve and adopt the recovery plan separately. All four classes must approve the plan.<sup>30</sup> Once the plan has been approved by the general meeting of creditors, it will be enforced against minority dissenting creditors.

When the judicial recovery plan is not approved by the general meeting of creditors, Article 58 of the Bankruptcy Law contains provisions on the cramdown of the judicial recovery plan.

The cramdown is merely the adoption of lower thresholds with regard to the approval quorum on the judicial recovery plan:

*“Article 58. 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 56-A 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 favorable 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 (3) classes with voting creditors, the approval of at least two (2) of them, or if there are only two (2) classes with voting creditors, the approval of at least one (1);*

*III – in the class that rejected it, the favorable vote of over one-*

<sup>27</sup> Brazilian Bankruptcy Law, Article 35

<sup>28</sup> Guidance Text, Brazil, Page 69

<sup>29</sup> Guidance Text Brazil Page 55

<sup>30</sup> Brazilian Bankruptcy Law, Article 45

*third (1/3) of the creditors, computed pursuant to article 45, paragraphs 1 and 2, hereof.*

*Paragraph 2. Judicial recovery may only be granted pursuant to Paragraph 1 of this article if the plan does not entail different treatment among the creditors of the class that rejected it.”*

The debtor shall submit clearance certificates of tax debts under Articles 205, 206 of Statute 5,172, of October 25, 1966 - Brazilian Tax Code in terms of Articles 151, thereafter in terms of Article 58, paragraph 1, III, “– *in the class that rejected it, the favorable vote of over one-third (1/3) of the creditors, computed pursuant to article 45, paragraphs 1 and 2, hereof.*

(question not entirely answered; comments about aspects not related to the issue]

There is a possibility of an order being granted by a bankruptcy court subject to requirements being met and based on Article 58.

- (c) The company has recently acquired new auto-components manufacturing machines which are deemed essential to the carrying on of the business, given the need of the company to adapt to a new market. The financing for the acquisition of the machinery was granted by Banco XPTO, a Brazilian financial institution. The financing is secured by a fiduciary title over the machines. Due to the rough financial situation of the company, the company has recently defaulted on the financing and were not able to pay some of the instalments that had fallen due. The board of directors is worried that the bank might take possession of the machinery, given its fiduciary security. Advise the company whether the stay period might keep it (the company) in possession of the machinery. **(5 marks) - 3**

#### The Facts

3. Financed by Banco XPTO.
4. Secured by a fiduciary Title over the new auto-components manufacturing machines.
5. Company defaulted – not paid some of the instalments.

Even upon an insolvency proceeding of the debtor, some creditors might hold specific securities or contracts which grant their claim immunity to any sort of restructuring. In this case, for creditors secured by a fiduciary title on the assets being the new auto-components manufacturing machines. Albeit they are not subject to the insolvency proceedings, these creditors may not retake possession of the collateral during the stay period, being 180 days and may be extended by court.

A fiduciary title is a *in rem* lien on assets securing the payment of a debt. The two differences between the fiduciary title and the mortgage, and other *in rem* guarantees, is that the title to the property of the asset is transferred to the creditor. The creditor can sell the property in case of default without the need to go to court.

Due to the above and as a consequence of the property rights belonging to the creditor,

in this case being, Banco XPTO and should the company get into judicial recovery, Banco XPTO is considered to own a claim that is not subject to the insolvency proceeding, because, a claim secured by fiduciary title cannot be adjusted by a restructuring plan. Further, Banco XPTO secured by fiduciary title over the machinery keeps the right, under certain circumstances, to take possession of the asset and sell the asset outside of the insolvency proceedings. The reason why fiduciary title is increasingly used when compared to other types of *in rem* guarantees as it offers additional protection to the creditor.

The perfection of a fiduciary title guarantee does not require a public deed, but the agreement must be duly registered. The fiduciary title on the machinery must be registered with the Registry of Titles and Documents of the place where the company is domiciled. A lack of registration leads Banco XPTO to not being able to enforce its guarantee – in the case of the company’s insolvency, the Banco XPTO would thus own an unsecured claim.

Although fiduciary titles provide for a quicker recovery of the collateral, it is still a very common situation under judicial recovery cases for a creditor who has a perfected security interest on an asset is not allowed to take possession of the asset. This seems to be perfectly valid during the stay period.<sup>31</sup> The problem, however, is that even after this term creditors might face difficulties in taking possession of the asset if the court considers the asset as being fundamental for the turnaround.<sup>32</sup>

Sometimes the stay period has been extended in several cases when the debtor was considered to not be in fault for the fact that the judicial recovery plan had not yet been approved as the time frames provided by the Bankruptcy Law are not always met in reality.<sup>33</sup> Further the Superior Court of Justice has already decided that creditors cannot automatically resume foreclosure measures as soon as the 180-day term is over.<sup>34</sup> There can be no expropriation without the consent of the Bankruptcy Court. This scenario sometimes makes it very difficult for the holder of a fiduciary title to enforce his rights, especially as the Courts tend to judge in favor of the debtor.

(there was no effective answer, only reproduction of the guidance text, apparently)

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<sup>31</sup> Article 49, Paragraph 3 of the Bankruptcy Law states that essential capital goods may not be removed from the debtor’s establishment during that period.

<sup>32</sup> Guidance text Brazil, Page 12 & 13

<sup>33</sup> STJ, AgRg on CC 111614, Second Joint Panel, Reporting Justice Nancy Andrighi, decided on November 10th, 2010; TJSP, AI 2000601-16.2016.8.26.0000, First Chamber Reserved for Business Matters, Reporting Appeal Judge Francisco Loureiro, decided on March 10<sup>th</sup>, 2016; TJSP, AI 2215674-15.2014.8.26.0000, First Chamber Reserved for Business Matters, Reporting Appeal Judge Francisco Loureiro, April 8<sup>th</sup>, 2015. Note that Federal Law 11.101/2005 used to read that the stay period would last for exactly 180 days, extensions being prohibited. Despite the Bankruptcy Law’s wording barring stay period extensions, the measure became popular as very few restructuring proceedings were sufficiently developed by the time the 180-day period expired. Anyhow, since the enactment of Federal Law 14.112/2020, which provides for the possibility of the 180 day stay period being extended a single time for another 180 days, certain courts have been more reluctant to extend the stay for a period that exceeds the statutory limit of 360 days: TJSP, AI 2293202-18.2020.8.26.0000, First Chamber Reserved for Business Matters, Reporting Appeal Judge Alexandre Lazzarini, April 9<sup>th</sup>, 2021; TJSP; AI 2200664- 81.2021.8.26.0000; First Chamber Reserved for Business Matters, Reporting Appeal Judge Alexandre Lazzarini, May 3<sup>rd</sup>, 2022. Guidance text Brazil page 14

<sup>34</sup> STJ, AgRg on CC 127.629, Second Joint Panel, Reporting Justice João Otávio de Noronha, decided on April 23<sup>rd</sup>, 2014; STJ, AgRg on CC 125.893/, Second Joint Panel, Reporting Justice Nancy Andrighi, decided on March 13<sup>th</sup>, 2013. Guidance text Brazil page 14

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**\* End of Assessment \***