

INSOLVENCY PROCEDURES IN BRAZIL – BASIC INFORMATION

Summary:

Section I: Debt Restructuring (p. 1)

Section II: BNK and JR Procedures (p. 2/7)

Section III: Categories of Creditors in JR (p. 8)

Section IV: Ranking of debts in BNK (p. 9/10)

Section I: Debt Restructuring

1. Negotiation without legal procedures: It saves time and money. If the Debtor succeed to negotiate with the major creditors, it will be easier to manage the conflicts with the minor creditors. It is difficult to negotiate with all the creditors. No legal benefits during the negotiation.
2. Extrajudicial Reorganization (ER): This is a mix between the Negotiation and the Judicial Reorganization (“**JR**”). The Negotiation phase is conducted without the formalities of the JR, but the Debtor must obtain the Judge approval to have his plan of payment executed and binding for all creditors submitted to the plan. The proceeding to obtain the Judge approval is very formal as is in the JR. Employees will not be bound by the agreement, and it will need to convince 60% of the debt on each other category. There is no the moratorium period of 6 months. Facing these facts, if Negotiation fails JR usually is the better solution.
3. Judicial Reorganization (“**JR**”): It will stop current and future execution of debts (payment moratorium) for at least 6 month from Judge accepting to process the request. The Debtor could face difficulties before the market to manage the business.
4. Bankruptcy (“**BNK**”): A Creditor or any Interested Person or Company can buy assets from the Debtor in the Bankruptcy Proceeding. This selling of assets is conducted by the Administrator and the Judge and occurs in a Public Auction. It could take several years to be resolved.

Section II: BNK and JR Procedures

1. **BNK At creditor's request:**
2. Threshold:
 - a. A Creditors who holds an enforceable document of debt (“título executivo”) can request the bankruptcy of his Debtor.
 - b. The document of debt has to be publicized in the Notary (“protesto”) and the minimum value of the debt to this request is BRL 31,520.00.
3. Documentation for service of the request is issued at the court and needs to be served to Debtor and return to the court file.
4. Debtor to respond within 10 days from the day of service note returned to the court folder.
5. Possible Debtor answers:
 - a. There is no debt:
 - i. Debtor has to prove that the debt does not exist. In this case Debtor can make a judicial deposit of the value of the debt, with interest and expenses of the lawsuit, as a bail. If Debtor wins, the deposit is reverted to Debtor. If Debtor loses, the deposit is reverted to the Creditor. If there is this bail the bankruptcy is not decreed.
 - b. There is a debt: If there is no payment or if it is not offered the bail mentioned above, the Judge must decree the bankruptcy of Debtor; or Debtor has the faculty to require the JR of the company in the same deadline mentioned in the item 4 above.
6. **Only JR (it is not mandatory the existence of a previous BNK request):**
 - a. To request the JR, Debtor needs to open a lawsuit and files the following information and documents:
 - i. Basic history of the company and how it got to that financial situation.
 - ii. Balance sheet and financial statements of the latest three years.

- iii. List of Creditors, including address, nature, class and the present value of the credit.
 - iv. List of the employees, including job, salary and values owed according to the labor rights.
 - v. Corporate documents.
 - vi. List of Assets of the controlling shareholder. The same list of assets for the Debtor officers.
 - vii. Statements of the bank accounts and financial assets.
 - viii. Certification of the Notary of debts (“protestos”).
 - ix. List of all lawsuits involving Debtor, including estimated values.
7. If the documents are regular the Judge will order the processing of the JR:
- a. Administrator is appointed. Usually a lawyer or economist. It will supervise, as external officer of the court, the process.
 - b. Payment moratorium starts to count. The Bankruptcy and Recovery Act provides **6 months** of moratorium, but some Judges extend this deadline since well justified. This moratorium will imply the suspension of all executions against Debtor, **except** the executions regarding credits not included in the JR (tax, fiduciary property and loans of foreign currency). The ordinary lawsuits that demands prove of the right of the Plaintiff will not be suspended until a judicial final decision recognizing the existence of the debt (ex: lawsuits of indemnifications contested by Debtor or labor claims contested by Debtor).
 - c. A Public Notice of the JR is made in the Official Gazette to make the JR public for all creditors. The creditors have 15 days to present their requests to be included in the JR or to rectify the value of their credits. Each request opens a legal procedure to be analysed by the Administrator and, if still are divergence about the credit, by the Judge.
 - d. Debtor will have **60 days** to present a recovery plan (“RP”). This RP:
 - i. Usually drafted by a financial advisor. It is not a must.

- ii. An economic evaluation of the assets has to be made by an economist or an accountant.
- iii. Shows how cash will be created to pay the creditors.
 - 1. By operating the business (so it is conditional to business success), or
 - 2. By selling assets,
 - 3. Or a combination.
- iv. Shows payment schedule for taxes (usually negotiated with Tax Authorities up to 84 instalments before the Brazilian Federal Revenue Office) and Categories (as per each Category own schedule).
- v. Each Category can be treated differently but no discrimination within the category is allowed, as payments are pro rata within the category.
- vi. Payment will be directly to creditor not to a pool.
- e. Upon presentation of the RP, the Judge orders the following:
 - i. If is the case, to return the plan and ask form clarifications.
 - ii. To ask creditors for feedback within **30 days**.
 - 1. If no rejection, plan approved.
 - 2. If one creditor or employee rejects the plan:
 - a. Judge will call for a Creditor Meeting.
 - b. Judge decision for that call could take a while and usually the meeting takes place within **60 to 120 days**.
 - i. At the Creditor Meeting:
 - 1. Approve:
 - a. This is done by 50% of each Category (by amount of debt or absolute number of employees and small companies, among

those present in the meeting)
voting in favour.

- b. If there is no approval of the recovery plan by all classes of creditors, the Judge can authorize the execution of the recovery plan if occur the following cumulative situations:
 - i. the favorable vote of Creditors representing more than 50% of the total credits;
 - ii. the approval of at least two classes of creditors;
 - iii. in the class that rejected the plan, the approval of at least Creditors representing 1/3 of the total credits of this class; and
 - iv. the recovery plan cannot treat differently the creditors in the class that rejected the plan.
- c. After the approval of RP Debtor has to present the certification of inexistence of tax debt (in practical Debtor has to negotiate with Tax Authorities

an specific plan of payment of the tax debt).

2. Reject the RP:
 - a. This moves the process to BNK.
 - b. The procedure of BNK initiates as described below.

8. If BNK:

- a. Administrator is appointed. Usually a lawyer or economist. This appointment cancels all corporate powers of Debtor officers, now taken by the Administrator.
- b. Debtor will have 5 days after the decree of bankruptcy to present the list of creditors.
- c. A Public Notice of the BNK is made in the Official Gazette to make the BNK public for all creditors. The creditors have 15 days to present their requests to be included in the BNK or to rectify the value of their credits. Each request opens a legal procedure to be analysed by the Administrator and, if still are divergence about the credit, by the Judge.
- d. Administrator can consider that running the business for a while it is important to the conservation of the assets before the selling; or can decide to stop the business activity.
- e. Immediately after the bankruptcy decree the Administrator can initiate the measures to the liquidation of assets of the Company, including in legal order of preference: (a) selling of the business operation as an unity; (b) selling of branches or separated units of the business operation; (c) selling of all the goods and inventory as an unity; and (d) separate selling of individual goods. The process of liquidation is made in a public auction (any creditor or third company or person can participate).

- f. Administrator can ask the court to invalidate agreements entered up (a) to 90 days of BNR request was first filed or (b) to 90 days of JR request, if is the case, or (c) to 90 days of public request for payment (“Protesto”).

Section III: Categories of Creditors in JR

- A. **Employees:** Past and future employees that have a claim.
- B. **Secure creditors:** Those with tangible guarantees (“in rem”) such as real estate, stockpiles and equipment. Not included personal guarantees or guarantees not backed by assets.
- C. **Small and micro entities** that are unsecured creditors:
 - a. Micro companies are those with up to BRL 360K annual gross turnover.
 - b. Small companies are those with higher turnover up to BRL 3,600K.
- D. **Other unsecured creditors:** Bigger turnover than the Small and Micro.

According to the Bankruptcy and Recovery Act credits based on “ACC” operation (loan of foreign money) and credits secured by fiduciary property are not classified in any category because these credits are not affected by the bankruptcy or judicial recovery.

Section IV: Ranking of debts in Bankruptcy

1. Fees owed to the judicial trustee and his assistants.
 - a. For the purposes of defining the amount to be paid as remuneration, the judge shall take in consideration the following aspects: (a) the debtor's payment capacity, (b) the level of complexity of the work and (c) the average market fees actually paid for similar tasks.
 - b. However, it cannot exceed 5% (five per cent) of the debt total amount of the listed creditors, in case of judicial reorganization, or of the assets final price of sale in the bankruptcy.
2. Labor-related claims and occupational accident claims, related to services rendered after the bankruptcy decree.
3. Funds provided by creditors to the bankruptcy estate.
4. Expenses from the bankruptcy proceeding (such as collection, administration and sale of the bankruptcy estate assets and distribution of the proceeds) and court costs.
5. Obligations arising from juridical acts performed during judicial reorganization proceedings, or after the bankruptcy decree, expenses and taxes related to the period after the bankruptcy decree.
6. Labour-related claims, limited to 150 minimum wages per creditor (BRL 118,200.00), and occupational accident claims, the rest unsecured.
7. Secured claims (that is, claims with in rem guarantees, such a mortgage or pledge to the limit of the value of the encumbered asset).
8. Tax claims, regardless of their nature and length of constitution (except for tax fines).
9. Special privileged claims (very specific legal situations).
10. General privileged claims (very specific legal situations).
11. Unsecured claims (including the balances of secured claims that exceed the value of the encumbered asset, balances of labour-related claims that exceed the limit referred to above and labour-related claims assigned to third parties).
12. Contractual penalties and fines for breach of criminal or administrative law, including tax related fines.

13. Subordinate claims (provided for by law or contract and the claims of partners and officers without an employment bond). Such as intercompany loan, personal loan of related party.