

Changes to Brazil's Corporate Insolvency Law

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Topics

New Reorganization and
Bankruptcy Act

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On December 24th, Federal Law 14.112/2020 was finally confirmed by the Brazilian Presidency, introducing significant changes to the legislation on judicial reorganization (recuperação judicial - "JR") and other insolvency proceedings governed by Federal Law 11.101/2005 ("Reorganization and Bankruptcy Law").

This article will consider only some of the most significant changes made by the new legislation.

One of the high points are the new kinds of protection given to investments in debtors under JR, whether by means of debt (DIP or debtor-in-possession financing) or acquisition of assets.

Under the new legislation, if authorized by the JR court, debtors under JR may contract DIP loans, offering their own or third parties' assets as collateral. The new legislation also makes it clear that DIP loans are excluded from the JR and will have priority for repayment over practically all other claims in the event of the debtor's bankruptcy. Lastly, if the loan has been disbursed by the lender, any modification of the JR judge's decision to authorize the DIP loan will not alter the exclusion of the claim from the JR or affect the collateral given to good-faith creditors.

On acquisition of assets, in addition to expressly providing that an individual productive unit (IPU) may be composed of assets of any kind, Law 14.112 makes it clear that the sale of an IPU to a good-faith creditor, as authorized by the JR court or as provided for by a JR plan approved by the general meeting of creditors, cannot be set aside or avoided after the transaction is closed.

As approved by Congress, Law 14.112 amended article 60 of the Reorganization and Bankruptcy Law to make it even clearer that acquirers of IPUs do not succeed in debtors' obligations of any kind. This provision, however, was vetoed by the Presidency, on questionable grounds related to potential environmental and anticorruption liabilities, casting a shade of uncertainty on investments in assets with such a risk profile.

As for tax claims, the new legislation makes some slight advances, such as increasing the number of installments for payment of tax debts, from 84 to 120, and introducing the possibility of settlements with the tax authorities, as provided for in Law 13.988/2020. The tax authorities continue to be excluded from the effects of the JR. However, they now have legal standing to make

submissions on various acts performed during the JR, including sale of the debtor's assets.

The Presidency vetoed important rules that would have reduced the tax cost associated with debt renegotiations and capital gains on sale of assets in insolvency proceedings.

Another significant change made by the new legislation is that creditors may now propose an alternative JR plan if (i) the plan presented by the debtor is rejected at the general meeting of creditors ("GMC") or is not voted on during the stay period (180 days, which may be extended for another 180 days) and (ii) the creditors at the GMC approve, by a majority of the creditors present at the meeting, the presentation of an alternative JR plan ("Creditors' JR plan").

Creditors' JR plans must meet certain conditions in addition to those applicable to any JR plan.

Among those conditions, (i) the plan must be supported by creditors representing more than 35% of the claims present at the GMC that approved presentation of a Creditors' JR plan, or 25% of all claims subject to the JR, and (ii) the plan may not impose on the debtor or its partners or shareholders a sacrifice greater than would result from bankruptcy.

As in any process of change, the modifications made by the new legislation are not free from criticism. Law 14.112/2020 came into effect 30 days after publication, on January 23rd, 2021 and will certainly cause intense debate among legal professionals, requiring adequate and uniform application by Brazilian courts, in order to achieve the underlying policies of Brazilian corporate insolvency regime.

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