INSOL INTERNATIONAL

THE RESTRUCTURING OF CORPORATE GROUPS

A GLOBAL ANALYSIS OF SUBSTANTIVE, PROCEDURAL AND SYNTHETIC GROUP PROCEDURES

INSOL INTERNATIONAL

International Association of Restructuring,
Insolvency & Bankruptcy Professionals

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PRESIDENT'S INTRODUCTION

Rapid technological and digital change and innovation have enabled business to be conducted across borders, very often making use of complex corporate group structures with various group entities, assets and creditors located in different jurisdictions across the world.

In this business and economic setting, there has never been a greater need for a consistent, predictable and uniform international framework for recognition, coordination and enforcement in relation to cross-border restructuring processes for group enterprises.

This has become a key focus point for the United Nations Commission on International Trade Law (UNCITRAL) through the activities of its Working Group V (Insolvency). In July 2019, UNCITRAL released the Model Law on Enterprise Group Insolvency (MLEGI), designed to address the specific needs of cross-border restructuring and insolvency processes impacting multiple group members, as distinct from the Model Law on Cross-Border Insolvency (MLCBI) which only deals with the insolvency context of a single debtor. The MLEGI draws upon some of the features identified in the European Insolvency Regulation Recast, and is also intended to operate in conjunction with Part 3 of the UNCITRAL Legislative Guide on Insolvency Law dealing exclusively with the treatment of enterprise groups in insolvency.

The adoption and implementation of the MLEGI – along with the further uptake of the MLCBI – will be priority areas for UNCITRAL, INSOL International, the World Bank and other international insolvency regulatory and policy bodies in the years ahead.

However, in the interim – and given that no jurisdiction has yet adopted and implemented the MLEGI – it is important to understand and analyse the various approaches taken by different countries to corporate group restructuring involving entities, assets and creditors across borders. It is also important to consider the potential for cooperation through novel means such as synthetic restructuring, taking after the cross-border undertakings offered by the joint English administrators in the landmark case of *Re Collins & Aikman Europe SA* [2006] EWHC 1343.

This new publication from INSOL International – *The Restructuring of Corporate Groups: A Global Analysis of Substantive, Procedural and Synthetic Group Procedures* – does precisely that. It consists of 18 country contributions, as well as a chapter looking specifically at how Brexit will shape corporate group restructuring recognition and cooperation in the United Kingdom and the European Union in future years. Each chapter identifies the potential for substantive, procedural and synthetic restructuring processes and draws attention to key cases, legislative provisions and international treaties. There is also a focus on future policy development that may shape the potential for coordinated proceedings and cooperation.

This book is an invaluable contribution to law reform and regulatory and policy development in relation to the implementation of a harmonised, consistent approach to cross-border restructuring processes in a manner that enhances efficiency, reduces costs and increases the prospect of viable enterprises being able to undergo successful corporate and business restructuring in the interests of debtors and creditors alike. Importantly, those outcomes also provide a broader benefit to financial stability and economic growth at this critical juncture in our global history.

I express my sincere thank you to each of our contributors for their time, expertise, commitment and patience in completing this project over a number of years, as well as to our team of INSOL International technical and administrative staff for their efforts in bringing the project to fruition.

I hope you enjoy reading this publication and will find it useful in your future pursuits.

Scott Atkins
President & INSOL Fellow
INSOL International
May 2022

FOREWORD

This book is a special INSOL International publication which explores and evaluates the legal, economic and practical benefits of substantive and procedural consolidation of corporate group restructuring processes in 17 jurisdictions across the globe.

In countries where consolidated group restructuring proceedings are not yet available, the book also explores whether the use of so-called "synthetic" consolidated group proceedings would be admissible under local legislation and could result in similar benefits to actual consolidation for all stakeholders involved. Synthetic, in this sense, is a term used to describe measures put in place to obtain the same or a similar result without following the normal procedure.

In addition to the 18 country contributions, Professor Dr Stephan Madaus from the Martin Luther University Halle-Wittenberg has analysed, in a separate chapter, the impact that the United Kingdom's departure from the European Union (EU) as a result of Brexit may have on established practices concerning the restructuring of international corporate groups, and the future of the United Kingdom as a European hub for global group proceedings.

Empirical studies have shown that, when a company is part of a group, there is a reduced prospect of the company becoming bankrupt in the first place (primarily on the basis of the reallocation of resources and risks across companies in the group, and the increase of debt-bearing capacity and the reduced cost of debt through the provision of intra-group debt guarantees) compared to where entities exist on a standalone basis.[1]

Those same studies show that, if one or more companies in a group do in fact become bankrupt, then the ability to use consolidated group restructuring or bankruptcy procedures can also significantly reduce costs (as compared to using insolvency processes for each individual entity) and therefore increase the potential return to creditors.

In that context, consolidated group restructurings can offer significant economic benefits. In cases where substantive and / or procedural consolidation options are limited, synthetic processes can achieve similar outcomes.

In fact, those very outcomes were achieved on a synthetic basis in the *Collins & Aikman* case, a main proceeding in the United Kingdom that was led by one primary administrator without opening secondary proceedings in the different EU Member States, after making a commitment that creditors in the other EU Member States would be paid dividends in a priority according to their local insolvency laws. The *Collins & Aikman* case resulted in a higher return for all the creditors in the different EU Member States, as compared to what restructuring on the individual legal entity basis would have achieved.

[1] N Dewaelheyns and Prof C Van Hulle, "Corporate Failure Prediction Modelling: Distorted by Business Groups' Internal Capital Markets?" (2006) *Journal of Business, Finance and Accounting*.

The *ratio legis* to this book was also meant to collect materials to support the proposal on consolidated group proceedings made by INSOL Europe on the Revision on the European Insolvency Regulation (EIR) in May 2012.[2] There, the idea was put forward that, regarding groups of companies, the centre of main interests (COMI) of the ultimate parent company ought to be deemed to be the COMI of the subsidiaries. The advantage would have been that, in the event of group insolvency, the court of the COMI would be able to safeguard the coordination of the main insolvency proceedings with respect to all the group companies and, secondly, the latter would in turn safeguard the application of the EIR then (the EIR Recast now) whenever the ultimate group COMI was located outside the EU.

My aspiration with this book is to provide an objective analysis of the current practices in different countries globally in relation to consolidated group restructuring and to make critical comments as to whether, even in the absence of legal options for substantive and procedural consolidated restructuring, synthetic legal group restructuring proceedings could be effectively used to achieve a more beneficial result than general coordination and cooperation procedures used in particular cases.

It is hoped that this book will be a valuable tool for practitioners, academics and the judiciary across the world and that the conclusions reached may serve as the basis for future law reform locally, regionally and globally.

This project would not have been possible without the help and support of many others. The initial acknowledgement must however go to the Technical Research Committee of INSOL International and Dr Sonali Abeyratne, Dr Kai Luck and Ms Waheeda Lafir in particular for all their assistance throughout the completion of the project, Ms Marie Selwood for the English language revision, and of course to all the chapter contributors to the book globally for their time, expertise and commitment. My final thanks go to Mr Neil Cooper, my mentor for over 30 years, who provided me with valuable insights in relation to the *Collins & Aikman* case and taught me to think out of the box and to always try and provide practical solutions to the benefit of all the stakeholders concerned in an insolvency or restructuring proceeding.

Nora Wouters
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May 2022

[2] R Van Galen, M Andre, D Fritz, V Gladel, F Van Koppen, D Marks QC and N Wouters, "Revision of the European Insolvency Regulation", Proposal INSOL Europe, 2012, 92-93.

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BRAZIL

1. Consolidated group restructurings versus cooperation or coordination procedures

Federal Law No 11.101/2005 (Brazilian Bankruptcy Law), recently amended by Federal Law No 14.112/2020, regulates business insolvencies in Brazil. In addition to this, there are specific rules on civil insolvency proceedings, applicable to consumers and non-business entities, and on the insolvency of financial institutions, co-operatives and other entities, which are excluded from the scope of the Brazilian Bankruptcy Law.

Under the Brazilian Bankruptcy Law, there are three insolvency proceedings available: a court-supervised reorganisation proceeding (*Recuperação Judicial*); an expedited pre-packaged reorganisation proceeding (*Recuperação Extrajudicial*); and a bankruptcy liquidation proceeding (*Falência*).

The bankruptcy liquidation proceeding is designed for individual corporate entities, there being no provision under the Brazilian Bankruptcy Law for dealing with joint filing of bankruptcy liquidation proceedings of companies of the same corporate group. There are, however, rules preventing the extension of the effects of the bankruptcy liquidation proceeding to related entities. The Brazilian Bankruptcy Law allows the corporate veil of the debtor company to be lifted if there is abuse of legal personality, characterised by deviation of purpose or fraud, provided that the requirements set forth in the Civil Code and the procedural rules of the Code of Civil Procedure are observed.

As for the judicial reorganisation proceedings, after nearly 15 years of absence, the matter was addressed by the reform brought by Federal Law No 14.112/2020, which sets forth express rules concerning procedural and substantive consolidation of corporate groups. Despite this, the rules introduced are either redundant or excessively open to interpretation, so the courts remain without a safe basis to apply procedural or substantive consolidation on a case-by-case basis.

Thus, despite the express rules introduced by the reform, the criteria applicable to corporate group insolvencies still have to be extracted from case law. This is not an easy task. First, relevant case law may differ greatly from federal state to federal state, as state courts have exclusive jurisdiction over insolvency matters. Second, the analysed precedents are non-binding,[1] and courts may therefore change their position with little or no regard to previous decisions, which means that judges of the same court may have completely opposing positions. All in all, despite all the efforts, currently there is no reliable and predictable course for all the aspects of joint filings for corporate group restructurings in Brazil.

- **Court-supervised reorganisation of corporate groups**

  The court-supervised reorganisation proceeding is basically a mechanism for forced renegotiation and the restructuring of debt. It was introduced into the Brazilian insolvency system in 2005, with the enactment of the Brazilian Bankruptcy Law.

  The proceeding starts with a petition filed by the debtor, accompanied by the mandatory documents listed in article 51. The court analyses the petition and, if it considers that all the formal requirements have been met, issues an initial order, thus commencing the reorganisation proceeding, staying all enforcement actions

[1] Brazil is a civil law country, in which the *stare decisis* principle has very limited application.

against the debtor and appointing a court trustee to supervise the activities of the debtor company. The debtor then has 60 days[2] to present a reorganisation plan to be voted on by its creditors at the creditors' meeting. During the proceeding, the debtor remains in possession of its business and continues to operate its activities normally. On the other hand, if the necessary majorities for approving the reorganisation plan are not obtained, the court-supervised reorganisation proceeding is converted into a bankruptcy liquidation proceeding.

It is very common for corporate groups to jointly file for a court-supervised reorganisation. Before the comprehensive legal reform in 2020, the debtor companies filed jointly based on the general rules on the matter contained of the Brazilian Code of Civil Procedure.[3] After the recent legal reform, article 69-G was introduced to the Brazilian Bankruptcy Law, allowing companies of the "same corporate group" to jointly file for reorganisation. Each debtor has to meet the legal requirements for filing for court-supervised reorganisation and shall submit the required documentation. The petition shall be filed before the court where the principal place of business of the corporate group is located. If the requirements are met, the court will appoint a single judicial administrator for the group and will order the procedural acts to be coordinated or performed jointly.

In general, even before the legal reform and the introduction of article 69-G, courts have authorised the commencement of joint reorganisation proceedings for corporate groups. Most litigation at this point involves other issues, such as which companies are part of the corporate group, which criteria should be applied to determine whether a company is part of the same corporate group, and the location of the principal place of business of the corporate group. But, in any event, the joint filings have widely been accepted by courts.

A study reproduced in an academic paper published before the reform demonstrates such wide acceptance of joint filings by courts.[4] The study conducted an empirical analysis of 41 court-supervised reorganisations involving multiple debtors, filed between 1 September 2013 and 1 October 2015, before the first and second lower civil courts for bankruptcy proceedings in the City of São Paulo (Bankruptcy Courts for the City of São Paulo).

The study found that, in all such proceedings, even before the legal reform and the inclusion of express provisions in regard to procedural and substantive consolidation, the two Bankruptcy Courts for the City of São Paulo admitted a single proceeding for the debtor companies and appointed one trustee for all companies, based on the above-mentioned civil procedure rule for multiparty lawsuits.

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[2] Article 219 of the new Brazilian Code of Civil Procedure, enacted in 2015, determines that only business days shall be counted for all legal time periods. There has been a certain amount of controversy over whether such provision is applicable to the insolvency proceedings regulated by the Brazilian Bankruptcy Law, especially since the inclusion of art 189, § 1°, I to the Brazilian Bankruptcy Law, which states that all time periods related to procedures set forth in the Brazilian Bankruptcy Law should be counted in calendar days. Even before the inclusion of this article, the latter has been the prevalent position of the courts, based on some precedents of the Superior Court of Justice – STJ.

[3] The current Brazilian Code of Civil Procedure was enacted in 2015. The previous code from 1976, however, contained the very same rule in its art 46.

[4] CEREZETTI, Sheila Neder e SATIRO, Francisco. "*A silenciosa 'consolidação' da consolidação substancial*", in Revista do Advogado No 131, October 2016, coord ADAMEK, Marcelo Vieira.

Even though there is no similar study for any other courts, this probably also holds true in other states as a matter of practice. The appellate courts have also endorsed such wide acceptance of joint filings.

Joint filings are thus widely accepted in Brazil, thereby pre-empting any necessity for cooperation and coordination between courts and insolvency practitioners (IPs), or the need for a group coordinator.

However, there are different rules applicable for *substantive* consolidation of debtor companies. Brazilian Courts have adopted different positions over the matter. The recent legal reform included express provisions on the topic, but these provisions are yet to be consistently construed by case law. Consequently, the guidelines for the application of substantive consolidation remain not entirely clear.

- **Bankruptcy liquidation proceedings of corporate groups**

The bankruptcy liquidation proceeding basically consists of a free and clear sale of all the company's assets (preferably in a bundle) in order to pay the creditors pursuant to the priority order provided in article 83 of the Brazilian Bankruptcy Law. It may be initiated either voluntarily by the debtor, or involuntarily by creditors or the court.

Voluntary bankruptcy liquidation proceedings are rare in Brazil. The bankruptcy liquidation proceedings have generally been regarded as value destructive. Moreover, bankruptcy liquidation proceedings have been heavily associated with fraudulent schemes, so courts did not shy from piercing the corporate veil of the debtor company to hold officers, shareholders and other affiliated companies liable for the debts of the bankrupt company. Courts even used to have the power to drag other companies belonging to the same corporate group, as well as officers and shareholders, into the bankruptcy liquidation proceeding (*extensão dos efeitos da falência*). Such possibility was eliminated by the recent legal reform, which prohibits any kind of extension of the effects of the bankruptcy liquidation to other companies not included in the initial request. The legal reform also intends to make bankruptcy proceedings far more effective and expeditious.

As the legal reform is recent and its benefits are still to be confirmed by case law, companies (and corporate groups) almost never voluntarily file for bankruptcy liquidation. It is common that corporate groups litigate aggressively to avoid even a single affiliated company being declared bankrupt and prefer to pre-emptively file for a court-supervised reorganisation, even when there is no going concern. This pre-emptive use of the reorganisation proceeding means that bankruptcy liquidation proceedings are usually commenced only after a reorganisation proceeding is forcibly converted into a bankruptcy liquidation proceeding, as it is clear that the debtor company has no going-concern value and is unable to comply with the reorganisation plan. This has been the case, for example, in the case of large corporate group proceedings in Brazil such as Varig[5] (the largest Brazilian

[5] Dockets no. 0260447-16.2010.8.19.0001, filed on August 13th, 2010, before the 1st Business Court of Rio de Janeiro (Bankruptcy Liquidation). Dockets no. 0071323-87.2005.8.19.0001, filed on June 17th, 2005, before the 1st Business Court of Rio de Janeiro (Judicial Reorganisation).

airline), Vasp[6] and Avianca[7] (each of which are also large airlines) and the Mabe Group[8] (a home appliances manufacturer). In such cases, court-supervised reorganisation proceedings were converted into bankruptcy liquidations, following the failure or inability to comply with the reorganisation plan. Since the court-supervised reorganisation proceeding of such groups was already substantively consolidated, the bankruptcy liquidation proceeding that followed was also consolidated.

More recently, as mentioned, the legal reform introduced significant changes to the bankruptcy liquidation proceeding in order to make it more agile and efficient. As some of the most notable measures, the deadlines for both the sale of the assets of the estate and the application of the bankruptcy discharge were drastically reduced. Whether such measures will actually make the procedure more efficient or stimulate its use in any way is yet to be seen.

- **Expedited pre-packaged reorganisation proceedings**

  An expedited reorganisation basically involves a prior out-of-court negotiation of a pre-packaged reorganisation plan between the debtor and its creditors, who then file for court confirmation of the reorganisation plan. The expedited reorganisation proceeding may only be filed by the debtor (creditors cannot file for an expedited reorganisation of the debtor). By the time of the filing, debtors must submit to the court a pre-packaged plan already endorsed and signed by the adhering creditors for it to be binding on non-adhering creditors.

  Although the recent legal reform aimed at incentivising the use of this mechanism, expedited pre-packaged reorganisation proceedings are still rare in Brazil in comparison with court-supervised reorganisation or bankruptcy liquidation proceedings. Nonetheless, corporate groups that have filed for confirmation of their pre-packaged reorganisation plans have done so jointly. Although there are no specific tests for procedural or substantive consolidation of debtors in expedited reorganisation proceedings, the rules applicable to court-supervised reorganisations shall be applied.

1.1 Corporate group versus individual legal entity

1.1.1 The insolvency and restructuring systems that are in force

As explained above, the recent legal reform introduced express rules on procedural and substantive consolidation of corporate groups. Article 69-G of the Brazilian Bankruptcy Law allows any companies of the "same corporate group" to file for judicial reorganisation jointly. This means that there will be a single procedure, with a single bankruptcy trustee, and with the possibility of a single joint reorganisation plan for all the companies. However, unless the court allows substantive consolidation of the debtors, there will be an individual creditors' meeting for each entity, in which deliberations over debt restructuring and recovery measures will be taken separately. In this scenario, the bankruptcy liquidation of one company will not necessarily entail

[6] Dockets no. 0070715-88.2005.8.26.0100, filed on July 1st, 2005, before the 1st Bankruptcy Court of São Paulo.

[7] Dockets no. 112565881-2018.8.26.0100, filed on December 10th, 2018, before the 1st Bankruptcy Court of São Paulo.

[8] Dockets no. 0005814-34.2013.8.26.0229, filed on May 3rd, 2013, before the 2nd Bankruptcy Court of São Paulo.

the liquidation of the others. As such, the proceeding may be split into as many others as necessary to reflect that some entities may remain under reorganisation while others may be liquidated.

In addition to procedural consolidation, article 69-J of the Brazilian Bankruptcy Law also for the substantive consolidation of corporate groups which file for reorganisation jointly, as long as the following cumulative criteria are met:

(i) debtors shall belong to the same corporate group;

(ii) debtors shall have filed for joint judicial reorganisation under article 69-G;

(iii) there shall be commingling of assets or liabilities between the debtors, which cannot be undone without excessive expenditure of time or resources; and

(iv) at least two of the following conditions must be verified:

(a) there must be cross-guarantees between debtors;

(b) there must be a relationship of control or dependency between the debtors;

(c) there must be partial or total coincidence between the shareholders or quotaholders of the debtors; and

(d) the debtors must present themselves to the market as a single economic entity.

If the substantive consolidation is imposed by the court under article 69-J, all the assets and liabilities of all the debtors will be pooled together, with the extinction of any intercompany claims and guarantees, and, for the specific purposes of the judicial reorganisation, the debtors will be treated as if they were a single economic entity. All the debtors will be subject to a single joint reorganisation plan, and all quorums and decisions will be made by a single consolidated meeting of creditors which will include all the creditors of all the debtor companies. Any bankruptcy liquidation decree will necessarily be imposed over all the debtors, and the substantive consolidation will tend to remain in place during the bankruptcy liquidation proceeding that will follow.

Although the reform has included express rules on the matter, the absence of which had been felt since the edition of the Brazilian Bankruptcy Law in 2005, the new rules do not entirely eliminate the uncertainties that existed in the previous scenario, as "core" aspects of substantive consolidation remain to be decided by courts on a case-by-case basis. Thus, we do not believe that the new rules represent any significant improvement on the matter of substantive consolidation, which will remain being addressed by case law on similar grounds.

1.1.2 Definition of a corporate group

Chapter XXI (Articles 265 to 276) of Federal Law No 6.404/1976 (Brazilian Corporate Law) adopts the legal concept of a corporate group.

Article 265 of the Brazilian Corporate Law states:

> "The holding company and its subsidiaries may, in accordance with this Chapter, constitute corporate groups through a group convention under which they oblige themselves to combine resources or efforts to realize their corporate purpose, or take part in common projects."

Articles 266 to 276 regulate internal relationships among the companies that comprise such formal corporate groups.

Even though the Brazilian Corporate Law provides such a legal framework for corporate groups, with a detailed applicable regime, very few holding companies execute formal legal group conventions with their controlled subsidiaries in order to become "legal corporate groups". In fact, it is commonplace among commentators and courts that such a legal framework is not used.

Thus, most corporate groups are characterised by a holding company that holds controlling stakes in subsidiaries without entering into formal legal group conventions. Such groups are called "*de facto*" corporate groups as opposed to "legal" corporate groups regulated by the Brazilian Corporate Law.

1.1.3 Legislation relating to corporate groups

The concept of a "corporate group" is also adopted in other pieces of legislation. In this regard, article 2, §2 of the 1942 Brazilian Labor Code establishes that

> "[w]henever one or more companies, each one being a separate legal entity, is under the direction, control or administration of another company, constituting an industrial, commercial or other economic activity group, such company shall be jointly and severally liable for the purposes of labor debts, with the company which is the main debtor."

Also, Brazilian case law, applying article 124 of the Brazilian Tax Code, holds affiliated companies belonging to the same corporate group liable for tax debts.

In competition law, article 88 of Law No 12.529/2012 also establishes that certain concentrations involving "groups" with revenues that exceed certain thresholds should also be analysed by the Brazilian Antitrust Authority.

In environmental law, other companies of the same corporate group are held responsible for environmental damages whenever the violating company is not capable of compensating the damages caused to the environment.

Finally, in insolvency proceedings, a decision by the Superior Court of Justice has ruled that

> "a corporate group […] exists when the various legal entities carry out their activities as if they were, in managerial, labor and assets terms, a single entity, it being legitimate to pierce the corporate veil of the bankrupt company so that the effects of the bankruptcy decree affect other companies."

This definition has been used, for example, by the 1st Bankruptcy Court for the City of São Paulo to verify the existence of the corporate group.

1.2 Corporate group versus individual corporate benefit

1.2.1 The existence and relevance of "corporate group benefits"

Article 245 of the Brazilian Corporate Law states:

> "Officers and directors may not, to the detriment of the company, favor an affiliated, parent or subsidiary company, and must ensure that transactions between affiliated companies, if any, comply with strictly commutative conditions or with adequate consideration; and the officers and directors shall be held personally liable for losses and damages resulting from acts committed in violation of the provisions of this article."

Thus, article 245 of the Brazilian Corporate Law expressly denies any form of "corporate group benefit".

Brazilian law also does not expressly deal with the matter of upstream or downstream guarantees. There is no express permission, prohibition or limit to the personal guarantees that can be provided by subsidiaries or parent companies. However, although such guarantees are possible and theoretically unrestricted, they should be provided under reasonable conditions and with a clear picture of the consideration that will be given to the guarantor, under penalty of the directors / officers being held liable under article 245 of the Brazilian Corporate Law.

1.2.2 Director liability

This is outlined above.

1.2.3 "Early warning systems"

There are no "early warning systems" in place in Brazil between the directors of individual legal entities and the parent entity. In fact, there is no warning system at all in Brazil, nor is there any obligation to file for bankruptcy in the event of insolvency, as explained below.

1.2.4 Pending or draft legislation

There is no pending or draft legislation relating to these issues.

1.3 Universalism versus territorial principle

1.3.1 Application of the modified universalism rules

As part of the legal reform in 2020, Brazil adopted a modified version of the 1997 United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency (Model Law). As such, Chapter VI-A, comprising article 167-A to article 167-Y, was introduced to the Brazilian Bankruptcy Law, to specifically regulate cross-border insolvencies. Although there are a few deviations from the

UNCITRAL text, local courts are allowed to exercise broad discretion to cooperate and communicate directly with foreign authorities.

The new rules provide for a streamlined procedure aimed at recognition of foreign insolvency proceedings. The foreign representative has standing to file for recognition of the proceeding in which it was appointed. Upon filing of the recognition proceeding, the court has discretion to grant any urgent provisional relief it finds appropriate, including a stay of proceedings to protect the assets.

A foreign proceeding will be recognised as main if filed in the country where the debtor has its centre of main interests. The court will recognise the foreign insolvency proceeding as non-main if it was filed in a country where the debtor has an establishment or assets.

The recognition of a foreign main proceeding triggers certain mandatory effects: a stay of enforcement actions and of individual actions of creditors aimed at collecting debt; a suspension of the statute of limitations; and the ineffectiveness of transfers of non-current assets of the debtors. In addition, upon recognition of a foreign insolvency proceeding, either main or non-main, the court has broad discretion to order any relief it finds appropriate to the foreign representative. Any such discretionary relief is subject to modification or termination by the court at the request of the foreign representative or of any interested party, provided that the interests at stake are adequately protected.

According to the new rules, and following the Model Law, the Brazilian court can exercise broad discretion to cooperate in cross-border insolvency cases to the maximum extent possible. As such, courts can engage in direct communication with foreign authorities and foreign representatives, including to request information or assistance, without having to resort to letters rogatory or any other formality. The court may also approve cross-border agreements or protocols which facilitate coordination and administration of multiple insolvency proceedings.

The new provisions also allow coordination of concurrent insolvency proceedings regarding the same debtor. These rules apply whether there is a local and a foreign insolvency proceeding, or multiple foreign insolvencies, regarding the same debtor taking place concurrently. The general principle under these coordination rules is that a main proceeding shall have worldwide reach and universal effects, while non-main proceedings shall be usually restricted to local assets.

As a result, following the enactment of the Model Law, Brazil seems to have fully incorporated the modified universalism approach to cross-border insolvencies.

1.3.2 Bilateral and / or multilateral treaties in force

Brazil is a signatory to the 1928 Convention of Private International Law, a treaty signed in Havana and intended to provide common rules on conflict of laws between American countries. The Bustamante Code, attached to such convention, provides, among other matters, for rules on cross-border insolvencies applicable to the signatory states. The treaty, which was only ratified by 15 Latin American countries, has seldom been applied in Brazil, and many of its rules are considered to be obsolete.

1.3.3 Pending legislation

There is no pending legislation on these matters.

1.4 Competent court and applicable law

The court of the principal place of business of the debtor has jurisdiction to hear its bankruptcy liquidation, reorganisation proceedings and expedited pre-packaged reorganisation proceedings as applicable (pursuant to article 3 of the Brazilian Bankruptcy Law). For this purpose, the case law tends to interpret the "principal place of business" as the place from which the company is managed, directed, or where the decisions are taken, or, depending on the case, the place where the main operational activities of the company take place. Such determination, however, can be controversial in many instances.

The Brazilian Bankruptcy Law has no specific provisions regarding the principal place of business of a corporate group. In general, the courts have applied the same criteria mentioned above in the case of a joint filing of the corporate group members, i.e. the chosen court must determine whether the principal place of business (based on the criterion mentioned above) of the group is located within its jurisdiction so that the court can extend its jurisdiction to the companies from other locations. As a result, courts may end up having jurisdiction over companies headquartered in different locations, as long as the "principal place of business" of the group is located within that court's jurisdiction.

However, as will be further explained below, the fact that there is a joint filing does not necessarily mean that there will be substantive consolidation, and it does not necessarily mean that there will be only one reorganisation plan for all group members.

If a bankruptcy liquidation or a reorganisation proceeding has already been commenced for a subsidiary, the parent company can still file for bankruptcy, but it must be filed with the court where its principal place of business is located. As a result, different courts may have jurisdiction over the proceedings filed by the parent and the subsidiary.

If one or more of the entities is incorporated abroad, and the court understands that the principal place of business of the group is located in the venue where it sits, it may allow the commencement a proceeding regarding the whole group (thereby extending its jurisdiction to any such foreign entity).

1.4.1 Applicable law that falls outside of the lex fori concursus *and related issues*

Regarding applicable law, Decree No 4.657/1943 regulates conflict of laws in Brazil. It does not contain any provision on insolvency proceedings, but the situations in which foreign statutes are applicable in Brazil are very limited.

Following the 2020 reform, Brazilian Bankruptcy Law contains a specific chapter on cross-border insolvencies (as described above). In this regard, Brazilian courts would generally apply Brazilian legislation to insolvency proceedings commenced in Brazil (as the *lex fori concursus*).

1.4.2 Harmonisation of substantive restructuring and insolvency laws

There are no known attempts to harmonise substantive restructuring and insolvency laws with those of other countries.

1.4.3 Applicable treaties or case law

There has been at least one case in which a Brazilian court, in Rio de Janeiro, has granted provisional temporary relief in a proceeding aimed at recognition of a foreign insolvency proceeding. Apart from that, there are no further treaties or relevant case law other than what is discussed above.

1.4.4 Upcoming new legislation

There is no proposed new legislation in this area.

2. Substantive consolidated restructuring proceedings versus synthetic group restructurings

Brazil has no rules allowing for synthetic secondary proceedings, nor on providing for compliance under local proceedings, of distribution schemes and priorities provided for in other countries. However, it has become common in Brazil for groups of companies, including foreign entities, to file for a local reorganisation and to be substantively consolidated, resulting in the application of Brazilian rules for all such entities and their creditors.

As a matter of fact, as mentioned above, even before the legal reform introduced formal statutory provisions regarding substantive consolidation, substantive consolidated corporate group reorganisation proceedings were possible in Brazil, and many of the biggest court-supervised reorganisation proceedings in Brazil involved corporate groups in substantive consolidation.

For example, the Oi Group[9] case was one of the biggest court-supervised reorganisation proceedings in Brazil so far, in which seven companies of the same corporate group, including two foreign entities, aimed to restructure a consolidated debt of around USD $20 billion. The case was filed in June 2016, and a formal court decision authorising the substantive consolidation between the debtors was issued on 21 August 2017.

Another example is the PDG Group[10] case, a court-supervised reorganisation that involved 512 debtor companies with a reported indebtedness of BRL $6.2 billion. The case was filed on 23 February 2017, and the joint reorganisation plan, presented by the debtors, all substantively consolidated, was approved by the creditors in a deliberation in which they were all pooled together, and confirmed by the Bankruptcy Court in December 2017.

There are many other examples of consolidated corporate group proceedings, either in court-supervised reorganisation proceedings or expedited pre-packaged reorganisation proceedings.

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[9] Dockets no. 0203711-65.2016.8.19.0001, filed on June 20th, 2016, before the 7th Business Court of Rio de Janeiro.

[10] Dockets no. 1016422-34.2017.8.26.0100, filed on February 23rd, 2017, before the 1st Bankruptcy Court of São Paulo.

However, it is important to stress that, prior to the legal reform, the Brazilian Courts had not adopted a uniform stance on the matter of substantive consolidation, and the criteria for its application varied greatly from case to case. As noted above, the express provisions regarding substantive consolidation introduced by the recent legal reform may not contribute to a uniform approach on the matter.

For example, the 1st and the 2nd Bankruptcy Courts of São Paulo have often diverged on the matter, and the precedents of the Court of Appeals of the State of São Paulo have also gone in different directions. Previously, up until 2015, neither the Bankruptcy Courts of São Paulo nor the Court of Appeals of the State of São Paulo applied different tests to allow joint filing and substantive consolidation.

So, for instance, the academic research paper noted above[11] has concluded that, for the analysed court-supervised reorganisation proceedings in the study, a joint filing automatically entailed substantive consolidation, even if there was no decision authorising the consolidation of assets and liabilities of the debtor companies. Once the Bankruptcy Courts of São Paulo had admitted a joint filing for a corporate group, a substantive consolidation would follow automatically, and the corporate group would simply present a single consolidated reorganisation plan, and creditors would vote on it as if they were all creditors of a single entity. And, even when such "silent" substantive consolidation was challenged, the Court of Appeals of the State of São Paulo would treat a "joint filing" and a "substantive consolidation" similarly.

From 2015 onwards, both the Bankruptcy Courts and the Court of Appeals of the State of São Paulo started to tackle the issue of substantive consolidation in their decisions.

The 2nd Bankruptcy Court of São Paulo has expressly considered substantive consolidation whenever issuing a commencement order. In such decisions, the court expressly stated that a joint filing does not necessarily entail substantive consolidation, and that the appointed court trustee should first analyse the extent to which the assets and liabilities of the debtors are commingled and render an opinion on whether a substantive consolidation of the group would be appropriate. Such a proceeding has been adopted, for example, in the Viver Group[12] and Bmart Group[13] court-supervised reorganisation proceedings.

In the Viver Group case, the court trustee (KPMG) issued an expert opinion concluding that a partial substantive consolidation would be more appropriate, meaning that 40 debtor companies could present a single consolidated reorganisation plan, but 16 other debtors that were special purpose entities (SPEs) would have to present separate plans. In the Bmart Group, the court trustee considered that the assets and liabilities were so commingled across the entities within the corporate group that a substantive consolidation was inescapable.

The 1st Bankruptcy Court of São Paulo has taken a different stance, usually authorising joint filings and substantive consolidation without requiring a previous opinion by the court trustee. An example is the case of PDG Group, which filed for reorganisation on 23 February 2017. PDG is a publicly held company, and its court-supervised

[11] See above, n 4.
[12] Dockets no. 1103236-83.2016.8.26.0100, filed on September 16th, 2016, before the 2nd Bankruptcy Court of São Paulo.
[13] Dockets no. 1012521-92.2016.8.26.0100, filed on February 11th, 2016, before the 2nd Bankruptcy Court of São Paulo.

reorganisation involves 512 debtor companies and reported indebtedness of BRL $6.2 billion. In the commencement order, dated 2 March 2017, the judge authorised the joint filing and appointed PriceWaterhouseCoopers as court trustee but did not order it to issue an opinion on the substantive consolidation of the PDG Group.

Furthermore, the Bankruptcy Appellate Panels for the State of São Paulo have issued opinions tackling the issue of substantive consolidation. In this regard, the OAS Group[14] was a case in which substantive consolidation was litigated very aggressively.[15] In this case, the 2nd Panel for Business Matters of the Court of Appeals of São Paulo issued a split opinion, authorising the substantive consolidation. In another case, however, the same 2nd Panel has recently ruled that substantive consolidation was inadmissible for the Alcometalic Group[16] and ordered each debtor company to present its own individual reorganisation plan.

In addition, there has been a trend among Brazilian Courts in some cases to modulate the effects of substantive consolidation, or to delegate such decision to the creditors. This results in cases in which, although the procedural consolidation is fully in place, substantive consolidation among the debtor companies applies only in part.

This has been the case, for example, for the Renova Group[17] (a renewable energy corporate group) reorganisation proceeding, in which the 2nd Bankruptcy Court of São Paulo accepted the joint filing (procedural consolidation) for all companies of the group, but at the same time ruled that the substantive consolidation should be applied in two different blocks of companies, thus creating two different groups of

[14] Dockets no. 1030812-77.2015.8.26.0100, filed on March 31st, 2015, before the 1st Bankruptcy Court of São Paulo.

[15] The OAS Group was one of the largest construction conglomerates in Brazil, but it faced a severe financial downturn after its involvement in Brazil´s largest corruption scandal. The group filed a joint reorganisation proceeding on 31 March 2015, which involved 10 companies from the group, including two foreign subsidiaries. On 1 April 2015, the 1st Bankruptcy Court for the City of São Paulo authorised the commencement of a consolidated proceeding of the OAS Group and appointed Alvarez & Marsal as judicial administrator for all the companies. The initial order is only four pages long, but only one single paragraph deals with the joint filing: "the multiparty lawsuit is well justified, in so far as all companies act systemically and integrate the same corporate group. Consequently, the preservation of the social and economic benefits arising from the healthy business activity (which is the object of the present proceeding) will be better furthered if the economic crisis is dealt with in a global manner, considering all the companies that integrate the economic group, and not separately."
On the same date as the commencement order (1 April 2015), the Noteholders of the OAS Group (headed by Aurelius) and Bondholders filed separate motions, requesting that the reorganisation proceedings be split and that different reorganisation plans be presented by each debtor company of the OAS Group. On 6 April 2015, the judge denied such motions, and stated that the "global solution" was more appropriate for the OAS Case. After this, on 4 May 2015, the Noteholders and Bondholders appealed to the 2nd Bankruptcy Appellate Panel for São Paulo state and later, on 15 May 2015, HSBC and Deutsche Bank also filed appeals against the initial order. The four appeals requested the separation of the court-supervised reorganisation proceeding and that each debtor company present a separate reorganisation plan. The public attorney sided with the creditors and issued an opinion on 25 June 2015, reasoning that it was in fact inadmissible that assets of companies in very different financial conditions should be consolidated, and that a substantive consolidation should not be effected. On 5 October 2015, after much apprehension, the 2nd Bankruptcy Panel rejected the appeals in a split decision, ruling that the substantive consolidation was permissible for the OAS Group. The appeals were heard by a panel of three judges, two of whom (Carlos Garbi and Carlos Marcelo Mendes de Oliveira) voted in favour of consolidation, and one (Fabio Tabosa) against it.

[16] Dockets no. 1044764-26.2015.8.26.0100, filed on May 11th, 2015, before the 2nd Bankruptcy Court of São Paulo.

[17] Dockets no. 1103257-54.2019.8.26.0100, filed on October 19th, 2019, before the 2nd Bankruptcy Court of São Paulo.

consolidated debtors, with two different creditors' meetings and a different reorganisation plan for each group of consolidated companies – all in the same consolidated proceeding.

On that note, we can also highlight the Odebrecht Group[18] reorganisation proceeding, in which 21 debtor companies jointly filed for judicial reorganisation, but the Court of Appeals of the State of São Paulo ruled that, even if the procedural consolidation was valid, the decision concerning substantive consolidation should be taken by each individual creditors' meeting of each of the debtors. As a result, some of the companies were substantively consolidated and had a single reorganisation plan approved, while others (where the creditors voted against substantive consolidation) had their own individual reorganisation plans.

3. Duty to initiate insolvency process

The only provision in the Brazilian Bankruptcy Law that may be interpreted as establishing an obligation for officers / directors to file for bankruptcy is article 105 of the Brazilian Bankruptcy Law, which reads:

> "The debtor in an economic-financial crisis that considers that he does not meet the requirements to file for a court-supervised reorganisation, must file for bankruptcy, explaining the reasons for the impossibility of continuing business activity."

However, while the duty is established under article 105, there is no specific timeline regarding when such voluntary bankruptcy liquidation should be filed. There is also no specific consequence, either to the debtor company or to its officers / directors, if this voluntary bankruptcy liquidation is not filed.

Within this context, under the Brazilian Corporate Law, it is incumbent upon the general shareholders' meeting to allow the officers / directors to file for bankruptcy or a court-supervised reorganisation. Only in urgent cases, and with the express approval of the controlling shareholder, can the officers / directors file for bankruptcy or a court-supervised reorganisation with the subsequent and immediate call notice to a general shareholders' meeting to deliberate on the matter.

Other than that, officers / directors do have fiduciary duties provided for in the Brazilian Corporate Law and could be held liable if they fail to act in the best interests of the individual legal entity.

The existence of a guarantee from an IP in another country would not impact on the duty under article 105 or the fiduciary duties.

4. Legal certainty and predictability

There is no requirement regarding publicity and the lines of communications that must be installed with the local courts or the local creditors, nor is an IP required to provide any guarantee pending the restructuring or bankruptcy liquidation procedure.

[18] Dockets no. 1057756-77.2019.8.26.0100, filed on June 17th, 2019, before the 1st Bankruptcy Court of São Paulo.

5. Consolidation of assets

5.1 Procedure with respect to the sale of the whole or part of a business

The sale of the whole or part of a business, outside bankruptcy, must follow the procedure / requirements established in the Brazilian Civil Code. Under article 1.144, any contract that involves the sale of part of a business (*estabelecimento*) will only produce its effects with respect to third parties (*erga omnes*) after being registered in the Commercial Registry.

Moreover, pursuant to article 1.145, if the sale has rendered the seller insolvent, then the validity of the sale will depend upon payment, in full, of all creditors of the seller, while such creditors must consent to the sale within 30 days. The buyer also remains liable for all debts that have been duly recorded in the acquired business (article 1.146). The Brazilian Civil Code does not contemplate special quorums or voting requirements for creditors for the sale of all or part of a business outside insolvency, and the consent must be unanimous.

In a restructuring proceeding, the debtor company may sell fungible assets without the need for prior authorisation. However, the sale of non-fungible assets must be preceded by a court authorisation, having heard the creditors' committee (if existing), pursuant to article 66 of the Brazilian Bankruptcy Law. Opposing creditors holding more than 15% of the total claims may convene a creditors' meeting to deliberate on the sale, after posting a bond to guarantee the full price offered.

Also, the sale of all or part of a business, within a restructuring proceeding, may be made free and clear of any liens and liabilities.

In this regard, under article 60 of the Brazilian Bankruptcy Law, the debtor company may sell part of its business, free and clear of all past liabilities, if the sale is: (i) expressly authorised in the reorganisation plan or by the court; and (ii) conducted in compliance with any means provided by article 142 of the Brazilian Bankruptcy Law (including a judicial auction, a competitive process, or a direct sale).

Thus, in a court-supervised reorganisation proceeding, creditors have voting rights on the reorganisation plan, which may include the sale of part of the business of the debtor. In voting on the plan, creditors are divided into four classes: (i) labour-related claims; (ii) secured claims; (iii) unsecured claims; and (iv) claims held by small-sized companies. Creditors whose claims are not affected by the reorganisation plan do not have the right to vote.

The reorganisation plan is approved in one of the following two ways:

- regular creditor majorities: creditors in each class vote to approve the plan. In classes (ii) and (iii) above (i.e. secured and unsecured creditors) the plan must be cumulatively approved: (a) by more than 50% of the creditors, in number, present at the creditors' meeting; and (b) by creditors whose claims represent more than 50% of the total amount of claims of creditors present at the creditors' meeting. In classes (i) and (iv), the plan must be approved by more than 50% of the creditors, in number, present at the creditors' meeting (regardless of the amount of claims held by such creditors); or

- "cram down": the judge may also approve the restructuring plan should the following cumulative requisites be present: (a) creditors holding more than 50% of the claims present at the creditors' meeting (regardless of the class of claims they belong to) vote to approve the plan; (b) the plan is rejected by no more than one class of claims; (c) at least one-third of the creditors in the dissenting class vote to approve the plan; and (d) the plan does not entail unfair discrimination among the creditors belonging to the dissenting class.

Majorities are calculated based on the creditors that effectively attended the creditors' meeting to vote on the plan. Creditors not attending the meeting, and unimpaired creditors as mentioned above, are not considered for the purpose of approval of the plan.

Creditors holding a security interest over the asset must expressly authorise the sale.

In a liquidation proceeding, the sale of all assets of the bankrupt estate is conducted by the trustee appointed by the court following a competitive bid process. Neither shareholders nor creditors have a say in the sale of bankrupt estate assets.

There is a provision in article 145 of the Brazilian Bankruptcy Law which provides that the court may authorise an alternative sale process if previously approved by two-thirds of creditors present at the creditors' meeting.

5.2 Difference in treatment with respect to tangible and intangible assets

Differences in the context of a restructuring proceeding are set out above.

5.3 Role of creditors and creditors' committees in a substantive consolidation

Under Brazilian case law, creditors of the entities being consolidated in an insolvency proceeding do not have to approve substantive consolidation. Rather, as noted above, it is ordered by the court, provided that the legal requirements are met.

However, even though the Brazilian Bankruptcy Law does not contain such an express provision, it is not prohibited that, even in cases that do not meet the legal criteria for substantive consolidation to be imposed by the court, the debtors may propose the substantive consolidation, which will have to be voted on by each general meeting of creditors. As long as the substantive consolidation is approved in the individual creditors' meeting of each company to be consolidated, the substantive consolidation will be applied.

5.4 Voting for or against a substantive consolidation

These matters are addressed above.

6. Equitable distribution and accountability of IPs

In the case of a sale outside a bankruptcy context, if the proceeds of the restructuring or liquidation are insufficient to pay off creditors, the sale may be considered invalid, unless creditors had consented to the sale within 30 days (article 1.145 of the Brazilian Civil Code).

In the case of an extrajudicial winding up of a company, regulated by articles 1.102 to 1.112 of the Brazilian Civil Code (*Liquidação Extrajudicial*), the shareholders, as well as the administrators of a company, would be held jointly and severally liable if the wound up company does not have a regular situation before the tax, labour and social security authorities (i.e. the proceeds of the restructuring or liquidation are insufficient to pay such debts).

In a court-supervised restructuring scenario, the restructuring plan must provide for the *pari passu* payment of creditors in each class of claims subject to the proceeding, according to the provisions approved by the required majorities of creditors. In some circumstances, courts will allow strategic suppliers to receive favourable treatment, provided that such treatment is reasonable and compatible with the commitment of future supply. In this regard, the creditors' meeting may, for example, approve a payment with a haircut or an extension of the debt maturities. If the debtor company fails to comply with the provisions of the restructuring plan, the court-supervised proceeding is converted into a liquidation proceeding.

Finally, in a liquidation scenario, the debtor is discharged upon the full payment of all creditors, the payment of more than 25% of the unsecured claims following realisation of all assets, the termination of the proceeding, or the lapse of three years following the bankruptcy decree, whichever occurs first.

7. Intercompany claims

7.1 Order of priority

Intercompany claims are subordinated claims in a bankruptcy liquidation and have no voting rights in a court-supervised reorganisation proceeding.

It is also worth noting that all claims held by the shareholders (and other members of the corporate group), by officers and by directors are classified as subordinated claims under a bankruptcy liquidation proceeding. Subordinated claims are the most junior claims under a bankruptcy liquidation and are only paid after all other pre-filing unsecured claims have been paid in full; these claims only take precedence over any sums to be returned to the shareholders.

In addition, related parties (such as the members of a corporate group) are not entitled to vote at creditors' meetings.

However, following the legal reform, claims held by shareholders and related companies are considered unsecured (instead of subordinated) if they derive from an arms' length transaction and were contracted under strictly market conditions.

7.2 Concepts that can alter priority

The concepts of "recharacterisation" of intercompany debt as equity or "equitable subordination" are not contemplated under Brazilian Law or case law. However, it should be noted that intercompany debt (that does not derive from arms' length transactions) is subordinated to all other claims in a bankruptcy liquidation proceeding (and senior only to equity).

8. Administering a complex estate in one single consolidated procedure

More than one group can exist within an enterprise group for insolvency purposes, even though there is no statutory provision for such or any settled case law. So, for example, in the Renuka[19] case, an enterprise group was divided into two subgroups for purposes of voting on the reorganisation plan. In this case, the 2nd Bankruptcy Appellate Panel mandated separate voting for the two "groups" that constituted the Renuka Group, reasoning that the Renuka Group was formed in 2010, when an Indian company (Shree Renuka) acquired two independent corporate groups which were active in the sugar and ethanol business and which had maintained some form of autonomy.

However, even though each "group" within the Renuka Group presented separate reorganisation plans and two different creditors' meetings were held for each group, there was a single proceeding for the whole enterprise group before a single judge, and with one court trustee for the enterprise group.

9. Handling an insolvent parent with a healthy subsidiary

It would be possible for solvent subsidiaries to be consolidated within an insolvent group. One of the reasons for this is that, under Brazilian Law, there is no insolvency test for a reorganisation proceeding – the only legal requirement being that the corporate group is undergoing a financial or economic crisis (regardless of actual solvency). Courts usually accept claims of financial or economic distress made by debtors without applying any specific test. Consequently, corporate groups may file jointly and include solvent subsidiaries in their petition.

Although there is no legal provision on this, creditors, on the other hand, have challenged the inclusion of solvent subsidiaries in court-supervised reorganisation filings. So, for example, in the OAS Group case referred to above, the bondholders appealed against the initial order, requesting that the subsidiary that had issued the bonds (SPE Gestão e Exploração de Arenas Multiuso SA) be excluded from the reorganisation, since they were the only creditors and there were enough assets to the pay the bonds. However, the 2nd Bankruptcy Appellate Panel rejected this argument, and considered that a "global solution" was more suitable.

[19] Dockets no. 1099671-48.2015.8.26.0100, filed on September 29th, 2015, before the 1st Bankruptcy Court of São Paulo.

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