

Richard Turton Award 2020

**Necessary reforms: adaptation of
insolvency regimes in Latin
America due to the crisis**

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Necessary reforms: adaptation of insolvency regimes in Latin America due to the crisis

The economic crisis caused by the COVID-19 pandemic has brought as a consequence that governments around the world seek the best ways to help companies address difficulties generated by the fall in their incomes.

In this context of systemic crisis, insolvency regulation not only has to face the increase in the number of applications, but it also has to innovate and provide specific alternatives to the urgent refinancing needs of companies, such as modernizing its proceedings in accordance with the limitations imposed by governments to stop contagion.¹ In response to this challenging scenario, governments have implemented different legal measures and Latin America has not been oblivious to these changes.

COVID-19 impacted Latin America at a moment of macroeconomic, political and social vulnerability, and so the effects of the pandemic have been stronger for this region.² In addition, institutional weakness is a feature of many public institutions of the region that are in charge of the application and supervision of the measures for the crisis, a situation which is also reflected in the insolvency regulatory landscape.

This article seeks to identify the main changes in insolvency matters in Latin American countries and how these have tried to remedy the deficiencies that existed before the COVID-19.

1. Use of digital platforms

Processing procedures through virtual platforms is the swiftest innovation that all countries have been implemented to guarantee access to justice and at the same time prevent the spread of COVID-19.

Although in Latin America there had been many previous attempts to introduce electronic procedures, the use of paper was by far the rule.

As a relevant adaptation to the crisis, most Latin American countries nowadays provide the option to review and follow the status of insolvency proceedings through online

¹ The international doctrine has begun to work on what has been called “emergency insolvency law”. Rojo, D. (May 11, 2020). *Reflexiones sobre el Derecho concursal de emergencia*. Blog of the Faculty of Law of the Autonomous University of Madrid. There are some problems that are: a) the scope (how far legislation and how far not), b) the real balance between the interests affected and those potentially affected, and c) the problem of time (how long should the measures taken last).

² Among the 15 countries in the world with the highest number of confirmed cases, there are four Latin American countries: Brazil, Peru, Chile and Mexico, according to figures from the US John Hopkins University updated to June 17. The Economic Commission for Latin America and the Caribbean (CEPAL) estimates that this year the Latin American economy will decline by 9.1%, being the hardest hit countries would be Argentina, Brazil, Peru and Venezuela.

portals of their judiciaries, such as Brazil³, Colombia⁴, Ecuador, Chile, and Mexico. Despite the fact that not all countries in the region have access to electronic files, the creation of virtual channels for the submissions of applications and communication is now the general practice.

As an interesting case, it should be noted that Colombia has implemented recently online platforms, artificial intelligence and electronic forms created specifically to handle the large number of applications related to insolvency proceedings. It is expected that these tools will be used permanently.⁵

Regarding Creditors' Meetings, a key element of insolvency proceedings, these were suspended for the pandemic, particularly during the COVID-19 lockdowns. However, most Latin American jurisdictions now permit these meeting to be held through virtual platforms.

As for the Brazil case, there is no binding norm for the courts on this matter, but a series of recommendations were approved in connection with insolvency matters, including that virtual meetings shall be authorized when these are necessary to maintain the business activities of companies in reorganization or for the beginning of payment to the creditors.⁶ At this time, certain virtual meetings have been performed normally, but there has also been a case in which a virtual meeting was deemed unacceptable to creditors⁷.

Moreover, in Peru, virtual Creditors' Meetings and all the formalities for carrying them out within the framework of insolvency proceedings are regulated by a directive enacted by the relevant authority⁸. From the effective date of this rule, all Creditors' Meetings have been held under virtual platforms.

2. Celerity access to the insolvency proceedings

³ It is worth highlighting the experience in Brazil, where the digitization of the judicial process has been regulated since 2006 by Law No. 11 419. Brazil is one of the pioneers in the consolidation of the digital process, which has recognises the electronic process as a reality in all courts in this country.

⁴ In Colombia, insolvency proceedings can be initiated before a judge or before an administrative authority that exercises jurisdictional functions: the Superintendent of Companies. In this country, virtual procedures were already operating prior to the COVID-19 pandemic, mainly for procedures carried out by the Superintendent of Companies.

⁵ Article 3 of Legislative Decree No. 772 of June 3, 2020. Likewise, recently the Superintendent of Companies created a digital tool called Insolvency Module (MI), which incorporates the technological tools indicated by de Legislative Decree for insolvency proceedings (https://www.supersociedades.gov.co/delegatura_insolvencia/Material-multimedia-Modulo-insolvencia/Paginas/Modulo-de-Insolvencia-MI.aspx)

⁶ Article 3 of Recommendation No. 63 of March 31, 2020. Available at <https://atos.cnj.jus.br/atos/detalhar/3261>. The recommendations seek to guide and standardize the treatment of the matter nationwide to the Brazilian Courts.

⁷ In the case of Cultura (Process No. 1110406-38.2018.8.26.0100) the virtual meeting was rejected by the court on the ground that it would cause difficulties for labor creditors to attend or to be represented in the meeting.

⁸ Directive N° 001-2020-DIR-COD-INDECOPI of May 24, 2020. Available at <https://busquedas.elperuano.pe/normaslegales/aprueban-la-directiva-n-001-2020-dir-cod-indecopi-denomina-resolucion-n-000055-2020-preindecopi-1866601-1/>. In Perú the authority for insolvency matters is INDECOPI, an administrative agency entrusted to supervise the legality of the proceedings.

One of the specific problems in the countries of the region in insolvency matters is the delay to commence insolvency proceedings, as well as the effects of this situation in the debtor protection and in the approval of the reorganization plan, problems that are exacerbated for the COVID-19 context. In such regard, the following changes have been adopted:

2.1. Changes in the ordinary proceedings

In Colombia, one amendment incorporated into the general insolvency regime is the requirements for the admission into a reorganization proceeding⁹. As a consequence of this change, the judge will not seek to establish the content or accuracy of the documents or the financial information provided by the debtor. This responsibility has been assigned exclusively to the debtor and their accountant or fiscal auditor, as appropriate. The judge may also order on the admission resolution the extension or updating of the information provided. This measure is temporary and streamlines the stages of the application process that previously took several months.

2.2. Creation of fast-track insolvency process

On the other hand, the creation of special insolvency procedures has also been chosen as an exceptional and emergency solution for companies. These procedures are mainly characterized by their short terms, transitory nature and can only be submitted by those who have been affected by the emergency caused by COVID-19.

At the Latin American level, Colombia and Peru are the countries that have special insolvency procedures in force to date. In the Peruvian case we have the following:

- The "**Expedited Insolvency Refinancing Procedure**"¹⁰ (PARC, for its initials in Spanish) is intended for companies to enter into a refinancing agreement with their creditors at reduced access costs. It can only be initiated by debtors and the approval of the refinancing plan by the Creditors' Meeting generates its automatic application to all the creditors of the company, and in no case implies that the partners or shareholders lose the administration of the debtor. Furthermore, the disapproval of the refinancing plan only generates the culmination of the procedure.

In contrast to the ordinary regime where the approval of the refinancing plan can take between 1 to 2 years in the best of cases, in the PARC, once the request is admitted by the court, the creditors' meeting is held within 55 business days. It should be noted that the burden of the insolvency authority to recognize labor and consumer debts has been removed in order to alleviate the great burden that the review of these applications represents and to meet the deadlines.¹¹

⁹ Article 2 of Decree No. 560 of April 15, 2020 and Decree No. 772 of June 3, 2020.

¹⁰ Legislative Decree No. 1511 of May 11, 2020 and its regulations Supreme Decree No. 102-2020-PCM of June 7, 2020. Debtor companies may only request acceptance to this procedure until December 31, 2020.

¹¹ Article 8 of Legislative Decree No. 1511 of May 11, 2020. Also, labor creditors and creditors related to the debtor do not vote in Creditors' Meetings. In compensation, the decree provides that at least 40% of the

In Colombia two fast-track insolvency procedures were created:

- **"Emergency negotiation of reorganization agreements"**¹², in this process, parties can reach an agreement in three months instead of six. It starts with a notice of the debtor's intention to negotiate with his creditors and, based on this, the authority makes a formal review of the documentation submitted, admits the request and initiates the negotiation process. In this period, negotiations with groups of particularly vulnerable creditors are exceptionally allowed. The resulting agreement and the claims of dissidents are reviewed and in a single hearing the agreement is confirmed or not. Failure in negotiating the agreement does not produce the liquidation of the debtor, but rather the opportunity to process a reorganization under the ordinary regime.
- **"Business recovery procedure"**¹³, is a quasi-judicial procedure in which debtors can choose to file for this reorganization in Chambers of Commerce, where the mediator assumes the functions of the judge and has powers to verify the qualification and graduation of credits and determination of voting rights. The procedure lasts three months to enable the debtor and the creditors to reach an agreement to reorganize its liabilities. With the conclusion of the payment agreement presented by the debtor, it may be submitted to the insolvency judge for validation in order to extend the effects of the agreement and decide on the objections and comments of the creditors who voted negatively or declined to participate in mediation.

Besides that, the pandemic makes micro, small and medium enterprises (MSMEs) especially vulnerable, and the use of insolvency mechanisms can be particularly costly for these companies.¹⁴ In view of this, in Colombia other expedited procedures were also incorporated applicable only for companies whose assets are equal to or less than 5,000 monthly legal minimum wages in force:

- **"Abbreviated reorganization process"**¹⁵, from the beginning of this process, a date is set for a hearing that must be held within the next three months to reconcile objections to voting rights and the graduation of credits, and to present the agreement to the judge. Then there will be another hearing to resolve the unconciliated objections and confirm the agreement.

funds or moneys allocated annually for the payment of claims must be allocated to labor claims and 10% to consumer loans.

¹² Article 8 of Decree No. 560 of April 15, 2020.

¹³ Article 9 of Decree No. 560 of April 15, 2020.

¹⁴ For more detail about the impact of COVID-19 for MSMEs, including MSME insolvency, see: <http://pubdocs.worldbank.org/en/879461586478617078/COVID-19-Outbreak-Support-to-Firms.pdf>

¹⁵ Article 11 of Decree No. 772 of June 3, 2020.

- **"Simplified judicial liquidation proceedings"**¹⁶, the time within which creditors must submit their claims is reduced from 20 to 10 days, after which the liquidator has two months to sell the assets to third parties or to the creditors who may make offers. If not all the assets are sold, an adjudication project is submitted to the Judge for allocating them to the creditors.

3. Mechanisms to help debtors in insolvency proceedings

Certain interesting measures were included to help and protect debtors in insolvency proceedings. Especially in Colombia within the legislative package in insolvency matters¹⁷, some of these are the following:

- **Rescuing companies in imminent liquidation status**, in the event that the end of the reorganization process has been declared and the start of the liquidation process has been ordered, any creditor may prevent the liquidation by providing new funds that cover at least all payable credits, as long as the patrimony of the debtor is negative and the creditor deposits the total cost of the operation.
- **Flexibility in the payment of petty credits**, prior to this modification from the admission of the reorganization request, the debtor was prevented from carrying out any acts of disposal of its assets. As a result of this modification, the debtor will be able to pay small credits that do not exceed 5% of the total external liabilities, without the need for authorization from the Superintendence of Companies. This payment can only be effective with the proceeds obtained from the sale of non-operational assets.
- **Debt discharge**, it is allowed that the debtor may effectively ignore all the debt that exceeds the total value of the company as a going concern. For the release of debt to be available, shareholders' and sponsors' claims shall be cancelled without payment.
- **Tax benefits**, companies that are in reorganization processes can access exemption benefits on different taxes. Likewise, there is the possibility that the Colombian tax authority negotiates and cancels debts such as penalties, interests and even principal.¹⁸
- **Incentives for DIP financing**, the obligations resulting from new financing provided between the beginning of the reorganization process and the confirmation of the

¹⁶ Article 12 of Decree No. 772 of June 3, 2020.

¹⁷ Decree No. 560 of April 15, 2020, Decree No. 772 of June 3, 2020 and Decree No. 842 of June 13, 2020

¹⁸ In the opinion of various authors, this measure may not be effective since the regulation does not oblige the Colombian tax authority to apply these reductions, so it is expected that public officials do not use their discretionary powers. Pereira, A. (May 1, 2020). *Flattening the Filing Curve for SMEs: Lessons from Colombia's Insolvency Reform*. Blog of the Oxford Business Law. Available at: <https://www.law.ox.ac.uk/research-subject-groups/commercial-law-centre/blog/2020/05/flattening-filing-curve-smes-lessons>

reorganization agreement shall be preferred over creditors' claims in the restructuring process and the authorization from the judge will not be required.¹⁹

- **Extension of payment terms of reorganization agreements**, quotas of the reorganization agreements in execution corresponding to the months of April, May and June 2020 were not considered due until July 2020.
- **Breach of the reorganization agreement**, the reorganization agreement will not terminate if an event of default of the obligations of the agreement occurs unless the breach extends for more than three months and not be remedied by the hearing.

Regarding the obligations of the reorganization plans, the following recommendations have also been adopted in Brazil²⁰:

- **Impossibility of executing the debtor's assets**, the judge must evaluate with exceptional caution, granting measures of eviction due to lack of payment, and enforcement acts of equity nature in claims that demand the fulfilment of defaulted obligations during the state of emergency.
- **Modifications to the reorganization plan**, the judge must authorize the presentation of any modification of the reorganization plan, when the decrease in the capacity to fulfil obligations due to the COVID-19 pandemic is proven, and if the current plan was being complied with by March 20, 2020.

4. Closing remarks

Insolvency law oversees the study of insolvency situations and their mechanisms for overcoming those problems, therefore the solutions offered by this area of law become important alternatives during this situation.

To be an effective option, processes must be fast, flexible and costs reduced, allowing the refinancing of debtors' liabilities or their orderly exit from the market. However, in many countries, the regulation on insolvency matters had stalled, as is the case in many Latin American countries.

With the arrival of the crisis generated by COVID-19, insolvency regimes had to face new problems such as the increase in insolvency applications, urgent refinancing needs of companies and the limits of the provisions issued to stop the expansion of the virus.

¹⁹ In case it is not possible to obtain new financing, the debtor may request authorization to obtain it under the following conditions: (i) secure the credit with any available unsecured assets, (ii) secure new financing with assets that already have an encumbrance through a second-degree lien, (iii) secure the credits with assets that already have a first-class lien, displacing the original encumbrance to a second class type, as long as the debtor proves that the affected creditor will remain protected. The creditors may propose financing options that are less onerous for the debtor.

²⁰ Recommendation N° 63 of March 31, 2020.

Thus, the laws have had to adapt to these new times and some governments have taken the opportunity to implement extraordinary measures for corporate rescue and make their procedures more flexible. Brazil, Chile and Mexico are some of the countries that are already working on reform projects.

Some of these measures are here to stay and, in any case, the implementation of these new formulas will provide the necessary knowledge to establish whether these allow financially troubled debtors to solve temporary or systemic problems.