Global Restructuring and Insolvency Guide - Brazil

| Contents |
| --- |
| To generate table of contents, right-click here and select **Update Field.** |

Please select a topic from the menu.

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# Initial Considerations

## Can you take security over all types of assets, including accounts receivable?

**Extrajudicial reorganization proceeding**

Yes.

**Judicial reorganization proceeding**

Yes, as long as this is set forth in the plan approved by the creditors' meeting.

**Bankruptcy**

No.

## What is the nature of the insolvency process?

**Extrajudicial reorganization proceeding**

An extrajudicial reorganization proceeding is an out-of-court process (similar to a pre-pack) to restructure a viable company's debt to avoid a formal insolvency process and/or judicial reorganization proceeding. It is a contractual agreement between the debtor and creditors (or some of them) to reschedule/modify the obligations. Once the agreement is signed, the debtor is entitled — as long as some requirements are fulfilled — to request its ratification in court in order to extend it to all the same-class creditors subject to such process.

**Judicial reorganization proceeding**

A judicial reorganization proceeding is a court process that aims to restructure a company's debts.

**Bankruptcy**

Bankruptcy is a court process consisting of (i) a declaration of a state of insolvency; and (ii), as a consequence, dissolution of the debtor by selling its assets and splitting the proceeds between the credits in accordance with the payment list set forth in the law.

## What is the solvency requirement for a company to file a case in this jurisdiction?

**Extrajudicial reorganization proceeding**

The debtor must be in financial distress, which means potential insolvency.

**Judicial reorganization proceeding**

The debtor must be in financial distress, which means potential insolvency.

**Bankruptcy**

The debtor must currently or imminently be cash flow insolvent.

## Is there a requirement to demonstrate COMI ("centre of main interests") for a company to file a case in this country?

**Extrajudicial reorganization proceeding**

Yes. Broadly, only Brazilian companies (i.e., companies that are registered in Brazil) may be entitled to request an extrajudicial reorganization proceeding.

**Judicial reorganization proceeding**

Yes. Broadly, only Brazilian companies (i.e., companies that are registered in Brazil) may be entitled to request a judicial reorganization proceeding. Note, however, that there are decisions granting the judicial reorganization of foreign companies jointly with Brazilian companies (in those cases, the foreign companies were not operational and were related to the granting of foreign investments). Additionally, recent changes in the Brazilian Bankruptcy Law seem to allow the filing of judicial reorganization lawsuits by foreign companies in Brazil, as long as such companies have their center of main interests in Brazil. There are still no lawsuits filed in the Brazilian courts involving this situation.

**Bankruptcy**

Yes. Note, however, that in the event of a piercing of a corporate veil, Brazilian courts understand that it is possible to declare a foreign company bankrupt in Brazil. Additionally, recent changes in the Brazilian Bankruptcy Law seem to allow the possibility of a foreign company being declared bankrupt in Brazil if the company has its center of main interests in Brazil. No lawsuits have been filed in Brazilian courts involving this situation.

## Is restructuring of both secured and unsecured claims possible?

**Extrajudicial reorganization proceeding**

Yes.

**Judicial reorganization proceeding**

Yes.

**Bankruptcy**

Secured and unsecured creditors will be paid according to their ranking (the Brazilian Bankruptcy Law provides the payment order in Article 83) and value.

## Are the claims of creditors and shareholders put into separate classes for purposes of voting and treatment under the plan or scheme?

**Extrajudicial reorganization proceeding**

The Brazilian Bankruptcy Law does not provide for the classification of creditors in extrajudicial reorganization. Debtors and creditors are free to establish a contractual classification, but that would only apply to the creditor parties that are signatories. However, only secured and unsecured credits may be renegotiated through extrajudicial reorganization proceedings.

**Judicial reorganization proceeding**

Yes. Creditors subjected to judicial reorganizations are divided into four classes: labor, secured, unsecured and small companies. In general, shareholders' creditors will be classified as secured or unsecured. Tax creditors cannot settle through judicial reorganization proceedings.

**Bankruptcy**

Yes. Since the bankruptcy process aims to liquidate the company, the proceeds must be divided once the assets are sold. The Bankruptcy Law states the following payment order: (i) superpriority creditors (for example, bankruptcy estate costs and loans granted during the judicial reorganization proceeding); (ii) labor credits up to 150 minimum wages; (iii) secured creditors; (iv) tax creditors; (v) unsecured creditors (which include contractual penalties and fines, including tax penalties); and (vi) subordinated credit (e.g., shareholders' credits).

## Is shareholder approval needed to commence a case? Are shareholders entitled to vote on a plan?

**Extrajudicial reorganization proceeding**

Yes, shareholder approval is needed to commence the case, as set forth in the Brazilian Corporate Law. In this case, there is no voting process for creditors. Note, however, that shareholders' credit is not considered for the quorum (half of the total amount of the credits involved in the extrajudicial reorganization proceeding) necessary for the debtor to request the court ratification of the agreement and, as a consequence, the extension of its terms and conditions to the remaining creditors of the class.

**Judicial reorganization proceeding**

Yes, shareholder approval is needed to commence the case, as set forth in the Brazilian Corporate Law. However, the debtor's shareholders, as well as its affiliated or controlled companies, are not entitled to vote on the reorganization plan. If the debtor or its shareholders have higher than 10% equity participation in other companies, such companies are also not entitled to vote on the reorganization plan.

**Bankruptcy**

N/A

## Is there an ability to bind minority dissenting creditors (i.e., cramdown)?

**Extrajudicial reorganization proceeding**

Yes. The law provides that the debtor may file for court ratification of the agreement reached in order to extend its terms and conditions to all creditors of the classes encompassed in the agreement as long as it is accepted by creditors representing over half of all claims of the same corresponding class of creditor.

**Judicial reorganization proceeding**

Yes. The judicial reorganization plan (i.e., the document providing all of the terms and conditions of the restructured debts) must be submitted to the creditors' meeting for approval. In the creditors' meeting, creditors are divided into four different classes: (i) labor creditors, (ii) secured creditors, (iii) unsecured creditors and (iv) small companies. The plan has to be approved by the present creditors, representing more than half of the total amount of claims presented at the general meeting of creditors and by the simple majority of all creditors present. Creditors belonging to the labor class shall approve the judicial reorganization plan by a simple majority of all creditors present, independently of their credits. lf the creditors' meeting rejects the plan, the court shall declare the debtor bankrupt. If the reorganization plan is not approved by the creditors in the meeting, the court may grant the judicial reorganization to the debtor if the following conditions are met (cramdown power): (i) favorable vote of creditors representing more than half of the amount of all claims represented at the creditors' meeting, regardless of their classes; (ii) approval of two classes of creditors or, if there are only two classes of voting creditors, the approval of at least one of them; and (iii) favorable votes of more than one-third of the creditors in the class that rejected the plan. Broadly, the reorganization plan is filed by debtor. However, in some specific cases, creditors are entitled to replace the debtor and file an alternative reorganization plan.

**Bankruptcy**

N/A

# Commencing the Process

## Who can commence?

**Extrajudicial reorganization proceeding**

The debtor. Moreover, there are some requirements that the debtor must fulfill to request extrajudicial reorganization, as follows: (i) the applicant may not be a bankrupted individual/entity (unless the responsibilities arising from the bankruptcy sentence have already expired); (ii) the applicant shall not have entered into judicial reorganization during the previous five years; and (iii) the applicant, its controlling shareholders and its managers shall not have been convicted of any bankruptcy crime in the past.

**Judicial reorganization proceeding**

The debtor. Moreover, there are some requirements that the debtor must fulfill to request judicial reorganization: (i) the debtor must have been performing its activities for more than two years; and (ii) the debtor must comply with the following requirements: (1) the applicant may not be a bankrupted individual/entity (unless the responsibilities arising from the bankruptcy sentence have already expired); (2) the applicant shall not have entered into judicial reorganization during the previous five years; and (3) the applicant, its controlling shareholders and its managers shall not have been convicted of any bankruptcy crime in the past.

**Bankruptcy**

Any creditor, debtor, spouse, any heir of the debtor, administrator of a will and debtor's shareholder. Only debts over 40 minimum wages justify the request of bankruptcy for one of the debtor's creditors. Moreover, the debt must be represented by a liquid obligation under a protested execution instrument or instruments.

## Is shareholder's consent required to commence proceeding?

**Extrajudicial reorganization proceeding**

Yes (please see the responses in the Initial considerations section above).

**Judicial reorganization proceeding**

Yes (please see the responses in the Initial considerations section above).

**Bankruptcy**

This depends on who filed for bankruptcy (please see the answer to "Who can commence?" above).

## Is there an ability to consolidate group estates?

**Extrajudicial reorganization proceeding**

The law does not state such a possibility, but it is a common practice.

**Judicial reorganization proceeding**

Debtors that are part of a group under common corporate control may file a single judicial reorganization lawsuit. As a general rule, debtors must file independent plans to present creditors with new terms and conditions to fulfill the obligations. Exceptionally, the judge may authorize the filing of a single plan, as long as at least two of the following requirements are met: (i) similarity of shareholders/managers among the debtors; (ii) existence of a control/dependence relation among the debtors; (iii) existence of cross-guarantees offered by the debtors; and (iv) joint action of the debtors in the business market.

**Bankruptcy**

No, except in the case of piercing of the corporate veil whereby a shareholder is included in the process (in this case, the shareholder will be liable for the debts of the bankrupt estate, but this shareholder will not be considered bankrupted). A court may pierce a corporate veil and hold shareholders personally liable for the obligations of a company in the case of abuse of the corporate veil, characterized by a deviation from the lawful purposes of a company or comingling of assets of a company and its shareholders.

## Is there any court involvement?

**Extrajudicial reorganization proceeding**

There could be if the debtor requests the ratification of the agreement to bind it to all the creditors in the same situation as those who signed it (i.e., in the same class).

**Judicial reorganization proceeding**

Yes

**Bankruptcy**

Yes

## Who manages the debtor?

**Extrajudicial reorganization proceeding**

The debtor retains its powers to appoint management.

**Judicial reorganization proceeding**

The debtor retains its powers to appoint management. However, management can be removed if the managers of the company, for example: (i) acted with malice, simulation or fraud against the interests of their creditors; (ii) have been convicted of a crime committed under previous judicial reorganization/bankruptcy or a crime involving property, public welfare or economic policy provided for by applicable law.

**Bankruptcy**

The court appoints a trustee that will be in charge of the liquidation.

## What is level of disclosure of process to voting creditors?

**Extrajudicial reorganization proceeding**

A plan is presented and discussed between creditors and the debtor.

**Judicial reorganization proceeding**

Prior to the approval of the plan, it is attached to the dockets and discussed by creditors in the general creditors' meeting.

**Bankruptcy**

N/A. Creditors will not vote in this procedure. The judicial administrator will seize all of the assets and sell them, and the proceeds will be split between creditors according to the payment order.

## What entities are excluded from customary insolvency or reorganisation proceedings, and what legislation applies to them?

**Extrajudicial reorganization proceeding**

A public company and joint stock company; public or private financial institution, credit union, trust, complementary pension entity, operator company of the health insurance company, insurance company, capitalization society and other legal equivalent to the above entities. The legislation that applies to financial companies is Brazilian Law 6024/1974.

**Judicial reorganization proceeding**

A public company and joint stock company; public or private financial institution, credit union, trust, complementary pension entity, operator company of the health insurance company, insurance company, capitalization society and other legal equivalents to the above entities. The legislation that applies to financial companies is Brazilian Law 6024/1974.

**Bankruptcy**

Public company and joint stock company; public or private financial institution, credit union, trust, complementary pension entity, operator company of the health insurance company, insurance company, capitalization society and other legal equivalents to the above entities. The legislation that applies to financial companies is Brazilian Law 6024/1974.

## How long does it generally take for a creditor to commence the procedure?

**Extrajudicial reorganization proceeding**

N/A, since it is a proceeding available to debtors.

**Judicial reorganization proceeding**

N/A, since it is a proceeding available to debtors.

**Bankruptcy**

A creditor can apply for the opening of insolvency proceedings. Between the application from the creditor and the initiation of the insolvency proceedings by the court, it used to take one week (in such period, the court will analyze if the legal requirements have been fulfilled).

# Effect of Process

## Does debtor remain in possession with continuation of incumbent management control?

**Extrajudicial reorganization proceeding**

Yes

**Judicial reorganization proceeding**

Yes. Debtor management retains its powers, which are exercised under the supervision of the court and the court-appointed judicial administrator. In some circumstances, the management is replaced (please see the answer above to the question related to the management of the debtor).

**Bankruptcy**

No

## What is the stay/moratorium regime (if any)? Is the stay or moratorium worldwide?

**Extrajudicial reorganization proceeding**

N/A

**Judicial reorganization proceeding**

The stay period is 180 days, but the judge can extend this period once, for an equal period of time.

**Bankruptcy**

N/A

## Is there a provision for debtor in possession or rescuer financing or superpriority or priming financing?

**Extrajudicial reorganization proceeding**

No

**Judicial reorganization proceeding**

Yes, the Brazilian Bankruptcy Law was recently amended not only to authorize a debtor-in-possession transaction with the debtor to finance its activities and the expenses of restructuring or preserving business activity value but also to recognize its superpriority in case of bankruptcy. However, all the obligations incurred by the debtor after the filing of the judicial reorganization lawsuit have superpriority over the credits that are subject to the judicial reorganization proceeding in case the debtor is declared bankrupt.

**Bankruptcy**

No

## Can procedure be used to implement a debt-to-equity swap?

**Extrajudicial reorganization proceeding**

Yes

**Judicial reorganization proceeding**

Yes

**Bankruptcy**

N/A

## Are third party releases available?

**Extrajudicial reorganization proceeding**

Yes

**Judicial reorganization proceeding**

Yes

**Bankruptcy**

Yes. However, the release has to be authorized by the court.

## Are the proceedings recognised abroad?

**Extrajudicial reorganization proceeding**

Yes, Brazil recently changed its Bankruptcy Law to adopt the UNCITRAL Model Law on Transnational Insolvency, including recognizing foreign insolvency proceedings in Brazil and cooperating with foreign authorities.

**Judicial reorganization proceeding**

Yes, Brazil recently changed its Bankruptcy Law to adopt the UNCITRAL Model Law on Transnational Insolvency, including recognizing foreign insolvency proceedings in Brazil and cooperating with foreign authorities.

**Bankruptcy**

Yes, Brazil recently changed its Bankruptcy Law to adopt the UNCITRAL Model Law on Transnational Insolvency, including recognizing foreign insolvency proceedings in Brazil and cooperating with foreign authorities.

## Has the UNCITRAL Model Law been adopted?

**Extrajudicial reorganization proceeding**

Please see the above response to the question "Are the proceedings recognized abroad?"

**Judicial reorganization proceeding**

Please see the above response to the question "Are the proceedings recognized abroad?".

**Bankruptcy**

Please see the above response to the question "Are the proceedings recognized abroad?".

## Can a debtor continue to carry on business during insolvency proceedings?

**Extrajudicial reorganization proceeding**

Yes

**Judicial reorganization proceeding**

Yes

**Bankruptcy**

No. However, bilateral agreements executed between a third party and the debtor are not automatically terminated by the bankruptcy and may be complied with by the trustee if it reduces or avoids damages to the insolvent entity.

# Other Factors

## Are there any wrongful or insolvent trading restrictions and what is the directors' liability?

**Extrajudicial reorganization proceeding**

A company is not obligated to file for an extrajudicial reorganization proceeding.

**Judicial reorganization proceeding**

In relation to corporations, there are decisions stating that the directors have the fiduciary duty to file for judicial reorganization. The directors may be required to pay indemnification to the company.

**Bankruptcy**

In relation to corporations, there are decisions stating that the directors have the fiduciary duty to file for bankruptcy. The directors may be required to pay indemnification to the bankruptcy estate.

## What is the order of priority of claims?

**Extrajudicial reorganization proceeding**

N/A.

**Judicial reorganization proceeding**

There is no order of priority of the claims during a judicial reorganization proceeding. Note, however, that the labor creditors must be paid within one year after the approval of the plan (this period of time can be extended to two years if: (i) the labor creditors approve such provision in the reorganization plan; (ii) the debtor posts a bond; and (iii) the labor credits have to be paid without any discount).

**Bankruptcy**

The following order will apply: (i) superpriority creditors (for example, bankruptcy estate costs and loans granted during the judicial reorganization proceeding); (ii) labor credits (limited to 150 minimum wages for each employee) and occupational accident claims; (iii) secured credits; (iv) tax claims; (v) unsecured credits (which include contractual penalties and fines, including tax penalties); and (vi) subordinated credit (e.g., the credits of the partners of the company and the managers of the company who do not have an employment relationship with the debtor).

## Do pension liabilities have any priority over other unsecured claims?

**Extrajudicial reorganization proceeding**

Pension liabilities can be considered to be labor and, as a consequence, be subjected to the same rules.

**Judicial reorganization proceeding**

Pension liabilities can be considered to be labor and, as a consequence, be subjected to the same rules.

**Bankruptcy**

Pension liabilities can be considered to be labor and, as a consequence, be subjected to the same rules.

## Is it possible to challenge prior transactions?

**Extrajudicial reorganization proceeding**

N/A

**Judicial reorganization proceeding**

Yes

**Bankruptcy**

Yes

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