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Research Project on Insolvency and Company Law

Report – Brazil

University of São Paulo Law School

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I. Introductory questions on the insolvency procedures available in the relevant jurisdiction.

1. What insolvency procedures – either liquidation or reorganization procedures – are available for distressed or insolvent companies?

A: The Brazilian Bankruptcy and Restructuring Act (Law no. 11,101/2005) ("BBRA") provides for three procedures for distressed or insolvent companies: judicial reorganization ("recuperação judicial"), extrajudicial reorganization ("recuperação extrajudicial") and liquidation ("falência"). These procedures are applied either to business companies or individual business people. While liquidation should take place when the business is no longer viable, reorganization mechanisms were designed for viable debtors that prove to be capable to overcome their economic and financial crisis.

There are two types of judicial reorganization: the so-called ordinary judicial reorganization, which represents the vast majority of cases and shall be the focus of the answers herein, and a special (but not exclusive) procedure for small businesses with more rigid rules in terms of means of reorganization. The latter consists of a special plan including labor claims, secured claims, and unsecured claims. Fiscal claims, fiduciary claims, and claims derived from forward foreign currency agreements, as well as claims arising from transfer of official funds cannot be included. The plan shall provide for payments of up to 36 equal monthly installments, with interest equivalent to the “SELIC” rate1.

BBRA also provides for two extrajudicial procedures: one binding only creditors who have signed the reorganization plan and another that binds all creditors included in the plan, since it has been approved by 3/5 of creditors of each sort included therein. In both cases, labor, fiscal, fiduciary claims, and claims derived from forward foreign currency agreements cannot be included.

2. Are there special insolvency procedures available for financial institutions or for other special classes of companies?

A: Law no. 6,024/1974 regulates two special insolvency procedures for private or non-federal public financial institutions and credit unions: intervention by the Central Bank of Brazil and extrajudicial liquidation. Normal liquidation under BBRA may also be requested in some situations.

Decree-law no. 2,321/1987 also provides for the so-called Temporary Special Administration Regime ("Regime de Administração Especial Temporária" –

1 The “Selic” rate is defined as the average adjusted rate of daily financing in the Special Settlement and Custody System for federal bonds.
RAET), which is applicable when the Central Bank of Brazil considers that a private or non-federal public financial institution in crisis can return to its normal operating status.

Special procedures also exist for purchasing pools (Law no. 5,768/1971 establishes that intervention by the Central Bank of Brazil and extrajudicial liquidation are applicable), supplementary pension entities (Complementary Law no. 109/2001, sections 44 to 53); health insurance companies (Law no. 9,656/1998, section 23), normal insurance companies and capitalization companies (Decree-law no. 73/1966, section 26 combined with sections 94 to 107), cooperatives (Law no. 5,764/1971, section 75), and electricity companies, while their public utility contracts are in force (Law no. 12,767/2012, sections 5 to 15 and 18).

3. Are there any specific legal provisions that apply to debt restructurings achieved without a full formal insolvency process?

A: Debt restructurings are fully regulated by private law and no specific legal provisions apply to them. Instead, BBRA expressly grants their legality in section 167, which means that the debtor and creditors are not obliged to follow an extrajudicial procedure as regulated by BBRA.

However, under one of the two types of extrajudicial reorganization existing in Brazilian law, it is possible for the debtor to request from the judge the confirmation of an out-of-court reorganization plan which binds only creditors that have expressly adhered to it. This alternative aims to prevent possible avoidances of the provisions set forth in the plan.

4. What are the commencement criteria for insolvency procedures?

A:

a) The reorganization procedures may commence only by the debtor’s application, and the criteria are provided for in section 48 of BBRA:

- The debtor has performed its regular business activities for at least two years prior to the application.

- The debtor has not previously been declared bankrupt or, if it has, the debtor has had all its obligations and liabilities declared extinguished by the court.

- The debtor must not have had a reorganization plan confirmed by the court in the past five years in both ordinary judicial reorganizations and in special procedures for small businesses.
- The debtor, any of its managers or controlling shareholders has not been found guilty of any bankruptcy crime under BBRA.

Additionally:

- The debtor must submit all documents required by section 51 of BBRA, including an explanation about the causes of the economic/financial distress; financial statements of the past three fiscal years; bank statements; a certificate issued by the protest officer; a certificate of Public Registry of Enterprises; the charter and minutes of the general meeting electing the managers; lists of creditors, judicial procedures, employees, and personal assets of controlling shareholders/partners and managers of the debtor.

- The company must also be economically viable. This viability shall be analyzed by the judge in a generic manner. Also, a disagreement exists on whether the judge or the creditors’ general meeting is the entity responsible for analyzing this viability.

b) A liquidation procedure may be requested by distressed debtors that do not meet the conditions to benefit from judicial reorganization. In addition, any creditor may request the forced liquidation of a debtor in the following circumstances:

- Failure by the debtor to comply with payment obligations in excess of 40 times the prevailing minimum wage, provided that a protest with a public registry has been lodged with respect to the corresponding indebtedness instrument.

- The existence of execution proceedings against the debtor where no assets have been attached or no money has been deposited to secure payment of the relevant obligations;

- The debtor has engaged in certain actions such as unjustified sales of assets or fraudulent schemes against the interests of creditors.

c) A judicial reorganization procedure may also be converted into liquidation in the following circumstances:

- The plan is rejected by the creditors

- The plan is not presented by the debtor during the sixty days after the commencement of the procedure;

- Failure by the debtor to comply with any obligation under the plan. According to section 61 of BBRA, the debtor will remain under judicial organization until all obligations provided for in the plan are fulfilled within a period of 2 years. If during this period the company fails to comply with any obligation under the plan, the judicial reorganization procedure shall be
converted into a liquidation procedure. After this 2-year period, should a breach of any obligation be set forth in the plan, any creditor may request the conversion into a liquidation procedure, as per article 62 of BBRA. Case law, however, has mitigated these previsions by allowing amendments to the plan.

5. Who can propose a restructuring plan? (e.g. corporate bodies, insolvency representatives, creditors)

A: Only the debtor through its officers can propose a restructuring plan, either under a judicial reorganization or an extrajudicial reorganization. However, the creditors may propose modifications to the plan, which must be approved by the debtor.

BBRA does not provide the possibility of creditors presenting an alternative reorganization plan, but this practice is relatively common in judicial reorganizations and has been endorsed by a number of courts, since the plan, in this case, is approved by all classes of creditors and by the debtor.

6. Please describe whether and to what extent shareholders’ rights can be affected by a situation of distress/insolvency of a company before and/or irrespective of the opening of a formal insolvency proceeding (e.g., are there any fiduciary duties of the shareholders to approve corrective measures/plans proposed by the board?)

A: No specific provisions exist concerning shareholders’ rights before and/or irrespective of the opening of a formal insolvency proceeding of a distressed/insolvent company.

II. Shareholders’ Rights in Companies Subject to Insolvency Proceedings

7. Are shareholders notified of the initiation of an insolvency process? If notification is individualized, what are the mechanisms used to identify shareholders?

A: Shareholders are not personally notified of the initiation of an insolvency process, neither in publicly nor in closely-held companies.

For publicly-held companies, Instruction no. 480/2009 of the Brazilian Securities Commission (“Comissão de Valores Mobiliários” – CVM) states that the company must send the following to CVM, through the electronic system available on CVM’s website:
- The initial petition of a judicial reorganization on the same day it has been filed with the court, together with all accompanying documents.

- Any application for confirmation of an extrajudicial reorganization plan, together with the accompanying accounting statements prepared to support the petition.

Likewise, the publicly-held company must send any application for liquidation to CVM, also through the aforementioned electronic system, provided it is based on a significant amount on the same day the company becomes aware of the application. The subsequent decision must also be communicated on the same day the company becomes aware.

Notwithstanding the provisions mentioned above, the application for any insolvency proceeding involving a publicly-held company, as well as any judicial suit that can affect its financial and economic situation, would be considered a material fact, as per CVM Instruction no. 358/2002 and, therefore, should be communicated to the market simultaneously to its reporting through any means of communication. The material fact should be reported by at least one of the following communication channels: (i) newspapers with a significant circulation, normally used by the company, and (ii) at least one news website that makes the information fully available through free access. The material fact must also be communicated to CVM, via internet, and to all stock exchanges or OTC markets in which the securities of the company are negotiated.

For closely-held companies, no similar provisions exist, and shareholders only become officially aware of the commencement of any insolvency process during the shareholders general meeting or when it is reported in the Court Gazette.

8. Are shareholders required to file claims in the insolvency proceeding? What are the consequences of not filing a claim?

A: As a rule, shareholders are not entitled to file any claim. The fact of being a shareholder does not grant any person the right to participate in an insolvency proceeding, because this is a prerogative of creditors. However, when a shareholder has a claim against the company that does not derive directly from the fact that he has an equity share in the company (e.g., tort claims), he may file his claim, but he shall not have voting rights under a conservative point of view (see answer to question 25 below). Should he not file his claim and when it is not included in the list of creditors, a shareholder may file it under an ordinary procedure.
9. Can shareholders continue to trade and transfer shares after the initiation of an insolvency proceeding affecting the company?

A: Normally, the initiation of an insolvency proceeding does not affect the trade of shares. However, in the case of publicly-held companies, the operating regulations of BM&FBovespa (the main Brazilian stock exchange) provides that trades of securities shall be suspended when the company files for judicial or extrajudicial reorganization, or when the stock exchange becomes aware that the company is under a liquidation proceeding. After this, the stock exchange shall seek clarification regarding the facts that led to the suspension. The suspension lasts for a maximum of 30 days, and may be extended at the stock exchange’s discretion.

10. Do shareholders have the right to request that a shareholders’ meeting is held, even if the company is insolvent? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: As a rule, the right to request a shareholders’ meeting is not affected when a reorganization procedure is in course. In the case of a liquidation procedure, the company is dissolved and, therefore, no shareholders’ meetings can be summoned.

According to article 64 of BBRA, when a reorganization procedure is in course, the debtor or its directors will continue conducting the business (“debtor-in-possession”). Therefore, in this situation, the shareholders have the right to request that a shareholders’ meeting be held.

11. Do shareholders have the right to request information in an insolvent company? Do they have information rights as to the progress of a reorganization procedure? Can they exercise that right vis-à-vis the directors of the company -if they remain in charge of the company-or vis-à-vis the insolvency representative?

A: Shareholders do not have a specific right to request information to the insolvent company. CVM Instruction 480/2009 grants that the main decisions and documents related to the insolvency procedure shall be promptly sent to CVM and shall be available to the market. Shareholders have, according to section 109 of the Brazilian Company Law, a general right to monitor the management of the business through the mechanisms provided for in the law (e.g., convening a fiscal counsel). No specific provision exists concerning the monitoring of insolvency representative activities by the shareholders.

A shareholder as an interested third party has the legitimacy to request information to the judicial administrator and to file an appeal. This matter was already decided by the Superior Court of Justice (Superior Tribunal de Justiça - “STJ”), in “Agravo Regimental” n° 216,589/SP. This legitimacy is justified for

2 “Agravo regimental” is a special appeal according to specific court regulations.
example due to a possible shareholder’s interest in the result of the sale of the insolvent company’s assets.

12. Can shareholders make proposals for nomination of directors, if the directors continue managing the company?

A: Yes. However, the law is not clear if this proposal can be made when new directors are appointed in the reorganization plan approved by the creditors, according to article 50, IV and V of BBRA.

13. If special categories of shares exist whose holders are granted additional governance rights, are these additional rights affected by the opening of an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: In Brazil, it is possible for a company to issue common shares or preferred shares. Companies listed in “Novo Mercado” (a special listing segment of corporate governance of BM&FBovespa) only issue common shares and provide strengthened governance rights to their shareholders. However, no specific provisions exist concerning the treatment of such rights during an insolvency procedure. It is possible to state that they are kept in full force and effect, but we must recognize that some measures approved in the reorganization plan can conflict with governance rights of shareholders (e.g., issuance of new shares through conversion of debt into equity without pre-emptive rights to existing shareholders; transference of control without tag-along rights). In these cases, it is reasonable to conclude that the court would confirm the plan and remove governance rights to ensure that the company shall be reorganized.

This conclusion is due to the broadly application of the so-called “principle of preservation of the company” by the court. Therefore, in the absence of a clear and specific regulation, and in order to preserve the distressed business that has shown signals of viability, shareholders’ governance rights can be removed.

Under a liquidation procedure, the governance rights do not exist anymore, since the company is dissolved, and the debtor is removed from the business direction (section 75 of BBRA).

14. Can shareholders challenge the decisions of the shareholders meeting, if it is still active? Do they retain the possibility of taking action against the acts of the directors? And against the acts of an insolvency representative? Is any authorization by a judicial or administrative body required to do so or, more generally, to exercise corporate rights? (If there are separate reorganization and liquidation procedures, does this affect the response?)
A: The decisions taken in a shareholders meeting can be challenged by shareholders if they were taken with a formal defect or in certain circumstances, such as abuse of voting rights by the controlling shareholder, conflict of interest, and so on.

Shareholders may also take action against the acts of the directors when they act maliciously, culpably or in dissonance with the law and the bylaws of the company (section 158, the Brazilian Company Law - Law no. 6,404/1976). First, the company itself is entitled to sue the directors, according to a decision taken in a shareholders meeting. If the action is not taken three months after the decision, any shareholder is entitled to do so. On the other hand, when the shareholders meeting does not approve this item of the agenda, then shareholders representing 5% of the corporate capital can sue the directors. Again, if the company is under a liquidation procedure, these rights do not exist, since the business, when still running, is conducted by the insolvency representative (in Brazil, he is called “judicial administrator” – “administrador judicial”).

The judicial administrator is appointed by the judge upon the commencement of a formal insolvency procedure. In a judicial reorganization, his role is basically to supervise the debtor in the management of its business, while in a liquidation process his main role is to collect and sell the debtor’s assets in order to pay the creditors. In turn, the judicial administrator is supervised by the judge and, if such is the case, by the creditors committee, when existent. The law does not provide any possibility for shareholders to take actions against the judicial administrator, but it is possible for them, as interested parties, whether individually or as a group, to communicate the court about any failure of the judicial administrator to comply with his duties. Finally, according to article 32 of BBRA, the judicial administrator is liable for the losses caused to the estate, to the debtor or to the creditors arising from malice or negligence.

15. Do shareholders have the right to call a special investigation of the affairs of the insolvent company?

A: BBRA does not contain any specific provision in this sense. This investigation could be conducted, in theory, by the fiscal counsel (“Conselho Fiscal”), or by the Board of Directors (“Conselho de Administração”), in the exercise of its role of supervising the officers and the company’s affairs.

16. Does the law provide for the establishment of a shareholders’ committee (or several committees, in case of different share classes)? What are their powers? Who bears the related costs?
A: The law does not provide any shareholders’ committee during an insolvency procedure in Brazil. BBRA provides the creation of a creditors’ committee, which is an optional body that may be constituted during the creditors’ general meeting in order to oversee the judicial reorganization process. It is a consulting body entitled to supervise the judicial administration activities and make recommendations about the administration of the assets. It is composed by one member of each class of creditors (labor-claim creditors, secured creditors, unsecured creditors, and creditors classified as micro and small businesses), all of whom are not remunerated. However, costs related to the fulfillment of legal duties of the committee may be reimbursed by the debtor, if duly supported, after the court’s approval. Convening a creditors’ committee is rare in Brazilian insolvency procedures.

17. Can shareholders voluntarily transfer shares of the company undergoing insolvency proceedings against any provisions in the articles/bylaws restricting transfers of shares?

A: If the articles of association, the bylaws or the stock exchange regulation provides that no shares can be transferred (e.g., the six-month lock-up restriction after a company’s public offering, for the controlling shareholder of a company listed in Novo Mercado) then the shares cannot be transferred. Specific provisions in this sense for companies undergoing insolvency proceedings do not exist. As a general rule, however, BBRA in article 50, II, lists the performance of spin-offs, the transfer of shares, mergers, among others as forms of judicial reorganization.

18. Can outstanding shares of the company undergoing insolvency proceedings be assigned to third parties without the consent of the relevant shareholders? If yes, under what conditions? Are existing shareholders entitled to compensation? What other safeguards are provided? (e.g., does the law include a principle according to which the affected shareholders should not receive less than in a liquidation procedure?)

A: No, only the relevant shareholders can assign their own shares. BBRA provides (section 50, II and III) that one of the possible means of reorganization is the assignment of shares or the change of control, respecting, however, the rights of shareholders, according to the applicable laws and regulations. Nonetheless, it is possible to say that the judge, after the debtor’s motion, could set aside such rights if he understands that it is in the best interest of the preservation of the company and its business.

19. Can outstanding shares of the company undergoing insolvency proceedings be cancelled without the consent of the relevant shareholders? If yes, under what conditions? Are existing shareholders entitled to compensation? What other safeguards
are provided? (e.g. does the law include a principle according to which the affected shareholders should not receive less than in a liquidation procedure?)

A: BRR A states (section 50, II) that through an inter alia plan, the debtor can propose the merger, acquisition, spin-off or transformation of the company, respecting the rights of shareholders. These operations can imply the cancellation of outstanding shares, which shall be substituted by shares or quotas of another company. According to the Brazilian Company Law (section 45), these operations grant the existing shareholders the right to withdraw. In this case, shareholders become entitled to a refund of the shares, to be calculated according to the bylaws. This amount shall be less than the net worth value of the company only when it is stipulated in accordance with the economic value of the company, to be measured by three experts. The right to refund does not exist when the company has liquidity and dispersion, as defined by the Brazilian Company Law (section 137).

It is reasonable to believe that, in some cases, the court may release the company from the refund obligation, if this measure impairs the reorganization of the company and, again, the principle of preservation of the company would prevail.

20. Do shareholders of the company undergoing insolvency proceedings have pre-emption rights over new issues of shares? Are there special conditions for the suppression of pre-emption rights if the company is insolvent (if there are separate reorganization and liquidation procedures, does this affect the response?).

A: BBRA does not contain specific provisions concerning this matter. Pre-emptive rights are regulated by the Brazilian Company Law and, theoretically, are still applicable during a reorganization procedure. Nonetheless, it is possible to say that the judge, after the debtor’s motion, could set aside such rights if he understands that it is in the best interest of the preservation of the company and its business, and the reorganization plan shall provide for in this sense.

In the case of liquidation, pre-emptive rights are not applicable as the company is dissolved.

21. Can shareholders retain a participation in the company that has emerged from an insolvency process (or in the company to which the insolvent company’s assets have been transferred) even if the company was insolvent according to a balance-sheet test? (i.e., where the value of its liabilities exceeds the value of its assets) If yes, under what conditions? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: Yes, shareholders do not lose their shares on the commencement or termination of an insolvency process. However, some proposals in the reorganization plan may
consist of a transfer of assets to a new company with new shareholders or only part of the shareholders of the distressed company. Therefore, the emerged company can be an “empty shell”, and its shares would be worth nothing. Furthermore, the fact that a company’s liabilities value exceeds the value of its assets does not affect the outcome of the process from a perspective of the shareholders’ rights, and they can hold their shares when the company is reorganized.

For liquidated companies, after all creditors are paid (which is rare in practice), shareholders could, in theory, carry on the business and maintain their condition of shareholders, if they want to do so.³

22. Are the ranking of classes of shares and the preferential rights of classes of shares affected (and if yes, to what extent) by the fact that the company is undergoing an insolvency process? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: No, unless the reorganization plan provides for differently, although this is not common in Brazilian reorganization processes.

In the case of liquidation, dissenting shareholders of any resolution passed by a shareholders meeting before the commencement of the process who have not been refunded, according to rights granted to holders of preferred shares in the bylaws of the company (section 17 of the Brazilian Company Law), shall be classified as unsecured creditors and they shall be paid before the holders of common shares (section 45, § 7, of the Brazilian Company Law). Furthermore, section 83 of BBRA establishes the order according to which the creditors shall be paid in cases of liquidation, and provides that all shareholders are to be paid together.

23. Can shareholders, in the course of an insolvency procedure, supply goods, services or financial resources to the company? If yes, under what conditions (e.g., judicial authorization)? What would their ranking position be towards other creditors?

A: It is possible, but there is no specific regulation for such transactions carried out by shareholders in the course of an insolvency procedure. No previous judicial authorization is needed and the transaction is subject to control by the judicial administrator, the creditors’ committee, if any, and the prosecutor.

If the transaction involves issuance of new equity by a company under a judicial or extrajudicial reorganization procedure, the shareholder is the last in the payment rank in the case of conversion into a liquidation procedure.

³ This conclusion was reached according to a decision taken by the Court of Appeals of the State of São Paulo, process no. 0123776-62.2008.8.26.0000, rendered on March 5, 2008.
On the other hand, if the transaction involves the supply of goods, services or cash to a company under judicial reorganization, then the corresponding credit, even if held by a shareholder, is classified as an administrative expense in the case of conversion into a liquidation procedure (section 67, BBRA), and it is ranked above all claims subject to judicial reorganization but below other administrative expenses (i.e., remuneration of the judicial administrator and his assistants; labor claims arising during the liquidation procedure; credits provided to the estate by the creditors during the liquidation procedure; expenses related to collection, administration, auction, sale of assets, and payment to creditors, as well as the judicial costs of the liquidation procedure; and fees for losing the suit). From a conservative standpoint, these claims would be ranked as subordinated claims (section 83, VIII, “b”, BBRA) and would be paid after all administrative expenses, labor claims, secured creditors, taxes, and unsecured creditors.

No similar approach is provided in the case of extrajudicial reorganization procedures.

During reorganization procedures (either judicial or extrajudicial), BBRA does not stipulate any order of payment. Therefore, if a shareholder of a company under judicial reorganization becomes a supplier of credit, goods or services to it, BBRA does not provide him with any preference of payment in relation to other creditors during the procedure, as this credit is not subject to the effects of the procedure (section 49, BBRA).

Finally, operations like these can be considered transactions with related parties and, in the case of publicly-held companies, they must be disclosed to the market.

24. Can shareholders, in their capacity as counterparties, be under a duty to continue a contractual relationship with the insolvent company during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?).

A: During a reorganization procedure, all the executory contracts continue to be binding for both the company-debtor and the relevant counterpart, regardless of whether such a counterpart is a shareholder of the company. However, there may be contractual clauses providing for early termination of a contract upon commencement of an insolvency procedure, and they are not regarded as invalid by law.

Although valid by law, these clauses can be mitigated in judicial reorganization procedures due to the principle of preservation of economically viable companies (section 47 BBRA). This understanding is also shared by the doctrine in cases of
public utility contracts.⁴ These contracts are governed by Law no. 8,666/93, which provides for the possibility of termination of contracts in the case of insolvency of the contracting company, but the commencement of a reorganization procedure does not imply an automatic termination of such contracts according to the aforementioned understanding.

In the case of a liquidation procedure, executory contracts are not terminated upon commencement of the procedure and can be fulfilled by the judicial administrator if he reduces or avoids further liabilities or when they are necessary for the maintenance and preservation of assets, after consent by the creditors’ committee, if any (section 117, BBRA). The counterparty may notify the judicial administrator within 90 days after the execution date of the term of his appointment, demanding his declaration, in 10 days, regarding the continuation of the contract (section 117, § 1, BBRA). The refuse to continue or the silence of the judicial administrator gives the counterparty the right to compensation, the amount of which shall be determined in ordinary proceedings, and shall be classified as an unsecured claim (section 117, § 2, BBRA).

25. Can shareholders (or companies of the same group) holding credit claims against the company under insolvency procedure participate in the creditors’ meeting and vote on the insolvency plan without restrictions? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: According to section 43 of BBRA, shareholders holding credit claims against the company under an insolvency procedure can participate in the creditors’ meeting, but they do not have voting rights. The prohibition also involves affiliates, parent companies, subsidiaries or companies that have shareholder(s) with a participation higher than 10% in the share capital of the debtor or in which the debtor or any of its shareholders or partners hold a participation greater than 10% of the share capital. They shall not be considered for purposes of verification of quorum and deliberation.

This rule also applies to the spouse or relatives by blood or affinity, collateral until the 2nd level, ascending or descending from the debtor, its managers, controlling shareholder(s), members of the board of directors, audit committees or similar councils of the company- debtor and the companies in which such persons perform those functions (section 43, sole paragraph, BBRA).

Depending on the origin and nature of the credit, one could assume that minority shareholders of the company would have voting rights in a creditors’ meeting

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summoned to vote the reorganization plan, when they have neither participated nor influenced the elaboration of the plan and when they hold credits against the company arisen from, e.g., tort claims or loan agreements. This is not a pacific conclusion.

26. If shareholders (or companies of the same group) do not hold credit claims against the company under insolvency procedure, must/can they participate in the creditors’ meeting? If that is the case, what rights or duties do they have in that meeting? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: BBLA states that shareholders can participate in the creditors’ meeting, but the law is not clear whether or not they must hold credits against the company. In this sense, the majority of the doctrine understands that shareholders (or companies of the same group) must hold credits against the company in order to participate in the creditors’ meeting, but without voting rights (see answer to question 25).

27. Do shareholders in an individual company have information rights as to the filing of insolvency proceedings by the parent or other related companies?

A: The law does not contain any specific provision in this sense. As a rule, shareholders of an individual company would be informed as to the filing of insolvency proceedings by the parent or other related companies through normal channels of disclosure, according to capital market rules, such as stock exchange or CVM communications, disclosure of material facts through the media, and Court Gazettes (see answer to question 7).

In the case of closely-held companies, no disclosure rules are available regarding material facts, such as the filing of an insolvency proceeding. However, the minutes of the shareholders’ meeting approving the commencement of an insolvency procedure by the parent or other related companies (see answer 32) must be published in Official Gazettes and newspapers with a significant circulation. Yet, the effectiveness of such disclosure is questionable.

III. The Role of the Shareholders’ Meeting in Companies Subject to Insolvency

Proceedings

28. Does the shareholders’ meeting continue to exist in insolvency proceedings? (If there are separate reorganization and liquidation procedures, does this affect the response?)

**A:** Yes, according to section 64 of BBRA, during a judicial reorganization the management of the company remains the same, and the meetings continue to take place. However, under a liquidation procedure, where the company is dissolved, the management is removed from the administration of the estate (section 75 of BBRA) and the main decisions concerning the estate are taken by the judicial administrator, the creditors’ meeting and the creditors’ committee, if any.

29. Does the shareholders’ meeting preserve all of its competences, generally? (If there are separate reorganization and liquidation procedures, does this affect the response?)

**A:** Yes, except under a liquidation procedure, where the company is dissolved and the main decisions concerning the estate are taken by the judicial administrator, the creditors’ meeting and the creditors’ committee, if any.

30. Does the shareholders’ meeting need to approve the accounts of the distressed/insolvent company?

**A:** As the company retains possession of its assets and continues operating the business, the shareholders’ meeting must approve the accounts of the company in every fiscal year. It is different in a liquidation process, where the debtor is removed from the administration of the estate (see answer to question 28).

31. Does the shareholders’ meeting have the power to dismiss directors – if directors are still in charge of the insolvent company? Can the shareholders’ meeting request the removal of the insolvency representative? (If there are separate reorganization and liquidation procedures, does this affect the response?)

**A:** Yes, the shareholders’ meeting holds the power to dismiss directors. If the company has a two-tier board structure (i.e., the business is led by officers and there is a board of directors to monitor the officers’ activities), the officers can be removed by the board of directors and the directors can be removed by the shareholders’ meeting. In a one-tier board structure, the shareholders’ meeting has the power to remove the directors. These rules are applicable only during a reorganization procedure (for liquidation procedures, see answer to question 28).
A shareholders’ meeting does not have the power to remove the insolvency representative (“judicial administrator”), which is appointed by the judge, either under a reorganization or a liquidation procedure. However, according to section 31 of BBRA, the judge has the power to remove the judicial administrator on his/her own initiative or by a reasoned request made by any interested party. Therefore, any individual shareholder, as an interested party, could request the removal of the judicial administrator.

32. Is a shareholders’ meeting authorisation required to start an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: Section 122, IX, of the Brazilian Company Law provides that a shareholders’ general meeting must previously approve any application for judicial reorganization or liquidation (in this case, when proposed by the debtor) by the managers of the company. However, in urgent cases the application can be filed by the managers, with the consent of the controlling shareholder, if any, before an immediate call of a shareholders’ general meeting to deliberate about the filing. This provision is applicable to both publicly- and closely-held companies.

33. Does the shareholders’ meeting need to approve an insolvency or reorganization plan? Can shareholders, even individually, challenge an insolvency or reorganization plan?

A: No. The reorganization plan is proposed by the managers of the company, unless the bylaws stipulate otherwise, which is not common.

One could support, however, that due to the fact that a reorganization plan is equivalent to a business plan, and the bylaws of some companies provide that this plan is subject to the approval by a shareholder’s meeting or the board of directors, then a shareholders’ meeting approval would be necessary.

Furthermore, BBRA does not give shareholders the right to challenge the insolvency/reorganization plan. Nevertheless, some of its provisions (e.g., merger, acquisition, change of bylaws, change of directors, and issuance of bonds (“debentures”) should be previously approved by a shareholders’ meeting. In the case of rejection of one or more proposals of the approved plan by the shareholders’ meeting, it is reasonable to believe that the judge would overrule the shareholders’ veto and confirm the proposal, if he understands that it is in the best interest of the preservation of the company and its business.

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6 This conclusion was reached according to decisions taken by the Court of Appeals of the State of São Paulo, processes no. 0154311-66.2011.8.26.0000, rendered on January 24, 2012; and no. 0066573-50.2005.8.26.0000, rendered on May 19, 2006.
34. Is a shareholders’ meeting decision required to issue new shares of the company undergoing insolvency proceeding? Can a new share issue be decided by the board? Can a new share issue be decided by the insolvency representative? If a capital increase has to take place through the conversion of claims into new shares, does this affect the response?

A: Yes, unless it is a company with authorized capital, according to its bylaws. In this case, the board of directors is entitled to issue new shares up to the limit set forth in the bylaws, regardless of the authorization of a shareholders’ meeting. This is not applicable during a liquidation procedure (see answer to question 28).

The judicial administrator does not have the power to decide the issuance of new shares.

The conversion of claims into shares does not affect the answer. However, it is reasonable to believe that a reorganization plan providing for the issuance of new shares or conversion of claims into equity would come into effect regardless of the resolution taken by the shareholders’ meeting, if the judge understands that the plan approved is in the best interest of the preservation of the company and its business.

35. Can an insolvency/reorganization plan affect the structure of the corporate entity (e.g., by merger, spin-off, or change of the legal form)? Is a shareholders’ meeting authorization required for this?

A: Yes. The reorganization plan can affect the structure of the corporate entity in several forms, according to section 50, II of BBRA. A shareholders’ meeting authorization is required. The third paragraph of the answer to question 33 above is also applicable in these cases.

36. On what conditions can the company carry on business during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?) Is a shareholders’ meeting authorisation required?

A: During a reorganization procedure, the debtor is kept in the business direction (section 64 of BBRA). Nevertheless, certain transactions are subject to previous judicial authorization, such as the disposal or burdening of assets that are included in the noncurrent assets, except if it is part of the reorganization plan (section 66 of BBRA). Also, in cases of a disposal of assets subject to a secured guarantee, the creditor holding the guarantee must explicitly approve its suppression or substitution, according to the first paragraph of section 50 of BBRA.
In some circumstances normally involving considerable amounts, and duly provided in the bylaws, a shareholders’ meeting can be required to previously approve certain transactions.

Upon the opening of a liquidation procedure, the court may establish the provisional continuation of the activities of the company under management of the judicial administrator (section 99, XI of BBRA). However, shareholders do not participate in the management of the company.

37. In the course of an insolvency procedure, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business operation of the company? Is a shareholders’ meeting authorisation required? (If there are separate reorganization and liquidation procedures, does this affect the response?)

A: The disposal or encumbering of assets that are listed as noncurrent assets can only take place in the case of evident usefulness as recognized by the judge, after consulting the creditors’ committee, except when the asset is listed in the reorganization plan (section 66 of BBRA), when no judicial authorization is required, since the creditors obviously approve the sale of the corresponding asset(s). The law does not differentiate between sales carried out within the ordinary course of business and those outside the ordinary course of business. Shareholders’ meeting authorization may be required, depending on the bylaws provisions.

The sale of the entire business can be made when it is part of the reorganization plan, but risk of tax and labor succession does exist, as the law is not clear in this regard. If the transaction involves a merger, an acquisition by another company, a spin off and so on, a shareholders’ meeting authorization is required (see answer to question 35).

BBRA also allows debtors to sell one or more divisions of the company, according to the reorganization plan, in this case without tax and labor succession (section 60, BBRA). Here, a shareholders’ meeting authorization may also be required, depending on the bylaws provisions.

In the case of rejection of one or more proposals of the approved plan by the shareholders’ meeting, it is reasonable to believe that the judge would overrun the shareholders’ veto and confirm the proposal, if he understands that it is in the best interest of the preservation of the company and its business.

Upon the opening of a liquidation procedure, the court may establish the provisional continuation of the activities of the company under management of the judicial administrator. However, the shareholders do not participate in the management of the company.
38. Does the shareholders’ meeting have any power in relation to a decision of the board or the insolvency representative to continue or reject any favourable, unfavourable or essential contract during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?).

**A:** Generally speaking, the shareholders’ meeting does not have this power, unless a previous authorization is provided according to the company’s bylaws.

Upon the opening of a liquidation procedure, the court may establish the provisional continuation of the activities of the company under management of the judicial administrator. However, the shareholders do not participate in the management of the company.

39. If an insolvency plan can be presented for a whole corporate group, must that plan be approved by the shareholders’ meetings of each company of the group, including of those that are balance-sheet insolvent? How are the different meetings’ decisions coordinated? Are there specific safeguards (e.g., any veto power or other remedy) for the minority shareholders of the companies that are not insolvent?

**A:** No, approval of a consolidated plan from shareholders’ meetings of each company of the group is not required, unless the bylaws stipulate otherwise, which is not common (see answer to question 33, which is also applicable for groups under an insolvency procedure). No specific safeguards for minority shareholders are provided by the Law.

The possibility of presenting only one plan for a whole corporate group is a topic being currently discussed in case law. This topic was recently raised in the reorganization process of OSX7, and it was decided that several plans should be presented.

It seems reasonable to support the possibility of presenting only one plan provided there are specific provisions for each company, individually considered.

40. If companies belonging to the same group file separate insolvency proceedings, are there specific requirements/mechanisms to provide for coordination of those proceedings? Are shareholders’ meetings of the relevant companies involved in the coordination mechanisms, if any?

**A:** No, there are no specific requirements/mechanisms to provide for coordination of different proceedings of distressed companies belonging to the same group. A recent attempt in this sense was carried out in reorganization processes of OGP (former OGX) and OSX (two publicly-held companies, with the same controlling shareholder, and deeply integrated in terms of operations). The application for a

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joint procedure had been accepted by the bankruptcy judge, but it was set aside by the Court of Appeals of the State of Rio de Janeiro\(^8\) because the net worth values, the creditors and the operations of the companies were completely different.

IV. Other Obstacles for Insolvency Procedures Found in Company Law

41. Please list any other legal provision in company law that, in your opinion or in your experience, may interfere with the insolvency procedure of a company in your jurisdiction.

A: In general terms, it is BBRA that normally interferes with the governance rules and rights of shareholders. Despite the fact that BBRA provides (section 50) that any means of reorganization contained in the plan must observe the applicable laws and regulations, it is common for courts to set aside rights and obligations arisen from company law or applicable regulations in order to assure that the company will emerge from bankruptcy and will be preserved, to secure jobs, pay creditors, and benefit society as a whole through the maintenance of the company in the market. This assertion is challengeable since such decisions do not normally involve a deep analysis to test whether the business is viable or not. In many cases, the losses for creditors and especially for minority shareholders are considerable.

Therefore, the lack of adequate regulations concerning the rights of the minority shareholders of a company under an insolvency procedure, particularly judicial or extrajudicial reorganization, harms the judicial system, and greatly affects this minority group. Questions should be addressed involving the right of shareholders to participate in the elaboration of the reorganization plan, their withdrawal rights, pre-emptive rights, the constitution of a committee to represent their interests during the procedure, their right to elect/remove a member of the board, their tag-along right, the effectiveness of a shareholders’ agreement during the reorganization, and the coordination of resolutions taken by a shareholders’ meeting or a creditors’ meeting.

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