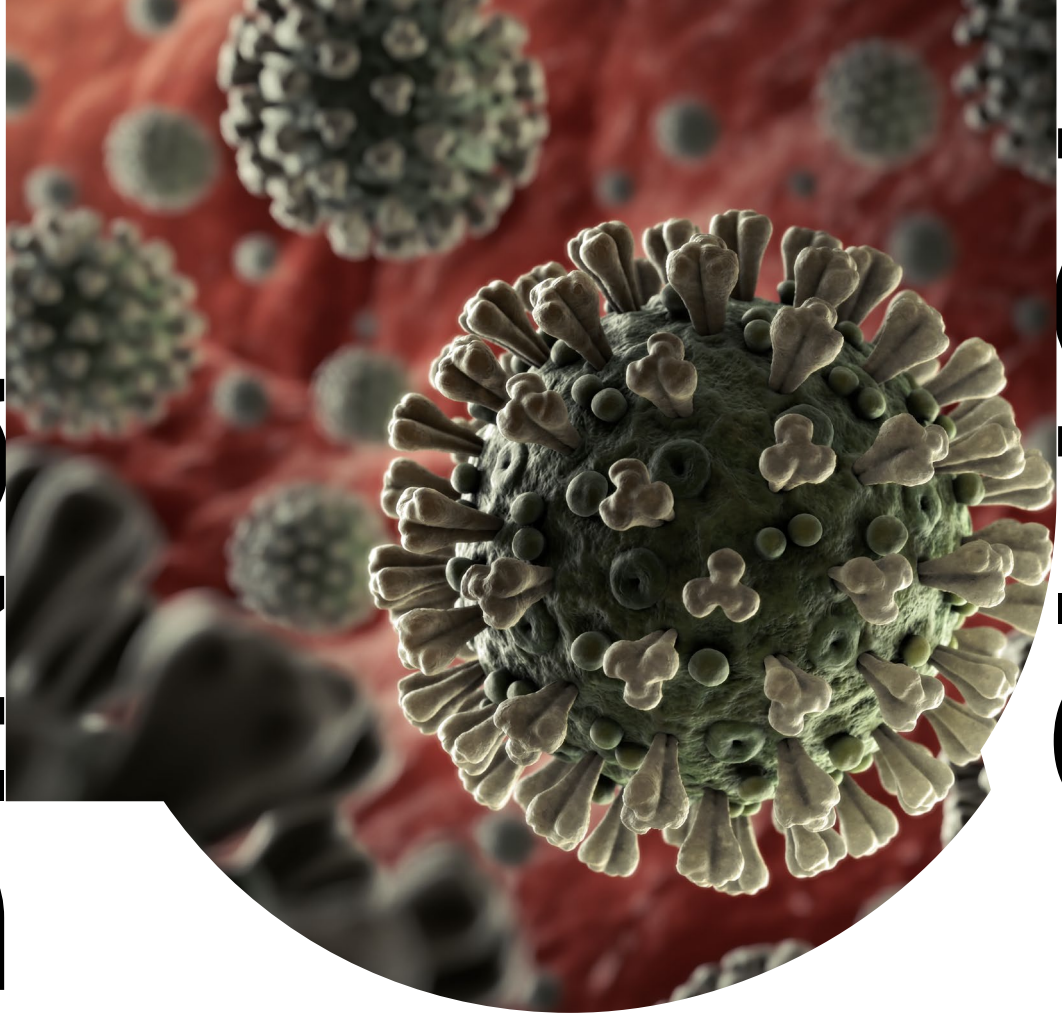
TRENDING TOPIC



MAR. 20

RESTRUCTURING AND INSOLVENCY

Coronavirus: Restructuring and insolvency

The main doubts of company directors about the consequences of the current Covid-19 pandemic in relation to insolvency, the PER, and the RERE.

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As a result of the spread of the Covid-19 virus, the World Health Organization declared a public health emergency of international concern (PHEIC) on 30 January 2020 and a pandemic on 11 March 2020. Against this background, on 13 March 2020, the Portuguese Minister of Internal Administration and Minister of Health signed an order declaring a state of alert that covers the whole country until 9 April 2020. Decree of the President of the Republic 14-A/2020 of 18 March declared a state of emergency due to the situation of public crisis resulting from the Coronavirus pandemic. The **state of emergency** covers the whole of Portugal and will last for 15 days, without prejudice to any renewals.

Besides the human consequences of Covid-19, the virus also has economic consequences. The restrictions and containment measures implemented to prevent the spread of the Covid-19 pandemic are having a global impact.

Portuguese and multinational companies are already suffering serious consequences. Some sectors of the economy, such as tourism, food and beverages, and travel are being directly affected more than others. However, the whole of the economy is feeling the effects and this suggests a serious economic and financial crisis is looming.

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Faced with this scenario, we have set out below some notes and explanations to address the questions most frequently asked about the possible consequences of breaches of contractual or other legal obligations arising from the current situation. We also take a look at the impact of this situation on the difficult decisions that have to be made by the directors and managers of the companies affected. In providing this information, we will refer to the legislation applicable to the PER (Special Revitalisation Process), the RERE (Out-of-court Business Recovery Scheme), and to insolvency.

1. Is the current Portuguese and international situation caused by the Covid-19 pandemic justification for (legitimate) breach of our obligations to our creditors?

The classification of a pandemic as a "case of *force majeure*" may have implications when it comes to compliance with contractual obligations. In some cases, this may lead to the debtor being released from its responsibility and the creditor not being able to demand the performance of an unperformed obligation or the payment of compensation for any loss or damage suffered. However, to have this effect, performance of the obligation must have become objectively impossible and not just "more onerous". If this situation is confirmed, it could lead to the application of the rules on a "change in circumstances" which, in exceptional cases, allows the party harmed by the change to ask for either *(i)* the termination of the contract, or *(ii)* its modification based on equity.

However, this situation must be examined on a case-by-case basis.

The current situation does not stop directors from taking preventive and proactive action in compliance with their duties under the law and the articles of association of the company. This includes negotiating with its creditors to adapt or modify the previously assumed obligations.

2. We have a recovery plan that was approved less than two years ago and we are at risk of not complying with it. Can we apply for a new PER?

The current legislation does not allow a company to have recourse to a new PER if the decision to approve the recovery plan in force was made less than two years ago. There is an exception for situations in which the company has fully implemented the plan or in which there are factors unrelated to the plan itself and where the subsequent change is outside the control of the company.

Covid-19 is an event of *force majeure* because it is unpredictable and totally unrelated to the regular operations and decisions made by companies.

Therefore, the current situation could justify recourse to a new PER, even if the above period of two years has not yet passed. However, we advise a case-by-case analysis of the situation.

Moreover, the suspension of deadlines and procedures resulting from Law 1-A/2020 does not apply to the periods (including grace periods and payment deadlines) established in recovery plans that have already been approved and ratified by the courts.

3. We have a recovery plan approved less than two years ago and we are already not complying with it. Can we apply for a new PER?

If the failure to comply with the plan began before the Covid-19 pandemic, that is, before the change in circumstances outside the control of the company, the court may hold that the company was already in an insolvency situation.

A "breach of obligations provided for in an insolvency plan or payment plan" is one of the indications of an insolvency situation provided for in the law. Therefore, the fact there has been a "subsequent change outside the control of the company" in the meantime that worsened its situation may not be enough to ground a new PER.

4. We have an ongoing PER or RERE and we are at the negotiation stage. Can the negotiation period be suspended?

Law 1-A/2020 provides for the suspension of deadlines in urgent and non-urgent procedures (including procedures before registry offices as is the case of the RERE), apart from the exceptions already mentioned.

Thus, the deadlines and the steps associated with PER and RERE processes are generally suspended, regardless of the stage they have reached.

This change in the law does not provide for the end of the period of suspension so, at present, it is not possible to anticipate how long it will remain in place.

After the end of the current period of suspension of deadlines and the consequent return to the normal course of these processes, it will be important to reassess the economic and financial situation of the company being recovered/restructured. It will also be necessary to look at their prospects for effective recovery to determine whether there is an interest and/or viability in the continuity of the process in question.

5. In view of the current situation, are we still under a duty to petition for the insolvency of the company?

Law 1-A/2020 did not provide for the suspension of the deadlines inherent to the duties of company directors, or of those relating to the obligations assumed towards creditors of the company. The Law simply provides that the "exceptional circumstances" referred to in article 7 constitute grounds to suspend limitation periods and expiry periods in all kinds of processes and procedures.

Therefore, we consider that company directors are still under a duty to petition for insolvency within 30 days of becoming aware of the situation.

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However, given the suspension of deadlines and procedural steps that is already in place, any insolvency proceedings that have been brought (at the request of company itself or at the request of a creditor) will be suspended until the general suspension is ended.

We note that any failure by the debtor or its directors to comply with the duty to petition for insolvency amounts to serious misconduct in relation to the situation of insolvency created. This assumes importance when it comes to the procedural step of deciding whether or not to classify the insolvency as culpable.

If the company is only in a difficult economic situation or merely in a situation of imminent insolvency, but still capable of recovery, it can use the PER or RERE to try to recover by adopting a recovery/restructuring plan. These processes will also be suspended under the provisions of article 7 of Law 1-A/2020.

6. Have there been any changes to the criteria to confirm an insolvency situation?

To date, there has been no legislative change regarding the criteria used to assess whether a company is in an insolvency situation and this is not expected to occur. However, there is an exception regarding the suspension/extension of certain deadlines to meet certain obligations (see some examples below [1]).

Thus, in general terms, a company continues to be in an insolvency situation when it is unable to meet its obligations as they fall due. This is particularly so when there is a general failure by the company to pay its debts to the Tax and Customs Authority or the Social Security, to its employees, or to the landlord or mortgage lender of the premises where the company operates. However, these obligations themselves may be changed as a result of the exceptional situation we are experiencing.

The current economic situation caused by the Covid-19 pandemic is affecting numerous Portuguese and international companies. As a result, we are expecting to see increased demands on the courts to analyse the criteria set out in the Insolvency and Corporate Recovery Code. It is expected, for example, that there will be greater tolerance for possible breaches that may arise in this period of pandemic.

With regard to the changes/extensions to deadlines to comply with certain obligations with an impact on establishing whether or not an insolvency situation exists, Decree-Law 10-A/2020 of 13 March has established exceptional and temporary measures relating to the spread of the new Coronavirus, COVID-19. It is important to note that this Decree-Law has already provided for the extension of the deadline to approve accounts. It states: "**General meetings of companies, associations or cooperatives, which must take place under the law or the articles of association, may be held up to 30 June 2020**". It has thus adapted one of legal indications of a situation of insolvency of a company: *a delay of more than nine months in approving and filing of accounts*.

1 For a more detailed information on all the changes, see the contents of the PLMJ Trending Topic dedicated to the subject of the Coronavirus here and you can also follow the updates on PLMJ's LinkedIn.

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In the same way, Order 104/2020-XXII of 9 March 2020 of the Secretary of State for Tax Affairs provided for the extension of the deadlines, with no additions or penalties, for voluntary compliance with various tax declaration obligations. These included the deadline for the special payment on account to make during the month of March, which was extended to 30 June 2020. This is relevant for the purpose of the criterion of *compliance with tax obligations*.

Moreover, Law 1-A/2020 has suspended the effect of notices of termination of residential and non-residential tenancy agreements given by the landlord. This may have some impact on the analysis of the legal indications of a situation of insolvency of a company resulting from the *widespread failure in the past six months, to pay rents for any type of leasing, including financial, instalments of the purchase price or loan guaranteed by the respective mortgage, in relation to the premises where the debtor carries on its activity or has its head office*.

We would also like to draw your attention to the fact that the suspension of effect of notices of termination of **residential and non-residential tenancy agreements** does not, however, mean that tenancy agreements can simply be breached, nor that the Landlord may not terminate the agreements for breach. The suspension only applies to the effects of the notice of termination of the agreement (such eviction and the demand for immediate payment of rents due or any compensation).

In any case, if companies anticipate that it will be impossible to comply with their obligations, or to comply with them on time, they should seek to justify their non-compliance in order to avoid claims of insolvency or other undesirable judicial actions. ■