

Portugal's *Extraordinary Business Viability Process*

Catarina Guedes de Carvalho writes on the new extraordinary process for company viability in response to the COVID-19 crisis in Portugal



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Following the international public health emergency, many Member States of the European Union declared national states of emergency. Portugal was among them and the declared state of emergency led to the necessary confinement of citizens and, consequently, to the paralysis of a number of activities.

These circumstances created a situation of financial constraint for businesses due to a lack of liquidity and, in many cases, this has prevented them from fulfilling their obligations.

As an initial reply in terms of implementing new measures to face this COVID-19 pandemic, the only direct, exceptional and temporary measure regarding the legal framework of insolvency and restructuring approved by the Portuguese authorities was to suspend the time limit for the debtor company itself to petition for insolvency¹, with effect from 7 April 2020.

As the economic crisis worsened, it quickly became clear that a further legislative response was needed in this area too. The COVID-19 pandemic is not going to disappear as quickly as expected and its effects are worsening and tending to last much longer than the worst initial estimates. The entire business sector has been affected and even viable companies are generally facing an enormous difficulty: a lack of liquidity.

The **Extraordinary Business Viability Process** (*Processo Extraordinário de Viabilização de Empresas* or “PEVE”) is one of the measures



provided for in the Economic and Social Stabilisation Programme, which is a plan devised by the Portuguese Government in order to respond to the economic and social difficulties caused by the pandemic.

The Portuguese government could have chosen to adapt the arrangements that already existed: the PER (*Special Revitalisation Process*) and the RERE (*Out-of-court Business Recovery Scheme*), which are the key pre-insolvency measures for companies, respectively of a judicial and out-of-court nature. Or it could have taken advantage of this moment to implement Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 – which was not done, admittedly because this could have led to an accelerated and, as such, poorly considered implementation. However, the Portuguese Government decided to go ahead and create a new

extraordinary legal framework, aimed exclusively at companies that are in a difficult economic situation or an insolvency situation, whether imminent or current, due to the COVID-19 pandemic, but are viable: the PEVE.

The aim of the PEVE is to obtain judicial approval of a debt restructuring agreement (“Viabilisation Agreement”) established out of court between the company and its creditors³, so we therefore admit it is a hybrid procedure in nature and it falls into the set of instruments typically called “fast-track-court-approval-procedures”⁴. The approval decision binds the company, the creditors signing the Viabilisation Agreement and the creditors listed by the company in the report of creditors⁵, even if they have not participated in the out-of-court negotiations.

At the time the application is submitted, the company should

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not have any PER pending. In addition, it must meet and prove the conditions necessary for its viability. It must also provide proof that on 31 December 2019 the company's liabilities were less important than its assets⁶. That is, in practice, it must provide evidence that its difficulties stem from the pandemic situation⁷. However, the law does provide for two exceptions:

- (i) micro and small businesses, where the liabilities may exceed the assets provided certain additional conditions are met; and
- (ii) businesses which, although not in a positive net position on 31 December 2019, have managed to regularise their financial situation under the transitional provisions allowing the use of the RERE by businesses in a situation of insolvency, provided they have deposited the restructuring agreement in due time.

The judge is responsible for checking that all the preconditions and requirements are met by issuing the order granting or opening the PEVE appointing the interim judicial receiver (*administrador judicial provisório* or "AJP"). The AJP plays a very important role (and this is not the case in the PER): to give an opinion on whether the agreement offers reasonable prospects of ensuring the viability of the company, and the judge will then use this opinion as a basis for the decision on whether to approve it.

In order to ensure that it is processed particularly quickly, in addition to shortened time limits and eliminated phase of presenting claims by the creditors, this extraordinary procedure enjoys priority to over other urgent procedures (insolvency proceedings and the PER).

Without prejudice to the general principle of intangibility of tax and social security claims, which remains untouched, express provision is made for the possibility to reduce the rate of interest on arrears, as well as prescribe other tax benefits

(identical to those of the PER and RERE) in the restructuring agreement, in order to achieve the financial consolidation of the company.

Initiation of the PEVE also has the effect of suspending any debt recovery proceedings and insolvency petitioned with respect to the company, as long as the insolvency has not yet been declared (procedural effects). The PEVE also prevents the suspension of the provision of essential public services to the company (substantive effects, because they affect creditors as party to a contractual relationship).

One of the main virtues of the PEVE is the fact that it promotes both financing and self-financing, especially by the shareholders, to make the company effectively viable. The PEVE safeguards the guarantees agreed between the company and its creditors, provided they are established to provide the company with the financial means necessary to operate. It also gives the shareholders, or any other persons in a special relationship with the debtor, who finance the company's activity, a general moveable credit privilege. Furthermore, any legal transactions provided for in the Viabilisation Agreement that included the effective provision to the company of new financial credits cannot be clawed back for the benefit of the insolvent estate.

This is a solution we welcome because we consider it not only to be of elementary justice, but also absolutely fundamental for the recommended recovery of a company that is viable but in difficulty⁸.

In addition, the Government has decided to make one-off changes to provide the existing judicial instruments for recovery with mechanisms for adapting to the COVID-19 pandemic⁹:

- (i) the possibility to grant additional time for the conclusion of the negotiations within the framework of the PER and for the proponent of an insolvency plan to adapt it;

- (ii) the application of the RERE to companies that are currently insolvent¹⁰ as a result of the COVID-19 pandemic but which are still likely to become viable and which can demonstrate that on 31 December 2019 their assets exceeded their liabilities or, although not in a positive net position on 31 December 2019, have managed to regularise their financial situation under the transitional provision allowing the use of the RERE by companies in a situation of insolvency; on condition that they have deposited the restructuring agreement in due time; and

- (iii) in cases where non-compliance with the approved insolvency plan is based on events occurring after 7 April 2020, the 15-day period to regularise the situation – failing which the moratoriums and forgiveness set out in it will be extinguished – will only begin to run after the law now approved ceases to be in force.

There are also two other measures that are easy to implement¹⁰, with the sole aim of responding immediately to the problem of the lack of liquidity of companies – namely, they involve the distribution to the creditors, as soon as possible, of large sums deposited in PER and insolvency proceedings (i.e., amounts due to the creditors but in the hands of the State). ■



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Footnotes:

- 1 A company is insolvent when it is not able to pay the debts that have fallen due (under article 3(1) of the Insolvency and Corporate Recovery Code – "CIRE"). Company directors/management have a legal obligation to submit an application for insolvency within 30 days of becoming aware of the insolvency situation (under article 18(1) of the CIRE). Breach of this legal obligation could lead to the insolvency being classified as culpable.
- 2 The creation of the PEVE was announced by the Government at the beginning of June and it is provided for in Law 75/2020 of 27 November. It entered into force on 28 November 2020 and it will remain in force until 31 December 2021, with the possibility of extension by government decree.
- 3 Creditors representing at least the majority of votes provided for the PER (majorities provided for in article 17-F(5) of the CIRE).
- 4 The PEVE is inspired to a great extent by the abbreviated PER (article 17-I of CIRE) and the RERE.
- 5 This report is presented by the company but can be challenged by any creditor.
- 6 The fact the liabilities are greater than the assets is one of the criteria for establishing insolvency (under article 3(2) and (3) of CIRE), but it does not trigger the above-mentioned duty of directors to petition for the insolvency of the company.
- 7 The Portuguese legislature includes a presumption already adopted by other jurisdictions. It can now, in fact, be presumed that, when companies were not insolvent on a certain date before the COVID-19 pandemic (in this case, 31 December 2019) and their insolvency occurred after the COVID-19 pandemic hit, this is a direct consequence of the extraordinary crisis, which, in turn, indicates a temporary insolvency that is, therefore, surmountable.
- 8 We highlight here the approach of professor and supreme court judge Catarina Serra, namely "A função (alternativa) do RERE como programa extraordinário para o apoio e a reanimação de empresas" in *Revista de Direito Comercial*, page 981 and following www.revistadedireitocomercial.com/a-funcao-alternativa-do-rere.
- 9 Measures included in the same Law 75/2020 of 27 November.
- 10 Under the current rules, only a company in a difficult economic situation or in a situation of imminent insolvency can turn to the RERE.