LUPICINIO
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NEWSLETTER ABOUT THE EFFECTS OF THE STATE OF ALARM

IN BANKRUPTCY LAW, WITH SPECIAL ANALYSIS OF PRE

BANKRUPTCY AND EXPRESS LIQUIDATION

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SUMMARY:

This Newsletter is a brief legal note that clarifies the concerns and uncertainties that the regulatory flood is generating to professionals and / or entrepreneurs in such a short period of time caused by the sudden and unpredictable appearance of the crisis of Covid-19 and that, moreover, has an imminent and positive impact, if known, on the professional and / or company. In this case, our work focuses on analyzing how the state of alarm, specifically, the R.D. law 8/2020, the R.D. 463/2020 and the Communications of the Permanent Commission CGPJ dated March 18, 2020, has affected the Bankruptcy Law. Furthermore, we have considered it appropriate, due to the more than possible harmful and negative effect that the present crisis may have on professionals and/or companies, to deepen the particular analysis of two legal "tools" offered by the Bankruptcy Law to professionals and/or entrepreneurs to safeguard their personal interests and/or their business, or, where appropriate, to reduce the liability, cost and tax involved in the liquidation of a company, such as: the pre-bankruptcy (Article 5bis of the Bankruptcy Law) and the express bankruptcy (Article 176bis4. of the Bankruptcy Law).

Over the course of 2019, several indicators appeared which allowed macroeconomic experts to predict an economic crisis during 2020 as a result of the cyclical stagnation of the economy. However, what nobody expected was the current crisis caused by COVID-19 causing around 40% of the world to be confined to their houses. This crisis has significantly affected Spain due to the high rate of infections and deaths that the country has seen caused by COVID-19.

What is certain is that the crisis as a result of COVID-19 is having and will continue to have a significant effect on Spain's industrial and business sectors as well as on global relations and international relations between businesses and professionals.

In fact, in the recent publication by the Bank of Spain "macroeconomic reference cases for the Spanish economy after COVID-19" (https://www.bde.es/f/webbde/SES/Secciones/Publicaciones/InformesBoletinesRevistas/ArticulosAnaliticos/20/T2/descargar/Fich/be2002-art10.pdf) the supervisory body, based on different scenarios depending on the duration, analyses the current situation, anticipating a fall in the P.I.B. of between 6.6% and 13.6%, a deficit of between 7% and 11% and an unemployment rate of between 18.3% and 21.7%.

However, from a few optimistic perspectives, we consider that the current economic crisis will be different to the one that came about at the end of 2008, after the fall of the American financial entity Lehman Brothers, and which had a large impact on Spain in terms of the housing and construction sectors, notwithstanding, that it caused a domino effect on various other sectors of the Spanish economy due to real estate and construction contributing considerably to our GDP.

In this case, as long as the state of alarm is lifted as soon as it is sensible to do so and we can return to normality in the professional world to some extent in the short term, it seems that we will encounter a cash flow crisis which will affect most sectors, therefore, we will be facing a crisis that in the short term will forcefully affect and amount in unison to the Spanish business and industrial fabric but that in the medium term, if we take the appropriate measures or actions that contain the lack of liquidity with the considerable help of the Government and Europe, the activity can be recovered at levels that allow the continuity of the business and / or profession.

Hence, the Government agreed at the end of March to mobilize 20% of our P.I.B. (some 200,000 million) and, among other items, the following was approved: (i) the start-up of a first section of the I.C.O. of 20,000 million euros (out of the 100,000 million euros to guarantee the liquidity of the companies most affected by the coronavirus crisis, and half of that amount will serve to guarantee new loans to SMEs and the self-employed; (ii) coverage line of the safe CESCE, with an item of 2,000 million euros; (iii) ICO line for the tourism sector, with an item of 400 million euros; etc.

In fact, although we are aware that said measures don't seem to be enough to help lessen the current crisis, the glimmer of hope is that the government has taken measures to inject cash into businesses and professional activities from the start. However, we can only hope

that Europe finally decides to adopt these measures too. In this, we can avoid a permanent and structural impact in the business and industrial sectors similar to that of the 2008 crisis.

If we learned anything (or we hope we did) from the previous crisis is that professionals, even more so, that businesses have to try to get ahead of and anticipate possible problems and consequences which could cause a worldwide economic crisis, with reasonable measures and actions, courageous, quick and innovative, as well as with the need to surround themselves with experts so they can help them take the right actions for their individual needs in order to help them better navigate the crisis. This is needed so that companies can come out stronger as a result.

In this contect, it is vital for professionals and businesses to be familiar with the details and the virtues of Bankruptcy Law, which offers endless possibilities to save a business, those such as: (i) the pre-contest -art. 5bis of the Bankruptcy Law-, with refinancing agreements .D.A. 4th and art. 71 bis of the Bankruptcy Law, or an advance agreement proposal -PAC-; (ii) ordinary bankruptcy; (iii) abbreviated contest with application accompanied by settlement plan -art. 191 ter of the Bankruptcy Law-; (iv) the express -art contest. 176 bis.4 of the Bankruptcy Law-; etc.

Notwithstanding that it would be necessary to analyze and study the particularities that each professional and / or company presents in order to know what is the best measure and action to take, we have considered it interesting to be "diametrically opposed" proposals to analyze in this brief legal note, the pre -contest and express contest.

1. **Effects of the State of Alarm on Bankruptcy Law**

Before going into detail, it is fitting that we briefly mention how the State of Alarm, as set out in the Royal Decree Law 8/2020, the Royal Decree 463/2020 and the Communiqués of the Permanent Commission CGPJ of 18/03/2020, The Bankruptcy Law, which, as you can see, roughly affects the extension of certain terms.

In view of the current temporary and extraordinary situation of the state of alarm, Article 43 of Royal Decree Law 8/2020 regulates the impact of the state of alarm on the new reality (temporary and extraordinary) of the deadlines for debtors who are in a situation of insolvency and who are still within the deadline for requesting the declaration of bankruptcy while the state of alarm is in force:

-The debtor who is in a situation of insolvency will not have the duty to request the declaration of bankruptcy.

- The Courts will not admit for processing the necessary applications for declaration of bankruptcy until two months have passed since the end of the state of alarm, which have been presented during this state or which are presented during these two months.

- In cases of voluntary competition, preference will be given and, therefore, they will be admitted for processing even if the application is dated later, that is, if an application for

voluntary competition has been submitted, it will be admitted for processing, with preference, even if it is dated later.

- In cases of pre-competition, the deadline for the declaration of the bankruptcy or for adhesion to the anticipated proposal of agreement will be suspended, i.e. the debtor who has communicated to the court with jurisdiction for the declaration of bankruptcy the initiation of negotiations with the creditors to reach a refinancing agreement, or an extrajudicial payment agreement, or to obtain adhesion to an anticipated proposal of agreement, even if the deadline referred to in Article 5bis of the Bankruptcy Law has expired.

2. The communications of art. 5bis Bankruptcy Law "pre-bankruptcy".

In essence, article 5bis of the Bankruptcy Law, popularly known as the "pre-bankruptcy", regulates the communication by the insolvent debtor to the competent Court of the beginning of negotiations with creditors to reach a refinancing agreement provided in the article 71 bis.1 and in the fourth additional Provision of the Bankruptcy Law, or to obtain adhesions to an anticipated agreement proposal (PAC).

The communication should be made before two months have elapsed since the insolvency status was known or should have been known. And, as we have already commented, the decree on the state of alarm allows the insolvent debtor to postpone said communication until two months after the end of the state of alarm.

In addition, the aforementioned article 5bis of the Bankruptcy Law allows the insolvent debtor to extend the terms to request the bankruptcy declaration without incurring any cause that could determine a negligent or guilty action on the part of the administrator / s. First, the debtor would have a period of three first months to reach a refinancing agreement, an out-of-court payment agreement or to obtain the necessary accessions for an advance agreement proposal; and, secondly, at the end of the previous period, the debtor would have an additional month of "grace" to request the declaration of insolvency, whether or not the agreements referred to in the previous term have been reached, provided that the state of insolvency.
En consecuencia, si el deudor insolvente comunica el pre-concurso tendría cuatro meses más de plazo, a los dos meses de plazo que otorga la Ley para que el deudor insolvente (art. 363.1.e. de la Ley de Sociedades de Capital en concordancia con el art. 5 de la Ley Concursal) solicite en tiempo y forma la solicitud de declaración de concurso.

Like any rule that is introduced with urgency and within the framework of a state of alarm, such as this one, it does not clearly, precisely and expressly reflect the real needs, in this case, of insolvent debtors. So well, we find that art. 43 of Royal Decree-Law 8/2020, which does not make it entirely clear whether the insolvent debtor who has benefited from the extension of the term provided for in the aforementioned art. 43, once the alarm state is over, you can choose the pre-contest as a preferred measure to present the contest in the two months following the cessation of the alarm status. In this sense, we find it adjusted to law to consider that, since the Bankruptcy Law has in its spirit and nature to safeguard the rights and benefit the professional and / or the company in bankruptcy, the state of alarm has ended and, therefore, the suspension of terms, the insolvent debtor is in the same legal

position as before the state of alarm, and therefore, may choose a direct bankruptcy or pre-bankruptcy.

Once confirmed that the state of alarm suspends the deadlines and, therefore, after its removal, the insolvent debtor, who has not done so before, may request the bankruptcy or communicate the pre-bankruptcy to the competent Court, it is necessary to clarify what it means, legally speaking, the suspension of the term due to the state of alarm. The suspension does not generate a new term but the resumption of the term at the time it was when it was suspended and, therefore, the duty to request or communicate the pre-contest, the suspensive effect being two months after the end of the status of alarm, supposes to retake the remaining term there where it was suspended.

It is importante to take this data into account because, as we mentioned at the start, it is vital to start to work on a post COVID-19 shock plan and therefore it is essential to know, where possible, the possible deadlines for filing pre-bankruptcy or bankruptcy. Furthermore, if the insolvent debtor wants to avoid the culpable qualification of the bankruptcy, which may, in its case, lead to the personal liability and/or disqualification of the administrator(s).

Given the importance of knowing the deadlines that we have, we will now explain how the suspension decreed by the state of alarm affects, differentiating between them is processed or not the communication of the pre-competition in advance of the decree of the state of alarm:

a) Pre-competition communications presented and not processed when the state of alarm was decreed:

In this case, in the context of the state of alarm, it would not be appropriate for the competent court to try to urge its authorisation, since it can hardly be considered that its omission could cause irreparable damage to the debtor, since, as we will explain later, the suspensive effects that the pre-competition has against actions that affect the debtor's assets and, now, is imposed by the current state of alarm.

b) Pre-competition communications presented and processed before the alarm state was decreed:

This case is more evident than the previous one and, as we have already mentioned, after the alarm has been declared, no procedural actions can be taken, so that their omission cannot cause irreparable damage to the debtor.

Once the far from easy task of explaining the cumbersome legal world of time limits has been completed, we will briefly summarize the most relevant and beneficial aspects of the communication of the pre-competition to the insolvent debtor, which are roughly as follows

- It prohibits the initiation of singular judicial and extrajudicial executions

- It suspends the singular judicial and extrajudicial executions that are in process at the date of the communication.

- The insolvent debtor may request the reserved nature of the communication, which may be lifted at any time. This is a very interesting question, if we take into account that, unfortunately in Spain, the pre-competition and/or the insolvency proceedings continue to have a very bad "press". Of course, this is due to the lack of knowledge about pre-award and bankruptcy proceedings, as well as the misleading use that certain debtors have made of them.

- No creditor can instigate the necessary insolvency proceedings.

- The administrative body of the company or the professional maintains full powers to manage and direct its activity.

However, it must be stressed that such measures will be taken only if and when such actions are directed against assets and/or rights that are necessary for the continuation of the applicant's business.

In this sense, it will be crucial to present a solvent pre-competition communication detailing clearly and precisely the assets required for the activity and, if applicable, the possible executions already initiated that may affect such assets, so that the competent Court may urge the suspension or halt of the same.

The effects of the pre-competition, within the time limits set by the Insolvency Law and which we have commented on above, will be maintained until any of the following circumstances occur, in roughly the same way

- To reach an agreement on refinancing as provided for in Article 71 bis.1 and in the fourth additional provision of the Bankruptcy Law

- Obtain the necessary support for the admission of an advance proposal of agreement (CAP)
- The declaration of insolvency by the insolvent debtor.

Furthermore, referring to an issue that would only affect financial creditors and which it is vital for the debtor to know in order to be able to negotiate the debt with the financial institutions, there is a legal quorum which, if complied with, obliges financial institutions that are not in favour of negotiating not to initiate or continue executions.

However, financial creditors may not initiate or continue executions that have been initiated prior to the communication of Article 3. 5 bis of the Insolvency Law, which are directed

against any assets and/or rights of the debtor's estate, i.e. they do not have to be necessary for the professional or business activity of the debtor, provided that the debtor proves that a percentage of more than 51% of the total financial liabilities have supported in writing "the commencement" of negotiations aimed at the signing of a refinancing agreement, as well as "their commitment" not to initiate or continue executions against the debtor while the negotiations are in progress.

With this, the legislator tries to generate an "environment" conducive to the consensus necessary to encourage financial institutions to reach a framework agreement on refinancing with the debtor by imposing on those financial institutions that are not interested in negotiating a period of time where they cannot damage the debtor's assets.

However, it should be borne in mind that the above provisions do not prevent secured creditors from exercising their rights in respect of the assets and rights to which their security is attached without prejudice to the fact that, once the procedure has been initiated, it will be paralysed.

In addition, in determining the best strategy for safeguarding the interests of the insolvent debtor, it is necessary to be aware that, upon notice of the pre-competition by the insolvent debtor, no further notice may be given by the same debtor within one year.

In short, we are dealing with a legal figure that, in the worst case, allows the insolvent debtor to obtain an extra period of four months to apply for bankruptcy, without incurring in a culpable and/or negligent administration. Well, the state of alarm has granted a period of "grace" that if it is well used can be essential to save the activity of the company and / or profession.

3. Express insolvency -art. 176 bis.4 of the Spanish Bankruptcy Law -.

Having analysed in the previous section the tool offered by the Insolvency Law to the insolvent debtor to avoid the declaration of bankruptcy, we will now explain a figure that is "diametrically opposed" to the figure of the pre-competition, if we consider the pre-competition, as a figure prior to the bankruptcy where the insolvent debtor seeks not to declare it, and express insolvency, as a figure where the insolvent debtor is clear that he has no realisable assets and, therefore, decides on a quick and direct formula that allows the exponential generation of liabilities and more expenses to be contained within the framework of the insolvency procedure.

In the current situation, unfortunately, there are or will be companies that the only possible solution is or will be the one provided for in Article 176 bis.4 of the Bankruptcy Law in accordance with Article 178.3 of the Bankruptcy Law -express insolvency-, which provides for companies lacking realisable assets that the bankruptcy proceedings should not be delayed in time, something that only harms the bankrupt's own creditors, increasing the costs of the process and reducing the value of the assets on whose realization their collection depends. To this end, this legal figure simplified and accelerated the bankruptcy procedure, favouring the anticipation of the liquidation, and allowing the conclusion of the bankruptcy to be expedited.

In express insolvency, the competent court issues an order that simultaneously declares and concludes the bankruptcy proceedings with the extinction of the bankrupt legal entity and its removal from the register due to the presumed insufficiency of the assets to meet the foreseeable credits against the estate.

Once this Order has become final, the Court will issue an order to cancel the registration in the Commercial Registry within a short period of time and, therefore, the full extinction of

the legal personality of the bankrupt party, in accordance with the provisions of Article 396 of the Law on Corporations.

In this type of insolvency proceedings, no insolvency administrator is appointed and, therefore, the competent court acquires special relevance by assessing and allowing the company to be extinguished immediately, with the same effects as an ordinary insolvency proceeding.

In addition to the fact that the insolvent debtor does not have sufficient realisable assets, the competent judge would analyse ex officio whether there could be any personal liability of the administrator/s due to culpable and/or negligent management. However, this last question is more theoretical than practical because rarely does the competent court have sufficient documentation for such an initial and prior assessment of whether the guilty classification of the insolvency proceedings is appropriate.

In practice, the Courts are dedicated to examining whether there are sufficient realizable assets to be able to pay at least the credits against the mass, that is, workers' salaries, taxes, bankruptcy administrator's fees, etc.

By way of example, we can mention the express insolvency of construction companies and/or developers, which the competent court decrees even though the company owns assets valued in millions of euros, all of which are encumbered with loans with mortgage guarantees for amounts greater than the current realization value of said assets. This generates that the realization of the same ones does not leave liquidity in the contest and, consequently, the competent Judge authorizes express insolvency.

Indeed, the following question arises: is it possible to bring a lawsuit against a company that has been extinguished? In this sense, we can answer with guarantees that it is because the majority of the Courts and Tribunals' jurisprudence is established, which defends the conservation of the active legitimacy of extinct companies (which can be sued), based on Articles 33, 395 and 396 of the Law on Capital Companies, which, in general terms, indicate that a limited company will only be understood to be extinct when all debts have been extinguished in their entirety and all assets have been liquidated. Inasmuch as, if the company has realizable assets, the mortgagee may file a lawsuit against the company, even if its registration has been cancelled.

Notwithstanding the foregoing, it is unquestionable that the insolvent debtor must clearly and precisely detail and prove that its actions at the head of the company have been diligent and that the insolvency situation has been generated by an objective cause, such as the Covid-19 crisis. Having said this, it is clear that no irregularities can be detected that could lead to an action for reinstatement, challenge or liability.

In this sense, it is important to be aware that we are dealing with an exceptional legal figure that can only be applied to companies, in very specific cases where they do not have assets or, if they do, it is very residual.

Furthermore, this figure is beneficial for the entrepreneur because when the insolvency is concluded at the same time as the declaration is made, the competition's qualification piece is not opened to find out if we are dealing with a guilty or fortuitous insolvency, so the administrator(s) are not disqualified from starting a new business "adventure" again.

As with the pre-bankruptcy, express insolvency is directly affected by the state of alarm with regard to deadlines, i.e. the deadline for filing has been halted and, if it has already been requested, the deadline is suspended and will be resumed two months after the end of the state of alarm.

However, the state of alarm affects the express insolvency in a special way because it makes it much easier for the company to justify and clarify the objective cause of insolvency, that is, with the current circumstances where a royal decree has forced many companies to stop their activities sine die and in the face of the obvious world economic crisis it is easier to be able to justify the situation of fortuitous, supervening and unforeseeable insolvency of the company. This question is clearly more difficult for undertakings to justify in normal market circumstances.

4. Brief conclusion.

It is more than likely that the current situation caused by the appearance of the Covid-19 and, consequently, the state of alarm will negatively affect a large number of professionals and companies, generating extremely complicated economic situations, unbearable cash flow tensions, liquidity problems, non-payments, and perhaps in some cases, the need to communicate pre-bankruptcy and/or declare bankruptcy.

Well, as we have been developing and by way of conclusion, the state of alarm has allowed the insolvent debtor to analyse his situation with a certain degree of relaxation when it comes to finding the best measure or action aimed at the survival of the business, but it should not be forgotten that if, in the end, the insolvent debtor has to "navigate" in a bankruptcy proceeding it is more than likely that the bankruptcy administrator will examine and analyse what has happened during the state of alarm, or if a diligent management has been made, or if on the contrary the professional or the company has deliberately aggravated the economic situation of the company, which could lead to a culpable qualification of the insolvency, and the consequences that this could have on the personal assets of the administrator/s.

In fact, in view of the current circumstances and repeated queries made to us by our clients on this matter, we have considered it appropriate to write this brief legal note in order to respond to these queries and to many others that have arisen along the "path" that we consider essential in order to make known how the state of alarm, on this occasion, affects the pre-bankruptcy and express bankruptcy proceedings, the effects and conclusions that we obtain from the ordinary bankruptcy proceedings being largely extensible.

Signed.
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