

Preventive restructuring frameworks in Portugal: (un)fair negotiation?

José Gonçalves Machado writes on the different games that are played within the preventive restructuring frameworks in Portugal

This brief analysis will outline the different principles that apply to and rules on negotiation and implementation for different restructuring plans under the Portuguese restructuring frameworks. The key questions are how far can contractual freedom and *par conditio creditorum* (“PCCP”) principles go and whether they can be harmonized.

The Portuguese preventive restructuring frameworks

The Portuguese preventive restructuring frameworks (“PPRF”) are negotiating tools specially designed to enable distressed and viable companies to restructure effectively and to continue business as a going concern. As negotiating tools, they have a common structure which can be divided into three phases: pre-negotiation phase, negotiation phase (including the drafting of a restructuring plan/“RP”) and conclusion (through adoption and, in some cases, court confirmation).¹

Under the Portuguese legal regime, there are three preventive restructuring tools:

- a. The Special Revitalization Process (*Processo Especial de Revitalização*/“PER”);²
- b. The Extrajudicial Business Recovery Regime (*Regime Extrajudicial de Recuperação de Empresas*/“RERE”);³ and
- c. The Guiding Principles for Extrajudicial Recovery of



Debtors (*Princípios Orientadores da Recuperação Extrajudicial de Devedores*/“Guiding Principles”).⁴

a. PER

The PER was clearly inspired by Chapter 11 of the US Bankruptcy Code. It contemplates a double procedure: an ordinary procedure and an abbreviated one (fast-track). The first is a reorganisation process in which all creditors are invited to negotiate a RP under the guidance of a judicial administrator with the supervision and confirmation of the court. The second is a hybrid procedure, since the RP is privately negotiated and approved before being subject to confirmation by the court (to bind “affected parties”).⁵ For these purposes, the negotiation phase can take place

using the RERE or an *ad-hoc* negotiation tool.

b. RERE

The RERE is an out-of-court procedure, designed to negotiate an RP under specific rules. The negotiation procedure is based on an initial protocol signed by the debtor and some creditors. In principle, the RP is contractual, only binding parties voluntarily agreeing. However, under the fast-track PER, parties are allowed to submit the plan to court to bind affected and dissenting parties. Subject to all necessary requirements being fulfilled, the court will confirm the plan and impose it on non-consenting affected parties.

c. Guiding principles

The Guiding Principles were developed based on international best practice, notably those in the



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Negotiating an ad-hoc RP under Guiding Principles allows the parties to freely set the terms of the negotiation and to reach an agreement quickly

INSOL Statement of Principles for a Global Approach to Multi-Creditor Workouts. The Guiding Principles were introduced to enhance negotiations in out-of-court and informal and *ad-hoc* restructuring procedures, thus providing the debtor and creditors with an accessible legal framework when negotiations either involve all creditors or only the main creditors. Negotiating parties do not have to follow a specific procedure, but are subject to certain duties of conduct, as in any contract negotiation.⁶ The Guiding Principles apply to negotiations taking place under the PER and the RERE.

Pros and cons of different games

Negotiating an *ad-hoc* RP under Guiding Principles allows the parties to freely set the terms of the negotiation and to reach an agreement quickly. It is appropriate in cases involving a small number of creditors, provided it can also avoid insolvency. Otherwise, the preference may be for a legal mechanism offering debtors and

creditors alike enhanced protection against insolvency.

In that event, RERE and PER are the negotiating tools normally used. The RERE has three obvious advantages:

- (i) It is usually confidential;⁷
- (ii) Under the PER, it provides important tax benefits;⁸ and
- (iii) Also, if the debtor is declared insolvent, the agreement providing for new financing cannot be declared void.⁹

Due to its voluntary nature, RERE does not suspend or prevent enforcement actions without the consent of those creditors. Similarly, the debtor can only obtain a stay if insolvency has not been declared and the petitioning creditor enters the negotiations.¹⁰

A stay of individual enforcement actions, alongside with the need to bind dissenting affected parties are two of the main reasons for a debtor to opt for PER, subjecting the RP to judicial control and confirmation. In this regard, RPs will be confirmed by the court if certain conditions are met, namely:

- (i) if it complies with the viability

- and the best interest of creditors tests; and
- (ii) it respects the *par conditio creditorum* principle (“PCCP”).

RPs can also be confirmed through a cross-class cram-down mechanism using the relative priority rule (“RPR”). From a practical point of view, The PCCP and the RPR may raise serious problems because they put the treatment of affected parties into perspective, in such a way as to avoid unfair treatment for some, without justifiable (or fair) reasons.¹¹

Often banks (and other strong creditors) impose certain conditions which are very difficult to accept under the PER confirmation rules. It may not be clear whether the restructuring measures infringe the PCCP and the cross-class cram-down rules (where applicable). This gives rise to legal uncertainty that debtors genuinely interested in reorganization want to avoid. As such, the debtor may face the following dilemma:

“either I give a special advantage to a certain creditor(s) through a confidential agreement, or the RP negotiated under the PER will fail and the company will probably be declared insolvent.”

To solve this dilemma, debtors are tempted to play different games (RERE and PER) to achieve the same goal. This is often done by using RERE together with the PER, taking advantage of the distinct protections each offers.

Fundamentals and limits for a competing and confidential plan

To a certain extent, the Portuguese legislator has taken this problem into account. If an RP negotiated under the RERE is signed by creditors representing the required majorities, the debtor can initiate a PER to obtain judicial confirmation of the RP.¹² However, in this case, the RP will no longer be confidential and must comply with the PER

approval criteria. Thus, the question is whether it is possible to negotiate one plan in the RERE and another in the PER, so that the first remains confidential as a type of “side agreement”? The answer is not obvious.

It is true that the debtor cannot submit more than one negotiation process to the RERE at the same time.¹³ However, once RERE proceedings have ended, the debtor is free to initiate a new RERE with the same or different creditors, as long as it does not breach the RP previously agreed.¹⁴ Likewise, the PER also allows successive applications, provided there is a two-year gap, unless new circumstances arise which justify a new RP.¹⁵

Moreover, the question arises as to whether the hypothesis in Article 194, n. 3 of the CIRE, (safeguarding the PCCP and limiting freedom of contract) applies to PER. If the answer is affirmative, any agreement by which the debtor grants advantages (not provided for in the RP) to a creditor in return for a certain conduct (namely regarding voting rights or not taking part in the negotiations at all) within the scope of the PER is void. If the answer is negative, or if there are some limits to that prohibition, then it may be legal to enter into a confidential agreement that confers a certain advantage on one or more creditors.

Therefore, does this prohibition apply to the PER (and, if so, to what extent)?

In favour, it could be said that, on the basis of the PCCP, Article 194 of the CIRE applies to the PER.¹⁶ The principle of good faith could also be called into question, especially the debtor’s duties of information, transparency and loyalty. The parties may not be acting in good faith by not revealing the existence of a parallel agreement with a particular creditor and taking advantage of:

- (i) the information obtained and shared in the PER; and
- (ii) the content of its RP (as a way of circumventing the

confirmation rules).

Even if all affected parties are better off and insolvency is avoided, the PCCP/RPR and the good faith principles will be violated.

To the contrary, it could be argued that PER applies only in pre-insolvency cases, which are substantially different from insolvency cases. In a pre-insolvency situation, the debtor’s freedom of contract cannot be impacted by the PCCP. Prior to insolvency, the debtor is not yet obliged to grant total priority to the interests of creditors in the same way as in insolvency.

Thus, the principle of freedom of contract could justify a certain mitigation of the PCCP, if the debtor is not insolvent. The primacy of preventive restructuring could also be invoked in this regard. At the end of the day, an RP negotiated outside the PER may be necessary to keep the company in business and to satisfy the best-interest-of-creditors test. In fact, according to Directive 2019/1023/EU, preventive restructuring frameworks may consist of one or more procedures, measures or provisions, some of which may take place out of court, without prejudice to any other restructuring frameworks under national law.¹⁷ From this perspective, it can also be said that PER applies (only) to those who are affected by the RP. Any other RP negotiated outside the PER takes on a life of its own.

In addition, not all hypotheses may be covered by that prohibition.¹⁸ The *quid pro quo* may not exist or may be difficult to demonstrate, where a creditor contemplated in the RERE refrains from participating in the PER. Furthermore, any confidential RP negotiated under the RERE cannot be called into question. In fact, the advantage granted through a confidential RP may not even violate the PCCP, if circumstances allow for more favourable treatment. This can be justified by the claims ranking and/or by the fact that creditors have provided necessary financial

support. However, anticipating the opposition from dissenting creditors and fearing the uncertainty about the outcome of the PER, the debtor usually prefers to play it safe.

Conclusion

In sum, if the debtor is not insolvent and the confidential agreement is necessary to stay in business and helps a debtor to comply with the best interest of creditors affected by the plan negotiated in the PER, then there is reason to give advantage to some creditors. The assumption may even be made that the agreement was negotiated in good faith. In that case, the principle of freedom of contract should prevail over the PCCP. If any of these conditions is not met, Article 194, no. 3 of the CIRE will apply. ■

Footnotes:

- 1 On pre-insolvency proceedings, see Nicolaes Tollenaar, *Pre-Insolvency Proceedings: A Normative Foundation and Framework* (OUP, 2019), 38-80.
- 2 Articles 17-A to 17-J, Portuguese Insolvency Act (*Código de Insolvência e da Recuperação de Empresas* (“CIRE”).
- 3 Law no. 8/2018 of 2 March.
- 4 Council of Ministers Resolution no. 43/2011 of 25th October. See José Gonçalves Machado, *Instrumentos de Recuperação de Empresas Pré-insolventes: Princípios Orientadores, RERE e PER* (Almedina, 2023).
- 5 See Article 4(2), Directive 2019/1023/EU.
- 6 See Nuno Manuel Pinto Oliveira, “Entre código da insolvência e ‘Princípios Orientadores’: um dever de (re)negociação?” *Revista da Ordem dos Advogados*, Ano 71, Vol. II/III, 2012, 677-689.
- 7 Articles 8 and 21, RERE.
- 8 *Ibid.*, Article 27.
- 9 *Ibid.*, Article 28.
- 10 *Ibid.*, Article 11.
- 11 For the concepts of ‘just and equitable’ or ‘fair’ in restructuring law, especially in a cramdown system, see Riz Mokhal *et al.*, “Cramdown: A Conceptual Framework” (28 October 2024), available via SSRN at: <https://ssrn.com/abstract=4990828>
- 12 Article 29, RERE.
- 13 *Ibid.*, Article 18 no. 1.
- 14 *Ibid.*, Article 18 no. 2.
- 15 Articles 17-F, no. 14 and 17-G, no. 8, CIRE.
- 16 *Ibid.*, Articles 17-F, no. 7.
- 17 Article 4, no. 5, Directive 2019/1023/EU.
- 18 See Luís Carvalho Fernandes and João Labareda, *Código da Insolvência e da Recuperação de Empresas Anotado* (3rd edn) (QuidJuris, 2015), 714.



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