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On Saturday, 14 March 2020, the declaration of the state of alarm was published in the Official State Bulletin (BOE) as a response to the public health emergency caused by COVID-19.

The declaration of a state of alarm has a series of consequences that affect the national territory. To this end, on Wednesday 18 March 2020, Royal Decree-law 8/2020 of 17 March on extraordinary urgent measures to deal with the economic and social impact of COVID-19 (the “**RDL 8/2020**”) was published in the BOE. This regulation provides for a series of measures affecting both the social and economic spheres.

The purpose of this briefing is to analyse the main developments in the area of pre-insolvency and insolvency following the publication of RDL 8/2020.

I. OBLIGATION TO FILE FOR INSOLVENCY

A. Recognition of insolvency

The debtor must file for insolvency within two months of the date on which they knew of or should have known of their state of insolvency¹. The state of insolvency implies that the debtor cannot regularly fulfil their obligations. The law also establishes several presumptions in which the debtor has been aware of this situation².

Notwithstanding the foregoing, for the purposes of knowing their financial situation and, if they are close to insolvency, the debtor should carry out an analysis of existing liquidity, as well as its short term estimates to know whether it will be able to continue to comply with its obligations.

B. Petition for Insolvency

RDL 8/2020, while the state of alarm is in force, has temporarily suspended the duty of individuals or legal entities that are in a state of insolvency to file for insolvency. Under normal conditions, as indicated above, the debtor must file the petition for the declaration of insolvency within two months from the date on which they knew of or should have known of their state of insolvency.

¹ Article 5.1 of Law 22/2003, of 9 July, on Insolvency (the “**LC**”)

² Article 5.2 of the LC: (i) insufficient free assets for payment in the framework of pending enforcements; (ii) general (not total) failure of the debtor's with regard to their payment obligations. There is no general failure with a slight delay or a sporadic or eventual non-payment; (iii) existence of seizures due to pending enforcements affecting the debtor's estate in a general way; (iv) a hasty or ruinous seizure or liquidation of assets, i.e. the assets disappear when, due to the action of the debtor itself or any person acting on its behalf, the assets cease to belong to that debtor. As to hasty or ruinous liquidation, this refers to instances where the sale is made with particular celerity and entails a serious loss of value; (v) failure to comply with the following obligations: (a) tax contributions due during the previous three months; (b) social security contributions and other collection items during the previous three months; and (c) payment of salaries, indemnities, and other remuneration of the labor relations during the last three monthly payments.

The suspension of this duty has various implications depending on the time at which the debtor's insolvency occurred. These effects must be analysed in the case of each company taking into account the time of occurrence of the insolvency with respect to the declaration of the state of alarm.

Regarding the duty to file for insolvency by those debtors who, prior to the declaration of the state of alarm, had made the communication of Article 5 *bis* of the LC, RDL 8/2020 also establishes the suspension of the duty to file a petition for the declaration of insolvency during the previous month. This duty will be resumed when the state of alarm ceases to be in force.

C. Involuntary Insolvency

Creditors are entitled to petition for the declaration of the debtor's insolvency³. However, RDL 8/2020 provides that if, during the period of the state of alarm, and up to two months after the end of the state of alarm, the courts will reject any petition for involuntary insolvency proceedings.

Two months after the end of the state of alarm, even if a petition for the declaration of involuntary insolvency has been submitted, RDL 8/2020 provides that courts will give preference to the petition for the declaration of voluntary insolvency submitted by the debtor, even if it is later than the petition for involuntary insolvency submitted by a creditor.

D. 5 *bis* Notification

Under normal circumstances, the debtor has the option of submitting the notification of Article 5 *bis* of the LC indicating the existence of negotiations to reach an out-of-court refinancing agreement (to be subsequently approved, if necessary) or to obtain the endorsement of a proposal of early agreement. Once this notification has been presented, the debtor has a period of three months to attempt to reach one of the aforementioned agreements. If this does not occur, within the following working month, the debtor must apply for an arrangement with creditors if it is still in a situation of insolvency.

The declaration of the state of alarm has led to the suspension of scheduled legal proceedings and procedural deadlines throughout the national territory. In this regard, the Permanent Commission of the General Council of the Judiciary has agreed that as long as the state of alarm is ongoing, the filing of procedural documents is not required. The presentation of these applications will be limited to those that have as their sole and exclusive object procedural actions declared urgent and not subject to delay by the instructions and agreements of the judiciary's governing body.

During the state of alarm, there is scope for a certain degree of interpretation of the non-applicability of Article 5 *bis* of the LC notification. Such notification must always be made with caution and in accordance with the specific circumstances.

³ Article 7a of the LC.

E. Petition for approval of refinancing agreements

If the debtor has obtained sufficient support from their creditors⁴, they can apply for judicial approval of the refinancing agreement reached and, if necessary, the extension of the terms granted to the dissenting creditors.

As we have seen, the resolution of the Permanent Commission of the General Council of the Judiciary establishes the suspension of scheduled judicial actions and procedural terms throughout the national territory. However, the suspension of procedural terms does not prevent the adoption of those judicial actions "*that are necessary to avoid irreparable damage to the rights and legitimate interests of the parties in the proceedings*".

Consequently, it may be argued that the request for approval of the refinancing agreement is a necessary action, which, if not carried out, would cause irreparable damage both to the debtor and to the creditors themselves.

II. LIABILITY OF DIRECTORS IN THE EVENT OF THE EXISTENCE OF GROUNDS FOR DISSOLUTION OF THE COMPANY OR FAILURE TO PETITION FOR INSOLVENCY

RDL 8/2020 has amended the liability regime of directors in two areas: (i) the corporate area; and (ii) the area of insolvency.

In the corporate context, the obligation of the directors to call a general shareholders' meeting when there is a legal or statutory cause for the dissolution of the company has been suspended. Thus, the statutory period in which the administrative body must convene the general shareholders' meeting to adopt the resolution to dissolve the company or the resolutions that have the purpose of nullifying the grounds, is suspended until the end of the state of alarm.

In view of the above, RDL 8/2020 also establishes that the directors will not be liable for the debts incurred by the company during the state of alarm.

With regard to the area of insolvency, although the delay in the petition for insolvency of a debtor which is a legal entity may involve the liability of the directors in the framework of the insolvency classification proceedings, RDL 8/2020 provides that, while the state of alarm is in force, a debtor who is in a state of insolvency will not have the duty to petition for the declaration of insolvency (*see* section I.B above). Consequently, it could be argued, subject to the aforementioned precautions and the specific case, that there would be issues in matters of director liability for delay in the petition for insolvency.

III. ENFORCEMENT AGAINST THE DEBTOR'S ASSETS

Regarding judicial enforcements, in circumstances where the proceedings are suspended due to the state of alarm, it is only possible to commence or resume those proceedings that have been paused if

⁴ Holders of financial debt liabilities.

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the suspension would cause irreparable damage to the creditor, which will be declared by the relevant judicial body.

In relation to extrajudicial enforcements, such as notarial enforcements or enforcements of financial guarantees⁵, they may be considered to be limited to urgent matters.

During the state of alarm, notary offices will not close in circumstances where they are considered public offices, but, in view of the restrictions on freedom of movement established in Royal Decree 463/2020, of 14 March, which declares the state of alarm, the Permanent Commission of the General Council of Notaries has established that notarial intervention is exceptional and that it must only address actions of an urgent nature (arising, for example, from the existence of peremptory deadlines or other matters which may result in financial loss or damage to the person concerned).

In this regard, it should be noted that notary public office workers do not fall within the subjective scope of reimbursable paid leave established in Royal Decree-law 10/2020 of 29 March, which regulates reimbursable paid leave for employees who do not provide essential services, in order to reduce population mobility in the context of the fight against COVID-19, given that they are considered to be workers who provide services in sectors classified as essential⁶.

The information contained in this Information Briefing is of a general nature and does not constitute legal advice. This document was prepared on 2 April 2020 and Pérez-Llorca does not assume any commitment to update or revise its contents.

⁵ Referred to in Royal Decree-law 5/2005 of 11 March on urgent reforms to boost productivity and improve public procurement.

⁶ Paragraph 17 of Annex I to Royal Decree-law 10/2020 of 29 March regulating reimbursable paid leave for employees not providing essential services, in order to reduce population mobility in the context of the fight against COVID-19.