Baker McKenzie.

Global Restructuring & Insolvency Guide

Colombia

Overview and Introduction

On 27 December 2006, the Colombian Congress enacted a complete insolvency regime for companies (Law No. 1116 of 2006 ("**Law No. 1116**"), which came into force on 28 June 2007. The insolvency regime governs domestic reorganisation and liquidation proceedings and also includes a chapter that provides coordination mechanisms within transnational insolvency proceedings.

The Colombian insolvency regime, applicable to companies and business groups, has two major objectives: on one side, the regulation of the proceedings that ensure creditors' protection; and on the other, monitoring and making it possible to recover and preserve companies that are still viable. The regime is based on principles aiming to guarantee that the proceedings will cover all of the debtors' assets. These principles are also oriented to ensure equality between debtors and creditors and the respect of fundamental rights. The insolvency regime enables debtors to enter into a long-term personalised payment agreement with their creditors, giving the company a chance to recover and pursue its activity.

The first amendment to Law No. 1116 was made by Law No. 1429, enacted on 29 December 2010. Law No. 1429 introduced changes to Law No. 1116 that aimed to make insolvency proceedings more agile and flexible, for example, by reducing the eligibility requirements for these proceedings, and by admitting only documentary evidence to challenge the inventory of the credits.

Since May 2011, the Colombian insolvency regime has included, through the Decree 1749 of 2011, provisions regarding the insolvency of business groups. These provisions are oriented to the transparency and coordination of insolvency proceedings involving two or more companies of the same business group. According to this decree, a business group is an integrated set of individuals, companies, trusts, or entities of any other nature that are involved in economic activities, linked or related to each other by the fact of being controlled or subordinated, or because most of their equity is owned or under the administration of the same individual or legal entity.

On 1 January 2016, the new General Procedural Code was enacted. This regulation includes a set of provisions governing insolvency proceedings for individuals not devoted to commercial activities.

Law No. 1676, enacted in 2013 (Law of secured movable assets – *Ley de garantías mobiliarias*), introduced some modifications to Law No. 1116. According to this law, creditors who constituted guarantees (i.e. security interests) over the debtor's moveable assets can enforce the guarantees to obtain payment of the debt, even if the debtor is admitted into reorganisation. However, the possibility of enforcing these guarantees applies only to the assets that are not necessary for the development of the economic activity of the debtor. If the debtor enters into liquidation proceedings, and the guarantees over the debtor's assets are registered, the guaranteed goods can be excluded from the group of liquidated assets in order to pay the debt, as long as there are no outstanding labour credits.

The above-mentioned is an exception to the rule established in Law No. 1116, according to which it is not permitted to start a collection proceeding against the debtor once the reorganisation proceeding starts or to pay the debt with an asset from the debtor unless the asset is awarded as a consequence of a liquidation proceeding.

The creditors that hold movable guarantees over the debtor's assets rank in the second class of credits (see "Creditor Ranking" below).

Applicable Legislation

Companies' insolvency regime is regulated by Law No. 1116, modified by Law No. 1429. Insolvency of business groups is regulated by Decree 1749 of 2011. However, these special regimes are supported by other general regulations. Some of the most important provisions regarding these matters are the Colombian Code of Commerce, and Law Nos. 222 of 1995 and No. 550 of 1999, which contain provisions applicable to the insolvency regime.

Individuals who are not engaged in commercial activities have an independent regime. The General Procedural Code provides the proceeding to be followed in this case. The structure of this proceeding is similar to the one provided for companies.

Insolvency Regime for Individuals Not Engaged in Commercial Activities

According to article 538 of the General Code of Procedure, any individual who is not engaged in commercial activities and is involved in a payment suspension situation (understood in Colombian legislation as a person's inability to pay two or more creditors for more than 90 days or when acting as a defendant in one or more collection proceedings) is entitled to request the commencement of an insolvency proceeding according to the provisions established in this code.

These insolvency proceedings, meaning the debt negotiation and validation of agreements, have to be carried out before a Conciliator member of any Conciliation Centre of the domicile of the debtor, duly authorised by the Ministry of Justice (*Ministerio de Justicia*), including Public Notaries. If any controversy within the proceedings is out of the scope of the competence of the Conciliator, the proceedings are to be carried before the Civil Municipal Court of the domicile of the debtor. This court is also competent whenever the payment agreement reached within the insolvency proceedings is challenged and during the liquidation process.

Request for the Negotiation of the Debt

According to article 539 of the General Code of Procedure, the insolvency proceeding starts with the debtor filing a request for the negotiation of the debt. In this request, the debtor explains the circumstances that led to the payment suspension situation and includes a proposal for the negotiation of the debts. The proposal has to be clear, objective and consistent with the debtor's current economic situation and credit record. The request for the negotiation of the debt includes, among other things, the following information:

- A complete list of all the creditors, presented in the order provided by the Civil Code, the nature and amount of each debt, the date on which the debt was incurred and the documents in which it is supported;

- A complete list of all the assets, including those that are located in foreign countries, indicating if there are any encumbrances or seizure measures over the assets;

- A complete list of all pending judicial and administrative procedures in which the debtor is involved;

- A certificate given by the debtor's employer with information about the incomes or, if the debtor is an independent worker, a declaration containing this information; and

- The amount of resources available for the payment of the obligations, discounting expenses necessary for the subsistence of the debtor and of persons depending on him, if any.

Negotiation of the Debt

Once the request is accepted, the Conciliator in charge starts the negotiation of the debt. The proceedings for the negotiation of the debt take place within a 60-day period starting on the date of the acceptance of the request. This term can be extended for 30 additional days upon request from the debtor or from any of the creditors included in the final list of credits.

The negotiation of the debt takes place at a hearing scheduled within 20 days after the acceptance of the request. During this hearing, the Conciliator indicates the amount of each debt and the value of the assets as reported by the debtor. At this point, the creditors are allowed to request clarifications regarding their own credit or regarding any other credit submitted for approval, and are entitled to file objections. If no objections are filed, the credits and assets detailed by the Conciliator at the beginning of the hearing are considered as definitive and the negotiation to consider and accept the payment proposal filed by the debtor with the request is formally opened.

If objections are filed, the Conciliator seeks to reach an agreement between the debtor and its creditors and is entitled to request the submission of evidence in order to resolve the objections and differences between the parties. If no agreement is reached, the Conciliator will declare the conciliation failed and will send the evidence and written objections to the competent judge.

If an agreement is reached, it is subject to the following rules:

- It has to be formalised within 60 or 90 days following the date in which the request was accepted;
- It has to be approved by two or more creditors representing at least 50% of the total value of the debt and must be expressly accepted by the debtor;
- It must include all the creditors prior to the acceptance of the request;
- It must respect the creditor priority rules established by Colombian laws;
- If the agreement involves legal acts affecting property subject to registration, a copy of the agreement shall be registered before the competent authority;
- In any case, the payment agreement will become a novation of the obligations unless there is an agreement between the debtor and each creditor involved in the proceeding; and
- The credits must be paid within five years from the date the agreement was subscribed.

Once the agreement has been approved, it can be modified upon request of the debtor or of the creditors that represent at least one-fourth of the value of the unpaid debts.

The approval of the payment agreement suspends all collection proceedings against the debtor. These proceedings will remain suspended until the total fulfilment or failure of the agreement is verified. The agreement constitutes a collection title, i.e. a document containing a clear, express and enforceable obligation. Ordinarily, a creditor may initiate collection proceedings in order to obtain the fulfilment of the obligation contained in a collection title. However, a payment agreement will not be enforceable, and creditors will not be permitted to file a collection proceeding, until the Conciliator officially declares the breach of the agreement.

When the undertakings contained in the agreement are not fulfilled, the debtor or any of the creditors are entitled to request the scheduling of a new hearing to discuss possible modifications to the agreement. If no modifications are agreed, or if the debtor does not comply with the new undertakings as agreed, the Conciliator will declare the failure of the agreement. As a consequence, the pending judicial collection proceedings against the debtor that were suspended will be resumed.

Among the most important provisions introduced by the General Procedural Code are those that provide for the recognition of private agreements and the liquidation of existing assets. The recognition of private agreements, governed by article 562 of the above-mentioned code, allows individuals not devoted to commercial activities to structure a payment agreement with two or more creditors that represent at least 60% of the total debt and to present the agreement before an authority to be recognized as valid. This private agreement has the same beneficial effects as a payment agreement negotiated before a Conciliator.

If these negotiation tools fail, or if the commitments adopted therein are not fulfilled by the debtor, it is possible to file for a liquidation proceeding before Civil Courts. This proceeding is also regulated by the General Procedural Code and its purpose is to reach an agreement to liquidate available assets

and pay the pending obligations. If no agreement is reached, the judge will hold a hearing to adjudicate assets to pay the existing debts. This is the last step of the insolvency proceeding for individuals not devoted to commercial activities.

Companies' Insolvency Regime

Law No. 1116 of 2006

This provision regulates both reorganisation and liquidation proceedings for individuals, companies and institutions dedicated exclusively to commercial activities in Colombia.

Acknowledged Entities

Law No. 1116 regulates reorganisation and liquidation proceedings regarding the following persons:

- Commerce-involved individuals and companies;
- Mixed economy companies;
- Branches of any foreign company;
- Trust assets regulated by national laws and focused on business; and
- Other entities covered by the provisions of Law No. 1116.

Some excluded entities are:

- Stock market entities;
- Entities supervised by the financial regulator;
- Public service entities; and
- Territorial entities and decentralised entities.

The above-mentioned entities will follow a different proceeding and will not be sheltered by the benefits and opportunities afforded by this special regime.

Competent Authorities

The competent authority may vary depending on the nature of the entity that is requesting the reorganisation or liquidation proceeding. The Superintendency of Corporations (*Superintendencia de Sociedades*) is, by virtue of Decree No. 2179 of 2007 and Law No. 1116, the competent authority tasked to carry out reorganisation and liquidation proceedings regarding companies, industrial economy corporations, branches of any foreign company and commerce-involved individuals. For other cases, i.e. reorganisation and liquidation of trust assets, the competent authority will be the Civil Circuit Court or as determined within special regulations.

Legal Requirements to Initiate These Proceedings

According to Law No. 1116, there are specific grounds for a debtor to request admission to an insolvency proceeding, whether as a reorganisation or as a liquidation proceeding.

However, in principle,[1] any of the above-mentioned proceedings require that the debtor is in a payment suspension situation (understood in Colombian legislation as the inability to pay two or more creditors for more than 90 days or when acting as a defendant in one or more collecting proceedings)

[1] In principle because the liquidation proceeding may begin due to the breach of the reorganisation agreement, in which case the payment suspension situation will not be required.

or that, due to particular circumstances of the market or to internal difficulties of the company, it is foreseeable that the debtor will not be able to pay for the obligations it has acquired.

Reorganisation Proceeding

The reorganisation proceeding aims to preserve companies which are still financially viable through an agreement with its creditors, so that all credits are included and paid as the insolvent company recovers financially. When no agreement is accomplished or when the insolvent company does not fulfil the agreement, the liquidation process starts immediately.

The reorganisation proceeding protects the debtor from an inevitable bankruptcy situation. The reorganisation process is collective, which means that all creditors are summoned to submit their credits and participate in the decision-making process. An automatic stay applies. Creditors will not be entitled to carry out collection proceedings against the debtor to collect the debts that were incurred prior to the beginning of the reorganisation proceeding, as these debts are part of the reorganisation proceeding and may only be satisfied therein.

Among the specific requirements a debtor must comply with in order to be admitted to a reorganisation proceeding is the obligation of maintaining accounting records according to the legal provisions and not having pending social security obligations.

A promoter is appointed to guide the proceeding and perform technical financial duties. The promoter, among other duties, proposes a payment agreement according to the projected cash flow of the company.

Pursuant to Law No. 1116, whenever a reorganisation agreement is approved by a plurality of creditors representing at least the absolute majority of the votes cast defined proportionally according to the value of each debt, the decision must be confirmed by the competent authority, either the Superintendency of Corporations or the civil court, during a special hearing. The competent authority may give its approval to the reorganisation agreement or suspend the hearing and require the agreement to be amended. If the authority does not approve the agreement, it must order the dissolution of the company and the liquidation of its assets for distribution among the creditors, according to the debt priorities established by law.

Breach of the agreement on the terms confirmed by the authority, and the non-fulfilment of any social security or other administration obligation[2] during the period the agreement is in force, will have the same consequence as the non-approval of the agreement.

Whenever the debtor or a creditor denounces the failure to comply with the reorganisation agreement or the administration obligations, the authority will set a date for a unique special hearing to apply measures to solve the situation. If this contingency is not settled within the hearing, the judge will declare the termination of the agreement and continue to a liquidation proceeding.

Creditor Raking

Not all creditors are treated equally. Much like other insolvency proceedings, Colombian legislation establishes a ranking for creditors within a reorganisation or liquidation process. The Colombian Civil Code (articles 2488 to 2511) establishes the preference and order in which creditors must be paid:

- The first class to be paid corresponds to employment-related obligations and special tax-related obligations.
- The second class includes creditors who have a pledge constituted in their favour.
- Creditors who have a mortgage belong in the third class.
- Other tax-related obligations and strategic suppliers to the business belong in the fourth class.

[2] These obligations refer to the expenses incurred in the reorganisation proceeding and any other obligation incurred by the debtor after the initiation of the reorganisation proceeding.

- Finally, all other creditors who have a title such as a promissory note or contract with no guarantees are part of the fifth class and are paid last.

- Credits with related companies are subordinated and paid after the fifth class.

External creditors are paid before paying the internal debt, i.e. before returning equity to shareholders. Furthermore, if a shareholder has not paid its equity, or social liability is extended beyond such contributions (by law or by the company's bylaws), the liquidator within a liquidation process may start a process against that shareholder to collect the owed sum in order to pay external creditors.

Some credits are legally delayed, which means they are only paid when all the others have been fulfilled. These debts include those owed to persons specially related to the debtor. The law defines "specially related" as “corporations related among them as parent companies, subsidiaries or branches, or the company and its administrators, statutory auditors and attorneys at law in some cases.” These obligations will not be delayed if they arise from new resources offered to the company after its admission into the insolvency process.

Order of the Proceedings

Request for admission. In order for a company to be admitted into a reorganisation process, it must submit all relevant financial information, including information about assets and credits, a projected cash flow to pay all pending obligations and a business reorganisation plan. Creditors may also request the admission. The request must include:

- A complete list of all the creditors, presented in the order set forth by the Civil Code, the nature and amount of each debt, the date on which the debt was incurred and the documents in which it is supported.

- A complete list of all the assets, including those that are located in foreign countries, indicating if there are any encumbrances or seizure measures over the assets.

- A complete list of all pending judicial and administrative procedures in which the debtor is involved.

Decision to admit the company. This first decision of the Superintendency of Corporations is to open the reorganisation proceeding. With this decision, the Superintendency orders the company to make the required publicity, orders the registration of the decision in the corresponding Chamber of Commerce and may order injunctive relief.

Submission of the credits. Whoever is interested may present relevant information and evidence for its credit to be taken into account within the proceeding. This is the opportunity to make sure the information related to the credit is included in the record and the credit is taken into account within the process.

The project of ranking and qualification of credits and rights to vote. With the information provided by the company, the promoter presents a project to rank and qualify the pending credits and rights to vote.

Objections. Creditors are entitled to challenge the project of ranking and qualification if they consider that it does not correctly reflect their credit or rights to vote.

Conciliation hearing. If the objections presented are not resolved by a direct arrangement between the company and the creditors, the Superintendency will summon a conciliation hearing seeking for an agreement. Finalizing this hearing, the Superintendency will adopt a final version of the ranking and qualification of credits and rights to vote and will determine the timeframe to present the reorganisation agreement.

Reorganisation agreement. The reorganisation agreement must be subscribed within the four months following the conciliation hearing. Taking into account the cash flow of the company, the promoter must present the reorganisation agreement approved by the majority of votes (50% plus one vote). The reorganisation agreement must include all pending credits as recognised in the ranking and

qualification and must respect the creditor ranking and preferences. If the reorganisation agreement is not presented in time, the Superintendency will designate a liquidator.

Verification hearing. After approving the reorganisation agreement, the Superintendency will summon and carry out a hearing to receive observations and validate its legality. Annual meetings will be scheduled to review and verify the fulfilment of the agreement.

Judicial Liquidation Proceeding

This special regime refers to the proceeding by means of which the authorised judicial authority disposes of the debtor's assets in order to transform them into money and hence, ensure the fulfilment of the economic obligations contracted by the debtor by paying the creditors. This process of liquidating the assets may take place by direct sale or by private auction, each following specific rules oriented to protect the assets and guarantee that a higher profit is taken for the proceeding.

After the auction or sale is over, the proceeds are distributed among the creditors. In cases where it is not possible to sell all the available assets, the law provides a mechanism for the remaining assets to be distributed among the creditors, either in respect of the payment priority or via a judicial decision.

A judicial liquidation process may be initiated as a consequence of the failure of a reorganisation agreement in accordance with the terms of Law No. 1116 or whenever there is cause for an immediate judicial liquidation as stipulated by Colombian law.[3]

Whenever a company or individual starts a judicial liquidation proceeding, the contracts entered into by the company or individual will be automatically terminated, except those that are necessary to preserve the debtor's assets, or as authorised by the competent authority trying the proceeding.

The liquidation proceeding will end with the final liquidation of the debtor's assets or with a reorganisation agreement. The Colombian insolvency regime gives a last chance to the debtor and its creditors to reach a payment agreement, even if the liquidation proceeding is already in course. In fact, once the inventory of all the assets and the votes cast have been approved – prior to the commencement of the sales – the opportunity to try to reach a new reorganisation agreement can be requested.[4] If the request is accepted, the liquidation proceeding will be suspended until an agreement is reached. If no agreement is reached, the suspension of the proceeding will be lifted and the liquidation will continue.

The liquidation proceeding concludes with the dissolution of the company. If the debtor is a commerce-involved individual whose bad faith or intent to defraud is demonstrated, the judicial authority trying the proceeding may prohibit the individual from undertaking commercial activities for up to 10 years.

Out-of-Court Mechanisms

When agreed to by the debtor, insolvency law allows a group of creditors representing more than half of the amount to be claimed in the possible reorganisation or liquidation proceeding to execute a written extrajudicial agreement that will have the same effect as a reorganisation agreement. This agreement is valid *per se*. However, the parties may ask the authority that would have been competent to preside over the reorganisation proceeding to initiate a validation procedure to verify that the agreement respects the following matters:

- Correct percentages required to endorse the agreement;
- Confirmation that the negotiations were held under every publicity requirement and that every creditor was notified thereof;

---

3 These causes may vary from the will of the stockholders of the company for external reasons, such as the decision of a competent authority.

4 The Colombian regime provides that the liquidator or at least 35% of the creditors voting may request a new chance to conclude a reorganisation agreement.

- Confirmation that the agreement grants the same recognition to every creditor depending on the quality of its credit;

- The exclusion of any illegal or abusive clause in the agreement; and

- Fulfilment of every legal requirement.

If the competent authority validates the extrajudicial agreement, it will have the same effect as an agreement reached within a reorganisation proceeding. Similarly, if an extrajudicial agreement that has been validated is breached, the rules applicable to a breach of an agreement reached within a reorganisation proceeding would apply.

Business Groups Insolvency Regime

Decree 1749 of 2011

This provision regulates both reorganisation and liquidation proceedings for business groups in Colombia.

Acknowledged Entities

According to Decree 1749 of 2011, a business group is an integrated set of individuals, companies, trusts, or entities of any other nature that are involved in economic activities, linked or related to each other by the fact of being controlled or subordinated, or because most of their capital is owned or under the administration of the same individual or legal entity.

Competent Authorities

The Superintendencies of Corporations and the Civil Courts are the competent authorities tasked to carry out reorganisation and liquidation proceedings regarding business groups. The Superintendency of Corporations is competent whenever any of the companies or members of the group are subject to its control.

Legal Requirements to Initiate These Proceedings

The request to initiate the reorganisation or liquidation proceedings of a business group can be filed by two or more of the group members as long as none of the petitioners are excluded from the insolvency regime according to Law No. 1116.

The request should also respect all the requirements set forth in Law No. 1116. In addition, the existence of the business group must be demonstrated.

Reorganisation Proceeding

The reorganisation proceeding may be carried out separately for each member as a debtor or jointly for all the members upon decision of the Superintendency of Corporations or upon request of any member of the group. The creditors of any of the members against which an insolvency proceeding has already started may also request for the proceeding to be carried out jointly.

The reorganisation proceeding should respect the identity of each one of the members of the group, unless a judicial liquidation proceeding is initiated with the consolidation of the assets of all the members in order to ensure the effectiveness of the proceeding. The consolidation of the assets can also be requested by the petitioner of the liquidation proceeding.

Judicial Liquidation Proceeding

The judicial liquidation proceeding of business groups follows the same rules set forth in Law No. 1116. However, as previously mentioned, there are special provisions related to business groups, such as provisions governing the consolidation of assets and regarding the coordination of the proceedings, including coordinated and joint hearings. These provisions are contained in Decree 1749 of 2011.

Cross-Border Insolvency Proceeding

The Colombian insolvency regime provides for cooperation between Colombian authorities and foreign countries that intervene in insolvency proceedings. This cooperation is intended to protect the debtor and its creditors and to create a safe framework for foreign investment and commerce.

The provisions regarding cross-border insolvency are applicable whenever:

- A foreign court or a foreign representative[5] requests the assistance of Colombia regarding a foreign insolvency proceeding;
- Foreign assistance is required regarding an insolvency proceeding carried out according to Colombian laws;
- Simultaneous proceedings in Colombia and in a foreign country are being carried out regarding a single debtor; or
- Debtors or interested third parties in a foreign country ask to intervene in an insolvency proceeding according to Colombian laws.

In case of conflict between the insolvency regime and any obligation accepted by Colombia through international treaties involving one or more foreign states, the obligation will prevail.

The liquidator within a proceeding in Colombia is authorised to act within foreign proceedings according to Colombian law, whenever there is no conflict with the laws governing the foreign proceeding.

It is very important to stress that Colombian authorities must respect Colombian public policy. As a consequence, measures adopted in foreign proceedings that are against public policy will not be adopted in Colombia.

Conclusions and Additional Observations

The insolvency regime in Colombia provides advanced methods to promote the recovery of potentially stable companies and, especially, the guarantees given to their creditors. The inclusion of strategic suppliers within the debt payment priority and the possibility for the creditor to request injunctive relief within the proceedings are some of the privileges provided by these regulations. These provisions not only represent a major development towards equality between debtors and creditors, but also afford an incentive for foreign investors seeking a fair insolvency regime that guarantees the recognition and payment of debts derived from business activities.

Colombia

Baker & McKenzie Colombia S.A.S.
Avenue 82 No. 10-62 6th Floor
Bogota
Colombia

T +57 1 634 1500 / 644 9595
F +57 1 376 2211

[5] A foreign representative is the person or the organ designated in a foreign proceeding to administer the reorganisation or liquidation of the assets or business of the debtor, or to act as a representative in a foreign proceeding.