

Global Restructuring & Insolvency Guide

Venezuela

Overview and Introduction

In Venezuela there are two regimes applicable to insolvent individual merchants and companies: moratorium (“*atraso*”); and bankruptcy (“*quiebra*”). This Guide sets forth a description of the main aspects of these insolvency regimes.

In addition to the moratorium and bankruptcy proceedings described below, the following regulated entities domiciled in Venezuela are subject to special insolvency regimes:

- insurance companies authorised by the Superintendent of the Insurance Activity (“**SAA**”) to conduct insurance activities in Venezuela;
- securities intermediaries authorised by the National Superintendent of Securities (“**SNV**”) to conduct securities intermediation activities in Venezuela; and
- banks authorised by the Office of the Superintendence of Banking Sector Entities (also known as the “Superintendent of Banks”) (“**Sudeban**”) to conduct banking activities in Venezuela.

These special regimes are beyond the scope of this Guide.

Applicable Legislation

The insolvency regimes in Venezuela (moratorium and bankruptcy) are governed by the Venezuelan Code of Commerce¹ (“**Commercial Code**”), which sets forth the regulations for the moratorium and bankruptcy proceedings applicable to individual merchants and companies. The Venezuelan insolvency regimes do not apply to individuals who are not merchants.

Moratorium

Moratorium is a benefit that a court may grant to companies and individual merchants whose assets exceed their liabilities but, due to an excusable lack of liquidity, are unable to pay their debts at maturity.

The objective of the moratorium is to grant the debtor a term not exceeding 12 months to satisfy its creditors. The original term may be extended by the court for an additional term of up to 12 months under certain circumstances.

If, during the term of the moratorium, the debtor is unable to satisfy all of its creditors or is not able to reach a settlement with the creditors, the debtor will automatically become subject to bankruptcy proceedings.

Conditions and Requirements to Trigger the Moratorium

Moratorium is available to those debtors whose assets exceed their liabilities (i.e. who are not insolvent), but due to a lack of liquidity cannot pay their debts at maturity.

In order to be eligible for a moratorium, the debtor must show that the lack of liquidity is excusable.

¹ Published in Official Gazette No. 475, dated 23 July 1955.

Parties that may Initiate the Moratorium

Moratorium is commenced by the debtor's petition only. The petition must be filed by the debtor before a competent court.

Main Consequences Arising from the Moratorium

Management of the Debtor's Business

As a general rule, debtors continue to operate and administer their day-to-day business within the scope of the plan for liquidating outstanding debts. Nevertheless, the court imposes several restrictions on the debtor in respect of the management and disposition of its assets. The debtor must obtain prior approval of the court to sell, pledge, mortgage, borrow money, compromise, collect receivables, make payments or perform any other acts which are necessary for the purposes of liquidating its assets and satisfying its creditors. The debtor is also subject to supervision by the creditors' committee. In addition, under certain exceptional circumstances, the debtor also may be completely deprived by the court of the management of its business.

Mandatory stay

One of the main consequences of a moratorium is that debts contracted prior to the moratorium mature by operation of law and become due.

Additionally, non-privileged debts contracted before the declaration of a moratorium are subject to stay and creditors are not entitled to sue for collection of their credits. Conversely, privileged debts and secured debts before the declaration of a moratorium are not subject to stay and secured creditors are entitled to sue for collection and may foreclose on the collateral, during the moratorium.

As a result of the moratorium, debts are automatically accelerated with respect to the debtor, but automatic acceleration does not apply to co-obligors. Creditors whose actions against the debtor are subject to stay may freely collect their mature receivables from the debtor's co-obligors if the co-obligors are jointly and severally liable with the debtor.

Debts contracted after the declaration of a moratorium are not subject to stay, provided that they have been authorised by the moratorium court and the creditors' committee.

Set-Off during the Moratorium

The general rule in Venezuela is that the set-off of debts and credits takes place by operation of law, provided that: (i) the debtor and the creditor have reciprocal obligations; (ii) each debt consists of money or assets of the same kind; and (iii) both debts are mature. Set-off operates up to the value of the lesser debt.² However, there are no statutory provisions specifically regulating the set-off of debts after the moratorium. Therefore, as with many other insolvency issues under Venezuelan law, there is no certainty of result.

In the absence of specific regulations, commentators have almost unanimously held that set-off cannot take place after the moratorium because such a transaction would negatively impact the rights of other creditors of the debtor. These commentators apply Article 1,340 of the Civil Code,³ which states that set-off cannot operate if it prejudices the rights of third parties.

A few Venezuelan commentators support the argument that, as a matter of equity, set-off may take place during the moratorium, provided that the reciprocal debts and credits arise from the same contract. However, we are not aware of case law or judicial precedents supporting this view.

Preference Period

Because the moratorium presupposes that the debtor is not insolvent, there is no preference period in a moratorium which may affect the enforceability of transactions executed by the debtor prior to the

² Civil Code, Articles 1,331 and 1,333.

³ Published in Official Gazette No. 2,990, dated 26 July 1982.

moratorium. However, when the moratorium is converted into or otherwise followed by a bankruptcy, the preference period could be of up to a maximum of two years and 10 days prior to the bankruptcy decree. Certain transactions executed during the preference period could be declared void or voidable by the bankruptcy court. These transactions are listed below.

Priorities and Privileges in the Payment of the Debtor's Obligations

Because the moratorium is designed to assist the company in reaching an amicable arrangement with the creditors, it does not necessarily involve the liquidation of the assets of the debtor and the distribution of the proceeds thereof pursuant to the rules of priorities. Nonetheless, if assets are liquidated, the distribution of the proceeds follows the order of priorities and privileges applicable in case of bankruptcy, described below.

Approximate Length and Termination of the Moratorium

Pursuant to the Commercial Code, the moratorium should not exceed 12 months. This term may be extended by a court under certain circumstances for an additional term of up to 12 months.

A moratorium may be revoked by the court and converted into bankruptcy under any of the following circumstances:

- the existence of debts which were not declared by the debtor in the petition for a moratorium;
- assets listed by the debtor in its petition that, in fact, do not exist;
- failure by the debtor to comply with any obligation imposed by the court during the moratorium;
- the discovery of fraud or bad faith by the debtor; or
- insufficiency of the debtor's assets to satisfy at least two-thirds of the claims against the debtor.

A moratorium proceeding may be dismissed at any time upon: (i) withdrawal of the petition by the debtor; (ii) payment of all debts; (iii) execution of an agreement with all creditors; or (iv) a court order revoking the benefit. Early termination of the moratorium proceeding under any of these conditions will result in a bankruptcy decree.

Bankruptcy

Unlike a moratorium, bankruptcy is neither a protection nor a benefit. In the ordinary course of events, bankruptcy leads to the liquidation of the bankrupt estate by the trustee or receiver appointed by the bankruptcy court.

Bankruptcy may be in any of the three following forms:

- fortuitous, if arising from fortuitous circumstances or *force majeure*;
- negligent, if caused by the negligence or imprudence of the bankrupt; and
- fraudulent, if arising from the fraudulent conduct of the bankrupt.

In case of negligent or fraudulent bankruptcy, the bankrupt is subject to the criminal sanctions provided for in the Venezuelan Criminal Code.⁴

Conditions and Requirements to Trigger the Bankruptcy

Bankruptcy is a proceeding applicable to companies and individual merchants that are insolvent. This has been generally interpreted to mean that companies or individual merchants: (i) are generally unable to pay their debts at maturity; and (ii) do not meet the requirements to apply for a moratorium.

⁴ Published in Official Gazette No. 5,768, dated 13 April 2005.

Parties that may Initiate the Bankruptcy

Under Venezuelan law, bankruptcy may be initiated by:

- the debtor. Directors of companies which become insolvent must file for a bankruptcy proceeding within three days after the date of suspension of payments (i.e. the date on which the company becomes generally unable to pay its debts at maturity);
- one or more creditors; or
- a court denying or revoking a petition for a moratorium, or declaring the expiration of the term of the moratorium.

Main Consequences arising from the Bankruptcy

Management of the Debtor's Business

The debtor's assets and businesses are administered by the creditors through the receiver. The company is completely deprived of its capacity to manage its assets.

Mandatory stay

The mandatory stay in cases of bankruptcy is the same as in a moratorium. In addition, from the date of the bankruptcy decree, interest ceases accruing to unsecured creditors and creditors grandfathered by a civil law general privilege, but continues accruing in favour of secured creditors.

Set-Off during the Bankruptcy

The same set-off rules applicable in moratorium proceedings apply in cases of bankruptcy.

Preference Period

Certain transactions executed by the debtor during the preference period could be void or avoidable. The preference period is determined by the bankruptcy court and may extend back to a maximum of two years and 10 days prior to the decree.

The following transactions are void if executed by debtors during the preference period, and the bankruptcy court is obligated to declare their nullity:

- gratuitous conveyances of real or personal property;
- creation of security interests, privileges or preferences in respect of pre-existing debts;
- payment of debts prior to maturity (including a payment through a set-off or any other mechanism of payment of debts which are not mature);
- payment in kind of debts payable in cash.

All other payments made by the debtor in respect of mature debts, including any potential set-off, and all other acts for consideration performed by the debtor during the preference period are voidable, provided that the relevant third party had knowledge of the financial condition of the debtor at the time of the transaction. The court has the authority to decide upon the validity or nullity of any transaction that qualifies as a voidable transaction.

Priorities and Privileges in the Payment of the Debtor's Obligations

The proceeds of the liquidation of the debtor's personal property must be distributed among creditors in the following order of priority:

- creditors holding labour claims up to certain statutory limits;

- creditors holding claims for legal expenses incurred during the proceedings to preserve the property for the benefit of all creditors;
- creditors holding security interests in specific collateral;
- creditors having claims which enjoy special civil law privileges or liens on personal property by operation of law (e.g. liens on personal property in the possession of the creditor for any amounts due in connection with the construction, maintenance and improvement of such personal property); and
- unsecured creditors.

The proceeds of the liquidation of the debtor's real property must be distributed among creditors in the following order of priority:

- creditors holding claims that enjoy a special civil law privilege or a lien on specific real property by operation of law (e.g. expenses incurred for the benefit of all creditors in the attachment, deposit or judicial sale of the property; and taxes for the current and preceding year, registration fees and inheritance taxes);
- claims secured by a mortgage with respect to specific mortgaged property;
- creditors holding labour claims, including past due salaries, severance benefits and any other credits arising from an employment relationship;
- creditors having claims which enjoy special civil law privileges or liens on personal property by operation of law; and
- unsecured creditors.

Upon the liquidation of the debtor's assets, the proceeds thereof must be distributed pursuant to the order of priorities set forth above. Each category of priorities must be fully satisfied before the proceeds of the liquidation may be used for the payment of subsequent categories. However, creditors having priority over specific collateral and who are not fully satisfied with the proceeds of such specific collateral participate in the distribution of the proceeds of other assets of the debtor (with respect to their deficiency claims) as unsecured creditors.

Within the same category of priorities, the proceeds of the liquidation, if insufficient to fully satisfy such category, will be distributed *pro rata* among the creditors in proportion to the amount of their claims.

Approximate Length and Termination of the Bankruptcy

Bankruptcy terminates with the liquidation of the bankrupt estate by the receiver. In the absence of clear and conclusive regulations, it is not possible to predict the approximate length of a bankruptcy proceeding.

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