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Bankruptcy, Insolvency & Rehabilitation Proceedings in Chile

ILN RESTRUCTURING & INSOLVENCY GROUP



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KEY FACTS OF BANKRUPTCY, INSOLVENCY & REHABILITATION PROCEEDINGS UNDER CHILEAN LAW

I- Introduction

Law N° 20.720 on Reorganization and Liquidation (“The Law”) modernized insolvency proceedings in Chile, promoting the rehabilitation (reorganization) of companies and individuals, balancing the interests of both creditors and debtors to renegotiate debts. The Law entered into force in October 2014, and since its first decade of application some minor reforms have been implemented.

Accordingly, one of its principal aims is to encourage the restructuring of debts, as debtors can obtain stays of proceedings and continue trading under the supervision of a trustee. Debtor’s essential suppliers are payable in their original terms and conditions, which facilitates the continuity of business.

The exchange with essential suppliers will be considered a secure credit in case of liquidation.

It is essential for the success of the reorganization that the debtor receives the creditors’ support. The creditors act and vote in creditors’ meetings and the Law protects the principle of equality of creditors (*par conditio creditorum*). However, main creditors have important rights as well, for instance, in appointing the trustee/liquidator and in renewing the period of protection for the debtor.

If the creditors reject the reorganization plan, the debtor goes into liquidation. As a result, the Law considers liquidation as a

last resource and an appropriate proceeding for inviable debtors.

Although some exceptions, insolvency proceedings are submitted before Civil Courts (there are not full-time courts dedicated exclusively to bankruptcy in Chile).

The Law also created the Insolvency and Reorganization Agency (“the Agency”), which

inspects the adequate implementation of the insolvency proceedings, controlling the role of trustees and liquidators. There is also a rehabilitation proceeding for individuals which is processed before the Agency. This Agency manages the Insolvency Gazette, where the most important insolvency orders are published.

The next sections will describe the main features of insolvency proceedings in Chile, before analyzing other interesting matters, namely, Chilean rules on restitutionary remedies, insolvency criminal offences and ineligibility of directors, cross-border insolvency and tax aspects.

II- Insolvency proceedings

1) Reorganization of Companies

a) Judicial Reorganization

The debtor may file a reorganization request to restructure its debt. In doing so, the debtor should submit the following documents:

- A list of all its assets, including a commercial assessment, disclosing their location and whether they are subject to any guarantee.
- A certificate subscribed by an independent auditor with a list of its debts, including the name, address, contact information, and the percentage of every creditor on the debt, expressing who the 3 main creditors are, excluding related creditors.
- Accounting books and accurate financial information.

Likewise, the debtor has to request the Agency the appointment of a trustee (and a substitute trustee). This process is conducted before the Agency with the participation of the 3 main creditors.

Having appointed the trustee, the Court issues the reorganization order, which legal effects are as follows:

- The debtor is granted a 60-day stay of proceedings. This term can be extended for another 60 days with the acquiescence of 2 or more creditors which represent at least 30% of the debt, excluding related creditors. Similarly, this term can be extended for an additional 60 days if 2 or more creditors, which represent more than 50% of the debt approves the extension, excluding related creditors.
- The reorganization is not ground for early termination of contracts. This means that creditors should comply with contracts entered into with the debtor, otherwise the credits are postponed.
- The debtor is under supervision of the trustee and has several limitations to render new guarantees, sell assets, and modify its articles of association.
- Although the debtor can raise new funds, there are limitations. The new credits cannot exceed the 20% of its debts, unless 30% or more of

the creditors accept this, excluding related creditors.

- New financiers are paid in the agreed terms and will be secured credits in case of liquidation (similar to the debtor in possession figure).
- The order establishes the date of the creditors' meeting, where the reorganization plan will be voted.
- The creditors have 15 days from this order to demonstrate before the Court their power of attorney to approve, modify or reject the reorganization plan. This is necessary to participate in the creditor's meetings.
- Similarly, the creditors can claim their credits within 15 days if they do not agree the amount and category established in the debtor's list.

The debtor is free to prepare its reorganization plan, considering the foregoing limitations but negotiation is necessary to obtain creditors' acceptance. The trustee has to submit a report to suggest the approval or rejection of the reorganization plan, at least 3 days before the creditors' meeting.

In order to succeed, the reorganization plan requires the support of at least 66% of the creditors with right to vote - excluding related creditors-, considering the different categories



(secured, unsecured credits) in which the plan is divided.

b) Out-Of-Court Reorganization

The debtor has the option of reorganizing its debt directly with the support of 2 or more creditors which represent at least 75% of the debt in every category, excluding related creditors. The agreement must be entered into before a notary -or a faith officer-. Nonetheless, once accepted it requires Court's approval. The Court's role is to verify that the formalities and mandatory provisions (quorums) are complied with. Moreover, the debtor has to publish the agreement in the Insolvency Gazette. Creditors who might be excluded can oppose the agreement within 10 days from the publication. While the Court's leave is processed, the debtor is granted stays of proceedings.

2) Liquidation of Companies

a) Voluntary Liquidation

A company may file an application to obtain its own liquidation under an insolvency scenario. The debtor is required to produce the following documents:

- A list of all its assets, including a commercial assessment, disclosing their location and whether they are subject to any guarantee. In the case of real estate or assets registered in public records, certificates are also necessary.
- A list of its debts, including the name, address, contact information of its creditors, stating whether they have secured or unsecured credits.
- A list of the legal proceedings commenced against the debtor.
- A list of its employees.
- Financial information and bank account statements considering a period of 2 years before the liquidation.
- An affidavit on the accuracy of the documents provided to the court.

b) Forced Liquidation

A creditor may file an application to claim the liquidation of its debtor in the following scenarios:

- If the debtor is in breach of an obligation established in a "executive title" (a document which demonstrates an enforceable right that does not require a declaration i.e. a cheque). This ground cannot be invoked against debtor's guarantors.
- If there are 2 or more debt collection proceedings against the debtor in connection to 2 or more unpaid executive titles, provided that the debtor has not offered enough assets to pay its debts within 4 days after service.
- If the debtor has closed its headquarters/offices and the location of its managers is unknown, provided that the company has not left any representative to respond to claims and its obligations.

The creditor has to submit before the court the same list of documents required for the voluntary liquidation.

Also, interim measures can be granted to freeze debtor's assets.

The court will call both the creditor and the debtor for a hearing, where the debtor might adopt any of these attitudes:

- Offering enough assets and proposing a term to pay its debts. Have the debtor failed to comply with this term, the debtor goes into liquidation.
- Accepting the creditor's claim, so that the debtor goes into liquidation.
- Requesting the court to commence a judicial reorganization proceeding.
- Opposing the claim. This leads to a summary proceeding, where the debtor might invoke limited grounds for defense. If the court rejects the opposition, the debtor goes into liquidation.
- In any of these scenarios, the debtor is obliged to disclose the name, address, and contact information of its 3 main creditors. If this information is not provided, the debtor goes into liquidation.

As the effects of the liquidation order are the same in both voluntary and forced liquidation, they will be treated in the next section.

c) Effects of liquidation proceedings

The Agency appoints a liquidator (and a substitute liquidator) with the participation of the 3 main creditors.

Having appointed the liquidator, and provided that the requirements set out above are fulfilled, the court issues the liquidation order.

This order is published in the Insolvency Gazette and obliges to

- Deliver all the debtor's post to the liquidator.
- Consolidate all the proceedings commenced against the debtor before the court where the liquidation is processed.
- Inform the public that it is forbidden for the debtor to receive any payment, otherwise it will be null and void. This is because the liquidator manages the debtor's affairs during the process.
- Publish in the Insolvency Gazette that the creditors have the right to claim their credits within 30 days of the publication.
- Serve the order on overseas creditors by the most efficient method.
- Register the order in Public Registers in case of registered assets.
- Determine the date of the first creditor's meeting.

The main effects of the liquidation order are as follows:

- The liquidator manages the debtor assets and affairs during the process.
- As such, the creditor has the power to seize debtor's assets.



- Stays of proceedings are granted. Thus, the creditors are obliged to claim their credits within the liquidation.
- The debtor can continue its business under certain circumstances.
- All credits against the debtor are duly enforceable, even though they were originally subject to instalments or deadlines.

The Law discharges the debtor from the outstanding debts that cannot be paid after the liquidation of its assets.

3) Renegotiation for individuals

Individuals may file an application for a renegotiation proceeding before the Agency, where they have 2 or more outstanding debts for more than 90 days in connection with 2 or more creditors. It is necessary that the amount of the debt exceeds a threshold (circa USD 3,000).

During the renegotiation of its debt, the debtor is granted stays of proceedings.

4) Summary Reorganization and Liquidation for Micro-entities

Micro-entities and small companies may apply for summary reorganization or voluntary liquidation. The aim is to establish cost-effective alternatives to either renegotiate or liquidate the debts of small-scale enterprises. Individuals have also the option of applying for voluntary summary liquidation.

A creditor is entitled to commence a forced summary liquidation proceeding against a micro-entity or an individual.

There are 2 grounds for forced summary liquidation:

- a) If there are 2 or more outstanding debts established in executive titles, provided that 2 or more debt collection proceedings against the debtor have been commenced, and the debtor has not offered enough assets to pay its debts within 4 days after service.
- b) If the debtor has closed its headquarters/offices and the location of its managers is unknown, provided that the company has not left any representative to respond to claims and its obligations. This ground only applies to micro entities and not to individuals.

The Law also grants the debtor stays of proceedings in the context of summary applications.

III- Restitutionary remedies

The Law provides remedies for creditors and the trustee/liquidator to recover assets/money transferred by the debtor to third parties in prejudice of its creditors in an insolvency scenario. Depending on the ground, these remedies seek the restitution of assets in connection to transfers or contracts entered into by the debtor between 1 and 2 years before the liquidation/reorganization order.

IV- Criminal offences and ineligibility of directors

The Law establishes criminal offences for debtors, where they have entered into contracts to diminish their assets with the clear purpose of damaging their creditors.

Also, there are criminal offences for debtors, where they hide their assets or provide false information to the trustee/liquidator, and where the debtor has not complied with its obligations of maintaining accurate accounting books and financial information before 2 years of the liquidation/reorganization order.



Liquidators and trustees might commit criminal offences where they obtain unlawful benefits in insolvency proceedings.

Individuals who have committed insolvency criminal offences are ineligible as directors of companies. This prohibition also applies to individuals who are parties to insolvency proceedings in the capacity as debtor or as administrators or representatives of debtors in insolvency proceedings.

V- Cross-border insolvency

The Law provides a chapter on cross-border insolvency rules, promoting cooperation and recognition of foreign proceedings, protecting the rights of both national and overseas creditors. The law also regulates the effects of parallel proceedings.

VI- Tax aspects

For tax purposes, the liquidator represents the debtor before the Chilean Tax Authority. As such, the liquidator is responsible for handling the

debtor's tax obligations (tax returns, sworn statements, invoice issuance, withholdings, etc.). Regarding tax offenses, the liquidator might be liable if there is participation in fraudulent acts committed during its administration.

During a liquidation proceeding, the Tax Authority may issue a tax assessment on taxes owed by the debtor, without any prior procedure or notice.

Additionally, any amount waived or condoned by a creditor from debts included in a judicial reorganization agreement, is treated, on one hand, as a deductible expense for the creditor, and on the other, as a taxable income for the debtor. However, credits must be at least one year old and independent to any related parties.

Creditors who issued unpaid invoices to debtors may choose to either allocate the VAT paid for such invoices to any taxes due or request its reimbursement. This benefit is also limited to unrelated creditors and debtors.