

legal memo

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2020-2.0: Some legal guidance for a restart of the year



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You surely remember Sleeping Beauty or The Princess and the Frog. European storytelling is full of children's tales featuring idle kissing royalty. COVID-19 has brought 2020 to a halt, transformed it in a zombie year. But unlike the children's stories, when the pandemic is finally over and business can fully resume their activities, they are most likely to see themselves transformed into an ugly toad. What can we do about it? This short note tries to address some of the questions you may come across in your fight to redress this unforeseen change in condition.

1. Who might be interested in this article?

This note is not intended for those who have thrived in the current pandemic, it might not even be for you, if you can rely in your own resources to restart the activity again, or if you lost any hope in your business and are considering liquidation. It is a note mostly intended for those many who are planning to restart their activity again but need a push in the financial structure of their businesses.

2. What can help me out to restart?

Answers are obvious:

1. Fresh money to finance your activity and any existing debts
2. A stay in payments
3. A haircut on existing debts

A combination of all 3 alternatives above.

3. What can I expect from the Government Measures?

There is almost a new one every week, so it is hard to make a summary that lasts, but in any event a bit of 1 & 2.

- a) Underwriting of loans by the State
- b) Deferral of tax payments and social security contributions.

a) Underwriting of loans:

i. Who grants the loans?

Spanish Government, via ICO (Instituto Oficial de Crédito), who will manage the underwriting of loans with banks.

ii. Up until what amount?

Up to 80% of the loans and renewals made to SMEs and local authorities; for the rest of the companies, 70% of our loans and 60% of renewals. For the tourist and hotel sectors, the guarantee will be of 50%.

iii. What can the borrowed money be used for?

Paying suppliers, salaries, rentals of premises, offices and facilities supply costs working capital needs and other cash flow issues.

iv. Which requirements need to be met?

1. Not being on insolvency proceedings on March 17th, 2020.
2. Not being a default debtor listed in CIRBE on December 31st, 2019.
3. Be a Company or a self-employed with: (i) a registered office in Spain, (ii) affected by the impact of COVID-19.

b. 1) Deferment of taxes:

i. Which taxes can be deferred?

- a) Payment of debts arising from tax returns whose deadline expires between March 13th and May 30th, 2020
- b) Output Vat
- c) Tax debts derived from withholdings and account payments
- d) Account payments of Corporate Income Tax

ii. Who can request its deferral?

SMEs and self-employed professionals whose turnover is below 6.010.121,04 euros in 2019.

iii. How do I apply for deferral?

Once your tax returns or self-assessments are submitted, you should request the deferral to the appropriate Tax Authorities.

iv. Are tax filing deadlines affected?

Yes, but only for those whose turnover was below 600.000€ in 2019. RDL 14/2020 has approved an extension for filing and payment of tax returns and tax self-assessments, extending the term from April 15th up until May 20th.

v. What is the maximum deferrable amount?

Up to 30,000€.

vi. For how long can the payments be deferred?

Up to 6 months.

vii. What cost in deferring?

Interest will only accrue as from the third month of deferment.

b. 2) Deferment of social security contributions:**i. Which taxes can be deferred?**

It depends on whether you are a self-employed individual or a company.

a) Self-Employed entitled to an extraordinary allowance:

Those who have been forced to a closure of their professional activity or who have seen their professional revenues fall by more than 75% due to the Covid-19 situation. In both cases, the Self-Employed person will be exempted from paying any social security contributions due throughout the State of Alarm. In July, they will be able to defer the payment of the contribution but will be charged a reduced 0.5% interest rate.

b) Self-employed people who have maintained their activity:

They may defer payment of April's social contribution, subject to paying a reduced interest rate of 0,5%. For the following months of May to July, the deferral will be exempt from any interest payment.

c) Companies that have filed a force majeure ERTE:

They are exempted from paying their contributions during the period of suspension of the contracts or the reduction of working hours. At the end of this period, they may request deferment of contributions, subject to paying a 0,5% interest rate.

d) Companies that have maintained their activity:

They may also benefit from payment deferral in their social contributions. In relation to March, the deferral will be subject to a 0,5% interest rate.

Fulfilling the legal requirements, they may ask for a 6 months deferral without interest. If the legal requirements are not met, they will have to pay a 0,5% interest rate.

ii. Up to what amount?

RDL 11/2020 does not set a ceiling on the amount of social security contributions which may be deferred.

iii. For how long can the payments be deferred?

Up to 6 months.

iv. What cost in deferring?

In those cases, in which the deferment may have a cost, that will be 0,5% of the total deferred amount.

4. What can I do in case I am not eligible for the additional financing or cannot afford the cost? How about if my revised business-plan does not work out?

We suggest you continue reading.

5. Can I try friendly negotiations with any creditors?

Yes, you may, and it may be a workable solution for you, particularly if you have just a few. However, if you want to impose terms of settlement to a broader group of creditors, a friendly negotiation may not work, as you will lack the compelling force of the law to impose terms on the group.

6. But I have heard all tenants are not paying their loans. Why don't I do the same?

A landlord is like any other creditor, with some distinctive features: it normally has a deposit to cure himself against defaulting tenants and has the power to keep it. As of today, current Spanish Government anti-COVID-19 measures do not entitle tenants to default or make a unilateral stay in payments. You will need to assess your worthiness as a tenant. You may still wish to act unilaterally but you will then need luck.

7. What do I have to do with the employees affected by an ERTE, in case I cannot afford their salaries once they are back?

You will probably have no option but dismiss them. In the case of several dismissals, which vary depending on the number of employees a company has, the redundancy will have to be made through a collective dismissal procedure (ERE).

i. Which conditions are required?

Depending on the cause alleged.

ii. How much will it cost?

Depending on the outcome of the negotiations with the employees, but the minimum cost is of 20-day severance payment per employee, plus legal expenses.

8. How can I reach the agreement?

Usually by paying the employees a severance payment above the standard 20 days.

9. What happens if the agreement is not reached?

You can still go ahead dismissing them and pay a 20-day severance payment. However, employees can challenge the dismissal before a Court to void the dismissal, if they succeed the cost of the measure will increase substantially.

10. Are directors obliged to file insolvency proceedings at some point?

Yes, they are, within two months since they were aware, or should have been aware, of the Company's insolvency. If some of the circumstances here below arise, it shall be assumed that the directors were aware of the insolvency. Those circumstances being:

- Widespread non-payment of the debtor's obligations.
- The existence of pending foreclosures that affect the debtor's assets.
- Unlawful removal or hasty or ruinous liquidation of the Company's assets by the directors.
- Non-payment of the Tax Obligations, Social Security contributions for the last three months.
- Non-payment of wages and salaries and other remuneration deriving from employment relationships for the last three months.

However, the two months deadline has been halted by RDL 10/2020 on the light of the current pandemic. The counting will resume once the State of Alarm finalizes. For those companies who might have incurred in any of the test circumstances during this period, RDL 10/2020 has given them an additional two months term as from the end of the State of Alarm to address the situation.

11. How can I gain extra-time and try to negotiate new terms with creditors?

One option is filling for pre-insolvency proceedings and benefit from the temporary stay in payments, provided by this procedure, to try and sort out the situation.

The main features of pre-insolvency proceedings are:

- It effectively protects you from your creditors, putting pressure on them to reach a settlement agreement.
- You remain free to run your business as you wish.
- You may choose who to pay and to negotiate alternative payment terms.
- No Company's assets needed to carry out the business activity may be seized during the pre-insolvency period.
- No receiver appointed.

All too good but it will last barely 4 months.

12. Any tips on how to address the situation?

Yes, as usual, they are simple to advice but harder to implement.

- a) Anticipate. Do not address the situation as an ultimate recourse when you have run of cash, you are only diminishing your chances of making it work.
- b) Prepare a credible plan. Creditors want to understand and be treated with deference before deciding on giving their agreement.
- c) Seek advice, use it to negotiate terms on the first instance and just step in if required, to save your credit.

13. What should be done in these four months?

Reach an agreement or a repayment proposal with your creditors, the agreement may include payment moratorium or a reduction of existing credits or a combination of both.

14. Is the vote of all creditors required?

No, it will be enough with the vote of 3/5 of your total debt to obtain a binding agreement upon all your creditors, including those dissenting.

15. What is next?

If you reach a settlement with your creditors, you are off the hook. You have refinanced your debt and you just need to hope revenue projections will work.

If you do not reach an agreement, you have two possibilities:

- To do nothing, which may trigger several future problems, as you are unprotected against creditors. It is also risky from the perspective of the director's personal liability.
- To file for insolvency.

16. Is there anything good in filling for insolvency?

It is basically a need you may have both to protect the assets of the Company and fulfil your duties as a director.

17. What are the main differences between an insolvency and a pre-insolvency procedure?

Many, as the pre-insolvency is essentially an unregulated window of opportunity, to try to reach an agreement with creditors, while insolvency proceedings are a sort of final station, the company either gets out of them with a settlement or is liquidated.

18. Can I carry on trading?

It is an option; you may opt to continue trading or file for liquidation at the beginning of the proceedings or any time before. Once you file for liquidation, you will be discharged from your duties as directors and the receivers will take full control of the Company, in which case, your prospects of saving whatever you wish to save from the business, will be reduced considerably.

19. So, may I have a second opportunity to save the business?

Yes, but in order to succeed, you will need at some point during the proceedings the endorsement of your creditors.

Moreover, the procedure will require more of your attention. To start with, you will need to submit detailed accounting information, including a full list of creditors and comprehensive corporate records. This will require a review of their accuracy, introduce wherever needed adequate explanation on any potential disparity between their accounting and real value. This is because your tenure as director will be much often reviewed. Once the insolvency is filed, you will remain in control of management, but the Court will appoint a receiver, who will supervise your activity.

You may then run the initiative to propose a settlement, but your proposal is subject to several rules, most notably the need to consider the creditors ranking. The settlement proposal must consider that some creditors are privileged while other are subordinated. Privileged creditors may have a preferential right to be paid above all others (a part of the salaries, taxes, social security contributions), others may have the right to enforce a security over a certain asset to recover their credit (mortgage holders, pledgees...). Subordinated creditors (such as for instance parties specially related with the company or with the shareholders). Whereas privileged creditors will have collection preference, subordinated creditors will only be paid once all other creditors have been paid.

To get your proposal approved, you will need at least a simple majority of the representative of the ordinary creditors to vote in favour. This minimum quorum is strengthened by the law, depending on how aggressive your proposal is towards creditors. If the required voting of creditors is obtained, then it will all depend on the Court's decision, based on the receiver's report.

20. Is there a third chance?

No, this is the last one. If you fail to convince your creditors on your repayment plan, the company will go into liquidation.

21. Are all creditors affected by the terms of your proposal?

No, just ordinary and subordinated creditors. Privileged Creditors shall only be affected if they agree to, or if a reinforced majority of them, voted in favour of the specific proposal they may be offered as a group.

22. Are these the only alternatives to save the company?

Not exactly, though the measures above are all those that will keep you as the owner of the business. Besides them, you may also try to find a buyer for the company or for the productive unit and try to reach with him some sort of understanding (which may include a buy-back option).

23. When can the buyer step in and make the offer?

Anytime. You may submit the offer to purchase the Company on applying for the declaration of the insolvency, in which case you may need the endorsement of creditors representing 10% of the total liabilities. If the buyer is found at a later stage of the proceedings, the minimum endorsements required to submit the offers will climb up to 20% of the total credits. In both cases, the proposal will need to be ratified by the creditors in accordance with the majorities provided in the law.

24. Is there a possibility to buy the company at a bargain for lump-sum and forget about the creditors?

Yes, there is, but only if the company gives up hopes of continuity and files for insolvency. In this case, the law privileges the sale of the productive unit as a going concern.

25. What is the advantage of buying at liquidation?

The advantage is obviously for the buyer, often the winner of an auction started by the receiver, he will set the price without taking over the creditors, except for labour and social security credits.

26. Can I reach an agreement with the buyers in any of the alternatives?

Yes, you may, although it is not advisable that you or any person specially related to you or to the insolvent company appears to be in control of the purchaser. In such case, the purchase may lose the exemption to pay existing credits that the law grants him.

27. Can I get hold of any COVID-19 financing for this restructuring?

You may certainly not file for pre and/or insolvency and apply for a loan thereafter, however, it seems possible to obtain the financing first and seek thereafter an improvement of your terms with creditors through a restructuring of your debt.

28. Can a purchaser of the productive unit of an insolvent company get the financing?

Apparently yes.

29. Any other important issues I may wish to consider?

So many but, if you have come all this way and read all these questions, you may prefer contacting at the mail address below and chat with us.

If you require any further information do not hesitate to contact us at info.barcelona@ecija.com

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