

## CASE REVIEW SECTION

# The Sweet Smell of Success: Brazilian Confectioner, Indústria de Produtos Alimentícios Cory, Obtains a Fresh Start under Brazil's New Bankruptcy and Restructuring Law

Christopher Andrew Jarvinen,\* Associate, Paul, Weiss, Rifkind, Wharton & Garrison LLP, New York, USA

After more than seven months of often difficult negotiations with its major creditors, one of Brazil's largest family-owned manufacturers of confectionary products, Indústria de Produtos Alimentícios Cory ('Cory'), has restructured debt totaling the equivalent of USD 57 million.

Cory, which markets such well-known Brazilian brands of candies and cookies as Icekiss and Show Gol, is one of the first companies to undergo a successful judicial reorganisation (*recuperação judicial*), a court-supervised proceeding similar to the chapter 11 process under the United States Bankruptcy Code, pursuant to Brazil's year-old New Bankruptcy and Restructuring Law (*Nova Lei de Falências e Recuperação de Empresas*) ('NBRL').

Cory is not alone. Since the NBRL went into effect on 9 June 2005, more than 1,000 Brazilian companies have commenced one of its three, court-supervised proceedings. About 130 have been judicial reorganisations with bankruptcy liquidations (*falências*) comprising the rest. And although a number of Brazilian companies are currently rumoured to be preparing to initiate court cases under the NBRL's third option, the out-of-court reorganisation (*recuperação extrajudicial*), none has done so. The out-of-court reorganisation, a flexible restructuring proceeding somewhat analogous to a 'pre-packaged' reorganisation in the United States, will permit financially distressed companies to seek court approval for one or more pre-packaged plans negotiated with individual, or groups of, creditors.

'A major challenge during Cory's reorganisation has been sustaining constructive negotiations among the debtor's sole shareholder, the state Development Bank of Minas Gerais ['BDMG'] which holds 80% of Cory's secured debt, 13 other secured lenders, 250 employees and hundreds of unsecured trade creditors,' stated Antonio Carlos Mazzuco, reorganisation counsel to Cory

and a partner with São Paulo-based Madrona, Hong, Mazzuco, Kawamura Sociedade de Advogados.

Cory was no stranger to the bankruptcy process when it commenced a judicial reorganisation in 2005. The combination of a disastrous decision to expand Cory's business in 1999 by purchasing a chain of money-losing home appliance stores, combined with soaring prices for raw materials, principally sugar, used in the manufacture of Cory's confections resulted in the company incurring a significant amount of unanticipated debt that resulted in the company being declared bankrupt in May 2004 under Brazil's six-decade-old, prior bankruptcy law (the outdated Decree-Law No. 7661 of 21 June 1945).

The prior bankruptcy law offered very few legal and financial tools to help debtors like Cory shed enough debt to repair their balance sheets, because the old law provided debtors with a very limited debt discharge, restricted to a statutorily prescribed percentage of *unsecured* claims. The prior bankruptcy law also prohibited debtors from negotiating individualised rehabilitation plans directly with creditors.

'Approximately one-third of Cory's USD 57 million debt represented *secured* claims. As such, Cory needed to restructure both its secured and unsecured obligations, something that the NBRL now authorises debtors to do,' explained Mazzuco.

During August 2005, the court overseeing Cory's existing case under the prior bankruptcy law agreed to convert it to a judicial reorganisation, thereby paving the way for Cory to enter into restructuring negotiations with its major creditors.

A successful reorganisation by Cory will have a tangible impact on many parties other than just Cory's sole shareholder. 'With annual revenues of almost USD 40 million and with approximately 250 employees, Cory is an important employer, producing more than 1,200

### Notes

\* Christopher Andrew Jarvinen is also the president of the New York section of the *Instituto Brasileiro de Gestão e Turnaround* (Brazilian Institute of Corporate Management and Turnaround) ('IBGT'). Views expressed in this article are those of the author and not necessarily those of Paul, Weiss, Rifkind, Wharton & Garrison LLP or the IBGT.

tons of sweets and 500 tons of cookies a month at state-of-the-art manufacturing facilities located in the Brazilian states of São Paulo and Minas Gerais,' stated Salvatore Milanese, a director with KPMG Corporate Finance in São Paulo who advised Cory on its financial restructuring.

Under the terms of Cory's consensual reorganisation plan, 'the maturities on Cory's approximately USD 19 million in secured debt and USD 28 million in unsecured bank loans will be pushed out between 15 to 18 years at favourable interest rates, thereby cutting Cory's debt by 75% on average,' indicated Milanese.

'The treatment of general unsecured creditors will depend upon the size of their claims,' added Milanese. Unsecured creditors agreed to be paid over time, with holders of allowed claims in amounts less than USD 15,000 receiving lump-sum distributions totaling 80% of such claims within 90 days after the effective date of the plan, claimants with claims between USD 15,000 and USD 50,000 being paid in 48 monthly installments with interest at 1% per annum, and claimants holding claims over USD 50,000 receiving 50% of their distribution in 180 monthly installments with interest at 1% per annum and the remaining 50% in a balloon payment at the end of the period.

A unique aspect of Cory's reorganisation plan is the creation of a board of directors comprised of four directors, one of whom will be Cory's sole shareholder. The sole shareholder will also nominate the three remaining directors, one from each of the three classes of claims (secured, general unsecured and employees), but the relevant class will have the final right to approve or reject the sole shareholder's nominee.

In the event of a voting tie among the four directors, the board member approved by the class of secured creditors will determine the outcome.

To assure transparency in Cory's post-confirmation business operations, the reorganisation plan empowers the three board members approved by the classes of claims to choose the company's chief financial officer and chief operating officer.

Another notable feature of Cory's reorganisation plan is that the company can be sold to a third-party over the objection of the sole shareholder if, among other requirements, the purchase price is at least equal to the net present value of Cory's scheduled debt (to be determined based on a formula comprised of Brazil's basic interest rate (SELIC), the inflation rate and a spread).

After the third creditors meeting held a few months ago, Cory obtained overwhelming creditor support for the proposed reorganisation plan, and it was recently confirmed by the court.

The NBRL 'infuses new vigour into the corporate reorganisation process in Brazil because, unlike the prior bankruptcy law, creditors now play a major role in a debtor's restructuring,' indicated Jorge Queiroz, the president of the Brazilian Management and Turnaround Institute (*Instituto Brasileiro de Gestão e Turnaround*) a São Paulo non-profit organisation dedicated to educating the public about the NBRL. 'If a debtor is unable to obtain the requisite creditor support for its proposed reorganisation plan, the debtor most likely will be forced to liquidate,' added Queiroz.

'With close to 6 million registered family-owned businesses in Brazil,' Queiroz believes that 'Cory's reorganisation could serve as a model for other family-owned businesses encountering severe financial distress.'

In sharp contrast to the spectacle that has resulted in Brazilian commentators labelling the judicial reorganisation of Varig (the Brazilian airline) the first restructuring '*novela*' (i.e., a soap opera) under the NBRL, 'the judicial reorganisation of Cory, by combining a viable business plan with the right mix of professionals, is quietly on track to fulfil the NBRL's primary goal to provide Cory with a "fresh start", that is, the elimination of burdensome debt that will give the company a realistic opportunity to continue as a going concern, repay creditors, employ a workforce and provide dividends to its sole shareholder,' concluded Queiroz.