

## ALL CHANGE IN THE GULF: THE NEW DIFC INSOLVENCY LAW

The introduction of the new insolvency law (DIFC Insolvency Law No 1 of 2019 and the DIFC Insolvency Regulations 2019 on 13 June) is the latest in a number of law reform initiatives taking place in the Gulf. Each of the reforms are aimed at encouraging trade and investment in the region. The DIFC insolvency law follows recent bankruptcy reforms introduced in the UAE and the KSA. It shares common themes, such as the use of formal restructuring procedures as a means of allowing debtors a fresh start, provides a mechanism for binding non-consenting creditors, and seeks to promote a range of efficient and cost-effective procedures.

The new insolvency regime also aims to bring the DIFC in line with international best practice. This is with a view to increasing transparency and predictability in terms of outcome, so that all stakeholders can have confidence in the regime. It enhances what's on offer in terms of the restructuring tools available to debtors and creditors, by increasing the range of procedures available - new rehabilitation and administration processes, sit alongside existing procedures (CVAs, receiverships and liquidation). In keeping with international trends, the enhancements contained in the new law focus more on restructuring and business rescue, rather than liquidation.

In order to ensure an appropriate balance between the different stakeholders, the new insolvency law offers protection for debtors seeking to restructure, whilst at the same time ensures creditors' rights are protected in terms of their priority rights and maintaining exemptions for certain financial market transactions. Other changes are designed to modernise and improve the efficiency and effectiveness of the law and how it operates in practice, with the aim of maximising returns and thereby encouraging trade and investment in the region.

### WHAT'S NEW?

#### Rehabilitation

The new insolvency law introduces a debtor in possession regime known as rehabilitation. Rehabilitation allows creditors to vote on a rehabilitation plan promoted by the debtor with a view to restructuring its business (see the high-level overview at the end of this briefing setting out the different steps required to facilitate a rehabilitation). Rehabilitation comes with the benefit of an automatic stay for a period of 120 days, certain protections against contractual

#### Key issues

- Introduces debtor in possession procedure
- Facilitates rescue finance
- Allows management to be replaced in certain circumstances by an administrator
- Modernises winding up
- Adopts UNCITRAL Model Law

termination, and a mechanism that allows a dissenting minority of creditors to be bound to the rehabilitation plan. Creditors are invited to consider and support the plan and for these purposes are categorised into different classes to formally vote on the plan. The court is consulted on the formulation of the classes. Ordinarily, the plan needs 75% of creditors in each class to support the plan and the court to approve it. However, in certain circumstances, as long as (i) one class of creditors affected by the plan approves it, (ii) no creditor is worse off than in liquidation and (iii) no junior creditor gets paid before senior creditors are paid, the court may still approve the plan (often referred to as "cross-class cram down"). In addition, the court is able to sanction new finance during the rehabilitation process, whilst ensuring that existing secured creditors are protected. The cram down mechanism and new rescue finance take their inspiration from the US Chapter 11 reorganisation procedure. For others familiar with the English scheme of arrangement, similarities may be drawn in terms of the two-stage court process and the same majority threshold, but, as previously mentioned, the DIFC rehabilitation process has more sophisticated enhancements in the form of the automatic stay, contractual termination protections and the ability to bind creditors across classes.

## **Administration**

One of the other key aspects of the new insolvency law is the appointment of an independent administrator by the court where there has been mismanagement. The administrator has a limited role to either facilitate a company voluntary arrangement or propose a rehabilitation plan or a scheme of arrangement under the Companies Law. Alternatively, the administrator may simply be tasked with investigating any wrong-doing by the debtor and/or its management.

## **Winding up**

Other changes include modernising the winding up procedures, streamlining the appointment process for the appointment of a creditors' committee in a winding up, and clarifying the process for dissolution.

## **Cross-border co-operation**

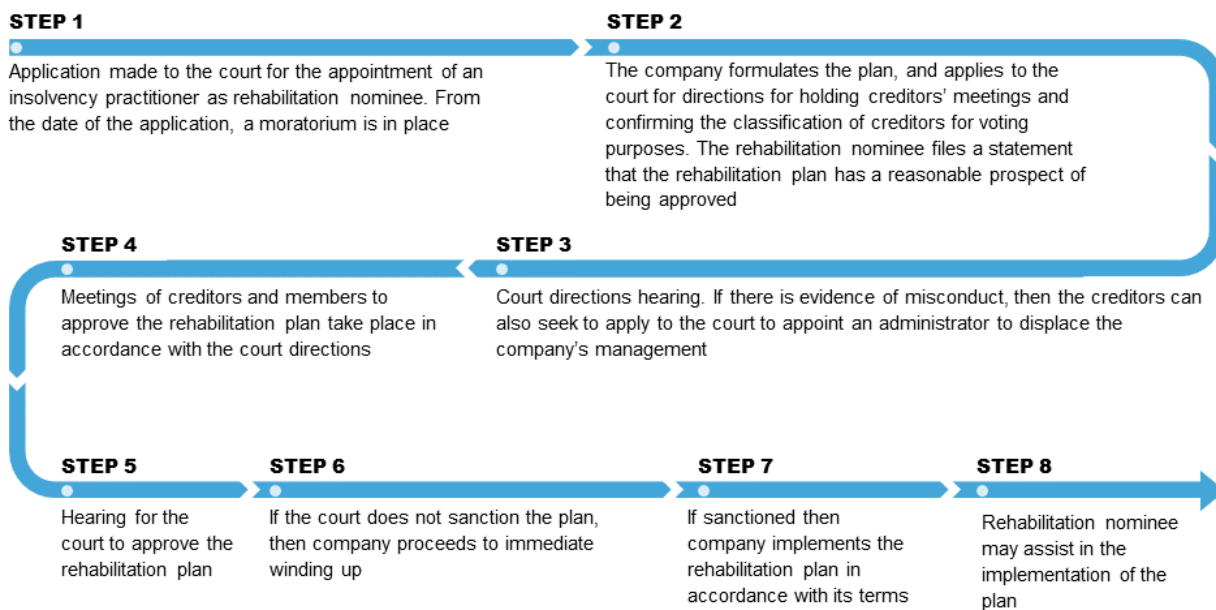
Furthermore, the new law adopts the UNCITRAL Model Law on Cross Border Insolvency with a view to encouraging co-operation and co-ordination between insolvency proceedings taking place in different jurisdictions. The Model law is an important aspect of the DIFC developments recognising the cross-border nature of many businesses and ensuring fairness and creating efficiencies to lead to a more predictable regime and providing a more favourable environment for trade and investment.

## **Concluding thoughts**

The introduction of the new law represents another step forward in insolvency legislative reform in the GCC. The new rehabilitation procedure is particularly innovative, including not only an automatic moratorium but also contractual termination protections and the ability to bind creditors across classes. Interestingly, these are key aspects which already form part of the new DIFC insolvency law, are only just being considered in further reforms anticipated in the UK and announced at the end of August 2018. They also form part of the EU Directive on preventive restructuring frameworks which is due to be published in the next couple of weeks. In this regard, the DIFC could be

viewed not just to be keeping up with international trends, but very much at the forefront of developments.

## OVERVIEW OF REHABILITATION



### Clifford Chance's role

A team led by Adrian Cohen including Gabrielle Ruiz, Melissa Coakley, Robin Abraham, Nicola Reader, and Cheuk yin Cheung, worked with the legal team at the DIFCA (led by Jacques Visser and Tarek Hajjiri) from the policy stages of the new law through to its implementation.

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