

The New DIFC Insolvency Law

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The DIFC has introduced a new Insolvency Law (Law No. 1 of 2019) ('New Insolvency Law') as a means of enhancing and facilitating a more efficient and effective bankruptcy regime within the free zone. The New Insolvency Law was enacted on 30 May 2019 and came into force on 6 June 2019.

Rather than a wholesale overhaul of the existing law, new concepts have been introduced to provide debtors and creditors a larger toolkit to deal with insolvency situations. We examine three of these new concepts below.

1. Debtor in Possession Regime - Rehabilitation

Where the directors of a company consider that it is likely the company may become unable to pay its debts, they can notify the court in writing (the 'Rehabilitation Plan Notification') that they intend to make a proposal to the creditors of the company and submit a rehabilitation plan (the 'Rehabilitation Plan'). On receipt of such application the court shall convene and an automatic moratorium shall apply to all creditors in respect of the company and its assets wherever they may be located at the time of the Rehabilitation Plan Notification.

Rehabilitation allows the debtor to remain in control and continue to manage its business and assets as the directors are authorised to continue managing the company's affairs except in cases where there is evidence of fraud, dishonesty, incompetence or mismanagement of the company. The board of the company shall appoint one or more insolvency practitioners as rehabilitation nominee(s) prior to the Rehabilitation Plan Notification and the name and qualifications of such nominee(s) shall be set out in the Rehabilitation Plan Notification.

The crucial benefit of the rehabilitation procedure is that, unless otherwise ordered by the court, an automatic moratorium of 120 days shall immediately apply to all creditors (secured or unsecured and without their consent), thus preventing any enforcement proceedings against the debtor. A Rehabilitation Plan application shall, amongst other matters, have the following effects:

- it shall not render any undue debt due and payable;
- any contrary provision in any contract or applicable law shall be deemed unenforceable during the moratorium period;
- any termination provision in any contract linked to insolvency of the debtor shall cease to have effect during the moratorium period unless the court decides otherwise or the company agrees to such termination; or
- a creditor is precluded from exercising any right of set-off in respect of the obligation due from the company (with the exception of the limitations provided for by the DIFC Netting Law No. 2 Of 2014 in relation to netting agreements).

The creditors are invited to consider the Rehabilitation Plan and if at least three quarters in value of any class of creditors or shareholders agree to the Rehabilitation Plan and it is sanctioned by the court, it then becomes binding on all persons within such class. However, the law also has a 'cram down' mechanism that can apply across the classes of creditors in certain circumstances which has the effect of adding additional flexibility to the procedure favourable to the debtor.

If, following the vote of each class of creditors and shareholders, any member of a class considers the Rehabilitation Plan to be unfairly prejudicial or not in good faith or believes that a violation of the requisite procedures has taken place, an application challenging the Rehabilitation Plan may be submitted to the court.

If the court does not sanction the Rehabilitation Plan the court shall immediately proceed to take steps to wind up the company.

2. Appointment of Administrator in Cases of Mismanagement

An interesting new feature is the introduction of an independent administrator. Where an application for rehabilitation has been made and there is evidence of misconduct, one or more creditors may make an application regarding the appointment of an administrator. Notice of the application for the appointment of an administrator must be given to all creditors of the company. The court may adjourn or dismiss the application or make such other order as it thinks fit.

The administrator must be a person who is registered as an insolvency practitioner in the DIFC and for the period in which the court order is in force, the affairs, business and property of the company shall be managed by the administrator whilst a moratorium shall continue to apply. On appointment of the administrator, any petition for winding up shall be dismissed and any administrative receiver shall vacate their position.

Creditors and shareholders may also apply to the court for protection of their interests if they believe the business and property of the company have been managed by the administrator in a manner that is unfairly prejudicial to them.

3. Adoption of UNCITRAL Model Law

The new law also incorporates the UNCITRAL Model Law ('Model Law') which is designed to assist in cross-border insolvency proceedings in cases involving companies which have assets or creditors in more than one country. The Model Law has been fully adopted into the New Insolvency Law (apart from the insertion of relevant DIFC law concepts).

The Model Law applies where: (i) assistance is sought in the DIFC in connection with foreign proceedings; or (ii) assistance is sought in a foreign country in relation to proceedings under the DIFC Insolvency Law; or

(iii) foreign proceeding and proceedings under the DIFC Insolvency Law are taking place concurrently; or
(iv) creditors or other interested persons in foreign countries are interested in commencing or participating in proceedings under the New Insolvency Law.

The Model Law seeks to ensure that insolvency officials from one jurisdiction are recognised in other jurisdictions and in case foreign proceedings and proceedings under the New Insolvency Law are taking place concurrently, regarding the same debtor, the court shall seek co-operation and co-ordination with the foreign jurisdiction.

The New Insolvency Law seeks to adhere more closely to international best practice, with particular reference to modernisation changes made in other jurisdictions. His Excellency Essa Kazim, Governor of DIFC, stated: "Ensuring that businesses and investors can operate across the region with confidence is crucial to our role in connecting the economies of East and West. We are committed to continuously enhancing our legislative infrastructure in order to give leading global institutions the certainty and access they need to capture the opportunities within the MEASA region, through Dubai."

The New Insolvency Law introduces the latest insolvency procedures with a view to modernising a law that was only 10 years old. This reflects the DIFC's ability to stay at the forefront of global best practice so that the free zone remains one of the premier financial hubs.

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