

A tale of corporate insolvency options for distressed debtors

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*"It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of light, it was the season of darkness, it was the spring of hope, it was the winter of despair."
(Charles Dickens)*

Over the last couple of years, UAE corporate and trading sectors have seen unprecedented financial distress leading to major corporate collapses on account of different economic factors which have lately been exacerbated by the onset of COVID-19. The financial distress was instigated by the commodity crises of 2015 and 2016 which led to declining cash flows of over-leveraged trading companies in the UAE which led to the corporate collapse of renowned mid-market trading entities which had diminishing or negligible cash flows and substantial outstanding debt in the form of working capital facilities from banks and financial institutions. Whilst this period saw various out-of-court restructurings and formation of creditor committees and debt restructurings but this also triggered legal reforms in the UAE with the revamping of the UAE onshore companies' legislation and various free zone companies' regulations and, more importantly, the enactment of a new corporate insolvency law with a view to benefitting the creditors and debtors alike. However, it has been observed that the financially distressed debtors were reluctant to seek bankruptcy protections under the, then nascent, corporate insolvency laws and similarly the creditors also restricted themselves to the tried and tested debt recovery options with notably few bankruptcy cases being adjudicated in local courts. Nevertheless, even after such legal reforms, the financial distress became more contagious and recently infected some of the large corporate groups in commodities, healthcare, real estate and construction sectors which led to further legal reforms in the bankruptcy laws and the such potentially insolvent entities more encouraged to seek stronger bankruptcy protection through local courts or the courts of ADGM and DIFC.

The purpose of this article is to provide some brief illustrative case studies where distressed debtors have sought the assistance of the enabling corporate insolvency regime to seek certain protections by undergoing administration, voluntary liquidation or composition with creditors. The article will also endeavour to cover certain illustrative examples where the creditors have considered options under local law and practice to either rescue or liquidate their debtors.

NMC Healthcare Group - ADGM administration

NMC Group, one of the largest private healthcare providers, collapsed in early 2020 on account of its purported involvement in fraudulent transactions when the group reported a large amount of undisclosed debt early in 2020 with a significant mismatch between the debt and the cash flows. NMC Healthcare Plc (the ultimate parent) was placed in administration in early April 2020 with the appointment of an UK based administrator. In relation to the UAE operating subsidiaries the group adopted a different approach by avoiding seeking protection under the UAE bankruptcy regime (possibly due to the limited tenor of debt

restructuring (i.e. between 3 to 5 years) and decided to re-domicile into the ADGM as ADGM companies in accordance with the Continuance Regime recognised and regulated by the ADGM Companies Regulations. Once the continuance was accepted in the ADGM, the UAE subsidiaries applied to the ADGM Courts for an administration order with the intention to continue the business of the UAE subsidiaries under the supervision of a court appointed administrator in accordance with the ADGM Insolvency Regulations which are almost identical to the UK insolvency regime. The administration of the re-domiciled UAE Companies in the ADGM allows for the financial reorganisation of the UAE subsidiaries under the protection of a statutory moratorium during which creditors are prevented from taking legal action against, or petitioning for the winding-up of the UAE subsidiaries based on the ADGM court order. Further the ADGM court order, in conjunction with the appointment of an administrator, also approved priority funding arrangement (and roll of existing equivalent debt) in accordance with the applicable provisions of the ADGM Insolvency Regulations. It is important to note here that the implementation of ADGM order onshore UAE; it is still not clear as to how such an order will be implemented in the UAE Courts (excluding Abu Dhabi Courts which are subject to the Protocol entered into between ADGM Courts and Abu Dhabi Courts). It is understood that the appointed administrators along with the appointed creditors committee propose a financial reorganisation plan which will be presented to the creditors for voting in accordance with the ADGM Insolvency Regulations.

UAE Exchange

UAE Exchange is one of the largest currency exchange houses in the UAE. As a result of the internal investigations conducted at the parent entity level (Finabl), in early March 2020, the UAE Central Bank announced, in an official notice, that it will oversee UAE Exchange Centre's management. UAE Exchange Central, being supervised by the UAE Central Bank, has suspended remittance services at the time until internal investigations were concluded by the UAE Central Bank. All operations of the UAE Exchange Centre have been placed under the supervision of the UAE Central Bank. The UAE Central Bank's involvement aimed at stabilising the currency exchange market, as the parent entity of UAE Exchange considered insolvency of UAE Exchange. It is clear that the Central Bank did not allow this to happen. The Central Bank exercised its powers under the Federal Law no. 14 of 2018 (the 'Banking Law'), which grants the Central Bank certain powers in relation to distressed or violating financial institutions. Those powers include placing the institution under the management of the UAE Central Bank, merging or reorganising the financial institution, liquidation and/or revocation of licence or change management. Unlike insolvency, the UAE Central Bank's supervision of the management of a financial institution, it does not suspend judicial proceedings by any creditors against such distressed or violating financial institution.

Financial restructuring committee

In 2020, the Financial Restructuring Committee ('FRC') (constituted under the UAE Bankruptcy Law) accepted applications from certain UAE companies, to supervise the financial restructuring of such companies. The FRC issued a notice to all creditors of the designated companies to lodge their claims with the FRC (which is similar to the commencement of bankruptcy proceedings). The FRC further informed creditors to co-operate with the FRC and that there will be further details to be provided in relation to creditor voting and implementation of a 'reorganisation plan'. No further details have been made available public since the issuance of such notices by the FRC. Application to the FRC has recently gained momentum in the UAE by some of the larger distressed UAE entities since the amendment to the UAE Bankruptcy Law which expanded the domain of the FRC. The FRC includes members representing Ministries (Finance, Economy and Justice), Emirates (Abu Dhabi, Dubai and Sharjah) and authorities (the UAE Central Bank and the Securities and Commodities Authority), including the Chairman, the Deputy

Minister of Finance. The financial restructuring through the FRC is a non-judicial option for distressed companies and can be initiated prior to applying to local courts for preventative composition or bankruptcy. Once the FRC accepts an application for supervising financial restructuring, the FRC appoints an expert who operates similar to a trustee in bankruptcy (albeit with a limited powers) and such expert would evaluate the financial status of the applicant, try to reach an agreement with creditors, provide suggestions to the applicant on continuity of business, etc. The trustee does not have the authority to liquidate the applicant company. It is important to note that any financial restructuring under the auspices of the FRC does not impose a moratorium on any judicial proceedings against the debtor or its assets during the course of such restructuring.

Non - Financial Free Zone insolvency options

In addition to the UAE bankruptcy law, some of the economic free zones have also included, in their respective companies regulations, certain insolvency provisions which allow free zone entities to be wound up voluntarily on a solvent basis as well as to be liquidated by the creditors of such free zone entities on an insolvent basis by the appointment of a liquidator by the creditors who will take control of the insolvent free zone entity in accordance with the applicable free zone regulations and such appointment should be approved by the free zone authority. It is also important to note that some free zone regulations (e.g. the DMCC) expressly provide an option of winding up under the UAE bankruptcy law. In a recent liquidation of a commodities firm in the DMCC, the creditors appointed a liquidator in accordance with the DMCC regulations at a creditors meeting which was subsequently approved by the DMCC Authority with a view to the establishing a liquidation committee to conduct the necessary debt mapping, asset tracing and liquidation of such insolvent firm's assets. A legal issue arose in such proceedings as to whether any creditor can initiate and sustain a legal action against such a free zone entity under liquidation. It appears that unless any creditor-driven liquidation, in accordance with the free zone regulations, is not submitted to the local courts (under the UAE bankruptcy law) such liquidation process would not afford the moratorium against legal action as prescribed under the UAE bankruptcy law.

In a recent creditor-driven bankruptcy of a company incorporated in a free zone in Ras Al Khaimah (dealing in the trading of metals) the proceedings were unusually concluded. The company was unable to meet its financial obligations to various suppliers which led one of the company's creditors to file for the bankruptcy of the company with an aim to liquidate the company's assets and benefit from the proceeds of the sale of any of the assets. In accordance with the court's instructions, other creditors joined the bankruptcy proceedings once publicly notified. However, it is interesting to note that the liquidation did not proceed as the court appointed trustee was not able to trace any assets or reach any of the company's managers or staff.

Creditor take over

Recently, creditors (particularly consortium of bank lenders) have explored and, in some cases, implemented plans on attempting to indirectly take over the management and control of defaulting debtors particularly where the managing shareholder has absconded. In some cases, particularly in the information technology and health care sector, creditors requested the court to appoint a judicial guardian over such defaulting companies and their assets as well as oversee the management of the operations of such companies with periodic reporting to the court. In such cases the claimants would need to demonstrate to the court the urgency and the underlying risk of an operating company under negligent management. It is important to note that all revenue earned by the company under such guardianship would be paid into court. Essentially under the judicial guardianship arrangement, the creditors can benefit

from the appointment of a competent guardian to manage the business and revive the cash flow with view to secure the repayment of the outstanding facilities.

Whilst there is a cautious optimism in 2021 with the stimulus packages continuing in the first quarter and potential easing of liquidity squeeze, there are still struggling businesses with challenging cash flow issues which may pursue various avenues on seeking protection under the existing insolvency regimes or directly engaging with creditors for non-judicial restructurings. Therefore, with the current reforms in the insolvency space, 2021 may provide more clarity and potentially jurisprudence in this area with the existing administrations, creditor compositions and liquidations potentially culminating this year.

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