# Sometimes even The Castle must go

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## Last resort

While a lender is highly likely to explore other options first, if a borrower is unable to remedy an event of default under a loan agreement then the lender may be left with little choice but to enforce its security, which is, after all, in place for just such a scenario, to allow a lender to meet a demand on a borrower.

In circumstances where the DIFC or ADGM Courts have jurisdiction (particularly where the relevant asset is based in those jurisdictions) then there are internationally recognised common law regimes for enforcement under which a lender may enforce its security. Lenders, in particular, can have confidence that there are remedies available to them, even as a last resort. As we see below, both the DIFC and ADGM regimes are, to a very large extent, similar and follow familiar English common law legal procedures.

The relevant regimes are established for the most part in the DIFC Real Property Law 2018 and the ADGM Real Property Regulations 2015.

## When may a lender enforce?

Usually, either the loan agreement or the security document will provide that, on the occurrence of an event (such as a breach of a covenant made under the agreement; the most obvious being a covenant to repay, or an insolvency event) then the lender may serve a demand on the borrower, requiring payment of the secured liabilities.

Service of a formal demand, which must be in compliance with the provisions of the security document with regards to giving notice, will mean that all sums due under the loan agreement become due and payable. Even if a formal demand is not required, perhaps because the security document expressly removes the need to make a demand, service may prompt a borrower to remedy the default or at least increase its efforts to do so.

Once a demand has been served, then a lender's right to enforce its security will be determined either by the security document itself, or by way of remedies available under the relevant DIFC or ADGM laws.

# Jurisdiction

The jurisdiction of the DIFC Courts is governed by Dubai Law No. (12) of 2004 Concerning Dubai International Financial Centre Courts (the 'Judicial Authority Law'). Article 5(A)(1)(e) of the Judicial Authority Law is perhaps of most relevance where the asset is real property located in the DIFC, and provides that the DIFC Court has jurisdiction over "any claim or action over which the Courts have jurisdiction in accordance with DIFC Laws and DIFC Regulations." The DIFC Real Property Law applies to all real property in the DIFC (Article 3) and the Dubai Real Estate Laws will not apply unless expressly stated in such laws that it applies in the DIFC (Article 9(1)).

Where a party wishes to enforce security over non-property assets then the DIFC Court will still have jurisdiction under Article 5(A) of the Judicial Authority Law where, in simple terms, a party is a DIFC Establishment (as defined) and particularly where a contract expressly provides for DIFC jurisdiction.

In the ADGM, the Court's jurisdiction is governed by Law No. (4) of 2013 Concerning Abu Dhabi Global Market (the 'Founding Law'). Article 13(6) of the Founding Law provides that the ADGM Court "shall solely consider and decide on matters relating to the activities of the Global Market" including "any request which the Global Market Courts has the jurisdiction to consider under the Global Market Regulations" which includes matters of real property as set out in the ADGM Real Property Regulations.

Further, and as in the DIFC, the ADGM Court will also have jurisdiction to enforce non-property assets where a party is a Global Market Establishment or where a contract expressly provides for ADGM jurisdiction (Article 6, Founding Law).

# Enforcement options available

### *Appoint a Receiver*

A lender which holds security over an asset may consider the appointment of a receiver to take charge of the asset, collect any rent and, if necessary, sell it for the purpose of paying the secured liability.

The security document shall provide for the appointment of a Receiver (Article 42, DIFC Insolvency Law 2019 and Section 152, ADGM Insolvency Regulations 2015), such as in the case of a mortgage, and should set out what the Receiver is entitled to do for example, to run the borrower's business, or to sell any assets required to pay the secured liabilities.

In the DIFC, where a mortgage entitles a lender to appoint a Receiver then it may do so under Article 68 of the DIFC Real Property Law. Similarly, in the ADGM a Receiver is appointed under Section 61 of the Real Property Regulations but unlike in the DIFC, the Receiver would be appointed by the ADGM Court upon an application by the lender.

However, appointed, the Receiver is the agent of the borrower and must, if selling assets, obtain the best price reasonably obtainable in the circumstances (Section 156 ADGM Insolvency Regulations). Indeed, if the Receiver sells a property then he or she will be subject to the same duties as if the lender were selling (Article 68(2), DIFC Real Property Law and Section 61(2), ADGM Real Property Regulations).

The advantages of appointing a Receiver lie in their expertise in managing and if necessary disposing of assets, without interference from a borrower, whilst their costs are added to the loan. If a property has an income stream, this may be an attractive option. The disadvantage is that it is likely to bring an end to the parties' relationship and the property may not sell or cover the loan in full (with the Receiver's costs reducing the amount ultimately recovered by a lender).

### *Appointment of an Administrator*

In an insolvency situation, where a lender considers that a DIFC Establishment already under a rehabilitation plan (and being mismanaged or subject to misconduct), or a company registered under the ADGM Companies Regulations 2020 is unable to pay its debts then it may consider making an application to the relevant Court (under Part 4 the DIFC Insolvency Law 2018, or Section 8 of the ADGM Insolvency Regulations 2015) to appoint an Administrator to take over and control the borrower's business with a view to either rescuing the business or to, at least, repaying the secured liabilities, as far as possible.

Additionally, in the ADGM, if a lender holds a qualifying charge, being a charge over the whole or substantially the whole of a borrower's assets, then it may also appoint an Administrator where the charge expressly provides for such appointment (Section 21, ADGM Insolvency Regulations 2015).

However, the Administrator is not controlled or directed by the lender and (as an agent of the borrower company) must act in the interests of creditors as a whole. Administration is also a lengthy and costly process which a lender may see as a disadvantage, particularly in light of the other options available such as appointment of a receiver, or exercising a power of sale.

### *Possession*

Article 63, DIFC Real Property Law and Section 56, ADGM Real Property Regulations provide that, following default by a borrower, a lender may take possession of a property secured by a registered mortgage. Upon possession, which is obtained by taking physical possession or upon an order of the Court, a lender may collect rent and receive profit in relation to that property. It is a rarely used remedy given that the lender will be liable for the property whilst in possession for example, in respect of insurance and environmental issues, and will be required to account to the borrower for rent and profit received. A lender may therefore prefer to appoint a Receiver, as described above, to take charge of the property and act as a buffer between the lender and borrower.

### *Foreclosure*

While an available remedy for lenders (Article 70, DIFC Real Property Law and Section 62, ADGM Real Property Regulations), foreclosure is not commonly used to enforce security because it is expensive and lengthy, requiring an application to Court, which will control the process. Additionally, following foreclosure a lender will lose the right to pursue the borrower for any additional amounts owed under a loan agreement in circumstances where the value of the secured property is not enough to satisfy the outstanding amounts. In that respect, foreclosure is generally only advantageous in the unlikely enforcement scenario where secured assets are worth more than secured liabilities.

### *Power of sale*

Where a lender has a power of sale over an asset, whether under a security document (usually a mortgage) or under the general law, then it may sell the secured asset and use the proceeds to pay off the secured liabilities.

Where a mortgage provides for a power of sale it will also set out when that power becomes exercisable. That is generally upon an enforcement event which may be defined as an event of default as set out in the relevant loan agreement, likely the same event which caused the demand to be sent.

Where a lender holds a registered mortgage, even if that mortgage security does not expressly set out the power of sale, the DIFC Real Property Law 2018 (Article 63) and the ADGM Property Regulations 2015 (at Section 56) both provide for a mortgagee lender's power of sale.

In both the DIFC and ADGM, the lender must abide by certain duties, for example to obtain the best price reasonably obtainable for the Property, and the lender must apply the proceeds of sale in the prescribed way. Before exercising a power of sale a lender must also provide notice to the mortgagor, who is generally the borrower, as well as any guarantor, other registered mortgagees (and in the DIFC also the Registrar).
In the DIFC, that notice must provide a period of 60 days to allow the borrower to remedy a default before the mortgagee lender may exercise its power of sale or any other remedy set out in Article 63, including entering into possession (and collecting rents) or applying to the Court to foreclose. In the ADGM the notice period is 30 days before a mortgagee may exercise its powers.

Following a sale of a property under a power of sale, the purchaser will take the property free of other interests, including any liability under the mortgage and any subsequent registered interests in the property (Article 66, DIFC Real Property Law and Section 59, ADGM Real Property Regulations).

### *Court ordered sale*

The advantage of a Court ordered sale is that the lender may additionally seek permission to buy the property itself. This would benefit both the lender and the borrower in circumstances where it might be difficult to find a buyer, or where interested parties are not willing to pay the minimum reserve price which the Court will set. If a lender is permitted to bid for and purchase the property in an open market sale (which it would not be able to do if it exercised a power of sale) then the borrower can be satisfied that the best price reasonably obtainable has been reached.

We are aware that lenders in the UAE may be less willing to rely on an express (or implied) power of sale than say English lenders and have seen modifications to mortgage security which requires the permission of the Court prior to exercising a right to sell.

Where a lender's power of sale has been limited in such a way, the ADGM Court, nevertheless, may still provide the lender with a remedy by way of a very wide statutory jurisdiction under Rule 184 of the ADGM Court Procedure Rules 2016. Rule 184 provides that in "*any proceedings relating to real property, the Court may order the real property, or part of it, to be sold, mortgaged, charged, exchanged or partitioned.*"

A similarly wide discretion applies in the DIFC, pursuant to the DIFC Court Law 2004 which provides (at Article 20) that the Court "*has the power, in matters over which it has jurisdiction to make any orders,* *including interlocutory orders, and to issue or direct the issue of any writs it considers appropriate.*" Further, the DIFC Law of Damages and Remedies 2005 provides (at Article 35) that "where a person commits a breach of any requirement, duty or obligation which is imposed under any DIFC Law the Court may… make any other order that the Court thinks fit." It is therefore submitted that, in circumstances where a Court ordered sale is appropriate, or required, the DIFC Court may make such an order, just as in the ADGM.

As we can see, some remedies do not necessarily require any Court approval. Where opposition is expected or where there is a dispute as to the existence of an event of default a lender may take the view that an order from a Court is required before enforcing their security. The ADGM and DIFC Courts are certainly jurisdictions that should inspire confidence for lenders both when negotiating loan facilities, or when considering enforcement of security.

***For further information please contact Jonathan Brooks (j.brooks@tamimi.com).***

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***The Castle*** *is a comic treasure, telling a story of the little guy trying to argue the "law of common sense" in an attempt to keep the family home. Unfortunately, in the world of commercial reality there is often no 'little guy' trying to hang on, no heart strings to pull on, just a complete default of a loan agreement, leaving a lender with nothing but its security to rely on.*