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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 7E**

**UNITED ARAB EMIRATES**

This is the **summative (formal) assessment** for **Module 7E** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 7E**. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentnumber.assessment7E]**. An example would be something along the following lines: 202021IFU-314.assessment7E. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **8 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

The **most significant barrier**, historically, to the development of a culture of distressed business rescue in the UAE has been:

1. The failure of the responsible authorities to enact laws which would encourage a business rescue culture.
2. The low rate of business failure in the UAE.
3. The owners of failed businesses are liable as a matter of criminal law for the failure of their business.
4. There could be criminal law consequences for business owners arising from the security agreements which a business might have with its creditors.

**Question 1.2**

What is the **principal difference** between the “mainland” UAE Bankruptcy Law and the insolvency laws of the two financial centres (the DIFC and the ADGM)?

1. The insolvency laws of the financial centres govern the insolvency of financial service businesses only, while the Bankruptcy Law governs the insolvency all other businesses.
2. The insolvency laws of the financial centres have no application and cannot be enforced in the UAE “mainland” (that is, outside of the financial centres), while the Bankruptcy Law is the only applicable law governing insolvency in the UAE “mainland”.
3. The Bankruptcy Law drew on the experiences of a number of jurisdictions, while the insolvency laws of the financial centres are based on the insolvency laws of one other country.
4. The Bankruptcy Law incorporates substantial elements of Islamic law, while the insolvency laws of the financial centres are based on the common law.

**Question 1.3**

Which statement **correctly describes** the relationship between the Courts of the DIFC and the Courts elsewhere in the UAE?

1. The judgments and orders of the Courts of the DIFC are not enforceable outside of the DIFC.
2. The judgments and orders of the Courts of the DIFC are enforceable elsewhere in Dubai only through the Dubai Courts.
3. The judgments and orders of the Courts of the DIFC are enforceable elsewhere in Dubai only after recognition for enforcement by the Joint Judicial Committee.
4. The judgments and orders of the Courts of the DIFC are not capable of enforcement outside of Dubai.

**Question 1.4**

As regards security in Mainland UAE a secured creditor’s rights, both in relation to real and personal property security, are not substantially affected by any formal insolvency process; the secured creditor can generally enforce its rights notwithstanding the debtor’s insolvency. Is this statement **True or False**?

1. True.
2. False.

**Question 1.5**

Which statement **is correct** in relation to the operation of security interests for both real and personal property in the DIFC?

1. The law regulating security interests in land and personal property in the DIFC is based on Australian law.
2. A mortgagee of land in the DIFC requires a court order to allow it to repossess land subject to a mortgage.
3. The regulating security interests in land and personal property in the DIFC is based on English common law.
4. There are separate registers in which security interests in both land and personal property in the DIFC can be registered.

**Question 1.6**

Which of the following statements is **incorrect** in relation to creditor rights following the Court’s decision to commence preventive composition under the UAE Bankruptcy Law up until the approval of the scheme?

1. All legal claims and proceedings and any judicial enforcement procedures against the debtor are suspended, unless otherwise decided by the Court.
2. The commencement of preventive composition procedures will also suspend any criminal proceedings brought in relation to a dishonoured cheque, including against the signatory of the cheque.
3. Creditors may not bring or pursue claims against persons jointly liable with the debtor or any guarantors of the debtor’s debts.
4. Secured creditors may enforce their securities provided they have obtained Court permission to do so.

**Question 1.7**

Which of the following **is not** a consequence or possible outcome of the commencement of Preventive Composition?

1. Interest on debts owed by the debtor stops accruing on the date of commencement of Preventive Composition.
2. The debtor can borrow further money during the period of preventive composition, with the Court’s permission.
3. The debtor is not allowed to change its ownership in any way.
4. The Court can order the rescission of effective contract to which the debtor is a party.

**Question 1.8**

Which of the following **is not** a basis for an application to the Court for the commencement of bankruptcy proceedings under the UAE Bankruptcy Law?

1. If a secured creditor, having security over all or substantially all of the assets of a debtor, takes steps to enforce its security.
2. If a creditor (or a group of creditors) has given notice to a debtor requiring the debtor to pay a debt of AED 100,000, and the debtor has failed to discharge the debt within 30 business days of that notification.
3. Following the annulment or rescission of Preventive Composition by the Court.
4. If a debtor is in default of its payment obligations for 30 consecutive business days.

**Question 1.9**

Rehabilitation is a new DIFC insolvency procedure introduced by the 2019 law, which allows companies unable to pay their debts but able to reach agreement with its shareholders and creditors to agree to a plan referred to as a Rehabilitation Plan to achieve a court sanctioned plan that binds creditors. In regard to the rehabilitation procedure, which of the following statements is **incorrect**?

1. In order to initiate the rehabilitation process the company is required to make an application to court submitting the rehabilitation plan and nominating the proposed rehabilitation nominee.
2. A moratorium comes into effect for an initial 180 days, preventing creditors from commencing or continuing legal action against the company.
3. The moratorium disapplies contractual provisions that would otherwise enable a contract to be terminated upon insolvency.
4. Any creditor materially prejudiced by the moratorium may apply to court seeking the disapplication of the moratorium in relation to a particular contract.

**Question 1.10**

Which of the following statements **is not** correct?

1. The DIFC Courts will enforce judgments and arbitration awards from other countries in accordance with the Riyadh Convention (Riyadh Arab Agreement for Judicial Co-operation).
2. The DIFC Courts will enforce judgments and awards from other countries if there is a memorandum of understanding with the Courts of that country which enable the DIFC Courts to do so.
3. The DIFC Courts will enforce arbitration awards from other countries in accordance with the New York Convention for the Recognition and Enforcement of Foreign Arbitration Awards.
4. The DIFC Courts will enforce judgments and arbitration awards from other countries, even if the debtor has no presence of any type in the DIFC.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 2 marks]**

What is the key point of distinction regarding the registration of real property interests, including mortgages, in the different emirates of the UAE? What is the key difference between the sale of mortgaged real property following a debtor default if that real property is in a financial free zone or if the real property is in “mainland” UAE?

Each emirate maintains its own land registration system for the registration of real property interests and so the registration of real property interests, including mortgages, can be subject to different laws and procedures in each emirate.

In regards to the sale of mortgaged real property following a debtor default:

1. If that property is in the financial free zone, without court order, and following entering into possession of the land by providing 60 days’ notice to certain relevant parties, the mortgagee can sell the whole or part of the land, receive rents and profits from the land and apply the proceeds of sale in payment of the debt; whereas
2. If that property is in mainland UAE, the mortgagee will need to obtain a Court order for sale in order to sell the mortgaged property and once this has been obtained, the Court’s execution department will handle the sale.

**Question 2.2 [maximum 4 marks]**

Preventive Composition and Restructuring are both insolvency processes that an entity can adopt under the UAE Bankruptcy Law. They share a number of similarities regarding the entry into and conduct of each of the respective processes. While the processes are different, various “actors” assume similar roles in each process. For all of the processes, which actor is responsible for each of the following:

1. A decision on any application to commence an insolvency process;
2. A primary determination as to whether a debtor’s proposal should be adopted;
3. Confirmation of the primary determination as to whether a debtor’s proposal should be adopted;
4. For supervising the implementation of the insolvency process by the debtor.
5. The Court.
6. The debtor’s creditors (only those whose debts have been admitted may vote, except that the Court may direct that creditors whose debts have been admitted on an interim basis may vote, and secured creditors may not vote, unless they have surrendered their securities).
7. The Court.
8. The trustee.

**Question 2.3 [maximum 2 marks]**

Under the UAE Bankruptcy Law, for a debtor, what is the key difference between the circumstances which could give rise to an application to commence Preventive Composition or an application to commence Bankruptcy (whether leading to Restructuring or Liquidation)?

An application to commence preventive composition can only be made by the debtor and must be made under Article 6 of the UAE Bankruptcy Law where the debtor is experiencing financial hardship and requires assistance to reach settlements with its creditors. An application for preventive composition will terminate the requirement for the debtor to initiate bankruptcy proceedings in certain circumstances under UAE Bankruptcy Law.

This is in contrast to an application to commence bankruptcy, which can follow a number of different circumstances and be made by either a debtor or a creditor. These circumstances include the following (but are subject to the Federal Decree Law 21 of 2020, currently in place for the period from 1 April 2020 to 31 July 2021):

1. If a debtor is in default of its payment obligations for 30 consecutive business days.
2. If a creditor (or a group of creditors) has given notice to a debtor requiring the debtor to pay a debt of AED 100,000, and the debtor has failed to discharge the debt within 30 business days of that notification.
3. Following the annulment or rescission of preventive composition by the Court.

**Question 2.4 [maximum 2 marks]**

What is the key difference for a creditor regarding the commencement of Preventive Composition or Bankruptcy of a debtor?

The key difference for a creditor regarding the commencement of preventive composition or bankruptcy of a debtor, is that only the debtor can pursue an application to commence preventive composition; whereas, either the debtor or creditor can submit the application to Court for an order initiating bankruptcy proceedings.

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1 [maximum 5 marks]**

Briefly explain the historical background to the introduction of the Bankruptcy Law. Describe which entities the Bankruptcy Law applies to and how it has been received and applied in the UAE.

Law No 18 of 1993 relating to commercial transactions contained certain insolvency provisions for those engaged in commerce, via a bankruptcy process to be pursued through the Courts; however, this was rarely used and insolvency law was generally considered as underdeveloped in the UAE (particularly highlighted in 2009, when Dubai World faced the possibility of defaulting on its debts). This changed when the Federal Decree Law (No 9) of 2016 was introduced in 2016 and amended in 2019 and 2020 (the **Bankruptcy Law**). The Bankruptcy Law repealed the provisions of Law No 18 of 1993 which related to insolvency, and replaced these with a consolidated insolvency regime for commercial insolvencies, which applies to all companies governed by the Commercial Companies Law, companies which are wholly or partly owned by the federal or local government and which have chosen to submit to the Bankruptcy Law, free zone companies (other than those incorporated in the ADGM or DIFC), any individual who is a “trader” and professional firms (Article 2, Bankruptcy Law).

Then, in 2019, the Federal Decree Law (No 19) of 2019 (the **Personal Bankruptcy Law**) was adopted, which established a consolidated insolvency regime for those insolvencies which did not fall within the remit of the Bankruptcy Law. The provisions of the Personal Bankruptcy Law largely mirror the Bankruptcy Law provisions.

It has been reported that the introduction of the Bankruptcy Law has been “heralded”[[1]](#footnote-1) and welcomed by the practitioners, with international law firm HFW stating that the revisions made the law “more fit for purpose”[[2]](#footnote-2). However, it has also been reported that the introduction of the Bankruptcy Law has had limited impact due to the lack of both understanding of the legislative framework and bankruptcy experience amongst local practitioners[[3]](#footnote-3). This may all change as businesses continue to collapse as a result of the pandemic and the associated lockdowns and an uptake in use of the Bankruptcy Law is likely to occur over the coming year, once the temporary COVID relief measures are lifted.

**Question 3.2 [maximum 8 marks]**

If a debtor company seeks to enter bankruptcy, describe the ways in which the Court is required to be actively engaged in the Restructuring in Bankruptcy Process (assume that a restructuring is possible, that there are no unusual features to the bankruptcy, there are no secured creditors and there has been no criminal conduct by any person involved in the debtor). Your answer should provide references to the legislation.

Chapter Four of the Bankruptcy Law[[4]](#footnote-4) regulates the restructuring in bankruptcy process (Article 67(1)) and the Court is required to be actively engaged and involved with the entire restructuring in bankruptcy process, from liaising with the trustee and determining the disputes of creditors to issuing the final decision. The key steps of the restructuring in bankruptcy process, which the Court is involved in, are set out below.

1. In order to commence the restructuring, either the debtor or creditor must apply to the Court in accordance with the provisions of the Bankruptcy Law and pursuant to Articles 68 and 69 respectively. Once the application is made, the Court will first consider whether the documents submitted are sufficient to determine the application – if they’re insufficient, then the Court may grant an extension so that additional details or documents can be provided (Article 73(3)). In addition, the Court may decide to appoint an expert to assist in the evaluation of the debtor’s status (Article 77(1)) and summon any person who may possess information relevant to the application (Article 80(1)).
2. Next, the Court shall determine the application within five (5) business days from either the date the application is filed or the date the export’s report is filed, and if the application meets the requirements under the Bankruptcy Law, then the Court shall order the commencement of the restructuring procedure (Article 78). The Court also has discretion to dismiss an application where there has been a failure to submit documents and details required or to accept it, even where there are shortcomings in the application, if considered proper by the Court and subject to the interests of creditors (Article 79). The Court shall also decide (upon request of an interested party or of its own accord) to take necessary measures to manage the debtor’s assets (Article 81(1)).
3. If the Court decides to accept the restructuring application, then the Court shall appoint a trustee (Article 82). The Court is further involved even after the appointment of the trustee as the trustee may file with the Court any application that would assist the trustee in the performance of the assignment (Article 83), including with respect to suspending interest and other penalties for non-payment (Article 163), and any grievances that interested parties have with the estimation of fees and expenses of the trustee will be determined by the Court (Article 85(3)). The Court may also at any time replace the trustee appointed or appoint additional trustees or experts, as necessary (Article 86(1)), and the trustee may apply to the Court to be discharged from its duties (Article 86(2)).
4. The trustee shall be responsible for preparing the list of creditors of the debtor and establishing the list of the names of creditors who submitted their claims and depositing copies with the Court (Article 89 and Article 93); however, the Court shall be responsible for determining any grievance against the claims listed (Article 94(2)) and for approving the list of the creditors whose debts are accepted (Article 94(8)).
5. Next, the trustee’s report on the debtor’s business will be reviewed by the Court and the Court shall verify that it includes all claims (Article 97(1)). The Court may also instruct the trustee to make certain amendments to the report (Article 97(2)).
6. Then, there will be a hearing for consideration of the report and it will be the Court’s decision on whether to proceed with the restructuring and to instruct the trustee to prepare a plan for the restructuring of the debtor’s business, where the debtor expresses willingness to continue the business and upon hearing the trustee’s statement that it would be possible to do so and for the business to be profitable again within a reasonable period of time (Article 98).
7. If the Court issues a decision to proceed with the restructuring, it is also the Court’s decision on whether the initial term of three (3) months provided in order for the trustee to prepare the restructuring plan is extended (Article 99) and the trustee is required to liaise with the Court on a regular basis (at least every 21 business days) on the progress of the restructuring plan (Article 100).
8. Once the restructuring plan has been prepared, the trustee shall deposit a copy with the Court (Article 101(1)), which the Court shall review to ensure it takes into consideration the interests of all parties and may instruct the trustee to make amendments (Article 103(1)).Then, the Court shall instruct the trustee to issue within five (5) Business Days, invitations to the creditors to attend a meeting to discuss and vote on the restructuring plan (Article 103(3)).
9. The Court also has the ability to issue a decision establishing creditors’ committees to discuss the plan and propose amendments (Article 104(1)) and it’s in the Court’s discretion to decide whether to approve or dismiss any proposed amendments (Article 105(3)).
10. At the creditors’ meetings, the right to vote on the restructuring plan generally is limited to the ordinary creditors whose debts are finally accepted; however, the Court again has involvement here and may permit the creditors whose debts are provisionally accepted to vote on the restructuring plan (Article 106).
11. Following approval by a majority vote of the creditors, it will be the Court who has final decision on whether to approve the restructuring plan and its decision will be final and binding (Article 108).
12. It’s the trustee’s role to supervise the implementation of the plan (Article 114(1)), but the Court is still involved here as the trustee must submit a report to the Court on the progress of implementation every three (3) months, report any default in the plan’s implementation to the Court (Article 114(2)) and ask the Court for approval of any amendments to the plan, which the trustee considers necessary during implementation (Article 114(3)).
13. Upon fulfilment of the obligations provided for in the restructuring plan, the Court shall (at the request of the trustee, debtor or interested party) issue a decision confirming completion of the implementation of the restructuring plan and the conclusion of the debtor’s restructuring procedures (Article 115). It is also in the Court’s power to terminate a restructuring and commence liquidation on its own initiative or on the application of an interested party or if the scheme’s implementation is impossible (Articles 118 and 123).

**Question 3.3 [maximum 2 marks]**

In any insolvency system that involves the forced compromising of individual creditor claims, the requirement for court involvement is to ensure that the rights of all parties, including individual creditors, are being protected. The UAE Bankruptcy Law requires a high degree of Court involvement. Briefly describe (100-150 words) whether you consider that the level of Court involvement in approving a restructuring to be appropriate. Provide reasons for your answer.

I think the high level of Court involvement in the restructuring process is crucial for it to operate effectively, particularly in a jurisdiction where the process is relatively new and practitioners are still gaining experience on the process. The Court should have the necessary expertise and independence to make decisions in the interests of both the debtor and the creditors as a whole and the Court’s oversight helps to combat the unpredictability and uncertainty around the process, which can be created by the lack of precedent and expertise and experience of local practitioners and market players. The Court’s involvement also ensures the trustees have accountability to an independent body, the timeline is complied with and both the debtor and creditors have a body to whom they can address their objections, which will then be resolved by final and binding decisions.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

VGK LLC operates a restaurant chain in various locations in Dubai. It was a thriving and successful business but had to cease operations temporarily due to the effects of COVID-19. It has exhausted all available funds and has no cash to pay creditors. VGK LLC owns a restaurant site which is under development, but the development is not expected to be completed for seven months. The site had been purchased by one of VGK LLC’s shareholders and was transferred to VGK LLC on the basis that payment for the site would be made by VGK LLC to the shareholder in full in 2024. In the meantime, the shareholder holds a mortgage over the property for the unpaid purchase price.

**Answer the questions that follow:**

**Question 4.1 [maximum 5 marks]**

The process of Preventive Composition requires adherence to a number of time-frames. Briefly outline the necessary steps and 10 specific steps that will determine the maximum time taken between making an application (the first step) and the registration of the scheme following final approval (the tenth and final step before its implementation).

Assume that: an expert’s report is required by the Court; there are no disputes about whether a creditor is accepted or not; there are no amendments to the proposed scheme by the Court; the scheme is accepted by the creditors without the requirement for any adjournment of the creditors’ meeting; the scheme is approved by the Court following the meeting; and there are no other extensions.

By way of overview of the process, an application for preventive composition must be made by the debtor to the Court, who will determine whether or not to accept the application. The Court may appoint an expert to assist it with making this determination. If the application is accepted, a trustee shall be appointed by the Court who shall prepare a list of creditors, who have submitted claims in respect of the debtor, and prepare the proposed scheme, both of which the trustee shall deposit with the Court. If each of these are satisfactory and in accordance with the provisions of the Bankruptcy Law, the Court shall then order meetings of creditors to vote on the scheme. If approved by the creditors by a statutory majority holding at least two thirds in aggregate of the total ordinary debt, the proposed scheme shall be submitted to the Court for final approval. Once approved, it shall be registered by the trustee. The necessary steps to be completed between making an application for preventive composition and the registration of the scheme, following final court approval, along with the time frames they are required to be completed in, are set out in detail in numbers 1-10 below. These steps make the assumptions stated in the facts and all references to “Articles” in this answer refer to Articles of the Bankruptcy Law.

1. First, the debtor (VGK LLC) shall apply to the Court to commence the Preventive Composition procedure in accordance with Article 6.
2. The Court may appoint an expert to prepare a report on the financial position of the debtor, including an assessment as to whether the conditions required to accept the application are met and whether the debtor’s assets are sufficient to implement the Preventive Composition (Article 13(1)-(2)). The Court shall determine the duties and remuneration of the expert and the period for submission of the expert report, provided that such period shall not exceed 20 business days from the date the expert is notified of the appointment (Article 13(4)).
3. The Court shall then decide whether to accept or reject the application within 5 business days from the date on which the expert submits the report (Article 14(1)).If the Court decides to accept the application for Preventive Composition, it shall appoint a trustee and shall notify the trustee of the appointment within 1 business day from the issuance of the order (Article 17).
4. Immediately upon appointment, the trustee shall carry out an inventory of the debtor’s assets (Article 22(1)). The trustee shall prepare a register of all the known creditors of the debtor and provide a copy to the Court (Article 24(1)). In addition, within 5 business days of receiving the notice of appointment, the trustee shall: (i) publish the decision to commence the procedure in two widely distributed daily newspapers, one in Arabic and the other in English, and invite any creditors to submit their claims and supporting documents to the trustee; and (ii) notify all creditors with known addresses to provide their trustee with their claims and supporting documents. In each case, creditors’ shall be required to submit their claims within 20 business days from the date of publication of the decision to commence the preventive composition procedure (the **Creditors’ Claim Period**) (Article 35).
5. Following the expiry of the Creditors’ Claim Period, the trustee shall prepare the list of creditors who have submitted claims and deposit such list with the Court within 10 business days of expiry of the Creditors’ Claim Period (Article 37(1)). The trustee shall publish the lists within 3 business days of depositing the list with the Court (Article 37(2)). The debtor and every creditor has 7 business days from the date of publication of the list to object to the list (Article 38(1)) and any objection shall be determined within 10 business days from the date of submission (Article 38(2)). The Court shall then approve the list of creditors whose debts are finally and provisionally accepted (Article 38(8)).
6. The debtor shall assist the trustee with preparation of the proposed scheme for submission to the Court within 45 business days from the date of publication of the commencement order (Article 40(1)).
7. The Court shall review the proposed scheme within 10 business days from the date of submission to ensure it takes into consideration the interests of all parties and if it finds the proposed scheme satisfactory, it shall instruct the trustee to invite the creditors to a meeting to discuss and vote on the proposed scheme within 5 business days (Article 42(1)-(2)). The invitation to the creditors’ meeting shall be published in two widely distributed local daily newspapers, one in Arabic and the other in English, and the meeting shall be held within 15 business days from the date of publication of the invitation or as determined by the Court in its discretion (Article 42(3)-(4)).
8. At the creditors’ meeting, the trustee and debtor shall explain the terms of the proposed scheme (Article 44(1)) and the ordinary creditors whose debts have been finally accepted (subject to the exception in Article 45(2)) shall vote on the proposed scheme (Article 45(1)). The proposed scheme will be approved by the creditors if (i) the majority of the creditors permitted to vote, vote in favour of the scheme, and (ii) such majority of creditors who voted in favour hold in the aggregate at least two thirds of the accepted value of the total ordinary debts (Article 47(1)).
9. Following approval of the scheme by the creditors, the trustee shall within 3 business days from the date of such approval (the **Court Approval Period**), present the proposed scheme to the Court (Article 49(1)). Any creditor whose debt is accepted and who voted not to approve the scheme may object to the draft submitted to the Court within 3 business days from the expiry of the Court Approval Period and the Court shall determine such objection within 5 business days from the date the objection is filed (Article 49(2)).The Court shall issue its decision approving the scheme on an urgent basis and this decision shall be binding on all creditors (Article 49(3)).
10. Within 7 business days from the date of the Court’s approval of the scheme, the trustee shall register the Court’s decision in the commercial or professional register (as the case may be) and publish the decision in two widely distributed local daily newspapers, one in Arabic and the other in English (Article 54).

**Question 4.2 [maximum 5 marks]**

VGK LLC’s creditors rejected the proposed Preventive Composition scheme after a process of nearly four months. During that time, creditors, including staff, were not paid. The owners consider that without creditor support, restructuring would be impossible and liquidation is the only option available. With specific reference to the facts described above, describe the process that would be followed as part of any liquidation and, in particular, considering who could be appointed as trustee.

Following the rejection by VGK LLC’s creditors of the proposed preventive composition scheme and the decision by the owners that the restructuring would be impossible without creditor support, the process set out below would then be followed.

1. The Court may decide of its own accord or following application of a creditor to terminate the preventive composition procedure and to convert it to a declaration of bankruptcy where the scheme is impossible to implement (which, based on the owners’ believe, would be satisfied) and terminating the procedure would result in a cessation of payment by the debtor for more than 30 successive business days as a result of the debtor’s distressed financial position or the debtor is in a state of over-indebtedness (which presumably is the case, given that VGK LLC has exhausted all available funds and has no cash to pay creditors) (Article 65(2)). Where a judgment is issued declaring the company’s bankruptcy and liquidation of its assets, all the joint partners in the VGK LLC shall also be declared bankrupt (Article 142(1)).
2. Once the Court has made the decision to convert the preventive composition procedure to a liquidation, the appointment of the preventive composition trustee shall be terminated (unless the Court decides otherwise and that trustee is appointed as the bankruptcy trustee) and the Court shall carry on with the bankruptcy procedure and liquidation of the VGK LLC’s assets (Article 66).
3. The Court shall appoint a trustee pursuant to Article 126, where the Court has ordered a declaration of bankruptcy and liquidation of assets. For bankruptcy procedures, a creditor of the debtor, any person against whom a final judgment is issued in connection with certain dishonesty offences, or a person who has been a partner, employee, auditor or agent of the debtor in the preceding 2 years may not be appointed as the trustee (Article 84). This means that the shareholder of VGK LLC is precluded from being appointed as trustee. For completeness, a spouse, in-law or kin up to the fourth degree of the debtor may also not be appointed as trustee, but given that VGK LLC is a corporate entity, this won’t apply. The Court shall also appoint one or more secretaries for the joint partners in the company – their bankruptcy procedures shall be independent in terms of their realisation of debts, management and completion (Article 142(3)).
4. The Court shall notify the trustee of the appointment and within 3 business days of receiving the notice of appointment, the trustee shall publish the decision to commence liquidation in two widely distributed daily newspapers (Article 128). The trustee shall instruct VGK LLC’s creditors to submit any final claims within 10 business days from the publication of the judgment (Article 129). The trustee shall notify the Court and the debtor on a monthly basis of the progression of the bankruptcy and liquidation (Article 134(1)).
5. The trustee shall make a final audit of the creditors’ claims (except that the trustee shall not complete such audit if the trustee finds that the proceeds of the sale of the debtor’s assets will be all spent on payment of legal fees or secured debts) (Article 130).
6. The trustee shall liquidate all of the debtor’s assets with the exception of those assets to be kept pursuant to the Bankruptcy Law (Article 132(1)). If it is found that VGK LLC’s assets are insufficient to settle at least 20% of its debts, the Court may order all or any of the members of the board of directors or the managers, to pay its debts in certain circumstances where those persons are responsible for the losses and if in the two years prior to the proceedings, any such persons acted in a way where they used commercial methods without considering their risks, undertook transactions for insufficient consideration or preferred certain creditors in the payment of their debts over other creditors with the intent to cause harm to other creditors (Articles 144 and 147).
7. The trustee shall distribute the liquidation proceeds according to the priority among creditors, upon approval by the Court (Article 137(1)). Section 6 of Chapter 5 of the Bankruptcy Law requires that distributions are made in the following order:
8. Secured debts shall rank in priority to ordinary creditors (Article 185(1)). Where assets are subject to a security interest, the proceeds of sale are to be applied in payment of the debts owed the secured creditor, less the trustee’s costs of sale (deducted pursuant to Article 185(2)), with any surplus after sale being returned to the debtor (Article 137(6)-(7) and Article 188(1)). If the value of the secured assets is insufficient to pay the full amount of the debt secured by that charge, the outstanding balance shall be ranked as an ordinary debt (Article 137(6) and Article 188(2)). As the restaurant site is secured by a mortgage in favour of VGK LLC’s shareholders, they would be paid the secured amount (i.e. the unpaid purchase price), upon sale of the site (provided that such amount obtained from the sale is sufficient to satisfy the amount secured by the mortgage).
9. For all other assets, the payment waterfall is as follows (Article 189):
   1. The fees of the Court, the trustee and any expert
   2. Employees’ unpaid wages and up to a maximum of three months’ unpaid salary (this means that VGK LLC’s employees, who have not had wages paid, would rank as a preferred creditor for the amount of the first three months of their unpaid salary)
   3. Alimony debts under a judgment against the debtor
   4. Amounts due to government authorities
   5. Costs incurred in supplying the debtor with goods and services following the commencement of the bankruptcy
   6. Unsecured ordinary creditors (this would include the amounts due to the VGK LLC’s employees for the fourth month of unpaid salary)
10. Upon completion of the final distribution of VGK LLC’s assets to its creditors, the Court shall issue a decision to conclude the liquidation, including the final list of creditors and the amounts remaining unpaid, and shall instruct the trustee to publish that decision in two widely distributed local newspapers (Article 138(1)). The trustee will return to the debtor all of the documents in its custody (Article 138(2)).
11. Following conclusion, any creditor whose debt was accepted but not repaid in full may enforce that debt against any remaining assets of the debtor in order to recover the outstanding balance (Article 138(4)).

**Question 4.3 [maximum 5 marks]**

VGK LLC incorporated and registered a fully-owned subsidiary company in the DIFC to operate a restaurant in the DIFC, The subsidiary is called VGK Limited and it is incorporated as a DIFC company. VGK Limited is also unable to pay its debts. What actions can VGK Limited’s creditors take if they wish to see VGK Limited liquidated in the DIFC? In particular, who can take such actions and what steps would have to be taken? If the VGK was to be wound up, who would be responsible for it and what process would be adopted for addressing creditor claims in the winding up?

If VGK Limited’s creditors wish to see VGK Limited (the **Company**) liquidated in the DIFC (and assuming that the Company has not passed its own resolutions in respect of its solvency and a voluntary winding-up), its creditors can make an application for the winding up of the Company to the Court (Article 83, DIFC Insolvency Law[[5]](#footnote-5) - all other references to an “Article” in this answer is a reference to an Article of the DIFC Insolvency Law).

The Company may be wound up by the Court if it is unable to pay its debts (Article 81(b)). Pursuant to Article 82, the Company will only be deemed as unable to pay its debts if:

1. a creditor to whom the Company is indebted a sum exceeding $2,000.00 which is due and payable has served a written demand on the Company, by leaving it at the Company's registered office, requiring the Company to pay the sum due and the Company has for 3 weeks thereafter, neglected to pay the sum or agree terms relating to its payment to the reasonable satisfaction of the creditor;
2. execution or other process issued on a judgment, decree or order of any Court in favour of a creditor of the Company is returned unsatisfied in whole or in part;
3. it is proved to the satisfaction of the Court that the Company is unable to pay its debts as they fall due; or
4. it is proved to the satisfaction of the Court that the value of the Company's current assets is less than the amount of its current liabilities, taking into account its contingent and prospective liabilities.

It seems most likely that the creditors will wish to pursue an application under option (a) above and so there will need to be a creditor whose debt has exceeded $2,000 and has served a written demand on the Company, which has remained unpaid for 3 weeks. For completeness, it’s worth noting that an application to the Court for compulsory winding up may also be submitted by the Company and its directors (as well as a creditor or the creditors, including any contingent or prospective creditor(s)) (Article 83).

Following the order of the Court that the Company should be wound up, the creditors may nominate a person to be liquidator (Article 90(2)). The liquidator is responsible for winding up the affairs of the Company and for ensuring that the assets of the Company are secured, realised and distributed to the Company’s creditors (Article 93) and has a broad range of powers as set out in Schedule 3 of the DIFC Insolvency Law. In particular, the liquidator may call for claims for creditors and has the power to prove, rank and pay creditors’ claims and may do all such things as may be necessary for winding up the Company’s affairs and distributing its assets (paragraphs 1, 8 and 13 of Schedule 3).

To address a creditor’s claim in liquidation, the creditor must submit a proof of debt to the liquidator and provide supporting information to allow the liquidator to verify the claim (DIFC Insolvency Regulations[[6]](#footnote-6), regs 6.16 and 6.17). The liquidator will then admit or reject any proofs of debt for the purposes of determining whether to make a payment to the creditor (reg 6.19, DIFC Insolvency Regulations). The liquidator’s decision in this regard may be appealed by the creditor by application to the Court within 21 days of receiving notice of the decision (reg 6.20, DIFC Insolvency Regulations). The liquidator may declare and distribute a dividend among the Company’s creditors whenever the liquidator has sufficient assets (reg 6.46, DIFC Insolvency Regulations). All debts of the Company will rank equally in any distribution, unless the debts are preferential debts (reg 5.47, DIFC Insolvency Regulations and Article 75).

**\* End of Assessment \***

1. HFW, “UAE insolvency - A new era or another false dawn?”, published on Lexology on 17 May 2021 and available at: https://www.lexology.com/library/detail.aspx?g=76dbbb82-fd6f-4d8d-b0e6-539354389f5c#:~:text=The%20UAE%20established%20a%20formal,the%20Bankruptcy%20Law%20was%20passed.&text=For%20the%20first%20time%2C%20distressed,financial%20restructuring%20and%20composition%20procedures. [↑](#footnote-ref-1)
2. Ibid. [↑](#footnote-ref-2)
3. Ibid. [↑](#footnote-ref-3)
4. Federal Decree Law (No 9) of 2016 as amended in 2019 and 2020, available at: <https://www.mof.gov.ae/en/lawsAndPolitics/govLaws/Documents/Bankruptcy%20law%20in%20English%2004%20May%202017%20%28ready%20for%20publishing%29.pdf>. All references to Articles within this response are references to Articles of the Bankruptcy Law. [↑](#footnote-ref-4)
5. Insolvency Law DIFC Law No.1 2019, available at: <https://www.difc.ae/application/files/5016/0153/9517/Insolvency_Law_No_1_of_2019.pdf> [↑](#footnote-ref-5)
6. DIFC Insolvency Regulations 2019, available at: <https://www.difc.ae/application/files/6115/6032/5954/Insolvency_Regulations.pdf/> [↑](#footnote-ref-6)