



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: [studentID.assessment7E]. An example would be something along the following lines: 202223-336.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 "studentID" 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 2023. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2023. 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 10 pages.**

ANSWER ALL THE QUESTIONS

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

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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

One of the most significant barriers to the restructuring process in the UAE has been:

- (a) The failure of the responsible authorities to enact laws which would encourage a business rescue culture.**
- (b) The low rate of business failure in the UAE.**
- (c) The absence of a moratorium on creditor actions after the commencement of a bankruptcy proceeding inhibits the restructuring process.**
- (d) 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)?

- (a) 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.**
- (b) 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".**
- (c) The Bankruptcy Law drew on the experiences of a number of jurisdictions, while the DIFC and AGDM insolvency laws and regulations are primarily based on the insolvency laws of one other country.**

Commented [SE2]: The correct answer is C.

(d) 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 in mainland UAE?

- (a) The judgments and orders of the courts of the DIFC are not enforceable outside of the DIFC.**
- (b) The judgments and orders of the courts of the DIFC are enforceable elsewhere in Dubai only through the Dubai courts.**
- (c) 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.**
- (d) 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?

- (a) True.**
- (b) 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?

- (a) The law regulating security interests in land and personal property in the DIFC is based on Australian law.**
- (b) A mortgagee of land in the DIFC requires a court order to allow it to repossess land subject to a mortgage.**
- (c) The regulating security interests in land and personal property in the DIFC is based on English common law.**

- (d) **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?

- (a) **All legal claims and proceedings and any judicial enforcement procedures against the debtor are suspended, unless otherwise decided by the court.**
- (b) **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.**
- (c) **Creditors may not bring or pursue claims against persons jointly liable with the debtor or any guarantors of the debtor's debts.**
- (d) **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?

- (a) **Interest on debts owed by the debtor stops accruing on the date of commencement of preventive composition.**
- (b) **The debtor can borrow further money during the period of preventive composition, with the court's permission.**
- (c) **The debtor is not allowed to change its ownership in any way.**
- (d) **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?

- (a) **If a secured creditor, having security over all or substantially all of the assets of a debtor, takes steps to enforce its security.**

(b) 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.

(c) Following the annulment or rescission of preventive composition by the court.

(d) If a debtor is in default of its payment obligations for 30 consecutive business days.

Question 1.9

Rehabilitation is a 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?

(a) 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.

(b) A moratorium comes into effect for an initial 180 days, preventing creditors from commencing or continuing legal action against the company.

(c) The moratorium disappplies contractual provisions that would otherwise enable a contract to be terminated upon insolvency.

(d) 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 incorrect?

(a) 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).

(b) A foreign judgment is enforceable in mainland UAE as long as there is reciprocity between the UAE and the foreign state issuing the judgment for which enforcement is sought.

(c) The ADGM courts may recognise reciprocity with a foreign jurisdiction in the absence of an applicable treaty if the Chief Justice of the Courts is satisfied that

Commented [SE3]: The correct answer is B.

substantial reciprocal treatment will be assured regarding recognition and enforcement in that foreign country of the judgments of the ADGM courts.

(d) 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 in total]

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Question 2.1 [maximum 2 marks]

Commented [SE5]: 2/2

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 of the emirates has its own land registration system, which means that the registration and enforcement of mortgages is likely to vary slightly across the UAE. Nevertheless, the overarching substance of the law should be the same.

If a debtor were to default on their "on-shore" registered mortgage, the mortgagee would have to enforce their security through the courts by petitioning the local judge to sell the property in order to settle the debtor's outstanding obligations. It appears that in order to initiate the sales process, the mortgagee does not necessarily need to obtain a court judgement in relation to the mortgage debt, although (time and costs are permitting) it is usually better to take the belt and braces approach when dealing with local courts.

As far as "off-shore" security is concerned, DIFC has a separate register of ownership for land. In the event of default by the debtor, the mortgagee can take ownership of the land without court involvement. Instead the creditor would provide 60 days' notice to relevant parties, after which they can sell the entire plot (or portions) of land, receive rents and profits, in addition to applying the proceeds from sale to offset the outstanding liability. ADGM has adopted a similar position to DIFC.

Question 2.2 [maximum 4 marks]

Commented [SE6]: 2/4

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. Which actor is responsible for each of the following processes?

(a) A decision on any application to commence an insolvency process.

Debtor (assume we are looking for the “common” actor in both cases, since a creditor can initiate “an insolvency process” as well)

(b) A primary determination as to whether a debtor’s proposal should be adopted.

A court-appointed expert

(c) Confirmation of the primary determination as to whether a debtor’s proposal should be adopted.

Court

(d) To supervise the implementation of the insolvency process by the debtor.

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)?

Preventive composition is a corporate rescue procedure initiated by the debtor, via an application to the court for the appointment of a composition trustee. At the time of the application to the court, the debtor cannot be insolvent using either the balance sheet or the cash-flow test. Furthermore, this rescue procedure is limited to debtors who had not previously entered preventive composition and are not currently subject to bankruptcy proceedings.

On the other hand, either a debtor or one of its creditors can petition the court for the initiation of bankruptcy proceedings. A debtor is obliged to initiate bankruptcy proceedings if it has been in default for 30 consecutive business days, although they may be exempted from the initiation of bankruptcy proceedings during a period of an Emergency Financial Crisis as established by the UAE Cabinet.

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?

Preventive composition procedure can only be initiated by a debtor under the circumstances described above. Therefore, a creditor cannot initiate this procedure, although they will have to submit their “proof of debt” in order to be able to vote on any scheme proposed by the debtor and the composition trustee. In addition, unsecured creditors are most certainly impacted by the initiation of preventive

Commented [SE7]: A decision on an application (which has already been submitted by a debtor or creditor) is made by the court.

Commented [SE8]: This is the role of the unsecured creditors.

Commented [SE9]: 2/2

Commented [SE10]: 2/2

composition proceedings as a result of a moratorium on financial, legal and criminal proceedings.

On the other hand, a creditor (or a group of creditors) can initiate bankruptcy proceedings, providing a statutory demand for an amount in excess of AED100,000 has been outstanding for more than 30 days. There is no clear guidance on what constitutes a "debt", and therefore a number of stakeholders can initiate bankruptcy proceedings including shareholders, a "controlling body" and the public prosecutor. Likewise, a debtor may be exempted from bankruptcy proceedings during a period of an Emergency Financial Crisis as established by the UAE Cabinet.

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

Question 3.1 [maximum 5 marks]

Commented [SE11]: 5/5

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.

At a high level, the Bankruptcy Law applies to "on-shore" entities, companies registered in free-zones without their own insolvency laws (e.g., Jebel Ali Free Zone) as well as individuals engaged in commercial activities in a personal capacity. State owned enterprises are not subject to the provisions of the Bankruptcy Law unless they have explicitly opted into it.

Considering the UAE only became a nation in 1971, as a federation of six emirates (subsequently expanded to seven), it would be fair to say that its rapid economic growth over the last five decades has played a substantial role in transforming the country's legal landscape. It is no surprise that the local insolvency law initially catered primarily to traders and were therefore not best placed to address the insolvencies of the likes of Dubai World in 2009. In response to these challenges, Federal Decree Law (Number 9) of 2016 (the Bankruptcy Law) was adopted (and subsequently amended in 2019, 2020 and 2021), repealing the bankruptcy provisions of Commercial Transactions Law from 1993. Furthermore, in 2019, issues relating to personal bankruptcy were addressed through Federal Decree Law (Number 19).

In addition to a rapidly growing economy that is diversifying away from natural resources, there are further challenges the Bankruptcy Law has to navigate as it looks to develop. First of all, each emirate retains jurisdiction over matters not reserved for the federal government. Second, enforcing debt in the UAE is possible both via civil and criminal law provisions (although bounced cheques are no longer considered a criminal offense providing they were not issued in bad faith). On a related point, UAE's economic transformation has been attracting an increasing number of entrepreneurial expatriates, who when faced with financial difficulties tend to abscond, especially in situations where they have given personal guarantees to obtain substantial loans from local lenders. Finally, new free zones have been springing up across the UAE, each one

with its own set of laws meant to encourage FDI. Having to navigate this many dimensions in a single country with a civil code that does not rely on precedent thus quickly becomes challenging.

Overall, the trajectory of the Bankruptcy Law and its implementation in the UAE is positive. For example, during the Covid-19 pandemic, the UAE government passed the Federal Decree Law (Number 21) of 2020, whereby the debtors can avail of certain bankruptcy protections during periods of "Emergency Financial Crisis" (as determined by the UAE Cabinet). More recently, KBBO used provisions of the Bankruptcy Law to file for protection from creditors, raise new funds, appoint international trustees and engage in restructuring negotiations. In addition to the administration of NMC (albeit moved offshore to ADGM), this is substantial progress relative to some legacy insolvencies such as JBF RAK LLC and Arabtec Holding PJSC.

Question 3.2 [maximum 8 marks]

Commented [SE12]: 8/8

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.

Application

At the outset, the court receives the application (from either the debtor¹ or the creditor²) to initiate the bankruptcy proceedings and appoints an expert³ (from a panel of experts). Although the expert will form a view on the debtor's financial situation and the likelihood of a successful restructuring, in this initial stage, the court is also involved in reviewing documentation submitted in support of the bankruptcy application. Depending on the review of the documents, the court may decide to reject the application altogether⁴ or ask for further information to be submitted⁵. Finally, the court may decide to join other parties to the proceedings as well as make interim orders.⁶ If the court is satisfied with the submitted documentation, and the trustee's report suggests necessary conditions have been met for the debtor to go through a possible restructuring, the court will make an order to commence the bankruptcy proceedings.

Trustee

¹ Bankruptcy Law, article 68.

² Idem, article 69.

³ Idem, article 77.

⁴ Idem, article 79.

⁵ Idem, article 80.

⁶ Idem, article 81.

At this stage the court also needs to appoint a trustee. The trustee will either be nominated by the debtor or chosen from a table of experts approved by the Financial Restructuring Committee. Should the trustee appointment get challenged by a creditor, the court also needs to rule on this objection within five business days.

Timelines

Important to note here that the timelines suggested in the text are provisional and can be extended, especially if the debtor's situation is complex. Considering all the decisions at this stage rest with the court this introduces an additional overhang on the success of the restructuring process as secured creditors (as well as unsecured but creative and litigious creditors) may initiate actions that would be detrimental to debtor's prospects to continue as a going concern. Our situation is somewhat simplified in that there are no secured creditors and debtor's management has not been involved in any criminal activities.

Creditor claims

If there were secured creditors, they would need to get the court's approval (within 10 business days of filing an application to enforce their security against the debtor) so as to ensure there is no collusion between the secured creditor and the debtor that would unduly disadvantage other creditors. It would not be uncommon for a property to be subject to security interests of multiple creditors, in which case the court would have to make a determination on the order of priority for each security.

The court is also tasked with resolving any objections from either the debtor or the creditors, in relation to the list of creditor claims that have been lodged with the court (and subsequently publicised). Although a creditor may be admitted on an interim basis (e.g., for voting purposes), the court needs to finally determine a list of creditors.⁷ Assuming this is a complex restructuring, with dozens of creditors, it is not hard to see how this could potentially add to any proposed timelines for the restructuring. Furthermore, it is not entirely clear why a detailed review of creditor claims is necessary at this stage (save for the vote on the appointment of the trustee or subsequently on the restructuring proposal) if the debtor is not expected to continue as a going concern and no dividend is expected from the estate. Presumably it is because the court can (if it is so inclined) appoint supervisors of the rehabilitation procedure and they are drawn from both secured and unsecured creditors.

Trustee's report and scheme approval

⁷ Idem, article 94.

Once the trustee has prepared their initial review of debtor's financial position, the court is required to review the report and make sure it takes into account all creditor claims.⁸ The court may decide that the restructuring is not viable and could order the debtor to proceed to liquidation. Alternatively, the court will order the trustee to document a scheme that would restructure the debtor's existing liabilities. Once the scheme has been reviewed by the court (and providing no amendments need to be made to take into account all of the stakeholders' interest) the trustee will call a meeting of the creditors for a vote on the proposed restructuring scheme. Key point to note here is that the court may direct the formation of classes of creditors, which could obviously have an impact on the outcome of creditor approval.⁹ Assuming the scheme has been approved by the creditors, the trustee needs to submit it to the court for final approval.¹⁰ Should the court reject the scheme, it is either returned to the trustee for further revisions, or the debtor is put into liquidation.

Implementation

Court's role in the implementation is largely consultative, in that the trustee monitors the progress of the scheme and report back to the court on any failures or potential amendments need to be made to the scheme. The court can then either approve proposed amendments (in part or in full) or reject them.¹¹ Assuming that at the completion of the scheme all of the debtor's liabilities have been discharged as agreed, the court then needs to confirm (and advertise) the complete implementation of the scheme.¹² However, if the implementation of the scheme is not feasible, the court may terminate the preventive composition proceedings and place the debtor into liquidation. At that point, the trustee will step aside, while the court remains in control of the bankruptcy procedure aimed at realising the estate's assets and repaying creditors.¹³

Question 3.3 [maximum 2 marks]

Commented [SE13]: 2/2

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 to 150 words) whether you consider that the level of court involvement in approving a restructuring to be appropriate. Provide reasons for your answer.

Overall, the level of court involvement in UAE's onshore bankruptcy proceedings is substantial and resembles the French bankruptcy process, which should not come as a major surprise given the influence Egypt (and therefore France) has on local

⁸ Idem, article 42.

⁹ Idem, article 43.

¹⁰ Idem, article 49.

¹¹ Idem, article 55.

¹² Idem, article 56.

¹³ Idem, article 66.

legislation. This in itself is not an issue, although it is probably amplified by the existence of parallel courts, multiple jurisdictions and the recency of local bankruptcy legislation. On top of that, local courts cannot rely on precedent (both due to the novelty of the procedures and the nature of civil-law) which adds further uncertainty to the bankruptcy process. However, given the trajectory of the UAE economy, and the importance of bankruptcy legislation to the country's global business rankings, it is likely that these teething issues will be resolved sooner rather than later, even if it sometimes means moving bankruptcy proceedings offshore to deal more effectively with the estate (e.g., **NMC**).

Commented [SE14]: One additional point to note is that due to the heavy involvement of the UAE courts, insolvency proceedings can take a very long time, which becomes costly for debtors (and creditors who could otherwise be paid).

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

Commented [SE15]: 15/15

RZA LLC operates a restaurant chain in various locations in Dubai. It was a thriving and successful business but has been negatively impacted by the increase in global food prices. It has exhausted all available funds and has no cash to pay creditors. RZA 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 RZA LLC's shareholders and was transferred to RZA LLC on the basis that payment for the site would be made by RZA LLC to the shareholder in full in 2024. In the meantime, the shareholder holds a mortgage over the property for the unpaid purchase price.

Question 4.1 [maximum 5 marks]

Commented [SE16]: 5/5

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.

At a high level, in order for RZA LLC to go through preventive composition they would naturally need to first apply for the procedure, receive court approval to initiate the process and eventually work with a trustee to develop a scheme that would subsequently need to be approved by both the creditors and the court.

Further assumptions:

- **A court expert is available and sufficiently qualified to take on the case;**
- **There is no objection to the appointment of the trustee (would add another 10 business days);**

- *No secured creditor enforcement (i.e., given they are one of the shareholders) (would add another 10 business days at the very least); and*
- *No requests for extension for the scheme to be documented (20 business days).*

More specifically, the rate-determining steps are as follows:

- i. Application to the court and court instructing an expert to prepare a report on RZA LLC*
- ii. Preparation of an expert report - 20 business days from court instruction (20)*
- iii. Court issuing their opinion on RZA LLC's suitability for the preventive composition procedure - 5 business days from the date of the application or from the date of the expert's report (5)*
- iv. Once appointed, the trustee publishes court's decision to commence the scheme within five business days (5)*
- v. Creditors are invited to submit their claims within 20 business days of the publication of the court's decision (20)*
- vi. Once creditors have submitted their claims, the trustee publishes a list of claimants within 10 business days (10)*
- vii. Preventive composition plan / scheme is submitted to the court within 45 business days from the date of publishing the scheme commencement (45)*
- viii. Court reviews the draft scheme within 10 business days to make sure it takes into account all the relevant stakeholders (10)*
- ix. Once satisfied the court instructs the trustee to issue within 5 business days an invitation for a creditors' vote (5)*
- x. Creditors' meeting is held within 15 business days of the invitation being sent to the creditors (15)*
- xi. Once the scheme is approved by the creditors it needs to be put before the court within 3 business days for urgent approval (3)*
- xii. Finally, the trustee registers the court's decision confirming its approval and publishes the scheme within 7 business days*

In total therefore, it would seem that in a non-controversial case, it could take up to 115 days to move from an application stage to approval and registration of a preventive composition scheme, which would suggest RZA LLC would need to have close to four months' worth of working capital financed ahead of the filing so as not to disrupt operations and put the company under further distress. Naturally, if RZA LLC had the capacity to get that kind of funding ahead of filing for preventive composition, it is unlikely they would file to begin with. However, more recent onshore cases (e.g., KBBO) have been able to raise DIP financing after the bankruptcy procedure was initiated, which hopefully gives some hope to future restructuring efforts.

Question 4.2 [maximum 5 marks]

Commented [SE17]: 5/5

RZA 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.

Since the creditors are unlikely to approve preventive composition scheme, the court is required to make an order for the liquidation of RZA LLC's assets and the distribution of debtor's proceeds to creditors in prescribed order of priority.

The court will first need to appoint a trustee to oversee the liquidation, and in this case, given that RZA LLC had already gone through a preventive composition procedure under the supervision of a trustee, it would make sense for the same trustee to remain in situ. However, it can also be argued that since the original trustee did not manage to successfully restructure the debtor, they may not be the right person for the job and another trustee may be better suited. At this stage this is also a commercial decision, as "restructuring trustee" fees are likely to rank ahead of the "liquidation trustee" fees.

Once the trustee has been appointed, they have to advertise their appointment (within 3 business days) and invite all creditors to submit their claims (within 10 business days). If the estate does not have sufficient assets to cover legal fees and repay secured creditors, the trustee is not obliged to review creditor claims (as there will be no dividend to the unsecured).

During the course of the liquidation, the trustee is expected to report to the court on a monthly basis, primarily informing the court on the asset disposal process and any bids received for RZA LLC's assets. Asset sales are meant to be conducted through public auction over the course of six months (not ideal!), although this period can be extended by up to two months with court approval. In case of any objection to the disposal of a particular asset (or a specific value), court will have the final say.

Assuming RZA LLC has sufficient assets to be liquidated, any realisations would be applied in the following order (subject to court approval and approval of the creditor waterfall):

- i) Proceeds from sales of secured assets (less asset realisation costs) to be distributed to secured creditors;*
- ii) Proceeds from unsecured assets:*
 - a. Court costs;*
 - b. Trustee's costs (presumably both the restructuring trustee and the liquidation trustee get paid in full);*
 - c. Unpaid wages and salaries (capped at three months' salary);*
 - d. Government dues (e.g., VAT); and*
 - e. RZA LLC's operating costs incurred post-petition.*

Assuming that the liquidation has been successfully completed, this needs to be advertised, and at that point any unsecured creditors who have not been paid in full (or at all) can enforce against any of the RZA LLC's remaining assets.

Question 4.3 [maximum 5 marks]

Commented [SE18]: 5/5

RZA LLC incorporated and registered a fully-owned subsidiary company in the DIFC to operate a restaurant in the DIFC. The subsidiary is called RZA Limited and it is incorporated as a DIFC company. RZA Limited is also unable to pay its debts. What actions can RZA Limited's creditors take if they wish to see RZA Limited liquidated in the DIFC? In particular, who can take such actions and what steps would have to be taken? If the RZA 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?

Fundamentally this depends on the relationship the creditors have with RZA Limited ("RZA DIFC" or the "Company"). If it is clear that the Company is unable to pay its debts as they come due, and the directors (being rational economic actors) decide to pass a resolution to wind up the Company, creditors could have a say in their appointment of the liquidator, form a liquidation committee and thereby be informed of the progress of the winding up procedure. Alternatively, if Company management is intent on continuing to trade whilst insolvent (hoping that better times are just around the corner), thereby worsening the position of its existing creditors any one of the Company creditors could issue a statutory demand for more than USD2,000, and once the demand remains unsatisfied for a period of 21 days petition the court to wind up RZA DIFC. Finally, if the creditors can demonstrate that the Company is either cash flow or balance sheet insolvent to the DIFC courts (or the DIFC Authority) and that winding up of RZA DIFC is in the best interest of the DIFC, the Company would be wound up.

Once a decision to wind up RZA DIFC has been taken, a liquidator (a qualified insolvency practitioner) will be appointed - either by virtue of a shareholders' resolution or by the DIFC court, depending on which procedure is initiated. Nevertheless, creditors could have a say in the appointment of the liquidator through a creditors' meeting (either through the CVL process or by the provisional court appointed liquidator calling for a creditors' meeting specifically for this purpose in a compulsory liquidation). Liquidator once appointed will look to maximise the value of estate and distribute proceeds of any asset realisations in accordance with the law. Beyond purely monetizing assets, the liquidator will also have the option to carry on trading (if it will enhance returns to creditors), enter into new contracts (acting as agent of the Company not in his personal capacity), disclaim onerous contracts where needed and potentially pursue third parties who may have tried to put the Company's assets beyond the reach of creditors.

Assuming the estate of RZA DIFC has sufficient assets to cover the costs of winding up (at the very least), the liquidator will need to ascertain the identity and claim amount for each of the Company's creditors before making any dividend distributions. In order to do so, the liquidator will invite creditors to submit their proofs of debt, with

supporting documentation so that the claim can be adjudicated. Naturally, the liquidator can challenge the validity of creditor's claims, ask for additional information, reject or accept them. If a creditor is not satisfied with the liquidator's decision (e.g., claim was not admitted in full or at all), they may appeal to the DIFC court within 21 days. Once finalised (and assuming the list does not include any secured creditors to the extent their security is fully covered), the list of creditor claims will be used to make distributions.

It is important to note that all unsecured creditors, with the exception of the liquidators' expenses and employee related preferential claims, will be settled proportionately based on available assets, on a pari-passu basis (assuming there is no prior subordination agreement that comes to light).

Once all the assets have been realised, liquidation expenses settled, preferential claims dealt with, and remaining unsecured creditors repaid, the Company will be dissolved (assuming there are no objections from the DIFC court or interested parties) and the liquidator released from their duties in relation to the winding up.

*** End of Assessment ***

Commented [SE19]: 46/50. 92%