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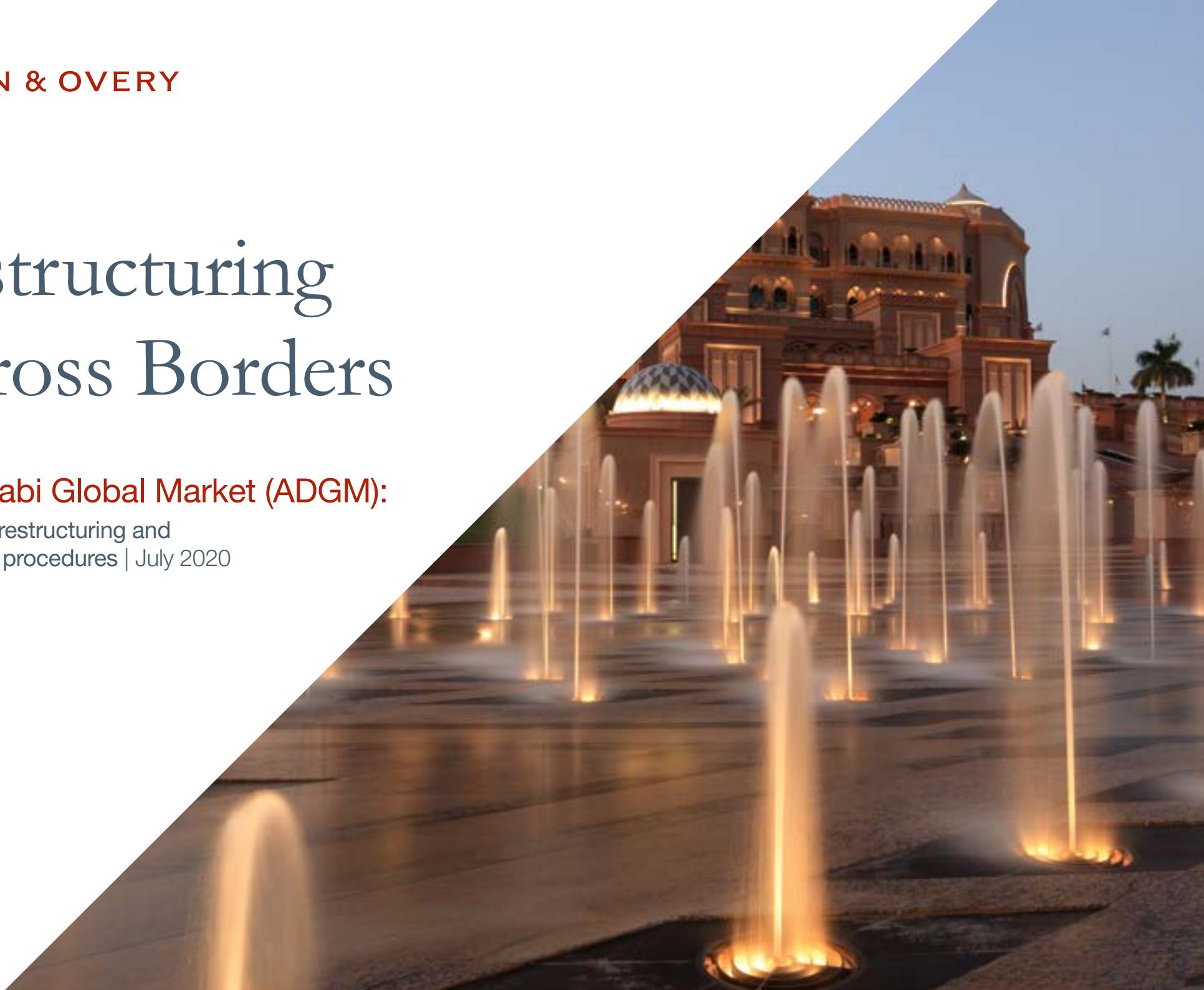
Restructuring Across Borders

Abu Dhabi Global Market (ADGM):

Corporate restructuring and insolvency procedures | July 2020



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Contents

Introduction

The Abu Dhabi Global Market (**ADGM**) was established as a financial free zone pursuant to Abu Dhabi Law No 4 of 2013 and Federal Decree No 15 of 2013. Established as an independent jurisdiction within the UAE, the ADGM is empowered to create its own legal and regulatory framework for all civil and commercial matters. Accordingly, the ADGM has promulgated its own laws relating to insolvency and corporate restructuring. Onshore UAE laws relating to the same subject matter do not apply in the ADGM.

The principal restructuring and insolvency options under ADGM law are:

- receivership / administrative receivership;
- administration;
- deeds of company arrangement (in conjunction with an administration);
- schemes of arrangement; and
- liquidation.

Each of the processes noted above is governed by the Abu Dhabi Global Market Insolvency Regulations 2015 and certain amendments thereto (the **ADGM Insolvency Regulations**) (other than the scheme of arrangement which is governed by the Companies Regulations 2020 (the **ADGM Companies Regulations**)).

In addition, the Application of English Law Regulations 2015 (the **ADGM Common Law Regulations**) purport to incorporate, to a large extent, the common law of England (including the principles and rules of equity) into ADGM law. As such, to the extent that the English common law addresses any issues in relation to the relevant subject areas, such laws should (subject to certain limited exceptions) apply equally under ADGM law.

The insolvency procedures which are available under ADGM law draw much of their substance from the corresponding English law regimes.

Certain regulated financial institutions within the ADGM are also subject to the Bank Recovery and Resolution Regulations 2018 (the **ADGM Bank Recovery and Resolution Regulations**). Similar to other jurisdictions, the ADGM Bank Recovery and Resolution Regulations seek to address systemic risks posed by the potential failure of significant financial institutions. The content of the ADGM Bank Recovery and Resolution Regulations is beyond the scope of this note.

Enforcement of security

A secured creditor need not apply to any court to enforce its security interest. In practice, a secured creditor would most likely appoint a receiver or administrative receiver to collect in and dispose of an asset which is subject to ADGM law security. The manner in which a receiver or an administrative receiver would be appointed is set out in more detail in the relevant section below.

Broadly speaking, a secured creditor will also benefit from any additional rights of enforcement which exist under English common law (pursuant to the ADGM Common Law Regulations). Given the expansive nature of the English common law however and the limitations which are set out in the ADGM Common Law Regulations, a more detailed assessment of this area should be undertaken before seeking to rely on any particular area of the English common law in an ADGM context.

Administration

In keeping with its over-arching rescue and rehabilitation culture, the ADGM Insolvency Regulations provide for an administrator to be appointed to take over the management of a distressed company. An administrator may be appointed via one of the following routes:

– by the debtor company itself (or by the directors of the debtor company) if the debtor company is unable or is unlikely to be able to pay its debts;

– by a creditor which holds security over the whole or substantially the whole of the debtor company's assets, where the security document contemplates such appointment of an administrator and where the relevant security has become enforceable; and

– by the court upon the application of the debtor company, its directors or one or more creditors of the debtor company, if the court is satisfied that the debtor company is unable or is unlikely to be able to pay its debts.

The first two appointment routes noted above do not require the approval of the court although notice of intention to appoint the administrator must be: (i) provided to other interested parties; and (ii) filed with the court.

Once appointed, the duties of an administrator are owed to the creditors of the debtor company as a whole and not to the creditors (if any) which might have appointed the administrator. The administration must be carried out for one of the following purposes:

– to rescue the company as a going concern;

– to achieve a better result for the company's creditors as a whole than would be likely if the company were wound up without going into administration; or

– to realise property in order to make a distribution to one or more secured or preferential creditors.

The administrator must, in the first instance, seek to pursue the first objective. The second objective may only be pursued by the administrator if the administrator considers that the first objective is not reasonably practicable or that the second objective would achieve a better result for the company's creditors as a whole. The third objective only applies if the administrator thinks that it is not reasonably practicable to achieve either of the other objectives, and that to pursue such an objective would not unnecessarily harm the interests of the creditors of the company as a whole.

For so long as an administrator is appointed, no resolution may be passed to wind up the company. Additionally, no step may be taken to enforce security over the company's property and no other legal proceedings may be brought against the company except with the consent of the administrator or the court.

Upon the appointment of an administrator, any administrative receiver of the company must vacate office and any receiver of a part of the company's property must also do so if the administrator requires.

The ADGM Insolvency Regulations provide for a regime on priority financing for companies in administration. This regime has similarities to the priority financing regime under the Chapter 11 process in the United States.

An administrator has the following options to avail priority financing:

– it can obtain new unsecured credit as an expense of the administration which will rank ahead of unsecured creditors and creditors holding floating charges; or

– if the administrator is unable to obtain financing in accordance with the above, it can apply to the court to approve new financing on the following basis:

  a. on the basis that it will hold priority over any or all expenses of the administration;

  b. on the basis that it will be secured against unencumbered property of the debtor;

  c. on the basis that it will be secured against encumbered property of the debtor (albeit ranking behind the existing security);

  d. on the basis that it will be secured against encumbered property of the debtor and will rank ahead of existing security provided that the administrator is unable to obtain credit via any other means and there is "adequate protection" for the affected secured creditor. In any hearing on this basis, the administrator has the burden of proof on the issue of "adequate protection".

When "adequate protection" is required, such protection may be provided by requiring the administrator to make cash payments, providing additional or replacement security interest or granting such other relief as will result in the realisation of an equivalent interest in the property. "Adequate protection" is provided if the court is satisfied that (1) the provision of new financing would enable the administrator to achieve one of the purposes of the administration; and (2) the grant of the security interest referred to in (d) above is likely to result in a better result for each creditor than would likely be achieved if the new security was not granted.

Receivership/administrative receivership

The ADGM Insolvency Regulations draw a distinction between receivers on the one hand and administrative receivers on the other hand. The role of a receiver is to collect in and sell any part of the secured property on behalf of a creditor. The role of an administrative receiver is wider than this as an administrative receiver is authorised to take over the management of the business of the debtor company.

A receiver may be appointed by a secured creditor where the relevant security document contemplates such an appointment.

An administrative receiver, however, may only be appointed by a secured creditor which holds security over the whole or substantially the whole of the assets of the debtor company and where such appointment relates to:

– a capital market arrangement involving a debt of at least USD50 million; or

– a project financing which includes step-in rights and is expected to incur a debt of at least USD50m.

Both receivers and administrative receivers are required to act in the interests of the persons by whom or on whose behalf they were appointed and are required to:

– act in good faith in carrying out their functions;

– manage any property of the company with due diligence; and

– when exercising a power of sale of property of the company, use reasonable care to obtain the best price reasonably obtainable in the circumstances.

As noted above, upon the appointment of an administrator, any administrative receiver of the company must vacate office and any receiver of part of the company's property must also do so if the administrator requires.

Deeds of company arrangement

The ADGM Insolvency Regulations permit a company which is in administration to enter into a settlement arrangement with its creditors (known as a **Deed of Company Arrangement**). Importantly, this process cannot be utilised unless the debtor company has first been placed into administration.

A Deed of Company Arrangement is a binding arrangement between creditors and the company under which creditor claims are compromised. There is no prescribed form for such an arrangement and the content and terms will be fact specific and will depend on the negotiations which take place between the administrator and the creditors.

To become effective, the Deed of Company Arrangement must be approved by creditors representing a majority (in value) of those creditors voting on the matter. A Deed of Company Arrangement will not be approved though if those creditors voting against it represent more than half in value of the creditors that are not "connected" to the debtor company.

If the Deed of Company Arrangement is approved in the manner outlined above, it will bind all unsecured creditors, even those who voted against the Deed of Company Arrangement. A secured creditor, however, will only be bound by the Deed of Company Arrangement if the secured creditor has positively voted in favour of the same or, if the ADGM court has, on the application of the administrator, made an order to this effect. The ADGM court will only make such an order if it is satisfied that: (i) allowing the secured creditor to realise or otherwise deal with the security would have a material adverse effect on achieving the purposes of the Deed of Company Arrangement; and (ii) the secured creditor's interests will be adequately protected following the making of such order and the implementation of the Deed of Company Arrangement. A Deed of Company Arrangement must ensure that the priority status of certain preferential creditors (employee and pension payments for the three month period prior to the commencement of the liquidation) is not worse than the priority which would be afforded to such preferential creditors in an insolvent liquidation.

Once approved, the administrator will administer the Deed of Company Arrangement unless the creditors resolve to appoint another person to do so.

Liquidation

The ADGM Insolvency Regulations provide a framework for an orderly liquidation and winding-up of a debtor's assets.

A liquidation may be proposed by the debtor itself, the directors of the debtor or by any creditor of such debtor and may be approved by the ADGM court if one or more of the following criteria have been satisfied:

– the shareholders of the debtor have, by way of special resolution, resolved that the debtor be wound up;

– the debtor is unable to pay its debts (either on a cash flow or balance sheet basis or following a failure to pay a debt of more than USD2,000 within three weeks of formal demand);

– the ADGM court has made an order of winding-up pursuant to any other provision of ADGM law; or

– the ADGM court is of the opinion that it is just and equitable that the debtor be wound up.

Any liquidation must be formally approved by the ADGM courts and, if so approved, will be binding on the debtor and all of its creditors.

Once a liquidation has been approved by the court, creditors wishing to share in the proceeds of the liquidation will need to prove in the insolvency.

Immediately following the issuing of a winding up order by the court, no further proceedings may be brought against the debtor except with the permission of the ADGM court.

Schemes of arrangement

The ADGM Companies Regulations provide a framework for a debtor company and its creditors to agree and implement a scheme of arrangement (a **Scheme of Arrangement**) which will be binding on the debtor company and all of its creditors.

The Scheme of Arrangement is closely modelled on the English law scheme of arrangement. Accordingly, creditors will be divided into aligned classes and the Scheme of Arrangement will be put to the vote of each such class of creditor.

In order to be approved, a Scheme of Arrangement must be approved by 75% (in value) of each class of creditor. Unlike under the English law equivalent, there is no requirement for a Scheme of Arrangement to be approved by a majority (by number) of each class of creditors, making it less likely that a Scheme of Arrangement could be prevented by a number of low value creditors.

If approved in the manner set out above and otherwise approved by the court, the Scheme of Arrangement will bind the debtor company and all of its creditors which were entitled to vote on the Scheme of Arrangement. Importantly, the Scheme of Arrangement will, if approved, bind dissenting creditors including dissenting secured creditors.

Unless a Scheme of Arrangement is being carried out in conjunction with another insolvency procedure which benefits from a moratorium (eg an administration), the Scheme of Arrangement will not trigger any moratorium on winding-up or other legal proceedings being brought against the debtor company.

Voidable transactions

The ADGM Insolvency Regulations provide that a liquidator or an administrator may make an application to the court to set aside the following transactions:

– transactions at an undervalue; and

– preferences.

To constitute a transaction at an undervalue or a preference: (i) the debtor company must be in administration or liquidation; and (ii) the relevant transaction must have been entered into (in the case of a transaction at an undervalue or a preference which is given to a connected person) within the two year period preceding the onset of insolvency or (in the case of a preference which is given to an unconnected person) within the six month period preceding the onset of insolvency. Transactions entered into in the period between presentation of a petition for the making of an administration or liquidation order and the order being given will be caught also.

A transaction will constitute a "transaction at an undervalue" if the debtor has: (i) made a gift to a person or otherwise receives no consideration under the transaction; or (ii) received consideration under the transaction with a value, in money or money's worth, which is significantly less than the value, in money or money's worth, of the consideration provided by the debtor.

No order will be made in respect of a transaction at an undervalue if the court is satisfied that: (i) the debtor entered into the transaction in good faith and for the purposes of carrying on the business of the debtor; and (ii) at the time of the transaction, there were reasonable grounds for believing that the transaction would benefit the debtor.

A transaction will constitute a "preference" if: (i) the debtor enters into a transaction with one of its creditors; and (ii) the effect of the transaction is to place that creditor in a position which, if the debtor were placed into insolvent liquidation, would be better than the position it would have been in had that transaction not been entered into.

No order will be made in respect of a preference unless the court is satisfied that the debtor was influenced by a desire to prefer the relevant person. In the case of a transaction entered into with a "connected" person, there will be a rebuttable presumption that such a desire existed.

Ranking of creditors

In an insolvent liquidation, secured creditors will rank ahead of unsecured creditors to the extent of the value of the relevant secured asset and as between other secured creditors in respect of the same secured asset, in the order in which those security interests were perfected. If a secured creditor has realised its security and the realisations were insufficient to discharge the secured debt, such creditor may prove for the remaining amount as an unsecured creditor.

Amounts owing to unsecured creditors will rank in the following order of priority:

– all expenses properly incurred in the winding-up, including expenses incurred by the liquidator;

– preferential creditors (employee and pension payments for the three month period prior to the commencement of the liquidation); and

– general unsecured creditors of the debtor company,

and, in each case, creditors in the same category will rank equally with each other.

Cross-border recognition

The ADGM Insolvency Regulations incorporate and apply the UNCITRAL Model Law on Cross Border Insolvency (the **Model Law**). Accordingly, foreign insolvency officials may apply for recognition of insolvency proceedings commenced in other jurisdictions or for the cooperation of the ADGM courts in connection with such foreign insolvency proceedings. In accordance with the Model Law, if an ADGM court determines that the "centre of main interests" in relation to a particular insolvency is in a jurisdiction other than the ADGM, the ADGM courts should recognise the foreign proceedings as being the "foreign main proceedings" and should stay any insolvency proceedings in respect of the same entity which have been initiated in the ADGM.

So far as we are aware, cross-border insolvencies with an ADGM nexus remain untested in the ADGM courts so it is difficult to predict with certainty how the same would play out in practice.

Key contacts

If you require advice on any of the matters raised in this document, please call any of our partners or your usual contact at Allen & Overy.

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Further information

Developed by Allen & Overy's market-leading Restructuring group, "Restructuring Across Borders" is an easy-to-use website that provides information and guidance on all key practical aspects of restructuring and insolvency in Europe, Asia, the Middle East and the U.S.

To access this resource, please click **here**.

For more information, please contact:

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