Critical Examination of Saudi Restructuring Law in the Light of United Kingdom and United States Experiences

Faisal Ibrahim F Alfawzan

Submitted in accordance with the requirements for the degree of Doctor of Philosophy (PhD)

The University of Leeds

School of Law

January 2022

The candidate confirms that the work submitted is his own and that appropriate credit has been given where reference has been made to the work of others

Acknowledgments

I am most thankful to Allah Almighty for providing me with the opportunity, means and perseverance to complete this study.

Many have supported me along my thesis journey. First, I would like to express my deepest thanks to my supervisors, Professor Duncan Sheehan and Professor Gerard McCormack. I owe them a massive debt of gratitude for their valuable advice and guidance, helpful comments and constant support during the period of my research.

Additionally, this research would not have been completed without the support of my family. I would like to express my gratitude to my mother and my brothers and sisters for their prayers, support and encouragement during my path towards the completion of this study. I am also sincerely grateful to my wife, Abeer, whose constant support, encouragement and motivation empowered me along the way. Finally, I would like to thank my daughter, Nouf, whose presence has filled my world with joy and made this work much easier for me.

Abstract

The evolution of the 'rescue culture' and rehabilitation of companies and businesses in corporate insolvency has received global attention for decades. Chapter 11 in the US Bankruptcy Code 1978 is thought to have significantly influenced the development of corporate rescue processes across the globe. Indeed, Chapter 11 has widely been considered the gold standard for corporate restructuring that many jurisdictions have attempted to emulate. Moreover, the socio-economic benefits of adopting rescue-oriented insolvency legislation have been actively promoted by international organisations such as the World Bank, the United Nations Commission on International Trade Law (UNCITRAL) and the International Monetary Fund (IMF). Providing formal restructuring procedures in addition and as an alternative to liquidation procedures is regarded by these organisations as a criterion for the international respectability of a nation's insolvency laws. Corporate reorganisation is based on the presence of a distinction between the going concern value of the distressed business and its liquidation value. If the going concern value of a company is higher than the value extracted from the liquidation of its assets, the reorganisation procedure may be an attractive alternative to liquidation. In this scenario, it would be more advantageous for creditors if the business continues to operate, and it would be in the interest of society if a firm that is worth more alive than dead is successfully restructured. The enactment of the Bankruptcy Preventative Settlement (BPS) Law in 1996 represented the first step toward providing formal rescue procedures for distressed businesses in Saudi Arabia. However, that law was criticised and rarely applied in practice mainly due to its brief content. Given the absence of comprehensive formal restructuring procedures provided by the BPS, the outcome of restructuring cases relied heavily on the court's discretion, which was highly unpredictable. Modernising the laws governing business activities has been one of the central initiatives taken by the Saudi government to attract foreign investment. This is viewed as essential to accomplishing the ultimate goal of achieving the Kingdom's 2030 Vision: the diversification of economic sources and the reduction of the country's dependence on oil as a main source of income. One of the remarkable changes in the Saudi commercial law area is the introduction of the first comprehensive Bankruptcy Law (BL) 2018, which was enacted in February 2018. BL 2018 provides two restructuring procedures: preventative settlement (PS) and financial restructuring (FR). This thesis examines the rules of corporate restructuring under these two procedures with reference to the UK and US's invaluable experiences. The examination focuses on four particular aspects of restructuring procedures: access to restructuring procedures, control of

companies during procedures, moratorium against creditors' actions, and restructuring plans. Referring to the laws in the UK and the US regarding the above aspects is highly important, as the Saudi legal system can learn valuable lessons from these well-developed jurisdictions. Moreover, the UK's and the US's experiences are helpful in progressing Saudi restructuring law, especially because the UK and the US were two of the main jurisdictions that Saudi lawmakers looked at as models when they sought to modernise bankruptcy law in general and restructuring procedures specifically.

Table of Contents

List of Abbreviations

ABI	American Bankruptcy Institute
APR	Absolute Priority Rule
BGL 2007	Board of Grievances Law 2007
BL 2018	Bankruptcy Law 2018
BLG 1992	Basic Law of Governance 1992
BPF	British Property Federation
BPS 1996	Bankruptcy Preventative Settlement Law 1996
CA 2006	Companies Act 2006
CCL 1931	Commercial Court Law 1931
CGIA 2020	Corporate Governance and Insolvency Act 2020
CLDP	Commercial Law Development Program
CLR	Company Law Review (UK)
CVA	Company Voluntary Arrangement
DIP	Debtor-in-Possession
DOCA	Deed of Company Arrangement
DTI	Department of Trade and Industry (UK)
EA 2002	Enterprise Act 2002
EU	European Union
FDI	Foreign Direct Investment
FR	Financial Restructuring
GCC	Gulf Cooperation Council

IA 1986	Insolvency Act 1986
ILRC	Insolvency Law Review Committee (Singapore)
IMF	International Monetary Fund
JL 2007	Judiciary Law 2007
MENA	Middle East and in North African
MOC	Ministry of Commerce
PIP	Practitioner-in-Possession
PMD	Pre-Moratorium Debt
PS	Preventative Settlement
SARE	Single Asset Real Estate
UAE	United Arab Emirates
UK	United Kingdom
UNCITRAL	United Nations Commission on International Trade Law
US	United States
VA	Voluntary Administration

List of Cases

United Kingdom:

A.E.S. Barry Ltd. v TXU Europe Energy Trading [2004] EWHC 1757 (Ch).

Air Ecosse Ltd v Civil Aviation Authority (1987) 3 BCC 492.

Bernhard's Sport Surfaces Ltd v Astrosoccer4U Ltd [2018] BCC 147.

Biosource Technologies Inc v Axis Genetics Plc [2000] 1 BCLC 286.

BNY Corporate Trustee Services Ltd v Eurosail-UK 2007-3BL Plc (2013) 1 WLR 1408.

Bristol Airport Plc v Powdrill [1990] Ch 744.

Carr v British International Helicopters Ltd [1994] ICR 18.

Commissioners of Inland Revenue v Adam & Partners Limited [2000] BCC 513.

Commissioners of Inland Revenue v Adam & Partners Ltd [2001] 1 BCLC 222.

Discovery (Northampton) Ltd v Debenhams Retail Ltd [2020] BCC 9.

Doorbar v Alltime Securities Ltd (No 2) [1995] BCC 728.

Exchange Travel Agency v. Triton plc [1991] BBC 341.

Gigi Brooks Limited (2015) EWHC 961 (ch).

Hammonds (A Firm) v Pro-Fit USA Ltd (2007) EWHC 1998 (ch)

In re Cheyne Finance plc (No 2) [2008] Bus LR 1562.

In re Ophir Energy Plc [2019] EWHC 1278 (Ch).

In Re Virgin Atlantic Airways Ltd [2020] BCC 997.

Inland Revenue Commissioners v Bland [2003] EWHC 1068 (Ch).

Inland Revenue Commissioners v The Wimbledon Football Club Ltd & Ors [2004] BCC 638.

Lazari GP Ltd v Jervis [2013] BCC 294.

Lazari Properties2 Ltd v New Look Retailers Ltd [2021] EWHC 1209 (Ch).

Magical Marketing Ltd v Phillips [2008] FSR 36.

March Estates Plc v Gunmark Ltd [1996] 2 BCLC 1.

Metro Nominees (Wandsworth) (No 1) Ltd v Rayment [2008] B.C.C 40.

Mourant & Co Trustees Ltd v Sixty UK Ltd (In Administration) [2010] BCC 882.

Prudential Assurance Co Ltd v PRG Powerhouse Ltd [2007] BCC 500.

Razzaq v. Pala [1997] 1 WLR 1336.

Re AA Mutual International Insurance Co Ltd (2004) EWHC 2430 (ch)

Re Anglo American Insurance Co Ltd [2001] 1 BCLC 755.

Re Anglo-Continental Supply Company Limited [1922] 2 Ch 723.

Re Atlantic Computer Systems pls (no.1) [1992] Ch 505.

Re British Aviation Insurance Co Ltd [2006] BCC 14.

Re BTR Plc [1999] 2 BCLC 675.

Re BTR Plc [2000] 1 BCLC 740.

Re Colt Telecom Group Plc (No.2) [2002] EWHC 2815 (ch).

Re David Meek Access Ltd [1993] BCC 175.

Re Debtor (No 101 of 1999) (No 1) [2001] 1 BCLC 54.

Re Debtor (No 222 of 1990), Ex p Bank of Ireland [1992] BCLC 137.

Re Debtor (No.140 IO of 1995) [1996] 2 BCLC 429.

Re DeepOcean [2021] Bus LR 632.

Re DeepOcean [2021] EWHC 138 (Ch).

Re Dianoor Jewels Ltd [2001] 1 BCLC 450.

Re Divine Solutions (UK) Ltd [2004] CLY 2116.

Re Frankice (Golders Green) Ltd [2010] EWHC 1229 (Ch).

Re Gatnom Capital & Finance Ltd [2010] EWHC 3353 (Ch).

Re Hawk Insurance Co Ltd [2002] BCC 300.

Re Lomax Leisure Ltd [2000] BCC 352.

Re National Bank Ltd [1966] 1 WLR 819.

Re Noble Group Ltd [2019] BCC 349.

Re Osiris Insurance Ltd [1999] 1 BCLC 182.

Re Railtrack Plc [2002] 1 WLR 3002.

Re Savoy Hotel Ltd [1981] ch 351.

Re Stronghold Insurance Company Limited [2018] EWHC 2909 (Ch).

Re Sunbird Business Services Limited [2020] EWHC 2493.

Re T&N Ltd [2007] Bus L R 1411.

Re TDG Plc [2009] 1 BCLC 445.

Re Telewest Communications plc (No 2) [2005] BCC 36.

Re Telewest Communications Plc (No.1) [2004] BCC 342.

Rhondda Waste Disposal Ltd [2001] Ch 57.

Safe Business Solutions Ltd v Cohen [2017] EWHC 145 (Ch)

Sea Assets Ltd v Perusahaan Perseroan (Persero) PT Perusahaan Penerbangan Garuda Indonesia [2001] EWCA Civ 1696.

South Coast Construction Limited v Iverson Road Limited [2018] B.C.C. 123.

Sovereign Life Assurance Co v Dodd [1892] 2 QB 573.

The Financial Conduct Authority v Carillion Plc [2021] EWHC 2871 (Ch).

United States:

A.H. Robins Company, Inc. v. Piccinin 788 F 2d 994 (4th Cir 1986).

Barnette v. Evans 673 F 2d 1250 (11th Cir 1982).

Commodity Futures Trading Comm'n v. Weintraub 471 US 343, 356 (1985).

Cwcapital Asset Mgmt, LLC v Burcam Capital II, LLC, No 5:13-CV-278-F (E D N C June 24, 2014).

FGH Realty Credit Corp v Newark Airport/Hotel Ltd Partnership, 155 B R 93 (D N J 1993).

Hanson v First Bank of South Dakota, NA, 828 F 2d 1310 (8th Cir 1987).

In re 203 North LaSalle Street Ltd. Partn., 190 B.R. 567 (Bankr. N.D. Ill. 1995).

In re 266 Washington Associates 141 B R 275 (Bankr E D N Y 1992).

In re Alyucan Interstate Corp, 12 BR 803 (Bankr D Utah 1981).

In re Avila 311 BR 81 (Bankr ND Cal 2004).

In re Aztec Co, 107 B R 585 (Bankr M D Tenn 1989).

In re Bailey Ridge Partners, 571 BR 430 (Bankr ND Iowa 2017).

In re Barakat, 99 F 3d 1520 (9th Cir 1996).

In Re Batt, 322 BR 776 (Bankr ND Ohio 2005).

In re Bonner Mall Partnership, 2 F 3d 899 (9th Cir 1993).

In re Boston Post Road Ltd P'ship, 21 F 3d 477 (2d Cir 1994).

In re Breitburn Energy Partners LP, 582 B R 321 (Bankr S D N Y 2018).

In re Calpine Corp, 365 BR 401 (SDNY 2007).

In Re Century/ML Cable Venture 294 BR 9 (Bankr S D N Y 2003)

In re Chateaugay Corporation, 89 F 3d 942 (2d Cir 1996).

In re Colorado Springs Spring Creek Gen Imp Dist, 177 B R 684 (Bankr D Colo 1995).

In Re Commercial Mortg. and Finance, Co., 414 BR 389 (Bankr ND Ill 2009).

In re Curtis Center Ltd Partnership, 195 B R 631 (Bankr E D Pa 1996).

In Re Dovell, 311 BR 492 (Bankr SD Ohio 2004).

In Re Euro-American Lodging Corp, 357 BR 700 (Bankr S D N Y 2007).

In re Exide Technologies, 303 B R 48 (Bankr D Del 2003).

In re F.T.L., Inc., 152 BR 61 (Bankr ED Va 1993).

In re Frascella Enterprises, Inc, 360 B R 435 (Bankr E D Pa 2007).

In re Fussell, 928 F 2d 712 (5th Cir 1991).

In re Georgetown Ltd Partnership, 209 B R 763 (Bankr M D Ga 1997).

In re Green Hills Dev Co LLC, 445 BR 647 (Bankr S D Miss 2011).

In re Greenwald, 34 BR 954 (Bankr SDNY 1983).

In re Greystone III Joint Venture, 995 F 2d 1274 (5th Cir 1991).

In re Harmsen 320 BR 188 (BAP 10th Cir 2005).

In re Herron, 60 B R 82, 84 (Bankr W D La 1986).

In re Holywell Corp, 913 F 2d 873 (11th Cir 1990).

In re Johns-Manville Corp, 36 BR 727 (Bankr S D N Y 1984).

In re Kent Terminal Corp., 166 BR 555 (Bankr SDNY 1994).

In Re Landing Associates, Ltd, 157 B R 791 (W D Tex 1993).

In re Mac Donald, 755 F 2d 715 (9th Cir 1985).

In re Main Line Corp, 335 B R 476 (Bankr S D Fla 2005).

In re Marsch, 36 F3d 825, 828 (9th Cir 1994).

In re Marvel Entertainment Group 140 F.3d 463 (3d Cir 1998).

In re Mid-Atlantic Handling Systems LLC, 304 BR 111 (Bankr DNJ 2003).

In re Multiut Corp, 449 B R 323 (Bankr N D Ill 2011).

In re Murel Holding Corp 75 F 2d 941 (2d Cir 1935).

In re Panther Mountain Land Dev, 686 F 3d 916 (8th Cir 2012).

In re Pegasus Agency, 101 F 3d 882 (2d Cir 1996).

In re Randi's, Inc, 474 B R 783, 56 Bankr Ct Dec 187 (Bankr S D Ga 2012).

In re Richard Buick 126 B R 840 (Bankr E D Pa 1991).

In re River Family Farms, Inc, 85 BR 816 (Bankr ND Iowa 1987).

In re Robbins 964 F 2d 342 (4th Cir 1992).

In re Save Our Springs (S O S) Alliance, Inc, 632 F 3d 168 (5th Cir 2011).

In re Saypol, 31 BR 796 (Bankr SDNY 1983).

In re SGL Carbon Corp, 200 F3d 154 (3rd Cir 1999).

In re Shippers Interstate Service Inc., 618 F 2d 9 (7th Cir 1980).

In re SPM Mfg. Corp., 984 F.2d 1305, 1315-16 (1st Cir 1993).

In re Sunedison, Inc, 575 B R 220 (Bankr S D N Y 2017).

In re Texaco Inc, 84 BR 893 (Bankr S D N Y 1988).

In re Texas Star Refreshments 494 B R 684 (Bankr N D Tex 2013).

In re the Gibson Group, Inc., 66 F.3d 1436, 1442 (6th Cir. 1995).

In re The Score Board Inc, 238 BR 585 (DNJ 1999).

In re Universal Life Church, Inc, 128 F 3d 1294 (9th Cir 1997).

In re W R Grace & Co, 475 B R 34 (D Del 2012).

In Re Williamson-Blackmon, 145 BR 18 (Bankr ND Ohio 1992).

In re Woodbrook Associates, 19 F 3d 312 (7th Cir 1994).

In Re: Sentry Operating Company of Texas, 264 B R 850 (Bankr S D Tex 2001).

Lockyer v Mirant Corp, 398 F 3d 1098 (9th Cir 2005).

Louisville Joint Stock Land Bank v Radford, 295 US 555 (1935).

Marshall v. Tauscher (In re Tauscher), 7 Bankr 918 (Bankr ED Wis 1981).

Matter of Davis, 691 F 2d 176 (3d Cir 1982).

Pennzoil Co. v. Texaco Inc., No. 84-05905 (Tex. Dist. Dec. 10, 1985).

Re Gruntz 202 F 3d 1074 (9th Cir 1999).

Re Lazarus Burman Associates 161 BR 891 (Bankr EDNY 1993).

Re Steven P. Nelson 140 BR 814 (Bankr MD Fla 1992).

Ritchie Capital Management, LLC v Jeffries, 653 F 3d 755 (8th Cir 2011).

Small Business Admin. v. Rinehart 887 F2d 165 (8th Cir 1989).

SPCP Group, LLC v Biggins, 465 B R 316 (2011).

Travelers Insurance v Bryson Properties, XVIII, 961 F 2d 496 (4th Cir 1992).

United Savings Ass'n v Timbers of Inwood Forest Assocs, Ltd, 484 US 365 (1988).

Windsor on the River Associates, Ltd. v. Balcor Real Estate Finance, Inc, 7 F 3d 127 (8th Cir 1993).

Wright v Union Central Life Ins Co, 311 US 273 (1940).

Younger v. Harris 401 US 37 (1971).

Saudi Arabia:

Case number 523 (2020).

Case number 1960 (2020).

Case number 3289 (2019).

Case number 433 (2019).

Case number 8170 (2019).

Case number 16153 (2019).

Case number 10312 (2019).

Case number 10553 (2019).

Case number 2107 (2020).

Case number 7079 (2020).

Case number 6831 (2019).

Case number 10957 (2019).

Case number 2501 (2019).

Case number 5102 (2019).

Case number 4979 (2020).

Case number 15316 (2021).

Case number 5208 (2020).

List of Legislation

United Kingdom:

Companies Act 1862

Companies Act 1985

Companies Act 2006

Company Directors Disqualification Act 1986

Corporate Insolvency and Governance Act 2020

Enterprise Act 2002

Insolvency Act 1985

Insolvency Act 1986

Insolvency Act 2000

Insolvency Rules 1986

Insolvency Rules 2016

United States:

Bankruptcy Act 1800

Bankruptcy Act 1898

Bankruptcy Code 1978

Chandler Act 1938

Saudi Arabia:

Bankruptcy Law 2018

Bankruptcy Preventative Settlement Law 1996

Board of Grievances Law 2007

Commercial Court Law 1931

Commercial Papers Law 1962

Council of Ministers Resolution No. 939 dated 22/10/2018

Explanatory Note to the Bankruptcy Preventative Settlement Law 1996

Implementation Mechanism of the Judiciary Law and The Board of Grievances Law (Implementation Mechanism 2007)

Implementation Regulations of BPS 1996

Implementing Regulations of BL 2018

Judiciary Law 2007

Law of Chamber of Commerce and Industry 1980

Law of the Council of Ministers

Law of the Shura Council

Municipalities and Villages Law 1977

Shura Council Resolution No 114 (1955)

The Basic Law of Governance 1992

Other Jurisdictions:

Australian Corporations Act 2001

Egyptian Trade Law 1999

European Union Restructuring Directive (Directive 2019/1023)

French Commercial Code 2005

French Commercial Code of 1808

German Insolvency Code (*Insolvenzordnung*) 1999

Irish Companies (Amendment) (No. 2) Act 1999

Jordanian Insolvency Act 2018

Jordanian Trade Law 1966

Singapore Companies (Amendment) Act 2017

UAE Federal Law No 18 of 1993

Chapter 1: Introduction

In this thesis, the rules of corporate restructuring introduced under the new Saudi Bankruptcy Law (BL) 2018 will be examined with reference to the United Kingdom's and the United States' invaluable experiences in this area. The study is designed to determine whether restructuring procedures in BL 2018 are likely to be effective for rehabilitating viable but distressed businesses, as they were intended to do. The UK and U. S. experiences provide valuable guidance for evaluating and refining Saudi restructuring law, as policies and practices from these two jurisdictions were referenced when drafting BL 2018. In order to achieve reliable and comprehensive results, the main aspects of restructuring procedures will be examined in this study, namely, access to restructuring procedures, control of company during procedures, moratorium against creditors' actions, and restructuring plan. This chapter explains the background to the study; its originality, objectives, and methodology; and the arrangement of chapters.

1.1 Background

The evolution of the 'rescue culture' and rehabilitation of companies and businesses in corporate insolvency has received global attention for decades. The success of Chapter 11 in US Bankruptcy Code 1978 is believed to have significantly influenced the development of corporate rescue procedures across the world. Since then, the approach to corporate insolvency in many countries shifted from the traditional method of liquidation to the newer practice of rehabilitation.[1] Corporate reorganisation is based on the assumption that the going concern value of a distressed business is more than its liquidation value.[2] LoPucki and Whitford have noted that the existence of reorganisation procedures is commonly based on the presence of a distinction between the going concern value of the distressed business and its liquidation value.[3] If the going concern value of a company (the present value of the company's future earning power) is higher than the value extracted from the liquidation of its assets, the

[1] Pieter Kloppers, 'Judicial Management-A Corporate Rescue Mechanism in Need of Reform' (1999) 10 Stellenbosch L. Rev. 417, 417.

[2] Charles J Tabb, 'The Future of Chapter 11' (1992) 44 SC L Rev 791, 804. In contrast, the premise that the going concern value of the distressed firm may commonly exceed its liquidation value has been challenged by Baird, who argued that 'the set of conditions that make a corporate reorganization preferable to a corporate liquidation is exceedingly narrow [and] there are a large number of cases for which a reorganization seems clearly inferior to the alternatives'. Douglas G Baird, 'The Uneasy Case for Corporate Reorganizations' (1986) 15 J Leg Stud 127, 128.

[3] Lynn M LoPucki and William C Whitford, 'Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies' (1992) 141 U Pa L Rev 669, 758.

reorganisation procedure may be an attractive alternative to liquidation. In this scenario, it would be more advantageous for creditors as a whole if the business continues to operate, and it would be in the interest of society if a firm that is worth more alive than dead is successfully restructured.[4]

Over the past several years, many European jurisdictions have apparently tried to emulate the US Chapter 11 legislation by moving away from liquidation-based regimes towards regimes that promote business rehabilitation.[5] Germany, for example, was one of the first European countries to take Chapter 11 as a model for their reforms in insolvency law.[6] Section 1 of the German insolvency Code (*Insolvenzordnung*), which went into effect in January 1999, states that 'the purpose of insolvency proceedings is the collective satisfaction of the debtor's creditors through realisation of the debtor's assets and distribution of the proceeds or through agreement on an alternative arrangement in an insolvency plan, particularly in order to maintain the enterprise'. Moreover, the most recent development in corporate rescue in Europe was the enactment of the new European Union Restructuring Directive (Directive EU 2019/1023 of the European Parliament and of the Council of 20 June 2019).[7] The overall objective of the Directive is to remove the obstacles to freedom of establishment and the free movement of capital arising from differences in the laws and procedures applied across the EU member states on restructuring and insolvency.[8] The European Commission proposal in 2016 suggested that:

> Boosting jobs and growth in Europe requires a stronger rescue culture which helps viable businesses to restructure and continue operating while channelling enterprises with no chance of survival towards swift liquidation, and gives honest entrepreneurs in distress a second chance. This proposal is an important step towards such a change of culture.[9]

[4] Daniel J Bussel and David A Skeel, JR, *Bankruptcy* (10th edn, Foundation Press 2015) 523.
[5] Martin Gudgeon and Shirish Joshi, 'The Restructuring and Workout Environment in Europe' in Ben Larkin (ed), *Restructuring and Workouts: Strategies for Maximising Value* (2nd edn, London: Globe Law and Business 2013) 8.
[6] See Bianca Schwehr, 'Corporate Rehabilitation Proceedings in the United States and Germany' (2003) 12 International Insolvency Review 11.
[7] The Directive was published in the Official Journal of the European Union on 26 June 2019. The Directive must be implemented by EU Member States by 17 July 2021, with the possibility of extension up to one year.
[8] Directive 2019/1023, Recital (1).
[9] COM (2016) 723 final, p 7.

One of the main elements of the Directive was the introduction of the new preventive restructuring framework, which must be provided by EU member states to enable the restructuring of debtors where there is a likelihood of insolvency.[10]

Additionally, the socio-economic benefits of adopting rescue-oriented insolvency legislation have been actively promoted by international organisations, such as the World Bank, the United Nations Commission on International Trade Law (UNCITRAL), and the International Monetary Fund (IMF). Providing formal restructuring procedures in addition and as an alternative to liquidation procedures is regarded by these organisations as a criterion for the international respectability of a nation's insolvency laws.[11]

In 1982 in the United Kingdom, the Cork Committee, chaired by Sir Kenneth Cork, published a report (Cork Report) that provided a comprehensive overview of insolvency law in the United Kingdom and made a number of recommendations for 'radical reforms' to the United Kingdom insolvency regime. Such recommendations included promotion of a rescue culture, under which preservation of jobs is enabled and the immediate sale of debtors' assets is avoided.[12] The Cork Report can be considered the first move towards development of a formal rescue regime in the United Kingdom. As a response to the Cork Report, two rescue procedures were introduced under the Insolvency Act 1985, which was replaced by the Insolvency Act (IA) 1986. Those procedures involved Administration and Company Voluntary Arrangement (CVA). A number of significant changes in the UK corporate insolvency law were introduced in Enterprise Act (EA) 2002, which was 'designed to facilitate company rescue and to produce better returns for creditors as a whole'.[13] EA 2002 abolished administrative receivership to a large extent, the procedure for which was providing an extreme amount of power to creditors holding floating charges, who, due to their secure position, may not be interested in rescuing distressed companies.[14] EA 2002 also facilitates entry to the administration procedure by allowing an out of court appointment of an administrator by either the floating charges holder, the company or the company's directors. Moreover, the enactment of the Corporate Insolvency

[10] Directive 2019/1023, Article 1(1)(a).
[11] John Armour, Audrey Hsu and Adrian Walters, *Report for the Insolvency Service: The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings* (The Insolvency Service 2006) 4.
[12] Marjan Marandi Parkinson, *Corporate Governance in Transition: Dealing with Financial Distress and Insolvency in UK Companies* (Palgrave Macmillan, Cham 2018) 53.
[13] Christopher Mallon, Alex Rogan and Martyn Cukier, 'Restructuring in England and Wales' in Christopher Mallon (ed), *Restructuring Review* (11th edn, Law Business Research Ltd, London 2018) 106.
[14] John Armour and Riz Mokal, 'Reforming the Governance of Corporate Rescue: The Enterprise Act 2002' [2005] Lloyd's Maritime and Commercial Law Quarterly 28, 29.

and Governance Act (CIGA) 2020 was the most recent reform of the UK corporate insolvency and restructuring law. Among the reforms provided by CIGA 2020 was the introduction of two corporate restructuring procedures: a stand-alone moratorium procedure and a restructuring plan procedure (Part 26A scheme), which includes a cross-class cramdown mechanism.[15]

Meanwhile in Saudi Arabia, prior to the enactment of BL 2018, the rules that governed bankruptcy were dispersed between two pieces of legislation. The first and primary one was Commercial Court Law (CCL) 1931, which included some provisions governing liquidation of bankrupt individuals or companies.[16] The second legislation was Bankruptcy Preventative Settlement Law (BPS) 1996, a formal rescue procedure intended to help viable distressed businesses avoid bankruptcy. The old bankruptcy regime was subject to criticism and was rarely relied upon to resolve bankruptcy disputes, which were commonly settled outside the court system.[17] There were many factors that might explain why relying on the formal bankruptcy procedures under the old regime was not a favourable option for parties to resolve their disputes.

One of these factors and arguably the key one was the absence of a functional rescue procedure that could be used to preserve viable enterprises.[18] Rescue procedures provided by BPS were criticised and rarely used for many reasons.[19] One of these is the lengthy and detailed requirements the debtor had to meet to become eligible to seek settlement. For example, at the time the settlement proceeding is commenced, the business should have been operating for at least three years.[20] Another defect in the rescue process in BPS was the narrow scope of moratorium provided against creditors' actions brought during ongoing settlement proceedings. Moratorium in BPS applied only to claims of unsecured creditors whose debts were created before the settlement proceeding began; they did not cover actions brought by secured creditors or claims relating to post-petition debts.[21] Another shortcoming in the old bankruptcy regime in general, and not limited to BPS, is uncertainty surrounding the outcome of proceedings commenced under that regime. Since provisions of BPS and CCL were very

[15] CIGA 2020 came into effect on 26 June 2020.
[16] CCL, arts 103-137.
[17] Patrick Venter and James Sprayregen, 'Bankruptcy Reform in Saudi Arabia' (2016) 34 Law Journal Newsletters 2-6.
[18] Dina Elshurafa, 'Insolvency Laws in Saudi Arabia: Time for Change?' (2012) 9 International Corporate Rescue 300, 305–306.
[19] These reasons are discussed in chapter 2 of this thesis.
[20] Implementation Regulations of BPS, art 5.
[21] Implementation Regulations of BPS, art 19.

brief and did not deal with many important bankruptcy matters, the judgment in these matters was subject to the discretion of the court. Considering the broad authority given to judges in these cases, in addition to the fact that the judges were not obliged to follow case law, it was theoretically expected, at the least, to have a difference in the outcomes of bankruptcy cases, even if those cases had identical facts.

A clear example showing the attitude of markets towards the old law is the case of the Al-Ittefaq Steel Products Company, a well-respected Saudi company that, because of a collapse in steel prices in 2009, suffered from financial difficulties. After two-and-a-half years of negotiations and consultations, in 2011 the company reached an out-of-court agreement with its creditors, 18 Saudi and international banks. The debt of US$2 billion was restructured over 6 years to allow the company to survive and regain its solvency. Both the company and its creditors agreed not to rely on the court system to solve their dispute due to the system's inherent uncertainty.[22]

Modernising the laws governing business activities has been one of the central initiatives taken by the Saudi government to attract foreign investment. This is viewed as an essential way to accomplish the ultimate goal of achieving the kingdom's 2030 Vision, which is to diversify economic sources and to reduce the dependence on oil as a main source of income.[23] Updating the bankruptcy law and replacing its outdated provisions was given high priority by Saudi lawmakers when seeking to modernise the business laws of the kingdom, as the defects of the old bankruptcy regime and its ambiguousness were seen as obstacles discouraging foreign parties from investing in the kingdom.[24] In order to reform the bankruptcy law of the kingdom, a benchmarking study was undertaken by the Saudi Ministry of Commerce and Industry with seven different insolvency regimes, which are considered to have well developed practices to handle bankruptcy cases. The benchmarked jurisdictions were the Czech Republic, England and Wales, Germany, France, Japan, Singapore, and the United States.[25] The Ministry also considered some supra-national sources, such as legislation and proposals at the EU and UNCITRAL level. The central objective for the desired bankruptcy law, as indicated in its

[22] Elshurafa (n 18) 306.
[23] 'Saudi Arabia Vision 2030 Homepage - Vision 2030' 81–82 <https://www.vision2030.gov.sa/> accessed 12 September 2021.
[24] Grahame Nelson and Mohammed Negm, 'The New Saudi Arabian Bankruptcy Law' (2018) 307 Law Update 38, 38–41.
[25] Ministiry of Commerce and Industry, *Saudi Insolvency Law Project, Policy Paper* (2015) 3.

policy draft paper issued by the Ministry of Commerce and Industry, is to encourage financial activity, including circumstances where debtors may suffer distress and may be either viable enough to be rehabilitated or liquidated in a cost-effective process so that the capital can be reallocated.[26]

The benchmarking study paved the way for the introduction of the first national comprehensive bankruptcy Law (BL), which came into effect in August 2018. The new law replaces bankruptcy provisions in the CCL and BPS and now serves as the only legislation governing bankruptcy in the kingdom.[27] It provides three main procedures: Preventative Settlement, Financial Restructuring, and Liquidation.

The focus of this study is limited to Preventative Settlement (PS) and Financial Restructuring (FR) procedures, as they represent the corporate rescue procedures provided under BL 2018. Such procedures are designed to forestall the need for liquidation if the survival of the business is feasible. The two processes share many features with the rescue procedures in the UK law, as well as with Chapter 11 of the US Bankruptcy Code 1978. Such similarities are expected, as England/Wales and the United States were two of the main jurisdictions that Saudi lawmakers looked at as models when seeking to modernise bankruptcy law in general and restructuring procedures specifically.

1.2 Originality

The restructuring provisions introduced under BL 2018 have been largely transplanted from foreign jurisdictions, and they are, to a large extent, new to the Saudi legal environment. To deal with this newness, the study could provide the national legal system with guidance on how to implement rescue provisions from the experiences of well-developed jurisdictions, namely, the United Kingdom and the United States, as these two systems had been looked at as models by Saudi lawmakers when drafting the new law. Accordingly, the study would be the first one to critically examine the Saudi restructuring law with comparison to the laws of the United Kingdom and the United States.

[26] ibid 5.
[27] BL 2018, art 230.

Literature concerning corporate rescue in Saudi bankruptcy laws and regulations is scarce. The shortage of literature on the new law is reasonable, as the law has not been in effect for long, but lack of literature is not limited to the new law. Bankruptcy law, in general, and corporate rescue specifically under the old law were not popular topics among academics, as those topics were rarely discussed in academic books or articles. It is possible that the old law's unpopularity and minimal usage discouraged academics from conducting research on bankruptcy law. Therefore, the significance of conducting this study stems from the fact that it can help to fill the gaps in the literature and add to knowledge in various matters related to restructuring law.

1.3 Research Objectives

This study concentrates on formal corporate rescue procedures in Saudi bankruptcy law, PS and FR, with reference to the formal rescue mechanisms applicable in the United Kingdom and Reorganisation process in Chapter 11 of the U. S. Bankruptcy Code. The goal of this study is to determine whether the rescue procedures under Saudi bankruptcy law are functional and effective for rehabilitating struggling but viable businesses. Accordingly, the sub-objectives of the study are as follows:

1. Explore the historical development of bankruptcy law in Saudi Arabia and investigate reasons behind the introduction of the new 'rescue-oriented' bankruptcy law.
2. Provide a general overview of the formal restructuring procedures provided under Saudi bankruptcy law.

Although the first two objectives are not original, still they are necessary to provide a foundation for achieving the subsequent, original objectives which are as follows:

3. Examine particular aspects of rescue procedures under Saudi law and compare how the United Kingdom and the United States address these aspects, which are listed below.
    A. Access to restructuring procedure.
    B. Control of company during restructuring period.
    C. Moratorium/Automatic stay on creditors' actions.
    D. Restructuring plan.
4. Identify and address strengths and weaknesses of existing rescue procedures.
5. Highlight recommendations and suggestions to improve rescue procedures in Saudi Arabia.

Since the restructuring mechanisms provided under the new bankruptcy law are largely new to Saudi's legal community, referring to the laws in the United Kingdom and the United States regarding the above aspects is highly important, as the Saudi legal system can learn valuable lessons from the procedures from these well-developed jurisdictions.

1.4 Methodology

In order to achieve its objectives, this study applies the doctrinal method to identify and critically examine specific concepts of restructuring procedures under the new bankruptcy law of Saudi Arabia. Doctrinal research is a process by which the content of law is identified, analysed, and synthesised.[28] This method allows the researcher to critically examine legislation and case law, as well as to identify and analyse legal issues, based on the interpretation and examination of primary and secondary sources.[29]

There are two main reasons behind adopting the doctrinal methodology as the primary method for this study. First, it is stated that the 'doctrinal method is normally a two-part process [involving both] locating the sources of the law and then interpreting and analysing the text'.[30] Examining particular aspects of corporate restructuring rules in Saudi bankruptcy law, as well as in UK and US laws, is a crucial element of this thesis. Such examination is the foundation for further discussions over any practical and theoretical issues related to corporate restructuring. Therefore, the adoption of the doctrinal method is essential to this study, as it is based on close examination of texts of primary and secondary sources of corporate insolvency laws in the three jurisdictions mentioned above. Secondly, as Hutchinson states, doctrinal research is 'well suited to advocacy and finding solutions to legal problems'[31]. As one of the main objectives of this study is to identify any weaknesses in existing restructuring procedures in Saudi law and to highlight recommendations and suggestions for reform, conducting a doctrinal research is appropriate to fulfil that objective.

[28] Terry Hutchinson, 'Doctrinal Research: Researching the Jury' in Dawn Watkins and Mandy Burton (eds), *Research Methods in Law* (Routledge 2013) 9.
[29] ibid 11–12.
[30] Terry Hutchinson and Nigel Duncan, 'Defining and Describing What We Do: Doctrinal Legal Research' (2012) 17 Deakin Law Review 83, 110.
[31] Hutchinson (n 28) 28.

In addition to the doctrinal method, the thesis employs a comparative approach, as it refers to the formal corporate restructuring procedures in the UK and to reorganisation procedure under Chapter 11 of the US Bankruptcy Code 1978. The use of the comparative method is important to critically evaluate the efficacy of corporate restructuring procedures in Saudi bankruptcy law for enabling the rescue of distressed but viable businesses. The use of comparative law for critical evaluation of one's own law is supported by Smits. He argues that 'what the law ought to be' should be the main topic of legal research, and that comparative law plays an important role in answering this question, as foreign experiences could be considered a source of information in the normative discussion.[32] The importance of comparative analysis in evaluating the efficacy of national law is also emphasised by Siems. He states that a researcher should conduct a comparative analysis with an open mind and not set out to confirm pre-existing views. Hence, comparative experiences could enable the researcher to view his or her own legal system 'through the eyes of an outsider'.[33] The examination of the Saudi bankruptcy law in light of more developed legal systems could assist the researcher in identifying the shortcomings in the Saudi law and in producing reform recommendations. Indeed, comparative law provides a pool of models to be used to find solutions to problems identified in a national legal system and to make recommendations for legal reform.[34] Therefore, the use of the comparative method in this study serves two objectives: 1) evaluating the efficiency of the restructuring procedures in Saudi bankruptcy law, and 2) providing solutions to deal with any identified problem in Saudi law by referring to the UK and the US laws to learn how these problems were resolved in those jurisdictions.

The choice of the United Kingdom and the United States as comparators in this study is justified for two reasons. First, the two jurisdictions were the subjects of a benchmarking study carried out by the Saudi Ministry of Commerce and Industry during the process of drafting the new law. The Ministry stated that it had selected seven jurisdictions that have effective insolvency regimes from which to examine and analyse bankruptcy laws in order to benefit

[32] Jan M Smits, *The Mind and Method of the Legal Academic* (Edward Elgar Publishing 2012) 76.
[33] Mathias Siems, *Comparative Law* (2nd edn, Cambridge University Press 2018) 28. In this regard, Lepaulle states that 'to see things in their true light, we must see them from a certain distance, as strangers, which is impossible when we study any phenomena of our own country. That is why comparative law should be one of the necessary elements in the training of all those who are to shape the law for societies in which every passing day brings new discoveries, new activities, new sources of complexity, of passion, and of hope'- Pierre Lepaulle, 'The Function of Comparative Law with a Critique of Sociological Jurisprudence' (1922) 35 Harvard Law Review 838, 858.
[34] Esin Örücü, *The Enigma of Comparative Law: Variations on a Theme for the Twenty-First Century* (Springer 2013) 213.

from their experiences in drafting an effective bankruptcy law for the kingdom.[35] Accordingly, UK and US practices could be used as a normative standard for critical examination of the corporate restructuring procedures in Saudi bankruptcy law. Secondly, the two jurisdictions apply different sets of laws to deal with an insolvent company: the US reorganisation law is commonly labelled debtor-oriented, while the UK law is recognised as creditors-oriented.[36] Such differentiation could provide a positive diversity in philosophies and perspectives, thereby enriching the outcome of the study.

1.5 Arrangement of the Chapters

This thesis is divided into eight chapters. The first chapter introduces the research topic and background; the research originality, objectives, and methodology; and arrangements of the chapters. Chapter two presents the historical development of bankruptcy law in Saudi Arabia prior to enactment of BL 2018. The chapter illustrates the main features of the old bankruptcy regime in the kingdom and identifies the main shortcomings in that regime. An overview of BL 2018 and its formal procedures is provided in chapter three. Subsequent chapters present analyses of particular aspects of BL 2018 corporate restructuring procedures with reference to corporate restructuring procedures in the UK and Chapter 11 of the US Bankruptcy Code 1978.

More specifically, chapter four is concerned with commencement of restructuring procedures. The chapter examines the eligibility criteria and conditions that have to be satisfied for the commencement of restructuring procedure, in order to determine whether such criteria facilitate timely access to restructuring procedure, which is crucial for the success of restructuring process. Chapter five examines the issue of control over the debtor company's affairs during the reorganisation process under the Saudi BL 2018 regime. The chapter discusses the two managerial models for corporate reorganisation procedures available under Saudi law: the debtor-in-possession (DIP) model adopted under the PS process and the co-determination model adopted under the FR process. The advantages and drawbacks of both

[35] Ministiry of Commerce and Industry (n 25) 3.

[36] David Hahn, 'Concentrated Ownership and Control of Corporate Reorganisations' (2004) 4 Journal of Corporate Law Studies 117, 121. Professor McCormack challenges the traditional characterisation that US law in the sphere of corporate bankruptcy is pro-debtor, whereas UK law is pro-creditor, and suggests that such characterisation is something of an over-simplification. He states that although creditors in the UK have a greater role in the initiation of formal procedures than they do in the US, the creditors in the US may play a decisive role in the outcome of the restructuring process by their willingness to grant or deny a new financing and their influence over the terms on which such financing is provided. Gerard McCormack, 'Apples and Oranges? Corporate Rescue and Functional Convergence in the US and UK' (2009) 18 International Insolvency Review: Journal of the International Association of Insolvency Practitioners 109.

models are examined to determine their effectiveness and suitability for the Saudi legal environment.

Chapter six examines the moratorium or automatic stay on creditors' enforcement actions, which is an intrinsic feature of corporate restructuring procedures. The chapter addresses the importance and effects of the moratorium, its scope and duration, and the circumstances under which the stays can be lifted. Chapter seven discusses the reorganisation plan, which is the central element of the reorganisation procedure. The chapter considers a number of essential issues with respect to the restructuring plan under Saudi law. The consideration focuses on five key aspects of the restructuring plan: entitlement to vote on the plan, classification of claims, the threshold of creditors' acceptance of the plan, the court's confirmation of the plan and the rules of the cross-class cramdown provision. Finally, the research is concluded in chapter eight, which presents a summary of the findings and contains essential recommendations and suggestions to strengthen the efficacy of corporate restructuring procedures in Saudi Arabia.

Chapter 2: The Historical Development of Bankruptcy Law in Saudi Arabia

Before the introduction of the first comprehensive bankruptcy law in 2018, Saudi bankruptcy laws were regarded as complex and uncertain, rendering them rarely used.[37] Such laws failed to provide a robust rescue mechanism to protect troubled debtors who had the potential to survive if such a mechanism were provided.[38] The failure of the Saudi bankruptcy regime to cope with the complexity of the modern financial world and the inherent uncertainty of the regime have led many defaulted companies to seek out-of-court settlement with their creditors.[39]

Prior to the enactment of the BL 2018, there were two pieces of legislation based on which bankruptcy cases were decided: Chapter 10 of the Commercial Court Law (CCL) 1931 and the Bankruptcy Preventive Settlement Law (BPS) of 1996. Because the distinction between a merchant and non-merchant was adopted for the application of Saudi commercial law, only merchants, whether individuals or companies, were subject to the application of the bankruptcy laws provided by these two pieces of legislation.[40]

In order to have a clear picture of the development of bankruptcy law in Saudi Arabia, it is essential to understand the context in which such development has taken place. Accordingly, this chapter provides a background of the kingdom's legal system before moving to discuss the rules governing bankruptcy cases prior to the introduction of the new BL 2018. The chapter is divided into four parts. The first part is an overview of the legal system of the kingdom, the second part focuses on the bankruptcy rules under CCL, the third part addresses the formal rescue procedure provided in BPS, and the fourth part identifies the main shortcomings of the old bankruptcy regime.

[37]Alex Gross, 'Saudi Arabia to Introduce Revolutionary New Insolvency Law in 2016 | ESQUIRE Global Crossings' (2015) <https://www.restructuring-globalview.com/2015/12/saudi-arabia-to-introduce-revolutionary-new-insolvency-law-in-2016/> accessed 17 January 2019.
[38] Elshurafa (n 18) 305.
[39] Gross (n 37).
[40] Abdulrahman Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (Al Shegrey 2012) 299.

2.1 Legal System of Saudi Arabia

Islamic law is the overall legal system applied in Saudi Arabia. Unlike most other Islamic countries, the essential core of the Saudi legal system has never been influenced by Western laws, as the kingdom has never been subjected to Western colonisation.[41]

The Basic Law of Governance (BLG) of Saudi Arabia enacted in 1992 confirmed the role of Sharia in the Constitution of the kingdom[42]. Article 1 of that law states: 'The religion [of Saudi Arabia] is Islam, its constitution is the Book of God Most High [Quran] and the Sunna of His Prophet'. In addition, Article 7 states that 'rule in the Kingdom of Saudi Arabia draws its authority from the Book of God Most High and the Sunna of His Prophet. These two are sovereign over this regulation and all regulations of the state'. Moreover, the sovereignty of Sharia and its role as a legal system of the state is confirmed by Article 48, which indicates that 'the courts shall apply in cases brought before them the rules of the Islamic sharia in agreement with the indications [proofs] in the Book and the Sunna and the regulations issued by the ruler that do not contradict the Book or the Sunna'.[43] It is clear from Article 48 that the legality of any legislation issued by the Saudi government and the validity of any judicial judgment depend on their agreement with the provisions of Islamic law.

2.1.1 Legislation as a Source of Law in the Kingdom

It would be misleading to state that Sharia is the only source of law in Saudi Arabia. Of course, Sharia is the dominant law in the kingdom, but the scope of Saudi law is broader than Sharia.[44] Saudi law is composed of Islamic rules as well as regulations and acts adopted from foreign jurisdictions.[45] Most acts governing commercial activities in Saudi Arabia fall under these types of regulations.[46] For instance, the CCL 1931, which is the oldest commercial law in Saudi

[41] Frank E Vogel, *Islamic Law and Legal System: Studies of Saudi Arabia* (Brill 2000) 220.
[42] An official English translation of BLG is available at https://www.saudiembassy.net/basic-law-governance
[43] The Qur'an and the Sunna are regarded as the primary sources of Islamic law. The principles of Islamic law are established in the Qur'an, the Holy Book of Islam, and the Sunna, which contains the deeds and sayings of the prophet Mohammed. When primary sources do not address the matter in question, the role of secondary sources emerges. The main secondary sources are *ijma*, which presents the views of Islamic scholars arrived at by consensus, and *qiyas*, which means reasoning by analogy. The importance of the latter source is apparent when none of the primary sources is clear regarding the matter in question; thus, decisions must be established through analogy (*qiyas*) to similar cases that are addressed in the Qur'an or Sunna. See Abed Awad and Robert E Michael, 'Iflas and Chapter 11: Classical Islamic Law and Modern Bankruptcy' (2010) 44 Int'l Law 975; Farhad Malekian, *Principles of Islamic International Criminal Law* (2nd edn, Brill 2011).
[44] Nabil Saleh, 'The Law Governing Contracts in Arabia' (1989) 38 International and Comparative Law Quarterly 761, 764.
[45] Vogel (n 41) 4.
[46] Saleh (n 44) 765.

Arabia, originated from French Commercial Code of 1808.[47] The influence of Islamic law principles seems clear and direct on aspects of, for example, family and criminal law, whereas other commercial and administrative disputes are not fully or directly governed by Islamic law.[48] In this regard, Vogel accurately describes the legal system of Saudi Arabia as consisting of two types of rules: fundamental and dominant, as originated from Islamic law; and subordinate 'man-made' law.[49]

French law has had a remarkable influence on the early stage of Saudi commercial law development.[50] An example of this influence is the CCL, which was inspired mostly by the French Commercial Code of 1808.[51] Such an influence was a normal result of the drafting of most old Saudi regulations being carried out by Egyptian scholars who followed the French legal system.[52]

As is the case in most civil law jurisdictions, the distinction between commercial and civil law has been adopted in Saudi Arabia.[53] The idea of this distinction is that commercial laws, such as the CCL, apply only to a specific category of people or companies, i.e., merchants.[54] Article 1 of CCL defines a merchant as 'a person who undertakes commercial activities[55] as a profession'[56].

The distinction between commercial and civil laws was strongly acclaimed in the kingdom, as it enables the enactment of contemporary commercial codes without Sharia as the civil law of

[47] H S Shaaban, 'Commercial Transactions in the Middle East: What Law Governs' (1999) 31 Law and Policy in International Business 157, 165; Torki A Alshubaiki, 'Developing the Legal Environment for Business in the Kingdom of Saudi Arabia: Comments and Suggestions' (2013) 27 Arab Law Quarterly 371, 381.
[48] Ayoub M Al-Jarbou, 'Judicial Independence: Case Study of Saudi Arabia' (2004) 19 Arab Law Quarterly 5.
[49] Frank E Vogel, 'Islamic Governance in the Gulf: A Framework for Analysis, Comparison and Prediction' in Gary G Sick and Lawrence G Potter (eds), *The Persian Gulf at the Millenium. Essays in Politics, Economy, Security, and Religion* (Macmillan 1997) 275.
[50] See Saleh (n 44) 765; Maren Hanson, 'The Influence of French Law on the Legal Development of Saudi Arabia' (1987) 2 Arab Law Quarterly 272.
[51] Alshubaiki (n 47) 381; Ayoub M Al-Jarbou, 'The Role of Traditionalists and Modernists on the Development of the Saudi Legal System' (2007) 21 Arab Law Quarterly 191, 210.
[52] Saleh (n 44) 765.
[53] ibid.
[54] Mohammed Al-Jaber, *Saudi Commercial Law* (4th edn, Alshegrey Publisher 1996) 7. In the Anglo-American legal system, the law merchant was incorporated into the common law throughout the 17th and 18th centuries. Consequently, the complex complications arising from a separation between 'civil' and "commercial" law are essentially unknown in the common law system. See Rudolf B Schlesinger, 'The Uniform Commercial Code in the Light of Comparative Law' (1959) 1 Inter-American Law Review 11, 40.
[55] Article 2 CCL sets forth a list of activities that are considered commerce. Therefore, the practitioner of such activities is within the scope of the application to the body of commercial regulations.
[56] CCL art 1.

the state being distorted by modifications resulting from such enactment.[57] However, that does not indicate a complete abandonment of the role of Islamic law in the Saudi commercial sector. On the contrary, Islamic law as well as the commercial customs are consulted as the default law when there is a gap within the provisions of commercial regulations.[58] Therefore, due to its limited scope of application, commercial law has been considered subordinate to the overall law (i.e., Islamic law).[59]

2.1.2 Authorities of the State

Saudi authorities are divided into three types: legislative, judicial, and executive. The mandates of each are defined in Article 44 BLG. Furthermore, BLG determines the jurisdictions of these authorities and emphasises the role of the King as the head of each of them.[60] The executive body in Saudi Arabia is embodied in the King and the Council of Ministers, as well as public, independent and quasi-independent agencies.[61] Full authority over all executive and administrative affairs is executed by the Council of Ministers, which also has the authority to devise the internal and external policies of the kingdom, including those related to finance, education, the economy, defence, and other agencies of the state.[62]

The Council of Ministers is authorised to monitor ministers and government agencies to ensure that legislation is implemented acceptably.[63] The King has the responsibility to oversee and supervise the general policy of the government as well as the application of laws, regulations, and resolutions.[64] In addition, the King has the exclusive authority to appoint and remove each member of the Council of Ministers, as well as the exclusive authority to dissolve and reconstitute the Council.[65]

The legislative authority is assigned to three parties: The King, the Council of Ministers, and the *Shura* Council (the Consultant Council).[66] The role of these two legislative councils is demonstrated in Article 67 BLG, which states the following:

[57] Saleh (n 44) 765.
[58] Al-Jaber (n 54) 7.
[59] ibid.
[60] BLG, art 44.
[61] Inc IBP, *Saudi Arabia Company Laws and Regulations Handbook* (IBP USA 2012).
[62] Law of the Council of Ministers, arts 19 and 24.
[63] Law of the Council of Ministers, arts 19 and 24.
[64] Law of the Council of Ministers, art 29.
[65] BLG, art 57.
[66] Law of the Council of Ministers, art 19, and BLG, art 67.

> The Regulatory Authority shall be concerned with the making of laws and regulations which will safeguard all interests, and remove evil from the State's affairs, according to Sharia. Its powers shall be exercised according to provisions of this Law and the Law of the Council of Ministers and the Law of the *Shura* Council.[67]

The *Shura* Council consists of the speaker and 150 members appointed by the King.[68] The functions of the *Shura* Council are to propose new laws and provide its opinions on the general policies of the state, as referred by the president of the Council of Ministers. Essentially, these functions entail interpreting and revising laws and regulations and offering suggestions for improvement.[69] The resolutions of the *Shura* Council are referred to the King, who decides which resolutions are referred to the Council of Ministers.[70]

If both the *Shura* Council and Council of Ministers agree on resolutions, then the resolutions are issued after being approved by the King. If there is a disagreement between the two councils regarding the resolutions, the matter shall be returned to the *Shura* Council to decide what it considers appropriate and passed to the King for the final decision.[71]

The right to propose a new law or to amend an existing law is granted to every minister in relation to the operation of his or her ministry.[72] In establishing the positions and roles of the Council of Ministers and the *Shura* Council as legislative bodies, it should be stressed that their legislative authority is subject to the King's approval by royal decree.[73] Indeed, the King, as head of state and president of the Council of Ministers, enjoys wide and unrestricted power to approve or reject any law proposed by the *Shura* Council or Council of Ministers.[74] Therefore, legislative power in Saudi Arabia is shared among three bodies—the *Shura* Council, Council of Ministers and the King—with the King having the broadest legislative power.

Having established, albeit briefly, the characteristics of the executive and legislative authorities in Saudi Arabia, it is essential now to provide a general overview of the judicial authority

[67] BLG, art 67.
[68] Law of the Shura Council, art 3.
[69] Law of the Shura Council, arts 15 and 18 and the amended text of art 23.
[70] Law of the Shura Council, art 17.
[71] Law of the Shura Council, art 17.
[72] Law of the Council of Ministers, art 22.
[73] BLG, art 70.
[74] Abdullah F Ansary, 'A Brief Overview of the Saudi Arabian Legal System' (2020) <https://www.nyulawglobal.org/globalex/Saudi_Arabia1.html> accessed 18 January 2021.

within the kingdom. The independence of the judiciary's authority is stated in Article 46 BLG, which emphasises that in exercising their judicial authority, judges are not subject to any authority except Sharia.[75] Furthermore, all residents of the kingdom have equal right to litigate before the court.[76]

Prior to October 2007, Saudi Arabia had two types of courts: general (or Sharia) courts and administrative courts, known as the Board of Grievances. In addition to these two main judicial branches, jurisdiction has been granted to several quasi-judicial committees to hear certain types of cases,[77] including civil, commercial, criminal and administrative disputes arising from the application of some laws and provisions.[78] In general, Sharia courts had jurisdiction over cases that involve civil disputes and personal or family affairs, and most criminal cases,[79]whereas the Board of Grievances had jurisdiction to hear any public law dispute involving the government as a party.[80] Such a dual system has been followed by many Arabian countries, such as Egypt and Tunisia, which have adopted the civil law system.[81]

The most recent and remarkable update in the Saudi judicial system was made in October 2007 when royal decrees were issued by the late King Abdullah that introduced the new Judiciary Law (JL) and the Board of Grievances Law (BGL), which replaced the old laws of 1975 and 1982, respectively. In seeking such reforms, the kingdom has invested approximately US$1.8 billion.[82] The dual judiciary system remains in place following the recent reforms. The jurisdiction over civil, commercial and criminal proceedings is granted to the ordinary courts (Sharia courts), whereas jurisdiction over administrative proceedings is granted to the administrative courts (Board of Grievances). In addition, the entitlement granted to quasi-judicial committees to hear commercial, civil, and criminal disputes has been transferred to the jurisdiction of the ordinary courts.[83]

---

[75] BLG, art 46.
[76] BLG, art 47.
[77] Ansary (n 74).
[78] ibid.
[79] Al-Jarbou (n 48) 23.
[80] The Board of Grievances was established in 1955 by the Royal Decree No 2/13/8759.
[81] George N Sfeir, 'The Saudi Approach to Law Reform' (1988) 36 The American Journal of Comparative Law 729.
[82] Al-Riyadh, 'King Abdullah Approved the Judiciary and the Board of Grievances Laws' (Issue No 14344, 2 October 2007) <http://www.alriyadh.com/2007/10/02/article284080.html> accessed 21 March 2019.
[83] Implementation Mechanism of the Judiciary Law and The Board of Grievances Law (Implementation Mechanism 2007) para 1/9/1, issued by Royal Decree No M/78 of 1 October 2007. However, some committees

Perhaps the most important feature of the new JL is the creation of specialised courts. According to this law, the hierarchical structure of the ordinary courts is as follows:[84]

1. High Court, which is the highest court
2. Courts of Appeal
3. First-Instance Courts, which comprise General Courts, Criminal Courts, Personal Status Courts, Commercial Courts, and Labour Courts.

The jurisdiction to hear bankruptcy cases was granted to the Commercial Division of the Board of Grievances until September 2017, when the commercial courts began operating.[85] Since then, specialised bankruptcy divisions in the commercial courts have had full and exclusive jurisdiction over bankruptcy cases.[86]

2.2 Bankruptcy Under CCL Regime

Despite its ambiguous drafting, the CCL is considered by some Saudi scholars to be a comprehensive source because it addresses different areas of commercial law.[87] This law is divided into four parts, governing land and maritime trade, commercial papers and bankruptcy, companies and agencies, and some arbitration rules. Nevertheless, the CCL failed to provide a comprehensive set of rules to govern the areas that the law was designed to cover. Due to this inadequacy, many of its provisions have been replaced by different independent legislation.[88] With a number of its provisions being abolished and replaced by more modern laws, the importance of the CCL as a main commercial law in the kingdom has been compared to a 'glacier that [is] melting gradually'.[89]

It is unfortunate that bankruptcy, until August 2018, was one of the few remaining topics governed by the outdated provisions of the CCL. In order to provide a general overview of the bankruptcy regime in the CCL, this part addresses the nature of bankruptcy under the CCL

were exempted and not affected by this transfer, such as the Banking Disputes Settlement Committee, see ibid para 3/2.

[84] Ansary (n 74).

[85] Saudi Gazette, 'Commercial Courts Officially Launched - Saudi Gazette' <http://saudigazette.com.sa/article/519454> accessed 23 January 2019.

[86] Al-Hayat, 'Allocation of Chambers in Commercial Courts and Courts of Appeal' (28 December 2017) <http://www.alhayat.com/article/906833> accessed 23 January 2019.

[87] Alshubaiki (n 47) 382.

[88] For example, the Commercial Papers Law 1962 replaced chapters 6,7,8 and 9 of the CCL, which were governing commercial papers.

[89] Alshubaiki (n 47) 382.

regime, types of bankruptcy, the status of 'merchant' as a condition in bankruptcy, and some procedural issues of bankruptcy proceedings.

2.2.1 Definition and Nature of Bankruptcy in the CCL

In most Arab countries, bankruptcy used to be handled strictly by laws, as bankruptcy was seen wrongdoing on the part of the bankrupt entity or individual, which could affect the sustainability of the commercial market negatively.[90] This was also the case in Western Europe and the United States until the middle of 20th century. In these countries and during that period of time, bankruptcy was considered an indication of bad faith or at least a management failure on the part of the debtor, whose default in repaying the debt was perceived as a betrayal of social moral norms.[91] For an in-depth comprehension of bankruptcy under the CCL, one must first consider the definition of bankruptcy provided by the law in question.

Although the CCL did not define bankruptcy, Article 103 defined the bankrupt party as a 'person whose debts exceed his or her assets and who is thereby unable to discharge his or her liability for such debts'.[92] According to this definition and the provisions of Articles 103 to 137, bankruptcy can be defined as 'a collective mechanism aimed at liquidating the assets of a merchant who ceases to pay his or her commercial debts as a result of his or her inability to meet them'.[93]

The bankruptcy method applied in accordance with Chapter 10 of the CCL had four main features.[94] First, it was a collective mechanism in which a creditor was not entitled to take individual action against the bankrupt party; the right to take such action was granted to the creditors as a whole.[95] Second, it was a liquidation-based regime.[96] This meant that unless otherwise agreed upon by the creditors, liquidation was the only option provided to distressed

[90] Historically, business failure was not perceived as being an essential part of a healthy business environment in the Middle East and North Africa region. See Tim Ross and Christian Adams, 'Legal and Practical Issues for Restructuring and Insolvency in the UAE' (2010) First Quar The Quarterly Journal of INSOL International 15, 16.
[91] Rafael Efrat, 'The Evolution of Bankruptcy Stigma' (2006) 7 Theoretical inquiries in Law 365, 367.
[92] CCL, art 103.
[93] Mohammed Altabtabai, 'The Implications of Bankruptcy in Islamic Jurisprudence and Law' (Higher Judicial Institute, Imam Mohammad Bin Saud Islamic University 1995) 24.
[94] ibid.
[95] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 301.
[96] Tala Al Hejailan, 'Commercial Insolvency and Bankruptcy Regimes' in Alem & Associates and Alttayyar Law Firm (eds), *Business Laws of Saudi Arabia* (Thomson 2014) 2.

companies that sought to apply Chapter 10 of the CCL.[97] No formal rescue routes, such as reorganisation in Chapter 11 of the U. S. Bankruptcy Code or administration under the UK IA 1986, were available. Third, the provisions of Chapter 10 applied only to merchants (either individuals or companies). By contrast, a non-merchant debtor was subject to the general law applied by Sharia courts.[98] Fourth, the provisions of Chapter 10 applied only to debts arising from commercial transactions, whereas debts arising from non-commercial transactions are subject to Sharia rule.[99]

Bankruptcy under the CCL was considered to be too creditor-oriented and to have harsh and severe consequences on the bankrupt party and on his or her commercial reputation.[100] Such consequences included the detention of the debtor or placement of the debtor under the supervision of police when bankruptcy proceedings commenced.[101] In addition, as soon as a debtor was declared bankrupt, he or she was displaced from managing his or her business.[102] Moreover, the declaration of bankruptcy automatically led to depriving the bankrupt party from certain entitlements, such as serving on the local council[103] and being a member of a chamber of commerce.[104] In this regard, Saudi Arabia followed the old view that bankruptcy stigmatised the bankrupt party and made them incompetent for holding certain important positions in the state.[105]

---

[97] ibid.

[98] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 312–319.

[99] Abdulhadi Al-Ghamdi and Ben Younes Hosseini, *Commercial Law* (3rd edn, Al Shegrey 2009) 33.

[100]Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 329. When it comes to the consequences of bankruptcy, the influence of the 1808 Napoleonic Code de Commerce on the CCL seems remarkable, as the former relied heavily upon restrictive means as a substitute for probably inadequate market regulations. Under Napoleonic Code defaulted debtors were imprisoned and restructuring of debts was highly restricted. See Jérôme Sgard, 'Do Legal Origins Matter? The Case of Bankruptcy Laws in Europe 1808-1914' (2006) 10 European Review of Economic History 389.

[101] CCL, art 109. The Court shall, in accordance with its discretion, take either of the two options: arresting the bankrupt or placing it under the supervision of the police. It should be noted that the decision of the court to arrest the bankrupt is not considered a penalty, but a preventative measure aimed at ascertaining the availability of the debtor whenever the court needs to question him and inquire about the bankruptcy estate. Thus, the court may release the bankrupt if it finds that his detention is unnecessary. See Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 329; Altabtabai (n 93) 322.

[102] CCL, art 110.

[103] Municipalities and Villages Law 1977, art 11.

[104] Law of Chamber of Commerce and Industry 1980, art 4. The Chamber of Commerce and Industry is an organization that represents the commercial and industrial interests at the public authorities and works to protect and develop such interests. ibid art 1.

[105] Shawgi Sabeel, *The Implications of Declaring Bankruptcy in Islamic Jurisprudence and Law* (Al Neelain University 2017)129-132.

The harsh treatment of the bankrupt under the CCL may be because assisting creditors in enforcing their claims against the debtor's assets was the primary goal of bankruptcy law and serving such a goal was the principal justification for this. In this regard, a general reading of CCL indicates that it followed the traditional models of the U. S. Bankruptcy Act 1800, which was inspired largely by the 1732 Statute of George II, which was the English bankruptcy law in effect at that time.[106] Bankruptcy under these laws was not a method aimed at relieving overburdened debtors and reinvigorating the economy, but a device intended to help creditors enforce their rights and seek an allocation equal in value to the debtor's assets.[107] With this in mind, it can be understood why the interests of the bankrupt under the CCL were undermined in favour of the interests of the creditors, who were seen as prejudiced parties deserving more protection. Therefore, securing the rights of creditors by maximizing the value of the debtor's assets to increase the amount of creditors' recoveries was the main goal courts aimed to achieve when applying the provisions of the CCL, and the restrictions imposed upon the debtor were seen as necessary methods to achieve that goal.

In addition, it is argued that encouraging the credit market and supporting credit providers' confidence in the market justified the stringent measures taken against the bankrupt under the CCL, which considered bankruptcy a threat to that confidence. In other words, bankrupt parties under the CCL were treated strictly as their default in paying their commercial debts was considered a betrayal of the trust required in the commercial sector.[108] The philosophy behind this tough treatment is the traditional belief that the flourishing of the commercial sector depends heavily on the availability of credit, and to enhance such availability and to encourage finance providers, it is necessary to arm these providers with a powerful mechanism to enforce their rights against the defaulted debtor.[109] Such strict treatment was applied even if the defaulted debtor was conducting his or her business in good faith and his or her default was caused by an external cause, such as a recession in the national economy.[110] It was believed that the protection of credit markets necessitated oppressive instruments of social discipline, whatever the costs for the 'honest but unlucky trader'.[111] Thus, unless otherwise agreed upon

[106] See Charles Jordan Tabb, 'The History of the Bankruptcy Laws in the United States' (1995) 3 Am. Bankr. Inst. L. Rev. 5.
[107] Jason J Kilborn, 'A Brief History of U.S. Bankruptcy Law & Policy for Consumers and Businesses' (2008) 2 <https://ssrn.com/abstract=1302388> accessed 26 February 2019.
[108] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 301.
[109] ibid.
[110] ibid.
[111] Sgard (n 100) 400.

by the creditors, the default of commercial debts was generally unforgivable and could lead to unpleasant consequences for the debtor.[112]

Therefore, the negative social attitude toward bankruptcy and the stigma associated with it were reflected in the way bankruptcy cases were governed under the CCL. Bankruptcy under the CCL was considered too creditor-friendly, with an ultimate goal of liquidating the debtor's assets and achieving an equal distribution of proceeds of these assets among the creditors. In order to assure the fulfilment of this aim, the law imposed a strict measure on the debtor, whose failure to pay the debts was seen as a threat to the sustainability of the commercial market.

2.2.2 Types of Bankruptcy in the CCL

The CCL classified bankruptcy into three categories: real, negligent, and fraudulent.[113] A real bankrupt was defined as a person (either natural or legal) who has engaged in commerce on the basis of capital that is considered sufficient by trade standards.[114] It was also stipulated that such debtors should keep regular books of business and not be wasteful in their expenses.[115] If the merchants (natural or legal) complied with these conditions and yet their debts exhausted their assets as a result of an external cause, such as fire or any other loss, they should be classified as real bankrupt in accordance with Article 105.[116] Therefore, this type of bankruptcy occurred as a result of circumstances beyond the merchants' control and without negligence or failure to maintain capital.[117] An example of this is bankruptcy resulting from property damage brought on by force majeure, or bankruptcy resulting from fluctuations in market prices and conditions that prevent a merchant from meeting debts.[118] Unlike negligent and fraudulent bankrupts, real bankrupt is not subject to any criminal liability unless the debtor fails to provide documents required in accordance with Article 109 of the CCL, which provides that when the bankruptcy declaration is sought, 'the debtor must submit his or her commercial books to the court along with a schedule showing the debtor's capital from the start of trade to the date of bankruptcy in addition to all expenses, assets and liabilities'.[119] If such failure occurs, the

[112] Sabeel (n 105) 120.
[113] CCL, art 104.
[114] CCL, art 105.
[115] CCL, art 105.
[116] CCL, art 105.
[117] Khalid Al Rawis, 'The Concept of Bankruptcy in Saudi Commercial Law' (2012) 1 Journal of Legal and Economic Research 207, 227.
[118] ibid.
[119] CCL, art 109.

bankrupt or the director, in the case of corporate insolvency, could be subject to three months' to two years' imprisonment.[120]

The second category of bankruptcy was negligent bankruptcy. A merchant who was wasteful with expenses, failed to show financial deficiency to creditors, and continued to trade until running out of capital was considered negligent.[121] A negligent bankruptcy could result from the merchant's unreasonable extravagance or from the merchant's recklessness in entering into high-risk transactions which caused the merchant to default on contractual obligations, as well as when the trader hid the inability to pay creditors and continued to trade until the debts exhausted the assets, in part or in whole. Since negligent bankruptcies resulted from the debtors' actions and decisions, the CCL dealt with it as a crime punishable by imprisonment of between three months and two years.[122]

There may be some similarities between the provision of negligent bankruptcy in the CCL and the wrongful trading provision provided in section 214 of the UK IA 1986.[123] Section 214 was introduced in IA 1986 to allow the liquidator, in an attempt to swell the asset pool for creditors of an insolvent company, to commence proceedings against the company's directors personally if it can be proved that directors did not take appropriate steps to minimise potential company losses after they first knew or ought to have concluded that avoidance of insolvent liquidation was not a reasonable prospect.[124]A director found guilty of wrongful trading may be ordered by the court to make such contribution to the company's assets as the court thinks proper.[125] In addition, and pursuant to section 215 under the declaration of wrongful trading, the court might provide for the liability to pay a contribution to be a charge on any debt or obligation due from the company to the director, or on any mortgagee or charge or any interest in a mortgage or charge on assets of the company held by or vested in the director, or any person acting on behalf of the director, or claiming as assignee from or through the director, unless the assignee

[120] CCL, art 137.
[121] CCL, art 106.
[122] CCL, art 137.
[123] For more details about wrongful trading, see: Andrew Keay, 'Wrongful Trading: Problems and Proposals' (2014) 65 N. Ir. Legal Q. 63; Andrew Keay, 'Wrongful Trading and the Liability of Company Directors: A Theoretical Perspective*' (2005) 25 Legal Studies 431; Andrew Keay and Michael Murray, 'Making Company Directors Liable: A Comparative Analysis of Wrongful Trading in the United Kingdom and Insolvent Trading in Australia' (2005) 14 International Insolvency Review 27; Andrew Campbell, 'Wrongful Trading and Company Rescue' (1994) 25 Cambrian Law Review 69.
[124] IA 1986, s 214.
[125] IA 1986, s 214.

was a *bona fide* purchaser for value.[126] As a further penalty imposed in the case of wrongful trading, the court may impose a disqualification order for up to 15 years on the liable director.[127]

A similarity between the provision of negligent bankruptcy in the CCL and the wrongful trading provision in the UK IA1986 is that both of these provisions are triggered when directors fail to take appropriate steps to minimise potential company losses when they knew or ought to have concluded that there was no reasonable prospect of avoiding insolvency.[128] In other words, liability of directors under these two provisions is founded on negligence of such directors.[129] However, there is a crucial difference in the nature of liabilities imposed by these two provisions. While the liability of a director under the wrongful trading provision in IA 1986 is purely civil[130], the liability established under the negligent bankruptcy provision in the CCL is criminal, subjecting the liable director to the possibility of imprisonment of between three months and two years.[131] The difference between the two liabilities is procedural. Proceedings for wrongful trading can only be initiated by liquidators[132]or administrators,[133] while criminal proceedings against a director in negligent bankruptcy under the CCL regime could only be commenced by the public prosecutor.[134]

The third type of bankruptcy in the CCL was fraudulent bankruptcy, which is bankruptcy arising from the merchant's will and intent to harm creditors using deceitful methods to hide assets or transfer ownership of assets to others to prevent creditors from claiming their debts.[135] This type of bankruptcy was the most severe type, and the CCL dealt with it harshly and rigorously: it was considered a criminal offence punishable by three to five years' imprisonment for the merchant and those involved in concealing the assets or arranging the fraud.[136] Although the fraudulent debtors were not, technically, considered bankrupts insofar

[126] IA 1986, s 215.
[127] Company Directors Disqualification Act 1986, s 10.
[128] Altabtabai (n 93) 70; Andrew R Keay and Peter Walton, *Insolvency Law : Corporate and Personal* (4th edn, LexisNexis 2017) 656.
[129] Rawis (n 117) 228; Anthony O Nwafor, 'Fraudulent Trading and the Protection of Company Creditors: The Current Trend in Company Legislation and Judicial Attitude' (2013) 42 Common Law World Review 297, 299.
[130] Royston Miles Goode, *Principles of Corporate Insolvency Law* (4th edn, Sweet & Maxwell 2011) 665 ; Fiona M Tolmie, *Corporate and Personal Insolvency Law* (2nd edn, Cavendish Pub 2003) 365.
[131] CCL, art 137; Rawis (n 117) 228.
[132] IA 1986, s 214 (1).
[133] IA 1986, s 246ZB.
[134] Abdulmajid Almansour, *Corporate Insolvency* (1st edn, Eshbelia 2012) 756.
[135] Rawis (n 117) 229–230. CCL, art 107.
[136] CCL, art 136.

as they had sufficient assets to discharge their debts, the law treated them as bankrupts in order to distribute their assets involuntarily among their creditors.[137] The involuntary distribution of assets was a penalty enforced on fraudulent debtors in addition to imprisonment.

The analogy with the rules of fraudulent trading in the UK law might be more relevant in the case of fraudulent bankruptcy under CCL. Fraudulent trading under the UK law is committed by any person who is knowingly involved in business with a company with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose.[138] Unlike the provision of wrongful trading, in the case of fraudulent trading, neither criminal nor civil liability is limited to directors or persons within the management of the company, but can be imposed on any persons, including complete outsiders who were knowingly parties to the fraud.[139] A party found guilty of fraudulent trading may be faced with civil and criminal actions.[140] The civil action is provided in section 213 of IA 1986, while section 993 of the Companies Act 2006 provides for criminal prosecution of fraudulent trading. Only liquidators[141] or administrators[142] may bring civil action against parties involved in fraudulent trading as provided for in section 213 of IA 1986, while criminal proceedings provided for in section 993 of the Companies Act 2006 must be commenced by the Crown.[143] Furthermore, criminal proceedings under section 993 may be commenced regardless of whether the company is in liquidation, whereas civil action under section 213 of IA 1986 may only be brought when the company has entered into liquidation[144]or administration.

Criminal liability in fraudulent bankruptcy under the CCL regime shared some features with criminal liability for fraudulent trading provided for under section 993 of the UK Companies Act 2006. First, under both statutes, liabilities are not confined to directors or others involved in the management of the company but extend to any person who is knowingly involved in the company's business with the intent to defraud creditors.[145] Second, the imposition of these criminal liabilities does not depend on the company being in liquidation. As mentioned above, criminal action may be brought for fraudulent trading under section 993 of CA 2006 regardless

[137] CCL, art 107; Altabtabai (n 93) 73.
[138] IA 1986, s 213; Companies Act 2006, s 993.
[139] Goode (n 130) 659.
[140] Keay and Walton (n 128) 667.
[141] IA 1986, s 213 (2).
[142] Under IA 1986, s 246ZA.
[143] Keay and Walton (n 128) 667.
[144] ibid.
[145] ibid 668–669; Goode (n 130) 659; Rawis (n 117) 230.

of whether the company is in liquidation or not.[146] The position was the same in the case of fraudulent bankruptcy proceedings under the CCL regime, which could be initiated whether or not the company was in the course of liquidation.[147]

Perhaps the main difference is found in the type and length of the penalty imposed on offenders of fraudulent trading and fraudulent bankruptcy. Offenders of fraudulent bankruptcy under the CCL regime were subject only to three to five years' imprisonment, and were not subject to a financial penalty.[148] Pursuant to section 993 of the UK CA 2006, a person found guilty of a fraudulent trading offence is, upon conviction, subject to imprisonment for up to 10 years or a fine (or both)[149], and on summary conviction in England and Wales, subject to imprisonment for up to 12 months or a fine not exceeding the statutory maximum (or both).[150]

It should be noted that all three categories of bankruptcy identified under the CCL regime were governed generally by the same process, except when it came to some issues like the penalty of imprisonment, which is certain in cases of fraudulent and negligent bankruptcies, and only imposed in real bankruptcy if the bankrupt failed to cooperate and provide the court with required documents.[151] In addition, the real and negligent bankrupts were allowed to receive a reasonable amount of money out of the liquidation pool in order to meet their daily financial needs, whereas the fraudulent bankrupt was not entitled to receive such an amount.[152]

2.2.3 Merchant Status as a Necessary Condition for Applying Bankruptcy Provisions

Articles 103 to 137 of the CCL concerned the bankruptcy of merchants, either individuals or companies,[153] but did not apply to non-merchants, such as consumer debtors.[154] By relying merely on the strict literal interpretation of the definition of 'bankrupt' in Article 103, which

[146] CA 2006, s 993(2).
[147] CCL, art 107.
[148] CCL, art 136.
[149] CA 2006, s 993(3)(a).
[150] CA 2006, s 993(3)(b).
[151] CCL, arts 109,136,137.
[152] CCL, art 118.
[153]Although the CCL contains rules governing the bankruptcy of individuals, its language does not indicate its application to corporate insolvency. In practice, however, such rules are applicable to corporate insolvency. See Elshurafa (n 18) 302.
[154] Bankruptcy in most Arab countries is recognised as a system that applies exclusively to merchants, either individuals or companies. See Belal A Badawy, 'Corporate Bankruptcy Requirements and Impacts : Under the Egyptian Law' (2013) 27 Journal of Sharia and Law 67.

did not explicitly mention the requirement of merchant status, it may be argued that the legislation did not require the debtor's status to be that of a merchant to apply for bankruptcy provisions. However, this argument does not seem convincing based on other articles that explicitly state that merchant status was a necessary condition for applying the bankruptcy provisions.[155] Furthermore, the provisions of bankruptcy were in Chapter 10 of the CCL, which regulated only commercial transactions carried out by merchants.[156] Clearly, bankruptcy provisions in the CCL applied exclusively to merchants. Having established this, it is logical to ask how a debtor could be considered a merchant and thus subject to the application of bankruptcy provisions in the CCL.

2.2.3.1 Acquiring Merchant Status

The requirement for acquiring merchant status applied to natural persons as well as legal persons, as not all companies were considered merchants.[157] The first article of the CCL defined a merchant as 'a person who undertakes commercial activities as a profession'.[158] Accordingly, scholarly legal and judicial views hold that to acquire merchant status, three elements were required:[159] professional work in a trade activity, performance of such work in the name and account of the performer, and legal capacity to engage in commercial transactions.

A person was considered a professional in commerce if he or she was accustomed to practising it and relied on it as a basic source of sustenance.[160] In this regard, Article 2 of the CCL listed activities considered as commerce;[161] the practitioner of such activities was within the scope of the aforementioned application of the law.[162] It should be noted that it was unnecessary for

[155] For example, Article 105 CCL states that 'a real bankrupt is a person who is engaged in the work of commerce'. Also, Article 106 states that a negligent bankrupt is a 'merchant who was wasteful in his expenses and did not show his financial deficiency to creditors and continued to trade until he ran out of capital'
[156] See Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 315; Zaynab Salama, 'Exceeding the Assets of the Debtor as a Condition to Declare Bankruptcy' (1993) 77 Public Administration Journal 77, 96.
[157] Al-Jaber (n 54) 44; Al-Ghamdi and Hosseini (n 99) ch 2.
[158] CCL, art 1.
[159] For more details, see Al-Ghamdi and Hosseini (n 99) 111; Al-Jaber (n 54) 99; Said Yahya, *Al Wajiz in Saudi Commercial Law (Arabic)* (Arab Modern Office 2015) 110.
[160] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 313.
[161] Examples of these activities are the purchase of goods with the intention of selling them, transport services of all kinds, brokering and agency. CCL, art 2.
[162] CCL, art 2.

commerce to be the individual's sole profession, but it had to be his or her main profession.[163] However, pursuant to the requirement of professional work in commerce activities, merely undertaking a few commercial transactions that did not rise to the level of a professional was inadequate for obtaining merchant status.[164] Acquiring such a status and thus being subject to the application of the CCL provisions, including those related to bankruptcy, entailed undertaking commercial transactions permanently and continually as a means of earning a living.[165]

Moreover, the performance of commercial activities had to be carried out in the name and account of the performer.[166] This condition, although not explicitly mentioned in the CCL, was implicit, since trade is based on credit, which is personal in nature and entails responsibility and liability.[167] Therefore, the performer was not considered a merchant who carried out business in the name and account of others, such as workers in shops, even if they worked in senior management.[168] One might ask whether agents and broker were considered merchants given the fact that they enter into commercial transactions in the name and account of their principals.

Interestingly, merchant status was granted to brokers and agents, despite the fact that they conduct commercial transactions in the names and accounts of others.[169] Legislators considered brokerage and agency as commercial activities[170], which qualify brokers and agents for merchant status as long as they practise brokerage and agency in their names and accounts.[171] Therefore, practising in brokerage or agency businesses was the matter the legislators looked at when they ascribed the broker and agent the status of merchant, regardless of the fact that the substance of such businesses requires the broker or agent to perform transactions in the names and on the accounts of others.[172]

[163] Al-Ghamdi and Hosseini (n 99) 64.
[164] Al-Jaber (n 54) 99.
[165] ibid.
[166] ibid 106.
[167] ibid.
[168] Al-Ghamdi and Hosseini (n 99) 69; Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 313–314.
[169] Al-Ghamdi and Hosseini (n 99) 71.
[170] CCL, art 2.
[171] Al-Ghamdi and Hosseini (n 99) 71.
[172] ibid.

The third and final element required for obtaining merchant status in accordance with Saudi commercial law was having the legal capacity to perform commercial transactions.[173] This eligibility requirement was assumed to be attained when a person reached 18 years of age.[174]A person who had yet to do so could be authorised to perform commercial business.[175] In such a case, he or she would be deemed fully qualified and would thus acquire the status of merchant within the limits of such authorisation.[176]

Qualifying for merchant status under the CCL bankruptcy provisions involved different factors for companies. The laws of Arab countries have differed in criteria for distinguishing between commercial and civil companies. Some laws, including the Egyptian Trade Law,[177] have adopted the formal standard, where each company is considered commercial and thus subject to the application of commercial laws, including bankruptcy rules, even if the objective for which the company was founded is not commercial.[178] However, Saudi law, similar to Jordanian law,[179] has adopted a substantive standard which states that a company acquires commercial status according to the purpose for which it was founded; if it was established to conduct a commercial activity identified in Article 2 of the CCL, then it was a commercial company; and if it was established for non-commercial work, then it was a civil company and therefore not subject to the bankruptcy provisions in the CCL.[180] As a result of adopting the substantive standard to distinguish between commercial and non-commercial companies in Saudi law, many companies were deemed ineligible for CCL bankruptcy provisions because the activities undertaken by these companies were not considered to be commercial according to the narrow list provided in Article 2 of the CCL.[181] Therefore, as these companies did not acquire merchant status, they were not subject to the application of bankruptcy provisions in the CCL, which were confined to merchants.[182] For example, bankruptcy provisions did not apply to legal firms, as professionals working in the legal sector were not considered to be performing commercial activity according to Article 2 CCL. The bankruptcy of such

[173] CCL, art 4.
[174] *Shura* Council Resolution No 114 (1955).
[175] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 314; Al-Jaber (n 54) 109; Al-Ghamdi and Hosseini (n 99) 75.
[176] Al-Ghamdi and Hosseini (n 99) 76.
[177] Egyptian Trade Law 1999, art 10.
[178] Hosni Al-Masry, *Bankruptcy* (Hasan Publisher 1987) 43.
[179] Jordanian Trade Law 1966, art 9(1).
[180] Al-Ghamdi and Hosseini (n 99) 135.
[181] Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135–136.
[182] Almansour (n 134) 226.

companies, excluded from the scope of CCL rules, used to be handled by the general courts in accordance with Sharia rules in bankruptcy, which is addressed briefly in a subsequent section.

Having established this, it is necessary to address another main element required for applying the bankruptcy provisions provided by the CCL. The main element is that debts subject to the application of Chapter 10 of the CCL must have arisen from commercial transactions.

2.2.3.2 Requiring Debts to Be Commercial

Most commercial laws in Arab countries require debts to have arisen from the exercise of commerce (i.e., commercial debts) to justify the declaration of bankruptcy of a merchant who fails to pay the debts.[183] One of these laws is the Jordanian Trade Act 1966, which expressly states in Article 316[184] that the rules of bankruptcy apply to 'every trader who stops paying his commercial debts'. In addition, Article 645(1) of the UAE Federal Law No 18 of 1993 states that 'any trader that ceases payment of his commercial debts on due dates, due to his financial fluctuation or credit instability, may be declared bankrupt'.[185]

However, and unsurprisingly due to its poor drafting, the provisions of the CCL were unclear in this regard. The CCL did not explicitly require the defaulted debts to have arisen from the exercise of commerce to justify the declaration of bankruptcy. Since the literal wording of Article 103 CCL did not explicitly stipulate that the debt should be commercial, AbdulGhani argues that it is permissible to declare the bankruptcy of a merchant in accordance with the provisions of CCL when he or she fails to pay a non-commercial debt.[186]

However, this view does not seem accurate, as the provisions of bankruptcy are contained in the CCL, which was a law concerned with commercial activities only. Therefore, any debt arising from non-commercial activities was not covered by the scope of the CCL.[187] Instead, any dispute related to the bankruptcy of a debtor who fails to pay non-commercial debt is subject to the rules of Islamic law, and the jurisdiction over such dispute is granted to Sharia

[183] Ziad Diab, *Corporate Insolvency in Islamic Jurisprudence and Comparative Law* (Dar Alnafaies 2011) 159.
[184] This article and all insolvency provisions in the Jordanian Trade Act 1966 have been replaced by the new Jordanian Insolvency Act 2018.
[185] UAE Federal Law No 18 of 1993, art 645(1).
[186] Mutamad AbdulGhani, *The Foundations of Bankruptcy in Islamic Jurisprudence and Comparative Law* (Egypt Printing Company 1985) 77.
[187] Salama (n 156) 96.

courts.[188] In confirmation of this, royal decrees were issued stating that debts to which the CCL provisions of bankruptcy applied were those arising from the practice of a trade, meaning that debts arising from non-commercial works did not fall within the scope of these provisions.[189] Therefore, Saudi jurisprudence settled on the requirement that debts had to be commercial in order to justify a bankruptcy declaration when the debts were unpaid.[190]

It should be noted that once a debtor was declared bankrupt in Saudi law, all relevant creditors, whether the debts arose from commercial or non-commercial transactions, could participate in bankruptcy proceedings.[191] In other words, only commercial debts could be used to justify the opening of bankruptcy proceedings under the provisions of the CCL. However, once such proceedings were opened, any creditor of a commercial or non-commercial debt could participate in the proceedings. Issues regarding bankruptcy proceedings are addressed in the following subsections.

2.2.3.3 Jurisdiction over Bankruptcy of Non-Merchant Under The Old Regime

As previously explained, the CCL and BPS bankruptcy provisions applied to traders, either individuals or companies, while the cases of non-trader bankruptcy were heard by general courts subject to their interpretation of Islamic rules. As so, it is relevant to outline briefly the rules of bankruptcy from Islamic perspective.

According to the Qur'anic conception, it is not just a breach of legal or contractual obligation not to repay a debt when the debtor has the capacity to do so, but it is also a sin and a violation of the Quranic principles: "*O you who have believed, fulfil [all your] covenants*"[192]. In spite of the great emphasis given by Islamic law on the debtor's obligation to repay debt, Islamic law at the same time encourages the creditor to discharge the debt as a matter of charity, especially if the debtor suffers a financial hardship making it impossible to fulfil the debt. As a Quran verse states: *"But if the debtor is in straitened circumstance, let him have respite until the time*

[188] Almansour (n 134) 234.
[189] For example, Royal Decree No 921/4 of 1983 provides that the bankruptcy provisions provided for in the CCL shall apply to the debtor as long as his debt arose from the exercise of commerce.
[190] Yahya (n 159) 74; Al-Ghamdi and Hosseini (n 99) 26; Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 316.
[191] CCL, art 111.
[192] Quran 5:1.

of ease; and whatever you remit by way of charity is better for you, if only you know"[193]. Also, the settlement between debtor and creditors is strongly encouraged, and the parties are free to formulate the terms of their settlements insofar as such terms do not offend Islamic principle.[194] Of course, creditors are not always willing to settle with their debtors. Therefore, Islamic law has created methods for handling disputes that arise between creditors and the debtor in bankruptcy cases.

A bankruptcy proceeding under Sharia principles is initiated by one or more creditors who have to convince the judge of the validity of their debts and that the debts have become due. A debtor is bound to pay in accordance with his or her agreement and is not allowed to commence a proceeding, based upon insolvency or bankruptcy, to release the debtor from a repayment commitment.[195] Hence, as the majority of Islamic jurists stated, a bankruptcy proceeding under Sharia law is always an 'involuntary' proceeding.[196]

Upon initiation of the proceeding, the judge may find it necessary to issue a preliminary distraint order to prevent the debtor from managing, disposing of, or encumbering assets until the debtor's insolvency status has been determined.[197] If the debtor is determined insolvent, then the final restraint order will be issued.[198] Distraint Orders have four legal effects: (1) the creditors' claims attach to the debtor's assets; (2) the debtor is prevented from administering his or her assets; (3) the creditor who finds his specific actual goods in the possession of the debtor is more entitled than the rest of the creditors for their return.; and (4) the debtor's assets are liquidated to repay the creditors' debts.[199]

Management of bankruptcy affairs is delegated to a trustee appointed by the court.[200] The trustee must allocate and value debtor assets before liquidating them and distributing the

[193] Quran 2:280.
[194] See Awad and Michael (n 43) 990–991.
[195] Michael JT McMillen, 'An Introduction to Shari'ah Considerations in Bankruptcy and Insolvency Contexts and Islamic Finance's First Bankruptcy (East Cameron)' (2011) 4 <https://ssrn.com/abstract=1826246> accessed 5 January 2019.
[196] ibid.
[197] Awad and Michael (n 43) 988–990.
[198] ibid.
[199] Shaikh Muddassir H Siddiqui, 'Insolvency in Shari'ah and Law: A Comparative Study' in Tarek M Hajjiri and Adrian Cohen (eds), *Global Insolvency and Bankruptcy Practice for Sustainable Economic Development* (Palgrave Macmillan, London 2016) 147–179; Awad and Michael (n 43) 988–990.
[200] McMillen (n 195) 5.

proceeds to the creditors.[201] If, after the completion of distribution of debtor assets, a creditor is not paid in full, then the debtor, unless being forgiven by the creditor, would remain obliged legally and morally to repay the unpaid amount when capable of doing so.[202] The lack of discharge of debt under Islamic bankruptcy law is argued to be consonant with the Islamic prohibition of interest late fees.[203] As the debt does not increase over time thanks to the prohibition of interests, the debtor has a lifetime to whittle it down.[204]

In conclusion, three points highlight the main aspects of bankruptcy under Islamic law. First, bankruptcy proceedings, according to the majority of Islamic jurists, are involuntary, which means that the right to initiate such proceedings is granted exclusively to creditors. Second, upon the commencement of bankruptcy proceedings, debtors are prohibited from managing their property, as the rights of creditors attach to such property from the moment the proceedings commence. Third, the distribution of proceeds of the debtor's assets to the creditors does not automatically discharge the debtor from any remaining unpaid debt. Unless discharged by the creditor, the debtor would remain obliged legally and morally to repay the remaining amount of debt whenever capable of doing so.

2.2.4 Procedural Issues of Bankruptcy Under The CCL

This section considers the following issues related to bankruptcy proceedings under the CCL regime: (1) commencement of proceedings, (2) test adopted to determine insolvency of debtor, (3) declaration of bankruptcy, and (4) administration of the bankrupt's business thereafter.

2.2.4.1 Who Has The Right to Seek a Bankruptcy Declaration?

Arab laws have ranged between lenient and rigid on who has the right to initiate bankruptcy proceedings. Some laws, such as Egyptian law, grant the right to establish such proceedings to the debtor, his or her creditors, the court on its own initiative,[205] and, in some cases, the public prosecution authority.[206] In this regard, Saudi law, as embodied in the CCL, is considered rigid,

[201] ibid.
[202] Yousef Al- Shabaily, 'Corporate Insolvency in Islamic Jurisprudence and Law.' (2009) 7 Center for Research and Islamic Studies, Cairo University 303, 332.
[203] Awad and Michael (n 43) 981.
[204] ibid.
[205] This is an exception to the general principle that the courts do not decide on what is not required by one of the litigants or parties involved in the case.
[206] Egyptian Trade Law 1999, art 552. One of the cases in which the Egyptian law permits the courts to declare bankruptcy through their own motions is when the petition of bankruptcy is withdrawn by the creditor who had

limiting the right to institute bankruptcy proceedings to the creditor and debtor only.[207] According to Article 108 of the CCL, 'the bankruptcy declaration shall either be made at the request of the bankrupt directly or at the request of one of its creditors'. Therefore, in contrast to the laws of other Arabic countries, the CCL did not offer a provision that empowered the court or public prosecution to declare bankruptcy through their own motions; the right to seek a bankruptcy declaration was granted exclusively to the debtor and his or her creditors.

2.2.4.2 Bankruptcy Test

Determining whether a debtor is insolvent is a crucial point in bankruptcy procedures.[208]Generally speaking, there are two main tests that are applied to decide whether a person or company is insolvent. The first is known as the cash flow test, and the second is the balance sheet test.[209] Under the cash flow test, debtors, whether individuals or companies, are considered insolvents if they are unable to pay their due debts.[210] This means that the inadequacy of the debtor's available sources to pay the due debts is a sufficient reason to consider such a debtor insolvent. Under the balance sheet test, however, a person or company is insolvent if their liabilities are larger than the value of their assets.[211] This means that the debtor has inadequate assets to discharge their liabilities.[212] It is highly possible for a business to be asset-wealthy and pass the balance sheet test but to be insolvent under the cash flow test. Equally, such a business might fail to pass the balance sheet test because its liabilities are larger than its assets but be able to satisfy the cash flow test, as it has resources to pay its due debts.[213]

Determining the insolvency of individuals or companies was not a straightforward task under Saudi law. The literal interpretation of Article 103 of the CCL applied by Saudi courts meant that they implemented a hybrid balance sheet 'negative equity' and cash flow 'failure to pay' test to determine bankruptcy.[214] A bankruptcy declaration required that the absence of

initiated it. In this case, the court is permitted to declare the bankruptcy on its own motion if it is convinced that all requirements of bankruptcy are met.

[207] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 318.

[208] Goode (n 130) 110–113.

[209] ibid.

[210] Keay and Walton (n 128) 16.

[211] ibid.

[212] ibid.

[213] ibid.

[214] Paul Latto, 'Saudi Arabia's Proposed New Insolvency Law and Commercial Pledge Law | Insights | DLA Piper Global Law Firm' (2016) <https://www.dlapiper.com/en/dubai/insights/publications/2016/03/saudi-arabia-new-insolvency-law/> accessed 23 January 2019.

sufficient assets was the reason for the default on due debts.[215] This meant that both cash flow and balance sheet tests had to be satisfied to establish the insolvency of individuals and companies.

The application of this requirement was often problematic, as it required an assessment of the debtor's financial position and an assurance that sufficient assets were not available to meet the debt. This test has been criticised because it required creditors to initiate lengthy and complex procedures in order to verify the financial position of the debtor.[216] To facilitate bankruptcy proceedings, proposals were made to adopt a 'cash flow' test of bankruptcy when the failure of the debtor to pay due debts is a sufficient reason to declare bankruptcy, without regard to the debtor's financial position or assets.[217]

The hybrid test is no longer applied under the BL 2018. Passing either cash flow test or balance sheet test is sufficient to apply for any one of the three main procedures under the new regime (Preventive Settlement, Financial Restructuring, and Liquidation).[218] More details about the new regime are found in the following chapter.

2.2.4.3 Declaration of Bankruptcy and The Administration of The Bankrupt's Affairs

Following the declaration of bankruptcy of the debtor, the bankruptcy decision shall be advertised by the court, including publication of the decision in the *Official Gazette* to inform the debtor's creditors.[219] Moreover, criminal actions and imprisonment may apply to debtors who have acted negligently or fraudulently.[220] In addition, the declaration of bankruptcy results in depriving the bankrupts from certain rights. For example, those who have been declared bankrupt are ineligible to serve in local councils or to be members in chambers of commerce.[221] In order to regain those rights, the bankrupt must repay all debts and fulfil the penalty imposed if any.[222]

---

[215] Salama (n 156) 92.
[216] Euler Hermes, 'Collection Profile: Saudia Arabia' (2017) 7 <https://www.eulerhermes.com/content/dam/onemarketing/ehndbx/eulerhermes_com/en_gl/erd/collection/Saudi_Arabia.pdf> accessed 23 January 2019.
[217] See Altabtabai (n 93) 55.
[218] BL 2018, arts 13, 42, 92.
[219] CCL, art 111.
[220] CCL, arts 136-137.
[221] Municipalities and Villages Law 1977, art 11 and Law of Chamber of Commerce and Industry 1980, art 4.
[222] CCL, art 132 and 133.

After the bankruptcy of the debtor is declared by the court, the bankruptcy procedures are carried out by court appointees, who determine the bankrupt's debts and assets. This information is presented to the creditors in order to decide the fate of the bankrupt and his or her assets, i.e., whether they will be sold at auction with the proceeds distributed among the creditors, in proportion to the debt owed, or by reconciling with the bankrupt.[223]

Displacing the bankrupt from the management of his or her business after the bankruptcy declaration was one of the major consequences of bankruptcy under the CCL. In accordance with Article 110 of the CCL, after a bankruptcy was declared by the court, the bankrupt party was prohibited from managing his or her business and any action taken contrary to this Article was deemed void.[224] The authority to administrate and supervise the bankrupt's affairs was assigned to a council formed by the secretary, who was appointed by the court, and two members nominated by the creditors.[225] The assets of the debtor, as well as the debts owed to and by him or her, were presented to the court by the authorised council. Then, following the court order, all assets of the debtor were sold at auction and all debts owed to him or her were collected by the council.[226]

Finally, the proceeds from sale of the debtor's assets were distributed to creditors in accordance with the *pari passu* principle.[227] Debts, such as those due to housing rent, employee payroll, claims, and mortgage payments, were considered preferential debts and had priority over those of other unsecured creditors.[228] By completing the distribution of the debtor's assets among the creditors, the bankruptcy automatically ended. However, unlike the case in the United States and the United Kingdom, there was no possibility of discharge of unpaid debts after the bankruptcy procedure ended under the CCL. This meant that if a creditor had not been fully paid after the distribution of proceeds, that creditor had the right to litigate against the debtor and claim the unpaid part of the debt whenever the debtor acquired sufficient funds.[229]

[223] Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 332.
[224] CCL, art 110.
[225] CCL, art 112.
[226] CCL, arts 113 and 114.
[227] CCL, art 122.
[228] CCL, arts 119 and 121.
[229] CCL, art 130.

2.3 Bankruptcy Preventive Settlement Law 1996

Because of the harsh nature of bankruptcy under the provisions of the CCL and its dire consequences on debtors, it was necessary to provide a formal mechanism for avoiding bankruptcy.[230] Such a necessity derived from the fact that facing financial difficulties and defaulting on debts was mostly, to some degree, inevitable and normal, even for high-profile firms in Saudi market.[231] Therefore, to respond to such a necessity, the BPS was issued in 1996. The BPS applied to every merchant,[232] whether an individual or company, who suffered from financial difficulties and feared the imminence of insolvency.[233] It provided the debtor with two options. At the first stage, it allowed the debtor to reach an amicable conciliation with his or her creditors in order to avoid bankruptcy under the supervision of the Conciliation Committee at the Ministry of Commerce and Industry.[234] If an amicable conciliation was unsuccessful or the debtor did not consider it an advantageous choice, then the debtor could apply to the Commercial Court to request a bankruptcy preventive decision.[235] It is worth mentioning that only debtors could request a settlement process under this law.[236] In contrast, under the CCL, creditors and debtors could initiate bankruptcy proceedings.[237] This part addresses BPS in regard to conditions for applying for settlement under this regime, formation of a settlement request, managing the debtor's business after the opening of the settlement procedure, moratorium or automatic stay on creditors' actions, and the requirements for approving the settlement plan.

2.3.1 Conditions for Applying the BPS

Article 1 BPS, as well as Article 5 of its Implementation Regulations, provided detailed conditions for obtaining a settlement. According to Article 1, the right to seek a preventive settlement was granted to 'every merchant—individual or company—whose financial situations have been distressed in the manner according to which the cessation of paying debts

[230] Abdulrahman Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (Imam Mohammad Bin Saud Islamic University 2010) 3.
[231] ibid 5.
[232] Since bankruptcy, according to the provisions of the CCL, applies only to merchants, it is logical to conclude that the bankruptcy preventive settlement law application scope is limited to merchants as well. See Zaynab Salama, 'Bankruptcy Preventative Settlement in Saudi Law' (1997) 36 Public Administration Journal 347, 353.
[233] BPS, art 1.
[234] BPS, art 1.
[235] BPS, art 2.
[236] BPS, art 1.
[237] CCL, art 108.

is feared'.[238] Article 5 of the Implementation Regulations listed more detailed conditions for a debtor seeking a settlement. For example, it required a merchant to act in good faith and to have performed commercial activities for at least 3 years.[239] Accordingly, this section addresses three main requirements for application of the BPS: three years' performance in commerce, acting in good faith, and disturbance in the financial situation of the merchant.

2.3.1.1 Three Years' Performance in Commerce for Settlement Application

The Saudi legislators followed other legislators in neighbouring countries in requiring that the merchant petitioning for settlement should have exercised trade for a specified period of time.[240] Article 5 of the Implementation Regulations stated that a debtor who filed for settlement should have been trading for a period of not less than three years.[241]

It is thought that by imposing such a requirement, the legislators intended to exclude companies that were incompetent to conduct regular business practices for a sustained period in the competitive trade market.[242] Hence, the BPS served exclusively businesses that had experienced the misfortunes and distress of trade for at least three years.[243] However, it seems that this justification was based on the presumption that the incompetence of the new company to conduct business was the sole reason such the business had encountered financial difficulties. Such presumption may not always be correct; the business failure may have been caused by different, possibly external, factors, such as changing markets and economic conditions or any cause not related to the administrative capabilities of the debtor.[244]

The requirement of three years has been criticised by Salama as she argues that when a new company was deprived of the right to seek formal settlement in accordance with BPS

[238] BPS, art 1.
[239] Implementation Regulations of BPS, art 5.
[240] In the UAE, preventive settlement was available for any trader provided he or she has traded continuously for one year before the submission of the settlement application. Article 833 of UAE Federal Law No 18 of 1993, see Latham & Watkins, 'Restructuring and Insolvency in the United Arab Emirates' (2011) <https://www.lw.com/upload/pubContent/_pdf/pub2881_1.pdf> accessed 12 February 2019; Ross and Adams (n 90) 15. In addition, Article 726(1) of Egyptian Commercial Law No 17 of 1999 states that: 'The petition for bankruptcy composition shall not be accepted unless the petitioner has exercised trade continuously during the two years prior to submitting the petition'.
[241] Implementation Regulations of BPS, art 5.
[242] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 15.
[243] ibid.
[244] See Vanessa Finch and David Milman, *Corporate Insolvency Law: Perspectives and Principles* (3rd edn, Cambridge University Press 2017) 131–135; Jim Everett and John Watson, 'Small Business Failure and External Risk Factors' (1998) 11 Small Business Economics 371.

provisions, such a company may be encouraged to take its own path to avoid the risk of bankruptcy.[245] Such a path may include concealing the truth about the company's financial distress from its creditors and incurring new debts in the false hope of survival until the situation becomes worse and it is too late for the business to be rescued, the result of which is not in the best interests of either the company or its creditors.[246] Interestingly, while in the United Kingdom the displacement of management resulting from the issuing of an administration order is argued to discourage directors from the early filing of rescue procedures,[247] the issue of such encouragement seems to have been a luxury for new Saudi companies that had not met the requirement of three years' performance of trade, as these companies were not only discouraged from the early filing of rescue procedures but also denied the right to file for a rescue procedure at all.

It should be noted that the three years requirement was abolished under the BL 2018, which has replaced the BPS. The abolition of such a requirement may indicate the willingness of Saudi legislators to enhance the availability of rescue procedures for distressed businesses. Issues regarding restructuring procedures under the BL 2018 are addressed later in this thesis.

2.3.1.2 Conducting Business in Good Faith

A bankruptcy settlement, in accordance with the BPS, was considered an advantage that should be granted exclusively to a good-faith merchant.[248] It is argued that the requirement of good faith in a merchant seeking a settlement was intended to prevent misuse of a settlement in the manner of fraud or evasion of obligations by the debtor.[249] With this in mind, it is logical to ask what constitutes good faith.

The requirement of good faith stipulates that the exercise of trade shall be taken with credibility and integrity and in accordance with the laws and customs of trade.[250] Accordingly, any act involving fraud or deceit or any serious violation of the laws and customs of trade would lead

[245] Salama (n 232) 355–356.
[246] ibid.
[247] See Gerard McCormack, 'Control and Corporate Rescue–an Anglo-American Evaluation' (2007) 56 International & Comparative Law Quarterly 515, 528.
[248] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 17.
[249] Salama (n 232) 362.
[250] Article 5 of the Implementation Regulations of BPS provides that a merchant shall be deemed to have good faith if he or she has credibility and integrity. The article states that such credibility is evident from the merchant's commitment to carry out the duties imposed by commercial laws and commercial practice.

to merchants being denied the right to apply for bankruptcy preventive settlement.[251] Article 5 of the Implementation Regulations provided examples of actions considered by the law to be indicative of a trader acting in bad faith.[252] These actions included failure to keep commercial books, issuance of a bad cheque, and concealment or disposal of any trader assets with the intention of harming creditors.[253]It should be noted that the issue of good faith in BPS was based on the facts, and the courts had discretionary power, on a case-by-case basis, to decide whether a conduct of the debtor was contrary to good faith or not.[254]

2.3.1.3 Disturbance in The Financial Situation of The Merchant

Article 1 BPS required that for a bankruptcy preventive settlement application to be accepted, the merchant's financial position had to be distressed in a manner that he or she feared being unable to pay his or her debts. It seems that the law required a merchant to be in constant vigilance of his or her financial viability, and to initiate a request for settlement at the first sign of financial disturbance and not wait for his or her financial situation to worsen to a point where the debts could not be paid and the business was irrecoverable.[255] Accordingly, a minor financial disturbance was not a justification for a settlement request; such a disturbance had to be severe to the degree that cessation of paying debts was feared. Requiring such a level of severity was considered by some scholars as a means of preventing a settlement from being sought by debtors as a first remedy to financial difficulties, instead of trying to rehabilitate their financial position.[256] Therefore, to be able to file for settlement under the BPS, the financial position of the debtor had to be mid-range. In other words, the disturbance to the debtor's financial situation could not be minor in a way that cessation of debt payment was not feared, but at the same time could not be too severe in a way that the debtor could not pay the due debt at all.

This requirement could be problematic when it applied to debtors who passed the cash flow insolvency test but did not pass the balance sheet test, as their assets were greater than their liabilities. These debtors, as noted previously, could not be declared bankrupt under the

[251] Aziz Aloqily, 'Bankruptcy Preventive Settlement' (1984) 8 The Journal of Law – Kuwait University 11, 21.
[252] Implementation Regulations of BPS, art 5.
[253] Implementation Regulations of BPS, art 5.
[254] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 18; Salama (n 232) 364; Aloqily (n 251) 12.
[255] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 19.
[256] See Mohsen Shafiq, *Eygption Commercial Law* (1st edn, Dar Nashr Althaqafah 1951) 885; Salama (n 232) 358; Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 19.

provisions of the CCL, which required them to pass both its insolvency tests.[257] These debtors also were not entitled to commence a settlement procedure under the provisions of the BPS, as ceasing to pay debts made it too late to apply for settlement.[258] Therefore, there was a legislative gap in this case, as neither of the two sets of bankruptcy legislation applied to the debtor in question, which indicates a legislative failure. Depriving the debtor who stopped paying debts from the right to apply for preventative settlement might be acceptable if the failure to pay due debts was considered grounds to declare the bankruptcy of the debtor. If that were the case, then it could be argued that by failing to pay due debts, the debtor was at the stage of bankruptcy and then it was too late to seek settlement.[259] However, as ceasing to pay due debts was not considered a ground (on its own) to declare bankruptcy under the CCL, such cessation should have at least entitled the debtor to apply for settlement under the provisions of the BPS.

2.3.2 Formation of a Settlement Request

For a settlement to be granted, several obligations had to be fulfilled by the debtor. Article 2 BPS requires the debtor to document, in the petition, the reasons for the disturbance of his or her financial position, the terms of the settlement that he or she proposed, and the means of implementation, if any. In addition, the debtor should provide the following:

> (A) A detailed statement of its movable and immovable property[260] and their book values when the settlement is requested.
> (B) The names of creditors and debtors, their addresses, the amount of their rights and debts, and the securities, if any.
> (C) An acknowledgment by the merchant that no previously granted settlements were being implemented.
> (D) Permission to request the settlement granted by the majority of the partners if the debtor is a General Partnership or a Limited Partnership; or by the ordinary general assembly in the other kind of companies.
> (E) Any other documents specified by the Implementation Regulations.

[257] Almansour (n 134) ch 4.
[258] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 19.
[259] Even in some countries where the passing cash flow test was a ground to declare bankruptcy, it was still permissible for a debtor who stops paying his due debts to file for settlement. See UAE Federal Law No 18 of 1993, art 831 and Egyptian Commercial Law No 17 of 1999, art 725(2).
[260] In civil law jurisdictions, property is divided into movable and immovable, and these two terms are roughly equivalent to the common law distinction between personal property and real property. David S Clark and Tuğrul Ansay, *Introduction to the Law of the United States* (2nd edn, Kluwer Law International 2002) 217.

After submission of a settlement request, the court reviewed the request to ensure that it followed the guidelines provided by the BPS and its Implementation Regulations.[261] If the court was satisfied that all requirements had been met, then the court opened the settlement procedure and appointed one of its judges to supervise the settlement process.[262] In addition, a trustee was appointed to assist in managing this process.[263]

2.3.3 Managing The Debtor's Business After The Opening of The Settlement Procedure

One of the tasks assigned to an appointed trustee was to supervise the debtor's affairs during the settlement process.[264] However, not all actions were at the same level of importance, and thus, not all of them were subject to the supervision of the trustee. The law distinguished between two types of debtors' actions: usual actions that were necessary for business; and unusual actions, such as making a pledge, posting bail, donating property, or engaging in any property-related conduct not required in ordinary business.[265] Although the debtor was free to conduct usual actions without seeking permission from the trustee, engaging in unusual action was not permitted unless authorisation was obtained from the settlement judge.[266]

It is believed that the reason for imposing restrictions on certain types of debtor actions was to protect the interests of creditors who might be harmed by these actions.[267] Such restrictions were also intended to prevent the debtor from dissipating assets by engaging in false contracts with third parties, such behaviour conflicting with the good faith required for obtaining a preventive settlement.[268] Determining whether an action taken by the debtor was usual or not was a matter of discretion applied by the courts on a case-by-case basis.[269]

[261] BPS, art 3.
[262] BPS, art 3.
[263] BPS, art 3.
[264] BPS, art 5.
[265] BPS, art 5.
[266] BPS, art 5.
[267] Salama (n 232) 373.
[268] ibid.
[269] ibid.

2.3.4 Moratorium or Automatic Stay on Creditors' Actions

A moratorium or automatic stay is considered a fundamental tool of protection for companies during rescue procedures.[270] As soon as the rescue procedure commences, the moratorium provides a distressed company with 'breathing space' from its creditors, as it stops all proceedings brought against the company or its assets.[271] The aim of a moratorium is to protect a company for a period of time, within which it could resolve its financial problems without interference from creditors.[272]

The importance of a moratorium in corporate rescue procedures was recognised by Saudi legislators, as Article 11 BPS stated that as soon as the settlement procedure was opened, any proceedings commenced against the debtor should be suspended. Claims that had been commenced prior to the opening of the settlement procedure were also subject to suspension.[273] However, claims brought against the debtor's partners and his or her guarantors were not subject to suspension or a stay.[274] Therefore, the creditors were permitted to commence proceedings against the debtor's partner and its guarantor, as they were not protected by the provisions of the moratorium.

The scope of a moratorium in Article 11 BPS was limited, because it covered only claims brought against the debtor by unsecured creditors who were bound by the settlement, even if they did not participate in the procedure or voted against it.[275] Moreover, the moratorium did not apply to creditors whose debts were created after the opening of the settlement procedure, as the settlement did not apply to such debts.[276] Therefore, creditors whose debts were created after the opening of the procedure and secured creditors[277] were not prevented from enforcing their securities or contractual rights against the debtor during the settlement procedure.

---

[270] Vernon Dennis and Alexander Fox, *The New Law of Insolvency: Insolvency Act 1986 to Enterprise Act 2002* (Law Society 2003) 160.
[271] Gerard McCormack, *Corporate Rescue Law: An Anglo-American Perspective* (Edward Elgar 2008) 156.
[272] Keay and Walton (n 128) 97.
[273] BPS, art 11.
[274] BPS, art 11.
[275] Implementation Regulation, art 19.
[276] BPS, art 9.
[277] In contrast, a secured creditor is affected by moratorium in UK administration and automatic stay in the US Chapter 11. See Schedule B1, para 43(2) of the UK Insolvency Act 1986 and Section 362(a) of the US Bankruptcy Code. The scope of moratorium under these two regimes is addressed in more detail in Chapter 6 of this thesis.

Excluding claims of secured creditors from the scope of a moratorium under the BPS regime provided inadequate protection for a company undergoing BPS procedure. Preventing the enforcement of security interests during a moratorium may be critical to facilitating the reorganisation of the debtor company.[278] For example, the property subject to security interests might be necessary for the company to continue its business operations throughout the reorganisation process.[279] Allowing the enforcement of security interests over such property may disrupt the business and, therefore, undermine the prospective reorganisation.[280] Therefore, it could be concluded that the tight ambit of a BPS moratorium failed to facilitate the achievement of the ultimate aim of the regime, which was to help viable and distressed businesses avoid bankruptcy.

2.3.5 The Requirements For Approving The Settlement Plan

A meeting was held by the settlement judge, trustee, debtor, and creditors to determine the validity and amount of each debt and to discuss the terms of the settlement plan proposed by the debtor.[281] The settlement plan could include fixing debt instalments, postponement of due dates, and/or discharge of a portion thereof.[282] It could also include the selection of new management of the distressed company.[283] It should be noted that the right to vote on a settlement plan was granted only to unsecured creditors whose debts—whether commercial or non-commercial—arose prior to the decision to open the settlement proceedings.[284]The settlement plan was binding if it was approved by a majority of the creditors representing two-thirds in value of the undisputed debts.[285] However, final approval by the court was required for the settlement plan to be enforced.[286]

2.4 Shortcomings of The Old Law and The Need For Reforms

Investigating the bankruptcy regime under the old law clarifies why such a regime was not commonly used by defaulting companies. Indeed, the bankruptcy regime was perceived by

[278] Thomas H Jackson, *The Logic and Limits of Bankruptcy Law* (Beard Books 2001) 181.
[279] Charles Jordan Tabb, *Law of Bankruptcy* (4th edn, West Academic Publishing 2016) 252.
[280] ibid.
[281] Implementation Regulations, art 15.
[282] BPS, art 8.
[283] BPS, art 8.
[284] Implementation Regulations, art 15.
[285] BPS, art 7.
[286] Implementation Regulations, art 15(5).

many scholars as complex and uncertain,[287] which led the kingdom to be ranked at the bottom of the Resolving Insolvency Rank provided by the World Bank in 2018.[288] Perhaps the main reasons for the criticisms of the old regime were its limited scope of application, the uncertainty surrounding its procedures, and its lack of a rescue culture.

The limited range of application was one of the main shortcomings of the old bankruptcy system, which applied exclusively to merchants. The problem of this limitation of application was more obvious in the case of corporate bankruptcy. Under the old regime, a company acquires commercial status, thus becomes subject to bankruptcy rules in CCL and BPS, only if it was established to conduct one of the commercial activities identified in Article 2 of CCL. Consequently, the rules of bankruptcy were not applicable to a number of companies with large capital and employees, only for the reason that activities undertaken by these firms were not considered commercial activities according to the limited list of commercial transactions provided in Article 2 of CCL.[289] Excluding these firms from the scope of the bankruptcy regime was criticised by scholars who argued that such exclusion is at odds with the uniformity of corporate rules.[290] The scholars state that in order to ensure such uniformity of rules governing companies, Saudi legislators ought to follow the Egyptian law, which adopts the 'formal standard', where all companies are subject to bankruptcy regime regardless of whether the activities undertaken by these companies are considered commercial or not.[291] Some scholars went further, proposing that the application of bankruptcy law should not be limited to merchants or commercial activities only.[292] In their views, the distinction between commercial and non-commercial activities in most cases is difficult to determine, due to the complexity of business transactions and because the list provided by the law is limited and falls short in keeping up with such complexity.[293] Moreover, the bankruptcy practices of the United Kingdom and the United States were provided as well-developed models to be followed in this

[287] Latto (n 214) 3.
[288] World Bank, 'Resolving Insolvency - Doing Business - World Bank Group' <http://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency> accessed 19 March 2019. It is worth noting that the World Bank has now discontinued the Doing Business rankings. See 'World Bank Group to Discontinue Doing Business Report ' <https://www.worldbank.org/en/news/statement/2021/09/16/world-bank-group-to-discontinue-doing-business-report> accessed 10 December 2021.
[289] Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135.
[290] Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135.
[291] Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135.
[292] Yousry Abu Saada, 'Bankruptcy' (Al Azhar University 1985) 20.
[293] ibid.

regard, as the application of bankruptcy or insolvency rules in these jurisdictions is not confined to traders only.[294]

Remarkably, the importance of distinguishing between merchant and non-merchant as a trigger for the application of bankruptcy law has been largely abandoned in the new Saudi BL 2018, which applies to any individual or company undertaking activities aimed at gaining profits, regardless of whether these activities are considered commercial or not, according to Article 2 CCL.[295]

In addition, the absence of a rescue culture was another defect in the Saudi bankruptcy regime because liquidation was the only procedure regulated by the CCL, the main bankruptcy code in the kingdom.[296] The BPS represented the first effort by Saudi lawmakers to provide a rescue mechanism for distressed business. However, such a law did not meet the expectations of the market because its application involved wide interference from the court in managing debtors' affairs.[297] Such intervention was not usually welcomed by either debtors or creditors, as it could increase the level of complexity and time of the procedure.[298]

The limited scope of the moratorium provided in the BPS might be another reason why the rescue option provided by this law was rarely used.[299] The moratorium scope in the Saudi BPS was limited to claims brought by unsecured creditors who were bound by the settlement.[300] This meant that the provisions of a moratorium in the BPS did not prevent secured creditors and other third parties from enforcing their securities or contractual rights.[301]

Other barriers that could prevent parties from relying on bankruptcy law to resolve their disputes were the uncertainty and inconsistency surrounding the application of regulations by the courts.[302] This may result from the fact that, under the old law, most of the basic questions which bankruptcy laws aimed to address were not answered clearly.[303] Therefore, because of

[294] ibid.
[295] BL 2018, art 4.
[296] Elshurafa (n 18) 305.
[297] Euler Hermes (n 216) 7.
[298] ibid; Latto (n 214) 3.
[299] Karaman, *Bankruptcy Preventative Settlement in Saudi Law* (n 230) 24.
[300] ibid.
[301] ibid.
[302] Gross (n 37).
[303] Latto (n 214) 3.

the lack of legislative guidance, the application of bankruptcy provisions under the old regime relied heavily on judges' discretion.[304] Indeed, it was difficult to predict the outcomes of exercising this type of wide discretion, which may explain why relying on the old law was not a favourable option for resolving bankruptcy disputes.[305]

The lack of a comprehensive and transparent corporate rescue regime in the Kingdom made reliance on the judiciary to resolve restructuring cases an unpopular choice, especially for foreign companies.[306] Due to the lack of sufficient provisions within BPS 1996, the outcome of restructuring cases, if any, relied on the court's discretion, which was usually unpredictable.[307] In regard to this situation, the Commercial Law Development Program (CLDP) of the U.S. Department of Commerce states: 'Prior to the passing of the new law [BL 2018], bankruptcy had presented a significant legal risk for U.S. companies and investors doing business in Saudi Arabia as the legal framework lacked transparency and predictability for creditors interested in investing in Saudi companies'.[308]

Therefore, limited scope of application, the absence of a rescue culture, and uncertainty about the bankruptcy proceedings caused by inadequate legislative guidance were considered the main defects of the Saudi bankruptcy regime. Such factors have resulted in formal court proceedings not being the preferred option for disputing parties seeking resolution.

In 2016, Saudi Arabia announced its Vision 2030, which aims at lowering the kingdom's dependency on oil as the main way of attracting foreign investment and creating more jobs for Saudi citizens.[309] To achieve such goals, lawmakers have already made remarkable steps towards amending and replacing numerous outdated commercial acts and towards introducing

[304] Gross (n 37).
[305] See World Bank, 'Survey on Insolvency Systems in the Middle East and North Africa' (2009) ch 14 <https://bit.ly/31coiQM> accessed 23 January 2019; Elshurafa (n 18) 301.
[306] See Elshurafa (n 18) 306.
[307] Reem Gasir and Mariam Al-Alami, 'Saudi Arabia Set to Welcome New Insolvency Law' [2016] Emerging Markets Restructuring Journal 15, 15.
[308] 'Saudi Arabia: CLDP Partners with Saudi Bankruptcy Commission in First Bankruptcy Conference | Commercial Law Development Program' <https://cldp.doc.gov/programs/cldp-in-action/saudi-arabia-cldp-partners-saudi-bankruptcy-commission-in-first-bankruptcy> accessed 18 December 2021. See also US-Saudi Arabian Business Council, 'Saudi Arabia's New Bankruptcy Law' (2018) 3–4 <https://ussaudi.org/wp-content/uploads/2019/09/November-2018.pdf> accessed 19 November 2019.
[309] 'Saudi Arabia Vision 2030 Homepage - Vision 2030' (n 23).

more effective and robust laws that offer investors the necessary level of protection.[310] Perhaps one of the remarkable changes in the Saudi commercial law area is the introduction of the first comprehensive bankruptcy law, which was enacted in February 2018. The law was introduced as a result of benchmarking conducted by the Saudi Ministry of Commerce and Industry with many high-ranking insolvency regimes, such as the United Kingdom and the United States.[311]An overview of the new bankruptcy regime in the kingdom is provided in the next chapter.

2.5 Conclusion

This chapter provides a historical background of Saudi bankruptcy law. Bankruptcy cases prior to the enactment of the new BL 2018 were subject to the application of two pieces of legislation: the CCL and the BPS. The application of bankruptcy rules was limited to merchants and entirely overlooked non-merchants, such as consumer debtors. The old regime was criticised for many reasons: mainly, its limited range of application, the absence of an adequate formal rescue procedure, and the uncertainty surrounding its application thanks to the lack of comprehensive legislative guidance. Such defects led the old bankruptcy regime to be rarely used, as it did not meet the expectations of the market. In 2016, the kingdom announced it Vision 2030, which proposes to diversify the economic sources of the state and to lower its dependence on oil. Such diversity includes attracting foreign investment. In order to ensure this goal, it is necessary to modernise the laws governing commercial activities and to provide a robust and clear legal structure and protection to make the national environment more welcoming. One of the landmark changes in Saudi commercial law is the enactment of BL 2018. The following chapter provides an overview of this new law and illustrates the main restructuring procedures provided to the troubled debtor under it.

[310]'Saudi Bankruptcy Law to Aid Struggling Businesses' <https://www.thenationalnews.com/business/economy/saudi-bankruptcy-law-to-aid-struggling-businesses-1.761538> accessed 12 September 2021.
[311] Ministiry of Commerce and Industry (n 25) 3.

Chapter 3: Overview of Saudi Bankruptcy Law 2018

This chapter provides an overview of the new bankruptcy law in the Kingdom of Saudi Arabia, including the objectives of the law, the scope of its application and the mechanism of its restructuring procedures. This general overview of the law provides the necessary foundation for theoretical and practical discussions provided in subsequent chapters. Accordingly, the chapter is divided into four parts aiming to answer the following questions: Why was it necessary to modernise bankruptcy law in the Kingdom (Part 1)? What are the main objectives of BL 2018 (Part 2)? To whom does BL 2018 apply (Part 3)? What are the restructuring procedures available under BL 2018 and how do they function (Part 4)?

3.1 The Need to Modernise Bankruptcy Law in Saudi Arabia

Bankruptcy provisions were first introduced in the Kingdom through the Commercial Court Law (CCL) of 1931. The bankruptcy provisions in that law were derived from the legal systems of that period, when bankruptcy was considered a stigma on debtors who had defaulted on their due debts. As reflected in those laws, bankruptcy was considered a threat to the stability of business life, necessitating harsh treatment for bankrupt debtors, whose fate was often at the mercy of their creditors, who had the ultimate power to liquidate the bankrupt debtors' assets.[312] The bankruptcy provisions under CCL 1931 were not designed to consider the economic and financial factors that led to the failure of the businesses that went bankrupt, nor were they designed to rescue distressed businesses that would have been able to restore their financial stability if they had received legal support.[313]

However, with the economic and financial growth the Kingdom had been experiencing, Saudi legislators recognised the need to establish rules that could help honest but unfortunate debtors get back on their feet and, thus, contribute to national economic growth. The legislators took note that some companies in the Kingdom had encountered financial difficulties that had led to the disruption of their businesses, and as a result, several had stopped paying their financial obligations, which negatively affected the country's economy.[314] This led to the late recognition of the significant role corporate rescue procedures could play in national economic development, which paved the way for the enactment of the Bankruptcy Preventative

[312] Abdulrahman Karaman, *Commercial Papers and Bankruptcy Procedures* (Dar Alejadh 2019) 283.
[313] ibid.
[314] See the Explanatory Note to the Bankruptcy Preventative Settlement Law (BPS) 1996, para 1.

Settlement (BPS) Law in 1996, the passage of which represented the first step toward providing formal rescue procedures for distressed businesses.

However, as discussed in chapter 2, this law was not commonly applied in practice due to its complexity and its limited content. Under the brief BPS provisions, which were presented in only 16 articles, many basic questions which restructuring laws aimed to address were not addressed clearly.[315] Due to the lack of sufficient provisions within BPS 1996, the outcome of restructuring cases, if any, relied on the court's discretion, which was usually unpredictable.[316]The limited content of the BPS 1996 and its other shortcomings discussed in the last chapter were highlighted by scholars who advocated for a radical change in the Kingdom's bankruptcy system, calling for legislators to enact laws based on leading modern international insolvency practices.[317]

Since the announcement of its ambitious Vision 2030 in April 2016, the Kingdom has been striving to create new opportunities for investment and build an economic and legal environment able to attract foreign capital. Indeed, foreign direct investment (FDI) is expected to play a principal role in helping some of the ambitious policies of Vision 2030 come to fruition. However, Saudi Arabia's FDI has been steadily decreasing over the last few years, as inward FDI flows have shrunk from $8.1 billion in 2015 to $1.4 billion in 2017.[318]Although the inward FDI flows to Saudi Arabia began to increase in 2018, rising to $3.2 billion,[319]that amount is still significantly lower than the FDI 2008 peak of $39 billion.[320] It is important to note that most of the inflows that contributed to the exceptional 2008 peak for inward FDI were directed to the oil-based petrochemical and refining industry.[321]Therefore, the subsequent decline has been a normal result of lower oil prices.[322] However, FDI has been identified as a critical player in achieving the aim of the 2030 Vision to diversify the Kingdom's economy away from oil revenues, so many efforts have been made recently to increase the Kingdom's

[315] See Wasim Al-Ahmad, *The New Saudi Bankruptcy Law* (Law and Economics 2019) 34.
[316] Gasir and Mariam Al-Alami (n 307) 15.
[317] See Al-Ahmad (n 315) 34–43.
[318] United Nations Conference on Trade and Development, *World Investment Report. 2018, Investment and New Industrial Policies* (United Nations 2018) 48.
[319] United Nations Conference on Trade and Development, *World Investment Report. 2019, Special Economic Zones* (United Nations 2019) 44.
[320] United Nations Conference on Trade and Development, *World Investment Report. 2009, Transnational Corporations, Agricultural Production and Development* (United Nations 2009) 57.
[321] ibid.
[322] United Nations Conference on Trade and Development, *World Investment Report. 2019, Special Economic Zones* (n 319) 44.

inward FDI flows outside the oil and gas sector. One of these efforts, for example, was a resolution issued by the Saudi Council of Ministers in October 2018 allowing 100% foreign ownership in road transport, recruitment and employment, audio-visual and real estate brokerage services.[323]

In order to be effective, incentives to attract FDI must be supported by clear and practicable legal frameworks. Accordingly, the Kingdom has been updating many of its business laws and regulations, the bankruptcy law being one of the most important that the Saudi government has sought to modernise. The government found it necessary to establish a bankruptcy law with consideration of recent experiences in developed jurisdictions and in line with recommendations made by concerned international organisations, such as the World Bank and UNCITRAL.[324] Having a reliable and functional insolvency law is acknowledged as a significant factor in gaining investors' confidence in the business environment of a state.[325] This is emphasised by the World Bank 'Doing Business' reports that consider resolving insolvency as one of the 10 crucial factors in determining a country's ranking regarding the ease of doing business.[326] Therefore, modernising the Saudi bankruptcy regime was deemed necessary to improve the Kingdom's ranking in the World Bank 'Ease of Doing Business' report, as it was ranked 94th out of 190 on the general ranking and 169th on the Resolving Insolvency indicator in 2017.[327]

In September 2016, the Saudi Arabian Ministry of Commerce (MOC) announced plans to enact a new bankruptcy law and published a draft of the proposed law, which followed its March 2015 publication of a policy paper that drew the broad skeleton of the suggested bankruptcy law. Then, on 23 February 2018, the long-awaited new Bankruptcy Law (BL) was published in the *Official Gazette* and went into effect on 14 August 2018. This new law, BL 2018, replaced the outdated bankruptcy provisions embedded within CCL 1931 and BPS 1996 and

[323] Council of Ministers Resolution No. 939 dated 22/10/2018.
[324] Ministiry of Commerce and Industry (n 25) 3.
[325] See Chris Umfreville and others, 'Recognition of UK Insolvency Proceedings Post-Brexit: The Impact of a "No Deal" Scenario' (2018) 27 Int Insolv Rev 422, 423.
[326] See 'Doing Business' <https://www.doingbusiness.org/> accessed 19 November 2019. Professor McCormack is sceptical about the accuracy of the World Bank reports on doing business (DB). He argues that the DB project appears to assume that if certain legal reforms are enacted, the intended economic consequences will more or less automatically follow. He adds that the DB project seems to somewhat overestimate the closeness of the connection between laws and economic outputs in the 'real' world. See Gerard McCormack, 'World Bank Doing Business Project: Should Insolvency Lawyers Take It Seriously?' (2015) 28 Insolv Intell 119; Gerard McCormack, 'Why "Doing Business" with the World Bank May Be Bad for You' (2018) 19 Eur Bus Org Law Rev 649.
[327] 'Doing Business 2017' <https://www.doingbusiness.org/en/reports/global-reports/doing-business-2017> accessed 19 November 2019.

has become the Kingdom's only comprehensive framework governing bankruptcy and insolvency for individuals and businesses. The new BL 2018 contains 17 chapters with 231 articles governing three main procedures, which are Preventative Settlement, Financial Restructuring and Liquidation. Additionally, the law provides for special and simplified bankruptcy procedures applicable to small businesses.

3.2 Objectives of the Kingdom of Saudi Arabia's Bankruptcy Law 2018

It is not common for Saudi laws and regulations to identify the statutory objectives they are designed to achieve. Identifying such objectives has typically been left to lawyers when discussing theoretical or practical issues associated with the laws and regulations in question. However, contrary to these common practices, Article 5 of the Kingdom's BL 2018 sets forth the statutory objectives of the insolvency proceedings contained therein. Article 5 states that bankruptcy procedures shall aim to:

> (a) enable a debtor who is bankrupt, distressed, or is likely to suffer financial difficulties to benefit from the bankruptcy procedures, restructure his financial position, resume his business, and contribute to economic development;
>
> (b) protect creditors' rights in a manner that ensures fair treatment;
>
> (c) maximize the value of bankruptcy assets, conduct proper procedures for the sale thereof, and ensure fair distribution of sale proceeds among creditors upon liquidation;
>
> (d) reduce the costs and duration of procedures and increase their efficiency, especially in restructuring the financial position of small debtors, or the sale of bankruptcy assets, and the distribution of sale proceeds among creditors in a fair manner within a specified period;
>
> (e) undertake administrative liquidation of a debtor whose assets are not expected to cover the costs of the liquidation procedure or the liquidation of small debtors.[328]

The objective set out in paragraph (a) of Article 5, which identifies the public policy intention to promote debtor rehabilitation, is especially important to the current study. The purpose of this research is to examine restructuring procedures in Saudi bankruptcy law to determine whether these procedures are likely to be effective for achieving the rehabilitative objective identified in paragraph (a) of Article 5. As stated in Chapter 1, this examination focuses on

[328] BL 2018, art 5.

four aspects of restructuring procedures: access to restructuring procedures, control of companies during procedures, moratorium against creditors' actions and restructuring plans.

3.3 Scope of Application of Bankruptcy Law 2018

As discussed in chapter 2, the application of Saudi Arabia's old bankruptcy regime embodied in its CCL 1931 and BPS 1996 was limited to individuals and companies that were categorised as merchants, in accordance with the traditional definition of merchant provided under Article 1 of CCL 1931.[329] Cases regarding the bankruptcy of individuals or companies that did not have merchant characteristics were subject to the jurisdiction of general courts applying the Sharia rules governing bankruptcy.

In order to be recognised as a commercial company (merchant) under the previous bankruptcy laws and, thus, qualify for application of either one of the two bankruptcy pieces of legislation, the activity for which a company was created had to be recognised as a commercial activity in accordance with the list of commercial activities provided under Article 2 of the CCL.[330] The commercial activities of a number of profitable businesses were not included on that list, which was narrow and inflexible, leading to situations where large companies with large amounts of capital and many employees were excluded from the scope of the application of the two bankruptcy legislations (CCL and BPS) only because the activities undertaken by these firms were not deemed commercial according to the strict and narrow list of Article 2 of CCL 1931.[331]

As noted, jurisdiction to hear bankruptcy cases concerning non-merchant individuals or companies was granted to general courts, which apply Sharia rules. The problem of applying Sharia rules to bankruptcy cases was that the outcomes were uncertain, principally due to Sharia rules applied by general courts not being codified.[332] The provisions and rules of Islamic

[329] Article 1 of the CCL defines a merchant as 'a person who undertakes commercial activities as a profession'. See Karaman, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (n 40) 315; Salama (n 232) 353.

[330] Examples of these activities are the purchase of goods with the intention of selling them, transport services of all kinds, brokering, and agency. CCL, art 2.

[331] See Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135.

[332] See Al-Jarbou (n 48); Alshubaiki (n 47). The idea of codifying Sharia had been strongly opposed by many Islamic scholars. The reasons provided by those against the idea of codifying Sharia vary. One of these reasons, and perhaps the most important, is the belief that such a step would lead to the distortion of Sharia and unjustified changes to its rules, changes that could lead eventually to its displacement as an overall law of the state. Opposition to codifying Sharia was also caused by the belief that such codification would limit the discretion granted to

law in many issues are debatable and open to different schools of thought and different interpretations,[333]and without adopting a certain type of interpretation to be applicable (codification), judges were, generally, free to apply whatever interpretation they believed to be the most appropriate Islamic judgment in the case in question.[334] To avoid such uncertainty, various scholars called for expanding the scope of application of bankruptcy legislation to cover every business entity, regardless of whether activity undertaken by such entity was categorised as a commercial activity under Article 2 of the CCL.[335]

Considering the central aim of the new BL 2018 to encourage economic activities, the Policy Paper of the BL 2018 Project expressly highlighted the fact that the concept of 'traders' provided under Article 2 of CCL was not broad enough to cover all entities that conduct economic activities. Therefore, as stated in the Policy Paper, the distinction between traders and non-traders would have no effect under application of the new BL 2018, which would be applicable to all individuals and companies conducting economic activities, whether or not such activities were recognised as commercial under Article 2 of CCL 1931.[336] Eventually, the distinction between traders and non-traders was abandoned, as BL 2018 applies to:'(a) natural persons engaging in commercial or professional activities,[337] or any other for-profit activities in the Kingdom; (b) commercial and professional companies, regulated entities,[338] as well as other companies and for-profit entities registered in the Kingdom; and (c) non-Saudi investors of a natural or legal personality holding assets in the Kingdom, or engaging in commercial or professional activities, or any for-profit activities through a licensed establishment in the

judges and compel them, in some cases, to decide against what they believe to be truthful or just. See Abdulrahmman Alshathri, *Codifying Sharia Law (Arabic)* (1st edn, Dar AlSomeie 2007) 23–47.

[333] After the death of the Prophet Mohammed, the Islamic scholars had to address several novel issues confronting the Islamic nation and produce legal solutions based on their independent reasoning (*ijtihād*). They were also contemplating problems that had not happened and employed their jurisprudential efforts in providing solutions to such hypothetical issues. As these scholars had various views and judgments, four principal Islamic Schools of Jurisprudence emerged: the Ḥanafī, Mālikī, Shāfiʿī and Ḥanbalī. The outcomes of these schools had to be based on the primary sources of the Quran and the Sunnah, and for this reason, other secondary sources of Sharia have developed, including *ijma*, which means a consensus, and *qiyas*, which means analogy. See Alshubaiki (n 47) 378.

[334] ibid 384.

[335] Al-Jaber (n 54) 169; Al-Ghamdi and Hosseini (n 99) 135.

[336] Ministiry of Commerce and Industry (n 25) para 4.1.

[337] Article 1 of BL 2018 defines professional activity as an 'activity practiced by a person as a profession for his own account, based on expertise, qualification, talent, or skill, without an employment contract with a beneficiary rendering him a subordinate thereto or subject to his control and supervision.'

[338] Regulated entity is defined as a 'person who is licensed to engage in a financial activity, or who manages a public facility in accordance with the provisions of Article 3 of [BL 2018].'— Article 1 of BL 2018. Examples of regulated entities are banks and utility companies.

Kingdom. This Law shall only apply to said investors' assets which are located in the Kingdom.'[339]

It is clear from the provision of Article 4 of BL 2018 that the bankruptcy law applies first to natural persons, whether they are traders, professionals, or any person conducting a profit-making activity. Second, the law applies to all legal persons, whether commercial or professional companies or regulated entities as defined in the law, and any entity aiming to gain profit, provided that this entity is registered in the Kingdom. Third, the bankruptcy law applies to non-Saudi investors, whether they are natural or legal persons, who practise a commercial or professional activity or any other profit-making business through a licensed establishment in the Kingdom. In this case, application of the bankruptcy law shall be limited to the investor's assets located in the Kingdom and shall not extend abroad.[340]

3.4 Restructuring Procedures under BL 2018

BL 2018 provides two restructuring procedures, namely, the Preventative Settlement (PS) and Financial Restructuring (FR). Although rehabilitation of distressed businesses is the ultimate objective of these two processes, their methods for achieving this objective differ in several ways. This section explains, in brief, how the PS and FR procedures operate and how they differ from one another. Then, the rationale behind the duality of restructuring proceedings in BL 2018 and the negative effects of this duality in practice are discussed.

3.4.1 Preventative Settlement Procedure (PS)

PS is thought to be the most flexible tool for restructuring under the BL 2018 regime.[341] Such flexibility is evident in the limited involvement of the court in the Settlement process.[342] The involvement of the court in this procedure is, for the most part, limited to two stages: the first hearing where the court determines whether to open the Settlement procedure, and the confirmation hearing that takes place soon after the voting process on the settlement proposal, where the court examines the merit of the settlement proposal and its compliance with fairness standards before sanctioning the proposal and making it binding over all creditors.[343]

[339] BL 2018, art 4.
[340] See Iman Suliman, *Commercial Papers and Bankruptcy* (Dar Alejadh 2019) 307–308; Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 296–298; Al-Ahmad (n 315) 60–66.
[341] See Al-Ahmad (n 315) 95.
[342] ibid 131.
[343] ibid 105.

Article 1 of BL 2018 defines the PS Procedure as 'a procedure aiming to facilitate reaching an agreement between the debtor and its creditors to settle its debts, where the debtor maintains the right to manage its activities'.[344] As demonstrated in this definition, PS is a debtor-in-possession driven procedure, allowing the incumbent management to remain in control of company affairs while seeking a settlement with its creditors to facilitate the business's survival.[345]

The right to initiate the PS procedure is exclusively granted to the debtor through an application to the Commercial Court.[346] The application request for the commencement of a PS procedure must be filed with the court together with the settlement proposal, which includes but is not limited to a statement of the financial situation of the debtor, the effects of the economic situation thereon, and the assignment of creditors into classes in accordance with the nature of their claims.[347]

Within 40 days of PS filing, the court holds a hearing to determine whether to open the procedure. When reviewing the PS application, the court will open the procedure if it is satisfied that the debtor's business is likely to continue, the creditors' claims can be settled within a reasonable timeframe, and the debtor has arranged with due diligence the creditors into classes, in a fair fashion.[348] Therefore, the court at this stage is not concerned with the fairness of the settlement proposal or its merits. Instead, the focus of the court at this point is on determining the feasibility and reasonableness of the proposal and ensuring the fair classification of creditors.[349] The role of the court at this hearing is also important in preventing any potential abuse of the restructuring procedure, such as using it to avoid or delay inevitable liquidation of non-viable businesses.[350]

Once the procedure is opened, the court may, upon a request from the debtor at the time of filing for the PS procedure, order a moratorium for a period not exceeding 90 days from the

[344] BL 2018, art 1.
[345] Clifford Chance, 'The New Saudi Insolvency Law and Its Implementing Regulations' (2019) 2 <https://www.cliffordchance.com/briefings/2019/07/the_new_saudi_insolvencylawanditsimplementin.html> accessed 26 August 2019.
[346] BL 2018, art 13.
[347] BL 2018, arts 14, 29; BL 2018 Implementing Regulations, art 16.
[348] BL 2018, art 15(1)(a).
[349] Suliman (n 340) 324–325.
[350] Al-Ahmad (n 315) 95. See also Ministiry of Commerce and Industry (n 25) 17.

date of procedure opening and may extend such period by 30 days one or more times at the request of the debtor, provided the total duration of the moratorium does not exceed 180 days.[351] When the moratorium is in force, certain actions against the debtor or its assets are stayed, such as applying for any bankruptcy procedures; enforcement procedures over any of the debtor's assets provided as a security interest, without consent of the court; and any action against the personal guarantor or the in-kind guarantor of the debtor's debt, without the consent of the court.[352]

Only the creditor or owner whose legal or contractual rights will be affected by the settlement proposal, including the reduction, postponement or instalment in the fulfilment of such rights, has the right to vote on the proposal.[353] The proposal is deemed accepted if approved by each class of creditors. Approval of a class is obtained if the proposal has been approved by the creditors whose claims represent two-thirds of the value of debts owed to voters in the same class.[354] Therefore, under the PS procedure, there is no possibility of cross-class cramdown, by which a restructuring proposal is involuntarily imposed by the court despite any objections by certain classes of creditors.[355]

Once the settlement proposal has been voted on, the court holds a confirmation hearing to decide whether to confirm the settlement proposal. The role of the court at this hearing is more than simply endorsing the majority vote.[356] Additionally, the court closely examines the merit of the settlement proposal and determines whether the proposal is in compliance with the standards of fairness.[357]

The limited involvement of the court in the debtor-in-possession style adopted under the PS procedure with regard to managing the company undergoing a restructuring process may make this procedure a preferable option for restructuring a company in distress. However, the lack of a cross-class cramdown option in the PS procedure might discourage the use of such procedure in favour of the FR procedure, where cross-class cramdown is permissible, as explained in the next section.

[351] BL 2018, art 18.
[352] BL 2018, art 20.
[353] BL 2018, art 27; BL 2018 Implementing Regulations, art 39. See Suliman (n 340) 334–335.
[354] BL 2018, art 31(2).
[355] See Ministiry of Commerce and Industry (n 25) 20.
[356] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 323.
[357] BL 2018, art 34(1).

3.4.2 Financial Restructuring Procedure (FR)

Article 1 of BL 2018 describes FR as a procedure that 'allows the debtor to reach an agreement with its creditors to reorganise its financials under the supervision of a court-appointed trustee'.[358] In general, the FR procedure is not debtor friendly in comparison to the PS procedure, as the former provides the court and creditors more room to intervene in the restructuring proceedings.[359] Court intervention in this procedure is primarily embodied in restrictions imposed regarding the management of debtor affairs during the reorganisation process, where the court appoints a trustee to supervise management of the debtor's business.[360]

Unlike the case under the PS procedure, the right to initiate a FR proceeding is not limited to the debtor. As per Article 42 of BL 2018, the debtor, the creditor or a competent authority (when the debtor is a regulated entity) may apply to the court to commence the FR procedure.[361]Also, and as per Article 41 of BL 2018, the court may, on its own motion or upon the request of a person with interest, order the commencement of the FR procedure upon its decision to terminate the PS procedure.

Filing an application to commence the FR procedure automatically results in a moratorium from creditor action. The initial period of the moratorium under the FR is 180 days, and the court may, at its own discretion or upon the request of the debtor or a trustee, extend the moratorium no more than 180 days.[362] Therefore, the moratorium against creditors' claims goes into effect automatically once the application for the FR procedure has been made, unlike in the PS procedure, where the moratorium is ordered only at the request of the debtor.[363]

Similar to the PS procedure, the court will open the FR process if it is convinced that the debtor's business is likely to continue and if the creditors' claims will be settled within a reasonable timeframe.

---

[358] BL 2018, art 1.
[359] Suliman (n 340) 344; Abdulmajid Almansour, *Procedures of the New Bankruptcy Law*. (Imam Mohammad Bin Saud Islamic University 2018) 45–47.
[360] See Simon Johnson, '" Equanimity between Creditors "? Spotlight on Saudi Arabian Insolvency Law Reform' (2015) 30 Butterworths Journal of International Banking and Financial Law 626; Suliman (n 340) 344.
[361] BL 2018, art 42.
[362] BL 2018, art 46(1).
[363] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 345–346.

Following acceptance of the FR application, a bankruptcy licensed trustee is appointed by the court to supervise the debtor's business and to guarantee the swift implementation of the FR process.[364] The appointed trustee enjoys a wide range of authority, including revisiting the debtor's contractual arrangements and terminating certain agreements, if such termination is necessary for the continuation of the business and does not result in material damage to the contracting party.[365] Furthermore, during the FR process, the debtor is prohibited from taking certain actions, such as receiving new funding, repaying due or postponed debts, and signing a new insurance contract that entails new obligations upon the debtor, without obtaining approval from the trustee.[366]

The restructuring proposal, which is formulated by the debtor with the trustee's assistance, is voted on by the creditors, who must be assigned into proper classes. The voting approach of the FR procedure is similar to that of the PS procedure in terms of classification of creditors, court confirmation of the restructuring proposal and acceptance thresholds (i.e. two thirds in value of creditors voting in each class). However, in this procedure, the court has the ability to confirm a FR proposal that does not obtain the approval of all classes of creditors (cramdown) if at least one class of creditors approves the proposal and the proposal is approved by the creditors whose claims represent at least 50% of the total value of the claims of the creditors voting in all classes, and if the court considers that the confirmation of the proposal realises the interests of the majority of creditors.[367] Regarding the cramdown mechanism, in the Policy Paper of the Bankruptcy Law project published in 2015, the Saudi Ministry of Commerce recognised that in some cases it may be essential to impose a restructuring to maintain the enterprise value and offer the debtor the best chance to rescue its business, which will eventually benefit the creditors as well.[368]

[364] BL 2018, art 50.
[365] Dario Najm, 'Commentary on the Saudi Arabian Bankruptcy Law' (2018) 6 <https://bsabh.com/commentary-on-the-saudi-arabian-bankruptcy-law/> accessed 23 January 2019.
[366] ibid.
[367] BL 2018, arts 79-80.
[368] Ministiry of Commerce and Industry (n 25) 20.

3.4.3 PS vs. FR

Following the review of the mechanisms of PS and FR procedures, in this section, the distinctions between these two procedures are demonstrated.

Both processes are designed to facilitate rehabilitation of viable distressed businesses and to help such businesses regain their financial health. However, the models adopted by these two procedures to implement the goal of corporate rescue are fundamentally different in some respects.[369] First, the right to file for the PS procedure is limited to the debtor, while such a right is extended to both creditors and the court under FR. Second, PS is a debtor-in-possession driven process, where incumbent management remains in charge of the business's affairs during the settlement process, with no interference from the court, whereas commencement of the FR procedure results in the appointment of a licensed trustee to supervise the conduct of the incumbent management, whose authority over the company's management is subject to the trustee's approval. Third, the moratorium in the PS procedure is granted only upon the request of the debtor when filing for the procedure, while under the FR procedure, the moratorium takes place automatically and immediately once the FR is applied for. Fourth, cross-class cramdown is not permissible in the PS procedure, as the settlement proposal must be approved by all classes, whereas the cramdown is possible within the FR procedure if at least one impaired class of creditors votes for the reorganisation proposal and the other conditions noted previously are met. Arguably, other than these four differences, the rules and provisions of these two procedures regarding other issues are almost identical, as the following chapters will illustrate.

[369] See Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 289; Suliman (n 340) 344–352; Al-Ahmad (n 315) 131; Almansour (n 359) 45–47.

Procedure	Who Can Initiate the Procedure?	Moratorium	Managing the Business Undergoing Restructuring Procedure	Voting Process
PS	Debtor only	Applies upon the request of the debtor	Debtor-in-possession	• Settlement proposal must be approved by all classes of creditors • Cross-class cramdown is not permissible
FR	Debtor/Creditor/ Court in some circumstances	Applied automatically once the application for procedure is filed	Debtor-in-possession but under supervision of court appointed trustee	• Restructuring proposal must be approved by all classes of creditors • Cross-class cramdown is permissible

3.4.4 The Duality of Restructuring Procedures in BL 2018 and its Possible Drawbacks in Practice

Having two restructuring procedures under BL 2018 has not been justified by the legislature. Even scholars who have written about the new bankruptcy law have focused their studies on the similarities and differences between the two procedures without seeking justification for the existence of two procedures for restructuring. Some scholars imply justification for the existence of the two restructuring procedures by arguing that the procedures are designed to address different degrees of financial distress.[370] They seem to suggest that the PS, which is the softer procedure of the two, is designed to rehabilitate businesses when the prospect of survival is very likely. If the debtor's financial situation is so promising that the likelihood of successful rehabilitation is high, then the lighter restructuring procedure (i.e. PS) may be more appropriate as, assumingly, there is no need in this situation for the appointment of a trustee to monitor and supervise the debtor's management during the restructuring process. If the success of the rehabilitation process is likely but not highly likely, then FR may be a more appropriate procedure, as it involves the appointment of a trustee to monitor and supervise the debtor's

[370] Suliman (n 340) 305.

management to ensure that the restructuring process proceeds as required and to enhance the likelihood of successful restructuring.[371]

However, this justification seems artificial and inaccurate, given the fact that the threshold financial test applied to determine debtors' eligibility to commence the restructuring procedure is identical in both procedures. It will be shown in Chapter 4 that both procedures are only available if the debtor is, or is likely to become, insolvent on either a cash flow or balance sheet basis.[372] The law does not discriminate between debtors whose prospect of rehabilitation is high and those whose prospect of rehabilitation is possible but not high. In the eyes of the law, both types of debtors are free to choose the restructuring procedure they think is appropriate, as long as they meet the threshold financial test and the court is satisfied that the business is likely to continue, and the creditors' claims will be settled within a reasonable timeframe.[373] Therefore, the degree of financial distress justification is not valid, and otherwise, there is no clear explanation for having two restructuring procedures under the new Saudi bankruptcy regime.

Having two restructuring procedures under BL 2018 may not seem problematic at first glance, but it is when the two procedures are examined closely. As the previous section clarified, the two characteristics of the PS procedure that most strongly distinguish it from the FR procedure are that, unlike the FR, the PS is a debtor-in-possession-driven process, and it does not contain a cross-class cramdown mechanism. However, as the subsequent chapters illustrate, these two characteristics are likely to have negative impacts in practice. First, as explained in Chapter 5, the debtor-in-possession model employed under the PS procedure does not seem suitable for the concentrated structure of the Saudi share market; the co-determination model adopted under the FR procedure seems more appropriate. Second, as illustrated in Chapter 7, due to the lack of a cross-class cramdown mechanism under the PS procedure, the courts have regularly terminated PS procedures upon the failure of the settlement proposal to obtain the acceptance of all classes of creditors.[374] Following such termination, the court usually, at its discretion or at the request of the debtor or any of the creditors, orders the commencement of the FR procedure on the basis that such a procedure is appropriate for proceeding, as it provides a

[371] ibid.
[372] BL 2018, arts 13, 42.
[373] BL 2018, arts 15(1)(a)(i), 47(2)(a)(i).
[374] Examples of this practice are case number 6831 (2019); case number 10957 (2019); case number 2501 (2019); case number 5102 (2019).

cross-class cramdown option to overcome the failure to meet the rigid voting quorum prescribed under the PS procedure. This practice involves an unnecessary increase in the cost and duration of the proceedings, contrary to the objectives of BL 2018 to reduce procedural costs and timeframes.[375]

Ideally, to address the negative impacts of these two characteristics of the PS procedure, given that the need for two restructuring procedures under the Saudi bankruptcy regime has not been clearly justified, abolishing the PS procedure and keeping the FR procedure as the only restructuring procedure may be the most appropriate action. Alternatively, two reforms should be introduced in the PS procedure. First, the PS should adopt the same co-determination model that applies under the FR process. Second, the cross-class cramdown mechanism should be available within the PS procedure. Admittedly, these two reforms, if implemented, would bring the PS and FR procedures close together, which is why, in the view of the author, abolishing the PS procedure and retaining the FR as the only restructuring regime seems the optimal option.

3.5 Conclusion

This chapter has provided a general overview of the Saudi bankruptcy law of 2018. The enactment of this law represents one of the most significant legal reforms in the Saudi Arabia legal system. Such reforms have been taken to facilitate and encourage foreign capital investments in the Kingdom. Indeed, FDI is expected to play a critical role in the Kingdom's achievement of its 2030 Vision goal of diversifying its economy away from oil revenues.

One of the distinguishing advantages of BL 2018 is its wide scope of application. This contrasts with the narrower scope of the old bankruptcy regime, which applied only to individuals and companies that were categorised as merchants according to the traditional definition of merchant provided under Article 1 of CCL 1931. The jurisdiction for hearing bankruptcy cases concerning non-merchant individuals or companies under the old regime was granted to general courts, which apply Sharia rules, but the outcomes of bankruptcy cases when Sharia rules were applied were uncertain, principally due to their lack of codification. This problematic uncertainty has been resolved by the introduction of BL 2018, which has a widely comprehensive scope of application, as it applies to all individuals and companies engaging in

[375] BL 2018, art 5(d).

commercial or professional activities or any other for-profit activities, regardless of whether such activities are categorised as commercial activities under the provisions of the CCL.

Another notable characteristic of the new BL 2018 is the importance it places on rehabilitating viable but distressed businesses. This objective is embodied in the two restructuring procedures provided under the new regime (i.e. PS and FR). This chapter has explained, briefly, the mechanisms of the two procedures, as an in-depth understanding of how these procedures function serves as the foundation for further, more focused discussions in subsequent chapters.

The following chapter discusses the accessibility of restructuring procedures under Saudi BL 2018. Mainly, the chapter examines the criteria that should be satisfied to access restructuring procedures in order to determine whether such criteria facilitate timely access to these procedures, which is crucial for the success of the restructuring process.

Chapter 4: Access to Restructuring Procedures

The first issue that needs to be considered when examining any restructuring procedure is the accessibility of such a procedure, or in other words, the standard that must be met for the commencement of that restructuring procedure. Commencement criteria that facilitate quick, cost-effective and convenient access to restructuring procedures have been suggested.[376] Indeed, restrictive access can prevent the restructuring procedure from commencing in a timely fashion, and the effects of this delayed commencement can be detrimental to the value of assets and diminish the prospect of a successful reorganisation.[377] At the same time, a total relaxation of the commencement standards may open the door for improper use of the restructuring procedure, whereby such a procedure is utilised not to resolve financial difficulties but to gain a strategic advantage, such as by shedding a company's contractual obligations, renegotiating its debts or prevaricating and depriving creditors of full payment on their claims.[378] Therefore, the need exists 'to balance encouraging early action on the one hand and providing too much opportunity for strategic behaviour on the other'.[379] In order to determine whether such a balance exists under the Saudi restructuring regime, this chapter examines the entry requirements for restructuring procedures under Saudi BL 2018.

The chapter is divided into three parts. The first two parts consider the entry requirements for restructuring procedures in the UK and the US laws. The third part then examines the entry requirements for restructuring procedures under Saudi law considering the UK and the US perspectives provided in the first two parts of the chapter.

4.1 Access to Restructuring Procedures from the UK Perspective

4.1.1 Overview of the UK Restructuring Regime

During the past four decades, the UK insolvency and restructuring regime has experienced three major reforms, introduced by three pieces of legislation: Insolvency Act (IA)1986, Enterprise Act (EA) 2002 and Corporate Governance and Insolvency Act (CGIA) 2020. No sophisticated system for corporate rescue existed in the UK until the 1980s, when Insolvency Act 1985 was enacted, soon after consolidated as IA 1986. Prior to the enactment of IA 1986,

[376] UNCITRAL, *Legislative Guide on Insolvency Law* (United Nations 2005) 45.
[377] ibid.
[378] ibid 53–54.
[379] Colin Anderson and David Morrison, 'The Commencement of the Company Rescue: How and When Does It Start?' in Paul J Omar (ed), *International Insolvency Law: Themes and Perspectives* (Ashgate Publishing Limited 2008) 92.

rescue of a viable business could be facilitated by either a receiver appointed by a floating charge holder to manage the company's affairs, or through a scheme of arrangement.[380]Receivership, however, was merely an enforcement weapon in the hands of floating charge holders and was not designed as a corporate rescue procedure.[381] The prospect of a company's rescue under receivership was dependent on whether such rescue coincided with the interests of the debenture holder to whom the administrative receiver owed a primary duty.[382] The scheme of arrangement, on the other hand, was introduced under Companies Act 1862; its application was limited to companies that were in the process of being wound up. The law was subsequently revised to allow such schemes to apply to solvent companies. Since then, the scheme of arrangement has been utilised by both solvent and insolvent companies to enter into compromises or arrangements with their creditors or members.[383] However, the scheme of arrangement under section 425 of Companies Act 1985 was described as cumbersome, complicated and expensive.[384] Moreover, the statutory provisions did not include a moratorium, pending sanction of the scheme by the court. Absent a moratorium, dissenting creditors could easily proceed with their claims against the wishes of those voting for the arrangement.[385]

The enactment of IA 1986 is considered a significant reform in UK insolvency law. This legislation was heavily inspired by the recommendations of the Review Committee on Insolvency Law, chaired by Sir Kenneth Cork. In June 1982, the Committee published the Cork Report, which advocated for fundamental reform of UK insolvency law. The report noted that, in many cases, the absence of effective rescue procedures had forced viable insolvent companies into liquidation and had led to potentially rescuable businesses closing down.[386] The Cork Report emphasised the importance of insolvency laws that 'provide a means for the preservation of viable commercial enterprises capable of making a useful contribution to the

[380] See Tolmie (n 130) 63; Rebecca Parry, *Corporate Rescue* (Sweet & Maxwell 2008) 3; Goode (n 130) 382.
[381] Goode (n 130) 382. The receivership procedure is 'a means whereby a creditor benefitting from a debt secured under a floating charge could appoint a receiver to take control of the assets subject to the security, effectively taking control of the company. The receiver's primary objective was to realise his client's security by applying funds released in the liquidation of an equivalent value of assets of the debtor company.' Paul J Omar and Jennifer Gant, 'Corporate Rescue in the United Kingdom: Past, Present and Future Reforms' (2016) 24 Insolvency Law Journal 40, 3.
[382] Parry (n 380) 4.
[383] Jennifer Payne, *Schemes of Arrangement: Theory, Structure and Operation* (Cambridge University Press 2014) 7.
[384] ibid 5.
[385] Goode (n 130) 382.
[386] Sir Kenneth Cork (Chairman), *Insolvency Law and Practice: Report of the Review Committee* (Cmnd 8558) (HMSO, 1982) ("Cork Report") para 496.

economic life of the country'.[387] Based on the report's recommendations, two new rescue procedures, the administration order and the company voluntary arrangement (CVA), were introduced.

The UK corporate insolvency law was further reformed by the enactment of Enterprise Act (EA) 2002. The reforms introduced in section 248 of EA 2002 substantially revised the administration procedure. The original administration regime under Part II of IA 1986 was replaced by the new administration regime under Part II of EA 2002, the provisions of which are now set out in the new Schedule B1 of IA 1986.

The most recent reform of UK corporate insolvency and restructuring law was the introduction of CGIA 2020. Among the reforms provided by CIGA 2020 was the introduction of two corporate restructuring procedures: a stand-alone moratorium procedure and a restructuring plan procedure (Part 26A scheme), which includes a cross-class cramdown mechanism. The commencement criteria for these two procedures and for the administration process, CVA and scheme of arrangement are considered next.

4.1.2 UK Administration

4.1.2.1 Overview

The administration order is a mechanism through which an external professional – the administrator – takes control of a company's affairs for the benefit of all creditors while actions are taken to formulate a rescue strategy to resolve the company's financial distress under the protection of a statutory moratorium.[388] Administration removes the incumbent management from control over the company's affairs in favour of an insolvency practitioner 'administrator', who acts as the officer of the court and administrates the company during the rescue proceeding.[389]

Administration has an overriding single objective, which is outlined in paragraph 3(1) of Schedule B1: rescuing the company as a going concern. If this objective is not reasonably practical or is not in the interest of the creditors as a whole, the administrator must then aim to

[387] ibid para 198(j).
[388] Mallon, Rogan and Cukier (n 13) 105.
[389] Marjan Marandi Parkinson, *Corporate Governance in Transition: Dealing with Financial Distress and Insolvency in UK Companies* (Palgrave Macmillan 2018) 55.

achieve a better result for the creditors as a whole than would be likely if the company were wound up. If neither of these two objectives is reasonably practical, then the objective the administrator must meet as a final option is realising property in order and making distribution to one or more secured or preferential creditors.[390]

Although the primary objective of administration is 'rescuing the company as a going concern', which is described as 'pure rescue', this outcome rarely occurs in practice; rather, the most common outcome of the rescue efforts in the administration process is 'corporate recycling', involving either a complete or partial going concern sale of the company's business.[391] Indeed, the emphasis in practice in the UK has been on business rescue rather than on pure corporate rescue.[392] The Association of Business Recovery Specialists (R3 Group) has classified rescue into three types – 'complete going concern sales', 'partial going concern sales' and 'full company survival' – and has noted that 'the two sale types were the most common…It is not surprising to find that full company survivals had a relatively low frequency'.[393]

Unlike US Chapter 11, administration is not a stand-alone reorganisation procedure.[394] Administration is merely a gateway to a variety of routes that the distressed company can take.[395] If corporate restructuring seems reasonably practicable, the administrator may advance a proposal for one of the following: a corporate voluntary arrangement (CVA) under Part 1 of IA 1986, a scheme of arrangement under Part 26 of Companies Act (CA) 2006 or a restructuring plan under the recently enacted Part 26A of CA 2006.[396]

4.1.2.2 Access to UK Administration

Administration as originally enacted was a court-centred process, as the appointment of the administrator could only be made by the court upon application by the company or its creditors. This was changed by EA 2002, which substantially revised the administration procedure. One significant change under the revised administration regime is that the administrator is no longer

[390] Harry Rajak, *Company Rescue and Liquidation* (3rd edn, Sweet & Maxwell 2013) 91–92.
[391] Keay and Walton (n 128) 82–83.
[392] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 10.
[393] R3, *Corporate Insolvency in the United Kingdom: A Decade of Change* <http://www.r3.organisation.United Kingdom/publications> 20 (as cited in Sandra Frisby, 'In Search of a Rescue Regime: The Enterprise Act 2002' (2004) 67 The Modern Law Review 247, 249.
[394] See Goode (n 130) 394.
[395] ibid.
[396] IA 1986, Schedule B1, para 49(3).

solely court-appointed; three methods of appointment are now possible. One is an out-of-court appointment by the holders of floating charges, the second is an out-of-court appointment by the company or the directors of the company and the third method is appointment through the court upon the application of the company, its directors, one or more of its creditors or a combination of these parties.[397] Notably, the company's out-of-court appointment of an administrator has been the predominate method for initiating the UK administration procedure since the enactment of EA 2002.[398]

If the application for the administration order is made by someone other than the qualifying floating charge holder, the court will not make the administration order unless it is satisfied that the company is unable or is likely to become unable to pay its debts as defined in section 123 of IA 1986[399] and that the administration order is 'reasonably likely' to achieve the purpose of administration.[400] The debtor company's inability or likely inability to pay its debts is also a prerequisite for an out-of-court appointment made by a person other than the holder of the qualifying charge.[401] The requirement of actual or impending insolvency does not apply when the administration application to the court is made by a holder of qualifying floating charges or when such holder appoints an administrator out of court.[402] In practice, however, for reputational reasons, holders of qualifying charges, such as banks, usually prefer not to appoint an administrator and leave that decision to the company or its directors, although they do have a say in the selection of the administrator.[403] As a result, the administration will mostly function only when a company is insolvent or when its insolvency is impending.[404]

---

[397] See Ian F Fletcher, 'UK Corporate Rescue: Recent Developments–Changes to Administrative Receivership, Administration, and Company Voluntary Arrangements–The Insolvency Act 2000, the White Paper 2001, and the Enterprise Act 2002' (2004) 5 EBOR 119.
[398] Goode (n 130) 417.
[399] Schedule B1 of IA 1986, paras 11(a), 111(1).
[400] Schedule B1 of IA 1986, para 11(b).
[401] Schedule B1 of IA 1986, para 27(2)(a).
[402] Schedule B1 of IA 1986, paras 35(1)(a), 35(2)(a). Paragraph 14(3) of Schedule B1 of IA 1986 states that 'a person is the holder of a qualifying floating charge in respect of a company's property if he holds one or more debentures of the company secured—
(a) by a qualifying floating charge which relates to the whole or substantially the whole of the company's property,
(b) by a number of qualifying floating charges which together relate to the whole or substantially the whole of the company's property, or
(c) by charges and other forms of security which together relate to the whole or substantially the whole of the company's property and at least one of which is a qualifying floating charge.'
[403] Sandra Frisby, 'Not Quite Warp Factor 2 yet? The Enterprise Act and Corporate Insolvency (Pt 1)' (2007) 22 JIBFL 327, 329.
[404] See Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 231; Rajak (n 390) 107.

4.1.2.3 The Requirement of Actual or Impending Insolvency

In defining the 'inability to pay debts', section 123 employs the two prime tests of insolvency (cash flow and balance sheet). Section 123(1)(e) provides that 'a company is deemed unable to pay its debts' if it is 'unable to pay its debts as they fall due' (which is the cash flow test). Following the balance sheet test as outlined in section 123(2), a company is deemed unable to pay its debts if it is proved 'that the value of the company's assets is less than the amount of its liabilities, considering its contingent and prospective liabilities'.

The cash flow test is concerned with debts that are currently due or will become due in the reasonably near future.[405] What constitutes the 'reasonably near future' depends on a variety of factors, most notably the nature of the business.[406] It is recognised that when the court has to consider time beyond the reasonably near future, the cash flow test becomes entirely speculative, and the balance sheet test becomes the only sensible method of determining insolvency.[407]

In practice, satisfying the cash flow test is relatively easier than meeting the balance sheet test, which relies heavily on the valuation of the company's assets and liabilities. The UK Supreme Court decision in *BNY Corporate Trustee Services Ltd v Eurosail-UK 2007-3BL Plc*[408] is the leading decision clarifying the balance sheet test for corporate insolvency contained in section 123(2) of IA 1986. In this case, to acquire a portfolio of subprime mortgage loans secured on residential properties in the UK, Eurosail, a special purpose entity set up by Lehman Brothers, issued loan notes in 2007. These notes were categorised into 5 main classes (A, B, C, D and E), each containing 14 subclasses (A1 through A14, B1 through B14 and so on). Class A1, which was the highest in payment priority among the notes, had already been repaid; the other junior classes were not repayable until 2045 at the latest unless an 'event of default' occurred. Condition 9(a) of the notes stated that upon the occurrence of certain specified events of default, the trustee of the noteholders might serve on the issuer (Eurosail) a written enforcement notice, declaring the notes to be due and repayable. One of the specified events of default, according to condition 9(a)(iii), was the issuer being 'deemed unable to pay its debts' as contemplated by section 123(1)(e) and (2) of IA 1986. The service of an enforcement notice

[405] *In re Cheyne Finance plc (No 2)* [2008] Bus LR 1562.
[406] *BNY Corporate Trustee Services Ltd v Eurosail-UK 2007-3BL Plc* [2013] 1 WLR 1408.
[407] ibid at 37.
[408] [2013] 1 WLR 1408.

would have impacted A2 and A3 noteholders significantly. The original conditions of the notes stated that for the interest payments, A2 and A3 classes ranked *pari passu*, but for principal repayment, the A2 class had priority over A3. If the enforcement notice were served, however, A2 and A3 would have ranked *pari passu* for both the payments of interest and the repayment of principal, and A2 would have had no priority over A3. Thus, the service of an enforcement notice was not in the best interest of A2 noteholders.

Eurosail signed currency swap agreements with a Lehman Brothers group to hedge its own risks in relation to currency fluctuations. These agreements were terminated following the Lehman Brothers' collapse in 2008. Although the termination of the currency swap agreements left Eurosail unprotected and vulnerable to fluctuations in the interest and currency rates and created a vital deficiency in the company's net asset position, the company continued to pay its debts. The A3 noteholders insisted that an event of default had occurred based on the company being insolvent according to the balance sheet test under section 123(2) of IA 1986. Accordingly, the A3 noteholders asked the trustee to serve an enforcement notice on the issuer, declaring the notes to be due and repayable. The trustee then applied to the court for a determination on whether the issuer (Eurosail) was 'unable to pay its debts' for the purposes of condition 9(a)(iii), which depended on the court's interpretation of section 123(2) of IA 1986.

The High Court and the Court of Appeal held that no event of default had occurred, as Eurosail was not balance sheet insolvent as defined by section 123(2) of IA 1986. In its hearing on the A3 noteholders' appeal, the Supreme Court upheld the decision of the Court of Appeal and dismissed A3 noteholders' appeal. Despite reaching the same conclusion on the construction of section 123(2) of IA 1986, the Supreme Court disagreed with the Court of Appeal's reasoning. The Court of Appeal, in its decision, had stated that section 123(2) applied 'to a company whose assets and liabilities (including contingent and future liabilities) are such that it has reached the point of no return'. While affirming the Court of Appeal's decision, the Supreme Court rejected the 'point of no return' test adopted by the Court of Appeal and insisted that the test should not pass into common usage as a paraphrase of the effect of section 123(2). The Supreme Court held that the court must be satisfied, 'on the balance of probabilities, that a company has insufficient assets to be able to meet all its liabilities, including prospective and contingent liabilities', to establish that a company is balance sheet insolvent within the meaning

of section 123(2).[409] The court asserted that, since the final date of redemption was 2045, Eurosail's ability to pay its debts could not be determined until closer to 2045.

Professor Goode observed that employing the balance sheet test requires valuation of the company's assets and liabilities, which is not achieved through an exact science but is based on a 'judgment as to the amount a willing buyer would pay in the market when dealing with a willing seller'.[410] As a result, the valuation required to determine balance sheet insolvency may be complex, detailed and laborious and may be difficult for the court to deal with effectively.[411]

As the wording of paragraph 11(a) of Schedule B1 of IA 1986 indicates, access to the administration process is not limited to companies that are actually insolvent; companies that are likely to become insolvent may also access the administration procedure. The term 'likely' requires definition in this context. The term was first introduced under amended section 8(1) of IA 1986, which provided that:

> Subject to this section, if the court —
> (a) is satisfied that a company is or is likely to become unable to pay its debts (within the meaning given to that expression by section 123 of this Act), and
> (b) considers that the making of an order under this section would be likely to achieve one or more of the purposes mentioned below,
> the court may make an administration order in relation to the company.

In *Re Colt Telecom Group Plc (No.2),*[412] Jacob J held that the word 'likely' in section 8(1)(a) meant more probable than not. Therefore, to establish that a company is likely to become unable to pay its debts, the court must be satisfied that it is more probable that the company will be unable to pay its debts than not. Jacob J rejected the argument that the mere existence of a real prospect of insolvency is enough to meet the likelihood threshold under section 8(1)(a). He stated:

> [I]t is not enough to merely to show [*sic*] a 'real prospect' of insolvency as opposed to insolvency being more likely than not. I cannot think Parliament intended that companies should be exposed to this kind of hostile proceeding where it is more likely than not that the company is not insolvent. Administration is a rescue procedure – it must be shown that rescue is probably needed before asking for a rescue team.[413]

[409] ibid at 48.
[410] Goode (n 130) 115.
[411] Kubi Udofia, 'Establishing Corporate Insolvency: The Balance Sheet Insolvency Test' (2019) 3 <https://papers.ssrn.com/abstract=3355248> accessed 1 October 2021.
[412] [2002] EWHC 2815 (ch).
[413] ibid at 26.

Because the wording of paragraph 11(a) of Schedule B1 replicates that of amended section 8(1)(a), Jacob J's interpretation of 'likely' in the latter is still relevant as an authoritative interpretation of the term as provided under paragraph 11(a) of Schedule B1.[414] The conclusion here is that, unless the administration is initiated by a floating charge holder, which is uncommon, the administration will mostly function only when a company is insolvent or its insolvency is impending.

4.1.3 UK Company Voluntary Arrangement (CVA)

4.1.3.1 Overview

As with the administration procedure, the enactment of the CVA procedure was based on Cork Committee recommendations. This procedure was designed to provide companies with a low-cost, quick and effective means to reach a compromise with their creditors to organise their debts.[415] The resultant compromise binds all creditors who were entitled to vote at the meeting approving the arrangement or would have been if they had received notice of the meeting.[416]

Perhaps the most attractive feature of the CVA is that commencement of the procedure does not result in displacing the incumbent management of the company. Such management remains in control over the company's affairs, subject to the supervision and assistance of a proposed nominee who subsequently converts to the role of supervisor once the CVA proposal obtains the required approval from creditors and shareholders. Therefore, management of the company during the rescue procedure under the CVA follows the 'debtor-in-possession' model, which is actively promoted by those who view the US Chapter 11 regime as the most favourable system for corporate rescue.[417]

However, the CVA does have several limitations. In its report published in 1993, the Insolvency Service noted several obstacles to using the CVA procedure.[418] The procedure's most severe defect is its lack of a statutory moratorium in the period between the commencement of the CVA procedure and the approval of the proposal. The absence of a

[414] Such interpretation has been followed in a number of subsequent cases, such as *Hammonds (A Firm) v Pro-Fit USA Ltd* (2007) EWHC 1998 (ch), *Re AA Mutual International Insurance Co Ltd* (2004) EWHC 2430 (ch) and *Gigi Brooks Limited* (2015) EWHC 961 (ch).
[415] A Smith and M Neill, 'The Insolvency Act 2000' (2001) 17 Tolley's Insolvency Law and Practice 84.
[416] IA 1986, Part 1.
[417] Fletcher (n 397) 127.
[418] Insolvency Service, *Company Voluntary Arrangements and Administration Orders: A Consultative Document* (HMSO 1993). See also Omar and Gant (n 381) 12.

moratorium allows individual creditors to enforce their claims against the company and sabotage any prospect of success for the company in reaching an arrangement with its creditors as a whole.[419] In practice, it is necessary to file for an administration order coupled with the CVA to benefit from the moratorium applicable under the administration order.[420] However, such a course of action is expensive, especially for small companies that cannot bear the costs involved in applying for administration.[421]

The CVA was reformed by the Insolvency Act 2000, which introduced a moratorium to the procedure. The availability of such a moratorium was limited to small companies.[422] This small company CVA moratorium was repealed, however, by the introduction of the new freestanding moratorium process that came into force on 26 June 2020.

4.1.3.2 Access to UK CVA

The CVA can be proposed by the company's director[423] or by the administrator or liquidator if the company is in administration or being wound up.[424] Unlike administration, a company is not required to be insolvent or unable to pay its debts to apply for the CVA.[425] The CVA proposal must provide for either a composition in satisfaction of the company's debts or a scheme of arrangement of its affairs.[426] If the CVA is initiated by the directors, they will appoint a nominee to act in relation to it. The directors must clarify in the proposal why they think the arrangement is desirable and why the creditors can be expected to concur with it.[427] The proposal must include a statement of the company's assets, any other assets that are proposed to be included in the arrangement, the company's liabilities and the manner proposed for dealing with them.[428]

[419] Fletcher (n 397) 127.
[420] Parry (n 380) 6.
[421] Smith and Neill (n 415) 84.
[422] To qualify as a small company and, thus, benefit from the statutory moratorium, the company must meet two or more of the requirements set out in section 382(3) of Companies Act 2006, namely: (1) turnover of not more than £10.2 million, (2) balance sheet total of not more than 5.1 million and/or (3) no more than 50 employees.
[423] IA 1986, s 1(1).
[424] IA 1986, s 1(3).
[425] Tolmie (n 130) 89.
[426] The meaning of composition or scheme of arrangement in this context is explained in Chapter 7 of this thesis.
[427] IR 2016, rule 2.2.
[428] IR 2016, rule 2.3 sets out the contents that must be included in the proposal.

Along with a statement of the company's affairs,[429] the proposal must be sent to the intended nominee unless the nominee is the administrator or liquidator of the company.[430] The nominee then has 28 days to report to the court whether he or she thinks the prospect of the proposed arrangement being implemented is reasonable and whether a meeting of the company and its creditors should be summoned to consider the proposal, and if so, the details of such meeting.[431] The nominee must also be convinced that the company's financial position as to its assets and liabilities are not substantially different from what was represented to the creditors and that no unavoidable manifest unfairness exists.[432] If the nominee suggests the meetings to be called, then unless the court otherwise directs, the nominee can hold the meetings as proposed. If the nominee is the administrator or the liquidator of the company, no report to the court is required, and the office holder may proceed to call the meetings as deemed appropriate.[433] The process of voting on a CVA proposal is discussed in Chapter 7 of this thesis.

While the absence of an insolvency requirement may make the CVA more accessible than administration, the lack of a moratorium in the CVA process may undermine its easy access advantage. Due to the absence of a moratorium, a proposed CVA might easily be frustrated by creditors enforcing their rights before the arrangement is approved.[434] A possible solution for this problem is to put the company into administration before initiating the CVA. As the administration provides a wide range of moratorium on creditors' collection efforts, it enables the administrator some respite from creditors' harassment while he or she tries to accomplish one of the statutory objectives of the administration. The formation and approval of a CVA would commonly be intended as a means for fulfilling the primary objective of administration, which is to rescue the company as a going concern.[435] However, the company's directors may not prefer this solution for three reasons. Firstly, upon the commencement of administration, the directors will automatically lose control of the company and the rescue process in favour of the insolvency practitioner.[436] Secondly, applying for administration will usually involve

[429] IA 1986, s 2(3)(b).
[430] In cases where a company is in administration or liquidation, the administrator or the liquidator will invariably take on the role of the nominee. See Keay and Walton (n 128) 145.
[431] IA 1986, s 2(2).
[432] *Re Debtor (No.140 IO of 1995)* [1996] 2 BCLC 429.
[433] IA 1986, s 3(2).
[434] Goode (n 130) 513.
[435] Peter Walton, Christopher Umfreville and Lézelle Jacobs, *Company Voluntary Arrangements: Evaluating Success and Failure* (R3 Association of Business Recovery Professionals 2018) 8.
[436] ibid.

additional time and expense, which may undermine the benefit of the CVA.[437] Thirdly, companies that are not 'technically' insolvent may have difficulty satisfying the administration requirement for the company to be unable or to be likely to be unable to pay its debts. In the latter scenario, the solvency of the company prevents it from benefiting from the administration moratorium.

Another option the company may use to overcome the obstacle presented by the lack of a moratorium in the CVA is to initiate the stand-alone moratorium process introduced by CGIA 2020 before initiating the CVA. However, with the restrictions in the new moratorium regime, accessibility to such an option seems limited. These restrictions are illustrated in the following section.

4.1.4 UK Stand-Alone Company Moratorium

4.1.4.1 Overview

One of the significant reforms that CIGA 2020 introduced is a freestanding moratorium that provides a distressed but viable company with breathing space in which to consider its restructuring and rescue options while remaining free from creditor action. The new moratorium procedure was one of the government's proposals for amending the UK debt restructuring regime published in August 2018.[438]

Before CIGA came into force in June 2020, the Schedule A1 CVA moratorium was the only debtor-in-possession restructuring regime in the UK that included a moratorium. However, as the government report observed in 2018, this regime was rarely used in practice and was criticised for being restricted to small companies, for being burdensome for the insolvency practitioner acting as a nominee, for being bureaucratic and for carrying a risk of personal liability.[439] Therefore, the government proposed a new stand-alone moratorium procedure in

[437] Ian F Fletcher, *The Law of Insolvency* (3rd edn, Sweet and Maxwell 2002) 427.

[438] BEIS, *Insolvency and Corporate Governance (Government Response)* (2018) 41ff. The 2018 proposals were based on a consultation published by the UK Insolvency Service in May 2016: Insolvency Service, *A Review of the Corporate Insolvency Framework: A Consultation on Options for Reform* (Insolvency Service 2016). The most significant reforms the CIGA has introduced based on the 2018 proposals are as follows: 1) the introduction of a new stand-alone moratorium procedure; 2) the introduction of a new restructuring plan procedure, which includes a cross-class cramdown mechanism; and 3) prohibition of 'ipso facto' clauses.

[439] BEIS (n 438) 43. As a condition to obtain a small company CVA moratorium available under the omitted Schedule A1 of IA 1986, an insolvency practitioner acting as a 'nominee' had to state that the company CVA proposal had a reasonable prospect of being approved and implemented and that the company was likely to have sufficient funds available to it with the proposed moratorium to enable it to carry on its business. In practice,

August 2018, which was implemented on 26 June 2020 when CIGA 2020 came into effect.[440]As a result of the introduction of the new moratorium procedure, the small company CVA was abolished.

Unlike the administration, the new moratorium is a freestanding procedure. It is not a gateway to a variety of insolvency procedures and may not even be followed by an insolvency procedure if the corporate rescue can be achieved during the moratorium or if the company succeeds in proposing a restructuring plan capable of obtaining the creditors' acceptance.[441] According to the government's explanatory notes on the legislation, the possible rescue outcomes of the moratorium include recovery of the company without further action/process; sale and/or refinancing outside insolvency; the CVA under Part 1 of the IA 1986; a scheme of arrangement under Part 26 of CA 2006; or implementing a restructuring plan under the new Part 26A of CA 2006.[442]

During the moratorium, the incumbent management remains in charge of the company's business, though subject to the supervision of an insolvency practitioner acting as a 'monitor'. The monitor's role is to track the company's compliance with the qualifying conditions throughout the moratorium period.[443]

The moratorium provides the company with a 'payment holiday' with respect to most of its 'pre-moratorium debts' (PMDs),[444] which are any debts or other liabilities that have fallen due either prior to or during the moratorium period but reflect an obligation that was incurred prior to the commencement of the moratorium.[445] However, the following PMDs are exempted from the payment holiday and must be paid during the moratorium period: (1) the monitor's remuneration and expenses; (2) goods or services supplied during the moratorium (which

however, nominees were often hesitant to make such a statement. Such reluctance may be because nominees were not usually in an appropriate position to make such a favourable opinion. Therefore, the concern that nominees may be personally liable for providing a defective opinion may be one of the critical reasons for the rare use of the Schedule A1 moratorium in practice. See Walton, Umfreville and Jacobs (n 435) 8.

[440] 'CIGA 2020' <http://www.legislation.gov.uk/ukpga/2020/12/contents/enacted/data.htm> accessed 28 June 2020.

[441] See Jennifer Payne, 'An Assessment of the UK Restructuring Moratorium' (2021) <https://ssrn.com/abstract=3759730> accessed 2 September 2021; Gerard McCormack, *Permanent Changes to the UK's Corporate Restructuring and Insolvency Laws in the Wake of Covid-19* (Insol-International 2020) 4.

[442] Department for Business Energy and Industrial Strategy, *Corporate Insolvency and Governance Bill (Explanatory Notes)* (HL 2020) 4.

[443] IA 1986, pt A1, ch 5, ss A34 to A41.

[444] IA 1986, pt A1, ch 4, s A18.

[445] IA 1986, pt A1, ch 4, s A18(3).

would otherwise be PMDs, as the relevant contract pre-dated the moratorium); (3) rent for a period during the moratorium (related to a lease that pre-dates the moratorium); (4) wages or salary arising under employment contracts; (5) redundancy payments; and (6) debts or liabilities arising under a contract (or other instrument) involving financial services.[446] According to Payne, excluding these debts from the payment holiday reduces the benefit of the new moratorium procedure in practice.[447]

In addition to the payment holiday, and in common with the administration moratorium, certain creditor actions are precluded by the new moratorium. For example, creditors are prevented from commencing formal insolvency proceedings.[448] Moreover, except with the permission of the court, no forfeiture or re-entry rights may be exercised, no steps may be taken to enforce security interests over the company's property and no legal process (other than certain employment-related proceedings) may be instituted or continued against the company or its property.[449]

4.1.4.2 Access to UK Stand-Alone Moratorium

The new moratorium goes into effect once the directors of a company file certain 'relevant documents' with the court.[450] Those documents include a record of the consent of the proposed party to act as the monitor in relation to the proposed moratorium and a statement from the proposed monitor that the company is an eligible company and that, in the monitor's opinion, 'it is likely that a moratorium for the company would result in the rescue of the company as a going concern'.[451] The initial moratorium lasts for 20 days, which can be extended in the same manner for an additional 20 days and can then be extended again with the consent of the pre-moratorium creditors for up to 12 months from the date of the initial filing.[452] The moratorium is automatically extended when the company proposes the CVA.[453] Moreover, the court has the discretion to extend the moratorium when a scheme of arrangement or the new restructuring plan (Part 26A scheme) is being considered.[454]

[446] IA 1986, pt A1, ch 4, s A18(3).
[447] Payne, 'An Assessment of the UK Restructuring Moratorium' (n 441) 9.
[448] IA 1986, pt A1, ch 4, s A20.
[449] IA 1986, pt A1, ch 4, s A21.
[450] IA 1986, pt A1, ch 2, ss A3 to A8.
[451] IA 1986, pt A1, ch 2, s A6.
[452] IA 1986, pt A1, ch 3, ss A10 to A12.
[453] IA 1986, pt A1, ch 3, s A14.
[454] IA 1986, pt A1, ch 3, s A15.

Although the new moratorium procedure is considered an important reform in the UK restructuring law, some restrictions in the new moratorium regime may limit its use in practice. The first of these is the procedure's narrow ambit of application. In contrast to the administration procedure, the stand-alone moratorium is available only to 'eligible companies'.[455] A company is considered 'eligible' for this type of moratorium unless it is included in the list of exclusions provided under Schedule ZA1.[456] This list is broad, including such business types as banks, insurance companies and investment exchanges and securitisation companies.[457] The exclusion of these types of companies may be justified by the fact that such companies are already subject to a bespoke insolvency regime.[458] However, controversially, the list of excluded business types extends beyond these to also exclude from eligibility companies that have engaged in capital market arrangements incurring a debt of at least £10 million.[459] As a result of this exclusion, numerous small- to medium-sized enterprises (SMEs) and larger businesses with bond financings are not eligible for the stand-alone moratorium.[460] This exclusion was described as unduly restrictive and was subject to a proposed amendment in Parliament.[461] The amendment, however, was not adopted.

Another factor that may limit the use of the stand-alone moratorium in practice is its high threshold.[462] As mentioned previously, the new moratorium can be obtained or continued only when the proposed monitor states that it is likely that the moratorium will result in the rescue of the company as a going concern. This condition implies the objective of the new regime is the rescue of the company as a going concern and that the aim is survival of the company itself, rather than survival of all or part of the company's business. This objective is both more limited and more ambitious than the objective of administration, which is rescuing the company as a going concern, although that objective is rarely achieved in practice.[463]

---

[455] IA 1986, pt A1, ch 1, s A1.
[456] IA 1986, Sch ZA1.
[457] IA 1986, Sch ZA1, paras 3–12.
[458] Emily Saunderson, 'The CIGA Moratorium: A Lifeline for UK Companies?' (2020) 17 International Corporate Rescue 342, 342; Mark Phillips, William Willson and Clara Johnson, 'Corporate Insolvency and Governance Act 2020 A Breath of Fresh Air' [2020] South Square Digest 5, 7.
[459] IA 1986, Sch ZA1, para 13.
[460] Phillips, Willson and Johnson (n 458) 7.
[461] See Viscount Trenchard's contribution to Parliament on Wednesday 21 October 2020 <https://bit.ly/3pXcvx6> accessed 28 January 2021.
[462] Paul Sidle, 'The New Standalone Moratorium Procedure under CIGA 2020' [2020] Corporate Rescue and Insolvency 119, 122.
[463] Glen Davis, 'The Role of the Monitor in a Rescue Moratorium' [2020] South Square Digest 18, 19.

Imposing such a high entry threshold has been argued as providing protection against the moratorium being abused by 'zombie' companies that are not economically viable and are not capable of rescue.[464] At the same time, the application of this strict entry requirement is likely to limit the use of the new moratorium.[465] In order to satisfy this requirement, the proposed monitor is required to be highly certain that the moratorium will result in the rescue of the company as a going concern. Demonstrating such a level of certainty may be very difficult at the early stage when the moratorium protection is sought, which may make the new moratorium inaccessible for a number of distressed but viable companies.[466]

Considering these limitations of the new moratorium procedure, the moratorium provided under the administration process seems more accessible for distressed companies seeking restructuring.

4.1.5 UK Scheme of Arrangement

4.1.5.1 Overview

The scheme of arrangement as set out in Part 26 of CA 2006 is a flexible procedure designed to allow a company to reach a compromise or arrangement with its creditors or members or any class of them.[467] Originally, schemes could only be used by companies in the course of being wound up,[468] but the law has changed to allow schemes to be used for various purposes beyond insolvency, such as for mergers and takeovers and as restructuring tools for companies experiencing financial difficulties.[469] The scheme procedure involves three main steps:[470](1) proposing the scheme and applying to the court to order creditors' or members' meetings to be summoned, (2) meetings of creditors or members to vote on the scheme proposal and (3)

[464] See Phillips, Willson and Johnson (n 458) 10; Payne, 'An Assessment of the UK Restructuring Moratorium' (n 441) 14.
[465] Sidle (n 462) 122; Payne, 'An Assessment of the UK Restructuring Moratorium' (n 441) 18.
[466] Sidle (n 462) 122. A proposal was presented in the House of Lords to lower this threshold from 'would' to 'could', but the proposal was withdrawn without a vote. See CIC Bill, HL Bill 113(a) Amendments for Committee, 10 June 2020 <https://publications.parliament.uk/pa/bills/lbill/58-01/113/5801113(a).pdf> accessed 28 January 2021.
[467] Companies Act (CA) 2006, pt 26, ss 895–901.
[468] Joint Stock Companies Arrangement Act 1870.
[469] See Raquel Agnello and Ben Griffiths, 'Creditor Schemes of Arrangement and Company Voluntary Arrangements in Recent Debt Restructurings' (2013) 6 Corporate Rescue and Insolvency 1, 2; CLR, *Modern Company Law for a Competitive Economy: Completing the Structure* (2000) 206.
[470] *Re Hawk Insurance Co Ltd* [2002] BCC 300.

seeking court sanction of a scheme that has obtained the approval of the appropriate majority of creditors or members.

Like the CVA, and in contrast to the administration procedure, the scheme of arrangement does not involve appointing an insolvency practitioner to formulate and implement the scheme or to manage the company's affairs during the scheme process. Instead, the scheme allows the existing management to stay in control of the company and does not deter it from 'taking remedial action by holding out the real prospect of a ceding of control to an outside IP'.[471]

Despite its significant benefits, the scheme has some drawbacks, which are thought to weaken its effectiveness as a restructuring tool.[472] The most severe defect of the scheme is its lack of a statutory moratorium. The absence of moratorium protection prior to the court sanction of the scheme makes the scheme vulnerable to being frustrated by individual creditors' enforcement actions.[473]

4.1.5.2 Access to UK Scheme of Arrangement

The first step of the scheme procedure after forming the proposed scheme is applying to the court for creditors' or members' meetings to be summoned. Such application can be made by the company, by any of the company's creditors or members or by the administrator or liquidator when the company is in administration or liquidation.[474] Unlike administration, the scheme of arrangement is accessible to both solvent and insolvent companies: the scheme can be proposed and approved regardless of whether the company is in actual or impending insolvency.

After the application is made, the court holds a hearing to decide whether a creditors' meeting should be summoned. The focus of the court at this stage is not on the merits or the fairness of the scheme[475] but on whether the creditors or members should be divided into separate classes for voting purposes. At this stage, the court has wide discretion with which to order the terms

[471] Finch and Milman (n 244) 412.
[472] See Insolvency Service, *A Review of Company Rescue and Business Reconstruction Mechanisms* (DTI 2000) para 43.
[473] See Cork Report, para 406.
[474] CA 2006, s 896(2). The scheme can be used to achieve one of the statutory objectives of administration. See Finch and Milman (n 244) 411.
[475] *Re Telewest Communications Plc (No.1)* [2004] BCC 342.

for conducting creditors' meetings.[476] The issues of classification of creditors, approval and sanction of the scheme are discussed in Chapter 7 of this thesis.

Although it is possible for creditors to initiate a scheme, such initiation is relatively uncommon in practice; schemes are generally commenced by the company.[477] One reason it is unusual for schemes to be initiated by creditors is that the court has no jurisdiction to sanction a scheme that has not been approved by the company.[478] Moreover, as Payne observed, creditors' insufficient knowledge about the debtor company's financial state may prevent them from initiating the scheme without the debtor company's approval.[479] Disclosure obligations, which include disclosing the effect of the scheme, any material interests of the directors of the company and the effect of those interests on the proposed scheme, must be satisfied when the scheme is proposed.[480] As Payne argued, meeting such disclosure obligations would be extremely difficult if not impossible for creditors without support and cooperation from the debtor company.[481] The same point was highlighted by Bork, who stated that creditors do not usually apply for the scheme of arrangement because 'they are not privy to the knowledge required to bring such an application'.[482]

As with the CVA, the absence of the insolvency requirement facilitates the accessibility of the scheme of arrangement and allows companies to take timely rescue steps at the first sign of financial difficulties before their financial condition becomes hopeless.[483] However, due to the scheme's lack of a moratorium, distressed companies may need to commence the scheme after entering into administration or into the new stand-alone moratorium process in order to benefit from the statutory moratorium provided under these two procedures, which is not available under the scheme of arrangement.

[476] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 36–38.
[477] ibid 29.
[478] *Re Savoy Hotel Ltd* [1981] ch 351.
[479] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 31.
[480] CA 2006, s 897.
[481] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 31.
[482] Reinhard Bork, *Rescuing Companies in England and Germany* (OUP Oxford 2012) 144.
[483] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 232.

4.1.6 UK Restructuring Plan Procedure (Part 26A Scheme)

4.1.6.1 Overview

A restructuring plan is a new reorganisation tool introduced by CIGA 2020.[484]It enables a company experiencing financial difficulties to propose a compromise or arrangement with its creditors to restructure its business.[485]The new procedure is found in Part 26A that was added to CA 2006. To a large extent, the new procedure mirrors the existing scheme of arrangement procedure under Part 26 of CA 2006.[486]Under both procedures, for voting purposes, creditors are placed into classes based on their rights. The classes then vote on whether to accept or oppose the plan or scheme, and if accepted, final approval by the court is required to make the plan or scheme binding.

Even though the scheme of arrangement under Part 26 and the latest Part 26A scheme are highly similar in many ways, the two do differ with respect to three matters: the eligibility criteria, voting thresholds and availability of a cross-class cramdown mechanism under the Part 26A scheme.[487] The first matter is considered in the following section, while the second and third matters are illustrated in Chapter 7 of this thesis.

4.1.6.2 Access to UK Part 26A Scheme

Like the scheme of arrangement, the first step of the Part 26A scheme procedure after forming the proposed restructuring plan is applying to the court for creditors' or members' meetings to be summoned. Such application can be made by the company, by any of the company's creditors or members or by the administrator or liquidator when the company is in administration or liquidation. After the application is made, the court holds a convening hearing to decide whether a creditors' meeting should be summoned to vote on the restructuring plan.

In common with the scheme of arrangement, a company does not have to be in actual or impending insolvency to be eligible to use the Part 26A scheme. However, at the convening

[484] See, generally, McCormack, *Permanent Changes to the UK's Corporate Restructuring and Insolvency Laws in the Wake of Covid-19* (n 441) 14FF; Robin Dicker and Adam Al-Attar, 'Cross-Class Cram Downs Under Part 26A Companies Act 2006, Corporate Insolvency and Governance Act 2020, Schedule 9' [2020] South Square Digest; Adam Gallagher, Toby Smyth and Madlyn Gleich Primoff, 'Is the New UK Restructuring Plan a Viable Alternative to Chapter 11?' (2020) 39 American Bankruptcy Institute Journal 24.
[485] Department for Business Energy and Industrial Strategy (n 442) 5.
[486] See Alfino Eu, 'Valuation Issues in the UK Restructuring Plan' (2021) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3776876> accessed 2 September 2021.
[487] CA 2006, s 901G.

hearing, the court will not order a meeting of creditors to vote on the restructuring plan under the Part 26A scheme unless the company satisfies two conditions:[488] (A) the company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern; and (B) the purpose of the plan is to eliminate, reduce, prevent or mitigate the impact of those financial difficulties.

To satisfy condition A, the actual or anticipated financial difficulties must be serious enough to raise the possibility that the company will be unable to continue operations as a going concern.[489] In *Re Virgin Atlantic Airways Ltd*,[490] the court was satisfied that condition A was met in relation to the company where the evidence shows that if the restructuring plan is not approved, the company's capacity to do business as a going concern would be seriously harmed, with the likelihood that it will enter into administration with a view to liquidating the business. Similarly, in *Re DeepOcean*,[491] the applicant companies stated that they had a severe financial underperformance that forced them to continuously require funding from their parent company (DeepOcean Group). However, the parent company was not able to continue providing this financing without putting its financial stability in jeopardy and so was unlikely to continue supplying the funding. Therefore, the court was satisfied that condition A was met because the underperformance that had given rise to the applicant companies' financial difficulties had imperilled their ability to continue to carry on business as a going concern.

Notably, condition B is only concerned with the plan's purpose, which must be to eliminate, reduce, prevent or mitigate the effect of the financial difficulties mentioned in condition A. Condition B is not concerned with the likelihood of the plan accomplishing its purpose. In other words, if the court verifies that the objective of the plan is to address the financial crisis, this would be sufficient to satisfy condition B, even if the possibility of the plan achieving its purpose is in doubt. This establishes a low entry threshold in contrast to the high threshold imposed under the stand-alone moratorium regime, under which the moratorium can be obtained or continued only when the proposed monitor states that it is likely that the moratorium will result in the rescue of the company as a going concern.

[488] CA 2006, s 901A.
[489] *Re DeepOcean* [2021] Bus LR 632.
[490] [2020] BCC 997.
[491] [2021] Bus LR 632.

4.1.7 Concluding Remarks

This part demonstrates that the UK law provides five formal procedures that can be used by distressed companies to restructure their debts: administration, CVA, stand-alone moratorium, scheme of arrangement and Part 26A scheme. The access criteria for these procedures vary significantly. Unlike administration, the absence of an insolvency requirement in the CVA, scheme of arrangement and Part 26A scheme facilitates the accessibility of these procedures and allows companies to take timely rescue steps at the first sign of financial difficulties before their financial condition becomes hopeless. However, the easy access advantage of these three procedures may be undermined by their lack of a moratorium. The absence of moratorium protection makes restructuring processes vulnerable to being frustrated by individual creditors' enforcement actions.

The absence of a moratorium in these three procedures can be overcome by bringing such procedures within the umbrella of either administration or the stand-alone moratorium processes. However, to benefit from these two procedures, a company needs to satisfy the seemingly restrictive access criteria of the two regimes. Administration will mostly function only when a company is insolvent or likely to be insolvent. On the other hand, the stand-alone moratorium regime imposes a higher entry threshold, according to which the moratorium can be obtained or continued only when the proposed monitor states that it is likely that the moratorium will result in the rescue of the company as a going concern.

4.2 Access to Restructuring Procedures from the US Perspective

4.2.1 Overview of the US Restructuring Regime

Corporate reorganisation law in the United States is rooted in what is called a 'federal equity receivership'. For a long time, especially between the late 19th and early 20th centuries, the US Statutory Bankruptcy Law provided no satisfactory alternative to liquidation for dealing with corporate failure.[492] Even the first federal comprehensive bankruptcy statute, Bankruptcy Act 1898, was centred on the liquidation rather than the rehabilitation of distressed companies. This legislation governed the bankruptcy of both individuals and businesses and provided for a full discharge but did not provide for a reorganisation process for the distressed debtor.[493]

The lack of a viable statutory procedure to deal with corporate failure caused severe problems for the railroad industry in the 19th century.[494] The industry was experiencing dreadful financial difficulties, but no appropriate solution was available through federal bankruptcy law. At the time, keeping the railroads operating was more important than the unwieldy liquidation of railroads' assets spread across many states.[495] These factors and public interest in maintaining the operation of railroads throughout the country contributed to the need to reorganise the distressed railroad companies. To address this need and to fill the statutory gap, the federal equity receivership was applied.[496]

A receivership was usually initiated by a creditor petitioning the federal court to exercise its equity jurisdiction and appoint a receiver to manage the debtor company's assets. The receiver would take title to the assets, halting creditor collection attempts. Furthermore, the receiver had the authority to keep the debtor's business operating while looking for a buyer for the assets, thus, preserving the going concern value for the assets. Creditors were paid out from the proceeds of the receiver's foreclosure sale of the debtor company's assets.[497]

Another milestone in the history of US corporate rescue law dates back to 1938, when three rehabilitation chapters were enacted under the Chandler Act of 1938. Each chapter provided a

[492] Bussel and Skeel, JR (n 4) 525.
[493] Richard F Broude, 'How the Rescue Culture Came to the United States and the Myths That Surround Chapter 11' (2000) 16 Tolley's Insolvency Law and Practice 1, 3.
[494] Tabb, 'The History of the Bankruptcy Laws in the United States' (n 106) 21.
[495] Bussel and Skeel, JR (n 4) 525.
[496] See Troy A McKenzie, 'Bankruptcy and the Future of Aggregate Litigation: The Past as Prologue?' (2013) 90 Wash. UL Rev. 839, 851.
[497] See Tabb, *Law of Bankruptcy* (n 279) 1043.

different form of reorganisation procedure. Chapter X, 'Corporate Reorganization', applied to large companies with publicly held debt or stock; Chapter XI, 'Arrangements', applied to smaller companies; and Chapter XII 'Real Property Arrangement by Persons other than Corporation' was concerned with real estate arrangements for individuals or other noncorporate entities.[498] Subsequently, these three business reorganisation chapters merged into a single chapter, the current Chapter 11 of Bankruptcy Code 1978.

The purpose of Chapter 11 'is to provide a debtor with legal protection in order to give it the opportunity to reorganize, and thereby to provide creditors with going-concern value rather than the possibility of a more meager satisfaction through liquidation'.[499] Warren and Westbrook argued that Chapter 11 merits a prominent position among the exceptional laws that have shaped the American economy and society and then reverberated throughout the globe.[500] Indeed, Chapter 11 has been commonly cited as a gold standard for corporate restructuring that many jurisdictions have tried to emulate.[501]

A Chapter 11 case starts with the filing of a petition in bankruptcy court. The filing of the petition triggers the automatic stay that prevents individual creditors from taking actions against the company and its assets without court permission. The petition filing, in most Chapter 11 cases, does not result in displacement of the incumbent management, which remains in control of the company's operations during the reorganisation procedures. All the quotidian operations of the company and its investment and financing decisions are controlled by the management in its capacity as a debtor-in-possession. Moreover, within the first 120 days after the petition filing, the debtor has the exclusive right to propose a Chapter 11 plan, which would then be put to the creditors for a vote. Finally, after obtaining the creditors' approval, the plan must be confirmed by the court to be binding.

[498] See Alfred N Heuston, 'Corporate Reorganizations Under the Chandler Act' (1938) 38 Colum L Rev 1199.
[499] *In re the Gibson Group, Inc*, 66 F3d 1436, 1442 (6th Cir 1995).
[500] Elizabeth Warren and Jay Lawrence Westbrook, 'The Success of Chapter 11: A Challenge to the Critics' (2008) 107 Mich L Rev 603, 604.
[501] See Meng Seng Wee, 'The Singapore Story of Injecting US Chapter 11 into the Commonwealth Scheme' (2018) 15 European Company and Financial Law Review 553; Schwehr (n 6) 11; Bob Wessels and Stephan Madaus, 'Restructuring Reform with Pre-Insolvency Proceedings – Where Is the EU Heading To?' in Jennifer Gant (ed), *Harmonisation of European Insolvency Law* (INSOL-Europe 2017) 202; Elizabeth Warren, *Chapter 11: Reorganizing American Businesses: Essentials* (Aspen Publishers 2008) 15.

4.2.2 Access to US Chapter 11

Typically, Chapter 11 is commenced voluntarily when the company files a petition with the bankruptcy court. The US bankruptcy code also permits the involuntary commencement of Chapter 11 by creditors, although such commencement is subject to certain restrictions that do not exist in the voluntary commencement context. The voluntary and involuntary routes into Chapter 11 are discussed in turn next.

When Chapter 11 is filed voluntarily, which is the most common scenario, the company is not required to be insolvent. By not imposing insolvency as an eligibility requirement to access Chapter 11, the US bankruptcy code permits the strategic use of Chapter 11, enabling companies to file for Chapter 11 for reasons other than insolvency.[502] Indeed, Chapter 11 has been used by businesses in many ways for various reasons, such as to reduce labour costs and to resolve potential tort liabilities.[503]

One of the most notable examples of the use of Chapter 11 outside the scope of insolvency is the case of *Manville*.[504] In 1982, Johns-Manville Corporation filed for Chapter 11 to resolve an enormous dilemma it faced resulting from an uncontrollable increase in asbestos lawsuits brought against it due to its long-time use of products containing asbestos, which were discovered to have caused health injuries for many people. Another example of the strategic use of Chapter 11 is the case of *Texaco* in the late 1980s.[505] Prior to filing for Chapter 11, Texaco was ordered by a Texas jury to pay its rival Pennzoil $10.53 billion in damages for Texaco's unlawful interference in Pennzoil's attempts to acquire Getty Oil.[506] By filing for Chapter 11, Texaco successfully prevented Pennzoil from enforcing the award judgment; subsequently, Texaco reached an agreement with Pennzoil to reduce the awarded damages from $10.53 billion to $3 billion.[507]

Although the lack of an insolvency requirement for access to US Chapter 11 allows the use of the reorganisation regime for tactical purposes, solvent companies are not always permitted to

[502] For more information about the strategic Chapter 11 provision, see Kevin J Delaney, *Strategic Bankruptcy: How Corporations and Creditors Use Chapter 11 to Their Advantage* (2nd edn, Univ of California Press 1998).
[503] Bruce G Carruthers and Terence Charles Halliday, *Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States* (Clarendon Press Oxford 1998) 266.
[504] *In re Johns-Manville Corp*, 36 BR 727 (Bankr S D N Y 1984).
[505] *In re Texaco Inc*, 84 BR 893 (Bankr S D N Y 1988).
[506] *Pennzoil Co v Texaco Inc*, No 84-05905 (Tex Dist Dec 10, 1985).
[507] William C Whitford, 'What's Right About Chapter 11' (1994) 72 Wash. ULQ 1379; Delaney (n 502) 152.

file for Chapter 11. Indeed, a petition for Chapter 11 must be filed in good faith.[508] The absence of good faith when filing for Chapter 11 may result in the court's dismissal of the petition upon the creditors' request.[509] The doctrine of 'good faith filing' developed through case law, and the courts have defined that doctrine in different formulations. In the case of *Marsch,*[510] the Ninth Circuit described the good faith requirement as a test to determine 'whether a debtor is attempting to unreasonably deter and harass creditors or attempting to effect a speedy, efficient reorganization on a feasible basis'. In the case of *SGL Carbon,*[511] the Third Circuit stated that the good faith doctrine required a Chapter 11 filing to have a 'valid reorganizational purpose'.

The issue in the case of *SGL Carbon* was to determine if a Chapter 11 'petition filed by a financially healthy company in the face of potentially significant civil antitrust liability complies with the requirements of the Bankruptcy Code'.[512] SGL Carbon Corporation, a producer and retailer of graphite products, had filed for Chapter 11 after becoming a target of a class-action antitrust lawsuit. The company's petition was challenged by some creditors, who called on the court to dismiss the case on the grounds that the company filed for Chapter 11 in bad faith as a 'litigation tactic designed to frustrate the prosecution of the civil antitrust claims pending against SGL'. The court in the first instance refused to dismiss the case on bad faith grounds and held that the filing complied with the objectives of Chapter 11 because the litigation was threatening the operations of SGL by 'distracting its management, was potentially ruinous and could eventually force the company out of business'.[513] However, in the appeal hearing, the Third Circuit reversed the judgment of the first instance court and concluded that SGL Carbon's petition for Chapter 11 had not been filed in good faith and may be dismissed. The Circuit described the company's filing as 'premature' and having been made for an inappropriate purpose, which was purely to obtain a tactical advantage against the plaintiffs in the antitrust litigations. The court asserted that although a company is not required to be insolvent to file for Chapter 11 and the bankruptcy code promotes early filing to allow distressed companies to reorganise before their situation becomes unsalvageable, encouraging early filing does not mean that 'premature filing' or filing a petition that lacks a 'valid

[508] See Ali M M Mojdehi and Janet Dean Gertz, 'The Implicit Good Faith Requirement in Chapter 11 Liquidations: A Rule in Search of a Rationale' (2006) 14 Am Bankr Inst L Rev 143.
[509] ibid.
[510] *In re Marsch*, 36 F3d 825, 828 (9th Cir 1994).
[511] *In re SGL Carbon Corp*, 200 F3d 154 (3rd Cir 1999).
[512] ibid at 156.
[513] ibid at 158.

reorganizational purpose' is permissible.[514] The conclusion that can be drawn from the case of *SGL Carbon* is that, while insolvency is not a requirement for voluntary filing for Chapter 11, petitions by solvent companies must have a 'valid reorganizational purpose', and the absence of such purpose will justify the dismissal of the filing on bad faith grounds.

Although rarely occurring in practice, Chapter 11 may be accessed involuntarily. If a company has 12 or more creditors, the company may be involuntarily forced into Chapter 11 if an involuntary petition is filed by 3 or more creditors holding unsecured, non-contingent, undisputed claims with an aggregate value of $10,000 or more and the company is 'generally not paying [its] debts as such debts become due unless such debts are the subject of a bona fide dispute'.[515] If the company has fewer than 12 creditors, the petition only needs to be filed by 1 or more of the qualified creditors holding unsecured, non-contingent, undisputed claims with an aggregate value of $10,000 or more.[516]

Most of the difficulties in practice relate to the debtor's 'general failure to pay' its debts.[517] The code does not define the term 'generally not paying'; the court determines whether the debtor's failure to pay its due debt is general on a case by case basis.[518] In deciding whether the debtor's default is general, the court considers various factors, such as the number of unpaid claims, the amount of such claims, the materiality of the non-payments and the debtor's overall conduct in its financial affairs.[519] An important aspect is that default on one single debt would not usually be sufficient to meet the 'general failure to pay' standard unless such single debt constituted a substantial portion of the total debts.[520]

The 'general failure to pay' is a variant of the 'cash flow' test. The difference between the 'general failure to pay' standard and the traditional cash flow test is that the focus of the cash flow test is on the ability of the debtor to pay its due debts, while the focus of the 'general failure to pay' standard is on whether the debtor is 'in fact' paying its debts. The ability of a

[514] ibid at 164.
[515] Bankruptcy Code, s 303(b)(1).
[516] Bankruptcy Code, s 303(b)(2).
[517] Tabb, *Law of Bankruptcy* (n 279) 157.
[518] Robert E Ginsberg and others, *Ginsberg & Martin on Bankruptcy* (5th edn, Wolters Kluwer Law & Business 2018) 66.
[519] See *In re Harmsen* 320 BR 188 (BAP 10th Cir 2005).
[520] See, eg, *In re Century/ML Cable Venture* 294 BR 9 (Bankr S D N Y 2003); *In re Euro-American Lodging Corp*, 357 BR 700 (Bankr S D N Y 2007).

debtor to pay its debts is irrelevant to determining whether the involuntary petition is appropriate.[521]

Creditors do not usually have ready access to the evidence needed to establish the general failure of the company to meet its current obligations. This inability to access details on the financial condition of the debtor company is thought to be an obstacle that discourages creditors from initiating involuntary proceedings against defaulted companies under Chapter 11.[522]Nevertheless, a company's creditors still have significant influence in pushing the company to initiate rehabilitation procedures. Indeed, companies often apply for the restructuring procedure because of pressure from creditors.[523] Secured creditors, especially, have a powerful influence in compelling a company to initiate restructuring procedures by threatening to enforce their security interests. Therefore, as indicated by Block-Lieb, 'the line between voluntary and involuntary filings is an ambiguous one because debtors often file voluntary petitions in reaction to creditors' collection efforts'.[524]

The conclusion here is that the insolvency of the debtor is not required for voluntary filing for Chapter 11, but such filing must have a valid reorganisational purpose. Filing for voluntary Chapter 11 merely to gain tactical advantages is not permissible. The debtor's failure to pay its due debts is, on the other hand, grounds for involuntary Chapter 11 relief, and the focus of the court in determining whether such grounds are met is on whether the debtor is actually not paying its debts, not on the debtor's ability to pay such debts.

[521] *In re Green Hills Dev Co LLC*, 445 BR 647 (Bankr S D Miss 2011). See also Tabb, *Law of Bankruptcy* (n 279) 157; Ginsberg and others (n 518) 65.
[522] Susan Block-Lieb, 'Why Creditors File so Few Involuntary Petitions and Why the Number Is Not Too Small' (1991) 57 Brook. L. Rev. 803, 837; Zinian Zhang, 'Commencement of Corporate Reorganisations in China from an Anglo-American Perspective', *Insights from theory into restructuring and phoenixing activity* (INSOL International Academics' Colloquium 2016) 30.
[523] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 125; Lynn M LoPucki, 'The Debtor in Full Control--Systems Failure under Chapter 11 of the Bankruptcy Code' (1983) 57 Am. Bankr. LJ 99, 115.
[524] Block-Lieb (n 522) 804.

4.3 Access to Restructuring Procedures Under Saudi Law

As illustrated in the previous chapter, restructuring procedures under Saudi BL 2018 are court central. The procedures can only be initiated with the court's approval after a hearing is held to consider the commencement application. Such an application can only be made by the debtor under the Preventative Settlement (PS) procedure,[525] whereas the debtor, the creditor or a competent authority (when the debtor is a regulated entity) may apply to the court to commence the Financial Restructuring (FR) procedure.[526] Also, the commencement of the FR procedure may be ordered by the court, on its own motion or upon the request of a person with interest, upon the court's decision to terminate the PS procedure.[527]

When considering whether to order the commencement of restructuring procedures under the BL 2018 regime, the court must be satisfied that certain requirements have been met. The most important requirements among these are that 1) the company is or is likely to become insolvent (insolvency test),[528] and 2) the company's activities are likely to continue if the restructuring is commenced and the creditors' claims will be settled within a reasonable timeframe (viability test).[529] These two requirements are examined in light of the UK and the US perspectives provided in the first two parts of the chapter.

4.3.1 Actual and Impending Insolvency Under Saudi Law

A crucial point to consider when discussing the commencement of restructuring procedures is whether insolvency is required for the use of such procedures. Under Saudi law, the two restructuring procedures under the provisions of BL 2018 cannot be commenced unless the court is satisfied that the debtor company is insolvent, distressed or likely to suffer from financial difficulty leading to distress. The law defines an 'insolvent' debtor as one whose debts have consumed all its assets and defines a 'distressed' debtor as one who has stopped paying its debts as they fall due.[530] These definitions indicate that the law requires the debtor company to pass either of the two traditional insolvency tests (balance sheet and cash flow) to have access to either the PS or FR procedures. Moreover, the law expands such accessibility to include companies that are not yet technically insolvent but are likely to suffer financial

[525] BL 2018, art 13.
[526] BL 2018, art 42.
[527] BL 2018, art 41.
[528] BL 2018, arts 15(1)(a)(ii), 47(2)(a)(ii).
[529] BL 2018, arts 15(1)(a)(i), 47(2)(a)(i).
[530] BL 2018, art 1.

difficulties that will lead to the cessation of paying due debts. However, the term 'likely' has not been tested in practice yet, as all pending restructuring cases concern either cash flow or balance sheet insolvent companies. Thus, whether the courts will interpret the term 'likely' generously to allow commencement of the reorganisation process when a real prospect of insolvency exists, or if the term will be given a stricter interpretation to mean that the insolvency is more probable than not, remains uncertain.

The courts have applied the insolvency requirement strictly when considering applications for the commencement of restructuring procedures under BL 2018. In practice, the first issue the courts usually address when considering applications for the commencement of the PS or FR is whether the debtor company is or is likely to become insolvent.[531]

In imposing actual or impending insolvency as a requirement for access to restructuring procedures, Saudi law is similar to the UK administration regime, which mostly functions only when a company is insolvent or likely to be insolvent. This is different from the US approach, in which insolvency is not required in the case of the voluntary filing of Chapter 11, but such filing may be dismissed by the court if it finds that the petition was not filed in good faith.

One of the main criticisms of imposing the insolvency requirement in restructuring processes is that it prohibits early attempts to rescue distressed businesses.[532] Arguably, because of this requirement, companies are not allowed to commence rescue procedures until the possibility of being rescued is no longer feasible. Seeking rehabilitation in the early stages of financial difficulties is critical to the success of the rehabilitation process, but by imposing the insolvency test, such early rescue attempts may be hindered. In addition, the insolvency entry requirement for restructuring procedures may negatively impact the interests of creditors. An individual creditor can pre-empt the insolvency test once that creditor becomes aware that the company stands a chance of becoming insolvent. Hence, individual creditors may seize assets that, under insolvency, would be distributed to the creditors as a whole in an orderly manner.[533]

However, under the UK administration process, some factors may justify imposing actual or impending insolvency as an entry requirement. The law aims to limit the use of rescue

[531] See, eg, case number 523 (2020); case number 1960 (2020); case number 3289 (2019).
[532] See McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 119; Goode (n 130) 391.
[533] See Anderson and Morrison (n 379) 91.

procedures to companies that are in real need of rescue.[534] The concern that the lack of an insolvency requirement would encourage the use of restructuring procedures for merely strategic purposes may be legitimate, in which case imposing the insolvency requirement would avoid such an abuse of procedures.[535]

However, while this justification for the insolvency test may be relevant and acceptable in the context of the administration procedure in the UK, such a justification may not be relevant or valid under the Saudi BL 2018 restructuring procedures. The minimal court involvement in the administration procedure makes imposing the insolvency requirement necessary to counter the abusive use of the procedures. The position is fundamentally different under Saudi law, where the restructuring procedures are heavily subject to judicial supervision. In this respect, the two restructuring procedures under Saudi BL 2018 are closer to those under US Chapter 11, as both are court central, and neither offers an out-of-court route to commencing the procedures, unlike the administration procedure under UK IA 1986.

The lack of an insolvency test under US Chapter 11 may be justified on the basis that the procedure begins with the filing of a petition to the court. That gives the courts the opportunity to dismiss the petition for 'cause', such as the absence of good faith. As such, the court's role in the Chapter 11 process, including its ability to dismiss the case based on the absence of good faith, may provide sufficient protection against the abusive use of the procedure, thus making the insolvency requirement unnecessary.[536] This point was highlighted by the Australian Corporations and Markets Advisory Committee in 2004 when it considered easing the Voluntary Administration (VA) procedure entry threshold test, which required that 'the company is insolvent, or likely to become insolvent at some future time'.[537] The Committee rejected the proposal to ease this threshold and voted against adopting any of the alternative tests that had been proposed. One of these rejected tests was a 'good faith' test similar to that

[534] *Re Colt Telecom Group Plc (No 2)* (2002) EWHC 2815 (ch) at 26.
[535] Anderson and Morrison (n 379) 90.
[536] ibid.
[537] Corporations Act 2001, section 436A. The Australian VA procedure, found in Part 5.3A of the Corporations Act 2001, is quite similar to the UK administration regime. The procedure involves the appointment of a qualified insolvency professional (the 'voluntary administrator') who assumes complete control of an insolvent or near-insolvent debtor company. The administrator is required to draft a plan for the future of the company's business, known as a Deed of Company Arrangement (DOCA), in consultation with creditors. If the creditors agree to this plan, it is then executed. If no agreement is reached on the DOCA, the company will proceed to winding-up procedure. See Andrew Keay, 'A Comparative Analysis of Administration Regimes in Australia and the United Kingdom' in Paul J Omar (ed), *International Insolvency Law: Themes and Perspectives* (Ashgate Publishing Limited 2008); Saul Fridman, 'Voluntary Administration: Use and Abuse' (2003) 15 Bond L. Rev. i.

found in US Chapter 11. The Committee justified its rejection to adopt the good faith test as follows: 'A good faith only test would not be appropriate unless there was an extensive increase in the level of judicial supervision to test the basis for the application, as occurs under Chapter 11'.[538]

The extensive level of judicial supervision that arguably justifies the lack of an insolvency requirement under US Chapter 11 is established in the context of restructuring procedures under the BL 2018 regime. In fact, judicial supervision under BL 2018 is more extensive than it is under US Chapter 11, as restructuring procedures under BL 2018 can only be initiated with the court's approval after a hearing is held to consider the commencement application, which differs from the initiation of voluntary restructuring under US Chapter 11, which commences automatically upon voluntary petition by the debtor to open the procedure and does not require court approval. Under Chapter 11, the court will only intervene in the commencement of the procedure if the voluntary petition has been challenged by creditors or in the case of involuntary filing. Given the high level of court involvement in the commencement of restructuring procedures under BL 2018 and the safeguard that involvement provides against the abuse of such procedures, the existence of insolvency as an entry requirement seems redundant. Therefore, due to the similarity between US Chapter 11 and Saudi restructuring regimes regarding the level of judicial supervision over the restructuring process, easing the current insolvency threshold in Saudi bankruptcy law and adopting into it a good faith test like that which exists under the US Chapter 11 regime seems appropriate.

Another factor that justifies easing the insolvency threshold for entry into restructuring procedures under BL 2018 is the Saudi law's lack of alternative restructuring regimes for companies that are experiencing financial difficulties but fall short of actual or likely insolvency. What may limit the drawbacks of the insolvency requirement under the UK administration regime is the availability of other formal restructuring procedures, such as the CVA and scheme of arrangement, for which insolvency is not an entry requirement, despite the defects in these two procedures compared to administration.[539] Such an alternative formal restructuring regime is not available in the context of Saudi law; therefore, the only possible

[538] Corporations and Markets Advisory Committee, *Rehabilitating Large and Complex Enterprises in Financial Difficulties: Report* (2004) 25.

[539] The availability of alternative restructuring regimes for companies experiencing financial difficulties that fall short of actual or likely insolvency was used by the Australian Corporations and Markets Advisory Committee as a justification to reject the proposal to ease the current insolvency threshold of entry into the VA procedure; ibid.

resolution for a solvent company in need of restructuring is to reach an amiable informal agreement with all its creditors to restructure its debts, but such an agreement is usually difficult to reach, especially for larger companies with a greater number of creditors.

In summary, the fundamental difference between Saudi reorganisation processes and the UK administration regime in relation to the level of court involvement in the restructuring process, and the absence of alternative restructuring regimes for companies with financial difficulties that fall short of actual or likely insolvency in the Saudi legal system, make relaxing the current insolvency prerequisite for entering into reorganisation procedures under BL 2018 by adopting the good faith test in its stead appropriate, in the opinion of the author.

4.3.2 Viability of Business Subject to Restructuring Procedures Under Saudi Law

In addition to the actual or impending insolvency of the company, the viability of the company is another fundamental condition the court must determine and consider when deciding whether to order the commencement of the restructuring procedure. Applying the provisions of BL 2018, the court cannot order the commencement of either the PS or FR unless it is satisfied that 'the company's activities are likely to continue, and the creditors' claims will be settled within a reasonable timeframe' if the court approves commencement of the restructuring procedure.[540] The court's focus when conducting the viability test is on whether the company, given the opportunity to benefit from the restructuring procedure, is likely to overcome its financial distress and settle its debts with creditors within a reasonable period. At this stage, the court is not concerned with the feasibility of the restructuring plan but, rather, with the company's ability to overcome financial distress and continue to operate if restructured.[541]

The viability requirement may reflect the legislature's desire to limit the use of restructuring procedures to those circumstances for which the prospects of the successful reorganisation of the business are good.[542] Liquidation seems to be the only resolution when a company's financial conditions are hopeless, making the continuation of its operation unlikely. The court's rejection of an application to commence the restructuring procedure when a company's

[540] BL 2018, arts 15(1)(a)(i), 47(2)(a)(i).
[541] Suliman (n 340) 127.
[542] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 201.

financial conditions are disrupted to a hopeless extent may preserve the creditors' returns, which may otherwise be diminished due to the probable failure of the restructuring.[543]

An example that illustrates the way the court applies the viability test is case number 9794,[544]which concerns an application made by an insurance company to the court to commence the FR procedure after the company incurred huge losses at the end of 2018, with debts exceeding 115 million Saudi riyals. One of the factors the court considered when deciding to open the procedure was that the company's shareholders at the extraordinary general meeting (EGM) had agreed to increase the company's capital, thereby reducing the percentage of losses and increasing the possibility of a successful restructuring. Another reason that convinced the court of the company's viability was the fact that the company previously suffered accumulated losses in 2014 and 2015 amounting to about 138 million Saudi riyals and was able to overcome the losses, ultimately achieving net profits exceeding 60 million Saudi riyals in 2016. Significantly, based on these two factors, the court concluded that the company's business was likely to continue and that the creditors' claims were likely to be settled within a reasonable timeframe. Accordingly, the court ordered the commencement of the FR process.

Another example of how courts apply the viability test is case number 13619,[545] which concerns an application made by a construction company to the court to commence the FR procedure after the company incurred huge losses with debts exceeding 32 million Saudi riyals. The court rejected the application to commence the FR procedure for the company on the grounds that the company no longer owned the equipment and tools necessary to practice contracting activity and it no longer owned any assets. Therefore, according to the court, the company's business was not likely to continue.

From a comparative perspective, the viability test under Saudi restructuring law seems like the high entry threshold imposed under the UK stand-alone moratorium regime. Under this regime, the moratorium can be obtained or continued only when the proposed monitor states that it is likely that the moratorium will result in the rescue of the company as a going concern. In contrast, neither justification for the viability of a business or the probability of its being

[543] Finch and Milman (n 244) 201.
[544] (2019).
[545] (2019).

reorganised successfully is explicitly required for commencement of US Chapter 11, and neither are they requirements for the commencement of the UK administration, CVA, scheme of arrangement and Part 26A scheme. This difference may be explained by looking at the multiple possible outcomes these procedures may seek to achieve compared with the restructuring procedures under BL 2018 and the UK stand-alone moratorium, for which the only aim is the reorganisation of the distressed company. More specifically, pure corporate rescue, as opposed to business rescue, is the only outcome BL 2018 reorganisation procedures and the UK stand-alone moratorium are designed to achieve. The two regimes are not constructed to function in situations in which the objective of rescuing a company as a going concern is unachievable. This contrasts with the position under US Chapter 11. Although its primary objective is the reorganisation of a business experiencing financial difficulties, Chapter 11 can also be used as an efficient means of liquidation.[546]

The same can be said about the administration process in the UK, as 'rescuing the company as a going concern' is not the only objective of this process. Instead, the administration procedure aims to achieve a hierarchy of objectives: to rescue the company as a going concern; failing that, to accomplish a better result for the creditors as a whole than would be likely if the company were wound up; and failing that, to realise the property in order and make distribution to one or more secured or preferential creditors.[547] Also, the CVA, scheme of arrangement and Part 26A scheme may be proposed as stand-alone procedures or to supplement other main procedures, such as administration or liquidation. The scheme of arrangement, especially, can be utilised to achieve an outcome other than corporate restructuring, such as a merger or takeover.

Therefore, imposing the viability test to determine the eligibility of the company to enter into restructuring procedures under the BL 2018 regime seems reasonable and compatible with the

[546] The Chapter 11 plan may 'provide for the sale of all or substantially all of the property of [the debtor], and the distribution of the proceeds of such sale among holders of claims or interests'- Bankruptcy Code § 1123(b)(4). In fact, Chapter 11 may be a more cost-effective device for liquidation than Chapter 7, because under Chapter 11, the management of the company would remain in possession and control over the liquidation process, while under Chapter 7 a trustee would be appointed to administrate the process of liquidating the company's assets. See Scott D Cousins, 'Chapter 11 Asset Sales' (2002) 27 Del. J. Corp. L. 835, 837. Chapter 7 of the US Bankruptcy Code is titled "Liquidation". 'Chapter 7 provides for the independent liquidation (i.e., sale) of the debtor's assets owned at the time of the bankruptcy filing and distribution of the net proceeds of the sale to creditors, pro rata, in accordance with statutory rules.' David G Epstein and Steve H Nickles, *Principles of Bankruptcy Law* (2nd edn, West Academic Publishing 2017) 6.

[547] IA 1986, Schedule B1, para 3.

fact that rescuing the company as a going concern is the only objective of these procedures. The procedures are not designed to function in circumstances in which such an objective is unachievable. Thus, the viability test may serve as a filtering tool to prevent the procedures from being used by hopeless companies as a method to delay inevitable liquidation.

4.4 Conclusion

This chapter discussed the accessibility of restructuring procedures under Saudi BL 2018. Mainly, the chapter examined the criteria that should be satisfied to access restructuring procedures. The access criteria should serve two essential policies. On the first hand, the requirements should be designed to enable the distressed company to access rehabilitation procedures at an early stage of financial difficulties and before it is too late for the company to be rescued. On the other hand, the access criteria should not be too easy to satisfy to allow the abusive use of restructuring procedures. While the latter policy may be served under the Saudi restructuring regime, the former does not seem to be served.

When considering whether to order the commencement of restructuring procedures under the BL 2018 regime, the court must be satisfied that two requirements have been met: the actual or impending insolvency and viability of the company subject to the restructuring process. The imposing of the insolvency test as an entry requirement for reorganisation procedures under BL 2018 is, in the opinion of the author, redundant and may hinder early attempts at rehabilitation, which is a statutory objective of BL 2018. The existence of the insolvency test in the context of the UK administration procedure has been determined to be likely to provide protection against the abusive use of the procedure, considering the minimal court involvement in the commencement process of the UK procedure. However, the position is fundamentally different under the BL 2018 restructuring processes, which are court central and subject to an extensive level of court supervision. Similar to the US Chapter 11 process, the high level of court involvement in the commencement process of the BL 2018 restructuring proceedings provides sufficient protection against the abuse of such actions. Considering the extent of judicial protection provided, the insolvency test seems to be not only unnecessary but, in fact, problematic. Accordingly, the author advocates for relaxing the current insolvency test and employing a good faith requirement similar to what is contained in US Chapter 11.

Proving the viability of the company subject to the reorganisation process is another main entry requirement of BL 2018 restructuring procedures. Unlike the insolvency test, the viability requirement seems justified and reasonable when such requirement is considered in the context of the statutory objective that BL 2018 reorganisation processes are purposed to achieve. As rescuing the company is the only goal such processes aim to accomplish, the viability test serves as a filtering tool to prevent hopeless companies, which have no reasonable prospect of continuation, from using the reorganisation procedures to delay their inevitable liquidation.

Having discussed the access requirements for restructuring procedures under Saudi BL 2018, the following chapter examines control of the debtor company during the reorganisation period, which, if handled effectively, will enhance the possibility of success for the rehabilitation process.

Chapter 5: Control of The Company's Business During The Restructuring Process

The management of a company's affairs during the restructuring process is critically important because the success of the reorganisation process depends heavily on whether such management is exercised properly. This chapter aims to closely examine the issue of control over the debtor company's affairs during the reorganisation process under the Saudi BL 2018 regime in light of the relevant UK and the US laws. The chapter is divided into two parts. The first part describes the two leading global models for corporate reorganisation, i.e. the debtor-in-possession (DIP) model and the practitioner-in-possession (PIP) model. Following these descriptions, normative arguments promoting the two models and identifying their relative shortfalls are presented. The second part of this chapter discusses the two managerial models for corporate reorganisation procedures available under Saudi law: the DIP model adopted under the PS process and the co-determination model adopted under the FR process. The advantages and drawbacks of both models are examined to determine their effectiveness and suitability for the Saudi legal environment.

5.1 Managing Firms in Reorganisation: Two Models of Control

Generally speaking, there are two popular approaches to the management of firms undergoing reorganisation.[548] The first is the debtor-in-possession (DIP) model established in US Chapter 11. This model allows the incumbent management to stay in control of the company's affairs during the period of restructuring. The second model is practitioner-in-possession (PIP), found in the UK administration procedure. This model mandates that control of the company's business be removed from the incumbent management in favour of an appointed official practitioner. In this part of Chapter 5, the mechanics of these models are examined, and their advantages and weaknesses are discussed.

[548] See, generally, Qi Lijie, 'Managerial Models During the Corporate Reorganization Period and Their Governance Effects: The UK and US Perspective' (2008) 29 Company Lawyer 131.

5.1.1 The US Approach: Debtor-in-Possession

The debtor-in-possession (DIP) model for management of a company's affairs during the restructuring process is considered the distinguishing characteristic of US Chapter 11.[549] The DIP model mandates that the pre-petition management of the distressed company remain in control of the company and administrate the reorganisation process through to its completion.[550] The daily operations of the company are controlled by the incumbent management, who enjoys a wide range of power, including making investment and financing decisions.[551] The management also has the power to decide which route the company should take, either reorganisation or liquidation.[552] Moreover, the right to file a reorganisation or liquidation plan is exclusively granted to the incumbent management as the DIP for the first 120 days following the date of the order for relief.[553] In its role as the DIP, the incumbent management of the debtor company obtains the powers, rights and duties of the trustee. This was explicitly expressed by the US Supreme Court, which stated that the adoption of DIP 'is premised upon an assurance that the officers and managing employees can be depended upon to carry out the fiduciary responsibilities of a trustee'.[554] Thus, the directors of the company must exercise their control not only in the interests of the shareholders but also in the interests of the company's creditors.[555]

The DIP is not the only method by which the Chapter 11 process can be administrated. While the DIP model is the norm in most Chapter 11 cases, in exceptional circumstances, a trustee may be appointed by the court upon the request of a party in interest or the US Trustee 'for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management'[556] or 'if such appointment is in the interests of creditors, any

[549] Tabb, *Law of Bankruptcy* (n 279) 1049.
[550] Section 1107 of the bankruptcy code states that 'a debtor in possession shall have all the rights, …and powers, and shall perform all the functions and duties …of a trustee serving in a case under this chapter'.
[551] Section 364 of the bankruptcy code provides the debtor with the opportunity to receive credit necessary to fund the restructuring case by offering the post-petition lenders priority over administrative expenses or pre-petition secured claims.
[552] Section 1123(b)(4) of the bankruptcy code provides that the Chapter 11 plan 'may provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among holders of claims or interests'.
[553] Bankruptcy Code, s 1121(b).
[554] *Commodity Futures Trading Comm'n v. Weintraub* 471 US 343, 356 (1985).
[555] Bussel and Skeel, JR (n 4) 532. For more discussion on this dual role of the directors, see Daniel B Bogart, 'Liability of Directors of Chapter 11 Debtors in Possession: "Don't Look Back--Something May Be Gaining On You"' (1994) 68 Am Bankr LJ 155.
[556] Bankruptcy Code, s 1104(a)(1).

equity security holders, and other interests of the estate'.[557] Moreover, section 1104(e) provides that the US Trustee shall request the appointment of a trustee 'if there are reasonable grounds to suspect that current [management] . . . participated in actual fraud, dishonesty, or criminal conduct in the management of the debtor or the debtor's public financial reporting'. However, as noted, the appointment of a trustee to manage a company's affairs during the restructuring process in Chapter 11 cases is the exception rather than the rule.[558]

The rarity of appointing trustees to manage companies during restructuring under Chapter 11 may indicate that the DIP system is functioning well and the creditors either trust the incumbent management to administrate the reorganisation or that the creditors had pushed the company to replace its management prior to or shortly after the company filed for the Chapter 11 procedure.[559] Indeed, appointment of a trustee is not the only option in the hands of creditors who are not satisfied with the conduct of the existing management. Such creditors may, before the Chapter 11 process begins, force the debtor company to replace its management with a new one that the creditors trust to manage the company throughout the reorganisation process.[560] Moreover, creditors may prefer not to seek the appointment of a trustee for other reasons, including the fear of retribution by the debtor if the court rejects the motion to appoint a trustee.[561] Furthermore, the creditors may fear that the appointed trustee's lack of familiarity with the company's financial management may result in inefficient administration of the organisation's operations. Thus, despite their reservations about current management's conduct, creditors may view retaining existing management as the most appropriate choice, given the precise knowledge about the company's financial condition that this management possesses, knowledge that is often not available to the external trustee.[562] The bottom line here

[557] Bankruptcy Code, s 1104(a)(2).

[558] In *re Marvel Entertainment Group* 140 F.3d 463 (3d Cir 1998) at 471. See also AJ Levitin, *Business Bankruptcy: Financial Restructuring and Modern Commercial Markets* (2nd edn, Wolters Kluwer Law & Business 2018) 363; Kelli A Alces, 'Enforcing Corporate Fiduciary Duties in Bankruptcy' (2007) 56 U Kan L Rev 83, 84; A Mechele Dickerson, 'Privatizing Ethics in Corporate Reorganizations' (2008) 93 Minn L Rev 875, 900.

[559] American Bankruptcy Institute, *Final Report and Recommendations on the Reform of Chapter 11* (American Bankruptcy Institute 2014) 27.

[560] John D Ayer, Michael L Bernstein and Jonathan Friedland, 'Bad Words to a Debtor's Ear' [2005] Am. Bankr. Inst. J 20, 20.

[561] American Bankruptcy Institute (n 559) 27.

[562] Clifford J White III and Walter W Theus Jr, 'Chapter 11 Trustees and Examiners After BAPCPA' (2006) 80 Am Bankr LJ 289. See also Peter F Coogan, Richard Broude and Herman Glatt, 'Comments on Some Reorganization Provisions of the Pending Bankruptcy Bills' (1975) 30 Bus. Law. 1149, 1156. (noting that '[e]xcept where dishonesty [of the debtor] is gross, creditors usually prefer to operate with the devil they know rather than with a trustee, receiver, or other stranger, whose on-the-job training will be at the creditors' expense.').

is that the small number of trustee appointments under Chapter 11 cannot be used as an indicator, in itself, to determine the success of the DIP model.

In fact, the effectiveness and appropriateness of the DIP model has been subject to debate. Advocates of the DIP scheme point to its advantages. One of these is the expertise and knowledge the incumbent management has in relation to the debtor company's financial affairs and business.[563] It has been argued that allowing the pre-petition management to continue to control the company's business is likely to warrant the company's smooth transition into Chapter 11; furthermore, it would avoid the need for additional time and expenses resulting from the appointment of an outsider trustee who 'frequently has to take time to familiarize himself with the business before the reorganization can get under way. Thus, a debtor continued in possession may lead to a greater likelihood of success in the reorganization'.[564] Another advantage of employing the DIP model in reorganisation procedures is that such employment may encourage the distressed company's directors to commence the reorganisation procedure upon early signs of distress.[565] Such a distinct advantage of the DIP approach was considered by the US Congress when the bankruptcy code was drafted, as the Congressional record reads: 'Proposed chapter 11 recognizes the need for the debtor to remain in control to some degree, or else debtors will avoid the reorganization provisions in the bill until it would be too late for them to be an effective remedy'.[566] In other words, knowing that their jobs will be preserved after commencement of the restructuring procedures, directors will be more likely to invoke the reorganisation proceedings in a timely fashion and before the corporate restructuring becomes unachievable.[567]

---

[563] HR Rep No 595, 95th Cong, 1st Session 233 (1977) noting that 'very often the creditors will be benefited by continuation of the debtor in possession, both because the expense of a trustee will not be required, and the debtor, who is familiar with his business, will be better able to operate it during the reorganisation case'.

[564] ibid. See also Jonathan C Gordon, 'Government Guaranties for Corporate Bankruptcies' (2018) 43 Vt. L. Rev. 251, 263. (arguing that 'the debtor, as opposed to a trustee, is more familiar with its business and is thus better able to manage its operations. The debtor would not require time or money to learn about the business because the debtor is already familiar with it. A trustee, on the other hand, would require valuable time and money from the estate to educate itself. Such time and money must be preserved whenever possible and used efficiently to maximize the value of the estate'); David A Skeel Jr, 'Markets, Courts, and the Brave New World of Bankruptcy Theory' (1993) 1993 Wis. L. Rev. 465, 517.

[565] See McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 132–133; Elizabeth Warren, 'Bankruptcy Policymaking in an Imperfect World' (1993) 92 Michigan Law Review 336, 372; James Edelman, Henry Meehant and Gary Cheung, 'The Evolution of Bankruptcy and Insolvency Laws and the Case of the Deed of Company Arrangement' (2019) 4 Lloyd's Maritime and Commercial Law Quarterly 571, 585.

[566] HR Rep No 595, 95th Cong, 1st Session 231 (1977).

[567] James J White, 'Harvey's Silence (Symposium: Letters to the Commission)' (1995) 69 Am. Bankr. LJ 467, 471.

On the other hand, the DIP model has been criticised for multiple reasons. One of these is the concern that such a model may encourage abuse of the reorganisation proceeding. It is argued that if the DIP model is applied in reorganisation cases and the PIP model is applied in liquidation cases, then directors have an incentive to seek reorganisation protection, even when reorganisation is not the appropriate route.[568] Bradley and Rosenzweig argued that adoption of the DIP model encourages directors of distressed companies to seek reorganisation procedures that employ the DIP method in order to avoid the liquidation option, even when liquidation seems to be the most suitable approach and makes more sense economically.[569] When a company experiences financial distress, management must consider all options available for addressing the problem. Among these options, liquidation of the company might be the optimal choice. However, the directors of the debtor corporation may deliberately avoid the liquidation option and seek the reorganisation protection in order to save their managerial position, which, in the liquidation scenario, would be taken by an external trustee. Thus, the incumbent management's desire to extend its managerial tenure makes it inherently biased towards reorganisation.[570]

The validity of the reorganisation bias argument may be undermined by the fact that the Chapter 11 process tends to be associated with a high rate of managerial turnover.[571] An empirical study conducted by Stuart Gilson on public companies that filed for Chapter 11 between 1979 and 1984 showed that managers lost their jobs within two years of filing in 71% of the cases.[572] Another study conducted by Ayotte and Morrison suggested that 80% of CEOs in a sample of publicly and privately held companies that filed for Chapter 11 in 2001 were replaced before or shortly after filing for Chapter 11.[573] These studies suggest that, contrary to the reorganisation bias argument, Chapter 11 provides no safe harbour for entrenched managers.[574]

---

[568] Hahn (n 36) 137.
[569] Michael Bradley and Michael Rosenzweig, 'The Untenable Case for Chapter 11' (1992) 101 Yale L.J. 1043, 1078.
[570] Hahn (n 36) 138.
[571] See Finch and Milman (n 244) 237; Carruthers and Halliday (n 503) 265; Susan Rose-Ackerman, 'Risk Taking and Ruin: Bankruptcy and Investment Choice' (1991) 20 The Journal of Legal Studies 277, 298.
[572] Stuart C Gilson, 'Management Turnover and Financial Distress' (1989) 25 J Financ Econ 241.Gilson also observed that 60% of managers of financially troubled companies that did not file for Chapter 11 and restructured out-of-court instead lost their jobs within two years of restructuring.
[573] Kenneth M Ayotte and Edward R Morrison, 'Creditor Control and Conflict in Chapter 11' (2009) 1 J Leg Analysis 511.
[574] ibid; Carruthers and Halliday (n 503) 265; Elizabeth Warren, 'The Untenable Case for Repeal of Chapter 11' (1992) 102 The Yale Law Journal 437.

Furthermore, other critics of DIP doubt the capability of the incumbent management to administrate the company's operations throughout the reorganisation process. Moss stated that leaving the pre-petition management in control of the restructuring process is 'like leaving an alcoholic in charge of a pub'.[575] However, it is safe to say that this concern is exaggerated and based on the presumption that the company's financial distress is always caused by the poor performance of the incumbent management. Clearly, this presumption is not accurate, as the financial distress may be caused by factors beyond the management's control.[576] Even in the case of mismanagement, the creditors, in the US Chapter 11 context at least, can exercise their influence to force the company to change its directors prior to or shortly after the commencement of the reorganisation proceeding.[577]

It is argued that the DIP model fits well and operates efficiently within the scope of Chapter 11 because the dominant form of US corporate ownership is the dispersed ownership system.[578]One of the features of this form of ownership is the separation of ownership of the company from the management of the company, where the owners do not have much influence on the administrative decisions of the company, unlike in the concentrated ownership system, where a few shareholders have control over the managers, as will be shown later. The directors of companies that are dispersed in ownership are independent in exercising their administrative activity. Therefore, it is not expected that they will be biased towards the shareholders' interests at the expense of creditors when managing the company's affairs during the reorganisation procedure.[579]

The suitability of the DIP model within the Chapter 11 regime has been also supported by the American Bankruptcy Institute (ABI) Commission. In its report, the Commission recommended retaining the DIP model. Before reaching such a conclusion, the Commission debated the utility of the PIP model as an alternative to the DIP approach. It determined that

[575] G Moss, 'Chapter 11: An English Lawyer's Critique' (1998) 11 Insolvency Intelligence 17, 18–19.
[576] Finch and Milman (n 244) 237. See also A Mechele Dickerson, 'The Many Faces of Chapter 11: A Reply to Professor Baird' (2004) 12 Am Bankr Inst L Rev 109, 127. Dickerson stated that 'bankruptcy law is premised on the belief that financial failures are caused by factors that lie beyond the control of the business and its managers. As such, these factors cannot be predicted or explained (i.e., exogenous risks) and are not caused by choices the managers made (i.e., endogenous risks)'.
[577] Ayer, Bernstein and Friedland (n 560) 20.
[578] Hahn (n 36); John Armour, Brian R Cheffins and David A Skeel Jr, 'Corporate Ownership Structure and the Evolution of Bankruptcy Law: Lessons from the United Kingdom' (2002) 55 Vand. L. Rev. 1699.
[579] Hahn (n 36) 130.

the PIP is the appropriate model in cases involving incompetent or fraudulent management and acknowledged that the bankruptcy code currently mandates the appointment of a trustee in these cases. However, the Commission concluded that the potential benefit of appointing a trustee in cases involving honest-but-unfortunate companies was 'significantly outweighed by the potential disruption, costs, and inefficiencies associated with the displacement of the debtor's management'.[580]

In relation to the high cost associated with appointing an insolvency practitioner, it is worthwhile to refer to the UK administration process as an example. Although the EA's introduction of out-of-court appointments in 2002 is thought to reduce its direct entry expenses, the administration remains an expensive restructuring tool.[581]Transferring the control from incumbent management to the administrator is the main factor behind the high cost of administration, as the company must pay the administrator's fees for the duration of the administration; this places extra financial pressure on an already ailing business.[582] These high costs have been even more acutely felt during the recent financial distress caused by the COVID-19 pandemic. With a large number of UK businesses seeking rescue from the financial dilemma in the context of an expensive traditional administration process, the need for a less practitioner-controlled (i.e. less expensive) restructuring device has become even more urgent. Such need has paved the way for what is known as a 'light touch' administration, discussed in detail in the following section.

In summary, the adoption of the DIP model may enhance the success of the reorganisation process in two ways. Firstly, it may encourage the timely commencement of the reorganisation procedure. Secondly, the incumbent management's familiarity and knowledge of the company's operations may facilitate the restructuring process and save the company additional time and costs that may result from the appointment of an outside trustee. On the other hand, entrusting the incumbent management to control the company's operations during the reorganisation procedure may not be the appropriate approach in cases where the corporate distress was caused by the poor performance of such management. Also, the DIP model may not be suitable for companies for which ownership is concentrated in the hands of a few strong

[580] American Bankruptcy Institute (n 559) 24.
[581] Finch and Milman (n 244) 324.
[582] See Insolvency Lawyers' Association, 'Changing the Narrative around Administration' (2020) <https://www.ilauk.com/news-events/news-view/changing-the-narrative-around-administration> accessed 5 June 2020.

shareholders, as the directors in such companies are controlled by the shareholders, who have significant influence and control over the management of the company. Such controlling shareholders may tend to direct the management to engage in high risk transactions that may result in reduction of the value of the reorganised estate, thereby increasing the creditors' losses.

5.1.2 The UK Approach: Practitioner-in-Possession

In contrast to the DIP approach adopted under the US Chapter 11 regime, control of the main reorganisation process (i.e. administration) in the UK is assumed by the insolvency practitioner, or 'administrator'. Upon the commencement of the administration proceedings, the company's board of directors may not exercise its management power without the consent of the administrator, who has control over the company's business and assets during the administration process.[583] As in the US, the share of ownership in UK public companies tends to be widely dispersed.[584] Given the similarity between the capital market structures of the two countries, it might be reasonable to question why the UK administration process employs the PIP model rather than the US Chapter 11 DIP model, which is thought to be effective for dispersed-owned companies. There are several possible reasons.[585] Perhaps the most important among these is that the UK attitude toward business failure is different than the US attitude.

Professor Goode has stated that the UK administration regime is based on the presumption that the company's insolvency is usually caused by the failure of its management; thus, the last people to leave in control during the reorganisation process are those who are responsible for the company's distress in the first place.[586] This is quite different from the US attitude, where the business failure is usually seen as 'the inevitable downside of entrepreneurship and risk'.[587]The cultural differences between the US and the UK in relation to the failure of a business was observed by Moss, who stated the following:

> In England insolvency, including corporate insolvency, is regarded as a disgrace. The stigma has to some extent worn off but it is nevertheless still there as a reality. In the United States business failure is very often thought of as a misfortune rather than wrongdoing. In England the judicial bias towards creditors reflects a general social attitude which is inclined to punish risk takers when the risks go wrong and side with creditors who lose out. The United States is still in spirit a pioneering country where the taking of risks is thought to be a good thing and creditors are perceived as being greedy.[588]

[583] IA 1986, schedule B1, para 64.
[584] Armour, Cheffins and Skeel Jr (n 578) 1700.
[585] See McCormack, 'Control and Corporate Rescue–an Anglo-American Evaluation' (n 247) 521.
[586] Goode (n 130) 394. See also Carruthers and Halliday (n 503) 246. (stating that 'in the UK, the idea that the same managers who led a firm into insolvency should stay to oversee its reorganization seemed absurd').
[587] JL Westbrook, 'A Comparison of Bankruptcy Reorganisation in the US with Administration Procedure in the UK' (1990) 6 IL&P 86, 143.
[588] Moss (n 575) 18.

Hahn provided another possible explanation for the apparent incongruity between the reorganisation regime and the ownership structure in the UK, suggesting that the inconsistency is somehow a consequence of an a-synchronised transition in the UK legislation.[589] The UK did not become a dispersed ownership market until the 1980s.[590] In the late 1970s and the early 1980s, the Cork Report, which was the basis for fundamental reform of the UK insolvency law, was drafted. At the time the Cork committee was drafting its report, the UK market was in the last phase of its shift from concentrated to dispersed ownership. That shift, according to Hahn, was not acknowledged by the Cork committee, so as the UK reformed its insolvency regime, it retained its manager-displacing orientation.[591] What may support this explanation is the fact that since the enactment of the Insolvency Act in 1986, the UK reorganisation regime has been subject to multiple reforms that have moved it, albeit slowly, to a more manager-controlled system. The first sign of such a shift in the UK insolvency law was the introduction of a management-controlled procedure for small companies through CVA with a moratorium under the Insolvency Act 2000. The most recent change that reflects this shift became official on 26 June 2020, when the UK Corporate Insolvency and Governance Act (CIGA) came into force. The CIGA introduced significant reforms to the UK insolvency law. One of these reforms was the introduction of a new stand-alone moratorium procedure. As illustrated in Chapter 4, the new stand-alone moratorium is a debtor-in-possession procedure, during which the directors remain in control of the company, but they are subject to the supervision of an insolvency practitioner 'monitor' who examines the company's compliance with the qualifying conditions throughout the moratorium period.[592]

Like the DIP model, the PIP approach has its strengths and drawbacks. It has been argued that entrusting control of the reorganisation proceedings to an external and independent practitioner is the most appropriate approach for concentrated-owned companies, where the ownership is strongly associated with the management and the large shareholders have a significant amount of influence over the directors' decisions. Thus, the appointment of an independent and objective insolvency practitioner to handle the company's business during the restructuring

[589] Hahn (n 36) 135.
[590] Brian R Cheffins, 'Does Law Matter? The Separation of Ownership and Control in the United Kingdom' (2001) 30 J Leg Stud 459.
[591] Hahn (n 36) 135. A similar point was highlighted by Armour, Cheffins and Skeel Jr, who stated that following World War II, 'while ownership was taking on a strongly dispersed character, the U.K.'s bankruptcy regime retained its manager-displacing orientation'. Armour, Cheffins and Skeel Jr (n 578) 1773–1774.
[592] IA 1986, pt A1, ch 5, ss A34 to A41.

may protect the creditors' interests that otherwise may have been undermined by the incumbent management's bias towards shareholders.[593]

In the context of the UK insolvency system, Finch pointed to another merit of the PIP model.[594] She stated that Hahn's argument on how the DIP model is a fairer model to adopt in the UK due to its dispersed ownership market – in which the risk of shareholder manipulation tends to be low – focuses on the relationship between directors and shareholders and underestimates the risks of manipulation by other interests. She goes on to state that in the case of many distressed UK companies, powerful creditors such as banks will hold floating charges over them. Due to their privileged position, banks may press the incumbent management (if it remains in charge) to adopt restructuring strategies that primarily protect the banks' interests with no regard for other less powerful creditors. Therefore, although the outside insolvency practitioners are not completely immune to such pressure, 'they are likely to be more resistant than the company's directors, who will not only be predisposed to keeping their major creditors happy, but may well be conditioned by their troubled experiences to give way to bank pressure'.[595]

On the other hand, critics of the PIP method highlight a number of drawbacks. Arguably the main drawback is the additional time and costs associated with appointing an outside trustee.[596] Indeed, replacing existing management with an insolvency practitioner could prove costly, time-consuming and disruptive, as the outside practitioner requires time and money to learn about the company.[597] The more complicated the company's structure, the longer the restructuring process takes and the more expenses the insolvency practitioner incurs that must be paid out of the distressed company's estate: 'Such time and money must be preserved whenever possible and used efficiently to maximize the value of the estate'.[598]

With an increasing number of businesses suffering financially as a result of the rapid spread of COVID-19, the traditional model of management displacement used in the UK administration process may be inappropriate, given the high costs of the model mentioned above. For that

[593] Hahn (n 36) 133; Armour, Cheffins and Skeel Jr (n 578) 1770.
[594] Vanessa Finch, 'Control and Co-Ordination in Corporate Rescue' (2005) 25 Legal Studies 374, 389.
[595] ibid.
[596] American Bankruptcy Institute (n 559) 24.
[597] See Skeel Jr (n 564) 517; Lijie (n 548).
[598] Gordon (n 564) 263.

reason, many UK insolvency trade association bodies and professionals have advocated for the application of what is known as a 'light touch' administration for businesses in financial difficulty due to the COVID-19 pandemic.[599] In a light touch administration, the incumbent directors continue to oversee the day-to-day management activities of the business, but they are subject to administrators' supervision and consent. This interrupts the 'normal' pattern of administration – the existing management is displaced, and administrators take control of the day-to-day management activities. It should be noted that a light touch administration is not a separate and new procedure. Administrators' authority to permit directors to exercise management powers is enshrined in Paragraph 64 of Schedule B1 of the IA 1986: 'A company in administration or an officer of a company in administration may not exercise a management power without the consent of the administrator'. The administrator's consent may be general or specific.[600] The principal benefit of the light touch approach is that it keeps the cost of administration down, as the administrator will only perform essential functions rather than exercising full executive and operational control of the company.[601]

Despite its cost-saving advantage, the light touch approach is not without risks. The main risk is the potential personal liability that administrators may face related to the incumbent management's conduct. Notwithstanding their ceding of control over daily management activities to the incumbent management, administrators remain personally liable for the company's conduct during the administration process. Fear of such liability may explain why administrators have been, understandably, very reluctant to adopt a light touch strategy – instead, they favour the default practice of removing the incumbent directors from any meaningful role in managing the company during the administration.[602]

---

[599] See Insolvency Lawyers' Association (n 582); 'UK's Light Touch Insolvency Administration Emerges' <https://www.natlawreview.com/article/covid-19-emergence-light-touch-administration-united-kingdom> accessed 29 June 2020.

[600] IA 1986, schedule B1, para 64 (2) (c).

[601] Insolvency Lawyers' Association (n 582) 2. It has been reported that a large number of UK retailers are expected to take advantage of the light touch administration to deal with the unprecedented financial distress and liquidity problems caused by the COVID-19 lockdown. On 06 April 2020, and after its sales plummeted under the lockdown, Debenhams became the first high street business in the UK to enter a light touch administration. See 'Companies Explore "Light Touch" Administration in Wake of Debenhams | Financial Times' <https://www.ft.com/content/76c7c985-ff8c-4707-b4e4-28eb7a8f7b62> accessed 29 June 2020.

[602] 'Enter Stage Left: The New "light Touch" Administration - Stevens & Bolton LLP' <https://www.stevens-bolton.com/site/insights/briefing-notes/enter-stage-left-the-new-light-touch-administration> accessed 29 June 2020. The *Financial Times* reports that KPMG, the supervisor of Debenhams' CVA in 2019, refused to get involved with the light touch plan because of its risks-'Companies Explore "Light Touch" Administration in Wake of Debenhams | Financial Times' (n 601).

Another drawback of the PIP model is related to when the reorganisation process is commenced. Efficient corporate restructuring demands the speedy initiation of the right insolvency procedure at the early emergence of financial distress. Due to their knowledge of the company's immediate state of affairs, the incumbent directors of the distressed company are usually the ones to begin this procedure.[603] It is argued that adopting the PIP model may discourage directors from commencing reorganisation in a timely fashion.[604] Knowing that the commencement of reorganisation proceedings will result in the loss of their management power in favour of the appointed practitioner, directors have an incentive to delay the reorganisation filing until it is too late for the company to be restructured. In their attempts to avoid bankruptcy, the directors may tend to engage in high-risk activities in the hope of rescuing the company from its distress.[605] Engagement in such activities may result in enormous losses and dissipate the remaining value of the company's assets and, therefore, frustrate any attempt at reorganisation.[606]

One way to counter the incentive for management to delay commencement of reorganisation is by threatening such delay with a legal stick. For example, English law contains so-called wrongful trading provisions established under IA 1986. The wrongful trading provisions allow the liquidator or the administrator to bring personal liability proceedings against the company's directors if it can be proved that the directors did not take appropriate steps to minimise potential company losses after they first knew or ought to have concluded that avoidance of entering insolvent administration or going into insolvent liquidation was not a reasonable prospect.[607] If such a failure is proved, the directors may be held personally liable for the

[603] Finch (n 594) 391.

[604] See, e.g. HR Rep No 595, 95th Cong, 1st Session 231 (1977) (stating the following: 'Proposed chapter 11 recognizes the need for the debtor to remain in control to some degree, or else debtors will avoid the reorganization provisions in the bill until it would be too late for them to be an effective remedy'); Skeel Jr (n 564) 517. (arguing that the 'immediate removal of management would create significant indirect costs both before and during bankruptcy. Prior to bankruptcy, managers would stall as long as possible rather than file a bankruptcy petition and immediately lose their jobs.')

[605] Dickerson (n 576) 134.

[606] Hahn (n 36) 139.

[607] IA 1986, s 214. A similar approach is taken under the German insolvency law (*InsO*) as section 15a(1) of this law provides that 'if a legal entity becomes illiquid or overindebted, the members of the representative body or the liquidators must apply for commencement of insolvency proceedings without undue delay but in any event no later than three weeks after the occurrence of illiquidity or over indebtedness'. The omission or delay of insolvency filing can lead to criminal and financial liability of the managers as stated in section 15 a (4), (5) of *InsO*. See Mihai Lanțoș, 'Wrongful Trading in Europe' (2018) 73 eurofenix 30.

company's debts. In addition, as a further penalty, the court may impose a disqualification order for up to 15 years on the liable directors.[608]

However, the practical difficulties of enforcement of the wrongful trading provision may weaken its efficiency in encouraging the early commencement of the rescue procedure. The main obstacle is that it is usually difficult for the liquidator or the administrator to identify the point in time at which the directors knew or ought to have concluded that avoiding liquidation was not a reasonable prospect.[609] The need for funding is another difficulty that may discourage the liquidator or administrator from initiating wrongful trading action. Investigating and then pursuing a wrongful trading action are quite expensive ventures.[610] A solicitor, Peter Fidler, stated in 2001 that at least £50,000 was needed to bring a wrongful trading action, even when the claim was small.[611] Therefore, due to its practical difficulties, the wrongful trading provision has rarely been relied on in practice, as indicated by the small number of reported cases.[612]

In summary, the PIP model may prove more functional with concentrated ownership systems, as appointing outside practitioners can provide a safeguard against any potential bias by the incumbent management toward the dominate shareholder in managing the reorganisation process. Some argue that such bias is inherent in concentrated ownership systems in which the ownership of a company is strongly associated with its management. However, this advantage of the PIP model may be outweighed by the potential disruptions, extra time and costs associated with the insolvency practitioner taking full control of the company's management during the restructuring process. Moreover, the displacement of the pre-filing management may incentivise directors to delay the reorganisation process until it is too late for the company to be effectively reorganised.

---

[608] Company Directors Disqualification Act 1986, s 10.
[609] Keay, 'Wrongful Trading: Problems and Proposals' (n 123) 68.
[610] ibid 69.
[611] Peter Fidler, 'Wrongful Trading after Continental Assurance' (2001) 17 IL&P 212.
[612] Keay and Walton (n 128) 664–665. It is worth noting that the CIGA 2020 contains certain temporary measures designed to assist UK companies in weathering the COVID-19 pandemic. One of these provisional measures is a temporary suspension of the wrongful trading provisions contained in Sections 214 and 246ZB of the Insolvency Act of 1986. Section 12 of the CIGA 2020 provides that in determining whether wrongful trading has occurred during the 'relevant period', the court will assume that a director 'is not responsible for any worsening of the financial position of the company or its creditors'. The relevant period in this context lasts from 1 March 2020 until 30 June 2020 or one month after the Act was approved, whichever is later. Additionally, as stated in section 41 of the CIGA, the suspension period can be either shortened or extended for up to six months by secondary legislation.

5.2 The Control Models Adopted Under the Saudi Corporate Reorganisation Regime

As noted previously, two reorganisation control models are available under Saudi BL 2018. PS is a DIP-type process, while the company's affairs during the FR process are jointly controlled by the pre-filing management and a trustee. The following subsections address the application of these two models under the Saudi restructuring law in order to determine their utility and suitability to serve the rehabilitative objectives of such law.

5.2.1 The Application and Effectiveness of the DIP Model under the PS Procedure

The debtor is the key player in the PS process under BL 2018. The incumbent management remains in control during the PS process with minimal involvement of the court over its decision-making authority. The court's approval is required in certain and exceptional situations, such as when the company seeks to obtain new secured credit or to terminate executory contracts.[613] Other than these specific circumstances, the incumbent management enjoys a great deal of control over the restructuring process during the PS procedure with no judicial supervision.[614]

Under this section, the author argues, first, that, in general, the DIP model in its current form applied under the PS procedure is not compatible with the corporate ownership system of Saudi companies and involves a significant risk of shareholder manipulation. Secondly, the PS procedure provides no measure to mitigate the risk of shareholder manipulation. The two points are observed in the following subsections.

[613] BL 2018, arts 25, 182. Art 25 provides that '[t]he court may, upon the request of the debtor during a court hearing notified to the counterparty, terminate any contract to which the debtor is a party to if such termination is necessary to protect the debtor's activity and if such termination is in the interest of the majority of the creditors, provided that such termination should not cause serious damage to the counterparty'. In relation to obtaining secured credit, art 182 states that '[t]he debtor may not obtain secured financing after the commencement of bankruptcy procedures except with court approval'.
[614] Al-Ahmad (n 315) 97.

5.2.1.1 The Risk of Shareholder Manipulation

In order to determine the optimal person to control the company during reorganisation, two crucial policies must be considered.[615] First, the reorganisation law must provide for an independent person to manage the company's operation during reorganisation. In its task of managing the reorganisation, the controlling person must act objectively and independently and must not be biased towards either creditors or shareholders. Indeed, the independence and objectivity of the controlling person are critical to ensuring the efficiency of the reorganisation process for the collective interest of all parties. The second policy to be considered is that the reorganisation law should promote early filing for reorganisation. The law should provide directors with an incentive to seek rehabilitation upon early signs of distress and before it becomes too late for the company to be rescued.[616]

However, it may be difficult to reconcile these two conflicting policies in one restructuring regime. While leaving the incumbent management in control during restructuring may encourage the timely commencement of rehabilitation, such an approach may, on the other hand, fail to provide the independence and impartiality needed during the reorganisation process. It is feared that entrusting the pre-filing management to handle the restructuring process may involve a high risk of management bias to act in the interests of shareholders only rather than acting in the collective interest of all parties.[617]

Determining whether the adoption of the DIP model of corporate reorganisation involves a high risk of bias toward shareholders depends on the ownership structure of the reorganised company. As mentioned previously, there are two systems of corporate ownership: dispersed ownership and concentrated ownership.[618] Ownership of the company, according to the dispersed ownership system, is dispersed in the form of many shares owned by a large number of investors who usually do not participate in the management of the company. Ownership of the company, according to the concentrated ownership system, is concentrated in the hands of a few shareholders who have control over the management of the company. The dispersed ownership system is common in the US and the UK, while the concentrated ownership system

[615] Hahn (n 36) 147.
[616] ibid.
[617] ibid.
[618] See generally John C Coffee Jr, 'The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control' (2001) 111 Yale LJ 1; Stephen R Goldberg, Dori Danko and Lara L Kessler, 'Ownership Structure, Fraud, and Corporate Governance' (2016) 27 J Corp Account & Finance 39.

is common in European countries other than the UK, in the Middle East and in North African (MENA) countries.[619] The Saudi corporate setting is characterised by a concentrated ownership structure, as most of the capital of the typical large Saudi firm is owned by a small number of controlling shareholders.[620]

While it is recognised that the DIP model is well suited for dispersed ownership companies because the management of these companies is separated from the ownership and the shareholders have no influence on the company's management, the DIP may not be the appropriate model of reorganisation control for concentrated ownership companies, where one shareholder, family or group of shareholders has majority or dominant control over the company's decision making[621] and where they have the power to monitor and replace the management. Due to their lack of independence, the directors, in order to secure their jobs, must prove their loyalty to the strong and dominate shareholders and perform in their interests. 'As a result, leaving incumbent management to run the corporation while in bankruptcy plays into the hands of the strong shareholders and exacerbates the risk of loss to the creditors.'[622] It is feared that when the company becomes insolvent, shareholders may tend to direct the management to engage in unjustifiable high-risk projects.[623] When the company is insolvent, the creditors have absolute priority over the shareholders in the value of a company. As their shares in the company become nearly worthless, shareholders will have nothing to lose and possibly a lot to win by engaging in reckless and high-risk investments.[624] If such projects were

[619] Jenifer Piesse, Roger Strange and Fahad Toonsi, 'Is There a Distinctive MENA Model of Corporate Governance?' (2012) 16 J Manag Govern 645.

[620] Abdulaziz Mohammed Alsahlawi and Mohammed Abdullah Ammer, 'Corporate Governance, Ownership Structure and Stock Market Liquidity in Saudi Arabia: A Conceptual Research Framework' (2017) 6 Accounting and Finance Research 17; Waleed M Al-Bassam and others, 'Corporate Boards and Ownership Structure as Antecedents of Corporate Governance Disclosure in Saudi Arabian Publicly Listed Corporations' (2018) 57 Business & Society 335; Omer Saeed Habtoor, Waddah Kamal Hassan and Khaled Salmeen Aljaaidi, 'The Impact of Corporate Ownership Structure on Corporate Risk Disclosure: Evidence from the Kingdom of Saudi Arabia' (2019) 15 Business and Economic Horizons 325.

[621] Hahn (n 36) 154; Armour, Cheffins and Skeel Jr (n 578) 1701. Armour, Cheffins and Skeel Jr stated that 'a manager-driven bankruptcy regime complements dispersed share ownership, while its manager-displacing counterpart aligns with a governance regime where concentrated ownership prevails'.

[622] Hahn (n 36) 133. In addition, Triantis points out that the incumbent management's bias to shareholders over creditors may be driven by the management's desire to promote a reputation of being faithful to shareholders interests. He stated that given the high probability of managerial replacement associated with the reorganisation process, managers are 'concerned about their reputation, which determines their ability to find new positions elsewhere. Unless a manager's career niche involves relatively short-term appointments to liquidate or turnaround firms in financial distress, she may seek to promote a reputation of being faithful to shareholder interests'. George G Triantis, 'Theory of the Regulation of Debtor-in-Possession Financing, A' (1993) 46 Vand L Rev 901, 917.

[623] See Lynn M LoPucki, 'The Trouble with Chapter 11' (1993) 1993 Wis. L. Rev. 729, 733; McCormack, 'Control and Corporate Rescue–an Anglo-American Evaluation' (n 247) 524; Finch and Milman (n 244) 238.

[624] Paul B Lewis, 'Trouble Down Under: Some Thoughts on the Australian-American Corporate Bankruptcy Divide' (2001) 2001 Utah L Rev 189, 224. See also LoPucki (n 623) 733. LoPucki argued that because the

successful, the shareholders would gain benefits, and if unsuccessful, the creditors would be the only parties to bear the loss and suffer as a result of the reduction in value of the reorganised estate.[625]

Global recognition of the US DIP approach to reorganisation may have encouraged Saudi lawmakers to transplant the US approach in the hope that it would function effectively in the same way it, arguably, does in the US. However, a law that functions well in one country will not necessarily function with the same efficiency if transplanted into another legal system.[626] The success of legal transplanting or borrowing depends on the ability of the foreign law to be adjusted to the environment of the recipient country.[627] The difference in corporate ownership structures between the US and Saudi Arabia should have been considered by Saudi lawmakers before transplanting the concept of DIP without modification into the Saudi restructuring law.

The incompatibility of the 'pure' DIP model with the concentrated structure of the Saudi share market does not necessarily imply that the PIP as the opposite of the DIP is the ideal choice for the Saudi restructuring regime. Although the PIP model may be more compatible with concentrated ownership than the DIP – as the appointment of an external trustee to handle the reorganisation process provides protection against the potential risk of shareholder manipulation – the benefit of such protection may be significantly outweighed by the inherent disadvantages associated with the PIP model.

It might be more appropriate for Saudi legislators to follow the European cautious approach of transplanting the DIP concept. The incompatibility of the DIP model with concentrated ownership system may have been contemplated by some leading European countries, such as France and Germany, which operate, in common with Saudi Arabia, under 'concentrated ownership' market systems. Both France and Germany, in their quest to reform their

shareholders 'retain the benefits of risk taking without suffering a corresponding share of the losses, it may be in their interests that the company take risks not justified by the expected returns to the company'. Similarly, Lewis argued that '[a]s equity investors lose their investment before debt investors do, the equity holder (in charge as debtor in possession) has nothing left to lose and, thus, does not bear the full burden of its risky behavior. As a result, an incentive is created for the equity holders to direct a firm to behave in an excessively risky fashion'. Paul B Lewis, 'Business Insolvency and the Irish Debt Crisis' (2012) 11 Rich J Global L & Bus 407, 438.

[625] Finch and Milman (n 244) 238.

[626] Rebecca Parry, 'Is UK Insolvency Law Failing Struggling Companies' (2009) 18 Nottingham LJ 42, 49; Alan Watson, 'Legal Transplants and Law Reform' (1976) 92 Law Q Rev 79, 81.

[627] Otto Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37 Mod L Rev 1, 6; Hideki Kanda and Curtis J Milhaupt, 'Re-Examining Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law' (2003) 51 Am J Comp L 887, 891.

restructuring laws, have sought to establish reorganisation regimes similar to Chapter 11 and referred to Chapter 11 as a model for an effective restructuring procedure.[628] Despite their attempts to copy the successful experience of Chapter 11, neither France nor Germany adopted the DIP model in the same form as it exists in Chapter 11, as they modified the model to make it more compatible with their legal environments. Germany, for example, introduced a 'self-administration' restructuring procedure that was inspired by US Chapter 11. As in the case of Chapter 11, the pre-filing management remains in its position in managing the company's business during the 'self-administration' procedure. However, unlike in Chapter 11, the pre-filing management's authority during self-administration is restricted and subject to the supervision of a court-appointed supervisor. The approval of the supervisor is required for any proposed transaction by the incumbent management outside its ordinary course of business.[629] The introduction of the French Safeguard (*sauvegarde*) procedure in 2005 was also inspired by Chapter 11,[630] but also unlike Chapter 11, upon the commencement of the French Safeguard procedure, the court appoints an administrator to oversee and assist the incumbent management in managing the company's business. While the incumbent management remains in control during Safeguard proceedings, its power is restricted, and it has no authority to make certain decisions, such as assumption or rejection of executory contracts or granting any further security over the company's property. Only the appointed administrator has the power to do so.[631]

This modified DIP model, or what is referred to as the co-determination model, is also adopted under FR, as will be shown later. This model is an attempt to marry the two popular models of reorganisation control (i.e. DIP and PIP).[632] It is thought that leaving the pre-filing management in possession would encourage it to commence reorganisation in a timely fashion. At the same time, the appointment of an external insolvency practitioner is said to provide protection

[628] See generally H Hess, 'Company Restructuring Pursuant to German Insolvency Law' (2014) 3 J Civil Legal Sci 170; Eric Cafritz and James Gillespie, 'French Bankruptcy Law Reform Assessed' (2005) 24 Int'l Fin. L. Rev. 41; Alexandra Szekely, Fiona Richardson and Adam Gallagher, 'Chapter 11 : One Size Fits All ?' (2008) 23 Journal of International Banking and Financial Law 1.
[629] German Insolvency Code 1999, section 275. See Carsten Gerner-Beuerle and Michael Anderson Schillig, *Comparative Company Law* (Oxford University Press 2019) 966.
[630] Robert Weber, 'Can the Sauvegarde Reform Save French Bankruptcy Law: A Comparative Look at Chapter 11 and French Bankruptcy Law from an Agency Cost Perspective' (2005) 27 Mich J Int'l L 257, 297; Paul J Omar, 'The Mutual Influence of French and English Commercial Laws in Insolvency' (2008) 19 Int Co Commerc Law Rev 136, 140.
[631] French Commercial Code, arts L620-L628. See Gerner-Beuerle and Schillig (n 629) 963.
[632] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 152.

against any potential risk of bias by the incumbent management in managing the company's business during reorganisation.[633]

Therefore, given the concentrated ownership structure of the Saudi market, the author suggests that leaving the incumbent management in full control during PS proceedings may involve high risk of bias by such management towards controlling shareholders at the expense of creditors. What makes the situation worse is the failure of PS in providing protective measures to mitigate any identified risk of abuse or bias by the incumbent management. That is discussed next.

5.2.1.2 The Absence of Protection Against Potential Shareholder Manipulation

As indicated in the previous subsection, given the concentrated ownership structure of the Saudi market, transplanting the Chapter 11 DIP model into the Saudi PS process without modification may create a risk of the process being manipulated by controlling shareholders, who may direct the incumbent managers to pursue actions that are not in the collective interest of all parties, especially creditors. What makes the condition worse is the current application of the DIP model under the PS procedure. Under this process, creditors are not provided with tools to tackle the incumbent management's potential bias towards shareholders. In contrast to Chapter 11, no creditors' committee exists under the PS regime to represent creditors' interests and monitor the conduct of management throughout reorganisation, nor does the PS grant creditors the right to request the appointment of a trustee to replace the incumbent management for cause, such as fraud, dishonesty, incompetence or mismanagement. The only remedy available in these circumstances is the court termination of the procedure upon the request of a party in interest.[634]

It is argued that the creation of a creditors' committee and the power of creditors to request the appointment of a trustee for cause under Chapter 11 provide important safeguards to fair management of the business by the DIP.[635] The ABI Commission has stated that these two measures represent checks on the DIP's power and decision-making authority.[636]

[633] Hahn (n 36) 150–152.
[634] BL 2018, art 39(g).
[635] Hahn (n 36) 141.
[636] American Bankruptcy Institute (n 559) 23.

Without a creditors' committee, it may be harmful to the interests of creditors if the debtor, as a DIP, has absolute freedom to act alone without oversight. Accordingly, in order to ease the negotiation process between the debtor and the company's creditors and as a counterweight to the DIP position, section 1102 mandates the US trustee to appoint a committee of unsecured creditors as soon as practical after the order for relief.[637] It has been consistently held by case law that members of the creditors' committee have a fiduciary duty to the constituents they represent.[638] In addition, committee members are required to be 'representative of the different kinds of claims'.[639] The committee of creditors performs several functions, which include the following:[640]

(1) consulting with the trustee or DIP concerning the administration of the case;

(2) investigating the acts and financial condition of the debtor;

(3) participating in the formulation of the reorganisation plan;

(4) requesting the appointment of a trustee; and

(5) performing such other services as are in the interest of those represented by the committee.

A scrutiny tool such as this is absent from the PS process, under which there is no provision for creation of a creditors' committee to oversee the incumbent management's conduct and represent the interests of unsecured creditors.

Similar to the creditors' committee, the creditors' right to request the appointment of a trustee to replace the incumbent management for cause under the Chapter 11 regime is thought to be effective in protecting creditors' interests against harmful conduct by the DIP management.[641] As mentioned previously, section 1104 of the US bankruptcy code allows courts to appoint a trustee upon the request of a party in interest or the US trustee if there is a 'cause' for such appointment, such as 'fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management'.[642] Also, the court may appoint a trustee 'if such appointment is in the interests of creditors, any equity security holders, and other interests of

[637] Epstein and Nickles (n 546) 97; Tabb, *Law of Bankruptcy* (n 279) 1062.
[638] See *In re SPM Mfg. Corp.*, 984 F.2d 1305, 1315-16 (1st Cir 1993); *In Re Commercial Mortg. and Finance, Co.*, 414 BR 389 (Bankr ND Ill 2009).
[639] Bankruptcy Code, s 1102(b)(1).
[640] See Bankruptcy Code, s 1103(c).
[641] See White III and Theus Jr (n 562) 289.
[642] Bankruptcy Code, s 1104 (a)(1).

the estate'.[643] Despite the small number of appointments of Chapter 11 trustees, the possibility of appointing a trustee may be used by creditors in their negotiations with the debtor company in a way that promotes meaningful results for the reorganisation process.[644] Gilson and Vetsuypens noted that when creditors are not satisfied with the way the incumbent management administrates the reorganisation process, creditors can force the company to change such management by threatening to petition the court to have a trustee appointed unless such a change is made.[645] Therefore, the possibility of appointing a trustee allows creditors to participate and alter any misconduct by the pre-petition management that could undermine the restructuring process.

Such power is not available to creditors under the PS process, which, unlike Chapter 11, does not provide for the appointment of a trustee to replace the incumbent management for cause, such as fraud, incompetence, or mismanagement. The only available option for creditors in these situations is to apply to the court to terminate the PS proceedings.[646] The court then, at its discretion or at the request of the debtor or any one of its creditors, may order the commencement of the FR procedure.[647] However, such conversion between the two procedures is likely to increase the time and the cost of restructuring, thereby reducing the value of the reorganised estate and increasing the losses of unsecured creditors.

Therefore, the current adoption of the DIP model in the Saudi PS procedure may open the door for the process to be abused and dominated by shareholders; moreover, the current PS does not provide creditors with an option for overseeing the conduct of the incumbent management or for requesting the appointment of a trustee. Such negative impact can be avoided by adopting the recommendation made in Chapter 3, which calls for abolishing the PS procedure and retaining the FR as the only restructuring procedure under BL 2018. Alternatively, the author recommends a fundamental change in the way the PS procedure is currently managed: the PS should adopt the same modified DIP (co-determination) model that applies under the FR process. The mechanism of such a model and its strengths and potential drawbacks are discussed in the following section.

[643] Bankruptcy Code, s 1104 (a)(2).
[644] American Bankruptcy Institute (n 559) 27.
[645] Stuart C Gilson and Michael R Vetsuypens, 'Creditor Control in Financially Distessed Firms: Empirical Evidence' (1994) 72 Wash ULQ 1005, 1012.
[646] BL 2018, art 39(g).
[647] BL 2018, art 41(c).

5.2.2 Control of the Company's Business During the FR Procedure

In contrast to the PS process, during the FR procedure, the incumbent management does not have full control over the company's business. Instead, while the directors remain in office after commencement of the FR, their power in managing the company's affairs is restricted and subject to the guidance and supervision of a court-appointed trustee.[648] The trustee supervises management's activity during the FR to ensure fairness of the procedure and its execution and to protect the interests of those affected by the procedure.[649] The incumbent management also must obtain the trustee's approval before undertaking any of the actions delineated in the law, which may impact the company's asset and liability position.[650] These actions are set out in paragraph (1) of Article (70) of BL 2018 as follows:

> (a) preparing the restructuring proposal and implementing its procedures, including inviting creditors to vote thereon;
> (b) requesting funding;
> (c) repayment of due or outstanding debts;
> (d) signing a new insurance contract entailing new obligations upon the company;
> (e) evicting any of the assets leased to the company and signing any lease contract necessary or beneficial for its business;
> (f) concluding any agreement or settlement with one or more creditors;
> (g) providing or renewing any security interest in favour of third parties;
> (h) changing any of the company's registered premises or office;
> (i) voting on a proposal of any debtor of the company under any of the bankruptcy procedures entailing waiving any of the company's rights;
> (j) concluding a contract for the provision of legal, accounting or other consultancy services to assist in the financial restructuring of its activities;
> (k) filing lawsuits or litigating in any proceeding before judicial, quasi-judicial and arbitration bodies;
> (l) appointing an agent to act on behalf of the company, except if such appointment falls within the scope of the ordinary course of business;
> (m) establishing a subsidiary or purchasing shares or interests in another company;
> (n) transferring ownership of all or some of the company's businesses or assets outside the normal course of business;
> (o) requesting the termination of the procedure.

If the incumbent management disposes of any of the company's assets beyond the scope of its ordinary course of business in violation of the provisions of paragraph (1)(n) of Article (70), then the court may decide – based upon a request from an interested party – to annul management's action, recover the assets or take any other actions it may deem appropriate,

[648] See Adli Hammad, 'Insolvency Law in Saudi Arabia' in Donald S Bernstein (ed), *The Insolvency Review* (17th edn, Law Business Research Ltd 2019) 311.
[649] BL 2018, art 57.
[650] Adli Hammad (n 648) 314.

without prejudice to the rights of third parties (acting in good faith). The person suffering from any harm may file a claim for compensation.[651]

Although the pre-petition management continues in control over the company's daily operations during the FR procedure, this continuation is not absolute but is conditional on the management's adherence to the rules stipulated in this procedure. Thus, Article 69(2) of BL 2018 allows the trustee to request the court to remove the pre-petition management if such management commits any act of negligence or mismanagement, demonstrates a lack of cooperation with the trustee or commits any of the offenses provided for in BL 2018. Upon its decision to remove the pre-filing management, the court may decide to transfer all the removed management's powers and responsibilities to the trustee, and the trustee may seek assistance from whomever it deems appropriate to assist in the management of the company's business.[652] Alternatively, the court may appoint new managers to replace the former management in handling the company's business, if the volume or type of such business so requires.[653]

As mentioned previously, the co-determination model of reorganisation control has been adopted in a number of European countries, such as France and Germany, which have concentrated ownership markets in common with Saudi Arabia.[654] Such a model stands in the middle between the US DIP and the UK PIP approaches.[655]

Hahn argued that the co-determination system is suitable for a concentrated market. He stated that such a system provides two significant advantages. On one hand, appointing an independent trustee is necessary to ensure that the reorganisation case is handled objectively and to protect the interests of all interested parties against any potential risk of bias by the incumbent management towards controlling shareholders. Thus, the involvement of an independent trustee in business decision-making provides a counterbalance against management's inherent bias towards shareholder. On the other hand, leaving the pre-filing management in office to jointly control the company with the appointed trustee may encourage the timely commencement of the reorganisation procedure by managers who may be

[651] BL 2018, art 71.
[652] BL 2018, art 69(2)(a).
[653] BL 2018, art 69(2)(b).
[654] See Gerner-Beuerle and Schillig (n 629) 961–972.
[655] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 152.

discouraged from doing so if commencement of the procedure would result in their being displaced.[656]

Leaving the pre-filing management in control may also enhance the efficiency of the restructuring process due to the knowledge and expertise such management possesses in relation to the company's business.[657] In addition, when compared with the PIP model, where the insolvency practitioner supersedes the company's management, the co-determination model is likely to be less expensive.[658] The UK 'light touch' administration procedure mentioned previously may provide evidence of this. The 'light touch' administration procedure, which can be described as a co-determination process, has recently become a preferable restructuring device for companies in distress. Such preference may be based on the fact that leaving the incumbent management in control of the company's daily business activities while the administrator performs essential restructuring functions may be less expensive and less disruptive than the traditional method of administration, which involves displacement of the pre-filing management, with full executive and operational control of the company assigned to the administrator.

Nevertheless, the co-determination system may raise some concerns. Rather than having one controller overseeing the company's business, the co-determination system employs a dual decision-making method. The dual decision-making structure of this system may produce clashes of opposing egos and interests. As Hahn observed:

> First, one of the fallibilities of shared authority and collective decision-making is human miscommunication. The flow of information between the various decision-makers is susceptible to errors, miscommunication and hence distortion. Secondly, between management and the trustee, the former enjoys superior access to information concerning the debtor. Because the two decision-makers represent different interest groups, management has an incentive to

[656] Hahn (n 36) 147. Lijie Qi seems sceptical of the merit of this argument, stating that '[s]haring authority with a trustee, although better treatment than being displaced, is still not attractive enough to guarantee an early filing. The large majority of owner-managers of concentrated ownership debtors still tend to solely control the undertakings by themselves as long as possible, reluctantly handing over half command to some outsiders until liquidation is imminent'. Lijie (n 548) 140. However, as stated by Hahn '[w]hen facing the choice whether to delay bankruptcy and risk liquidation or to file for reorganisation and participate in the turn-around efforts, management in a co-determination reorganisation regime is more likely to opt for the latter alternative'. Hahn (n 36) 151–152.

[657] In *re Marvel Entertainment Group*, 140 F.3d 463 (3d Cir 1998) at 471, the court stressed that the strong presumption against appointing an outside trustee 'finds its basis in the debtor-in-possession's usual familiarity with the business it had already been managing at the time of the bankruptcy filing, often making it the best party to conduct operations during the reorganization'.

[658] See Insolvency Lawyers' Association (n 582).

> withhold information from the other representative (the trustee), undermine the latter's effective decision-making and thus tip the scale of power and risk-taking in favor of its own constituency, the equityholders.[659]

In relation to the possibility of clashes between management and the trustee, it may be relevant to refer to the experience of the Irish examinership procedure.[660] As with the Saudi FR, the Irish examinership employs a co-determination system. The procedure involves the appointment of an examiner whose task is to formulate proposals and prepare a report for a compromise or a scheme of arrangement between the ailing company, its members and its creditors. During the period of examinership, the pre-petition management generally remains in charge over the daily operations of the company, though the court has the power to curtail any or all of the management's powers and transfer them to the examiner for cause.[661]

Professor McCormack stated that the clashes between the examiner and the incumbent management do not seem to be the norm in Ireland. Certainly, in cases where the examinership has been initiated voluntarily by the company, 'the relationship between management and the examiner has worked relatively harmoniously'.[662] This may indicate that when the examinership is initiated voluntarily by management, such management is more likely to be willing to cooperate with and assist the appointed trustee in achieving the objective of the examinership, which is the survival of the company as a going concern. The same point may apply to the Saudi FR procedure, which is usually initiated voluntarily by the debtor company. The voluntary initiation of reorganisation implies the management's willingness to reorganise. With such willingness, the incumbent management is expected to be supportive and cooperative in dealing with the trustee; otherwise, the reorganisation may not be successfully accomplished. Although the management is not likely to be uncooperative with the trustee in managing the company during the FR procedure, if this uncommon scenario occurs, the law provides a tool to deal it. This tool is reflected in the trustee's ability to request the court to remove the uncooperative management and to transfer all of the removed management's powers and responsibilities to the trustee.[663]

---

[659] Hahn (n 36) 152.
[660] The relevant law is provided under the Irish Companies (Amendment) (No. 2) Act 1999.
[661] For more information about the Irish Examinership see Thomas B Courtney, *The Law of Companies* (4th edn, Bloomsbury Professional 2016); Lewis, 'Business Insolvency and the Irish Debt Crisis' (n 624); Jonathan Mccarthy, 'Challenges in Finding the " Right " Approach to SME Rescue : The Example of Reforms to the Irish Examinership Process' (2019) 32 Insolvency Intelligence 43.
[662] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 154.
[663] BL 2018, art 69(2).

In summary, the co-determination model applied in FR is most suitable for the concentrated ownership market of Saudi Arabia in two regards. Firstly, the appointment of an objective trustee provides protection against potential shareholder manipulation. Secondly, leaving the incumbent management in control is the carrot this model provides to encourage directors' timely filing for reorganisation. Moreover, the possibility of removing the uncooperative management and transferring its powers to the trustee provides a solution for dealing with any unlikely clashes between the management and the trustee.

5.3 Conclusion

This chapter discussed the issue of control of companies undergoing reorganisation. The first part of the chapter pointed to the two global models of control for corporate reorganisation: the debtor-in-possession (DIP) model and the practitioner-in-possession (PIP) model. As this analysis demonstrates, both models have strengths, but neither is free from criticism.

This examination indicates that under the DIP model, allowing the incumbent management to remain in control during the reorganisation process may be advantageous for two reasons. First, it may incentivise the existing management to seek reorganisation in a timely manner. Second, due to the knowledge and 'know-how' the pre-filing management possesses pertaining to the company's operations, allowing that management to remain in charge may enhance the efficiency of the restructuring process and save the company the additional costs and time that would be required by an outside trustee to become familiar with the company's business.

Nevertheless, when the company's financial distress is related to the conduct or the poor performance of its management, leaving such management in control during the reorganisation process does not seem proper and may hinder the success of restructuring efforts. Moreover, the DIP model may not function well for concentrated-owned companies since the management and the ownership of such companies are strongly associated. As a result of this close alliance, the company's shareholders may have significant influence and control over the management. Thus, entrusting such management to handle the restructuring process may involve a high risk of management bias to act in the interests of the controlling shareholders only, rather than acting in the best interests of all parties. The risk of shareholder manipulation is considered low in dispersed ownership markets, where the company's management is separated from its

ownership, and the shareholders do not have much influence on the administrative decisions of the company.

Therefore, the PIP model may be more suitable for concentrated-owned companies than the DIP model, since the appointment of an independent and objective insolvency practitioner to manage the company's business during the reorganisation process may protect the creditors' interests that otherwise may have been undermined by the inherent bias of the prepetition management towards the controlling shareholders. However, the potential disruptions and the additional time and costs associated with appointing an outside trustee to control the company during the reorganisation represent significant drawbacks of the PIP-type process that may make it a less attractive restructuring device for companies in distress. Furthermore, the immediate removal of the prepetition management upon the commencement of the PIP-type process may incentivise such management to delay initiating the reorganisation process until it is too late for the company to be effectively restructured.

The second part of the chapter discussed the two managerial models for corporate reorganisation procedures under Saudi BL 2018: the DIP model employed under the PS process and the modified DIP or the co-determination model applied under the FR process.

The author argued that the DIP model employed under the PS procedure is not suitable for the concentrated structure of the Saudi share market, where many of the largest companies are closely controlled by strong shareholders. Considering the strong association between the ownership and the management in such companies, leaving the prepetition directors in full control over the company's business during the reorganisation process may increase the risk of the process being manipulated by the controlling shareholders. Furthermore, the PS process does not provide creditors with protective measures, such as the creation of a creditors' committee or the right to request the appointment of a trustee for cause, to counter the potential risk of shareholder manipulation, which can exacerbate the situation. The only remedy available for creditors to combat such risk is to apply to the court to terminate the PS procedure due to material breaches during the procedure or because the management committed an offence prohibited under the law. Upon its decision to terminate the PS process, the court may, based on its discretion, order the commencement of the FR procedure. Conversion between the procedures is likely to increase the time and costs involved in the restructuring. Accordingly, if the PS procedure is not abolished, as Chapter 3 recommends, altering the current DIP model

of control under the PS process and adopting the co-determination model applied under the FR procedure in its stead is highly recommended.

The co-determination system is more suitable for Saudi's concentrated ownership market than either the DIP or the PIP model. Such a system has been adopted in several European jurisdictions, such as Germany and France, which, like Saudi Arabia, are categorised as concentrated ownership markets. For the Saudi restructuring regime, the co-determination model provides three significant advantages that do not coexist in either the DIP or the PIP model. First, the appointment of an insolvency practitioner provides creditors with protection against the potential risk of bias by the incumbent management towards the controlling shareholders. This is in contrast to the DIP model, the current application of which, under the PS process, involves a high risk of shareholder manipulation.

The second benefit of the co-determination model for the Saudi reorganisation system is its encouragement for early filing of the restructuring process. In contrast to the PIP approach, under which the prepetition management is displaced once the restructuring proceeding commences, leaving such management in charge of the company's daily business activities under the co-determination system while subject to the supervision of the insolvency practitioner may incentivise it to seek reorganisation in a timely fashion.

The third merit of the co-determination system is related to the time, costs and efficiency of the reorganisation process. Allowing the pre-filing management to remain in charge of the company's daily business operations is likely to speed up the restructuring process and make it more efficient, due to the knowledge and familiarity such management has about the company's business. Furthermore, leaving the prepetition directors in charge of the day-to-day management activities of the business under the supervision of the insolvency practitioner is far less expensive than removing such directors and placing the full executive and operational control of the company in the hands of the insolvency practitioner.

The following chapter discusses the application of the moratorium under Saudi restructuring law. The examination focuses on two main aspects of the moratorium: its scope and the circumstances under which relief from the moratorium may be granted.

Chapter 6: Moratorium/Automatic Stay

The moratorium or automatic stay is a fundamental component of corporate restructuring procedures. It provides the distressed company with a brief respite from its creditors by temporarily barring all collection efforts and all proceedings against the company and its assets. By temporarily barring such actions, the moratorium provides the company with time during which it can negotiate with its creditors and formulate a proper restructuring plan.[664] Furthermore, the moratorium is designed to assist in keeping the company's assets together by preventing their piecemeal dismemberment by creditors.[665] Such dismemberment, if not restricted, would undermine the prospect of reorganisation.

Moratorium does not only benefit debtors: it also protects the interests of creditors by warranting an orderly administration of the debtor's estate.[666] In the absence of a moratorium, 'certain creditors would be able to pursue their own remedies against the debtor's property. Those who acted first would obtain payment of the claims in preference to and to the detriment of other creditors.'[667] Thus, by stopping individual enforcement and collection efforts, the moratorium restrains the competition among diligent creditors and ensures that each creditor is treated fairly. Importantly, the moratorium does not extinguish creditors' claims or other rights: it only delays their enforcement.[668]

Given the significance of the moratorium in the corporate reorganisation process, the purpose of this chapter is to examine the efficacy of moratorium under the Saudi restructuring law in light of the UK and the US experiences. The chapter is principally concerned with two key

[664] See HR Rep No 595, 95th Congress, 1st Session 340 (1977); UNCITRAL (n 376) 84. (Noting that the application of a moratorium during reorganisation proceedings 'facilitates the continued operation of the business and allows the debtor a breathing space to organize its affairs, time for preparation and approval of a reorganization plan').

[665] Wessels and Madaus (n 501) 213. This protective role of the moratorium has also been recognised by courts. For example, in the case of *Small Business Admin. v. Rinehart*, the US Court of Appeals noted that '[a] primary purpose of the automatic stay provision is to afford debtors in Chapter 11 reorganizations an opportunity to continue their businesses with their available assets' 887 F2d 165 (8th Cir 1989) at 168. Similarly, Patten J noted in the UK case of *A.E.S. Barry Ltd. v TXU Europe Energy Trading* that the moratorium 'is primarily concerned to avoid the assets of the Company from being removed by creditors whilst the administrators continue to attempt to achieve the statutory purposes for which the administration order was made' [2004] EWHC 1757 (Ch) at 14.

[666] See Jack F Williams, 'Application of the Cash Collateral Paradigm to the Preservation of the Right to Setoff in Bankruptcy' (1990) 7 Bankr Dev J 27; Scott T Silverman, 'The Administrative Freeze and the Automatic Stay: A New Perspective' (1994) 72 Wash ULQ 441; Donna Renee Tobar, 'The Need for a Uniform Void Ab Initio Standard for Violations of the Automatic Stay' (2002) 24 Whittier L Rev 3.

[667] HR Rep No 595, 95th Congress, 1st Session 340 (1977).

[668] Finch and Milman (n 244) 317; Robert A Johnson and Marilyn C O'Leary, 'Automatic Stay Provisions of the Bankruptcy Act of 1978' (1983) 13 NML Rev. 599, 602–603; Williams (n 666) 30.

issues: the scope of the moratorium and the circumstances under which relief from a moratorium may be granted. The chapter is divided into three parts. The first two parts demonstrate how those two key issues are addressed in the UK and US laws. The third part then examines how Saudi law addresses those issues in comparison to the UK and the US perspectives provided in the first two parts of the chapter.

6.1 Moratorium under the UK Administration

Currently, two restructuring processes provide the benefit of a moratorium in UK insolvency law: administration and the recently introduced stand-alone company moratorium procedure. For the purposes of this chapter, only the application of moratorium under the administration procedure is addressed. The limitation to the administration moratorium is justified by two reasons. First, the administration moratorium has been in force since its introduction in 1986; thus, it has been well tested in practice, distinguishing it from the new stand-alone moratorium which came into force in June 2020 and has not yet been well tested. Second, as illustrated in Chapter 4, unlike the administration procedure, the new moratorium regime's scope of application is narrow; it applies only to 'eligible companies', a distinction that excludes many companies.[669] Therefore, the moratorium provided under the administration process, compared to the stand-alone moratorium regime, is more accessible to distressed companies seeking restructuring.

The moratorium arguably represents the most distinctive feature of the administration procedure, as it provides the company temporary relief from being harassed by its creditors.[670]The significance of the protective moratorium as a key element of the administration process has been affirmed by the courts. In *Re Dianoor Jewels Ltd*,[671] Blackburne J noted:

> The fact that the making of an administration order may thwart the genuine claims of a third party is not a reason for not making it. … It frequently happens that a purpose of the making of an administration order is to stop the prosecution of legal proceedings against the company's property. It is none the worse for that.[672]

[669] IA 1986, Sch ZA1.
[670] Keay and Walton (n 128) 97.
[671] [2001] 1 BCLC 450.
[672] ibid at 458.

Basically, two forms of the moratorium exist within the administration process: interim moratorium and substantive moratorium.[673] The application of an interim moratorium is triggered as soon as the application for the administration order is filed in court, and it remains effective until the administration order is made or until the application is dismissed.[674] If the administration is sought through an out-of-court method, the interim moratorium applies from the date the notice of intention to appoint is filed in court.[675] If the appointment is made by a qualifying floating charge holder in accordance with paragraph 14 of Schedule B1, the interim moratorium applies from the date the notice of intention to appoint is filed and lasts either until the appointment is made or for a period of five business days starting with the date of filing if it ends without an administrator being appointed.[676] If the out-of-court appointment is commenced by the company or directors, the interim moratorium applies from the time the notice of intention to appoint is filed in the court in accordance with paragraph 27.[677] In this case, the interim moratorium lasts either until the appointment takes place or after a period of 10 business days from the date of filing if the notice of intention ends without the appointment being made.[678]

The objective of the administration procedure may be undermined if the moratorium were only applicable as soon as the company formally entered into administration.[679] For instance, in the absence of an interim moratorium, judgment creditors may attempt to act quickly to enforce their judgments against the company's property once they became aware of the intention to put the company into administration. The interim moratorium is intended to fill this gap and prevent this type of action, which would otherwise frustrate the administration process before it has even started.[680] The interim moratorium essentially follows the same terms as the substantive moratorium. However, as no administrator is in office, relief from the interim moratorium can only be sought from the court.

[673] See Finch and Milman (n 244) 316–317.
[674] IA 1986, Schedule B1, para 44.
[675] IA 1986, Schedule B1, para 44.
[676] IA 1986, Schedule B1, para 44.
[677] IA 1986, Schedule B1, para 44.
[678] IA 1986, Schedule B1, para 44.
[679] Keay and Walton (n 128) 97.
[680] ibid 97–98; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 158; Sanford U Mba, *New Financing for Distressed Businesses in the Context of Business Restructuring Law* (Springer 2019) 95–96.

When the company formally enters into administration either by court appointment or by out-of-court appointment, the interim moratorium is replaced with the substantive moratorium, which lasts until the end of the administration procedure. The scope of the substantive moratorium is discussed next.

6.1.1 Scope of Administration Moratorium

Generally speaking, the ambit of the moratorium operating in the administration procedure is very wide, as it blocks any kind of hostile legal actions against the debtor company.[681] Once the company is in administration, no resolution may be passed or order made for the winding up of the company.[682] Moreover, certain actions cannot be taken without the consent of the administrator or leave from the court. These actions include enforcing 'any security over the company's property', repossessing 'goods in the company's possession under a hire-purchase agreement', exercising the right of a landlord to forfeit a lease contract by peaceable re-entry to corporate premises and commencing or continuing any legal process against the company or its property.[683] Protection of the moratorium is also extended to cover property owned by the company but in the possession of third parties.[684]

The scope of the moratorium was subject to a great deal of litigation when the administration process was first introduced in 1986.[685] At that time, the boundaries of the administration moratorium had not yet been clearly established, and some ambiguity existed regarding the impact of the moratorium on certain types of actions. To eliminate these uncertainties, the courts have done their utmost to clarify the effect of the moratorium and to set out principles for the exercise of property rights despite the moratorium.

One of the ambiguities surrounding the moratorium under the original administration regime was the effect of that moratorium on the landlord's rights. It was uncertain whether the landlord of premises occupied by the company in administration could exercise his or her right of re-

[681] See David Milman, 'Moratoria in UK Insolvency Law: Policy and Practical Implications' (2012) 317 Co. L.N. 1, 3.
[682] Schedule B1, para 42. Nevertheless, this does not apply to winding up petitions presented on public interest ground under s 124A of IA 1986 or to petitions presented by the Financial Services Authority under s 367 of the Financial Services and Markets Acts 2000. ibid.
[683] See Schedule B1, paras 42–43.
[684] *Re Atlantic Computer Systems pls (no.1)* [1992] Ch 505.
[685] See Milman (n 681) 3; Radford Goodman, 'Testing the Boundaries of the Administration Moratorium' (2011) 4 Corporate Rescue and Insolvency 51, 52.

entry to the corporate premises in the case of breach of covenant, or whether the right of re-entry was prohibited by the moratorium.[686] It is difficult to exaggerate the importance of this point to a company in administration since the protection provided by the moratorium would be less effective in facilitating the rescue efforts if the company were deprived of access to its work premises.[687]

Forfeiting a lease by re-entry was not included within the list of actions restricted by the prior version of the moratorium under section 11 of IA 1986 as originally drafted. As such, judicial views were divided as to whether the exercise of such remedy could be categorised as an enforcement of security and, thus, subject to moratorium under section 11(3).[688] It was suggested in the case of *Exchange Travel Agency* v. *Triton plc*[689] that peaceable re-entry involved enforcement of security interests and, therefore, would be covered by the moratorium. However, judicial views changed by the time a decision was made in *Razzaq* v. *Pala,*[690] which put forward the dominant view that the ability of landlords to forfeit a lease by peaceable re-entry is unaffected by a moratorium. In 2000, the UK Department of Trade and Industry (DTI) recommended that the law be changed to bring the landlord's right of peaceable re-entry within the scope of the moratorium.[691] This change was introduced by section 9 of the Insolvency Act 2000, which expanded the scope of the moratorium to cover a landlord's right of forfeiture by peaceable re-entry. The remedy is now expressly included within the scope of the moratorium under the post-EA 2002 administration regime.[692]

In addition to the impact of the moratorium on landlords' rights, some degree of judicial uncertainty also existed concerning exactly what proceedings were covered by the moratorium under section 11(3)(d) (now paragraph 43 (6) of Schedule B1).[693] A very strict interpretation

[686] Peaceable re-entry 'was a procedure allowing a landlord to forfeit a lease without having to obtain a court order and could be instigated upon non-payment of rent or breaches of covenant by the tenant. All the landlord normally had to do in practice was to change the locks and exclude the tenant from the premises'. Finch and Milman (n 244) 310.
[687] ibid; Keay and Walton (n 128) 101.
[688] A review of the conflicting authorities over this issue was provided by Neuberger J. in *Re Lomax Leisure Ltd* [2000] BCC 352
[689] [1991] BBC 341.
[690] [1997] 1 WLR 1336.
[691] DTI/HM Treasury Report 'A Review of Company Rescue and Business Reconstruction Mechanisms' (DTI 2000) 37.
[692] See Schedule B1, para 43 (4).
[693] See Goode (n 130) 435–437; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 159–160. Although the wording of paragraph 43(6) is slightly different to that used under the old section 11(3)(d), the courts seem to regard decisions made under the original section 11(3)(d) as authoritative. See *Re Frankice (Golders Green) Ltd* [2010] EWHC 1229 (Ch) at 37.

of section 11(3)(d) was made by the Scottish Court of Session in *Air Ecosse Ltd v Civil Aviation Authority*.[694] In that case, the court suggested that 'other proceedings' in section 11(3)(d) should be given a restricted construction *ejusdem generis* with preceding provisions and, thus, be confined to proceedings brought by a creditor against the company in relation to a debt due by the company. This narrow construction has not been followed by the courts in subsequent decisions, however. Instead, the courts have adopted a very wide construction in which proceedings affected by the moratorium are not confined to claims brought by creditors against the company but include claims against the company by third parties.[695] Moreover, it has been held that the moratorium covers not only the civil proceedings but extends to stay criminal proceedings[696] and any judicial or quasi-judicial proceedings, such as arbitration proceedings[697] and applications to industrial tribunals.[698]

A clear example illustrating the judicial willingness to interpret the scope of the moratorium broadly was the Court of Appeal decision in *Rhondda Waste Disposal Ltd.*[699] In this case, a company (R) operated a landfill site under the terms of a waste management licence. The UK Environment Agency served an enforcement notice on (R), requiring compliance with the terms of the licence. An injunction was subsequently obtained, reflecting the terms of the notice. (R) was then given a six-month period in which to remedy the operation deficiencies, but it failed to do so and went into administration. The Environment Agency then commenced criminal proceedings against the company. The question was raised whether criminal proceedings were covered by the moratorium in the administration procedure, thus making it necessary to obtain consent from the administrator or leave from the court to commence or continue these proceedings against a company undergoing administration.

The Agency argued that criminal proceedings should not be stayed by the moratorium provisions. It stated that the court should follow the decision in *Air Ecosse Ltd v Civil Aviation*

---

[694] (1987) 3 BCC 492.

[695] See, e.g. *Biosource Technologies Inc v Axis Genetics Plc* [2000] 1 BCLC 286, where the court held that the prosecution of an action brought by a competitor for the revocation of a patent held by a company in administration involved the commencement or continuance of proceedings against the company for the purposes of s 11(3)(d) (now para 43(6) of Sch B1), and, therefore, required either the consent of the administrator or the leave of the court.

[696] *Rhondda Waste Disposal Ltd* [2001] Ch 57.

[697] See *Bristol Airport Plc v Powdrill* [1990] Ch 744 at 765; and *Carr v British International Helicopters Ltd* [1994] ICR 18 at 27.

[698] *Carr v British International Helicopters Ltd* [1994] ICR 18; and *Re Divine Solutions (UK) Ltd* [2004] CLY 2116.

[699] [2001] Ch 57.

Authority,[700] which had suggested that the moratorium provisions of IA 1986 only covered proceedings brought by creditors to enforce rights relating to the recovery of money or property. The Court of Appeal, however, was not convinced by the Agency's arguments and held that the words 'other proceedings' in IA 1986 clearly meant that no proceedings of any kind, criminal proceedings included, were to be permitted in the absence of leave.[701] The court noted that other provisions of the Act referred to criminal offences by the company, and that if the intention had been to exclude criminal proceedings from the scope of moratorium, there would have been a specific proviso to that effect.[702] Moreover, the court stated that the purpose of administration was to provide breathing space to the company to produce proposals for its creditors, and that such a goal could be hindered if criminal and civil proceedings were allowed to proceed without restrictions against the debtor undergoing administration.[703] Furthermore, the Court of Appeal stated that public policy supported the view that leave should be required for the commencement or continuation of criminal proceedings against a company in administration due to the vast extent of criminal offences that may be committed by companies and the fact that the interests of creditors may be negatively affected if criminal prosecution were allowed to proceed, without restriction, against the debtor company during the administration process. It was suggested that courts dealing with the administration procedure were uniquely placed to weigh the arguments for and against granting leave. Nevertheless, based on the facts of the case, and due to the seriousness and longstanding of the breaches involved, the court held that the interests of the creditors should not be allowed to trump all other considerations. Therefore, the court granted the Agency leave to continue the criminal proceedings against the company.

Moreover, the notion that the scope of the administration moratorium is designed to be construed broadly was emphasised in the recent case, *The Financial Conduct Authority v Carillion Plc*.[704] In this case, the court drew a distinction between the administration moratorium under paragraph 43(6) of Schedule B1[705] and the liquidation stay under section

[700] (1987) 3 BCC 492.
[701] *Rhondda Waste Disposal Ltd* [2001] Ch 57 at 27.
[702] ibid.
[703] ibid at 34.
[704] [2021] EWHC 2871 (Ch).
[705] Paragraph 43(6) provides that once the company is in administration, '[no] legal process (including legal proceedings, execution, distress and diligence) may be instituted or continued against the company or property of the company except (a) with the consent of the administrator, or (b) with the permission of the court.'

130(2) of IA 1986,[706] and stressed that the reach of the former is intended to be wider than the latter. Green J stated the following:

> As the purpose of para. 43(6) is wider than that of s.130(2) … in particular when the administrators are trying to save the company as a going concern or preserve its business in readiness for a sale, it is important to be able to prevent any interference or prejudicial action that may undermine that purpose and so the net should be drawn as widely as possible. Parliament's intention would have been to enable the court to control anything that might detrimentally affect the administrators fulfilling the purpose of the administration.[707]

Despite its wide range, the administration moratorium does not cover certain types of regulatory action in the context of regulated industries.[708] In the case of *Air Ecosse Ltd v Civil Aviation Authority,*[709] it was held that an application by a competitor to have the company's aviation licence revoked did not constitute proceeding within the meaning of section 11(3)(d), and therefore, neither the consent of the administrator nor the leave of the court was required. Similarly, in *Re Railtrack Plc*,[710] the Court of Appeal held that determination by the Rail Regulator of an application made by train operators to use the railway network could not be categorised as legal or quasi legal proceedings, and therefore, was not covered by the moratorium. The court defended its decision by stating that the determination in question fell within the statutory powers of the Rail Regulator who was obliged to exercise his powers in what served the national and public interest in having an efficient and effective railway system and that the exercise of these statuary powers should not be restricted by the fact that a particular company is in administration.

It is clear from the observations provided that the courts have played a critical role in interpreting the scope of the moratorium as widely as possible to provide companies in administration with adequate protection against all kinds of actions that may frustrate the prospect of their rescue. However, the courts have been, understandably, cautious not to construe the ambit of the moratorium too broadly in a way that would hinder regulators from exercising their statutory powers in serving the public interest.

---

[706] Section 130(2) states that '[when] a winding-up order has been made or a provisional liquidator has been appointed, no action or proceeding shall be proceeded with or commenced against the company or its property, except by leave of the court and subject to such terms as the court may impose.'
[707] *The Financial Conduct Authority v Carillion Plc* [2021] EWHC 2871 (Ch) [65].
[708] See William Trower QC and others, *Corporate Administrations and Rescue Procedures* (3rd edn, Bloomsbury Publishing 2017) 428.
[709] (1987) 3 BCC 492.
[710] [2002] 1 WLR 3002.

6.1.2 Relief from the Administration Moratorium

As illustrated in the previous section, the impact of the moratorium is procedural, since it is intended to temporarily suspend the enforcement of the creditors' rights, not extinguish them. Nevertheless, in some circumstances, the suspension imposed by the moratorium may maximise the losses incurred by creditors. For example, secured creditors may be adversely affected by a decline in the value of the secured property during the moratorium period. As a safeguard against such undesired impacts, IA 1986 permits the creditors of a company in administration to seek relief from the moratorium by obtaining either a leave from the court or the administrator's consent.

However, IA 1986 does not provide guidelines on how the discretionary power to grant relief from the moratorium should be exercised. The leading authority providing such guidelines is the Court of Appeal's decision in *Re Atlantic Computer Systems Plc*.[711] In that case, a company in administration had leased a large number of computers and then subleased them to a number of end users. Although the computers were not physically in the possession of the company because they had been subleased to other parties, the court held that the computers should remain in the company's possession for the purposes of the moratorium. Thus, owners of the computers could not repossess the computers from the sublessees without the consent of the administrator or the leave of the court. The Court of Appeal granted permission for repossession and emphasised the principle that 'an administration for the benefit of unsecured creditors should not be conducted at the expense of those who have proprietary rights which they are seeking to exercise, save to the extent that this may be unavoidable and even then this will usually be acceptable only to a strictly limited extent'.[712] The court also laid down a non-exhaustive set of factors to be considered by the courts or administrators when deciding whether to grant relief from a moratorium.[713] A summary of those factors is as follows:

1. The burden is on the person who seeks leave to show that the leave should be granted.
2. If granting the leave would not impede the purpose of the administration, then leave will usually be granted.
3. Otherwise, the court should balance the interests of the party seeking the relief with the interests of the other creditors.

[711] [1992] Ch 505.
[712] ibid at 542.
[713] ibid, per Nicholls LJ at 542–544.

4. In carrying out this balancing exercise, great weight should be given to the proprietary interests of the applicant. Administration 'should not be used to prejudice those who were secured creditors when the administration order was made in lieu of a winding up order'.[714]
5. Normally, a leave will be granted if significant loss would be caused to the applicant by the refusal. However, if granting the leave would cause substantially greater loss to other creditors, or would cause loss which is out of all proportion to the benefit which the leave would confer on the applicant, that may outweigh the loss to the applicant caused by a refusal.
6. In determining these losses, the court will consider a number of factors such as 'the financial position of the company, its ability to pay the rental arrears and the continuing rentals, the administrator's proposals, the period for which the administration order has already been in force and is expected to remain in force, the effect on the administration if leave were given, the effect on the applicant if leave were refused, the end result sought to be achieved by the administration, the prospects of that result being achieved and the history of the administration so far'.[715]
7. It will often be essential, when considering these suggested consequences, to assess the probability that they will occur.
8. The conduct of the parties may also be a relevant factor.

The court made it clear that the guidelines provided in this case are inadequate since the circumstances in which leave is sought will vary almost infinitely.[716] Nonetheless, three factors from these guidelines have been commonly relied upon by the courts when considering granting a leave from a moratorium: the impact of the leave on the purpose of the administration, the balance of interests and the conduct of the parties.

The first step the court would take when considering granting leave from a moratorium is to question whether such leave would impede the purpose of the administration. This seems logical since the moratorium is primarily intended to help the company achieve the purpose of administration. If it is established that such purpose would not be frustrated by the leave, the court would grant such leave without engaging in any further acts of balancing the interests of the applicant with those of the other parties. This would often be the case where the objective of the administration has already been achieved or substantially achieved.[717] For example, in

[714] ibid at 542.
[715] ibid at 543.
[716] ibid at 542.
[717] See, e.g. *Safe Business Solutions Ltd v Cohen* [2017] EWHC 145 (Ch); *Metro Nominees (Wandsworth) (No 1) Ltd v Rayment* [2008] B.C.C 40.

the case of *Lazari GP Ltd v Jervis*,[718] landlords applied for permission to forfeit a lease that they had granted to a company in administration, which was occupied by a purchaser under a pre-pack sale. The court granted permission on the grounds that the purpose of the administration had been substantially achieved by the sale agreement and granting the landlords permission to pursue their proprietary rights would not interfere with or adversely affect that result. Similarly, in *Magical Marketing Ltd v Phillips*,[719] the applicant company was granted leave to continue proceedings against the company in administration for infringement of copyright, breach of fiduciary duty and misuse of confidential information. An essential factor the court relied on in its decision was its finding that allowing the applicant company to pursue its claim would not impede the objective of the administration, which was achieved on the first day when the total assets and undertaking of the debtor company were sold to an associated company.[720]

It is when there is a likelihood that granting the leave would impede the purpose of the administration, which would normally be the case, that the court would move to engage in a difficult balancing exercise, weighing the legitimate interests of the applicant against those of the debtor and other creditors.[721] The applicant in this case must demonstrate that without obtaining the leave, he or she would suffer a loss of some kind, although this may not be sufficient grounds for granting the leave if that leave would cause a substantially greater loss to other parties.[722] An example illustrating how this balance of interests is exercised is the case of *Re David Meek Access Ltd*,[723] where the court refused to grant leave to lessors to repossess their goods, which were under the possession of the company in administration. The court justified its decision by stating that granting such leave would render the administration order pointless and cause significant losses to other creditors, outweighing the potential losses caused to the lessors by the refusal.

[718] [2013] BCC 294.
[719] [2008] FSR 36.
[720] ibid at 980.
[721] See David Milman, 'Moratoria on Enforcement Rights: Revisiting Corporate Rescue' [2004] Conveyancer Prop Law J 89, 99; Jennifer Payne, 'The Role of the Court in Debt Restructuring' (2018) 77 Cambridge Law Journal 124, 143.
[722] *Re Atlantic Computer Systems Plc* [1992] Ch 505 at 542.
[723] [1993] BCC 175.

Finally, the conduct of the parties may be a material factor in favour or against granting the leave.[724] For example, in the recent case of *Bernhard's Sport Surfaces Ltd v Astrosoccer4U Ltd*,[725] the applicant was granted permission to enforce an arbitration award against a company that had given notice of intention to appoint an administrator. The court based its decision on the fact that the notice of intention was entirely bogus and was part of a series of events designed by the company to avoid paying its debt. Moreover, in *Bristol Airport Plc v Powdrill*,[726] the Court of Appeal refused to grant leave because the applicants had received benefits under the administration and had only attempted to enforce their security at a later stage. Sir Nicolas Browne-Wilkinson V.-C. stressed that secured creditors who wish to enforce their security should make their positions clear to the administrator at the outset of the administration. 'To stand by and accept all the benefits of an administration and then, at the eleventh hour, seek to enforce a right which is inconsistent with the achievement of the statutory purpose is in my judgment unacceptable.' [727]

[724] See *South Coast Construction Limited v Iverson Road Limited* [2018] B.C.C. 123.
[725] [2018] BCC 147.
[726] [1990] Ch 744.
[727] ibid at 767.

6.2 Automatic Stay in the US Chapter 11 Procedure

As an immediate consequence of filing a Chapter 11 petition, an automatic stay is imposed on the commencement or continuation of most proceedings and enforcement actions against the debtor.[728] The stay is intended to bar all collection efforts by creditors and allow the debtor company to reorganise effectively.[729] The following sections discuss the scope of the stay and the situations for which a relief from the stay may be granted.

6.2.1 Scope of the Automatic Stay

Similar to the position under the UK insolvency regime, the scope of the automatic stay under US Chapter 11 was intentionally designed to be extremely broad so it would cover various forms of formal and informal actions brought by both secured and unsecured creditors against the debtor company and its estate.[730] Section 362(a) of the US Bankruptcy Code contains eight subparagraphs describing the acts and actions that are stayed. Most importantly, the stay bars the following conduct:[731]

1. The commencement or continuation of, including the issuance or employment of the process for, a judicial, administrative or other action or proceeding against the debtor, or to recover a claim against the debtor;
2. The enforcement of a judgment against the debtor or against property of the estate;
3. Any act to obtain possession of property of the estate;
4. Any act to create, perfect or enforce any lien against property of the estate or against property of the debtor;
5. Any act to collect, assess or recover a claim against the debtor.

The list of stayed acts provided under section 362(a) is comprehensive, which means an action not covered under this list is not barred by the stay.[732] Nevertheless, according to section 105(a), the court still has the jurisdiction to issue an injunction against any actions not covered by the automatic stay provision in section 362(a). Section 105(a) allows bankruptcy courts to

[728] John D. Ayer, Michael Bernstein and Jonathan Friedland, 'An Overview of the Automatic Stay' (2004) 22 The American Bankruptcy Institute Journal 1; David P Stromes, 'The Extraterritorial Reach of the Bankruptcy Code's Automatic Stay: Theory vs. Practice' (2007) 33 Brook. J. Int'l L. 277, 280.
[729] Daniel J Sheffner, 'Situating Reimposition of the Automatic Stay Within the Federal Common Law of Bankruptcy' (2015) 47 U. Tol. L. Rev. 447, 451.
[730] Williams (n 666) 28–29.
[731] Bankruptcy Code, s 362(a).
[732] Charles J Tabb and Ralph Brubaker, *Bankruptcy Law: Principles, Policies, and Practice* (4th edn, LexisNexis 2015) 190.

'issue any order, process, or judgment that is necessary or appropriate to carry out the provisions' of the Bankruptcy Code.[733]

Despite the similarities between the automatic stay under the US bankruptcy law and the moratorium under the UK administration procedure, they differ in two significant ways. First, in contrast to the UK administration moratorium, the US automatic stay is subject to a lengthy list of exceptions under the Bankruptcy Code. Second, unlike the administration moratorium, the automatic stay may, in limited circumstances, extend to protect non-debtor parties. These two features of the automatic stay are addressed next.

6.2.1.1 Exceptions to the Automatic Stay

Despite the wide scope of the stay, section 362(b) lists several excepted actions to which the automatic stay does not apply. These exemptions are believed to reflect the viewpoint of US Congress that certain interests should have priority over the narrow interests of debtor individuals and creditors.[734] Two critical exemptions are set out in subsections (1) and (4) of section 362(b). Subsection (1) exempts the commencement or continuation of criminal action or proceedings against a debtor, and subsection (4) exempts the commencement or continuation of an action or proceeding by a governmental unit to enforce police or regulatory powers. These two exceptions are illustrated in the following sections.

6.2.1.1.1 Criminal Proceeding Against the Debtor

The exemptions in section 362(b) encompass a wide cluster of various statutory objectives. One of the most significant of those objectives is that the bankruptcy case not be allowed to interfere with the operation of the government's fundamental functions.[735] Presumably, the interests of the body politic in facilitating the common good exceed the interests of the debtor and creditors.[736] This principle is classified most explicitly in section 362(b)(1), which excepts from the stay 'the commencement or continuation of a criminal action or proceeding against the debtor'.[737] As the legislative history accentuates, 'the bankruptcy laws are not a haven for

[733] Bankruptcy Code, s105(a).
[734] John D. Ayer, Michael Bernstein and Jonathan Friedland (n 728) 1.
[735] Tabb, *Law of Bankruptcy* (n 279) 266.
[736] ibid.
[737] Bankruptcy Code, s 362(b)(1).

criminal offenders'.[738]A similar rationale for this exemption was featured in *Barnette v. Evans*,[739] in which the Court of Appeals expressed the following:

> The purpose of bankruptcy is to protect those in financial, not moral, difficulty. The bankruptcy courts were not created as a haven for criminals … There is a public interest in every good faith criminal proceeding … , which overrides any interest the bankruptcy court may have in protecting the financial interest of debtors.[740]

The application of section 362(b)(1) is usually straightforward. The hard cases emerge, however, when the criminal proceedings constitute a disguised debt collection.[741] This may occur when the criminal law obliges the debtor to compensate a victimised creditor.[742] Indeed, the primary intention of the criminal proceeding may be to force the debtor to pay a debt. Permitting criminal proceedings meant to disguise debt collections to escape the ambit of the automatic stay may result in the victimised creditor being paid in preference to, and to the detriment of, other creditors.[743] To avoid this, some courts have interpreted the exception to the automatic stay set forth in section 362(b)(1) narrowly and held that such exception is inapplicable to criminal proceedings for which the primary motive is the collection of a debt.[744] However, this limited interpretation was criticised by the Court of Appeals in *Re Gruntz*.[745] The court stated the following about such restricted construction:

> [It] is at odds with the plain words of the statute. Quite simply, the Bankruptcy Code declares that S 362 does not stay 'the commencement or continuation of a criminal action or proceeding against the debtor.' On its face, it does not provide any exception for prosecutorial purpose … If the statutory command of the Bankruptcy Code is clear, we need look no further: it must be enforced according to its terms.[746]

---

[738] HR Rep No 95-595, 95th Cong, 1st Sess, at 342 (1977).
[739] 673 F 2d 1250 (11th Cir 1982).
[740] *Barnette v. Evans*, 673 F 2d 1250 (11th Cir 1982) at 1251.
[741] Johnson and O'Leary (n 668) 608.
[742] Typical examples of this scenario are bad check cases. The courts in these cases will usually demand the debtor make good on the bad check. See Tabb, *Law of Bankruptcy* (n 279) 266.
[743] ibid.
[744] See, e.g. *In Re Dovell*, 311 BR 492 (Bankr SD Ohio 2004); *In Re Batt*, 322 BR 776 (Bankr ND Ohio 2005); *In Re Williamson-Blackmon*, 145 BR 18 (Bankr ND Ohio 1992).
[745] 202 F 3d 1074 (9th Cir 1999).
[746] *In re Gruntz*, 202 F 3d 1074 (9th Cir 1999) at 1085. For more discussion on this case, see Alex Hart, 'Not Quite Foucault's Pendulum: An Analysis of Gruntz and Bankruptcy Court Jurisdiction over the Automatic Stay' (2001) 37 Tulsa L Rev 607.

Therefore, the dominant judicial view has been to adopt a literal interpretation of section 362(b)(1) and conclude that all criminal proceedings, regardless of their primary motives, are excluded from the scope of the automatic stay.[747]

However, while section 362(b)(1) excludes all criminal proceedings from the scope of the automatic stay, the courts can use section 105(a) to issue an injunction against the commencement or continuation of a criminal action against the debtor. Nevertheless, multiple courts[748] have held that the exercise of this power must be in accordance with the principles set out in the Supreme Court's decision in *Younger v. Harris*.[749] In that case, the Supreme Court determined that state criminal proceedings should not be enjoined by federal courts except under 'extraordinary circumstances' when the applicant can demonstrate a 'great and immediate' danger of 'irreparable injury' to his or her federally protected rights and the danger 'cannot be eliminated by [the movant's] defense against a single criminal prosecution'.[750] In principle, *Younger's* strict requirements are satisfied if the movant can show that the criminal proceeding was brought forward in bad faith or for the purpose of harassment.[751]

6.2.1.1.2 Police and Regulatory Power Exceptions

Subsection 362(b)(4) excludes actions initiating or enforcing the police or regulatory powers of a governmental unit from the automatic stay. The legislative history expresses that the exemption in subsection 362(b)(4) would apply 'where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law'.[752] This exception is based on the view that filing for the bankruptcy procedure should not, by itself, excuse compliance with other laws absent compelling bankruptcy-specific justifications.[753]

[747] ibid; Tabb, *Law of Bankruptcy* (n 279) 266.
[748] See, e.g. *In re Fussell*, 928 F 2d 712 (5th Cir 1991); *Barnette v. Evans*, 673 F 2d 1250 (11th Cir 1982); *Matter of Davis*, 691 F 2d 176 (3d Cir 1982).
[749] 401 US 37 (1971).
[750] ibid at 46.
[751] ibid at 49–50.
[752] HR Rep No 95-595, 95th Cong, 1st Sess, at 343 (1977).
[753] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 161; Tabb, *Law of Bankruptcy* (n 279) 270.

The police or regulatory power in this context has been defined extensively, enveloping a wide assortment of conduct intended to protect the economic interests or the health and safety of the public.[754] This expansive definition, however, may produce a contention between the objectives of governmental police and regulatory powers, on one hand, and the objectives of federal bankruptcy law on the other.[755] In fact, treating each activity of police and regulatory power as exempted from the automatic stay would derail the effectiveness of bankruptcy laws.[756] Hence, ensuring a fair application of this exception to the automatic stay has necessitated that the expression 'police or regulatory power' be narrowly construed.[757] Comments made during the legislative discussions regarding section 362(b)(4) demonstrated that: '[t]his section is intended to be given a narrow construction in order to permit governmental units to pursue actions to protect the public health and safety and not to apply to actions by a governmental unit to protect a pecuniary interest in property of the debtor or property of the estate'.[758] A restricted construction would include governmental actions intended to secure the environment and safeguard the public's health and safety but would exclude any action that aims to safeguard monetary interests. Thus, the government must not utilise the semblance of 'police or laws' as a cover for acquiring special treatment in its status as a creditor of the debtor.

A central point of contention regarding this exemption that is regularly disputed is whether the governmental unit is really practising its 'police or regulatory' power or, instead, if it is acting as a creditor attempting to collect a debt owed to the government.[759] The courts have devised two main tests to resolve this dispute.[760] First, the court may apply the 'pecuniary purpose' test, which examines whether the governmental proceedings relate principally to safeguarding the government's financial interest in the debtor's property and not to issues of public safety and health. If the government actions are aimed at safeguarding the government's financial interests, the section 362(b)(4) exemption will not be applicable.[761] Alternatively, the court

[754] See, e.g. *In re Greenwald*, 34 BR 954 (Bankr SDNY 1983); *In re Shippers Interstate Service Inc*., 618 F 2d 9 (7th Cir 1980).
[755] Richard J DeMarco Jr, 'Notes: Clean-Up Orders and the Bankruptcy Code: An Exception to the Automatic Stay' (1985) 59 St. John's Law Review 292, 297–298.
[756] ibid 298.
[757] ibid.
[758] 124 Cong Rec H 11,092 (daily edn Sept 28, 1978) (statement of Rep Edwards).
[759] John D. Ayer, Michael Bernstein and Jonathan Friedland (n 728) 1.
[760] See Kathryn R Heidt, 'The Automatic Stay in Environmental Bankruptcies' (1993) 67 Am. Bankr. LJ 69, 79; Murray Tabb, 'Competing Policies in Bankruptcy: The Governmental Exception to the Automatic Stay' (1985) 21 Tulsa LJ 183, 191.
[761] *In re Universal Life Church, Inc*, 128 F 3d 1294 (9th Cir 1997).

may apply a second test, the 'public policy' test, under which the court asks whether the government's action seeks to 'effectuate public policy', in which case the exemption applies, or adjudicate 'private rights', in which case the exemption will not apply.[762] A suit will not fulfil the 'public purpose' test if it is brought principally to advantage individuals or entities instead of some more extensive segment of the public.[763] Tabb asserted that, concerning environmental cases, the decision is almost invariably in favour of the government, regardless of what tests are utilised.[764]

The UK insolvency law contains no comparative exemption. Thus, the UK insolvency regime does not distinguish between circumstances in which the governmental unit's proceedings against the debtor are intended to protect public interests and those in which proceedings seek to protect the monetary interests of the government. The moratorium applies to all government proceedings, regardless of motive. When the moratorium hinders the statutory duties of a governmental body, the government body may seek relief from the moratorium by the administrator or the court. Moreover, there will be other cases in which the public interest is secured through a conclusion that the government's action does not constitute proceedings within the meaning of Schedule B1, paragraph 43, of IA 1986 and, therefore, not be halted by the moratorium.[765]

6.2.1.2 Application of the Automatic Stay to Non-debtors

As a general principle, the automatic stay does not apply to non-debtor entities.[766] Therefore, the stay is not applicable against non-debtor general partners of a debtor partnership, nor will the stay halt any actions against the guarantor of the debtor's debt. Nonetheless, in very limited circumstances, courts have applied two sections of the law to extend the automatic stay's scope to protect non-debtor parties in Chapter 11 cases: section 362(a) and section 105.[767]

By its language, section 362(a) applies only to actions against the debtor. Courts, however, have extended the scope of this section to protect non-debtor parties in 'unusual circumstances'. The 'unusual circumstances' standard was articulated in *A.H. Robins*

[762] *Lockyer v Mirant Corp*, 398 F 3d 1098 (9th Cir 2005).
[763] ibid at 1109.
[764] Tabb, *Law of Bankruptcy* (n 279) 269.
[765] Trower and others (n 708) 54.
[766] *In re Panther Mountain Land Dev*, 686 F 3d 916 (8th Cir 2012).
[767] *In re Bailey Ridge Partners*, 571 BR 430 (Bankr ND Iowa 2017).

Company, Inc. v. Piccinin[768] in which the Fourth Circuit set the condition that for the automatic stay to apply to non-debtors, unusual circumstances must be present. However, very few unusual circumstances justify extending the stay protection to claims against non-debtors.[769] In *Robins*, the court expressed that 'unusual circumstances' incorporate situations in which 'there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or finding against the debtor'.[770] In fact, this is what had occurred in *Robins*.

In that case, the debtor company filed for Chapter 11 after being overwhelmed by a flurry of product liability lawsuits related to a faulty contraceptive device it manufactured. Claimants brought civil actions against various key directors and officers of the debtor company as well. The company requested that the court expand the protection of the automatic stay to apply to the pending civil lawsuits against those directors and officials on the grounds that those parties were closely connected to the company, so allowing actions to proceed against them would inevitably impact the company's efforts to reorganise. The Fourth Circuit affirmed the lower court's conclusion that the officials' relationships with the debtor company constituted 'unusual circumstances' and, as such, justified the extension of the automatic stay under section 362(a)(1) to apply to the civil actions against those non-debtor parties. The lower court based its decision on the following grounds:

> (1) [The] continuation of litigation in the civil actions threatened property of [the debtor's] estate, burdened and impeded [the debtor's] reorganization effort, contravened the public interest, and rendered any plan of reorganization futile; and (2) that this burden on [the debtor's] estate outweighed any burden on the … claimants caused by enjoining their civil actions.[771]

The other alternative used by bankruptcy courts to enjoin actions against non-debtors is the wide power afforded them in section 105(a).[772] This section furnishes courts with the discretion to 'issue any order, process or judgment that is necessary or appropriate to carry out the

[768] 788 F 2d 994 (4th Cir 1986).
[769] *Ritchie Capital Management, LLC v Jeffries*, 653 F 3d 755 (8th Cir 2011).
[770] *A H Robins C, Inc v Piccinin*, 788 F 2d 994 (4th Cir 1986) at 999.
[771] ibid at 997.
[772] See, generally, Kathleen A Orr, 'Enjoining Foreign Actions Against Non-Debtor Entities: In Re Lyondell Chemical Company' (2010) 7 Intl Corporate Rescue 259.

provisions of this title'.[773] The utilisation of section 105 to stay creditors' claims against non-debtors should only be availed under special circumstances when failure to do so will negatively impact the bankruptcy estate and pressure the debtor through that third party.[774] In deciding whether to issue an injunction to stay creditors' claims against non-debtors under section 105, courts frequently consider four factors:

> (1) whether there is a likelihood of successful reorganization; (2) whether there is imminent irreparable harm to the estate in the absence of an injunction; (3) whether the balance of harms tips in favor of the moving party; and (4) whether the public interest weighs in favor of an injunction.[775]

In the recent case of *In re Bailey Ridge Partners*,[776] Iowa Bankruptcy Court relied on section 105 to stay claims by a Chapter 11 debtor's secured creditor against the debtor's guarantors and the co-borrower after determining that the guarantors and co-borrower played critical roles in the operation of the debtor company, which was likely to reorganise successfully and repay the creditor in full. Applying the four-factor test, the court determined that: (1) the debtor was likely to reorganise effectively; (2) the guarantors and co-borrower were crucial to the debtor's reorganisation due to the financial expertise and support they committed to the debtor such that allowing actions to proceed against the guarantors and co-debtor would likely lead to the cessation of the debtor's operations; (3) the balance of harm tilted in favour of the debtor because the creditor was fully secured; and (4) the public interest factor tipped in favour of granting the injunction to avoid litigation between the guarantors. As the debtor was likely to repay the creditor, the court stated that proliferating litigation between the guarantors, when the debtor may be able to pay, was against public interest.

Similarly, in *Re Steven P. Nelson*,[777] the court referenced section 105 to stay claims against the guarantor of a Chapter 11 debtor company. The guarantor was the president, the only shareholder and executive of the company. Considering his position, the court noted that the guarantor's services, expertise and knowledge were necessary to the reorganisation of the company. Therefore, permitting creditors' actions to proceed against the guarantor would

[773] Bankruptcy Code, s105(a).
[774] *In re River Family Farms, Inc*, 85 BR 816 (Bankr ND Iowa 1987).
[775] *In re Calpine Corp*, 365 BR 401 (SDNY 2007) at 409.
[776] 571 BR 430 (Bankr ND Iowa 2017).
[777] 140 BR 814 (Bankr MD Fla 1992).

drastically diminish his contribution to the company's reorganisation. Moreover, in *Re Lazarus Burman Associates*,[778] the court enjoined guaranty claims against the non-debtor principals of debtor partnerships because they were the sole individuals able to formulate, finance, negotiate and carry out the debtor's reorganisation plans.

Regardless of which component of the bankruptcy law the courts use as a basis to stay claims against non-debtors, staying such actions remains the exception rather than the rule, an exception available only in limited circumstances in which the benefit to the debtor's reorganisation clearly outbalances the detriment to the enjoined claimants.[779]

From a comparative perspective, the UK insolvency regime provides no authority to the courts to extend moratorium protection to cover claims against non-debtor parties. The administration moratorium does not impact creditors' actions against non-debtor parties such as guarantors. The position under Saudi bankruptcy law is rather different than those under these two jurisdictions. The moratorium in Saudi bankruptcy law expressly applies to actions against the guarantors of the debtor's debts. However, unlike the position under the US bankruptcy law, actions against non-debtor parties other than guarantors are not protected by moratorium under Saudi bankruptcy law. Also, in contrast to the US bankruptcy law, under which the actions against guarantors are stayed only in limited circumstances, the actions against guarantors of the debtor are always stayed by the moratorium under Saudi bankruptcy regime. The Saudi position in this issue is discussed in part 3 of this chapter.

6.2.2 Relief from the Automatic Stay

The effect of the automatic stay is not absolute. Section 362(d) enables the affected creditors to seek relief from the stay. This section provides two main grounds for granting the relief.[780] The first is set forth in subsection (d)(1), which provides that a 'party in interest' may apply to have the stay lifted 'for cause, including the lack of adequate protection of an interest in property…'.[781]

[778] 161 BR 891 (Bankr EDNY 1993).
[779] Tabb, *Law of Bankruptcy* (n 279) 265.
[780] See, generally, Daniel J Warren, 'Relief from the Automatic Stay: Section 362 (d)' (1986) 3 Bankr Dev J 199.
[781] Bankruptcy Code, s 362(d)(1).

As the Code provides no definition of the term 'cause' but merely lists the lack of adequate protection as an example where cause is constituted, it is understood that the lack of adequate protection is not the only cause that justifies relief from the stay.[782] By not defining what constitutes cause for granting relief, it seems that Congress purposely intended not to unnecessarily hinder the court's discretionary power in granting the relief when the circumstances of the case necessitate such granting.[783] This was affirmed in the case of *In re Robbins*,[784] where the court noted the following: 'According to section 362(d), the bankruptcy court may lift the stay "for cause." Because the Code provides no definition of what constitutes "cause," courts must determine when discretionary relief is appropriate on a case-by-case basis'.[785]

Nevertheless, to avoid unnecessary length, this thesis focuses only on the example of cause listed under section 362(d)(1) regarding the lack of adequate protection, in addition to the second basis for obtaining relief from the automatic stay set forth in subsection (d)(2). Based on section 362(d)(2), a secured creditor may obtain relief from the automatic stay with respect to an action against the property of an estate if '(A) the debtor does not have an equity in such property; and (B) such property is not necessary to an effective reorganization'.[786]

6.2.2.1 The Lack of Adequate Protection

The most common grounds for granting relief from a stay is the absence of adequate protection.[787] The notion of adequate protection finds its basis in the constitutional protection of property interests.[788] Moreover, Congress emphasised that the concept of adequate protection reflects the policy that '[s]ecured creditors should not be deprived of the benefit of their bargain'.[789] Adequate protection mandates that the value of the secured creditor's collateral position should not be permitted to decline during the term of the stay.[790] A secured

[782] John Francis Murphy, 'The Automatic Stay in Bankruptcy' (1985) 34 Clev. St. L. Rev. 567, 602.
[783] See *In re The Score Board Inc*, 238 BR 585 (DNJ 1999).
[784] 964 F 2d 342 (4th Cir 1992).
[785] ibid at 345; *In re Mac Donald*, 755 F 2d 715 (9th Cir 1985) at 717.
[786] Bankruptcy Code, s 362(d)(2).
[787] *In re Mid-Atlantic Handling Systems LLC*, 304 BR 111 (Bankr DNJ 2003); Epstein and Nickles (n 546) 20.
[788] *Wright v Union Central Life Ins Co*, 311 US 273 (1940); *Louisville Joint Stock Land Bank v Radford*, 295 US 555 (1935).
[789] HR Rep No 95-595, 95th Cong, 1st Sess, at 339 (1977); HR Rep No 95-595, 95th Cong, 2nd Sess, at 53 (1978).
[790] Lauris N Molbert, 'Adequate Protection for the Undersecured Creditor in a Chapter 11 Reorganization: Compensation for the Delay in Enforcing Foreclosure Rights' (1984) 60 NDL Rev. 515, 521; Douglas G Baird, *Elements of Bankruptcy* (6th edn, Foundation Press 2014) 204.

creditor that has an interest in the property of the estate is entitled to adequate protection to guard against reduction in the value of its collateral throughout the Chapter 11 case.[791] If the debtor is unable or unwilling to provide such protection, then this would be grounds for granting the secured creditor relief from the stay.[792]

Although the Code does not define 'adequate protection', section 361 suggests three nonexclusive methods for providing adequate protection. First, the debtor may provide periodic cash payments to the secured creditor equal to the value decrease in the secured creditor's interest in the collateral. Second, adequate protection may take the form of additional or replacement liens to compensate for the decrease in the original collateral's value. The third method is to provide the affected creditor some other kind of protection amounting to the 'indubitable equivalent' of the creditor's interest in the property. The term 'indubitable equivalence' comes from Judge Learned Hand's opinion in the case of *In re Murel Holding Corp,*[793] in which he stated that secured creditors must not be deprived of their collateral 'unless by a substitute of the most indubitable equivalence'.[794] An example of this third method is providing the secured creditor with a guarantee by a third party to compensate any decrease in the creditor's interest in the collateral.[795]

Albeit not explicitly referenced in section 361, the presence of an 'equity cushion', in itself, has been held to constitute adequate protection.[796] An 'equity cushion' is the amount 'by which the value of the collateral exceeds the amount of the debt'.[797] In *In re Avila,*[798] a secured creditor's motion to obtain relief from a stay to complete a foreclosure sale of the debtor's property was rejected. The rejection was decided after the court learned that the creditor was adequately protected by an equity cushion of 40% and that the debtor would suffer a significant loss if the foreclosure were finalised, unlike the creditor, who would suffer no economic loss from a denial of the relief motion.

[791] See *United Savings Ass'n v Timbers of Inwood Forest Assocs, Ltd*, 484 US 365, 371 (1988).
[792] Baird (n 790) 204; John D. Ayer, Michael Bernstein and Jonathan Friedland (n 728) 2.
[793] 75 F 2d 941 (2d Cir 1935).
[794] ibid at 942.
[795] HR Rep No 95-595, 95th Congress, 1st Session, at 340 (1977).
[796] See, e.g. *In re Alyucan Interstate Corp*, 12 BR 803 (Bankr D Utah 1981).
[797] Tabb, *Law of Bankruptcy* (n 279) 300.
[798] 311 BR 81 (Bankr ND Cal 2004).

The question that may arise in relation to the equity cushion is whether adequate protection gives the right to an over-secured creditor to maintain its equity cushion during the course of the reorganisation case. It has been argued that the secured creditor is entitled to adequate protection of its equity cushion. The justification for this argument is that (1) adequate protection should provide the secured creditor with the 'benefit of their bargain', and (2) the equity cushion itself is an integral part of that 'bargain', i.e. the creditor bargained for the collateral's value to remain a safe percentage exceeding the amount of the debt during the period of reorganisation.[799]

In the early years following enactment of the Code, this argument enjoyed a degree of judicial acceptance. However, the argument was dismissed in *Re Alyucan,*[800] in which the court held that such an argument misinterpreted the purpose of adequate protection. The court stated that 'the interest in property entitled to protection is not measured by the amount of the debt but by the value of [the secured property]'.[801] Therefore, unless the value of the creditor's collateral position is threatened, there is no need for adequate protection.

Thus, while the existence of the equity cushion by itself constitutes adequate protection and, therefore, justifies denying relief from a stay, the failure to maintain such a cushion is not grounds for obtaining relief from the stay.

6.2.2.2 Property Not Necessary for an Effective Reorganisation

Section 362(d)(2) provides other grounds for obtaining relief from the stay in relation to acts against the property of the estate. Under this basis, relief will be granted if two factors are established: (A) the debtor does not have equity in the property, and (B) the property is not necessary for an effective reorganisation. The party seeking relief under these grounds bears the burden of establishing that the debtor has no equity in the property. Once this is established, the burden moves to the debtor to prove that the property is necessary to the effective reorganisation of the company.[802] Hence, establishing that the debtor company lacks equity in the property is essential but not sufficient for obtaining relief from the stay under section

[799] See Tabb, *Law of Bankruptcy* (n 279) 301; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 167.
[800] 12 BR 803 (Bankr D Utah 1981).
[801] ibid at 808.
[802] *United Savings Ass'n v Timbers of Inwood Forest Assocs, Ltd*, 484 US 365, 372 (1988).

362(d)(2), unless the opposing debtor fails to prove that the property is necessary for an effective reorganisation.

In its attempt to convince the court to deny relief under section 362(d)(2)(B), it is not sufficient for the debtor company to establish that the property is necessary for reorganisation. The company must also demonstrate that its reorganisation effort is feasible. The necessary element is self-evident and easily established since, in almost every reorganisation case, the company needs to maintain and utilise its property if it is to have any possibility of reorganising. It is the issue of feasibility of reorganisation that is usually subject to heated disputes.[803]

A leading case illustrating the application of section 362(d)(2)(B) is the Supreme Court's decision in *Inwood.*[804] The court ruled that to successfully rely on section 362(d)(2)(B) to challenge the granting of relief, the debtor company must establish that 'a reasonable possibility of a successful reorganization within a reasonable time' existed.[805] What section 362(d)(2)(B) requires, the court stated, 'is not merely a showing that if there is conceivably to be an effective reorganization, this property will be needed for it; but that the property is essential for an effective reorganization that is in prospect'.[806] Therefore, in determining the feasibility of successful reorganisation, the court will insist on actual evidence of the reorganisation's likelihood, as opposed to merely the company's unsupported speculations and hopes for a successful reorganisation.[807] A secured creditor may prevail on the feasibility issue if it can establish that, legally, the company's reorganisation plan will not be confirmed because it will not receive the required approvals.[808]

[803] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 168.
[804] 484 US 365, 372 (1988). See Richard B Webber, 'Adequate Protection and the Undersecured Creditor: United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.' (1988) 41 Okla L Rev 637; Marc Forsythe, 'United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.: Undercollateralized Creditors Cry Timber to the Right to Compensation for Interest on the Value of Collateral' (1989) 20 Pac LJ 1309.
[805] *United Savings Ass'n v Timbers of Inwood Forest Assocs, Ltd*, 484 US 365, 376 (1988).
[806] ibid at 375–76.
[807] See *In re Pegasus Agency*, 101 F 3d 882 (2d Cir 1996); *In re Kent Terminal Corp*., 166 BR 555 (Bankr SDNY 1994); *In re Saypol*, 31 BR 796 (Bankr SDNY 1983).
[808] Tabb, *Law of Bankruptcy* (n 279) 311.

6.3 Moratorium Under Saudi Restructuring Procedures

A moratorium is available under both Saudi BL 2018 restructuring procedures: Financial Restructuring (FR) and Preventative Settlement (PS). The BL 2018 defines the moratorium as a 'suspension of the right to commence or continue any action or proceeding against the debtor, its assets or against the guarantor of the debtor's debts during a specific period under the provisions of the law'.[809]

Although the FR moratorium and the PS moratorium have identical effects, they differ in two ways.[810] First, under the FR process, the moratorium goes into effect automatically when the application for the procedure is made, whereas under the PS procedure, the moratorium must be requested by the debtor at the time of filing for the procedure and then ordered by the court.[811] The second difference is related to the moratorium period. Once the PS procedure is opened, the court may, if requested by the debtor at the time of filing for the procedure, order a moratorium for a period not to exceed 90 days from the date of procedure opening and may extend such period by 30 days one or more times at the request of the debtor, provided the total duration of the moratorium does not exceed 180 days.[812] On the other hand, the initial period of the moratorium under the FR is 180 days, and the court may, at its own discretion or upon the request of the debtor or a trustee, extend the moratorium no more than 180 days.[813] The moratorium under both procedures terminates when the moratorium period elapses, or before that if the commencement application is rejected, or when the court confirms the reorganisation proposal or terminates the procedure prior to its completion.[814]

The following sections examine the scope of the moratorium under the Saudi restructuring regime and the circumstances for which relief from a moratorium is granted. This examination is carried out in light of the UK and the US stands on those two issues, which were illustrated in the previous parts of this chapter.

[809] BL 2018, art 1.
[810] See Musab Idris, *Bankruptcy Procedures According to the Saudi Bankruptcy Law and Its Implementing Regulations* (1st edn, Law and Economics 2020) 34–50; Al-Ahmad (n 315) 106–134; Adli Hammad (n 648) 313–314.
[811] BL 2018, arts 17, 46(1).
[812] BL 2018, art 18(1).
[813] BL 2018, art 46(1).
[814] BL 2018, arts 18(2), 46(2).

6.3.1 Scope of Moratorium Under Saudi BL 2018

In comparison to the situation under the old regime, the scope of the moratorium under the new restructuring law is expanded to include a larger segment of the actions against the debtor company or its assets. However, in contrast to the UK and the US laws, the scope of a moratorium is addressed only briefly in Saudi BL 2018. As the following analysis shows, this brevity has resulted in a degree of uncertainty regarding the impact of the moratorium on certain types of actions.

Article 20(1) of BL 2018 sets out three paragraphs identifying the types of actions that cannot be commenced or continued when a moratorium is in force, which are as follows: (a) any action or proceeding against the debtor or its assets, including filing an application for the commencement of any bankruptcy procedures; (b) any enforcement procedure over any bankruptcy assets[815] provided as security interest, without consent of the court; and (c) any action against the personal guarantor or the in-kind guarantor of the debtor's debt, without the consent of the court.

6.3.1.1 Paragraph (a): Action or Proceeding Against the Debtor or Its Assets

This provision can be considered the most important feature of a moratorium, as it halts all enforcement and collection actions against the company or its assets, including the enforcement of pre-petition judgments obtained against the company or its assets, unless the court has approved such actions. The temporary restraint of these actions is necessary to protect against the dissipation of the company's assets, which would otherwise frustrate any attempt at reorganisation.[816]

In addition to suspending collection and enforcement actions, paragraph (a) stays the commencement and continuation of any proceeding against the company or its assets. The general term 'proceeding' is not defined, which produces a degree of uncertainty about exactly what proceedings are stayed by a moratorium under paragraph (a). For example, does the moratorium apply only to civil proceedings, or does it cover criminal proceedings as well? Is the impact of a moratorium limited to judicial proceedings or does it also halt quasi-judicial

[815] Article 1 defines 'bankruptcy assets' as '[t]he debtor's assets on the date of initiation of any of the bankruptcy procedures provided for in this Law or during the validity of any of the bankruptcy procedures'.
[816] Yasser Al-Aqili, *Explanation of the Provisions of Bankruptcy Law* (1st edn, Dar Al Rawda 2019) 113–117.

proceedings, such as arbitration proceedings and applications to industrial tribunals? The general and brief language of the statute provides no clear answers to these questions, so the courts are left with the heavy task of determining the boundaries of the scope of the moratorium.

Interestingly, the uncertainty about exactly what proceedings are stayed by a moratorium under Saudi bankruptcy law mirrors, to a large extent, the judicial uncertainty that existed in the early years following the 1986 introduction of the UK administration procedure. As discussed in Part 1, judicial ambiguity existed over exactly what proceedings were covered by the moratorium under Section 11(3)(d) of IA 1986 (now paragraph 43(6) of Schedule B1).[817] However, while the UK courts have largely resolved that uncertainty by providing a clear interpretation of what constitutes a proceeding according to Schedule B1, paragraph 43, of IA 1986 and, therefore, what is halted by the moratorium,[818] the similar issue under Saudi bankruptcy law has not yet been directly addressed by Saudi courts.

It may be argued that the moratorium under Saudi BL 2018 only covers civil proceedings in which the claimant takes the role of creditor, which the law defines as a 'person to whom a debt is proven to be owed by a debtor'.[819] However, from the author's point of view, this interpretation is incorrect because the term 'proceeding' is stated generally in paragraph (a) without any accompanying specification or limitation. If the legislator intended to exclude certain types of proceedings from the scope of the moratorium, the statute would have provided a specific provision to that effect. The generality of the term and the absence of any limitation or specification indicates that the term 'proceeding' is intended to be read broadly to cover all kinds of proceedings against the debtor or its assets. This means that when the moratorium is in force, no proceedings of any kind, including criminal, legal or quasi-legal proceedings, are permitted to proceed without the court's approval. This wide construction was partly supported by the Commercial Court in Jeddah in a case in 2019.[820] The court stated that the impact of the moratorium is not limited to judicial proceedings but extends to the proceedings before the quasi-judicial bodies. Although this wide interpretation is implied by the language of paragraph

[817] See Goode (n 130) 435–437; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 159–160.
[818] See, e.g., *Rhondda Waste Disposal Ltd* [2001] Ch 57; *Bristol Airport Plc v Powdrill* [1990] Ch 744; *Carr v British International Helicopters Ltd* [1994] ICR 18; and *Re Divine Solutions (UK) Ltd* [2004] CLY 2116.
[819] BL 2018, art 1.
[820] The decision of the Fourth Circuit in case No 433 (September 2019).

(a), the author suggests that paragraph (a) be amended to establish a clearer and more precise explanation to avoid any uncertainty and conflict in judicial interpretations.

In light of the foregoing, it seems that the moratorium under Saudi law is similar to the moratorium under the UK law in impacting all kinds of legal or quasi-legal proceedings against the debtor company or its assets,[821] in contrast to the position under the US regime, in which certain types of proceedings are excluded from the scope of the automatic stay.[822] The two significant exceptions of these, as illustrated in part 2, are the commencement or continuation of criminal proceedings and the commencement or continuation of an action or proceeding by a governmental unit to enforce police or regulatory powers.[823] According to Professor McCormack, these exemptions resulted from lobbying by special interest groups on US lawmakers.[824] He argued that these 'exemptions are difficult to justify or rationalise in the abstract and seem perhaps to be the product of political expediency'.[825] On the other hand, those who support the exclusion of these proceedings from the scope of the automatic stay argue that the exceptions are necessitated by the nature of these proceedings.[826] It is argued that the purpose of such proceedings is to protect the public interests, and to achieve their purpose, they should not be hindered by the automatic stay, the purpose of which is to serve a narrower segment of interests.[827]

However, the protection of public interests can be achieved without having to exclude such proceedings from the scope of the moratorium. Although the UK and Saudi moratorium apply to all proceedings without any listed exceptions, the laws provide grounds for granting relief from the moratorium if failure to do so would result in loss that exceeds the loss caused to the debtor and other creditors if the relief is granted. This standard will usually be satisfied in relation to proceedings that involve issues wider than the narrow commercial interests of the debtors and creditors, such as criminal proceedings and proceedings by a governmental body aiming to enforce regulatory powers.[828]

[821] *Rhondda Waste Disposal Ltd* [2001] Ch 57.
[822] See Tabb, *Law of Bankruptcy* (n 279) 266.
[823] Bankruptcy Code, s 362(b), sub-ss (1) and (4).
[824] McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 160.
[825] ibid.
[826] Heidt (n 760) 75. (stating that 'the filing of the bankruptcy petition is not a license to violate criminal laws or governmental regulations.')
[827] Tabb and Brubaker (n 732) 208.
[828] See Trower and others (n 708) 54.

Although the outcomes under all three jurisdictions will usually be similar in allowing criminal proceedings and proceedings brought by a governmental body to proceed notwithstanding the moratorium, the UK approach, which the Saudi law follows on this issue, seems more proper than the US method. Allowing such proceedings to continue under the former approach is the exception rather than the rule, which means that the burden is on the public prosecutor or the governmental unit to convince the court to abandon the default position and grant the relief, allowing the commencement or the continuation of such proceedings by establishing that granting the relief is necessary to protect public interests. Public prosecutors and the governmental units are usually powerful parties who are financially able to assume the burden of proof needed to convince the court to grant relief from the moratorium.

This works in the reverse under the US bankruptcy law, which excludes those types of proceedings from the ambit of the automatic stay. As demonstrated in Part 2, under this regime, the burden is on the debtor to convince the court to stay such proceedings when there is a justification for this stay.[829] However, requiring the debtor to carry this burden of proof may increase the financial encumbrance on the debtor who is already experiencing financial hardship. Therefore, the approach adopted under the UK and Saudi laws in which the moratorium applies to all kinds of proceedings with no exceptions seems more appropriate than the US approach.

6.3.1.2 Paragraph (b): Enforcement of Security

As discussed in Chapter 2, one of the main defects of the former Saudi restructuring law was the narrow scope of its moratorium.[830] The moratorium under the previous law did not cover actions brought by secured creditors. Accordingly, secured creditors could enforce their security interests against the company during the reorganisation process. This defect was amended by the introduction of BL 2018, under which the moratorium bars secured creditors from enforcing their security interests over any of the debtor company's assets provided as security interest except with the consent of the court.[831] This reform places a secured creditor in the Saudi bankruptcy regime on the same footing with his or her UK and US counterparts.

[829] Tabb, 'Competing Policies in Bankruptcy: The Governmental Exception to the Automatic Stay' (n 760) 188. *Marshall v. Tauscher (In re Tauscher)*, 7 Bankr 918, 920 (Bankr ED Wis 1981).
[830] Adam Al-Sarraf, 'Bankruptcy Reform in the Middle East and North Africa: Analyzing the New Bankruptcy Laws in the UAE, Saudi Arabia, Morocco, Egypt, and Bahrain' (2020) 29 Int Insolv Rev 159, 165.
[831] BL 2018, art 20(1)(b).

While security holders would retain their secured status in the bankruptcy case, they cannot enforce such security without the court's permission. Preventing the enforcement of security interests during a moratorium is critical to facilitating the reorganisation of the debtor company.[832] For example, the property subject to security interests might be necessary for the company to continue its business operations throughout the reorganisation process.[833] Allowing the enforcement of security interests over such property after the commencement of bankruptcy procedures may disrupt the business and, therefore, undermine the prospective restructuring.[834]

6.3.1.3 Paragraph (c): Action Against the Guarantor of the Debtor's Debts

The moratorium protection provided under BL 2018 is not limited to the debtor company but also covers actions brought against the guarantor of the company's debts.[835] Extending the protection of the moratorium to guarantors represents another notable feature of the new restructuring regime compared to the former law, which explicitly excluded claims brought against the debtor's guarantors from the scope of the moratorium.[836]

Regarding this issue, Saudi law is different from the UK regime, under which the moratorium has no effect on the actions and proceedings brought against the guarantors of the debtor company. It is also different from the US law, under which the automatic stay applies to actions against the guarantors only in limited circumstances.[837] Thus, the Saudi and the UK laws represent opposite sides pertaining to this issue, while the US law adopts a middle-of-the-road approach between these two sides. Considering this, one may ask whether the Saudi position on this issue is appropriate, and if not, then what should the alternative approach be?

First, extending the protection of a moratorium to the debtor company's guarantors may be critical to enhancing the prospect of reorganisation in many regards.[838] For example, in many cases, the guarantors are the debtor's corporate insiders, such as shareholders or directors. The expertise of these insiders may be heavily relied upon to effectively formulate and implement

[832] Jackson (n 278) 181.
[833] Tabb, *Law of Bankruptcy* (n 279) 252.
[834] ibid.
[835] BL 2018, art 20(1)(c).
[836] BPS, art 11.
[837] *In re Bailey Ridge Partners*, 571 BR 430 (Bankr ND Iowa 2017).
[838] See Barry L Zaretsky, 'Co-Debtor Stays in Chapter 11 Bankruptcy' (1987) 73 Cornell L Rev 213.

the company's reorganisation plan.[839] Such insiders may also be potential sources of funding for the reorganisation.[840] The contributions that the guarantors can provide for the reorganisation process may be hindered if the moratorium does not stay the actions of creditors against the guarantors for the company's debts. Therefore, an effective restructuring may necessitate the protection of the guarantors.

Leveneur highlighted another advantage of extending the moratorium protection to guarantors who are the directors of the debtor company.[841] He argued that such directors may delay the commencement of the reorganisation procedure as long as possible if they know that, because creditors cannot sue the principal debtor – the company – for payment of due debts during the restructuring procedure thanks to the statutory moratorium, the creditors will be induced to have direct recourse to the guarantors, i.e. the directors themselves. Therefore, the extension of the moratorium protection in this situation may encourage directors to initiate the rehabilitation process in a timely manner.

Notwithstanding the advantages of extending the moratorium to actions against the guarantors, such an extension undermines the very purpose of the guarantee agreement.[842] A primary object of a guarantee is to warrant repayment to the creditor upon the principal debtor's default. The guarantee assures 'a creditor that in the event the debtor defaults, the creditor will have someone to look to for reimbursement'.[843] This essential role of the guarantee agreement becomes more important when the principal debtor files for the reorganisation procedure, which provides a statutory moratorium prohibiting the recipient of the guarantee from taking any action against the principal debtor.[844] The automatic application of the moratorium to actions against the guarantors of the debtor contrasts with this traditional purpose of the guarantee agreement and undermines its value as a form of security.[845]

[839] ibid; *In re Bailey Ridge Partners*, 571 BR 430 (Bankr ND Iowa 2017); *Re Steven P. Nelson*, 140 BR 814 (Bankr MD Fla 1992).
[840] *Re Lazarus Burman Associates*, 161 BR 891 (Bankr EDNY 1993).
[841] Laurent Leveneur, 'Guarantees and Collective Procedures' in Wolf-Georg Ringe, Louise Gullifer and Philippe Théry (eds), *Current Issues in European Financial and Insolvency Law: Perspectives from France and the UK* (Hart Publishing 2009) 142.
[842] John J Lawson, 'Creditors Beware-A Guaranty May Not Be Such a Guarantee' (1989) 94 Dick L Rev 157, 175.
[843] *In re F.T.L., Inc.*, 152 BR 61 (Bankr ED Va 1993) at 63.
[844] Lawson (n 842) 157.
[845] ibid 175.

To preserve the benefits of extending the moratorium protection to actions against guarantors and avoid the undesired consequences of such an extension, the author suggests that the moratorium under Saudi BL 2018 should not apply automatically to actions against the guarantors of the debtor. Saudi law should follow the US approach, in which such actions are stayed only in limited circumstances.

As demonstrated in Part 2, Section 105(a) of the US bankruptcy code has been regularly relied upon to enjoin suits against the guarantors of Chapter 11 debtors.[846] This catch-all provision equips the courts with broad power to 'issue any order, process or judgment that is necessary or appropriate to carry out the provisions of this title'.[847] Relying on Section 105(a), the court will enjoin proceedings against guarantors of the debtor if the debtor can prove that (1) there is a likelihood of successful reorganisation; (2) there is imminent irreparable harm to the debtor's efforts of reorganisation if proceedings against the guarantor are not enjoined and (3) the balance of harm tilts in favour of the debtor.[848]

Interestingly, Saudi BL 2018 contains a catch-all provision similar to Section 105(a) of the US bankruptcy code. Article 6 of BL 2018 provides the following: 'The court shall issue judgements and decisions necessary for the application of the procedures stipulated in this Law, oversee the implementation thereof, decide disputes arising therefrom, and impose the penalties prescribed in this Law'. In principle, the courts can utilise Article 6 to enjoin actions brought against the guarantors of the debtor company when there is a solid justification for issuing such an injunction. As stated previously, this justification can be established only in limited circumstances when the debtor can prove that the enforcement of the guarantee agreement would harm the debtor's reorganisation efforts and cause significant losses to the debtor and other creditors, outweighing the potential losses caused to the recipient of the guarantee by enjoining its action against the debtor's guarantor.

In summary, the author recommends the moratorium provision under BL 2018 be amended so that it does not apply to the enforcement of guarantee agreements. Staying the enforcement of the guarantee should be permitted only in exceptional situations and based upon the court's discretion, exercising its broad authority under Article 6.

[846] *In re Bailey Ridge Partners*, 571 BR 430 (Bankr ND Iowa 2017); Orr (n 772) 259.
[847] Bankruptcy Code, s105(a).
[848] *In re Calpine Corp*, 365 BR 401 (SDNY 2007) at 409.

6.3.2 Relief from Moratorium

Similar to the UK and US laws, the Saudi bankruptcy law permits secured creditors to seek relief from the moratorium in order to be able to enforce their security interest. In common with the US regime, the only method to obtain relief under the Saudi law is by applying to the court. This is different from the UK law, under which relief from the moratorium can be granted by either the court or by the administrator.

BL 2018 sets out two grounds on which relief from the moratorium may be granted.[849] The first is Article 21(1)(a). Based on this provision, secured creditors may be granted relief from the moratorium to enforce their security interests if the court is satisfied that such enforcement would not harm the debtor's reorganisation efforts.[850] This is similar to the UK law approach established in *Re Atlantic Computer Systems Plc,*[851] in which Nicholls LJ stated that if granting the leave would not impede the purpose of the administration, then leave will usually be granted.[852] The US position with respect to this issue is somewhat similar to that of the other two regimes, albeit with some differences. As discussed in Part 2, based on Section 362(d)(2) of the US bankruptcy code, secured creditors can obtain relief from the automatic stay to enforce their security interests over the property of the estate if it is established that the debtor has no equity in the property and the property is not necessary for an effective reorganisation.[853]

The second grounds for granting relief from the moratorium to enforce security interests is provided in Article 21(1)(b), which applies to situations in which the enforcement of security interests is likely to harm the reorganisation process. According to this provision, such enforcement is allowed only if the court is satisfied that the rejection of such enforcement could cause serious loss to the secured creditor for which the debtor cannot compensate and where such loss surpasses losses caused to the debtor and the other creditors if the relief is granted.[854] Again, this mirrors the UK law approach in determining whether to grant leave from the moratorium in cases in which there is a likelihood that granting the leave would impede the purpose of the administration. In this case, the UK courts would engage in a balancing exercise,

[849] BL 2018, art 21(1).
[850] BL 2018, art 21(1)(a).
[851] [1992] Ch 505.
[852] ibid at 542.
[853] See Warren, 'Relief from the Automatic Stay: Section 362(d)' (n 780) 209ff.
[854] BL 2018, art 21(1)(b).

weighing the legitimate interests of the applicant against those of the debtor and other creditors.[855]

Secured creditors under both of these regimes must first demonstrate that without obtaining the relief, they would suffer a loss of some kind.[856] Then, the courts would balance between the proprietary rights of the applicant and the socially desirable objectives of the reorganisation procedure, and the relief to exercise these rights will usually be granted except in situations in which granting such relief would cause a substantially greater loss to the debtor and other creditors.[857] The US position with regard to this issue is different. As discussed in Part 2, the absence of adequate protection is the most common grounds for granting relief from a stay under the US bankruptcy law.[858] The notion of adequate protection mandates that the value of the secured creditor's collateral position not be permitted to decline during the term of the stay.[859] If the debtor is unable to provide such protection, then this would be grounds for granting the secured creditor relief from the stay.[860] The failure to provide adequate protection constitutes sufficient cause for relief from the stay, even if granting such relief would cause a substantially greater loss to the debtor and other creditors. The US courts do not carry on a balancing exercise in this scenario, as opposed to the case under the Saudi and UK laws.

6.3.2.1 The Absence of Guidelines

Although Saudi law has adopted a balance of interests approach similar to that applied in the UK regime in deciding whether to grant relief from a moratorium, unlike the latter, the former provides no guidelines on how this balance of interests should be exercised. BL 2018 merely directs the courts to balance the losses caused to the applicant by the moratorium against the losses that would be caused to the debtor and other creditors if the relief is granted in deciding whether to grant or deny relief accordingly[861] without providing guidelines on what factors the courts should consider when assessing these respective losses.

[855] Payne, 'The Role of the Court in Debt Restructuring' (n 721) 143; Milman (n 721) 99.
[856] *Re David Meek Access Ltd* [1993] BCC 175; Suliman (n 340) 329.
[857] *Re Atlantic Computer Systems Plc* [1992] Ch 505 at 542; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 174; Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 317.
[858] *In re Mid-Atlantic Handling Systems LLC*, 304 BR 111 (Bankr DNJ 2003); Epstein and Nickles (n 546) 20.
[859] Molbert (n 790) 521; Baird (n 790) 204.
[860] Baird (n 790) 204; John D. Ayer, Michael Bernstein and Jonathan Friedland (n 728) 2.
[861] BL 2018, art 21(1)(b).

One might argue that such guidelines should be provided by the courts, as has been the case under the UK law. However, unlike the UK's legal system, the Saudi legal system is based on civil law.[862] While the common law system is based on the concept of judicial precedent, in which courts play an active role in shaping the law, the civil law system relies on legislation as the primary source of law.[863] Moreover, the doctrine of *stare decisis* is not recognised in civil law systems as it is in common law.[864] This means that even if Saudi courts were to develop guidelines on the factors that should be taken into consideration when the balance of interests is exercised, unless endorsed by the statute, such guidelines will have no binding authority for the resolution of later cases. Therefore, the author recommends that BL 2018 or its implementing regulations establish a number of matters that must be considered by the courts when exercising the balance of interests required before deciding on granting or denying relief from the moratorium.

In setting out such guidelines, Saudi law may benefit from the UK experience and provide that, in carrying out the balance of interests exercise required before deciding whether to grant or deny relief from the moratorium, the courts should consider the following matters: the financial position of the debtor company; its ability to meet its loan obligations; the reorganisation plan; the period for which the moratorium has been in force and its remaining period; the effect on the debtor company and other creditors if the relief is granted; the effect on the applicant if relief is denied; and the prospect of reorganisation and its progress thus far.

Although the recommended guidelines are not intended to be and should not be regarded as exhaustive, the existence of such guidelines will warrant that certain essential factors are not overlooked by the courts when exercising this discretionary power. Moreover, the existence of such guidelines will safeguard against the conflicting decisions and the uncertainty that the absence of guidelines is likely to create.

[862] See Mohammed Al-Ghamdi and Paul J Neufeld, 'Saudi Arabia' in Damian Taylor (ed), *The Dispute Resolution Review* (10th edn, Tom Barnes 2018) 400.
[863] Caslav Pejovic, 'Civil Law and Common Law: Two Different Paths Leading to the Same Goal' (2001) 155 Poredbeno Pomorsko Pravo 7.
[864] The *stare decisis* doctrine mandates that 'earlier judicial decisions, usually of the higher courts, made in a similar case, should be followed in the subsequent cases, i.e. that precedents should be respected'. ibid 9.

6.4 Conclusion

This chapter highlights the importance of the moratorium as a fundamental component of the protection needed during a corporate reorganisation. The moratorium provides the distressed company with time to formulate and negotiate a restructuring plan without being pressed by multiple creditors' claims. It also protects the creditors by warranting an orderly and fair administration of the debtor's estate. The chapter then moves to examine the application of the moratorium under Saudi restructuring law in light of the UK and US regimes. The examination focuses on two main aspects of the moratorium: its scope and the circumstances under which relief from the moratorium may be granted.

The analysis demonstrates that, in common with the UK and US laws, the scope of the moratorium under the Saudi restructuring law is designed to be broad so that it covers various forms of actions against the debtor company and its property. One of the essential functions of a moratorium under Saudi bankruptcy law is the suspension of secured creditors' rights to enforce their security interests over any bankruptcy assets provided as security interest except with the consent of the court. Such a suspension represents a significant feature of the new Saudi reorganisation regime, distinguishing it from the former law under which the scope of the moratorium was very narrow and did not include the enforcement of security by secured creditors.

Moreover, the moratorium under the Saudi law is similar to the moratorium under the UK law in impacting all types of legal or quasi-legal proceedings against the debtor company and its assets, in contrast to the position under the US regime, in which certain types of proceedings, especially criminal proceedings and proceedings initiated by governmental units, are not affected by the automatic stay. The result of excluding these proceedings from the ambit of the automatic stay is that the burden of proof is placed on the debtor to convince the court to stay such proceedings, if justified. However, for the debtor who is already experiencing financial hardship, carrying out this burden of proof may increase its financial encumbrance.

The author argues that the UK approach, which the Saudi law follows on this issue, seems more proper than the US method. Under the UK approach, in which no proceedings are exempted from the scope of the moratorium, the burden is on the public prosecutor or the governmental unit to convince the court to grant relief, allowing the commencement or the continuation of

such proceedings by establishing that granting the relief is necessary to protect public interests. Unlike the distressed debtor, public prosecutors and governmental units are usually powerful parties that are financially capable of assuming the burden of proof needed to convince the court to grant relief from the moratorium. Therefore, the approach adopted under the UK and Saudi laws in which the moratorium applies to all kinds of proceedings with no exceptions seems more appropriate than the US approach.

Another issue this chapter discusses is the effect of a moratorium on claims brought against the guarantors of the debtor company's debts. These claims are automatically barred by the moratorium under Saudi law, in contrast to the UK law, under which the moratorium has no effect on the actions and proceedings brought against the guarantors of the debtor company.

Notwithstanding the benefits that the extension of the moratorium to actions against the guarantors may bring to the reorganisation process, such extensions contrast with the guarantee agreement's very purpose. A primary objective of a guarantee is to assure that upon the principal debtor's default, the guarantor will pay the creditor. The automatic application of the moratorium on claims against the debtor's guarantors interferes with this traditional purpose of the guarantee agreement and undermines its value as a form of security. Therefore, the author recommends the moratorium provision under BL 2018 be amended so that it does not apply automatically to actions against the guarantors of the debtor. Instead, Saudi law should follow the US approach, in which such actions are stayed only in limited circumstances when the debtor can establish that the enforcement of the guarantee agreement would harm the debtor's reorganisation efforts and cause significant losses to the debtor and other creditors, outweighing the potential losses caused to the recipient of the guarantee by enjoining its action against the debtor's guarantor.

Finally, the chapter discusses the issue of granting relief from the moratorium. It has been determined that, in common with the UK and US laws, under Saudi law, secured creditors are usually granted relief from the moratorium to enforce their security interests if it is established that such enforcement would not harm the debtor's effort toward reorganisation. When there is a likelihood that allowing the enforcement of security interests would impede the reorganisation process, Saudi law follows the UK approach in balancing the applicant's legitimate interests against those of the debtor and other creditors and deciding whether to grant or deny the relief accordingly. Such a balance of interests is not exercised in the US regime,

under which secured creditors are entitled to receive adequate protection to compensate for the decline of their collateral position during the term of the stay. The failure to provide adequate protection is sufficient grounds for relief from the stay.

Despite its adoption of a balance of interests approach similar to the approach applied in the UK regime, Saudi law provides no guidelines on what factors the courts should consider when carrying out the balance of interest exercise. Therefore, the author recommends that Saudi law may benefit from the UK experience in setting out such guidelines, which will ensure that certain essential factors are not overlooked by the courts when exercising this discretionary power and will safeguard against conflicting decisions and the uncertainty that the absence of guidelines is likely to create.

Having examined the application of the moratorium under Saudi restructuring law, the following chapter examines the restructuring plan, which is the central element of the reorganisation procedure.

Chapter 7: Restructuring Plan

The reorganisation plan is the central element of the reorganisation procedure.[865] Once approved, the terms of the plan serve as a blueprint of the debtor's obligations toward its creditors, outlining how much and when the creditors will be paid.[866] The provisions of the plan replace all claims that creditors had against the debtor prior to its approval.[867] This chapter addresses a number of important issues related to restructuring plans under Saudi bankruptcy law. Mainly, the chapter addresses the following issues: who may vote on the restructuring plan, how the plan is considered and approved, how dissenting creditors are treated, whether court confirmation is required, and the requirements for such confirmation. The chapter is divided into three parts. The first two parts demonstrate how these key issues are addressed in the UK and US laws. The third part then examines how Saudi law addresses these issues in light of the UK and the US perspectives provided in the first two parts of the chapter.

7.1 Restructuring Plan Processes Under the UK Restructuring Procedures

As illustrated early in this thesis, the UK administration is not a standalone reorganisation procedure, as opposed to US Chapter 11.[868] The UK administration is merely a gateway to a variety of routes the distressed company can take.[869] If corporate restructuring seems reasonably practicable, the administrator may advance a proposal for one of the following: a corporate voluntary arrangement (CVA) under Part 1 of IA 1986, a scheme of arrangement under Part 26 of Companies Act (CA) 2006 or a restructuring plan under the recently enacted Part 26A of CA 2006.[870] These three procedures differ considerably regarding the mechanism for voting on the reorganisation plan and its effect on the creditors, especially the secured creditors. The restructuring plan processes under the three procedures are considered in the following sections.

[865] UNCITRAL (n 376) 209.
[866] See HR Rep No 595, 95th Cong, 1st Sess, at 221 (1977); Tabb, *Law of Bankruptcy* (n 279) 1095; Epstein and Nickles (n 546) 112; M Jonathan Hayes, 'Formulating and Confirming a Chapter 11 Plan of Reorganization' (2000) 2 J. Legal Advoc. & Prac. 5.
[867] *In re Herron*, 60 B R 82, 84 (Bankr W D La 1986).
[868] See Goode (n 130) 394.
[869] ibid.
[870] IA 1986, Schedule B1, para 49(3).

7.1.1 Restructuring via Company Voluntary Arrangement (CVA)

One means by which a restructuring may be achieved is the CVA under Part 1 of IA 1986. Section 1(1) of IA 1986 states that a CVA proposal must provide for either a composition that satisfies the company's debts or a scheme of arrangement of its affairs;[871] as an alternative, the terms of the proposal may include a combination of the two.[872] The courts have taken a wide view on what constitutes a composition and a scheme of arrangement, which gives the company and its creditors a high degree of flexibility with which to negotiate and produce proposals that serve their interests.[873] A proposal is considered a composition if it offers to pay only a certain proportion of the company's debts, such as a payment of 50 pence for every 1 pound owed.[874] On the other hand, a proposal constitutes a scheme of arrangement if it offers to pay creditors in full but not immediately, instead establishing a schedule that denotes the dates and amounts for payments the company will make to its creditors.[875]

When the CVA is used for corporate restructuring, the CVA proposal may involve certain terms that are necessary to achieve this goal, such as the following: a moratorium (where no moratorium is already in place); injection of new funds to facilitate the continuation of the company's business; and the conversion of debt into equity, whereby creditors exchange their debts for shares in the company.[876] Moreover, in the case of a large company, the CVA proposal may involve a takeover of the company by a purchaser who is ready to inject capital or expertise.[877] The bottom line here is that the law is very flexible pertaining to the terms of the CVA proposal, as no restrictions are placed on what terms are included, provided that the proposal is 'reasonably capable of being described as a composition or a scheme of arrangement within the meaning of section 1 (1)'.[878]

[871] IA 1986, s 1(1).
[872] Keay and Walton (n 128) 140.
[873] See Parry (n 380) 153.
[874] *Commissioners of Inland Revenue v Adam & Partners Ltd* [2001] 1 BCLC 222.
[875] *March Estates Plc v Gunmark Ltd* [1996] 2 BCLC 1.
[876] See Goode (n 130) 505–506; Parry (n 380) 153–155.
[877] Keay and Walton (n 128) 140.
[878] *Commissioners of Inland Revenue v Adam & Partners Limited* [2000] BCC 513 at 524. In the case of *Inland Revenue Commissioners v Bland* [2003] EWHC 1068 (Ch), an individual voluntary arrangement (IVA) was set aside by the court on the grounds that the arrangement did not amount to either a composition or a scheme of arrangement.

7.1.1.1 Creditor Consideration and Approval of CVA Proposal

The CVA proposal needs to be approved by a majority constituting 75% or more[879] by value of the creditors who are present and vote on the resolution, either in person or by proxy.[880] For voting purposes, all creditors are treated as a single class; they are not divided into multiple classes, in contrast to the position taken under the scheme of arrangement. Once approved, the CVA becomes binding on the company and on all its unsecured creditors (1) who were entitled to vote at the creditors' meeting (regardless of whether they were represented at the meeting) and (2) who would have been entitled to do so had they had notice of the meeting.[881] Unlike the requirements of the scheme of arrangement, no sanction of the court is needed to make the CVA proposal binding. The proposal becomes binding immediately after being approved by the required majority. Also, unlike the scheme, the CVA is not binding upon secured creditors unless they agree to be bound by it.[882]

The general rule is that any creditor who receives notice of the creditors' meeting is entitled to vote on the CVA.[883] Although secured creditors are entitled to vote, their votes are not counted for the purpose of determining whether the required majority (75% in value) has been reached.[884] If a creditor's debt is partly secured, only the unsecured part of that creditor's claim will be counted. Excluding the votes of secured creditors when determining whether the required majority has approved the CVA seems justified since the CVA cannot affect these creditors' rights without their consent.

However, one controversial aspect of the CVA that has been the subject of recent criticism is that the votes of unsecured creditors whose rights are unaffected by the CVA are counted when determining whether the required majority has approved the CVA.[885] Indeed, the CVA has been commonly used to compromise the rights of certain creditors, mostly landlords, while other largely unaffected creditors approve the CVA. The British Property Federation (BPF) described this practice as abusive and unfair, arguing that the current rules guiding the CVA

[879] Before the amendments introduced by SI 2010/686, a CVA proposal had to be approved by a majority over 75% to be effective.
[880] Insolvency Rules 1986, r1 19(1).
[881] IA 1986, s 5(1).
[882] IA 1986, s 4(3).
[883] Insolvency Rules 1986, r1 17(1).
[884] Insolvency Rules 1986, r1 19(3).
[885] See 'The Abuse of CVAs Must End | EG News' <https://www.egi.co.uk/news/the-abuse-of-cvas-must-end/> accessed 10 April 2021.

process 'enable companies to unfairly engineer the weight attached to affected creditors' voting rights, often resulting in unaffected creditors approving CVAs with affected creditors being powerless'.[886] The BPF, therefore, urged the UK government to overhaul the CVA process by adopting a voting procedure that was fairer to those compromised by the CVA. To ensure this, the BPF recommended that the votes of unaffected creditors not be counted when determining whether the required majority has approved the CVA.[887]

Once the CVA is approved, implementation of the plan is usually supervised by the nominee, who becomes the supervisor upon approval of the CVA.[888] If the terms of the CVA are not satisfied – for example, if the business does not generate enough income to keep up with the monthly payments promised – the CVA may be terminated. Termination of the CVA will usually lead to the company being put into liquidation.

Generally, the absence of a formal court sanctioning stage and of separate class meetings of creditors in the CVA process have made it administratively simpler and less cumbersome than the scheme of arrangement.[889] The Cork Report of 1982,[890] which recommended the introduction of the CVA process, pointed out the difficulties associated with composing separate classes for voting on the scheme of arrangement and did not propose adopting a similar voting mechanism for the CVA process.[891]

On the other hand, the fact that the CVA proposal cannot affect the rights of secured creditors without their consent may be considered a significant disadvantage of the CVA, undermining its value as a restructuring tool.[892] This may also explain the results of the research conducted by Walters and Frisby, which revealed that the level of secured debt in companies using the CVA process is usually low or non-existent.[893] Nevertheless, the CVA may be the appropriate option for the restructuring of small companies due to its reduced complexity and cost

[886] BPF, 'Company Voluntary Arrangement (CVA) Briefing' (2020) para 28 <https://bpf.org.uk/media/3474/bpf-cva-briefing-2020.pdf> accessed 5 January 2021.
[887] ibid 17.1.
[888] IA 1986, s 7(2).
[889] See McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 70; Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 220.
[890] Kenneth Cork, *Insolvency Law and Practice: Report of the Review Committee* (HM Stationery Office 1982).
[891] ibid 400ff.
[892] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 222.
[893] Adrian Walters and Sandra Frisby, *Preliminary Report to the UK Insolvency Service into Outcomes in Company Voluntary Arrangements* (London : Insolvency Service 2011) 21.

compared to other procedures, like schemes; moreover, the fact that the CVA does not impact the rights of secured creditors may matter less because small companies are usually less dependent on secured debt as a source of finance.[894]

7.1.1.2 Challenge to the Creditors' Approval of the CVA

Although approval by the required majority immediately makes the CVA binding without the need for court involvement, section 6 of IA 1986 permits a dissenting creditor to apply to the court to challenge the CVA on the grounds of material irregularity or unfair prejudice. If the court upholds the challenge to the CVA on either of these two grounds, it may revoke or suspend approval of the CVA and/or direct the summoning of an additional meeting to consider the original or a revised proposal.[895]

Material irregularity refers mainly to breaches in the way the creditors' meeting is conducted.[896] Also, the failure to properly disclose material information related to the CVA in the proposal and the inclusion of false or misleading information of a material nature in the proposal both may constitute material irregularity.[897]

Unfair prejudice, on the other hand, may be less easy to determine. In principle, this concept aims to correct any disproportionate prejudice to a creditor or class of creditors compared with other creditors or classes of creditors,[898] such as differential treatment, an advantage given to a creditor or a restriction placed upon another creditor.[899] Generally, determining that a creditor has been prejudiced by the CVA is not difficult, as such prejudice is established if the CVA leaves a creditor in a less advantageous position than previously held.[900] What is often difficult is determining whether the prejudice is unfair.[901] Courts have frequently emphasised that the mere fact that the CVA proposal accords differential treatment to some creditors does not necessarily constitute unfair prejudice.[902] Indeed, some differential treatment may be essential to facilitate the continuation of the debtor's business. For example, the debtor may have to pay

[894] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 223.
[895] IA 1986, s 6(4).
[896] *Re Debtor (No 222 of 1990), Ex p Bank of Ireland* [1992] BCLC 137.
[897] *Re Gatnom Capital & Finance Ltd* [2010] EWHC 3353 (Ch).
[898] *Doorbar v Alltime Securities Ltd (No 2)* [1995] BCC 728 at 731–32.
[899] *Re Debtor (No 222 of 1990), Ex p Bank of Ireland* [1992] BCLC 137.
[900] *Prudential Assurance Co Ltd v PRG Powerhouse Ltd* [2007] BCC 500 at 72.
[901] ibid at 73.
[902] ibid at 88; *Re Debtor (No 101 of 1999) (No 1)* [2001] 1 BCLC 54; *Inland Revenue Commissioners v The Wimbledon Football Club Ltd & Ors* [2004] BCC 638 at 18.

some trade creditors in full in order to obtain supplies that are necessary for the continuation of the debtor's business.[903]

In determining the existence of unfair prejudice, the court will consider all circumstances of the plan, particularly, possible alternatives to the CVA, such as a scheme of arrangement or liquidation.[904] This approach was described in *Prudential Assurance Co Ltd v PRG Powerhouse Ltd*,[905] where Etherton J stated the following:

> In broad terms, the cases show that unfairness may be assessed by a comparative analysis from a number of different angles. They include what I would describe as vertical and horizontal comparisons. Vertical comparison is with the position on winding up…. Horizontal comparison is with other creditors or classes of creditors. In that context, another helpful guide, in the case of a CVA, is comparison with the position if, instead of a CVA, there had been a formal scheme of arrangement under [the Companies Act] on which the different classes of creditors would have been required to meet and vote separately.[906]

In *Powerhouse*, an electrical retailer (P), with financial support from its parent company, rented several high street stores. The parent company had given the landlords guarantees in relation to P's obligations under the leases. After encountering financial hardships, P wanted to close a number of its stores and enter into a CVA. Under the terms of the CVA, creditors with respect to closed premises would receive 28 pence for every pound owed, while other creditors' rights would remain unaffected. The CVA also contained provisions intended to release all claims against P regarding closed premises and to release the guarantees provided to the landlords by the parent company related to the closed premises. At the meeting of all of P's creditors, including creditors whose rights were unaffected by the CVA, the CVA was accepted by the requisite majority. The landlords challenged the CVA as unfairly prejudicial under section 6 of IA 1986 and asked the court to declare that the CVA was ineffective or invalid.

[903] See *Prudential Assurance Co Ltd v PRG Powerhouse Ltd* [2007] BCC 500 at 90; *Sea Assets Ltd v Perusahaan Perseroan (Persero) PT Perusahaan Penerbangan Garuda Indonesia* [2001] EWCA Civ 1696 at 45; *Discovery (Northampton) Ltd v Debenhams Retail Ltd* [2020] BCC 9 at 110; *Mourant & Co Trustees Ltd v Sixty UK Ltd (In Administration)* [2010] BCC 882 at 67.
[904] Parry (n 380) 197; Keay and Walton (n 128) 157; Finch and Milman (n 244) 436.
[905] [2007] BCC 500.
[906] ibid at 74.

Etherton J held that, in all circumstances, the CVA was unfairly prejudicial to the landlords. When comparing the position of the landlords under the CVA with their position under the liquidation scenario, Etherton J found that, by virtue of the guarantees on their hands, the guaranteed landlords were the class of creditors that would suffer least, if at all, upon liquidation of the debtor company. Nevertheless, these landlords were most prejudiced by the CVA, which compromised their claims against the debtor and its guarantor (the parent company). In other words, by stripping away the guarantees provided by the parent company, the CVA sought to leave the landlords in a significantly worse position than they would have been if the company were liquidated. This was held by Etherton J as 'an illogical and seemingly unfair result'.[907]

Furthermore, Etherton J held that such an unfair result would not be achieved under the scheme of arrangement, where creditors with guarantees would be in a class of their own and would be able to veto the scheme. Moreover, unaffected creditors would not be entitled to vote on the scheme of arrangement, as only creditors whose rights are affected by the scheme are able to vote. The reason why a different outcome can be achieved with the CVA is that, for purposes of voting on the CVA, all creditors are treated as one class, and this class includes every creditor that is entitled to be notified of a meeting to approve a CVA, including unaffected creditors. Therefore, 'the votes of those unsecured creditors who stood to lose nothing from the CVA, and everything to gain from it, inevitably swamped those of the guaranteed landlords who were significantly disadvantaged by it'.[908]

7.1.2 Restructuring via Scheme of Arrangement

Another option through which restructuring can be achieved is the scheme of arrangement under Part 26 of CA 2006. This process enables a company experiencing financial difficulties to enter into a compromise or arrangement with its creditors that, if approved by a required majority, is binding on all affected creditors.[909] The content of the scheme is not prescribed by

[907] ibid at 108.
[908] ibid.
[909] See, generally, Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383); Sarah Paterson, 'Reflections on English Law Schemes of Arrangement in Distress and Proposals for Reform' (2018) 15 European company and financial law review 472.

legislation, which provides a distressed company with a high degree of flexibility with which to formulate a proper restructuring plan, depending on its circumstances.[910]

The scheme procedure involves three main steps:[911] (1) proposing the scheme and applying to the court to order creditors' or members' meetings to be summoned, (2) holding meetings of creditors or members to vote on the scheme proposal and (3) seeking court sanction of the scheme that has obtained the approval of the appropriate majority of creditors or members.

After the application is made, the court will hold a hearing to decide whether a creditors' meeting should be summoned. The focus of the court at this stage is not on the merits or the fairness of the scheme[912] but on whether the creditors or members should be divided into separate classes for voting purposes. Moreover, at this stage, the court has wide discretion in ordering the terms on which creditors' meetings are conducted.[913]

7.1.2.1 Classification of Creditors

The issue of the appropriate composition of a class for the purpose of a scheme of arrangement has garnered much attention. Specifically, determining what constitutes a class has often been difficult,[914] and the difficulty was exacerbated by the former judicial practice of deferring classification to the sanctioning stage.[915] Under those circumstances, if the classes were incorrectly identified, the only option for the court was to refuse to sanction the scheme, even when no one objected. That practice was criticised by the Company Law Review (CLR)[916] and then by Chadwick LJ in *Re Hawk Insurance Co Ltd*[917] on the basis that such a practice involved a significant amount of wasted expense and time. Following these criticisms, in 2002 a Practice Statement was issued indicating that in order to save costs and court time, the composition of

[910] The only limit on the content of the scheme is that the proposed scheme must be capable of being described as a compromise or arrangement. Nonetheless, 'compromise' and 'arrangement' in the context of a scheme of arrangement have been interpreted broadly by the courts, and most restructurings will fall within the ambit of these two terms; See Parry (n 380) 234–235.
[911] *Re Hawk Insurance Co Ltd* [2002] BCC 300 at 12.
[912] *Re Telewest Communications Plc (No 1)* [2004] BCC 342.
[913] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 36–38.
[914] See, e.g. *Re Osiris Insurance Ltd* [1999] 1 BCLC 182; *Re Anglo American Insurance Co Ltd* [2001] 1 BCLC 755.
[915] Goode (n 130) 488.
[916] CLR (n 469) 207.
[917] [2002] BCC 300 at 19.

classes of creditors and the summoning of meetings must be identified and resolved at the stage of the first court hearing.[918]

The legislation does not specify what test should be employed to determine whether creditors, for the purpose of voting on the scheme, should meet as a whole or as separate classes. Instead, this test has been developed by case law. The test, which was first set out by Bowen LJ in *Sovereign Life Assurance Co v Dodd* [919] and then refined by Chadwick LJ in *Re Hawk Insurance Co Ltd,*[920] mandates that when the creditors affected by a proposed scheme have different rights in a way that they cannot consult together with a view to a common interest, they must be divided into different classes, and separate meetings should be convened for each class. Conversely, creditors with sufficiently similar rights to the rights of other creditors so that they can properly consult together should not be placed in separate classes, as such separation may give power of veto to a minority group.[921] Similarity and dissimilarity in this context are determined by reference to the creditors' legal rights against the company, not by reference to interests not derived from these rights.[922]

At least two essential points can be highlighted regarding the classification of creditors under the scheme of arrangement. Firstly, since they have similar legal rights, it seems that all unsecured creditors must be placed in one single class for the purpose of voting on a scheme.[923] Although the issue has not obtained judicial attention in the UK, separate classification of unsecured creditors for a 'business reason', for example, does not seem to be permitted under the UK scheme of arrangement, as opposed to the position under US Chapter 11, which is discussed later in this chapter. Secondly, simply identifying a dissimilarity in the creditors' rights does not constitute sufficient justification for placing them in different classes. Rather, the dissimilarity must be to the point that it is impossible for them to sensibly consult together

[918] *Practice Statement (Companies: Schemes of Arrangement)* [2002] 1 WLR 1345.
[919] [1892] 2 QB 573. In that case, the Court of Appeal held that for a scheme affecting an insurance company's policyholders, the policyholders whose policies were matured should be in a different class from the holders of unmatured policies. Bowen LJ stated that the term 'class' 'must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest'; ibid at 583.
[920] [2002] BCC 300.
[921] *Re Hawk Insurance Co Ltd* [2002] BCC 300, per Chadwick LJ at 33.
[922] *Re BTR Plc* [1999] 2 BCLC 675.
[923] *Re Hawk Insurance Co Ltd* [2002] BCC 300.

with a view to a common interest.[924] In other words, when it is possible for creditors with dissimilar rights to properly consult together, they must be put in the same class.

7.1.2.2 Approval and Sanction of the Scheme

The proposed scheme must be approved by the majority in number representing three fourths in value of the creditors or class of creditors present and voting either in person or by proxy at the meeting.[925] When the scheme involves several classes, all classes must approve the scheme. Unlike the case under US Chapter 11, cross-class cramdown is not possible under the UK scheme of arrangement. While dissenting creditors within a class can be crammed down, it is not possible to cramdown a whole dissenting class. Thus, the existence of one dissenting class will prevent the scheme from being sanctioned by the court.

Regarding the voting thresholds of the scheme, unlike the majority in value requirement, the 'majority in number', or headcount test, has proved controversial.[926] The test was criticised in 2001 by the Company Law Review (CLR), which described the test as 'irrelevant and burdensome' and proposed its abolition.[927] However, such a proposal has not been adopted by the government, and the majority in number requirement has been retained under Part 26 of CA 2006. Arguments for and against the majority in number requirement are discussed in part 3 of this chapter.

When the scheme is approved by the required majority, then an application must be made to the court for sanction of the scheme.[928] Once the court has sanctioned the scheme, it becomes binding on the company and all creditors affected by the scheme[929] (including unknown creditors who may have claims in the future arising out of existing facts and those who did not receive notice of the meeting to vote on the scheme).[930]

[924] *Re Stronghold Insurance Company Limited* [2018] EWHC 2909 (Ch).
[925] CA 2006, s 899(1).
[926] See Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 61–68; Finch and Milman (n 244) 416–417.
[927] CLR, *Modern Company Law for a Competitive Economy: Final Report* (2001) para 13.10; CLR (n 469) 207.
[928] CA 2006, s 899(1).
[929] CA 2006, s 899(3).
[930] *Re T&N Ltd* [2007] Bus L R 1411.

The court's role at the sanctioning stage is not just to rubber stamp the creditors' approval of the scheme.[931] Rather, the court will closely examine the substance of the scheme and consider three critical issues when determining whether to sanction it.[932] First, the court must be convinced that the statutory provisions have been followed. Second, the court must ascertain whether those who attended the meeting fairly represented the class/classes of creditors. Third, the court must be satisfied that the scheme's terms are fair.

A scheme is regarded as fair if the court is satisfied that 'an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve' it.[933] Nevertheless, the courts have emphasised that the proposed scheme does not need to be the only fair scheme or, from the court's perspective, the best scheme.[934] It is recognised that creditors are likely to have reasonable differences in their views on these issues.[935] Therefore, as pointed out by Lewison J in *Re British Aviation Insurance Co Ltd*,[936] 'the test is not whether the opposing creditors have reasonable objections to the scheme. A creditor may be equally reasonable in voting for or against the scheme. In such a case...creditor democracy should prevail'.[937]

Although courts are not bound to sanction schemes that have been approved by the correct majority of creditors,[938] courts very rarely refuse to sanction a scheme that has obtained such approval, when the classes were properly formed and no indication that the majority did not represent the class/classes of creditors is found.[939]

7.1.3 Restructuring via New Restructuring Plan Procedure (Part 26A Scheme)

Even though the scheme of arrangement under Part 26 and the latest Part 26A scheme are highly similar in many ways, the two do differ with respect to two issues related to restructuring

[931] See *Re BTR Plc* [1999] 2 BCLC 675; *Re TDG Plc* [2009] 1 BCLC 445.
[932] See *Re Anglo-Continental Supply Company Limited* [1922] 2 Ch 723 at 736; *Re Anglo American Insurance Co Ltd* [2001] 1 BCLC 755 at 762.
[933] *Re National Bank Ltd* [1966] 1 WLR 819 at 829.
[934] *Re Telewest Communications plc (No 2)* [2005] BCC 36 at 41.
[935] ibid.
[936] [2006] BCC 14.
[937] ibid at 33.
[938] *Re BTR Plc* [2000] 1 BCLC 740.
[939] See *Re British Aviation Insurance Co Ltd* [2006] BCC 14; *Re National Bank Ltd* [1966] 1 WLR 819.

plans. The first difference between the two procedures is related to voting thresholds. Under the new Part 26A scheme, the plan must be approved by at least 75% in value of the creditors within each class.[940] The additional majority in number requirement in the scheme of arrangement is not required under the Part 26A scheme.

The second and most important feature that differentiates the new Part 26A scheme from the traditional scheme of arrangement is the availability of a cross-class cramdown mechanism under the Part 26A scheme.[941] This feature empowers the court to confirm the plan on dissenting classes of creditors. Under section 901G, a restructuring plan can still be approved by the court, even if one or more classes do not vote in favour, as long as the court is convinced that: (1) if the plan is sanctioned, no members of the dissenting classes would be any worse off than they would be in the case of a relevant alternative (Condition A); and (2) the plan has been accepted by at least 75% in value of a class that would receive a payment, or has a genuine economic interest in the company, in the event of the relevant alternative (Condition B). The 'relevant alternative' is what the court considers most likely to happen to the company if the court does not sanction the restructuring plan.[942] Arguably, the application of the cross-class cramdown mechanism under section 901G is dictated by how the key phrases of 'genuine economic interest in the company' and 'relevant alternative' are construed and applied.[943]

The recent case *Re DeepOcean*[944] is the first case in which the court applied the cross-class cramdown provisions in section 901G. In this case, three UK affiliates of DeepOcean Group – DeepOcean 1 UK Limited (DO1), DeepOcean Subsea Cables Limited (DSC) and Enshore Subsea Limited (ES) – proposed three parallel restructuring plans to attain a solvent wind-down and avert the undesirable effects of insolvent liquidation on the rest of the group. While the restructuring plans of DO1 and ES were accepted by the majority of their creditors, the DSC's class of unsecured creditors failed to reach the required majority, as only 64.6% in value of the creditors within that class voted in favour of the DSC's restructuring plan. Nonetheless, by applying the cross-class cramdown provisions under section 901G, Trower J sanctioned all three restructuring plans at the sanctioning hearing.

[940] CA 2006, s 901F.
[941] CA 2006, s 901G.
[942] CA 2006, s 901G (4).
[943] McCormack, *Permanent Changes to the UK's Corporate Restructuring and Insolvency Laws in the Wake of Covid-19* (n 441) 25.
[944] [2021] EWHC 138 (Ch).

Trower J concluded that the two conditions of cross-class cramdown (Conditions A and B) were met. The judge first referred to Condition A, which requires that none of the dissenting class members would be any worse off than they would be in the case of the relevant alternative. Trower J stated that identifying the relevant alternative in this context is similar to the exercise the court may carry out when applying a 'vertical' comparison for the purposes of an unfair prejudice challenge to a CVA (i.e. comparing the outcome of the proposed CVA with the outcome of a realistically available alternative process [usually liquidation] and establishing a 'lower bound' below which a CVA cannot go).[945] Such a comparison was discussed previously in this part.

In most cases, the relevant alternative will be administration or liquidation of the company, and this was the case in *Re DeepOcean,* where the court concluded that liquidation was the most relevant alternative. However, Trower J noted that cases may exist for which identifying the relevant alternative is difficult, which makes it harder to determine the financial impact of the plan on creditors and to adequately assess whether section 901G has been satisfied.[946]

In *Re DeepOcean,* Condition A was met because the unsecured creditors (the dissenting class) would recover about 4% of their claims under the plan. In contrast, they would receive nothing under the relevant alternative (i.e. liquidation). Additionally, the court held that Condition B was satisfied. Condition B requires that the proposed plan be accepted by at least 75% in value of a class of creditors who would receive a payment or had a genuine economic interest in the company in the event of the relevant alternative. This is an evidence-based exercise. Nonetheless, it is noted from the *DeepOcean* decision that the supporting class's economic recovery under the relevant alternative does not have to be substantial to satisfy Condition B. In *Re DeepOcean,* the recovery for secured creditors (who supported the plan) was small in a liquidation situation (the relevant alternative). However, the small recovery was, in the court's view, sufficient for satisfying Condition B.[947]

[945] ibid at 30.
[946] ibid at 31.
[947] ibid at 40.

7.2 Reorganisation Plan in US Chapter 11 Procedure

Within the first 120 days after a petition for reorganisation is filed under US Chapter 11, generally referred to as the 'exclusivity period', the debtor has the exclusive right to propose a Chapter 11 plan for reorganisation.[948] The court may extend or reduce the exclusivity period if it finds cause to do so, but it cannot extend the 120-day period beyond 18 months from the date the case commenced.[949] Creditors may propose a reorganisation plan only if the debtor's exclusivity period has expired without the debtor having proposed a plan or if a trustee has been appointed.[950]

Before seeking creditors' approval of a reorganisation plan, the debtor company must prepare a disclosure statement that contains 'adequate information' regarding the debtor and the reorganisation plan such that it would enable a hypothetical investor to make an informed judgment on the plan.[951] The disclosure statement must be approved by the court. In addition, Chapter 11 creditor claims must be sorted into one or more classes according to their nature.[952] The entitlement to vote on the plan is only granted to classes of creditors or shareholders whose rights are 'impaired' (altered) by the plan.[953] Classes that receive nothing under the plan are deemed to have rejected the plan, so their votes do not need to be solicited;[954] classes that are not impaired by the plan are deemed to have accepted the plan, so their votes do not need to be solicited, either.[955] After the vote, if the creditors' approval has been obtained, the court must confirm the reorganisation plan in order for the plan to be binding.

[948] Bankruptcy Code, s 1121(b). On the 'exclusivity period', see Novica Petrovski, 'The Bankruptcy Code, Section 1121: Exclusivity Reloaded' (2003) 11 Am Bankr Inst L Rev 451; Neill D Fuquay, 'Be Careful What You Wish for, You Just Might Get It: The Effect on Chapter 11 Case Length of the New Cap on a Debtor's Exclusive Period to File a Plan' (2006) 85 Tex L Rev 431; Barbara E Nelan, 'Multiple Plans on the Table During the Chapter 11 Exclusivity Period' (1989) 6 Bankr Dev J 451.

[949] Bankruptcy Code, s 1121(d)(2)(A). This deadline appears to be absolute, which means that courts have no authority to extend it; see *In re Randi's, Inc*, 474 B R 783, 56 Bankr Ct Dec 187 (Bankr S D Ga 2012) (holding that courts may not rely on s 105 to extend the deadlines in s 1121).

[950] Bankruptcy Code, s 1121(c).

[951] Bankruptcy Code, s 1125(a)(1).

[952] Bankruptcy Code, s 1123(a)(1).

[953] Bankruptcy Code, s 1124.

[954] Bankruptcy Code, s 1126(g).

[955] Bankruptcy Code, s 1126(f).

7.2.1 Classification of Claims

The classification of claims, a crucial step in the Chapter 11 reorganisation plan confirmation process,[956] is intended primarily to ensure that differences in creditors' rights are recognised and that creditors are treated appropriately based on their different rights.[957] The classification of claims is important to the Chapter 11 voting process for several reasons.[958] First, creditor support for the reorganisation plan is determined according to acceptance by class. Specifically, the plan is considered accepted by a class of claims if creditors that hold more than one half in number of the claims in that class and at least two-thirds in value of the claims allowed to vote on the plan in that class approve the plan.[959]

Second, the debtor's plan must be accepted either by all impaired classes of creditors (i.e. consensual plan) or by at least one impaired class (i.e. cramdown plan) to be confirmed. Ideally, all impaired classes will accept the plan, in which case the debtor will not have to litigate on cramdown rules, thus avoiding any prohibitive delays and costs related to cramdown litigation.[960] If the acceptance of all impaired classes is not obtained, the debtor needs at least one consenting impaired class of creditors to 'cramdown' the plan on the dissenting class or classes under section 1129(b). Moreover, if claims are improperly classified, the court will not confirm the reorganisation plan.[961]

Section 1122(a) provides that claims can be placed in the same class only if they are 'substantially similar'.[962] The prime measurement of this similarity is the claim holder's relative priority for payment against the debtor's assets.[963] Thus, secured claims and unsecured claims are legally dissimilar because secured claims have the right to full payment before unsecured claims receive any recovery, so secured claims cannot be placed with unsecured

---

[956] See, generally, Tabb, *Law of Bankruptcy* (n 279) 1104; Scott F Norberg, 'Classification of Claims Under Chapter 11 of the Bankruptcy Code: The Fallacy of Interest Based Classification' (1995) 69 Am. Bankr. LJ 119; John C Anderson, 'Classification of Claims and Interests in Reorganization Cases Under the New Bankruptcy Code' (1984) 58 Am. Bankr. LJ 99; William Blair, 'Classification of Unsecured Claims in Chapter 11 Reorganization' (1984) 58 Am. Bankr. LJ 197; Linda J Rusch, 'Gerrymandering The Classification Issue in Chapter Eleven Reorganizations' (1992) 63 U. Colo. L. Rev. 163.
[957] *SPCP Group, LLC v Biggins*, 465 B R 316 (2011).
[958] See American Bankruptcy Institute (n 559) 257.
[959] Bankruptcy Code, s 1126(c).
[960] Hayes (n 866) 14.
[961] *In re Multiut Corp*, 449 B R 323, 333 (Bankr N D Ill 2011).
[962] Bankruptcy Code, s 1122(a).
[963] See, eg, *In re Frascella Enterprises, Inc*, 360 B R 435, 442 (Bankr E D Pa 2007) ('The similarity of claims is not judged by comparing creditor claims *inter se*. Rather, the question is whether the claims in a class have the same or similar legal status in relation to the assets of the debtor.').

claims in one class. Similarly, claims secured by different collateral, as well as those secured by the same collateral but with different rank, are not legally similar and, therefore, must be classified separately.[964]

While section 1122(a) prohibits placing claims in the same class if they are not substantially similar, it does not explicitly require placing similar claims in the same class, nor does it explicitly prohibit the separate classification of similar claims. This has created a longstanding debate on whether debtors have the discretion to separately classify substantially similar claims, and if they do, whether this discretion is limited in any way.[965] This issue almost always arises in relation to the classification of unsecured claims because such claims are, by nature, substantially similar.[966]

Debtors may wish to separately classify unsecured claims for several reasons.[967] First, for business purposes, a debtor may want to place trade creditors with whom the debtor has a continuous relationship in a separate class from other general unsecured creditors who have no such relationship with the debtor.[968] Additionally, the separate classification of unsecured creditors may be motivated by the debtor's attempt to ensure at least one consenting impaired class in order to cramdown the plan over the dissenting creditors under section 1129(a)(10).[969] As noted, for the plan to be confirmed by the court, section 1129(a)(10) requires that at least one impaired class accepts the plan. However, in some cases, the debtor may have difficulty satisfying section 1129(a)(10), a situation that often occurs in single asset real estate (SARE) cases.[970]

A typical SARE case usually has a few classes of creditors: (1) the mortgagee's secured claim against the debtor's real property, (2) the mortgagee's large unsecured deficiency claim and (3) several unsecured trade creditor claims.[971] Usually, the mortgagee is not supportive of the

[964] See *FGH Realty Credit Corp v Newark Airport/Hotel Ltd Partnership*, 155 B R 93, 99 (D N J 1993).
[965] Tabb, *Law of Bankruptcy* (n 279) 1106; Bruce A Markell, 'Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification' (1994) 11 Bankr. Dev. J. 1; Rusch (n 956) 182.
[966] Norberg (n 956) 120.
[967] See McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 257–262; Tabb, *Law of Bankruptcy* (n 279) 1106–1109.
[968] See, eg, *Cwcapital Asset Mgmt, LLC v Burcam Capital II, LLC*, No 5:13-CV-278-F (E D N C June 24, 2014).
[969] American Bankruptcy Institute (n 559) 259.
[970] See David R Hague, 'Sare Manipulation: The Hurdles in Single-Asset Real Estate Cases' (2018) 67 Cath UL Rev 280, 281.
[971] ibid 282.

reorganisation plan and aims to foreclose on the real property. As such, the debtor may need to classify the large unsecured deficiency claim of the mortgagee separately from the small unsecured claims of the trade creditors who are likely to vote in favour of the plan. Hague explained that if this separation is not allowed and all unsecured claims are placed in one class, 'the sheer size of a typical deficiency claim would generally allow the deficiency claimant to block confirmation by controlling the vote of a single unsecured creditor class. Without this separation, there would be no impaired accepting class and the SARE debtor could not confirm its plan – i.e., it would eventually lose its property (and its business) through a foreclosure.'[972] Therefore, the separate classification of unsecured claims may be necessary for the debtor to receive confirmation of the plan.

As indicated, section 1122(a) merely prohibits placing dissimilar claims in the same class; it does not explicitly require that all substantially similar claims be placed in the same class. Due to the bankruptcy code's silence on this matter, judicial views have varied on the extent to which similar claims (usually unsecured claims) can be classified separately. However, nearly all have agreed that classifying similar claims separately for the sole purpose of creating an accepting impaired class is not permissible.[973] This principle was articulated in the leading case of *In re Greystone III Joint Venture*,[974] in which the court held that 'one clear rule … emerges from otherwise muddled case law on §1122 claims classification: thou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan'.[975] Most courts consider separately classifying similar claims solely for the purpose of creating a consenting class as abuse of the bankruptcy process.[976] Thus, the debtor must advance a legitimate reason for separately classifying similar claims in order for such classifications to be permitted.[977]

[972] ibid; H Miles Cohn, 'Single Asset Chapter 11 Cases' (1990) 26 Tulsa LJ 523, 545.
[973] See, eg, *In re Barakat*, 99 F 3d 1520, 1523 (9th Cir 1996); *In re Boston Post Road Ltd P'ship*, 21 F 3d 477, 481–83 (2d Cir 1994); *In re Greystone III Joint Venture*, 995 F 2d 1274, 1279 (5th Cir 1991) ('[separate] classification may only be undertaken for reasons independent of the debtor's motivation to secure the vote of an impaired, assenting class of claims').
[974] 995 F 2d 1274, (5th Cir 1991).
[975] ibid at 1279.
[976] See *In re Holywell Corp*, 913 F 2d 873 (11th Cir 1990); *In re Curtis Center Ltd Partnership*, 195 B R 631 (Bankr E D Pa 1996); *Hanson v First Bank of South Dakota, NA*, 828 F 2d 1310, 1313 (8th Cir 1987) ('There is potential for abuse when the debtor has the power to classify creditors in a manner to assure that at least one class of impaired creditors will vote for the plan, thereby making it eligible for the cram down provisions.').
[977] *In re W R Grace & Co*, 475 B R 34 (D Del 2012); *In re Main Line Corp*, 335 B R 476 (Bankr S D Fla 2005).

The grounds for separately classifying similar claims that the courts have most frequently accepted are those based on business justifications.[978] For example, the courts have often allowed debtors to classify certain trade creditors with whom the debtor intends to have a continuing relationship separately from other general unsecured creditors, as the continuation and survival of the debtor's business may be heavily dependent upon the services and supplies provided by those trade creditors.[979] In *In re Richard Buick*,[980] a car dealer debtor separately classified its unsecured dealer-trade claims from other general unsecured claims. The debtor's plan proposed to pay the trade claims in full, whereas the other unsecured creditors would receive only 5% of their claims' value. The court found this justified because full payment of dealer-trade claims was necessary for the future success of the debtor's business.

Notably, although courts usually accept the separate classification of unsecured claims when done for business purposes, for many courts, the business reason may not be sufficient on its own to justify the separate classification of similar claims. For those courts, the debtor's business justification for separate classification of unsecured creditors may not be accepted unless the unsecured claims classified separately are treated differently.[981] It has been found 'that where all unsecured claims receive the same treatment in terms of the plan distribution, [the] separate classification of unsecured claims is highly suspect',[982] as it indicates that the real motive for separate classification of the unsecured claims may be to manipulate the vote on the plan.[983]

In addition to business justifications, classifying unsecured creditors who have interests that are at odds with the goal of the reorganisation plan separately from other unsecured creditors may also be allowed.[984] For example, unlike other unsecured creditors, an unsecured creditor who is a competitor of the debtor may have interest in the failure of the debtor's reorganisation.

---

[978] Tabb, *Law of Bankruptcy* (n 279) 1108; National Bankruptcy Review Commission, *Bankruptcy, the Next Twenty Years* (National Bankruptcy Review Commission 1997) 578.
[979] *In re Georgetown Ltd Partnership*, 209 B R 763, 772 (Bankr M D Ga 1997) ('Where, in order to successfully reorganize, it is necessary for a debtor to continue conducting business with certain unsecured creditors, a debtor is justified in separately classifying those creditors from other unsecured creditors.').
[980] 126 B R 840 (Bankr E D Pa 1991).
[981] *In re Greystone III Joint Venture*, 948 F 2d 134, 141 (5th Cir 1991) ('[debtor's] justification for separate classification of the trade claims might be valid if the trade creditors were to receive different treatment from [the under-secured creditor] …. Because there is no separate treatment of the trade creditors in this case, we reject [the debtor's] "realities of business" argument.').
[982] *In re Main Line Corp*, 335 B R 476, 479 (Bankr S D Fla 2005).
[983] *Travelers Insurance v Bryson Properties, XVIII*, 961 F 2d 496 (4th Cir 1992).
[984] Tabb, *Law of Bankruptcy* (n 279) 1108; McCormack, *Corporate Rescue Law--an Anglo-American Perspective* (n 271) 258; Markell (n 965) 44.

The non-creditor interest in this example may motivate the competitor to vote against the reorganisation plan to eliminate its business rival (the debtor), notwithstanding that the competitor as a creditor would receive little or no recovery of its claim when the reorganisation fails and the debtor enters into liquidation.[985] In other words, such a claimant may sacrifice its short-term creditor interest to serve its long-term competition interest. As stated in *In re Texas Star Refreshments*,[986] a non-creditor interest may give the creditor 'a different stake in the future viability of [the debtor business] that may cause it [the creditor] to vote for reasons other than its economic interest in the claim'.[987] Therefore, classifying unsecured creditors with interests contrary to the goal of the reorganisation plan separately from other unsecured creditors has usually been accepted by the courts.

In light of the foregoing, two straightforward rules restrict the classification of claims in the Chapter 11 process: '[d]issimilar claims may not be classified together; similar claims may be classified separately only for a legitimate reason'.[988] Such reasoning must be independent of the debtor's intent to create one assenting class in order to be eligible for cramdown provisions.[989]

7.2.2 Court's Confirmation of Chapter 11 Reorganisation Plan

A reorganisation plan that has been accepted by all classes of claims and interests is not binding until it has been confirmed by the court.[990] Indeed, court confirmation of a reorganisation plan is considered the ultimate goal or the culmination of the Chapter 11 process.[991] Once confirmed, the plan becomes binding on all parties to the reorganisation procedure, regardless of whether their claims are impaired under the plan and regardless of whether they voted in favour of the plan.[992]

---

[985] Markell (n 965) 44.
[986] 494 B R 684 (Bankr N D Tex 2013).
[987] ibid at 696. See also *In re Save Our Springs (S O S) Alliance, Inc*, 632 F 3d 168 (5th Cir 2011).
[988] *In re Chateaugay Corporation*, 89 F 3d 942, 949 (2d Cir 1996).
[989] *In re Greystone III Joint Venture*, 995 F 2d 1274, 1279 (5th Cir 1991).
[990] See Epstein and Nickles (n 546) 117.
[991] Mark G Douglas, 'Unscrambling the Egg or Redividing the Pie: Revoking a Chapter 11 Plan Confirmation Order' (2006) 2 Pratt's J. Bankr. L. 333; Tabb, *Law of Bankruptcy* (n 279) 1131.
[992] Bankruptcy Code, s 1141(a). See Tabb, *Law of Bankruptcy* (n 279) 1191. (arguing that the fact that a confirmed Chapter 11 plan binds dissenting creditors is a significant effect of the Chapter 11 process and distinguishes it from out-of-court settlements, which do not bind dissenting creditors).

To promote the finality of the Chapter 11 process, the confirmation order is usually inviolable;[993] according to section 1144, the court may only revoke the order upon the request of an interested party made within 180 days from the date the order of confirmation of the Chapter 11 plan is entered 'if and only if such order was procured by fraud'.

7.2.2.1 Statutory Requirements for Confirmation of Plan

The court must determine that a Chapter 11 reorganisation plan meets 16 requirements set out by section 1129(a) before it can confirm the plan. The most important requirements are that the plan complies with applicable laws and that the plan has been proposed in good faith.[994] The court must also be convinced that the plan is feasible, i.e. that the reorganisation plan is credible and that confirmation of the plan is not likely to be followed by liquidation or a need for further financial reorganisation.[995] Another critical requirement for confirmation of the Chapter 11 plan is that it must pass the 'best interests of creditors test', which requires each dissenting claim holder (including dissenting claim holders in classes that have accepted the plan) under the reorganisation plan to receive at least the equivalent to what it would have received in liquidation.[996]

The court can confirm a plan if all the requirements set out in section 1129(a) are met, including section 1129(a)(8), which requires the plan to be accepted by all impaired classes. Alternatively, at the request of the plan proponent, a plan accepted by at least one class of claims can still be imposed, or 'crammed down', on the dissenting classes if all the requirements set out in section 1129(a) other than paragraph (8) are met and the court determines that first, the plan does not discriminate unfairly against the dissenting class, and second, the plan is fair and equitable.[997] These two conditions are discussed in the following subsection.

[993] See Douglas (n 991) 333. (arguing that the lack of certainty about the validity and permanence of the transactions performed under a reorganisation plan would compromise the primary object of Chapter 11 as a rehabilitation means for ailing enterprises).
[994] Bankruptcy Code, s 1129(a)(2), (3).
[995] Bankruptcy Code, s 1129(a) (11).
[996] Bankruptcy Code, s 1129 (a) (7).
[997] Bankruptcy Code, s 1129 (b).

7.2.2.1.1 Additional Criteria for Cramdown of Dissenting Classes

7.2.2.1.1.1 Condition (1): The Plan Does Not Discriminate Unfairly

The first condition that must be met before cramming down an objecting class of creditors is that the plan does not discriminate unfairly against that class.[998] The unfair discrimination prohibition is a horizontal test that aims to ensure that the objecting class is not treated less favourably than other classes of equal rank without reasonable justification.[999] In other words, this requirement protects the dissenting classes 'against involuntary loss of their equal distribution rights *vis a vis* other creditors of equal rank'.[1000]

The prohibition of unfair discrimination when a plan is crammed down on a dissenting class is commonly confused with the issue of improper classification of claims under section 1122(a), which is not a cramdown issue.[1001] The analysis of a claim classification is generally restricted to consideration of whether a member of a particular class has similar claims, whether the separate classification of similar claims is justified and whether the purpose for the separate classification of similar claims is improper. Commonly, unequal treatment among classes is not addressed under the issue of claim classification.[1002]

Notably, not all forms of discrimination against similarly situated classes are necessarily prohibited: only 'unfair' discrimination is prohibited. Indeed, a Chapter 11 reorganisation plan may discriminate between classes of equal rank, provided such discrimination is fair.[1003] Thus, a determination is needed as to what kinds of discrimination are considered fair and are, therefore, allowable versus what kinds are considered unfair and are, therefore, prohibited under section 1129(b)(1). The bankruptcy code provides no guidance on this matter, nor does

---

998 Bankruptcy Code, s 1129 (b).

999 Bruce A Markell, 'A New Perspective on Unfair Discrimination in Chapter 11' (1998) 72 Am Bankr LJ 227.

1000 *In Re: Sentry Operating Company of Texas*, 264 B R 850, 865 (Bankr S D Tex 2001).

1001 Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York, 'Making the Test for Unfair Discrimination More" Fair": A Proposal' (2002) 58 The Business Lawyer 83, 85. However, this does not deny the fact that improper classification may be motivated by the debtor's attempt to ensure at least one consenting impaired class in order to cram down the plan over the dissenting creditors under section 1129(a)(10). See American Bankruptcy Institute (n 559) 259.

1002 Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York (n 1001) 86. Nonetheless, as noted in section 7.2.1, separating trade creditors from other unsecured creditors without treating trade creditors differently is received with a great amount of suspicion by some courts and implies that the real motive of separate classification is to manipulate the vote on the plan. See *In re Greystone III Joint Venture*, 948 F 2d 134, 141 (5th Cir 1991); *In re Main Line Corp*, 335 B R 476, 479 (Bankr S D Fla 2005; *Travelers Insurance v Bryson Properties, XVIII*, 961 F 2d 496 (4th Cir 1992).

1003 See Norberg (n 956) 162. (stating that section '1129(b)(1), which makes unfair discrimination a bar to cramdown, condones, by implication, fair discrimination').

case law set forth a uniform standard to determine when the rule of unfair discrimination is violated. As such, courts have developed different approaches to determine whether a reorganisation plan discriminates unfairly.[1004]

Most courts apply a four-part test, or what is called a 'broad test', to determine whether discrimination between similarly situated classes as proposed in a Chapter 11 reorganisation plan is unfair. The test requires that (1) the discrimination has a reasonable basis, (2) the discrimination is necessary to the reorganisation, (3) the discrimination is proposed in good faith and (4) the degree of discrimination is directly proportional to its rationale.[1005]

Despite its wide application, the four-part test has been criticised for being highly subjective and for its lack of predictability.[1006] The speculative and subjective nature of the questions employed in the four-part test have been argued as leading to unpredictability and uncertainty on whether a certain type or level of discrimination will be ruled unfair by the court.[1007]

Alternatively, many courts have adopted a more elastic test to determine whether a reorganisation plan discriminates unfairly.[1008] Under this test, a proposed discrimination will be allowed if the plan proponent can prove that, first, the discrimination is supported by a legally acceptable rationale, and second, the extent of the discrimination is necessary in light of the rationale.[1009] The discrimination will, however, rise to the level of unfairness when no reasonable justification can be made for the less favourable treatment of the dissenting class. In this case, the reorganisation plan cannot be crammed down on the dissenting classes.

[1004] For an expansive explanation and critique of these various approaches, see Denise R Polivy, 'Unfair Discrimination in Chapter 11: A Comprehensive Compilation of Current Case Law' (1998) 72 Am. Bankr. LJ 191; Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York (n 1001).
[1005] *In re Aztec Co*, 107 B R 585 (Bankr M D Tenn 1989).
[1006] Markell (n 999) 242–246; Polivy (n 1004) 205–207; Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York (n 1001) 92–94.
[1007] Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York (n 1001) 92.
[1008] Norberg (n 956) 162; Markell (n 999) 243.
[1009] *In re 203 North LaSalle Street Ltd. Partn.*, 190 B.R. 567, 585-86 (Bankr. N.D. Ill. 1995).

7.2.2.1.1.2 Condition (2): The Plan Is Fair and Equitable

The second prerequisite for cramming down a dissenting class of creditors is that the plan must be fair and equitable with respect to such a class.[1010] Unlike the prohibition of unfair discrimination, which is a horizontal test, the 'fair and equitable' requirement is a vertical test intended to protect against unfair treatment between creditors of different rankings.[1011] This requirement protects the dissenting class of creditors 'against involuntary loss of their priority status, vis a vis other classes of different rank'.[1012] Moreover, contrary to the prohibition of unfair discrimination, the meaning of the fair and equitable test has been elaborated on by the bankruptcy code. Section 1129(b)(2) sets forth minimum conditions that must be satisfied for a plan to be fair and equitable with respect to a dissenting class.

With respect to a dissenting class of secured creditors, a reorganisation plan is fair and equitable if it provides secured creditors with one of the following three alternatives:[1013] (1) The secured creditors retain their security interests to the extent of the allowed amount of their claims and receive deferred cash payments with a present value at least equal to the collateral's value. (2) The collateral is sold with the creditor's security interest attached to the proceeds of the sale. (3) The creditor receives an 'indubitable equivalent' of its security interest.

For a dissenting class of unsecured creditors, the reorganisation plan is fair and equitable with respect to such a class if the plan conforms with the 'absolute priority rule' (APR).[1014] The APR requires that unless a dissenting class of creditors is paid in full, no value can be distributed to any class of creditors junior to that dissenting class. This means that unless the plan purports to pay the dissenting unsecured creditors in full, the shareholders of the debtor company are not entitled to receive or retain any property through the reorganisation plan based on their shares. Moreover, although not expressly stated by the code, an unwritten corollary of the APR that has been consistently confirmed by the courts[1015] mandates that a class senior to

[1010] Bankruptcy Code, s 1129(b).
[1011] Richard Maloy, 'A Primer on Cramdown-How and Why It Works' (2003) 16 St Thomas L Rev 1, 13.
[1012] *In Re: Sentry Operating Company of Texas*, 264 B R 850, 865 (Bankr S D Tex 2001).
[1013] Bankruptcy Code, s 1129(b)(2)(A).
[1014] Bankruptcy Code, s 1129(b)(2)(B).
[1015] See Robert L Ordin and Sally McDonald Henry, *Ordin on Contesting Confirmation* (7th edn, Wolters Kluwer 2020) ch 12.

a dissenting class cannot receive more than 100% of its claims at the expense of the dissenting junior class.[1016]

Nevertheless, the mandate of the APR that shareholders cannot retain interests in the reorganised company unless dissenting creditors are paid in full is subject to one exception. Under the so-called 'new value exception', the shareholders may retain interests in the reorganised company even if the dissenting creditors are not fully paid provided the shareholders supply new capital contributions that are substantial, are necessary for a successful reorganisation, are in the form of money or money's worth and are reasonably equivalent to the value of the shareholders' retained interests in the reorganised company.[1017]

[1016] See *In re Exide Technologies*, 303 B R 48, 61 (Bankr D Del 2003); *In re Sunedison, Inc*, 575 B R 220, 227 (Bankr S D N Y 2017); *In re Breitburn Energy Partners LP*, 582 B R 321, 350 (Bankr S D N Y 2018).

[1017] See *In re Bonner Mall Partnership*, 2 F 3d 899, 908 (9th Cir 1993); *In re Woodbrook Associates*, 19 F 3d 312, 319–20 (7th Cir 1994).

7.3 Restructuring Plan Under Saudi Restructuring Procedures

As an introduction to this section, recall that Saudi BL 2018 contains two restructuring procedures: Financial Restructuring (FR) and Preventative Settlement (PS).[1018] The rules governing the process of reorganisation under these two procedures are identical in relation to the entitlement to vote on the plan, how the creditors' vote is conducted and the threshold for creditors' approval of the plan. Moreover, under the two procedures, if the creditors' approval has been obtained, in order for the plan to be binding the court must confirm the plan.[1019] Furthermore, and in common with the US and UK practices discussed in the previous sections, BL 2018 does not prescribe the content of the plan under either of its two restructuring procedures. This provides the company and its creditors a high degree of flexibility with which to negotiate and produce plans that serve their interests.[1020] Thus, the plan can accommodate several types of arrangements between the debtor company and its creditors, such as a rescheduling, reduction, deferral or instalment of the debtor's debts.[1021] The plan may also propose a debt-for-equity swap, whereby creditors become shareholders in the reorganised company.[1022]

Even though the FR and the PS procedures are indistinctively similar in many ways, they differ on one significant aspect: the availability of a cross-class cramdown mechanism. This mechanism, which empowers the court to confirm the plan, notwithstanding the existence of one or more dissenting classes of creditors, is available under the FR procedure but not under the PS procedure. This section examines the process of the restructuring plan under the Saudi restructuring regime in relation to the following issues: entitlement to vote on the plan, classification of claims, the threshold of creditors' acceptance of the plan, the court's confirmation of the plan and the cross-class cramdown mechanism. This examination is carried out considering the UK and US stands on these issues, which were illustrated in the previous parts of this chapter.

[1018] See, generally, Adli Hammad (n 648) 311–314.
[1019] BL 2018, arts 32, 80.
[1020] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 320; Al-Ahmad (n 315) 98.
[1021] Implementing Regulations of BL 2018, art 16(l).
[1022] ibid.

7.3.1 Entitlement to Vote on Restructuring Plan

The right to vote on the reorganisation plan under both Saudi BL 2018 restructuring procedures (FR and PS) is only granted to creditors whose rights are affected by the plan through reduction, deferral or instalment thereof.[1023] Therefore, the votes of unaffected creditors are not counted when determining whether the required majority has approved the reorganisation plan. On this issue, Saudi law is similar to the US law, under which the entitlement to vote on the Chapter 11 plan is only granted to classes of creditors or shareholders whose rights are 'impaired' (altered) by the plan.[1024] It is also similar to the position of the UK scheme of arrangement and the new Part 26A scheme, under which only creditors whose rights are affected by the scheme, or Part 26A, are entitled to vote. Moreover, this approach is in line with the recommendations of the United Nations Commission on International Trade Law (UNCITRAL), which seems to suggest that only creditors whose rights are modified or affected by the reorganisation plan should be entitled to vote on it.[1025] This contrasts with the position in the UK corporate voluntary arrangement (CVA), under which any creditor who receives notice of the creditors' meeting, including unaffected creditors, is entitled to vote on the CVA proposal,[1026] and as illustrated previously in this chapter, the votes of unsecured creditors whose rights are unaffected by the CVA are counted when determining whether the required majority has approved the CVA.[1027]

Limiting the entitlement to vote on the reorganisation plan to those whose rights are affected by the plan seems more appropriate than allowing unaffected creditors to vote and counting their votes when determining whether the required majority has approved the plan. Otherwise, the votes of creditors who are significantly disadvantaged by the plan can be swamped by the votes of creditors who stand to lose nothing from the plan. Nevertheless, this has been a common practice under the UK CVA procedure, which has been frequently used to compromise the rights of certain creditors, mostly landlords, when other largely unaffected creditors have approved the CVA.[1028] As stated previously, the British Property Federation

[1023] BL 2018, arts 27, 76; Implementing Regulations, arts 39, 45.
[1024] Bankruptcy Code, s 1124.
[1025] UNCITRAL (n 376) 235. ('The insolvency law should specify that a creditor or equity holder whose rights are modified or affected by the plan should not be bound to the terms of the plan unless that creditor or equity holder has been the given the opportunity to vote on approval of the plan.').
[1026] Insolvency Rules 1986, r 1.17(1).
[1027] See 'The Abuse of CVAs Must End | EG News' (n 885).
[1028] A recent case that demonstrates this practice is *Lazari Properties2 Ltd v New Look Retailers Ltd* [2021] EWHC 1209 (Ch). In this case, the clothing retailer (New Look) proposed the CVA to impose rent reductions on a number of its landlords. The landlords challenged the CVA on the grounds of unfair prejudice, arguing that the requisite

(BPF) has criticised this practice, describing it as abusive and unfair and arguing that the current rules governing the CVA process 'enable companies to unfairly engineer the weight attached to affected creditors' voting rights, often resulting in unaffected creditors approving CVAs with affected creditors being powerless'.[1029] The BPF, consequently, has urged the UK government to reform the CVA process by adopting a voting approach that is fairer to those compromised by the arrangement. The BPF recommended that the votes of unaffected creditors not be counted when determining whether the required majority has approved the CVA to ensure a fairer approach.[1030] Therefore, as it prevents the risk of the affected creditors' votes being swamped by the votes of unaffected creditors, the approach adopted under the Saudi restructuring procedures that restricts the unaffected creditors from voting on reorganisation plans seems appropriate.

7.3.1.1 Impact of Restructuring Plan on Secured Creditors

One of the shortcomings of the former and superseded Saudi restructuring law (BPS 1996) was that the reorganisation plan under that law could not affect the rights of secured creditors.[1031]On this issue, BPS 1996 was similar to the UK CVA, which cannot affect the rights of secured creditors without their consent.[1032] However, unlike the CVA, the former Saudi restructuring law provided no exception for the plan to affect the secured creditors' rights when they consent.

This defect was amended by the introduction of BL 2018, under which the restructuring plan can affect the rights of secured creditors without their consent if the plan has obtained the requisite approval.[1033] This amendment places the two restructuring procedures under BL 2018 on the same footing with US Chapter 11 and the UK scheme of arrangement and new Part 26A scheme, as the rights of secured creditors can be compromised under each of these procedures.

Allowing the restructuring plan to affect the rights of secured creditors is a desirable approach.[1034] In many restructuring cases, secured claims represent a significant portion of the

majorities at the creditors' meeting were secured with the votes of creditors whose claims against the company were unimpaired by the CVA. The challenge was rejected by the court, however.

[1029] BPF (n 886) para 28.

[1030] ibid 17.

[1031] BPS 1996, art 9.

[1032] IA 1986, s 4(3).

[1033] Idris (n 810) 39.

[1034] See UNCITRAL (n 376) 220; Jay Lawrence Westbrook, *A Global View of Business Insolvency Systems* (Martinus Nijhoff Publishers 2010) 153.

debts owed by the distressed company. In these cases, the modification of secured creditors' rights and the use of the encumbered assets may be necessary for the reorganisation process to succeed.[1035] The prospects of a successful restructuring in such cases may diminish, however, if the plan cannot bind the secured creditors and they are allowed to enforce their security interests through repossession or sale of the encumbered assets.[1036]

7.3.2 Classification of Claims

Like the positions under US Chapter 11 and the UK scheme of arrangement and Part 26A scheme, creditors' voting on the restructuring plan under both Saudi BL 2018 restructuring procedures (FR and PS) is conducted by classes of creditors. BL 2018 and its Implementing Regulations provide that if multiple creditors with rights of a different nature exist, they must be sorted into classes, each class comprising holders of similar rights.[1037]

The classification of claims is crucial in the context of corporate restructuring.[1038] The key objective of claims classification is to meet the criteria for providing fair and equitable treatment to creditors by treating similarly situated claims equally and ensuring that the reorganisation plan offers the same terms to all creditors in a particular class.[1039] Moreover, creditor support for the reorganisation plan is determined according to acceptance by class. A creditor's vote to approve or reject the plan is only recognised within the context of the class to which the creditor's claim belongs.[1040] If a class approves the plan, such approval binds all holders of claims within that class, including dissenting creditors.

Given the importance of claims classification in the context of corporate restructuring procedures, the rules governing such classifications should be clearly stated to avoid any potential abuse.[1041] The lack of such clear rules may open the door for vote manipulation by the gerrymandering of classes, through which classes of claims are artificially created to result in favourable outcomes for a certain restructuring that would not necessarily be achieved if the allocation of creditors into classes followed a more evident or natural method.[1042] For example,

[1035] UNCITRAL (n 376) 220.
[1036] ibid.
[1037] BL 2018, arts 29, 74; Implementing Regulations, art 16(q).
[1038] See, generally, Norberg (n 956) 119; American Bankruptcy Institute (n 559) 257–61.
[1039] UNCITRAL (n 376) 218; Westbrook (n 1034) 154.
[1040] Blair (n 956) 198.
[1041] Westbrook (n 1034) 154.
[1042] Gerard McCormack, *The European Restructuring Directive* (Edward Elgar Publishing Limited 2021) 194.

in procedures under which cross-class cramdown is possible, the debtor may attempt to artificially create multiple classes of similar claims to warrant the acceptance of at least one class, which is a key condition for cramming down.[1043] This is referred to as an 'underinclusive classification'.[1044] Similarly, especially in procedures in which the cross-class cramdown is not possible and the acceptance of all classes is required for the restructuring plan to be confirmed, the debtor may attempt to prevent the existence of a dissenting class by placing the claims of the dissenting creditors in one class with larger claims of consenting creditors, despite the difference in the nature of these claims, hoping that the votes favouring the plan will swamp those of the dissenting creditors.[1045] This is referred to as an 'overinclusive classification'.[1046]These kinds of gerrymandering of classes and artificial classification can be screened out and prevented by governing the classification of claims with a clearly defined rule.

Unfortunately, the rules governing the classification of claims under Saudi BL 2018 are far from adequate to achieve this goal. The rules merely state that each class should comprise holders of similar rights, without clarifying the criteria by which this similarity is measured. As a result, plan proponents have an unrestricted amount of freedom to set their own criteria of similarity for classifying the claims of creditors into different classes. For example, classifying creditors' claims as bank claims, supplier claims, and general claims has been a common practice.[1047]

More controversially, with no criteria against which to measure the similarity of claims in order to classify them, placing secured claims into one class with unsecured claims on the basis that these claims are of one type (for example, trade claims, bank claims and so on) has become both common practice and judicially acceptable.[1048] An example demonstrating this issue is case number 8170,[1049] which concerned a company restructuring under the PS procedure. In this case, all secured and unsecured claims against the company were placed in one class (the trade claims class). The total value of the claims under this class amounted to 28,629,000 Saudi riyals, 5 million of which represented a secured claim. The plan was accepted by creditors

[1043] Baird (n 790) 242.
[1044] Norberg (n 956) 120.
[1045] See, eg, case number 8170 (2019).
[1046] Norberg (n 956) 122.
[1047] See, eg, case number 16153 (2019).
[1048] See, eg, case number 8170 (2019); case number 10312 (2019); case number 10553 (2019).
[1049] (2019).

whose claims amounted to 19,930,000 Saudi riyals, representing 69.6% of the value of debts owed to voters in the whole class. This satisfied the statutory majority threshold, which provides that a plan is deemed accepted by a class if the plan has been approved by the creditors whose claims represent two-thirds of the value of debts owed to voters in the same class.[1050] After being approved by creditors, the plan, then, was confirmed by the court.

However, including the secured claim, whose holder voted in favour of the plan, in one class with unsecured claims was a highly influential factor in that case, as if this had not been done, the restructuring plan would not have been approved. That is, the majority threshold would not have been satisfied if the secured claim had been in a separate class. In this scenario, two classes of trade claims would have existed: a class that comprised unsecured claims worth 23,629,000 riyals, and a class that included a secured claim of 5 million riyals. The total value of the claims voting in favour of the plan within the unsecured class would have been 14,930,000 Saudi riyals, representing 63.1% of the value of debts owed to voters in the whole class, which is below the two-thirds in value threshold, meaning that class of unsecured claims would not have accepted the plan. As mentioned, cross-class cramdown is not available under the PS procedure, which means that the existence of one dissenting class would have prevented the plan from being confirmed by the court.

The outcome in the example case described would not be possible if class formation rules under Saudi BL 2018 followed leading international insolvency practices, under which secured claims are classified separately from unsecured claims. As stated previously in this chapter, placing secured claims in one class with unsecured claims is not condoned under either the UK or the US restructuring regimes.[1051] Under the US regime, claims can be placed in the same class only if they are 'substantially similar',[1052] the main measurement of which is similarity in the claim holder's relative priority for payment against the debtor's assets.[1053] Accordingly, secured claims and unsecured claims are legally dissimilar because secured claims have the right to full payment before unsecured claims receive any recovery; therefore, secured claims cannot be placed with unsecured claims in one class. The same outcome is achieved under the

[1050] BL 2018, art 31(2).
[1051] See Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 52–54; Tabb, *Law of Bankruptcy* (n 279) 1105.
[1052] Bankruptcy Code, s 1122(a).
[1053] See, eg, *In re Frascella Enterprises, Inc*, 360 B R 435, 442 (Bankr E D Pa 2007) ('The similarity of claims is not judged by comparing creditor claims *inter se*. Rather, the question is whether the claims in a class have the same or similar legal status in relation to the assets of the debtor.').

UK scheme of arrangement. The test employed to determine whether creditors, for the purpose of voting on the scheme, should meet as a whole or as separate classes provides that the creditors affected by a proposed scheme must be divided into different classes if they have different rights in a way that they cannot consult together with a view to a common interest.[1054]Similarity and dissimilarity in this context is determined by reference to the creditors' legal rights against the company.[1055]Applying this test, and as their rights are clearly differentiated, secured creditors should be separately classified from unsecured creditors for the purpose of voting on the scheme.[1056]

Furthermore, placing secured claims in the same class with unsecured claims for the purpose of voting on a reorganisation plan is against the recommendations mentioned in supranational sources, which Saudi legislators considered during the process of drafting the new BL 2018, particularly, legislation and proposals at the EU level and UNCITRAL.[1057] The UNCITRAL Legislative Guide on Insolvency Law recommends that, for purposes of voting on the reorganisation plan, secured creditors should be classified separately from unsecured creditors.[1058] According to the Legislative Guide, this separate classification offers minimal protection for secured creditors and recognises that their rights and interests are different from those of unsecured creditors.[1059] Likewise, the newly enacted European Union Restructuring Directive (Directive 2019/1023) requires that, for the purpose of adopting a restructuring plan, creditors of secured and unsecured claims shall be treated in separate classes.[1060] According to Recital 44 of the Directive, class composition 'means the grouping of affected parties for the purposes of adopting a plan in such a way as to reflect their rights and the seniority of their claims and interests. As a minimum, secured and unsecured creditors should always be treated in separate classes.'

Accordingly, the author recommends that the rules governing classification under Saudi BL 2018 be amended. The rules should provide that creditors' claims can be placed in the same class only if they are 'substantially similar', and such similarity should be measured mainly by the claim holder's priority for payment against the debtor's assets. Applying this test, secured

[1054] *Re Hawk Insurance Co Ltd* [2002] BCC 300.
[1055] *Re BTR Plc* [1999] 2 BCLC 675.
[1056] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 52.
[1057] See Ministiry of Commerce and Industry (n 25) 4.
[1058] UNCITRAL (n 376) 220.
[1059] ibid.
[1060] Directive 2019/1023, art 9(4).

and unsecured creditors should always be classified separately. The existence of this test is necessary, as it reflects the fundamental difference between the rights of secured and unsecured creditors, which necessitates that they not be treated as a single class for the purpose of voting on the restructuring plan. Moreover, the test safeguards against overinclusive classification, through which claims of a different nature are grouped together in an attempt to prevent the existence of a dissenting class, which can lead, where class-cross cramdown is not applicable, to the court denying confirmation of the plan. Case number 8170 described in this section exemplifies the overinclusion practice, which would not be permissible if the classification test proposed here were adopted.

7.3.2.1 Separate Classification of Similar Claims

While the BL 2018 rules on classification require that each class comprise holders of similar rights, the rules do not explicitly require that all similar claims be placed in the same class, nor do the rules explicitly prohibit the separate classification of similar claims. Therefore, the separate classification of similar claims is permitted with no restriction under Saudi BL 2018.

Placing similar claims, particularly unsecured claims, into separate classes may be justified in certain circumstances. For example, when the successful rehabilitation of the debtor's business is heavily dependent upon the services and supplies provided by certain trade creditors, the debtor may need to classify those trade creditors separately from other general unsecured creditors and provide the former with more favourable treatment than the latter.[1061]

However, allowing the separate classification of similar claims to proceed without any restriction, which seems to be the case under Saudi law, may facilitate vote manipulation in the FR procedure, under which the cross-class cramdown mechanism is available. Under this procedure, acceptance of the reorganisation plan by at least one class of creditors is a condition for imposing the plan on the dissenting classes. This condition provides the plan proponent with an incentive to artificially create multiple classes of similar claims to ensure that at least one class accepts the plan, thus satisfying the cramdown condition.[1062]

[1061] Tabb, *Law of Bankruptcy* (n 279) 1108; National Bankruptcy Review Commission (n 978) 578. See also *In re Georgetown Ltd Partnership*, 209 B R 763, 772 (Bankr M D Ga 1997); *In re Richard Buick* 126 B R 840 (Bankr E D Pa 1991).
[1062] Baird (n 790) 242.

The author recommends that Saudi law be amended to follow the US and UK laws, under which this kind of artificial creation of multiple classes is not permitted. As illustrated previously in this chapter, the separate classification of similar claims has been subject to examination and scrutiny by the US courts to ensure that an acceptable justification for this classification exists other than the debtor's desire to obtain the approval of one class and fulfil the cramdown condition.[1063] Similarly, the UK courts recognise that the debtor may have an incentive to create multiple classes of creditors when implementing the new Part 26A scheme, under which the acceptance of one class is a condition of the cross-class cramdown provision (Condition B).[1064] In *Re DeepOcean*,[1065] Trower J stated that the court would be prepared to revisit the conclusion reached on classes if it appears that the classes were artificially created to ensure that Condition B would be satisfied. Therefore, Saudi BL 2018 should include a rule that limits the plan proponent's authority to classify similar claims separately. Such separate classification should not be permitted except for a legitimate reason independent of the plan proponent's intent to create one assenting class in order to be eligible for the cross-class cramdown provision.

7.3.3 Voting Threshold

After establishing that creditor support for the reorganisation plan under Saudi law is determined according to acceptance by class, a reasonable component of the law to consider is the threshold for such acceptance. Under BL 2018, a class of creditors is deemed to have accepted the plan if the claims of creditors voting in favour of the plan represent two-thirds of the value of debts owed to voters in that same class.[1066]

A class's acceptance of the reorganisation plan under Saudi BL 2018 restructuring procedures is based only upon the approval of the majority of the creditors in value; the majority in number is not required. In this regard, the Saudi restructuring procedures are like the UK CVA and Part 26A scheme, under which the majority in number is not required.[1067] This contrasts with the UK scheme of arrangement and US Chapter 11, under which a class's acceptance of the

[1063] *In re Chateaugay Corporation*, 89 F 3d 942, 949 (2d Cir 1996); *In re Greystone III Joint Venture*, 995 F 2d 1274, 1279 (5th Cir 1991).
[1064] CA 2006, s 901G (5).
[1065] [2021] EWHC 138 (Ch).
[1066] BL 2018, arts 31(2), 79(2).
[1067] Insolvency Rules 1986, r1 19(1); CA 2006, s 901F.

reorganisation plan is established based on the acceptance of both the majority in value and the majority in number of claims within that class.[1068]

The utility of the majority in number or 'headcount' test is debatable.[1069] The main rationale for this test is to protect small creditors, meaning creditors with small claims. The test has been argued as effective for preventing creditors with large claims from imposing their support of a restructuring plan on small creditors against the small creditors' will.[1070] Notably, this was the concern that prompted the introduction of the headcount test in the UK scheme of arrangement[1071] and seems to explain why the UK government has not abolished the test, despite the Company Law Review's (CLR's) recommendation to do so.[1072]

However, while the headcount test may be thought to protect small creditors, at the same time, the test offers small creditors a significant veto power disproportionate to the value of their interest. Under reorganisation procedures in which the majority in number is required, creditors with small claims can block a restructuring plan accepted by the overwhelming majority of creditors in value.[1073] As a simplified example, in a situation in which a company's total debt is 1,000,000 riyals, when the majority in number is required, two dissenting creditors owed 50,000 riyals each can impose their rejection of the proposed plan on one accepting creditor with a claim of 900,000 riyals. Moreover, the headcount test may be subject to manipulation via debt-splitting,[1074] in which a portion of the debt is assigned to a 'friendly' creditor who is more likely to vote in the assignor's favour.[1075] In light of these criticisms of the headcount test, dispensing with this test in Saudi restructuring law seems prudent.

[1068] CA 2006, s 899(1); Bankruptcy Code, s 1126(c).
[1069] McCormack, *The European Restructuring Directive* (n 1042) 197. For discussion on the headcount test, see Finch and Milman (n 244) 416–417; Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 61–68; Nicolaes Tollenaar, *Pre-Insolvency Proceedings: A Normative Foundation and Framework* (Oxford University Press 2019) 222–225.
[1070] See Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 63–64; Al-Aqili (n 816) 183.
[1071] The test was first introduced in 1870 and was designed 'to place a check on the ability of creditors with large claims to carry the day'. CLR (n 469) 215.
[1072] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 64. The headcount test was criticised by the CLR, which described the test as 'irrelevant and burdensome' and proposed its abolition. CLR (n 927) para 13.10; CLR (n 469) 207.
[1073] Payne, *Schemes of Arrangement: Theory, Structure and Operation* (n 383) 64.
[1074] ibid 68.
[1075] McCormack, *Permanent Changes to the UK's Corporate Restructuring and Insolvency Laws in the Wake of Covid-19* (n 441) 18.

Along these lines, the argument that the headcount test is necessary to protect creditors with small claims can be responded to in two ways. First, this argument assumes that holders of small claims are always vulnerable parties in need of protection, which is an inaccurate assumption. According to Tollenaar, creditors with small claims might be considered lucky because their exposure to the debtor's default is relatively limited.[1076] He further asserted that a creditor with a small claim can be a powerful party, such as a large supplier. Equally, creditors with large claims like small sole traders may be weak parties. Tollenaar then asked, 'Is a powerful supplier that can use its commercial bargaining power to effect punctual payment and thus keep its exposure limited more "pitiable" than a trader with a weaker bargaining position who has had to accept a delay in payment and corresponding increase in exposure?'[1077] Tollenaar's viewpoints help to clarify why creditors with small claims should not automatically be considered weak parties in need of protection.

Second, if creditors with small claims need protection, such protection may be accomplished through other methods that do not involve the headcount test drawbacks. In advocating for the abolition of the headcount test from the UK scheme of arrangement, Payne argued that small creditors may be protected at the sanctioning stage, where the treatment of small creditors can be considered by the court when assessing the scheme's overall fairness.[1078] This argument seems applicable in the context of Saudi restructuring law, under which the fairness of the restructuring plan is assessed by the court when deciding whether to confirm the plan. The role of courts in confirming restructuring plans under the provisions of Saudi BL 2018 is discussed next.

7.3.4 Court Confirmation of Reorganisation Plan

In common with the UK scheme of arrangement and new Part 26A scheme and with US Chapter 11, the court must confirm restructuring plans that have been approved by the majority of creditors under any of the BL 2018 restructuring procedures to make the plan binding.[1079] The Policy Paper of BL 2018 stated that the court's role in confirming the reorganisation plan is necessary to ensure that the plan is fair and reasonable.[1080] Therefore, as is the case under

[1076] Tollenaar (n 1069) 223.
[1077] ibid.
[1078] Jennifer Payne, 'Intermediation and Bondholder Schemes of Arrangement' in Jennifer Payne and Louise Gullifer (eds), *Intermediation and Beyond* (Bloomsbury Publishing 2019) 184.
[1079] BL 2018, arts 32, 80.
[1080] Ministiry of Commerce and Industry (n 25) 7.

the UK and US laws, the Saudi court plays a more substantial role in the confirmation stage than simply rubber stamping the creditors' approval of the restructuring plan.[1081]

Saudi law adopted a brevity approach in the establishment of requirements that must be satisfied in a restructuring plan for the court to confirm the plan. Saudi BL 2018 provides that the court will confirm the restructuring plan upon verifying its compliance with standards of fairness.[1082] According to Article 35 of BL 2018, a plan is deemed to have met the standards of fairness if the following three requirements are satisfied: (1) the creditors' voting procedures are observed; (2) the creditors have obtained sufficient information to review the plan as well as the alternatives available to the debtor as compared to the items in the plan; and (3) the outstanding creditors' rights are observed, especially with respect to sharing losses and the distribution of new rights, benefits and securities. These three requirements apply equally to restructuring plans under the two BL 2018 restructuring procedures (FR and PS). However, an additional fourth requirement is called for under the PS procedure, which is acceptance of the plan by all classes of creditors.[1083] Thus, the cross-class cramdown provision is not part of the PS procedure, unlike the FR procedure, under which cross-class cramdown is possible, provided that certain conditions are met. These four requirements and the criteria for cross-class cramdown under the FR procedure are discussed in the following sections.

7.3.4.1 Requirement (1): Voting Procedures Are Observed

The purpose of requiring the court's verification that voting procedures were observed is to ensure that approval of the plan by the required majority of creditors was achieved through a fair voting process, free from material irregularities and manipulation.[1084] Thus, the violation of the voting process rules would result in the court's refusal to confirm the plan. For example, in case number 16153,[1085] the court refused to confirm a reorganisation plan for a debtor subject to the PS procedure after the court found that the debtor had manipulated the creditors' classification. In the plan attached to his application to commence the PS procedure, the debtor had classified the creditors into three classes: banks, suppliers and general creditors. While negotiating with the creditors, the debtor became aware that the class of suppliers and the class of general creditors would reject the plan, so he modified the classification by cancelling these

[1081] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 323.
[1082] BL 2018, arts 34(1), 80(2).
[1083] BL 2018, art 31(2).
[1084] See Almansour (n 359) 35; UNCITRAL (n 376) 228.
[1085] (2019).

two classes and merging their claims into one class with the claims of the banks, which had the largest portion of the value of the debts owed by the debtor and had expressed their acceptance of the plan. Clearly, this merger of classes had a substantial effect on the outcome of the procedure. Without such a merger, the supplier creditors and general creditors would have both constituted dissenting classes. Because cross-class cramdown is not possible under the PS procedure, the existence of any dissenting class prevents the plan from being confirmed by the court. The court considered this change of classification a manipulation that violated the integrity of the voting process and, accordingly, refused to confirm the reorganisation plan.

An equivalent of this requirement can be found within the UK and US regimes. In the UK, assessing the propriety of the voting process on the scheme, especially regarding the composition of classes and creditors' meetings to vote on the scheme, is part of the court's task when determining compliance with the statutory provisions.[1086] The court has no jurisdiction to sanction the scheme when classes are wrongly constituted or when the correct meetings of creditors have not been held.[1087] Likewise, in the US, non-compliance with the rules of voting on a Chapter 11 plan, such as when the claims are improperly classified or when the votes on the plan are improperly solicited, will result in the court's refusal to confirm the plan.[1088]

7.3.4.2 Requirement (2): Sufficient Disclosure of Plan's Terms

This requirement related to sufficient disclosure of the plan's terms is intended to ensure that, prior to voting on a plan, creditors have received adequate information on the plan's terms, enabling them to make an informed decision on whether to vote for or against the plan.[1089] In essence, creditors must be informed about how exactly the plan will affect their rights, how much of their claims will be paid and the timescales and forms of such payments.[1090] Moreover, the disclosure obligation mandated under Article 35 is not confined to the plan's terms: creditors should also be made aware of how their claims will be treated if the plan is not confirmed. As a restructuring plan is usually proposed as an alternative to liquidation, creditors must be informed of their expected recoveries in the liquidation situation. This information enables creditors to assess their financial positions under the plan compared with their positions

[1086] *Re Noble Group Ltd* [2019] BCC 349.
[1087] *Re The British Aviation Insurance Co Ltd* [2006] BCC 14; *Re T&N Ltd* [2007] Bus L R 1411.
[1088] See HR Rep No 95-595, 95th Cong, 1st Sess 412 (1977); *In re Multiut Corp*, 449 B R 323, 333 (Bankr N D Ill 2011); *In re Colorado Springs Spring Creek Gen Imp Dist*, 177 B R 684 (Bankr D Colo 1995).
[1089] Case number 2107 (2020).
[1090] Implementing Regulations, art 16.

under liquidation so they can determine which is more likely to offer them greater and faster recoveries – the plan or liquidation – and make decisions accordingly.[1091] Therefore, applying this requirement, the court may refuse to confirm the plan if it finds that the information disclosed to the creditors regarding the plan's terms was inadequate or misleading.

The US and UK laws include an equivalent to this requirement as well. In the UK, prior to the creditors' vote on the scheme of arrangement, they must be provided with a statement (explanatory statement) that explains the effect of the proposed compromise or arrangement.[1092] As observed by Snowden J in *In re Ophir Energy Plc*,[1093] the explanatory statement must contain all the information needed to enable 'creditors to form a reasonable judgment on whether the scheme is in their interests or not, and hence how to vote'.[1094] Similarly, in the US, before seeking creditors' approval of a Chapter 11 plan, the debtor must prepare a disclosure statement and the court must approve this statement. The disclosure statement must contain 'adequate information' regarding the debtor and reorganisation plan. The information will be considered adequate if it would enable a hypothetical investor to make an informed judgment on the plan.[1095] Under both regimes, and in common with Saudi law, the failure to adhere to the disclosure requirement constitutes grounds for the court to refuse to confirm the reorganisation plan.[1096]

7.3.4.3 Requirement (3): Creditors' Rights Are Observed

In contrast to the first and second requirements, the requirement related to ensuring that creditors' rights are observed seems ambiguous. While the requirement dictates that the plan must observe the creditors' rights, it does not provide a test upon which courts can determine whether this 'observance' is achieved, nor have the courts attempted to interpret this requirement in their orders confirming reorganisation plans. Almost all confirmation orders issued until the time of this writing merely state that the plans have observed the rights of the creditors, without explaining *how* this assessment was determined.

[1091] See UNCITRAL (n 376) 216–217.
[1092] CA 2006, ss 897, 901D; Practice Statement (Companies: Schemes of Arrangement under Part 26 and Part 26A of the Companies Act 2006) [2020] 1 WLR 4493.
[1093] [2019] EWHC 1278 (Ch).
[1094] ibid at 22.
[1095] Bankruptcy Code, s 1125(a)(1).
[1096] See *Re Sunbird Business Services Limited* [2020] EWHC 2493; *In Re Landing Associates, Ltd*, 157 B R 791 (W D Tex 1993); HR Rep No 95-595, 95th Cong, 1st Sess 412 (1977).

This requirement may be argued as implying that the treatment of creditors' claims in the reorganisation plan must conform to the priority of those claims under the provisions of BL 2018. However, this argument does not seem valid for two reasons. First, the application of priority rules provided under BL 2018 is explicitly limited to the liquidation procedure.[1097] These rules do not apply to the treatment of creditors' claims in restructuring procedures, as this treatment is governed by the terms of the plan agreed upon by the creditors.

Second, courts have regularly confirmed reorganisation plans with terms that clearly deviate from the priority rules by providing payment for unsecured claims before secured claims are fully paid.[1098] One may argue that the courts' confirmation of these plans, despite their non-conformity with the priority rules, was due to the secured creditors' approval of these plans and the absence of creditors opposing the plans' non-compliance with the priority rules. However, this argument seems to overlook the essential point that the court does not have the authority to confirm a reorganisation plan that fails to meet one of the requirements stipulated in Article 35, including, of course, this requirement, even if all creditors approve the plan and no creditor objects to it.[1099] In other words, if this requirement meant that the treatment of creditors in the reorganisation plan should always conform to the priority of these claims, which is unlikely, the courts would not be able, under any circumstance, to confirm reorganisation plans that deviate from the priority rules; this result is not supported by the common practice of courts in confirming plans of this kind.

Therefore, to avoid conflicting interpretations of this requirement and the conflicting judgments they may generate, the author recommends that this requirement be redrafted in clearer language that specifically designates the criteria upon which courts can determine whether the plan observes the creditors' rights.

[1097] Fahad Alarifi, 'The Bankruptcy Law of Saudi Arabia: Policy, Operation and Comparison' (Emerald Publishing Limited 2021) <https://www.emerald.com/insight/content/doi/10.1108/PRR-02-2021-0011/full/html> accessed 3 August 2021; Al-Sarraf (n 830) 166.
[1098] See, eg, case number 8170 (2019); case number 7079 (2020).
[1099] Karaman, *Commercial Papers and Bankruptcy Procedures* (n 312) 372–373.

7.3.4.4 Additional Requirement in PS Procedure: Plan Is Accepted by All Classes of Creditors

In addition to the three requirements provided under Article 35, the restructuring plan under the PS procedure must be accepted by all classes in order to be confirmed by the court. In common with the UK scheme of arrangement, the PS procedure does not provide for a cross-class cramdown mechanism to allow confirmation of the reorganisation plan despite the objection of one or more class of creditors. This cramdown mechanism is only possible under the FR procedure.[1100]

When choosing between the two restructuring procedures available under BL 2018, distressed companies tend to select the PS procedure over the FR procedure as the first remedy for their financial dilemmas for the apparent reason that the former does not entail the appointment of a trustee to supervise the managerial activities of the debtor. As illustrated previously, the PS process employs a debtor-in-possession (DIP) model of control, under which the incumbent management remains in control during the process, with minimal involvement of the court over its decision-making authority, whereas the FR process adopts a co-determination model, under which the process is jointly controlled by the pre-filing management and a court-appointed trustee.[1101] While the directors remain in office after commencement of the FR procedure, their power in managing the company's affairs is restricted in that it is subject to the guidance and supervision of a court-appointed trustee.[1102]

However, due to the lack of a cramdown mechanism under the PS procedure, courts have commonly terminated PS procedures upon the failure of the settlement plan to obtain the required acceptance by all classes of creditors.[1103] Following such termination, the court usually, at its discretion or at the request of the debtor or any of the creditors, orders commencement of the FR procedure on the basis that such a procedure is appropriate for proceeding, as it provides a cramdown option to overcome the failure to meet the rigid voting quorum prescribed under the PS procedure. This situation has a negative impact on the process.

[1100] Almansour (n 359) 46.
[1101] Adli Hammad (n 648) 311.
[1102] ibid.
[1103] Examples of this practice are case number 6831 (2019); case number 10957 (2019); case number 2501 (2019); case number 5102 (2019).

Case number 6831,[1104] which concerns one of the leading engineering companies in the country, exemplifies this negative impact created by the lack of a cramdown mechanism under the PS procedure. The company experienced financial difficulties and defaulted on repayment of its debts. The company applied for restructuring under the PS procedure, and the court approved the opening of the procedure on 27/02/2019. After months of delay and multiple modifications of the company's restructuring plan, the plan failed to obtain the approval of all classes of the company's creditors. One of the classes (the bank claims class) voted against the plan. Based on the failure to obtain the acceptance quorum required by the PS procedure, the court terminated the procedure on 09/09/2019 and, upon the company's request, ordered the commencement of the FR procedure. The commencement of the FR procedure resulted in the appointment of a trustee to undertake several tasks, most notably, supervising management of the debtor company during the procedure, assisting the debtor in preparing a new reorganisation plan, inviting the creditors to vote on the proposed plan and then seeking confirmation of the plan by the court, which was finally obtained on 12/02/2020. In other words, the absence of a cross-class cramdown mechanism in the PS procedure resulted in the debtor company having to start over a long and financially exhausting reorganisation process.

Clearly, this practice involves an unnecessary increase in the cost and duration of the proceedings, contrary to the objectives of BL 2018 to reduce procedural costs and timeframes.[1105] This increase in the cost and duration of the restructuring procedure is detrimental, not only to the debtor but also to creditors, as this increase is likely to cause a reduction in the value of the reorganised estate, thereby increasing creditors' losses. To address this problem and to avoid the unnecessary increase in time and expense resulting from converting from one restructuring procedure to another, adopting the recommendation made in Chapter 3, which calls for abolishing the PS procedure and retaining the FR as the only restructuring procedure under BL 2018, seems appropriate. Otherwise, a cross-class cramdown mechanism should be allowed for in the PS procedure.

[1104] (2019).
[1105] BL 2018, art 5(d).

7.3.5 Cramdown Rules Under FR Procedure

A restructuring plan under the FR procedure may be confirmed by the court in two cases.[1106] In the first case, the plan has obtained the acceptance of all classes of creditors.[1107] In this case, the court will confirm the plan provided the three requirements stipulated under Article 35, as outlined under section 7.3.4, are satisfied. In the second case, the plan has not obtained the acceptance of all classes,[1108] but the court can still confirm the plan provided that, in addition to the three requirements stipulated under Article 35 being met, the plan also meets the following three additional conditions provided under Article 80(2)(b): (1) at least one class of creditors accepts the plan, (2) the creditors whose claims represent at least 50% of the total value of claims of creditors voting in all classes vote in favour of the plan and (3) the court determines that confirmation of the plan is in the best interest of the majority of creditors.[1109] Following is a discussion of these conditions.

7.3.5.1 Condition (1): One Consenting Class

For the cross-class cramdown provision to be activated, the restructuring plan must be accepted by at least one class of creditors. This is in common with the UK and US regimes, as under both an affirmative vote of at least one affected class is the gateway to the cross-class cramdown mechanism.[1110] This condition precludes a court from using its cramdown authority when no affected class has voted in favour of the plan. The policy underlying this condition was explained by the US court in *In re 266 Washington Associates*.[1111] The court stated that the condition is designed to ensure that, before compelling the dissenting classes 'to shoulder the risks of error necessarily associated with a forced confirmation, there must be some other properly classified group that is also hurt and nonetheless favors the plan'.[1112] Therefore, the purpose of this condition is to ensure that the plan has the support of some affected creditors and to prevent confirmation of the plan in the absence of such support.[1113]

[1106] BL 2018, art 80(2).
[1107] BL 2018, art 80(2)(a).
[1108] BL 2018, art 80(2)(b).
[1109] BL 2018, art 80(2)(b).
[1110] CA 2006, s 901G(5); Bankruptcy Code, s 1129(a)(10).
[1111] 141 B R 275 (Bankr E D N Y 1992).
[1112] ibid at 287.
[1113] *Windsor on the River Associates, Ltd. v. Balcor Real Estate Finance, Inc*, 7 F 3d 127 (8th Cir 1993). See also Robert L. Ordin and Sally McDonald Henry (n 1015) ch 8; Alexander J Gacos, 'Reconciling the "Per-Plan" Approach to 11 USC § 1129 (a)(10) with Substantive Consolidation Principles Under In Re Owens Corning' (2018) 14 Seton Hall Circuit Review 294, 303; Norberg (n 956) 147.

Despite its underlying policy, the first condition may be subject to abuse.[1114] The condition may provide the plan proponent with an incentive to artificially create multiple classes of similar claims to ensure at least one class accepts the plan, thus satisfying the cramdown condition.[1115] As illustrated previously in this chapter, to safeguard against the risk of abuse this condition may bring, the author recommends that Saudi BL 2018 prohibit the separate classification of similar claims except for a legitimate reason independent of the plan proponent's intent to create one assenting class to be eligible for cross-class cramdown provisions.

7.3.5.2 Condition (2): Creditors with 50% in Value or More of All Claims Accept the Plan

This condition in Saudi law does not have an equivalent within the UK and US regimes. The condition requires that the plan be accepted by creditors whose claims represent at least 50% in value of the claims of creditors voting in all classes.[1116] The legislative history of BL 2018 does not explain the purpose for this condition. Moreover, since no equivalent for this condition can be found in the UK and US laws, referring to these two laws does not provide a basis for exploring and discussing the underlying policy of this condition and its utility. Interestingly, such a basis is found in Singapore's restructuring regime, under which a similar condition does exist.

Like the UK and the US, Singapore was one of the jurisdictions that Saudi legislators considered when drafting the provisions of BL 2018.[1117] Singapore's restructuring regime has been subject to wide-ranging reforms recently. The reforms, which have been implemented by Companies (Amendment) Act 2017, include incorporating some features of US Chapter 11 into the local scheme of arrangement.[1118] One of these is the cross-class cramdown feature, which is now possible under Singapore's scheme of arrangement when three conditions are met: (1) the scheme is accepted by at least one class, (2) the scheme is accepted by creditors

[1114] American Bankruptcy Institute (n 559) 260.
[1115] See Hague (n 970); Robin Dicker and Al-Attar (n 484).
[1116] BL 2018, art 80(2)(b).
[1117] Ministiry of Commerce and Industry (n 25) 3.
[1118] See Meng Seng Wee and Hans Tjio, 'Singapore as International Debt Restructuring Center: Aspiration and Challenges' (2021) <https://ssrn.com/abstract=3790235> accessed 19 August 2021; Ken Teo Chuanzhong, 'A Critical Evaluation of the New Cram-down Tool in Singapore's Restructuring Regime' (2021) 30 International Insolvency Review 267; Gerard McCormack and Wai Yee Wan, 'Transplanting Chapter 11 of the US Bankruptcy Code into Singapore's Restructuring and Insolvency Laws: Opportunities and Challenges' (2019) 19 Journal of Corporate Law Studies 69.

representing a majority in number and at least 75% in value of total claims of creditors present and voting in all classes and (3) the court is satisfied that the scheme is 'fair and equitable' to each dissenting class and does not 'discriminate unfairly' between two or more classes of creditors.[1119]

Therefore, in common with Saudi law, as a condition for the cross-class cramdown mechanism, Singapore's law requires that the scheme must be accepted by a certain majority of creditors voting on the scheme, ignoring that they have been placed into different classes. Nevertheless, the threshold required under Singapore's regime is higher than the threshold under Saudi law. While Singapore's law requires the acceptance of at least 75% in value, Saudi law only requires the acceptance of at least 50% in value. Furthermore, in addition to the majority in value, Singapore's law requires that the scheme be accepted by a majority in number of creditors present and voting on the scheme. This additional majority in number is not required under Saudi law.

Due to this condition, cross-class cramdown may be more difficult to accomplish under Saudi law than under the UK and US laws, under which such a condition does not exist. In the Singapore context, abolishing the 75% in value condition was suggested based on the requirement being unnecessary and overly restrictive.[1120] However, Singapore's Ministry of Law defended this requirement, arguing that it 'acts as a safeguard in a cram-down scenario'.[1121]The Ministry stated that the requirement is based on a recommendation made by the Insolvency Law Review Committee (ILRC) after it considered various arguments in favour of and against the introduction of cross-class cramdown provisions.[1122]

While most ILRC members were in favour of introducing such cramdown provisions, a minority of members objected on the grounds that cramming down relies on comparative valuations between rescue and liquidation, which are usually speculative or, in some cases, 'nuanced to make rescue sound more attractive'.[1123] The minority noted that the US has highly developed valuation methods, and its vast and sophisticated economy allows for better

[1119] Companies Act (Singapore) 2017, s 211H (3).
[1120] Ministry of Law, 'Ministry's Response to Feedback from Public Consultation on the Draft Companies (Amendment) Bill 2017 to Strengthen Singapore as an International Centre for Debt Restructuring (the "Draft Bill")' (2017) 18–19.
[1121] ibid 19.
[1122] ibid.
[1123] Ministry of Law, 'Report of the Insolvency Law Review Committee: Final Report' (2013) 155.

comparative analyses because usually other companies can be found in the US that operate in the same field as the distressed company. The same comparative analysis outcome, argued the minority, may not be possible in Singapore, with an economy smaller and less advanced than the US economy.[1124] In other words, the margin of error in the process of comparative valuation, upon which the cross-class cramdown provision relies, is higher in Singapore, which may be prejudiced to the dissenting class of creditors. Therefore, to safeguard against this potential risk and to allow courts to check against abuse of cramdown provisions, the Committee recommended that the threshold to a cross-class cramdown be high.[1125] One way in which this high threshold is implemented is the 75% in value requirement.

The same argument for a high threshold for the cross-class cramdown provision seems applicable in the context of Saudi law. Saudi Arabia's economy is smaller and less advanced than the UK and US economies. Thus, the margin of error in the process of comparative valuation, upon which the cramdown provision relies, is likely to be higher in the Saudi context than in the UK and US. Therefore, to protect the interests of dissenting classes against the risk associated with an inadequate valuation, the additional safeguard represented in the 50% in value requirement seems justified.

7.3.5.3 Condition (3): Plan Is in Best Interest of Majority of Creditors

The final and, arguably, the most important condition that the court must determine before it can confirm a restructuring plan under the FR procedure when one or more creditor class has objected to the plan is that the proposed plan is in the best interest of the majority of creditors.[1126] The courts have almost uniformly considered a comparison of the value of the distribution provided to creditors under the plan with the value of distribution creditors would receive if the plan were not confirmed and the debtor company went into liquidation to determine whether this condition has been met.[1127] If the distribution provided to creditors under the plan is equal to or greater than the distribution they would receive under liquidation, then the court has decided that the confirmation of the plan is in the interest of the majority of creditors. This judicial interpretation appears to align with the principles provided under the Policy Paper of BL 2018, which states that to impose the restructuring plan on dissenting

[1124] ibid 156.
[1125] ibid.
[1126] BL 2018, art 80(2)(b).
[1127] See, eg, case number 4979 (2020); case number 15316 (2021); case number 5208 (2020); case number 7079 (2020).

creditors, 'the court must be satisfied that creditors are no worse off [under restructuring] than in a liquidation'.[1128]

A similar condition exists in the UK law. Section 901G (3) of UK CA 2006 provides that, as a condition for cramming down a Part 26A plan on dissenting classes, the court must be satisfied that, if the plan is sanctioned, no members of the dissenting classes will be any worse off than they would be in the case of a relevant alternative. The 'relevant alternative' in this context is what the court considers most likely to happen to the company if the court does not sanction the plan.[1129] Therefore, this condition is aimed at protecting the interests of dissenting classes by ensuring that creditors will receive at least as much under the plan as they would receive if the plan were not confirmed.[1130] Similarly, dissenting classes are protected under US Chapter 11, section 1129(b)(1) of the US Bankruptcy Code, which states that a reorganisation plan can be crammed down on dissenting classes provided the plan does not discriminate unfairly and is fair and equitable with respect to the dissenting classes.

A critical point about this condition under Saudi law merits highlighting. The language that establishes this condition suggests that the condition concerns not only the interest of dissenting classes but, also, extends to the interest of creditors as a whole. This understanding is supported by judicial practice. The courts have interpreted this condition literally by not allowing the cross-class cramdown unless being satisfied that the majority of creditors, including classes that voted in favour of the plan, are not worse off under the restructuring than under liquidation.[1131]

The wide application of this condition contrasts with the UK and US approaches, under which the equivalents of this condition – section 901G (3) of UK CA 2006 and section 1129(b)(1) of the US Bankruptcy Code – only apply to dissenting classes. Furthermore, the wide application of this condition contrasts with the recommendation provided by the Policy Paper of BL 2018, which states that 'if a class is to be crammed down, it must be on the basis that it is fair to that class'.[1132] Thus, the legislative history of BL 2018 makes clear that this condition was intended to apply only to the dissenting creditors.

[1128] Ministiry of Commerce and Industry (n 25) 8.
[1129] CA 2006, s 901G (4).
[1130] UNCITRAL (n 376) 226.
[1131] See, eg, case number 5208 (2020); case number 7079 (2020).
[1132] Ministiry of Commerce and Industry (n 25) 8.

From the author's perspective, Saudi law should follow the US and the UK in limiting the scope of protection provided by this condition to the dissenting classes because expanding the application of this condition to include classes that have voted in favour of the plan undermines the democratic decision of the majority of creditors in these classes. Moreover, such expansion involves an increase in time and costs for the comparative valuation process, which is the substance of this condition. Such additional time and costs of the comparative valuation process would be avoided if the focus of such valuation is limited to the dissenting classes and does not extend to include accepting classes.

7.4 Conclusion

This chapter discusses the reorganisation plan, which is the central element of the reorganisation procedure. Once agreed upon, the plan's terms act as a blueprint for the debtor's obligations towards its creditors, outlining how much and when the creditors' claims will be paid. The chapter considers a number of essential issues with respect to the restructuring plan under Saudi law, considering the UK and US regimes. The consideration focuses on five key aspects of the restructuring plan: entitlement to vote on the plan, classification of claims, the threshold of creditors' acceptance of the plan, the court's confirmation of the plan and the rules of the cross-class cramdown provision.

In common with US Chapter 11 and the UK scheme of arrangement and Part 26A scheme, the right to vote on restructuring plans under the two Saudi BL 2018 restructuring procedures (FR and PS) is only granted to creditors whose rights are affected by the plan through reduction, deferral, or instalment thereof. The author argues that limiting the right to vote on the reorganisation plan to creditors whose rights are affected by the plan is more appropriate than permitting unaffected creditors to vote and counting their votes when determining whether the required majority has approved the reorganisation plan. Otherwise, the votes of creditors who stand to lose nothing from the plan can swamp the votes of creditors who are significantly disadvantaged by the plan.

The chapter then moves on to consider the issue of the classification of claims. In common with US Chapter 11 and the UK scheme of arrangement and Part 26A scheme, creditors vote on the reorganisation plan under Saudi law as part of a class. However, unlike the case in the

UK and the US regimes, the rules governing classification under Saudi law have not been clearly stated. The absence of adequate rules governing classification under Saudi bankruptcy law makes the manipulation of voting through the gerrymandering of classes easier for plan proponents to accomplish. To prevent the gerrymandering of classes and artificial classifications, the author recommends that the rules governing classification under Saudi BL 2018 be amended. The rules should provide that creditors' claims cannot be placed in the same class unless they are substantially similar and that such similarity be determined mainly by the creditor's priority for payment against the debtor's assets. Moreover, the author recommends that the separate classification of similar claims (underinclusive classification) also be restricted. The separate classification of similar claims should not be permitted except for a legitimate reason independent of the plan proponent's intent to create one assenting class in order to be eligible for cross-class cramdown provisions under the FR procedure.

Regarding the threshold of creditors' acceptance of the plan, class acceptance of the reorganisation plan under Saudi BL 2018 restructuring procedures has been shown to be based only upon the approval of the majority of the creditors in value; the majority in number, or what is referred to as the 'headcount' test, is not required. The author argues that dispensing with this test in Saudi restructuring law seems a proper approach since the test offers small creditors a significant veto power disproportionate to the value of their interest, allowing them to block the restructuring plan accepted by the overwhelming majority of creditors in value. Moreover, the test may be subject to manipulation in the form of debt-splitting.

A court confirmation of a restructuring plan that has been approved by the majority of creditors under any of the BL 2018 restructuring procedures is required in order to make the plan binding. A restructuring plan will be confirmed by the court if it satisfies three requirements stipulated under Article 35 of BL 2018: (1) the creditors' voting procedures are observed, (2) the creditors have obtained sufficient information to review the plan and (3) the creditors' rights are observed. In contrast to the first and second requirements, the third requirement seems ambiguous. While the requirement mandates that the plan must observe the rights of creditors, it does not clarify how such 'observance' is determined. This opens the door for conflicting interpretations of this requirement, which may lead to conflicting judgments. To avoid such undesirable results, the author recommends that this requirement be redrafted using clearer language that specifies exactly the criteria upon which courts can determine whether a plan observes the creditors' rights.

Finally, the chapter considers the rules of the cross-class cramdown mechanism under the FR procedure. Unlike the US and the UK law, as a condition for cramming down a plan on a dissenting class under the Saudi FR procedure, the plan must be accepted by creditors whose claims represent at least 50% in value of the claims of creditors voting in all classes. Due to this 50% condition, cross-class cramdown may be more difficult to accomplish under Saudi law than under the UK and US regimes. Nonetheless, from the author's point of view, the existence of this condition seems justified. Cramming down relies on comparative valuations between the distribution offered to dissenting creditors under the restructuring plan and the distribution they would receive in the event of liquidation; these valuations are highly speculative and involve a broad range of error and uncertainty. Unlike the UK and the US, which have highly developed valuation methods and vast and sophisticated economies that allow for better comparative analyses, Saudi Arabia's economy is smaller and less advanced, so the margin of error in the comparative valuation process upon which cramming down relies is likely to be higher. Therefore, to protect the interests of dissenting classes against the risks associated with inadequate valuations, the additional safeguard represented in the 50% in value requirement seems justified.

The following chapter presents a summary of the thesis's key findings and contains essential recommendations and suggestions to strengthen the efficacy of corporate restructuring procedures in Saudi Arabia.

Chapter 8: Conclusion

This thesis has examined the corporate restructuring regime of Saudi Arabia. Prior to the enactment of the BL 2018, no effective formal restructuring procedure existed in the Kingdom. The only formal rehabilitation regime was PSB 1996. However, that regime was criticised and rarely applied in practice mainly due to its brief content. With the absence of comprehensive formal restructuring procedures, the outcome of restructuring cases relied heavily on the court's discretion, which was highly unpredictable.

The Saudi government has taken a number of initiatives to modernise and reform the laws governing business activities in order to attract foreign investment. The encouragement of foreign investment is considered an essential way to accomplish the ultimate goal of achieving the Kingdom's 2030 Vision, which is to diversify economic sources and reduce the dependence on oil as a main source of income. Perhaps one of the remarkable reforms in the Saudi business law area is the introduction of the first comprehensive bankruptcy law, BL 2018, which was enacted in February 2018. The enactment of BL 2018 was a product of benchmarking conducted by the Saudi Ministry of Commerce and Industry, with many high-ranking insolvency practices, such as in the UK and the US.

BL 2018 provides two restructuring procedures, Preventative Settlement (PS) and Financial Restructuring (FR). This thesis has examined the rules of corporate restructuring under these two procedures with reference to the UK and US's invaluable experiences. The examination focusses on four particular aspects of restructuring procedures: access to restructuring procedures, control of companies during procedures, moratorium against creditors' actions and restructuring plans. The key findings that the thesis has highlighted and the recommendations it has suggested in relation to those four aspects are illustrated below.

8.1 Access to Restructuring Procedures

This research has examined the eligibility criteria and conditions that have to be satisfied for the commencement of the two restructuring procedures provided under Saudi BL 2018 in order to determine whether such criteria facilitate timely access to restructuring procedures, which is crucial for the success of the restructuring process. It has been demonstrated that to access any of the two procedures provided under BL 2018, a debtor company must pass two entry tests: (1) the company is or is likely to become insolvent (insolvency test), and (2) the company's

activities are likely to continue if the restructuring is commenced and the creditors' claims will be settled within a reasonable timeframe (viability test).

When considered in the context of the statutory objectives that BL 2018 reorganisation processes are designed to achieve, the viability test is justified. Because rescuing a company as a going concern is the only objective the BL 2018 restructuring procedures aim to achieve, the viability test functions as a filtering device, preventing non-viable companies, which have no reasonable prospect of continuation, from using the reorganisation procedures to delay their inevitable liquidation.

Unlike the viability test, the insolvency test as an entry requirement for reorganisation procedures under BL 2018 is not justified. The thesis has argued that the imposing of the insolvency test deprives distressed companies of seeking rehabilitation in the early stages of their financial dilemmas, which is critical to the success of the rehabilitation process.

The main argument for imposing actual or impending insolvency as an entry requirement for restructuring procedures is that this would limit the use of restructuring procedures to companies that are in real need of restructuring. It is argued that imposing insolvency as an entry requirement for restructuring procedures is necessary to prevent the abuse of the procedure, whereby such a procedure is utilised not to resolve financial difficulties but to gain a strategic advantage, such as depriving creditors of full payments on their claims.

This justification might be relevant in the context of the UK administration procedure as the minimal court involvement in this procedure makes imposing the insolvency requirement necessary to counter the abuse of the procedures. However, this justification does not seem relevant in the context of the BL 2018 restructuring processes. Unlike the UK administration procedure and similar to the US Chapter 11 procedure, the BL 2018 restructuring processes are court-central and subject to an extensive level of court supervision. The restructuring procedures under BL 2018 can only be commenced by the court's order after a hearing is held to consider the commencement application. This thesis has argued that the high level of court involvement in the commencement of restructuring procedures under BL 2018 provides a sufficient protection against the abuse of such procedures. With the safeguard that court involvement provides against the abuse of such procedures, the intended protective role of insolvency test against the abuse of procedures is superfluous. Therefore, given the similarity

between US Chapter 11 and Saudi restructuring procedures regarding the level of judicial supervision over the restructuring process, and in order to enhance the accessibility of the restructuring procedures, it is recommended to ease the current insolvency threshold in Saudi law and adapt into it a good faith test like that which exists under the US Chapter 11 procedure. Applying this test, the actual or impending insolvency of the debtor is not required for entering the restructuring procedure, but such entering must have a valid reorganisational purpose. The absence of such purpose will justify the court's dismissal of the commencement application on bad faith grounds. In other words, initiating restructuring procedures merely to gain tactical advantages should not be permissible.

8.2 Control of the Company's Business During the Restructuring Process

This research has examined the issue of control over the debtor company's affairs during the reorganisation process under Saudi BL 2018. The administration of a company's affairs throughout the restructuring process is vital since the success of the reorganisation process is strongly dependent on whether such management is conducted appropriately.

There are two prevalent approaches to the management of companies undergoing reorganisation. The first is the debtor-in-possession (DIP) model applied under the US Chapter 11. Under this approach, a company's incumbent management retains control of the company's activities throughout the restructuring process. The second model is practitioner-in-possession (PIP), which is used in the UK administration procedure. Under this model, the control of the company's operations is transferred from the incumbent management to an appointed official practitioner. Between those two models is the modified DIP model, or what is referred to as the co-determination model, which is an attempt to marry the two popular models of reorganisation control. Under the co-determination model, the incumbent management remains in office after the commencement of the restructuring procedure, but its power in managing the company's affairs is restricted and subject to the guidance and supervision of a court-appointed trustee.

Two reorganisation control models are available under Saudi BL 2018. The DIP model is adopted under the PS process, while the FR process adopts the co-determination model. This thesis has argued that the DIP model applied in the PS procedure is unsuitable for the concentrated structure of the Saudi share market, where many larger companies are tightly

controlled by powerful shareholders. Due to the tight relationship between ownership and management in such companies, keeping the pre-petition directors in full control of the company's activities throughout the reorganisation process may raise the danger of the process being manipulated by the dominant shareholders. Furthermore, the PS procedure does not offer creditors protective tools, such as the establishment of a creditors' committee or the opportunity to seek the appointment of a trustee for reason, to mitigate the possibility of shareholder manipulation, which might worsen the issue. This undesirable impact can be avoided by adopting the recommendation made in Chapter 3 of this thesis, which calls for abolishing the PS procedure and retaining its FR counterpart as the only restructuring regime under BL 2018. Indeed, this would be the optimal option, especially since the need for two restructuring procedures that work in parallel and seek to achieve the same goals and apply to the same type of debtors under the umbrella of Saudi BL 2018 has not been clearly justified. Alternatively, amending the present DIP model of control under the PS process and adopting the co-determination model utilised under the FR procedure as its substitute is highly recommended.

The co-determination model is better suited for Saudi Arabia's concentrated ownership market than either the DIP or the PIP model. Like a model that has been adopted in some European countries, such as Germany and France, which, like Saudi Arabia, are characterised as concentrated ownership markets. For the Saudi restructuring regime, the co-determination model offers three key benefits that do not coexist in either the DIP or the PIP model. First, the appointment of an insolvency practitioner protects creditors from the potential risk of bias by the pre-existing management towards the controlling shareholders. This is in contrast to the DIP model, whose present use under the PS process implies a substantial risk of shareholder manipulation.

The co-determination model's second advantage for the Saudi reorganisation system is that it incentivises early filing of the restructuring process. Leaving pre-petition management in charge of the company's daily business activities under the co-determination system while under the supervision of the insolvency practitioner may encourage the company to seek reorganisation in a timely manner. This is in contrast to the PIP approach, in which pre-petition management is displaced once the restructuring proceeding begins. The third advantage of the co-determination approach relates to the reorganisation process's time, cost and efficiency. Allowing the pre-filing management to retain control of the company's daily business activities is likely to expedite the restructuring process and make it more efficient, given the expertise

and familiarity with the company's business that such management has. Additionally, keeping the pre-petition management in charge of the business's daily management activities under the supervision of the insolvency practitioner is far less expensive than removing such management and vesting the insolvency practitioner with complete executive and operational control of the company.

8.3 Moratorium

Chapter 6 examined the application of moratorium under Saudi restructuring law. A moratorium is an essential tool of protection needed throughout a restructuring procedure. It temporarily halts all collection efforts and all proceedings against a debtor company and its assets during the restructuring process. By temporarily barring such actions, the moratorium offers the distressed company time to negotiate with its creditors and develop an appropriate restructuring plan. The moratorium also protects creditors by ensuring that the debtor's estate is administered in an orderly and equitable manner. When examining the application of the moratorium under the Saudi restructuring regime, this thesis has focussed on two primary aspects of the moratorium: its scope and the conditions under which the moratorium may be lifted.

The analysis has shown that, like the UK and US laws, the scope of the moratorium under the Saudi BL 2018 is intended to be comprehensive, covering a variety of actions against a debtor company and its property. Under BL 2018, one of the essential functions of a moratorium is the suspension of secured creditors' rights to enforce their security interests over any bankruptcy assets provided as security interest unless the court consents. This suspension is a fundamental feature of the BL 2018, separating it from the previous restructuring law (PBS 1996), under which the scope of the moratorium was narrow and did not cover the enforcement of security by secured creditors.

This thesis has argued that preventing the enforcement of security interests during a moratorium is crucial to assisting a debtor company's restructuring, particularly where the use of the property subject to security interests is essential for the company to continue operating during the reorganisation process. Allowing the enforcement of security interests over such property after the initiation of the restructuring process may disrupt the business and, as a result, undermine the prospective reorganisation.

Additionally, the research has shown that the moratorium under Saudi law is similar to the moratorium under UK law in that it halts all types of legal or quasi-legal proceedings against a debtor company and its assets. This is in contrast to the US regime, which excludes certain types of proceedings, most notably criminal proceedings and proceedings initiated by governmental units, from the scope of the automatic stay. By excluding these proceedings from the automatic stay, the burden of proof is placed on the debtor to convince the court to stay these proceedings if there is a justification for this stay. However, imposing this burden of proof on a debtor already in financial difficulty may increase its financial encumbrance. For this reason, this thesis argues that the UK approach, which Saudi law adopts on this matter, is more appropriate than the US approach. Under the UK approach, in which no proceeding is exempt from the moratorium's scope, the public prosecutor or governmental unit must convince the court to lift the moratorium, allowing the commencement or continuation of such proceedings, by establishing that lifting the moratorium is necessary to protect public interests. Unlike the distressed debtor, public prosecutors and governmental entities are often financially capable of shouldering the burden of proof required to persuade the court to lift the moratorium.

Another point the research has addressed regarding the scope of the moratorium is the moratorium's impact on claims brought against the guarantors of the debtor company's debts. The moratorium under Saudi law automatically stays these claims. This is distinct from UK law, under which the moratorium has no impact on the actions and proceedings brought against the guarantors of the debtor company. It is also distinct from the US law, under which the automatic stay applies to actions against the guarantors only in limited circumstances.

This thesis recognises that extending the protection of the moratorium to the debtor company's guarantors may be critical to increasing the likelihood of successful restructuring, especially in cases in which the guarantors are the debtor company's insiders, such as shareholders or directors. To effectively formulate and implement the company's reorganisation plan, the company may heavily rely on the expertise of these insiders. Insiders like this could also be potential sources of funding for the reorganisation. If the moratorium does not stay creditors' actions against the guarantors for the company's debts, the guarantors' contributions to the reorganisation process may be hampered. As a result, a successful restructuring may necessitate the protection of the guarantors.

Notwithstanding the benefits that the extension of the moratorium to actions against the guarantors may bring to the reorganisation process, this thesis argues that the automatic application of the moratorium on claims against the debtor's guarantors interferes with the guarantee agreement's very purpose. A primary objective of a guarantee is to assure that upon the principal debtor's default, the guarantor will pay the creditor. This traditional purpose of the guarantee agreement and its value as a form of security is undermined by the automatic application of the moratorium on claims against the debtor's guarantors. Therefore, it is suggested that the moratorium provision in BL 2018 be amended to not automatically apply to actions against the debtor's guarantors. Alternatively, Saudi law should adopt the US approach, in which such actions are only stayed in limited circumstances when the debtor can demonstrate that the enforcement of the guarantee would impair the debtor's restructuring efforts and cause significant losses to the debtor and other creditors, outweighing the potential losses caused to the recipient of the guarantee by enjoining its action against the debtor's guarantor.

In respect to the issue of granting relief from the moratorium, it has been determined that, as in the UK and US laws, under Saudi law, secured creditors may be granted relief from the moratorium to enforce their security interests, provided that such enforcement would not impede the debtor's reorganisation efforts. When it is likely that allowing the enforcement of security interests will obstruct the restructuring process, Saudi law adopts the UK approach of weighing the relief applicant's legitimate interests against those of the debtor and other creditors and deciding whether to grant or deny relief accordingly.

Notwithstanding its adoption of a balance of interests approach similar to that employed in the UK, Saudi law provides no guidelines on the factors that courts should consider when conducting the balance of interests analysis. Hence, it is recommended that BL 2018 or its implementing regulations specify a number of factors that courts must consider when determining whether to grant or deny relief from the moratorium. In establishing such guidelines, the author has suggested that Saudi law could take a page from the UK's book and state that the courts should consider the following factors when conducting the balance of interests analysis required before deciding whether to grant or deny relief from the moratorium: the debtor company's financial situation, its ability to meet its loan obligations, the reorganisation plan, the period for which the moratorium has been in force and its remaining period, the impact of granting the relief on the debtor company and other creditors, the impact

of denying the relief on the relief applicant and the prospect of reorganisation and its progress so far.

This thesis has argued that while the proposed guidelines are not meant to be and should not be regarded as exhaustive, the presence of such guidelines is necessary to assure that certain essential factors are not overlooked by the courts when exercising this discretionary authority. Moreover, the presence of such guidelines would protect against the conflicting judgments and the uncertainty that the lack of guidelines is likely to cause.

8.4 Restructuring Plan

Chapter 7 examined the restructuring plan, which is the central element of the reorganisation procedure. Once agreed upon, the plan's terms operate as a roadmap for the debtor's obligations towards its creditors, stating how much and when the creditors' claims will be paid. When examining the restructuring plan under the Saudi restructuring regime, the thesis has focussed on five core elements of the restructuring plan: right to vote on the plan, classification of claims, the threshold of creditors' acceptance of the plan, the court's confirmation of the plan and the rules of the cross-class cramdown provision.

This research has illustrated that the entitlement to vote on restructuring plans under the two Saudi BL 2018 restructuring procedures (FR and PS), in common with the US Chapter 11 and the UK scheme of arrangement and Part 26A scheme, is only granted to creditors whose rights are affected by the plan through reduction, deferral, or instalment thereof. This thesis has argued that confining the right to vote on the reorganisation plan to creditors whose rights are impacted by the plan is preferable to allowing unaffected creditors to vote and counting their votes when determining whether the requisite majority has accepted the reorganisation plan. Otherwise, the votes of creditors who are significantly disadvantaged by the plan can be swamped by the votes of unaffected creditors who stand to lose nothing from the plan.

In relation to the entitlement to vote on the plan, which is limited to affected creditors, the thesis has considered the plan's impact on secured creditors. The restructuring plan under BL 2018 can affect the rights of secured creditors without their consent if the plan has obtained the requisite approval. This represents a significant feature of the new Saudi reorganisation regime, distinguishing it from the former law under which the rights of secured creditors could not be

affected by the reorganisation plan. This thesis argues that allowing the plan to affect secured creditors' rights may be crucial for the success of the reorganisation process, especially in cases when secured claims represent a significant portion of debts owed by the distressed company. In these cases, modifying the rights of secured creditors and using the encumbered assets may be necessary to facilitate the success of the restructuring process.

With regard to the issue of classification of claims, it has been shown that creditors' votes on the restructuring plan under both Saudi BL 2018 restructuring processes (FR and PS) are conducted by classes of creditors, in common with the US Chapter 11 and the UK scheme of arrangement and Part 26A scheme. Unlike in the UK and the US laws, however, the rules governing classification under Saudi law have not been clearly articulated. While mandating that each class should comprise holders of similar rights, the rules do not clarify the criteria by which this similarity is measured. Thus, plan proponents have an unrestricted amount of freedom to set their own criteria of similarity, based on which the claims of creditors are categorised into different classes.

This thesis has argued that the absence of adequate rules governing classification under Saudi bankruptcy law makes the manipulation of voting through the gerrymandering of classes easier for plan proponents to accomplish. In the PS procedure, under which cross-class cramdown is not possible and the acceptance of all classes is required for the confirmation of restructuring plans, the inadequacy of classification rules allows the debtor to prevent the existence of a dissenting class by placing the claims of the dissenting creditors in one class with the larger claims of consenting creditors, despite the difference in the nature of these claims. Controversially, the absence of criteria against which to measure the similarity of claims in order to classify them has resulted in the common practice of placing secured claims in one class with unsecured claims on the basis that these claims are of one type (for example, trade claims). Similarly, the inadequacy of the classification rules allows the plan proponent to artificially create multiple classes of similar claims to ensure that at least one class accepts the plan, which is a condition for cross-class cramdown under the FR procedure.

Therefore, it is recommended that an amendment to the rules governing classification under Saudi BL 2018 be enacted to prevent these kinds of gerrymandering of classes and artificial classifications. First, the rules should prohibit creditors' claims from being placed in the same class unless they are substantially similar, and the similarity in this context is measured mainly

by the creditor's priority for payment against the debtor's assets. This test would provide minimum protection against the overinclusive classification, through which claims of a different nature (mainly secured and unsecured claims) are grouped together to prevent the existence of a dissenting class, which, when the cross-class cramdown provision is not applicable, can influence the court to deny confirmation of the plan. Second, the separate classification of similar claims (underinclusive classification) should be restricted. Placing similar claims into separate classes should not be permitted without a legitimate rationale for doing so that is unrelated to the plan proponent's intention to construct one assenting class in order to be eligible for cross-class cramdown provisions.

When it comes to the threshold of creditors' acceptance of the plan, it has been shown that class acceptance of the restructuring plan under Saudi law is based only upon the approval of the majority of the creditors in value. The majority in number or the 'headcount' test is not required. The author has argued that the headcount test provides small creditors with substantial veto power that is disproportionate to the value of their interest, enabling them to obstruct the restructuring plan approved by the vast majority of creditors in value. Moreover, the test may be open to manipulation in the form of debt-splitting. Hence, dispensing with this test in Saudi restructuring law is appropriate.

The main argument for the headcount test is that the test protects small creditors by preventing creditors with large claims from imposing their support of the restructuring plan on small creditors against the small creditors' will. However, such an argument is based on the presumption that the holders of small claims are always vulnerable parties in need of protection, which is not always the case. Moreover, even if those creditors need protection, such protection may be accomplished through other methods that do not carry the headcount test's drawbacks. In particular, the treatment of small creditors may be considered by the court when deciding whether to confirm the plan.

Another aspect the thesis has addressed in respect to restructuring plans is the court's confirmation of the plan. It has been illustrated that, similar to the US Chapter 11 and the UK scheme of arrangement and Part 26A scheme, obtaining the approval of the required majority of creditors is not sufficient to make the restructuring plan binding. In order to be binding, the plan must be confirmed by the court. Article 35 of BL 2018 sets out the requirements that have to be satisfied by the plan to obtain the court's confirmation. One of these requirements is that

the creditors' rights have been observed. However, while the requirement stipulates that the plan must observe creditors' rights, it does not specify how such 'observance' is assessed. This may create the possibility of conflicting interpretations of this requirement, which may lead to conflicting judgements. To prevent such unwanted effects, it is recommended that this requirement be rewritten using more precise language that explains explicitly the grounds upon which courts might assess whether a plan observes the creditors' rights.

In addition to the requirements stipulated under Article 35 of BL 2018, the restructuring plan under the PS process must be accepted by all classes of creditors. The cross-class cramdown mechanism is not available under the PS procedure; cramming down a dissenting class is only possible under the FR procedure. The lack of a cross-class cramdown tool in the PS process has been determined to have a negative impact in practice. Unlike the FR procedure, the PS does not entail the appointment of a trustee to supervise the managerial activities of the debtor; as a result, distressed companies usually select the PS procedure over the FR procedure as the first remedy for their financial dilemmas. However, since the PS procedure does not allow for cross-class cramdown, the courts have often terminated the PS procedure upon the failure to obtain the acceptance of all classes and then order the commencement of the FR procedure, under which the cross-class cramdown mechanism is available. This conversion from one restructuring procedure to another involves an increase in the cost and duration of the proceedings, contrary to the objectives of BL 2018 to reduce procedural costs and timeframes. Such unnecessary increases in expenses and time can be avoided if the PS procedure is abolished and the FR is retained as the only restructuring procedure under BL 2018. Otherwise, a cross-class cramdown mechanism should be available within the PS procedure.

The final issue this thesis examined in relation to the restructuring plan is the cross-class cramdown mechanism available under the FR procedure. This mechanism empowers the court to confirm the plan on dissenting classes of creditors. It has been shown that cross-class cramdown may be more difficult to accomplish under Saudi law than under the UK and US regimes. This is due to the fact that, unlike US and UK laws, as a requirement for cramming down a plan on a dissenting class under the Saudi FR procedure, the plan must be accepted by creditors whose claims represent at least 50% in value of the claims of creditors voting in all classes.

This thesis has argued that as cramdown relies on comparative valuations between the distribution offered to dissenting creditors under the restructuring plan and the distribution they would receive in the event of liquidation, and since these valuations are highly speculative and involve a broad range of error and uncertainty, the existence of the 50% value requirement is justified. While the economies of the UK and the US are large and sophisticated, allowing for robust comparative analyses, Saudi Arabia's economy is smaller and less developed, which is likely to result in a wider margin of error in the comparative valuation process on which cramdown is based. As a result, the added protection represented by the 50% value requirement is necessary to protect dissenting classes' interests from the risks associated with insufficient valuations.

Bibliography

AbdulGhani M, *The Foundations of Bankruptcy in Islamic Jurisprudence and Comparative Law* (Egypt Printing Company 1985)

Adli Hammad, 'Insolvency Law in Saudi Arabia' in Donald S Bernstein (ed), *The Insolvency Review* (17th edn, Law Business Research Ltd 2019)

Agnello R and Griffiths B, 'Creditor Schemes of Arrangement and Company Voluntary Arrangements in Recent Debt Restructurings' (2013) 6 Corporate Rescue and Insolvency 1

Al-Ahmad W, *The New Saudi Bankruptcy Law.* (Law and Economics 2019)

Al-Aqili Y, *Explanation of the Provisions of Bankruptcy Law* (1st edn, Dar Al Rawda 2019)

Al-Bassam WM and others, 'Corporate Boards and Ownership Structure as Antecedents of Corporate Governance Disclosure in Saudi Arabian Publicly Listed Corporations' (2018) 57 Business & Society 335

Al-Ghamdi A and Hosseini BY, *Commercial Law* (3rd edn, Al Shegrey 2009)

Al-Ghamdi M and Neufeld PJ, 'Saudi Arabia' in Damian Taylor (ed), *The Dispute Resolution Review* (10th edn, Tom Barnes 2018)

Al-Jaber M, *Saudi Commercial Law* (4th edn, Alshegrey Publisher 1996)

Al-Jarbou AM, 'Judicial Independence: Case Study of Saudi Arabia' (2004) 19 Arab Law Quarterly 5

——, 'The Role of Traditionalists and Modernists on the Development of the Saudi Legal System' (2007) 21 Arab Law Quarterly 191

Al-Sarraf A, ‘Bankruptcy Reform in the Middle East and North Africa: Analyzing the New Bankruptcy Laws in the UAE, Saudi Arabia, Morocco, Egypt, and Bahrain’ (2020) 29 Int Insolv Rev 159

Alarifi F, ‘The Bankruptcy Law of Saudi Arabia: Policy, Operation and Comparison’ (Emerald Publishing Limited 2021) <https://www.emerald.com/insight/content/doi/10.1108/PRR-02-2021-0011/full/html> accessed 3 August 2021

Alces KA, ‘Enforcing Corporate Fiduciary Duties in Bankruptcy’ (2007) 56 U. Kan. L. Rev. 83

‘Allocation of Chambers in Commercial Courts and Courts of Appeal to "Insolvency Cases" - Al Hayat Newspaper’ (28 December 2017) <http://www.alhayat.com/article/906833> accessed 23 January 2019

Almansour A, *Corporate Insolvency* (1st edn, Eshbelia 2012)

——, *Procedures of the New Bankruptcy Law.* (Imam Mohammad Bin Saud Islamic University 2018)

Aloqily A, ‘Bankruptcy Preventive Settlement’ (1984) 8 The journal of law – Kuwait University 1

Alsahlawi AM and Ammer MA, ‘Corporate Governance, Ownership Structure and Stock Market Liquidity in Saudi Arabia: A Conceptual Research Framework’ (2017) 6 Accounting and Finance Research 17

Alshathri A, *Codifying Sharia Law (Arabic)* (1st edn, Dar AlSomeie 2007)

Alshubaiki TA, ‘Developing the Legal Environment for Business in the

Kingdom of Saudi Arabia: Comments and Suggestions' (2013) 27 Arab Law Quarterly 371

Altabtabai M, 'The Implications of Bankruptcy in Islamic Jurisprudence and Law' (Higher Judicial Institute, Imam Mohammad Bin Saud Islamic University 1995)

American Bankruptcy Institute, *Final Report and Recommendations on the Reform of Chapter 11* (American Bankruptcy Institute 2014)

Anderson C and Morrison D, 'The Commencement of the Company Rescue: How and When Does It Start?' in Paul J Omar (ed), *International Insolvency Law: Themes and Perspectives* (Ashgate Publishing Limited 2008)

Anderson JC, 'Classification of Claims and Interests in Reorganization Cases Under the New Bankruptcy Code' (1984) 58 Am. Bankr. LJ 99

Ansary AF, 'A Brief Overview of the Saudi Arabian Legal System' (2020) <https://www.nyulawglobal.org/globalex/Saudi_Arabia1.html> accessed 18 January 2021

Armour J, Cheffins BR and Skeel Jr DA, 'Corporate Ownership Structure and the Evolution of Bankruptcy Law: Lessons from the United Kingdom' (2002) 55 Vand. L. Rev. 1699

Armour J, Hsu A and Walters A, *Report for the Insolvency Service: The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings* (The Insolvency Service 2006)

Armour J and Mokal R, 'Reforming the Governance of Corporate Rescue: The

Enterprise Act 2002' [2005] Lloyd's Maritime and Commercial Law Quarterly 28

Awad A and Michael RE, 'Iflas and Chapter 11: Classical Islamic Law and Modern Bankruptcy' (2010) 44 Int'l Law 975

Ayer JD, Bernstein ML and Friedland J, 'Bad Words to a Debtor's Ear' [2005] Am. Bankr. Inst. J 20

Ayotte KM and Morrison ER, 'Creditor Control and Conflict in Chapter 11' (2009) 1 Journal of Legal Analysis 511

Badawy BA, 'Corporate Bankruptcy Requirements and Impacts : Under the Egyptian Law' (2013) 27 Journal of Sharia and Law 67

Baird DG, 'The Uneasy Case for Corporate Reorganizations' (1986) 15 The Journal of Legal Studies 127

——, *Elements of Bankruptcy* (6th edn, Foundation Press 2014)

BEIS, *Insolvency and Corporate Governance (Government Response)* (2018)

Blair W, 'Classification of Unsecured Claims in Chapter 11 Reorganization' (1984) 58 Am. Bankr. LJ 197

Block-Lieb S, 'Why Creditors File so Few Involuntary Petitions and Why the Number Is Not Too Small' (1991) 57 Brook. L. Rev. 803

Bogart DB, 'Liability of Directors of Chapter 11 Debtors in Possession:" Don't Look Back--Something May Be Gaining On You"' (1994) 68 Am. Bankr. LJ 155

Bork R, *Rescuing Companies in England and Germany* (OUP Oxford 2012)

BPF, ‘Company Voluntary Arrangement (CVA) Briefing’ (2020) <https://bpf.org.uk/media/3474/bpf-cva-briefing-2020.pdf> accessed 5 January 2021

Bradley M and Rosenzweig M, ‘The Untenable Case for Chapter 11’ (1992) 101 Yale L.J. 1043

Broude RF, ‘How the Rescue Culture Came to the United States and the Myths That Surround Chapter 11’ (2000) 16 Tolley’s Insolvency Law and Practice 1

Bussel DJ and Skeel, JR DA, *Bankruptcy* (10th edn, Foundation Press 2015)

Cafritz E and Gillespie J, ‘French Bankruptcy Law Reform Assessed’ (2005) 24 Int’l Fin. L. Rev. 41

Campbell A, ‘Wrongful Trading and Company Rescue’ (1994) 25 Cambrian Law Review 69

Carruthers BG and Halliday TC, *Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States* (Clarendon Press Oxford 1998)

Cheffins BR, ‘Does Law Matter? The Separation of Ownership and Control in the United Kingdom’ (2001) 30 The Journal of Legal Studies 459

Clark DS and Ansay T, *Introduction to the Law of the United States* (2nd edn, Kluwer Law International 2002)

Clifford Chance, ‘The New Saudi Insolvency Law and Its Implementing Regulations’ (2019) <https://www.cliffordchance.com/briefings/2019/07/the_new_saudi_insolvency

lawanditsimplementin.html> accessed 26 August 2019

CLR, *Modern Company Law for a Competitive Economy: Completing the Structure* (2000)

——, *Modern Company Law for a Competitive Economy: Final Report* (2001)

Coffee Jr JC, 'The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control' (2001) 111 Yale Lj 1

Cohn HM, 'Single Asset Chapter 11 Cases' (1990) 26 Tulsa LJ 523

'Commercial Courts Officially Launched - Saudi Gazette' <http://saudigazette.com.sa/article/519454> accessed 23 January 2019

Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York, 'Making the Test for Unfair Discrimination More" Fair": A Proposal' (2002) 58 The Business Lawyer 83

'Companies Explore "Light Touch" Administration in Wake of Debenhams | Financial Times' <https://www.ft.com/content/76c7c985-ff8c-4707-b4e4-28eb7a8f7b62> accessed 29 June 2020

Coogan PF, Broude R and Glatt H, 'Comments on Some Reorganization Provisions of the Pending Bankruptcy Bills' (1975) 30 Bus. Law. 1149

Cork K, *Insolvency Law and Practice: Report of the Review Committee* (HM Stationery Office 1982)

'Corporate Insolvency and Governance Act 2020' <http://www.legislation.gov.uk/ukpga/2020/12/contents/enacted/data.htm> accessed 28 June 2020

Corporations and Markets Advisory Committee, *Rehabilitating Large and Complex Enterprises in Financial Difficulties: Report* (2004)

Cousins SD, 'Chapter 11 Asset Sales' (2002) 27 Del. J. Corp. L. 835

Dario Najm, 'Commentary on the Saudi Arabian Bankruptcy Law' (2018) <https://bsabh.com/commentary-on-the-saudi-arabian-bankruptcy-law/> accessed 23 January 2019

Davis G, 'The Role of the Monitor in a Rescue Moratorium' [2020] South Square Digest 18

Delaney KJ, *Strategic Bankruptcy: How Corporations and Creditors Use Chapter 11 to Their Advantage* (2nd edn, Univ of California Press 1998)

DeMarco Jr RJ, 'Notes: Clean-Up Orders and the Bankruptcy Code: An Exception to the Automatic Stay' (1985) 59 St. John's Law Review 292

Dennis V and Fox A, *The New Law of Insolvency : Insolvency Act 1986 to Enterprise Act 2002* (Law Society 2003)

Department for Business Energy and Industrial Strategy, *Corporate Insolvency and Governance Bill (Explanatory Notes)* (HL 2020)

Dickerson AM, 'The Many Faces of Chapter 11: A Reply to Professor Baird' (2004) 12 Am. Bankr. Inst. L. Rev. 109

——, 'Privatizing Ethics in Corporate Reorganizations' (2008) 93 Minn. L. Rev. 875

'Doing Business' <https://www.doingbusiness.org/> accessed 19 November 2019

‘Doing Business 2017’ <https://www.doingbusiness.org/en/reports/global-reports/doing-business-2017> accessed 19 November 2019

Douglas MG, ‘Unscrambling the Egg or Redividing the Pie: Revoking a Chapter 11 Plan Confirmation Order’ (2006) 2 Pratt’s J. Bankr. L. 333

Edelman J, Meehant H and Cheung G, ‘The Evolution of Bankruptcy and Insolvency Laws and the Case of the Deed of Company Arrangement’ (2019) 4 Lloyd’s Maritime and Commercial Law Quarterly 571

Efrat R, ‘The Evolution of Bankruptcy Stigma’ (2006) 7 Theoretical inquiries in Law 365

Elshurafa D, ‘Insolvency Laws in Saudi Arabia: Time for Change?’ (2012) 9 International Corporate Rescue 300

‘Enter Stage Left: The New “light Touch” Administration - Stevens & Bolton LLP’ <https://www.stevens-bolton.com/site/insights/briefing-notes/enter-stage-left-the-new-light-touch-administration> accessed 29 June 2020

Epstein DG and Nickles SH, *Principles of Bankruptcy Law* (2nd edn, West Academic Publishing 2017)

Eu A, ‘Valuation Issues in the UK Restructuring Plan’ (2021) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3776876> accessed 2 September 2021

Euler Hermes, ‘Collection Profile: Saudia Arabia’ (2017) <https://www.eulerhermes.com/content/dam/onemarketing/ehndbx/eulerhermes_com/en_gl/erd/collection/Saudi_Arabia.pdf> accessed 23 January 2019

Everett J and Watson J, ‘Small Business Failure and External Risk Factors’ (1998) 11 Small Business Economics 371

Fidler P, ‘Wrongful Trading after Continental Assurance’ (2001) 17 IL&P 212

Finch V, ‘Control and Co-Ordination in Corporate Rescue’ (2005) 25 Legal Studies 374

Finch V and Milman D, *Corporate Insolvency Law: Perspectives and Principles* (3rd edn, Cambridge University Press 2017)

Fletcher IF, *The Law of Insolvency* (3rd edn, Sweet and Maxwell 2002)

——, ‘UK Corporate Rescue: Recent Developments–Changes to Administrative Receivership, Administration, and Company Voluntary Arrangements–The Insolvency Act 2000, the White Paper 2001, and the Enterprise Act 2002’ (2004) 5 European Business Organization Law Review (EBOR) 119

Forsythe M, ‘United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.: Undercollateralized Creditors Cry Timber to the Right to Compensation for Interest on the Value of Collateral’ (1989) 20 Pac. LJ 1309

Fridman S, ‘Voluntary Administration: Use and Abuse’ (2003) 15 Bond L. Rev. i

Frisby S, ‘In Search of a Rescue Regime: The Enterprise Act 2002’ (2004) 67 The Modern Law Review 247

——, ‘Not Quite Warp Factor 2 yet? The Enterprise Act and Corporate Insolvency (Pt 1)’ (2007) 22 JIBFL 327

Fuquay ND, ‘Be Careful What You Wish for, You Just Might Get It: The Effect on Chapter 11 Case Length of the New Cap on a Debtor’s Exclusive Period to File a Plan’ (2006) 85 Tex. L. Rev. 431

Gacos AJ, ‘Reconciling the “Per-Plan” Approach to 11 USC § 1129 (a)(10) with Substantive Consolidation Principles Under In Re Owens Corning’ (2018) 14 Seton Hall Circuit Review 294

Gallagher A, Smyth T and Primoff MG, ‘Is the New UK Restructuring Plan a Viable Alternative to Chapter 11?’ (2020) 39 American Bankruptcy Institute Journal 24

Gasir R and Mariam Al-Alami, ‘Saudi Arabia Set to Welcome New Insolvency Law’ [2016] Emerging Markets Restructuring Journal 15

Gerner-Beuerle C and Schillig MA, *Comparative Company Law* (Oxford University Press 2019)

Gilson SC, ‘Management Turnover and Financial Distress’ (1989) 25 Journal of Financial Economics 241

Gilson SC and Vetsuypens MR, ‘Creditor Control in Financially Distessed Firms: Empirical Evidence’ (1994) 72 Wash ULQ 1005

Ginsberg RE and others, *Ginsberg & Martin on Bankruptcy* (5th edn, Wolters Kluwer Law & Business 2018)

Goldberg SR, Danko D and Kessler LL, ‘Ownership Structure, Fraud, and Corporate Governance’ (2016) 27 Journal of Corporate Accounting & Finance 39

Goode RM, *Principles of Corporate Insolvency Law* (4th edn, Sweet & Maxwell 2011)

Goodman R, 'Testing the Boundaries of the Administration Moratorium' (2011) 4 Corporate Rescue and Insolvency 51

Gordon JC, 'Government Guaranties for Corporate Bankruptcies' (2018) 43 Vt. L. Rev. 251

Gross A, 'Saudi Arabia to Introduce Revolutionary New Insolvency Law in 2016 | ESQUIRE Global Crossings' (2015) <https://www.restructuring-globalview.com/2015/12/saudi-arabia-to-introduce-revolutionary-new-insolvency-law-in-2016/> accessed 17 January 2019

Gudgeon M and Joshi S, 'The Restructuring and Workout Environment in Europe' in Ben Larkin (ed), *Restructuring and Workouts: Strategies for Maximising Value* (2nd edn, London : Globe Law and Business 2013)

H S Shaaban, 'Commercial Transactions in the Middle East: What Law Governs' (1999) 31 Law and Policy in International Business 157

Habtoor OS, Hassan WK and Aljaaidi KS, 'The Impact of Corporate Ownership Structure on Corporate Risk Disclosure: Evidence from the Kingdom of Saudi Arabia' (2019) 15 Business and Economic Horizons 325

Hague DR, 'Sare Manipulation: The Hurdles in Single-Asset Real Estate Cases' (2018) 67 Cath UL Rev 280

Hahn D, 'Concentrated Ownership and Control of Corporate Reorganisations' (2004) 4 Journal of Corporate Law Studies 117

Hart A, ‘Not Quite Foucault’s Pendulum: An Analysis of Gruntz and Bankruptcy Court Jurisdiction over the Automatic Stay’ (2001) 37 Tulsa L. Rev. 607

Hayes MJ, ‘Formulating and Confirming a Chapter 11 Plan of Reorganization’ (2000) 2 J. Legal Advoc. & Prac. 5

Heidt KR, ‘The Automatic Stay in Environmental Bankruptcies’ (1993) 67 Am. Bankr. LJ 69

Hejailan T Al, ‘Commercial Insolvency and Bankruptcy Regimes’ in Alem & Associates and Alttayyar Law Firm (eds), *Business Laws of Saudi Arabia* (Thomson 2014)

Hess H, ‘Company Restructuring Pursuant to German Insolvency Law’ (2014) 3 J Civil Legal Sci 170

Heuston AN, ‘Corporate Reorganizations under the Chandler Act’ (1938) 38 Columbia Law Review 1199

Hosni Al-Masry, *Bankruptcy* (Hasan Publisher 1987)

Hutchinson T, ‘Doctrinal Research: Researching the Jury’ in Dawn Watkins and Mandy Burton (eds), *Research methods in law* (Routledge 2013)

Hutchinson T and Duncan N, ‘Defining and Describing What We Do: Doctrinal Legal Research’ (2012) 17 Deakin Law Review 83

Idris M, *Bankruptcy Procedures According to the Saudi Bankruptcy Law and Its Implementing Regulations* (1st edn, Law and Economics 2020)

Inc IBP, *Saudi Arabia Company Laws and Regulations Handbook* (IBP USA

2012)

Insolvency Lawyers' Association, 'Changing the Narrative around Administration' (2020) <https://www.ilauk.com/news-events/news-view/changing-the-narrative-around-administration> accessed 5 June 2020

Insolvency Service, *Company Voluntary Arrangements and Administration Orders: A Consultative Document* (HMSO 1993)

——, *A Review of Company Rescue and Business Reconstruction Mechanisms* (DTI 2000)

——, *A Review of the Corporate Insolvency Framework: A Consultation on Options for Reform* (Insolvency Service 2016)

Jackson TH, *The Logic and Limits of Bankruptcy Law* (Beard Books 2001)

John D. Ayer, Michael Bernstein and Jonathan Friedland, 'An Overview of the Automatic Stay' (2004) 22 The American Bankruptcy Institute Journal 1

Johnson RA and O'Leary MC, 'Automatic Stay Provisions of the Bankruptcy Act of 1978' (1983) 13 NML Rev. 599

Johnson S, '" Equanimity between Creditors "? Spotlight on Saudi Arabian Insolvency Law Reform' (2015) 30 Butterworths Journal of International Banking and Financial Law 626

Kahn-Freund O, 'On Uses and Misuses of Comparative Law' (1974) 37 Mod L Rev 1

Kanda H and Milhaupt CJ, 'Re-Examining Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law' (2003) 51 Am J Comp L 887

Karaman A, *Bankruptcy Preventative Settlement in Saudi Law* (Imam Mohammad Bin Saud Islamic University 2010)

——, *Commercial Papers, Insolvency and Preventative Settlement in Accordance with the Law of the Kingdom of Saudi Arabia (Arabic)* (Al Shegrey 2012)

——, *Commercial Papers and Bankruptcy Procedures* (Dar Alejadh 2019)

Keay A, 'Wrongful Trading and the Liability of Company Directors: A Theoretical Perspective*' (2005) 25 Legal Studies 431

——, 'A Comparative Analysis of Administration Regimes in Australia and the United Kingdom' in Paul J Omar (ed), *International Insolvency Law: Themes and Perspectives* (Ashgate Publishing Limited 2008)

——, 'Wrongful Trading: Problems and Proposals' (2014) 65 N. Ir. Legal Q. 63

Keay A and Murray M, 'Making Company Directors Liable: A Comparative Analysis of Wrongful Trading in the United Kingdom and Insolvent Trading in Australia' (2005) 14 International Insolvency Review 27

Keay AR and Walton P, *Insolvency Law : Corporate and Personal* (4th edn, LexisNexis 2017)

Kilborn JJ, 'A Brief History of U.S. Bankruptcy Law & Policy for Consumers and Businesses' (2008) <https://ssrn.com/abstract=1302388> accessed 26 February 2019

Kloppers P, 'Judicial Management-A Corporate Rescue Mechanism in Need of Reform' (1999) 10 Stellenbosch L. Rev. 417

Lanţoş M, ‘Wrongful Trading in Europe’ (2018) 73 eurofenix 30

Latto P, ‘Saudi Arabia’s Proposed New Insolvency Law and Commercial Pledge Law | Insights | DLA Piper Global Law Firm’ (2016) <https://www.dlapiper.com/en/dubai/insights/publications/2016/03/saudi-arabia-new-insolvency-law/> accessed 23 January 2019

Lawson JJ, ‘Creditors Beware-A Guaranty May Not Be Such a Guarantee’ (1989) 94 Dick L Rev 157

Lepaulle P, ‘The Function of Comparative Law with a Critique of Sociological Jurisprudence’ (1922) 35 Harvard Law Review 838

Leveneur L, ‘Guarantees and Collective Procedures’ in Wolf-Georg Ringe, Louise Gullifer and Philippe Théry (eds), *Current issues in European financial and insolvency law: Perspectives from France and the UK* (Hart Publishing 2009)

Levitin AJ, *Business Bankruptcy: Financial Restructuring and Modern Commercial Markets* (2nd edn, Wolters Kluwer Law & Business 2018)

Lewis PB, ‘Trouble Down Under: Some Thoughts on the Australian-American Corporate Bankruptcy Divide’ (2001) 2001 Utah L. Rev. 189

Lewis PB, ‘Business Insolvency and the Irish Debt Crisis’ (2012) 11 Rich. J. Global L. & Bus. 407

Lijie Q, ‘Managerial Models during the Corporate Reorganization Period and Their Governance Effects: The UK and US Perspective’ (2008) 29 Company Lawyer 131

LoPucki LM, ‘The Debtor in Full Control--Systems Failure under Chapter 11 of the Bankruptcy Code’ (1983) 57 Am. Bankr. LJ 99

——, ‘The Trouble with Chapter 11’ (1993) 1993 Wis. L. Rev. 729

LoPucki LM and Whitford WC, ‘Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies’ (1992) 141 U. Pa. L. Rev. 669

Malekian F, *Principles of Islamic International Criminal Law* (2nd edn, Brill 2011)

Mallon C, Rogan A and Cukier M, ‘Restructuring in England and Wales’ in Christopher Mallon (ed), *Restructuring Review* (11th edn, Law Business Research Ltd, London 2018)

Maloy R, ‘A Primer on Cramdown-How and Why It Works’ (2003) 16 St Thomas L Rev 1

Maren Hanson, ‘The Influence of French Law on the Legal Development of Saudi Arabia’ (1987) 2 Arab Law Quarterly 272

Markell BA, ‘Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification’ (1994) 11 Bankr. Dev. J. 1

——, ‘A New Perspective on Unfair Discrimination in Chapter 11’ (1998) 72 Am. Bankr. LJ 227

Mba SU, *New Financing for Distressed Businesses in the Context of Business Restructuring Law* (Springer 2019)

Mccarthy J, ‘Challenges in Finding the " Right " Approach to SME Rescue :

The Example of Reforms to the Irish Examinership Process' (2019) 32 Insolvency Intelligence 43

McCormack G, 'Control and Corporate Rescue–an Anglo-American Evaluation' (2007) 56 International & Comparative Law Quarterly 515

——, *Corporate Rescue Law--an Anglo-American Perspective* (E Elgar 2008)

——, 'Apples and Oranges? Corporate Rescue and Functional Convergence in the US and UK' (2009) 18 International Insolvency Review: Journal of the International Association of Insolvency Practitioners 109

——, 'World Bank Doing Business Project: Should Insolvency Lawyers Take It Seriously?' (2015) 28 Insolv Intell 119

——, 'Why "Doing Business" with the World Bank May Be Bad for You' (2018) 19 European Business Organization Law Review 649

——, *Permanent Changes to the UK's Corporate Restructuring and Insolvency Laws in the Wake of Covid-19* (Insol-International 2020)

——, *The European Restructuring Directive* (Edward Elgar Publishing Limited 2021)

McCormack G and Wan WY, 'Transplanting Chapter 11 of the US Bankruptcy Code into Singapore's Restructuring and Insolvency Laws: Opportunities and Challenges' (2019) 19 Journal of Corporate Law Studies 69

McKenzie TA, 'Bankruptcy and the Future of Aggregate Litigation: The Past as Prologue?' (2013) 90 Wash. UL Rev. 839

McMillen MJT, 'An Introduction to Shari'ah Considerations in Bankruptcy and

Insolvency Contexts and Islamic Finance's First Bankruptcy (East Cameron)' (2011) <https://ssrn.com/abstract=1826246> accessed 5 January 2019

Milman D, 'Moratoria on Enforcement Rights: Revisiting Corporate Rescue' [2004] Conveyancer Prop Law J 89

——, 'Moratoria in UK Insolvency Law: Policy and Practical Implications' (2012) 317 Co. L.N. 1

Ministiry of Commerce and Industry, *Saudi Insolvency Law Project, Policy Paper* (2015)

Ministry of Law, 'Report of the Insolvency Law Review Committee: Final Report' (2013)

——, 'Ministry's Response To Feedback From Public Consultation On The Draft Companies (Amendment) Bill 2017 To Strengthen Singapore As An International Centre For Debt Restructuring (The "Draft Bill")' (2017)

Mohsen Shafiq, *Eygption Commercial Law* (1st edn, Dar Nashr Althaqafah 1951)

Mojdehi AMM and Gertz JD, 'The Implicit Good Faith Requirement in Chapter 11 Liquidations: A Rule in Search of a Rationale' (2006) 14 Am. Bankr. Inst. L. Rev. 143

Molbert LN, 'Adequate Protection for the Undersecured Creditor in a Chapter 11 Reorganization: Compensation for the Delay in Enforcing Foreclosure Rights' (1984) 60 NDL Rev. 515

Moss G, 'Chapter 11: An English Lawyer's Critique' (1998) 11 Insolvency

Intelligence 17

Murphy JF, ‘The Automatic Stay in Bankruptcy’ (1985) 34 Clev. St. L. Rev. 567

National Bankruptcy Review Commission, *Bankruptcy, the Next Twenty Years* (National Bankruptcy Review Commission 1997)

Nelan BE, ‘Multiple Plans on the Table During the Chapter 11 Exclusivity Period’ (1989) 6 Bankr. Dev. J. 451

Nelson G and Negm M, ‘The New Saudi Arabian Bankruptcy Law’ (2018) 307 Law Update 38

Norberg SF, ‘Classification of Claims Under Chapter 11 of the Bankruptcy Code: The Fallacy of Interest Based Classification’ (1995) 69 Am. Bankr. LJ 119

Nwafor AO, ‘Fraudulent Trading and the Protection of Company Creditors: The Current Trend in Company Legislation and Judicial Attitude’ (2013) 42 Common Law World Review 297

Omar PJ, ‘The Mutual Influence of French and English Commercial Laws in Insolvency’ (2008) 19 International Company and Commercial Law Review 136

Omar PJ and Gant J, ‘Corporate Rescue in the United Kingdom: Past, Present and Future Reforms’ (2016) 24 Insolvency Law Journal 40

Orr KA, ‘Enjoining Foreign Actions Against Non-Debtor Entities: In Re Lyondell Chemical Company’ (2010) 7 International Corporate Rescue 259

Örücü E, *The Enigma of Comparative Law: Variations on a Theme for the Twenty-First Century* (Springer 2013)

Parkinson MM, *Corporate Governance in Transition: Dealing with Financial Distress and Insolvency in UK Companies* (Palgrave Macmillan, Cham 2018)

Parry R, *Corporate Rescue* (Sweet & Maxwell 2008)

——, 'Is UK Insolvency Law Failing Struggling Companies' (2009) 18 Nottingham LJ 42

Paterson S, 'Reflections on English Law Schemes of Arrangement in Distress and Proposals for Reform' (2018) 15 European company and financial law review 472

Payne J, *Schemes of Arrangement: Theory, Structure and Operation* (Cambridge University Press 2014)

——, 'The Role of the Court in Debt Restructuring' (2018) 77 Cambridge Law Journal 124

——, 'Intermediation and Bondholder Schemes of Arrangement' in Jennifer Payne and Louise Gullifer (eds), *Intermediation and Beyond* (Bloomsbury Publishing 2019)

——, 'An Assessment of the UK Restructuring Moratorium' (2021) <https://ssrn.com/abstract=3759730> accessed 2 September 2021

Pejovic C, 'Civil Law and Common Law: Two Different Paths Leading to the Same Goal' (2001) 155 Poredbeno Pomorsko Pravo 7

Petrovski N, 'The Bankruptcy Code, Section 1121: Exclusivity Reloaded'

(2003) 11 Am. Bankr. Inst. L. Rev. 451

Phillips M, Willson W and Johnson C, 'Corporate Insolvency and Governance Act 2020 A Breath of Fresh Air' [2020] South Square Digest 5

Piesse J, Strange R and Toonsi F, 'Is There a Distinctive MENA Model of Corporate Governance?' (2012) 16 Journal of Management & Governance 645

Polivy DR, 'Unfair Discrimination in Chapter 11: A Comprehensive Compilation of Current Case Law' (1998) 72 Am. Bankr. LJ 191

Rajak H, *Company Rescue and Liquidation* (3rd edn, Sweet & Maxwell 2013)

Rawis K Al, 'The Concept of Bankruptcy in Saudi Commercial Law' (2012) 1 Journal of Legal and Economic Research 207

Robert L. Ordin and Sally McDonald Henry, *Ordin on Contesting Confirmation* (7th edn, Wolters Kluwer 2020)

Robin Dicker and Al-Attar A, 'Cross-Class Cram Downs Under Part 26A Companies Act 2006, Corporate Insolvency and Governance Act 2020, Schedule 9' [2020] South Square Digest

Rose-Ackerman S, 'Risk Taking and Ruin: Bankruptcy and Investment Choice' (1991) 20 The Journal of Legal Studies 277

Ross T and Adams C, 'Legal and Practical Issues for Restructuring and Insolvency in the UAE' (2010) First Quar The Quarterly Journal of INSOL International 15

Rusch LJ, 'Gerrymandering The Classification Issue in Chapter Eleven Reorganizations' (1992) 63 U. Colo. L. Rev. 163

Saada YA, ‘Bankruptcy’ (Al Azhar University 1985)

Sabeel S, ‘The Implications of Declaring Bankruptcy in Islamic Jurisprudence and Law.’ (Al Neelain University 2017)

Salama Z, ‘Exceeding the Assets of the Debtor as a Condition to Declare Bankruptcy’ (1993) 77 Public Administration Journal 77

——, ‘Bankruptcy Preventative Settlement in Saudi Law’ (1997) 36 Public Administration Journal 347

Saleh N, ‘The Law Governing Contracts in Arabia’ (1989) 38 International and Comparative Law Quarterly 761

‘Saudi Arabia: CLDP Partners with Saudi Bankruptcy Commission in First Bankruptcy Conference | Commercial Law Development Program’ <https://cldp.doc.gov/programs/cldp-in-action/saudi-arabia-cldp-partners-saudi-bankruptcy-commission-in-first-bankruptcy> accessed 18 December 2021

‘Saudi Arabia Vision 2030 Homepage - Vision 2030’ <https://www.vision2030.gov.sa/> accessed 12 September 2021

‘Saudi Bankruptcy Law to Aid Struggling Businesses’ <https://www.thenationalnews.com/business/economy/saudi-bankruptcy-law-to-aid-struggling-businesses-1.761538> accessed 12 September 2021

Saunderson E, ‘The CIGA Moratorium: A Lifeline for UK Companies?’ (2020) 17 International Corporate Rescue 342

Schlesinger RB, ‘The Uniform Commercial Code in the Light of Comparative Law’ (1959) 1 Inter-American Law Review 11

Schwehr B, ‘Corporate Rehabilitation Proceedings in the United States and Germany’ (2003) 12 International Insolvency Review 11

Sfeir GN, ‘The Saudi Approach to Law Reform’ (1988) 36 The American Journal of Comparative Law 729

Sgard J, ‘Do Legal Origins Matter? The Case of Bankruptcy Laws in Europe 1808-1914’ (2006) 10 European Review of Economic History 389

Shabaily YA-, ‘Corporate Insolvency in Islamic Jurisprudence and Law.’ (2009) 7 Center for Research and Islamic Studies, Cairo University 303

Sheffner DJ, ‘Situating Reimposition of the Automatic Stay Within the Federal Common Law of Bankruptcy’ (2015) 47 U. Tol. L. Rev. 447

Siddiqui SMH, ‘Insolvency in Shari’ah and Law: A Comparative Study’ in Tarek M Hajjiri and Adrian Cohen (eds), *Global Insolvency and Bankruptcy Practice for Sustainable Economic Development* (Palgrave Macmillan, London 2016)

Sidle P, ‘The New Standalone Moratorium Procedure under CIGA 2020’ [2020] Corporate Rescue and Insolvency 119

Siems M, *Comparative Law* (2nd edn, Cambridge University Press 2018)

Silverman ST, ‘The Administrative Freeze and the Automatic Stay: A New Perspective’ (1994) 72 Wash. ULQ 441

Skeel Jr DA, ‘Markets, Courts, and the Brave New World of Bankruptcy Theory’ (1993) 1993 Wis. L. Rev. 465

Smith A and Neill M, ‘The Insolvency Act 2000’ (2001) 17 Tolley’s Insolvency

Law and Practice 84

Smits JM, *The Mind and Method of the Legal Academic* (Edward Elgar Publishing 2012)

Stromes DP, 'The Extraterritorial Reach of the Bankruptcy Code's Automatic Stay: Theory vs. Practice' (2007) 33 Brook. J. Int'l L. 277

Suliman I, *Commercial Papers and Bankruptcy* (Dar Alejadh 2019)

Szekely A, Richardson F and Gallagher A, 'Chapter 11 : One Size Fits All ?' (2008) 23 Journal of International Banking and Financial Law 1

Tabb CJ, 'The Future of Chapter 11' (1992) 44 SC L Rev 791

Tabb CJ, 'The History of the Bankruptcy Laws in the United States' (1995) 3 Am. Bankr. Inst. L. Rev. 5

——, *Law of Bankruptcy* (4th edn, West Academic Publishing 2016)

Tabb CJ and Brubaker R, *Bankruptcy Law: Principles, Policies, and Practice* (Fourth Edi, LexisNexis 2015)

Tabb M, 'Competing Policies in Bankruptcy: The Governmental Exception to the Automatic Stay' (1985) 21 Tulsa LJ 183

Teo Chuanzhong K, 'A Critical Evaluation of the New Cram-down Tool in Singapore's Restructuring Regime' (2021) 30 International Insolvency Review 267

'The Abuse of CVAs Must End | EG News' <https://www.egi.co.uk/news/the-abuse-of-cvas-must-end/> accessed 10 April 2021

Thomas B Courtney, *The Law of Companies* (4th edn, Bloomsbury Professional

2016)

Tobar DR, ‘The Need for a Uniform Void Ab Initio Standard for Violations of the Automatic Stay’ (2002) 24 Whittier L. Rev. 3

Tollenaar N, *Pre-Insolvency Proceedings: A Normative Foundation and Framework* (Oxford University Press 2019)

Tolmie FM, *Corporate and Personal Insolvency Law* (2nd edn, Cavendish Pub 2003)

Triantis GG, ‘Theory of the Regulation of Debtor-in-Possession Financing, A’ (1993) 46 Vand L Rev 901

Trower W and others, *Corporate Administrations and Rescue Procedures* (3rd edn, Bloomsbury 2017)

Udofia K, ‘Establishing Corporate Insolvency: The Balance Sheet Insolvency Test’ (2019) <https://papers.ssrn.com/abstract=3355248> accessed 1 October 2021

‘UK’s Light Touch Insolvency Administration Emerges’ <https://www.natlawreview.com/article/covid-19-emergence-light-touch-administration-united-kingdom> accessed 29 June 2020

Umfreville C and others, ‘Recognition of UK Insolvency Proceedings Post-Brexit: The Impact of a “No Deal” Scenario’ (2018) 27 Int Insolv Rev 422

UNCITRAL, *Legislative Guide on Insolvency Law* (United Nations 2005)

United Nations Conference on Trade and Development, *World Investment Report. 2009, Transnational Corporations, Agricultural Production and*

Development. (United Nations 2009)

——, *World Investment Report. 2018, Investment and New Industrial Policies* (United Nations 2018)

——, *World Investment Report. 2019, Special Economic Zones* (United Nations 2019)

US-Saudi Arabian Business Council, 'Saudi Arabia's New Bankruptcy Law' (2018) <https://ussaudi.org/wp-content/uploads/2019/09/November-2018.pdf> accessed 19 November 2019

Venter P and Sprayregen J, 'Bankruptcy Reform in Saudi Arabia' (2016) 34 Law Journal Newsletters 2

Vogel FE, 'Islamic Governance in the Gulf: A Framework for Analysis, Comparison and Prediction' in Gary G Sick and Lawrence G Potter (eds), *The Persian Gulf at the Millenium. Essays in Politics, Economy, Security, and Religion* (Macmillan 1997)

——, *Islamic Law and Legal System : Studies of Saudi Arabia* (Brill 2000)

Walters A and Frisby S, *Preliminary Report to the UK Insolvency Service into Outcomes in Company Voluntary Arrangements* (London : Insolvency Service 2011)

Walton P, Umfreville C and Jacobs L, 'Company Voluntary Arrangements: Evaluating Success and Failure' (R3 (Association of Business Recovery Professionals) 2018)

Warren DJ, 'Relief from the Automatic Stay: Section 362(D)' (1986) 3 Bankr

Dev J 199

Warren E, ‘The Untenable Case for Repeal of Chapter 11’ (1992) 102 The Yale Law Journal 437

——, ‘Bankruptcy Policymaking in an Imperfect World’ (1993) 92 Michigan Law Review 336

——, *Chapter 11: Reorganizing American Businesses: Essentials* (Aspen Publishers 2008)

Warren E and Westbrook JL, ‘The Success of Chapter 11: A Challenge to the Critics’ (2008) 107 Mich L Rev 603

Watkins L&, ‘Restructuring and Insolvency in the United Arab Emirates’ (2011) <https://www.lw.com/upload/pubContent/_pdf/pub2881_1.pdf> accessed 12 February 2019

Watson A, ‘Legal Transplants and Law Reform’ (1976) 92 Law Q Rev 79

Webber RB, ‘Adequate Protection and the Undersecured Creditor: United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.’ (1988) 41 Okla. L. Rev. 637

Weber R, ‘Can the Sauvegarde Reform Save French Bankruptcy Law: A Comparative Look at Chapter 11 and French Bankruptcy Law from an Agency Cost Perspective’ (2005) 27 Mich. J. Int’l L. 257

Wee MS, ‘The Singapore Story of Injecting US Chapter 11 into the Commonwealth Scheme’ (2018) 15 European Company and Financial Law Review 553

Wee MS and Tjio H, ‘Singapore as International Debt Restructuring Center: Aspiration and Challenges’ (2021) <https://ssrn.com/abstract=3790235> accessed 19 August 2021

Wessels B and Madaus S, ‘Restructuring Reform with Pre-Insolvency Proceedings – Where Is the EU Heading To?’ in Jennifer Gant (ed), *Harmonisation of European Insolvency Law* (INSOL-Europe 2017)

Westbrook JL, ‘A Comparison of Bankruptcy Reorganisation in the US with Administration Procedure in the UK’ (1990) 6 IL&P 86

Westbrook JL, *A Global View of Business Insolvency Systems* (Martinus Nijhoff Publishers 2010)

White III CJ and Theus Jr WW, ‘Chapter 11 Trustees and Examiners After BAPCPA’ (2006) 80 Am. Bankr. LJ 289

White JJ, ‘Harvey’s Silence (Symposium: Letters to the Commission)’ (1995) 69 Am. Bankr. LJ 467

Whitford WC, ‘What’s Right About Chapter 11’ (1994) 72 Wash. ULQ 1379

Williams JF, ‘Application of the Cash Collateral Paradigm to the Preservation of the Right to Setoff in Bankruptcy’ (1990) 7 Bankr. Dev. J. 27

World Bank, ‘Resolving Insolvency - Doing Business - World Bank Group’ <http://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency> accessed 19 March 2019

——, ‘Survey on Insolvency Systems in the Middle East and North Africa’ (2009) <https://bit.ly/31coiQM> accessed 23 January 2019

‘World Bank Group to Discontinue Doing Business Report ’ <https://www.worldbank.org/en/news/statement/2021/09/16/world-bank-group-to-discontinue-doing-business-report> accessed 10 December 2021

Yahya S, *Al Wajiz in Saudi Commercial Law (Arabic)* (Arab Modern Office 2015)

Zaretsky BL, ‘Co-Debtor Stays in Chapter 11 Bankruptcy’ (1987) 73 Cornell L. Rev. 213

Zhang Z, ‘Commencement of Corporate Reorganisations in China from an Anglo-American Perspective’, *Insights from theory into restructuring and phoenixing activity* (INSOL International Academics’ Colloquium 2016)

Ziad Diab, *Corporate Insolvency in Islamic Jurisprudence and Comparative Law* (Dar Alnafaies 2011)