

THE NEW SAUDI INSOLVENCY LAW AND ITS IMPLEMENTING REGULATIONS

INTRODUCTION

The New Saudi Insolvency Law represents a significant step towards the achievement of Saudi Arabia's Vision 2030 and to improve the position of Saudi Arabia in the World Bank's Ease of Doing Business rankings. It seeks to deliver a law which is modern in its approach, comprehensive in its scope, and transparent, predictable, and efficient in its intended operation. The reforms focus on ensuring an efficient management of a debtor's estate, including the preservation of enterprise value where possible, and the maximisation of realisable value and redeployment of capital where necessary. In this briefing we summarise the New Saudi Insolvency Law and the impact it is likely to have in the region, not simply in dealing with distress but improving access to finance by ensuring more viable businesses are rescued and facilitating growth and sustainability in the overall economy.

WHEN?

The New Saudi Insolvency Law (Royal Decree M 50 of 1439, Resolution No 264 on 1439) was published in the Saudi Official Gazette Issue 4712 in February. The implementing legislation was enacted on 4 September 2018.

WHAT DOES IT SEEK TO ACHIEVE?

The primary objective of the New Saudi Insolvency Law is to encourage economic activity and is part of Saudi Arabia's Vision 2030 to promote international investment by making the Saudi economy investor friendly. We consider below some of the key aspects of the different procedures. Each procedure requires an application to be made at court, with prescribed information to be filed and the satisfaction of certain conditions. The New Saudi Insolvency Law promotes restructuring over liquidation and includes the ability to appoint officeholders to rehabilitate debtors, and where this is not possible, manage the liquidation process. This is with the aim of making the processes more efficient, but at the same time ensuring that they are fair and

Key issues

- Introduction of insolvency officeholders and less court involvement
- Promotion of a debtor in possession process
- Insolvency officeholder driven Rehabilitation
- Introduction of stay, rescue finance, cram down and restrictions on ipso facto provisions
- Liquidation procedures officeholder driven
- Simplified procedures for small debtors
- Ability to challenge unusual transactions and ability to hold management responsible for failure
- Financial market arrangements to be protected from the effects of procedures – with rules to follow
- Introduction of a Bankruptcy Commission

carried out with the interests of stakeholders in mind. A new Bankruptcy Commission has been formed under the New Saudi Insolvency Law which will perform several roles including: designating professional bodies to regulate and supervise officeholders; setting rates for remuneration; and being the liquidator of last resort.

WHO WILL IT APPLY TO?

The New Saudi Insolvency Law is to be generally available to private individuals who are involved in business and companies. In terms of jurisdictional scope, it applies to Saudi persons or foreign residents practicing commercial or professional activities, or any activity to realize profits in the Kingdom; Saudi registered companies; and Saudi branches of foreign companies. It applies to regulated entities such as banks, insurance companies, companies operating in the exploration of energy and resources, companies engaged in health care services, and educational services. In such cases the relevant regulator's consent is required before commencement. The legislation also envisages that over time subordinate legislation may be made to cater for the special characteristics of such entities.

NEW PROCEDURES UNDER THE NEW SAUDI INSOLVENCY LAW

The New Saudi Insolvency Law introduces a range of restructuring and liquidation procedures: Protective Settlement; Financial Restructuring; Liquidation; Small debtor's procedures and Administrative Liquidation.

PROMOTION OF A DEBTOR IN POSSESSION PROCESS: PROTECTIVE SETTLEMENT

This process allows the debtor to remain in possession and manage its own affairs whilst seeking a settlement with its creditors to facilitate business continuation. To commence the process, the debtor must already have formulated the settlement proposal and determined the classification of creditors for the purposes of voting. Once the court opens the process and confirms the classification of creditors in each class, the creditors may vote on the proposal. If two thirds of the creditors vote in favour, the court is then asked to approve the settlement proposal, which once approved by the court, becomes binding on all creditors, even if they did not vote in favour. At the same time as commencing the procedure, the debtor can seek a discretionary stay against litigation and security enforcement. It can also seek to obtain rescue finance in certain circumstances to be approved by the court.

INTRODUCTION OF INSOLVENCY OFFICEHOLDERS AND LESS COURT INVOLVEMENT

The New Saudi Insolvency Law sees the introduction of independent insolvency officeholders in the financial restructuring and liquidation procedures. Officeholders are nominated by the applicant in each of the relevant procedures who are chosen from a defined list published by the Bankruptcy Commission. The Bankruptcy Commission is to compile the defined list of officeholders who have the relevant qualifications, expertise, and experience. The officeholders are to be licensed and regulated by the Bankruptcy Commission. The officeholder is to ensure that stakeholders' interests are protected without the need for too much court involvement. Insolvency officeholders may also seek assistance from a creditors' committee

in carrying out their role; the creditors' committee may act as a useful sounding board for the appointed officeholder. The introduction of officeholders and creditors' committees is with a view to making the procedures under the New Saudi Insolvency Law more cost effective and efficient.

INSOLVENCY OFFICEHOLDER DRIVEN: FINANCIAL RESTRUCTURING

This process (also referred to as rehabilitation) allows a debtor to restructure its business. The process takes place under the supervision of the court and with the assistance of an independent officeholder. There is an automatic stay preventing litigation and security enforcement. As in the Protective Settlement procedure, meetings are convened to vote on a restructuring proposal once the court has approved the proposed classification of creditors. At the meetings, creditors may approve the restructuring by a two thirds majority. Where the majority is not achieved in each class, the Court may still approve the proposal provided at least one class of creditors affected by the proposal has approved it, and the majority creditors in terms of value of the total value of the claims have voted in favour. The proposal must also be considered to meet the requirements of fairness set out in the legislation. The nature of the proposal is not prescribed by the legislation, it can include rescheduling, debt for equity conversions, operational or financial adjustments. Termination provisions in contracts relating to insolvency procedures are also switched off during the process and rescue finance is available.

LIQUIDATION PROCEDURES ARE OFFICEHOLDER DRIVEN

There is a new streamlined liquidation procedure which ensures an efficient realisation of the assets in the estate and distribution to creditors. Debtors, creditors and regulators may initiate the liquidation procedure. For creditor driven applications, a minimum amount of unpaid debt is required, currently set at 50,000 Riyals. The liquidation is overseen by an officeholder who is approved by the debtor from a defined list (licensed and approved by the Bankruptcy Commission). There is very limited court involvement as the liquidator acts impartially in adjudicating claims and making distributions. At the end of the liquidation process, there is a mechanism which provides for the discharge of debts, so that debtors may in certain circumstances start afresh. An administrative liquidation procedure is also introduced to apply to debtors where there is unlikely to be any distribution to creditors. A delegated representative of the Bankruptcy Commission takes on the role of liquidator of last resort, to finalise the business and investigate the affairs of the debtor.

SIMPLIFIED PROCEDURES FOR SMALL DEBTORS

The New Saudi Insolvency Law also introduces modified versions of the main restructuring and liquidation procedures aimed at enabling small debtors to be rescued or liquidated in a cost efficient and time effective manner. The court has limited involvement in these procedures.

ABILITY TO CHALLENGE UNUSUAL TRANSACTIONS AND HOLD MANAGEMENT TO ACCOUNT

Offences concerning misconduct and mismanagement related to insolvency are also introduced by the New Saudi Insolvency Law, including the ability to

be disqualified from acting as a director in future cases. In addition, provisions for challenging prior transactions where there is a lack of consideration or preference to particular creditors also become subject to scrutiny under the New Saudi Insolvency Law.

CROSS BORDER INSOLVENCY PROVISIONS - COMING SOON!

There are provisions contained in the New Saudi Insolvency Law and Implementing Regulations aimed at promoting cross border co-operation, although the detailed rules on those aspects are not included in the Implementing Regulations. Instead, they are to follow in separate rules, but the legislation lays the foundations for such provisions.

INTRODUCTION OF A BANKRUPTCY REGISTER

To promote transparency and confidence in each of the procedures, the New Saudi Insolvency Law introduces a Bankruptcy Register which is accessible online. The purpose of the Bankruptcy Register is to provide information to third parties who may have dealings with or wish to enter into arrangements with distressed debtors. It puts them on notice that the debtor is distressed and the fact that an officeholder may have been appointed. It also alerts third parties to the effects of the procedures e.g. stay and enforcement. The on-line Bankruptcy Register operates in addition to the requirement to provide individual creditor notifications.

INTRODUCTION OF A BANKRUPTCY COMMISSION

As part of the modernised approach, the New Saudi Insolvency Law establishes a Bankruptcy Commission. The Commission has a wide-ranging role aimed at facilitating the practical application of the law. It includes: preparing prescribed application forms and notices for each of the procedures in collaboration with the Ministry of Justice; establishing a Bankruptcy Register; establishing a list of insolvency officeholders; administering the licensing and regulations of those officeholders; administering the Administrative Liquidation procedure and initiating disqualification proceedings in respect of mismanagement and misconduct cases.

SAFEHARBOURS FOR FINANCIAL ARRANGEMENTS - DETAILS OF THE EXEMPTIONS TO FOLLOW IN SEPARATE RULES

In keeping with international bankruptcy practice, it is recognised that to ensure the stability of the financial system, certain financial transactions will need to operate, notwithstanding the commencement of any insolvency procedures. The New Saudi Insolvency Law and Regulations provide for the Saudi Arabian Monetary Authority and the Capital Markets Authority in agreement with the Ministry of Commerce and Investment to determine the scope of arrangements that are protected from the effects of the new law. For example, netting and close out provisions are unlikely to be affected by any of the procedures commenced under the New Saudi Insolvency Law.

CONCLUSION

The success of the New Saudi Insolvency Law will to a large extent be dependent on how it is implemented in practice. The policy underpinning the new approach is very much in keeping with the 2030 vision and complements

the developments taking place generally in the Kingdom. The fact that the New Saudi Insolvency Law has been inspired by international bankruptcy principles, will no doubt go some way to reassure stakeholders in distressed situation and will hopefully encourage new investment from both within and outside of the Kingdom.

AS&H AND CLIFFORD CHANCE'S ROLE

The AS&H and Clifford Chance team led by Dr. Fahad Abuhimed, Khalid Al-Abdulkareem and Adrian Cohen including Saad Al-Dileym, Gabrielle Ruiz and Chris Poel, together with colleagues from offices around the Clifford Chance network of offices, have worked in conjunction with the Saudi Ministry of Commerce and Investment in the development of the law from the policy stage through to its implementation.

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