

THE UAE BANKRUPTCY LAW AND THE AVIATION INDUSTRY

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Watson Farley & Williams has developed the Global Aviation Restructuring Index (“GARI”), an online tool providing a comparative index of 50 restructuring processes in 25+ key aviation jurisdictions. GARI also assigns ‘debtor and creditor friendliness’ scores to each restructuring procedure, allowing for easy comparison across different procedures in the same or multiple jurisdictions. Please [click here](#) to access GARI.

The United Arab Emirates (“UAE”) is not included in GARI as yet, as its bankruptcy law is relatively recent. Its applicability to the aviation industry remains completely untested (UAE-based airlines having historically not been subject to any restructuring proceedings) and local airlines may not even fall under the law’s ambit. It is therefore unclear how, an airline might be restructured in the UAE, making it difficult to assign the GARI scoring system to the jurisdiction.

In line with GARI’s objectives, the following article provides:

1. an overview of the current UAE bankruptcy/restructuring regime;
2. a summary of the regime’s key processes outlined;
3. our view as to its potential applicability to the aviation industry; and
4. considerations regarding the issue of sovereign immunity.

BACKGROUND TO THE BANKRUPTCY LAW

This article is based on our review of both the English and the Arabic texts of UAE Federal Law No. 9 of 2016 on Bankruptcy (as amended) (the “Bankruptcy Law”) and UAE Federal Law No. 21 of 2020 on amending the Bankruptcy Law (the “Amendment Law”), amongst other things. The Arabic text is especially important as it is the versions of decrees/laws in that language that are definitive and binding, having precedent over those in English. Unless otherwise specified, any reference to an “Article” is to one in the Bankruptcy Law or Amendment Law (as applicable).

The Bankruptcy Law came into force on 29 December 2016, replacing the insolvency regime previously contained in the UAE’s Commercial Code (Federal Law No. 18 of 1993), with the aim of streamlining and modernising insolvency processes in the UAE. In general terms, this has been partially achieved.

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SCOPE AND APPLICATION OF THE BANKRUPTCY LAW

Article 2 of the Bankruptcy Law states:

"Article 2

The provisions of this Decree-Law shall be applied on the following:

- 1- The companies subject to the provisions of the Commercial Companies Law.*
- 2- The companies that are not established according to the Commercial Companies Law and owned in whole or in part by the Federal or local government, and of which the legislations of their establishment, their memoranda of association or articles of association stipulate that they shall be subject to the provisions of this Decree-Law.*
- 3- The companies and establishments in the free zones that are not subject to special provisions governing the procedures of preventive composition, restructuring or bankruptcy, taking into account the provisions of Federal Law no. (8) of 2004 on the financial free zones.*
- 4- Any person having the capacity of a merchant according to the provisions of the Law.*
- 5- Licensed civil companies of professional nature."*

APPLICABILITY OF ARTICLE 2 TO UAE AIRLINES

UAE airlines may be subject to the Bankruptcy Law if any aspect of Article 2 apply to them; in practice, this is likely to mean either Article 2(2) or Article 2(4):

- (i) if they made the relevant stipulation to "opt in" to the Bankruptcy Law in their memorandum and articles of association of any other law related to it (under Article 2(2)); or
- (ii) if they could or would be considered a "merchant" (under Article 2(4)), on the basis that airlines function as commercial entities. The Arabic text of the Bankruptcy Law, however, calls into question whether Article 2(4) applies to both corporate entities and individuals or simply the latter.

PROCESSES AND TESTS UNDER THE BANKRUPTCY LAW

The Processes

If the Bankruptcy Law applies, it provides for three processes:

(i) Preventative Composition Procedure (“PCP”) (under Chapter 3 of the Bankruptcy Law): A debtor-led process which aims to rescue struggling businesses by helping them reach a court-supervised settlement with their creditors. Whilst the debtor retains the right to run the business during this process, supervision is provided by a court-appointed trustee.

(ii) Bankruptcy (under Chapter 4 of the Bankruptcy Law), itself is split into two separate processes:

(A) a rescue and rehabilitation process (restructuring): A court-approved restructuring scheme where a debtor is insolvent, but the court determines their business is capable of rescue (for example, when the company’s management has shown willingness to try and recover the business, a return to profitability could be possible within a reasonable amount of time and its assets are sufficient to cover the restructuring); and

(B) a formal liquidation and distribution procedure: If the answer to either of the two Bankruptcy Tests is “yes”, and the relevant debtor has stopped paying debts for 30+ consecutive days *“due to instability of...financial position or debit financial disclosure”* (Article 68(1)), then the latter will be considered insolvent and the Bankruptcy Law places an obligation on them to file for bankruptcy within 30 days under either Bankruptcy Test (in accordance with Article 68). A request for commencement of bankruptcy proceedings under the Bankruptcy Law may be made by (in addition to the debtor itself), a creditor or creditors with a debt of at least AED 100,000 owed to them (subject to certain conditions), any relevant competent supervisory body and the public prosecution of the application would be in the public interest.

Bankruptcy Tests

To ascertain which process applies, the Bankruptcy Law provides for the following two tests (together, the “Bankruptcy Tests”):

(i) Has the company ceased payment of debts due for 30+ successive days?

(ii) Do the company’s assets not cover its liabilities?

The aim of the Bankruptcy Tests is to encourage struggling companies to restructure at an early stage.

Recent amendments to the Bankruptcy Law to address “Emergency Financial Crisis”

It is worth noting that the Amendment Law adds a new chapter to the Bankruptcy Law titled *“Chapter 15 bis – Bankruptcy Procedures during the Emergency Financial Crisis”*. This chapter covers periods of serious financial distress such as the Covid-19 pandemic.

“Emergency Financial Crisis” is defined as *“A general situation that affects trade or investment in the country, such as a pandemic, natural or environmental disaster, war, etc.”*. Although a definition is included within the Amendment Law, it goes on to provide that the UAE Cabinet shall determine when such a situation exists, as well as the period of the same, which would appear to indicate that a UAE Cabinet decision is required before a party can invoke and rely on the provisions of Chapter 15 of the Amendment Law.

A detailed analysis of Chapter 15 bis is beyond the scope of this note.

SOVEREIGN IMMUNITY

We would also like to note that although there is no concept of sovereign immunity under UAE law, Article 247 of the UAE Civil Procedures Code sets out a general prohibition on the enforcement against *“public property owned by the state or any of the Emirates”*. Similarly, Article 106 of the Cabinet Resolution prohibits placing under attachment any public or private property owned by the UAE or one of its Emirates. Waivers of immunity from execution, attachment or other legal process may not be valid and binding under UAE Law and there is a possibility that such waivers may be lawfully revoked. However, a counterparty and its assets (upon being or becoming directly or indirectly owned by the government or a ruler of an Emirate in an official capacity) are likely to be regarded as assets owned by an Emirate for the purposes of UAE Law.

Our experience is that government entities are inclined to take a commercial view on this issue and are therefore unlikely to claim immunity given the potentially damaging economic impact. In fact, it is common practice for government entities to settle disputes as oppose to engage in proceedings that risk reputational damage.

PRACTICAL IMPLICATIONS

From a strictly practical perspective, given the level of government funding available to airlines in the UAE, we believe it highly unlikely any of them will go bankrupt, let alone be forced into bankruptcy proceedings.

As mentioned above, there is a possibility that some of these airlines could argue that, because of the way the Bankruptcy Law is drafted, it does not apply to them.

In any event, many of them are financially backed by the government and would probably get bailed-out regardless, as evidenced most recently by the reported US\$4.8 billion of government aid received by the industry throughout the Middle East in 2020, most (a reported US\$4.1 billion) of which was distributed through direct cash injections, in order to help airlines navigate the heightened financial risks they faced as a result of the wider effect of the Covid-19 pandemic on the aviation industry.

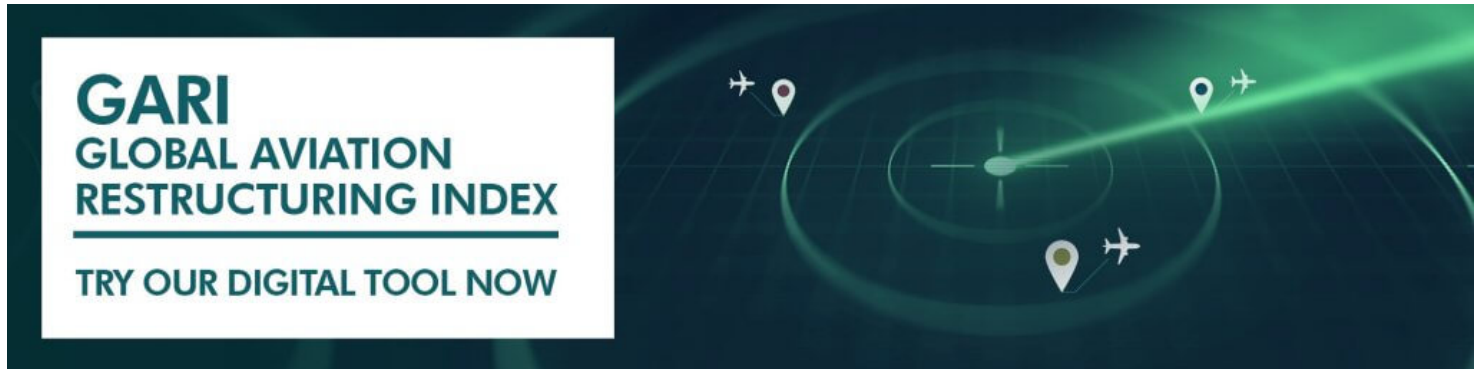
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Even if they were not bailed-out, the government could, in theory, seek to amend the Bankruptcy Law to deal with claims against them favourably. For example, in 2009, the Emirate of Dubai established a tribunal to deal with the settlement of claims against Dubai World and its subsidiaries. Dubai World was able to secure an agreement with its creditors to restructure their debt wherein the funds came from a Dubai government bail-out. There is, however, no formal obligation on the UAE government (nor the government of Dubai) to do this, although it should be noted that the Crown Prince of Dubai announced in March 2020 that the government of Dubai is fully committed to supporting its airlines through the Covid-19 pandemic crisis.

CONCLUSION

Whilst the introduction of the Bankruptcy Law is a long-awaited change to the legal landscape in the UAE, its applicability to airlines in the jurisdiction still remains somewhat unclear and, to date, untested.

Please do not hesitate to contact us if you have any questions regarding the above.



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