

# Saudi Arabia's New Bankruptcy Law: Analysing the First Cases

Saudi Arabia passed a new bankruptcy law last year that incorporated, for the first time in its history, modern alternatives to liquidating businesses. This much-anticipated law was meant to help the country attract foreign investment and support the economy by allowing debtors and creditors to engage in a transparent, predictable and efficient process under the supervision of Saudi's commercial courts. For several years now, judges in these courts have been involved in seminars and training workshops to help prepare them to rule on cases under the new law. An examination of cases decided since the law's enactment reveals the initial impact the law is having and how successful judicial engagement has been.

*L'Arabie saoudite a adopté l'année dernière une nouvelle loi sur la faillite qui contient, pour la première fois de son histoire, des alternatives modernes à la liquidation des entreprises. Cette loi très attendue était censée aider le pays à attirer les investissements étrangers et à soutenir l'économie en permettant aux débiteurs et aux créanciers de s'engager dans un processus transparent, prévisible et efficace sous le contrôle des tribunaux de commerce saoudiens. Depuis plusieurs années, les juges de ces tribunaux participent à des séminaires et à des ateliers de formation afin de se préparer à statuer sur les affaires relevant de la nouvelle loi. L'examen des affaires tranchées depuis l'entrée en vigueur de la loi révèle l'impact initial de la loi et le succès de son engagement judiciaire.*



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1. The views expressed in this article are those of the author and do not necessarily represent the views of, and should not be attributed to, Pillsbury Winthrop Shaw Pittman LLP.

2. The views expressed in this article are those of the author and do not necessarily represent the views of, and should not be attributed, the U.S. Department of Commerce or the Commercial Law Development Program. The authors have worked together on several technical assistance programs with Saudi judges and officials. Much of the information about Saudi's bankruptcy reform efforts is the result of direct knowledge derived from experience in public hearings and conferences and from the cases shared by the Saudi Bankruptcy Commission.

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## Introduction

Between 2015 and 2018, the Commercial Law Development Program (CLDP) of the U.S. Department of Commerce organised a series of bilateral and regional events with US and international bankruptcy experts to provide Saudi judges and officials with legislative solutions to strengthen their draft bankruptcy statutes. CLDP's approach focused on judicial participation during the legislative development stage in order to introduce new concepts to Saudi judges and officials as early as possible and incorporate their feedback in the legislative recommendations, taking into account their unique experience with resolving conflicts between debtors and creditors in the Saudi context. These engagements focused on the importance of expanding debtor eligibility, instituting an automatic stay, allowing for debtor financing, protecting creditor rights and guarantying their inclusion in restructuring procedures, clarifying the prioritisation of creditors, and incorporating cross-border provisions. The U.S. Bankruptcy Code featured prominently in these engagements given its reputation globally as a largely successful restructuring regime. CLDP also relied heavily on experts from and laws (actual and model) of the United Kingdom, Singapore and the United Nations Commission on International Trade Law.<sup>3</sup>

In 2018, after at least three years of consideration and drafting, Saudi Arabia enacted—and its courts began implementing—a new and comprehensive insolvency statute,<sup>4</sup> with accompanying regulations. The statute contains four procedures for administering a debtor's assets and liabilities:

- (1) protective settlement;
- (2) financial restructuring;
- (3) liquidation (by private trustee); and
- (4) administrative liquidation (by the government via the statute-created Bankruptcy Commission).

Separate chapters exist for small debtors under the first three procedures.

Since the law's enactment, various authorities, including the Ministry of Commerce & Investment and the Ministry of Justice, members of the judiciary, and the Bankruptcy Commission, have undertaken substantial efforts to educate the business, legal and other professional communities on the law in order to advance its effective implementation. CLDP has partnered with these entities to organise judicial workshops in Riyadh, at the U.S. Bankruptcy Court in the Southern District of New York, and in Singapore—simultaneously with the International Association of Restructuring, Insolvency & Bankruptcy Professionals (INSOL) Judicial Colloquium—on the role of courts, practitioners, and other constituents involved in restructuring cases.

The Bankruptcy Commission maintains and updates a website (in both Arabic and English), where copies of the statute, regulations, and other materials can be located.<sup>5</sup> The Bankruptcy Commission also provides regular educational announcements on its LinkedIn account, which as of this writing has more than 400 followers. CLDP and the Bankruptcy Commission have also partnered to conduct training, led by the U.S. Trustee Program, of the Commission's members on how to effectively monitor and support bankruptcy cases. And, in April of this year, a two-day lecture-style conference entitled "The First Conference on Resolving Insolvencies," with an estimated attendance of over 800 professionals, was organised in Riyadh by the Saudi Bankruptcy Commission in partnership with domestic and international organisations, including CLDP. In short, substantial efforts have been and continue to be undertaken by the Saudis and their strategic partners to enact and implement its modernised insolvency law.

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## The Law in Practice

Of course, the ultimate measure of the new law's success is whether it is used by the business and legal communities, and whether such usage becomes successful. A first step in this regard is for a debtor to gain access to the process. In contrast to US law, where the insolvency proceeding is opened or commenced automatically and without judicial intervention, Saudi law requires that the court approve the opening of a proceeding based upon a finding that the debtor has satisfied the criteria necessary for the applicable proceeding. Judicial interpretations of these case-opening provisions will be critical to the outcomes, and until now, there has been little indication of how Saudi courts would decide these threshold questions. A review of three memorandum decisions by the Commercial Court in Riyadh—a protective settlement, a reorganisation, and a liquidation—provides some insight into the Saudis' early-stage progress.<sup>6</sup> These decisions, together with other rulings issued by the Commercial Courts, also provide an opportunity to consider ways to help ensure the new law's future success.

In February of this year, the Court heard the case of *Al-Shehili Engineering Industries Co. Ltd.*,<sup>7</sup> where the debtor filed for protective settlement relief and requested the court to issue a moratorium against its creditors.<sup>8</sup> The Court describes the debtor as one of the

3. [https://www.uncitral.org/pdf/english/texts/insolven/05-80722\\_Ebook.pdf](https://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf)

4. A comprehensive analysis of the new Saudi statute and its compliance with U.S. and international best practices was published in an earlier edition of the MENA BLR. Al-Sarraf, Adam, "The Wave of Insolvency Reform Across the MENA Region: Analysing Saudi Arabia's New Bankruptcy Law," Lexis Nexis 2018 Second Quarter #02.

5. The Bankruptcy Commission's website is <https://bankruptcy.gov.sa>

6. Saudi Commercial Courts administering insolvency cases comprise three judges. The decisions summarized here are based upon unofficial translations from Arabic to English.

7. القضية رقم ٦٨٣١ لعام ١٤٤٠ شركة الشهيلي للصناعات الهندسية المحدودة المحكّمة التجارية بالرياض، الدائرة التاسعة

8. In contrast to the US bankruptcy law, where the moratorium (i.e., the "automatic stay") arises automatically upon case commencement, the moratorium under Saudi law arises only upon request and court approval.

leading companies in the Kingdom, with a 40-year old factory that it currently owns. The debtor produces refrigerators, pumps, concrete mixers and other similar products. The Court discusses the company's financial difficulties over the last two years. The Court addresses the financial position of the debtor through a variety of charts that describe its assets, liabilities, expenses, and revenue, as well as changes in equity, all during the 12-month period prior to 31 December 2018. The Court also focuses on the number of employees and their wages (116 employees at SAR 500 000 (approximately USD 133 000) per month), the number of executive bonds issued, and the fact that several creditors have already attempted to enforce their claims against the debtor. Important to the Court was the debtor's representation that it "is in negotiations with military authorities to conclude manufacturing contracts within the next two months," which would presumably enhance revenues. And the "registered trustee" stated that he had reviewed the debtor's settlement proposal and concluded that "we are likely to have the majority of creditors accept the proposal and that the proposal is feasible according to the company's capabilities..."

In light of these factors, the Court held that the proceeding should be opened, and that the moratorium should extend either for the earlier of 90 days and the Court's ratification of the settlement plan. In sum, the Court was sufficiently satisfied that the evidence supported giving the debtor an opportunity to obtain creditor approval of its settlement plan.

*With all this, the debtor was afforded at least the opportunity to save jobs, preserve enterprise value, and continue contributing to the economy.*

In April of this year, the Court heard the case of *Saudi Indian Company for Cooperative Insurance (Wafa Insurance)*<sup>9</sup>, where the debtor sought authority to proceed with a financial restructuring. The Court describes the publicly traded debtor as being in the business of selling health, auto and other insurance products. The Court details the annual cumulative losses from 2011 through 2018 (with the exception of 2016), reprints the debtor's balance sheet (showing modest equity value for the size of the company), and analyses the debtor's cash flow statements, concluding that the debtor was insolvent because it was not paying debts when due. Finding that the debtor's management had proposed a potentially feasible strategy for raising capital (approved by the Saudi Arabian Monetary Authority), and reasoning that:

"one of the objectives of the bankruptcy law is to enable the [debtor] to benefit from bankruptcy procedures, to regulate its financial situation, and to resume its activity and contribute to supporting and developing the economy,"

the Court granted the debtor's request to open the financial restructuring case. It then issued a stay against all actions, appointed an independent financial-restructuring trustee, set a bar date for creditors to file claims, and directed the debtor to submit its proposed restructuring plan within 150 days. With all this, the debtor was afforded at least the opportunity to save jobs, preserve enterprise value, and continue contributing to the economy.

In June of this year, the Court heard the case of *Shalaal Wadi Banna Food Service Establishment*<sup>10</sup>, where the debtor sought authority to liquidate. The decision describes the debtor as being owned by a Yemeni national and having been engaged in the restaurant and food catering business for ten years. The Court recounts that the debtor's expenses exceeded its revenues, liabilities exceeded assets, operations eventually ceased, and more than 23 recovery lawsuits were filed against the debtor. As of June 2019, the debtor's only assets were five vehicles and a modest amount of cash, as compared to alleged debts exceeding SAR 18 million (approximately USD 4.8 million). The Court describes and analyses the debtor's balance sheet and income statements in substantial detail.

In ruling on the application, the Court considered whether the debtor provided requisite notice to creditors of the hearing, concluding that it had. It then analysed and concluded that the debtor had satisfied the law's filing and insolvency requirements for opening a proceeding. However, while the Court found that the debtor should be liquidated, it was unwilling to appoint a private trustee due to the lack of funds to pay the anticipated administrative expenses of the liquidation, and instead ordered administrative liquidation by the Bankruptcy Commission. In doing so, the Court issued a stay of all proceedings against the debtor. Thereafter, the Bankruptcy Commission presumably took control of and sold the debtor's remaining assets, using the proceeds to make at least modest payments to creditors, though there is no efficient way to verify this.

## A Robust Beginning

Saudi Arabia is making demonstrably credible and substantial progress in its goal to successfully implement its new insolvency law. Its Ministries are focused on creating public awareness of law and educating professionals so that clients can effectively avail themselves of the law's benefits. A critical aspect to the success of any insolvency law is transparency. Obtaining access to judicial opinions and being able to evaluate how and why courts are ruling, should result in consistent decisions, thereby leading to greater predictability and confidence in the legal regime. The three cases discussed above appear to prove the commitment of some Saudi judges to these principles.

That said, other cases continue to be ruled upon with little or no analysis, and yet other cases, such as conglomerate *Ahmad Hamad Algosaihi and Brothers (AHAB)*, where the Court refused to open a protective settlement in April and yet weeks later agreed to open a financial restructuring, are difficult to evaluate due to the apparent absence of any publicly available decisions. Moreover, there appears to be no online docketing system whereby the ongoing status of a case, after its opening, can be monitored to determine creditor distribution rates, approved restructuring plans, and overall case success. In fairness, the Saudis have only one year under their belt with a dramatically new and modernised statute. Insolvency is a non-intuitive and difficult area of law. It takes time to figure out what does and does not work for a given business and legal culture. When taken as a whole, together with the demonstrated commitment of all involved, Saudi Arabia's future in this respect seems promising, especially if the efforts by many to be transparent becomes contagious.

9. القضية رقم ٩٧٩٤ لعام ٤٤١ هجرية المقدم من الشركة السعودية الهندية للتأمين (وفا للتأمين). المحكمة التجارية بالرياض، الدائرة التاسعة

10. القضية رقم ٩٩٠٧ لعام ٤٤١ مؤسسة شلال وادي بناء الخدمات الغذائية. المحكمة التجارية بالرياض، الدائرة التاسعة

أصدرت المملكة العربية السعودية قانون إفلاس جديد في العام الماضي ضم للمرة الأولى في تاريخها بدائل حديثة لتصفية الشركات. كان الهدف من إصدار هذا القانون الذي طال انتظاره، مساعدة البلاد على جذب الاستثمارات الأجنبية، ودعم الاقتصاد من خلال السماح للمدينين والدائنين بالمشاركة في عملية شفافة، وقابلة للتنبؤ، وفعالة، تحت إشراف المحاكم التجارية السعودية. ويشارك القضاة، منذ عدة سنوات، في هذه المحاكم عبر حلقات دراسية وورشات عمل تدريبية تهدف إلى المساعدة على تهيئتهم لإصدار الأحكام في القضايا بموجب القانون الجديد. إن تفحص القضايا التي تم البت فيها منذ تبني القانون تكشف عن الواقع الأولي الذي أحدثه القانون ومدى نجاح المشاركة القضائية.

### BIOGRAPHY

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