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Restructuring and insolvency issues: understanding and enhancing your position



Clearly there are some major economic challenges ahead. Many businesses may be able to withstand the challenges ahead but it may very well be that their trading counterparties (whether suppliers, customers or other stakeholders) will not. Whilst these times can represent an opportunity for some, such as potential acquirers (whether of businesses, assets or distressed debt), in most cases, the climate represents a threat to businesses.

Planning now for possible pitfalls and considering how to best protect your position going forwards should assist you: the key to protection will often be forward planning.

In this note we offer some comments about mitigating counterparty risk, as well as some more general points which it would be prudent to consider. Our team has also recently prepared an article focusing on the benefits of the preventive composition under the current bankruptcy regime - please [click here](#) for further information.

General points to consider

- Given the overall landscape many businesses will continue to trade in circumstances in which it is highly questionable as to what the future holds for them and whether they remain viable. Whilst wrongful trading obligations have been temporarily suspended in DIFC, this is not the case in the rest of the UAE. This means that companies will continue to incur liabilities without clear visibility as to whether such liabilities will be met. Hence the importance of the points below about mitigation of counterparty risk.
- Do you need to make adjustments to your own business, either operationally or financially, to protect you against economic threats? Are you facing financial distress, in which case what options should you be considering and are the directors obtaining appropriate advice on their duties?
- Remember that formal insolvency of a counterparty is not necessarily a disaster: it might even represent an opportunity. For example, if any purchaser of the distressed business needs to secure your support, and there is a prohibition on the assignment of your contract without your consent, you may be able to exert influence on the outcome of any sales process.
- Also, you may want to consider taking strategic advantage of a distressed situation with a view to bringing in house a particular stakeholder's business or acquiring a competitor and we have deep experience to help you with this.
- Do you have a refinancing on the horizon? If you are coming up to a refinancing consider whether a degree of financial or operational restructuring might assist you to refinance on better terms.

Mitigation of counterparty risk – some suggestions

- Are you able to identify the warning signs that one of your trading partners is in financial difficulties?
- Are you satisfied that your current trading terms protect you against insolvency risk? Should you tighten up payment terms, take security, request a guarantee from a related company, retain title to any supplies you make, and/or put in place trust arrangements in circumstances where such arrangements are recognised and enforceable?
- Are you confident that your contractual documents adequately protect you in the event of counterparty insolvency? Under the UAE bankruptcy law, the start or implementation of a protective composition or restructuring procedure after a declaration of bankruptcy is not sufficient to automatically cause the termination of an enforceable contract with the debtor, and therefore a party may not rely on an insolvency termination clause to suspend or relief its contractual obligations towards the debtor. Such relief is available to that party if, prior to the date of bankruptcy, protective composition or restructuring, that party invokes a debtor's contractual default. In view of this, are your termination provisions as wide and as flexible as possible?
- It may be possible to use any request for forbearance as an opportunity to improve the contractual position, but ensure that it is properly documented to prevent an argument that the ability to terminate (or other rights) have been waived or affected in some way.
- Termination won't always be the better course. If the counterparty is seeking to trade on out of difficulty and asks stakeholders for support, consider whether the recovery plan is feasible and fair. Can a commercial advantage be extracted? It's important to monitor progress so that you're well placed to react quickly if a recovery begins to appear doubtful.
- Do you have counterparties on which your business relies heavily, and if so have you taken steps to reduce the reliance? In some cases, a lack of alternative arrangements (e.g. to a key supplier) can make choices very limited so contingency planning is advisable.
- Do you have sufficient expertise to be able to negotiate with a counterparty in financial difficulties or an insolvency officeholder? On what terms might you be prepared to support? How do you analyse the merits of any support plan?
- Do you understand the different insolvency regimes and how they might affect your business and limit the exercise of your rights? For example, the court moratorium upon approving or ratifying a protective composition or restructuring procedure prevents unsecured creditor action, but does not prevent secured creditors from executing the securities issued by the debtor in their favour, nor does it prevent you terminating the contract, exerting commercial leverage or exercising rights of set-off.

What we can help with

- Advising all types of stakeholder on strategic options for formulating and implementing domestic and international restructuring solutions, whether implemented consensually, or through a mechanism such as a protective composition or a restructuring scheme.
- Advising all types of stakeholders in connection with corporate distress including options and contingency planning, refinancings, debt for equity swaps, workouts and turnaround strategies.
- Advising corporates, insolvency officeholders and all other types of stakeholders on corporate insolvency regimes, including protective compositions, restructuring schemes and liquidations.
- Advising corporates on issues arising by reason of counterparty distress (whether suppliers, customers or otherwise) and means of mitigating risk.
- Advising directors on their duties, obligations and options, in context of financial distress.
- Advising in connection with distressed investments or acquisitions of assets in distressed situations.
- Litigation: acting for insolvency officeholders and other parties in bringing/defending claims arising out of or in connection with any restructuring or insolvency.

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