



# **INSOL International**

## **The wave of insolvency reform across the region: Analysing the new bankruptcy laws in Morocco and Bahrain**

**JULY 2019**

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## Acknowledgement

With a wave of insolvency reform taking place across the MENA region, INSOL International is delighted to present a technical paper on the recent reforms that have been introduced in Morocco and Bahrain.

The aim of this technical paper is to evaluate whether the new 2018 bankruptcy statutes in Morocco and Bahrain have adequately addressed the main deficiencies of the past laws by measuring the laws' consistency with US and international best practices and identifying remaining deficiencies that could be addressed through implementing regulations, or through capacity-building initiatives. In addition to these crucial elements, there are other significant elements that must be incorporated for the restructuring mechanism to be effective, particularly for small businesses, which are the key drivers of economic growth in the region. This paper includes a discussion of these elements.

INSOL International would like to sincerely thank Adam Al-Sarraf, Attorney Advisor – International, Commercial Law Development Programme, US Department of Commerce, for making this technical paper available to the INSOL International membership. With the dearth of publications dealing with the insolvency laws in the MENA region, this technical paper will no doubt be a welcome addition to our members' libraries.

**July 2019**

## The wave of insolvency reform across the region: Analysing the new bankruptcy laws in Morocco and Bahrain\*

By Adam Al-Sarraf, Attorney Advisor – International, Commercial Law Development Program, US Department of Commerce\*\*

### 1. Introduction and background

Soon after the passage of Saudi Arabia's new bankruptcy code, which I analysed<sup>1</sup> last year, Morocco and Bahrain<sup>2</sup> enacted reforms to their own bankruptcy statutes. Unlike Saudi Arabia, which started from a zero,<sup>3</sup> both Morocco and Bahrain already had consolidated bankruptcy statutes, which were passed in the last 30 years.<sup>4</sup> However, these statutes were overly punitive and lacked the critical elements of a modern insolvency statute needed to effectively balance the interests of debtors and creditors. For example, the previous Bahraini bankruptcy statute, the Bankruptcy and Composition statute,<sup>5</sup> included a corporate reorganisation mechanism known as a "scheme of arrangement", but also blacklisted bankrupt persons from re-entering the marketplace for two years.<sup>6</sup> Morocco's bankruptcy code, which was updated in 1996 as part of a new commercial code,<sup>7</sup> previously included both a restructuring procedure and a preventive procedure. However, creditors were unable to vote on the reorganisation plan under that statute.<sup>8</sup>

The new 2018 Moroccan and Bahraini Bankruptcy statutes set out to address these and other deficiencies in their bankruptcy frameworks to both attract investment and encourage domestic economic growth through innovation and entrepreneurship. In March 2018, the Moroccan Parliament passed an update to Livre V "Book 5", its domestic bankruptcy code, which adds a "rescue" procedure with limited creditor participation while also adding additional creditor participation guarantees in its traditional judicial restructuring process.<sup>9</sup> As a result, Morocco's World Bank Doing Business Report score for "resolving insolvency" improved by more than 50% and its ranking jumped 63 places.<sup>10</sup> During the same period, Bahrain passed a new bankruptcy statute, which according to the Bahraini Economic Development Board "introduces measures to allow company reorganisation where the management is allowed to remain in place and continue business operations during administration, similar to Chapter 11 in the US."<sup>11</sup> The objective of this technical paper is to

\* The author wishes to acknowledge Judge Martin Glenn of the United States Bankruptcy Court for the Southern District of New York (SDNY) for his advice and recommendations during the preparation of this paper.

\*\* 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 US Department of Commerce or the Commercial Law Development Program.

<sup>1</sup> Al-Sarraf, A, "The Wave of Insolvency Reform Across the MENA Region: Analysing Saudi Arabia's New Bankruptcy Law", Lexis Nexis 2018 Second Quarter #02.

<sup>2</sup> <https://www.albawaba.com/business/bahrain-launches-new-bankruptcy-law-keep-investments-flowing-1195184>.

<sup>3</sup> Saudi Arabia received a zero from the Doing Business Report for the strength of its insolvency framework [http://www.doingbusiness.org/en/data/exploreeconomies/saudi-arabia#DB\\_rj](http://www.doingbusiness.org/en/data/exploreeconomies/saudi-arabia#DB_rj).

<sup>4</sup> The Moroccan bankruptcy code was updated in 1996 and the Bahrainis consolidated their bankruptcy provisions in a 1987 statute. Law No 11 Preventive.

<sup>5</sup> Legislative Decree No 11 of 1987 Promulgating the Bankruptcy and Composition Law.

<sup>6</sup> Article 33, (1987): "Any adjudicated bankrupt may not elect or become a member of...the Bahrain Chamber of Commerce and Industry or any professional society. He may not become a manager or a director of any company nor carry on the business of commercial agency or any import or export business..."; art 163: "All of the rights of which the bankrupt has been deprived by Article 33 shall be restored upon the lapse of two years..."

<sup>7</sup> Commercial Laws of Morocco, at p 33. <https://www.ebrd.com/downloads/sector/legal/morocco.pdf>.

<sup>8</sup> *Idem*, at 34.

<sup>9</sup> Dahir No 1/18/26 of the 2 Sha'ban 1439 (19 April 2018), promulgating Law No 73/17 on Insolvent Enterprises amending and completing Law No 15/95 Establishing the Commercial Code, was published in the Arabic-language version of the Official Gazette No 6667 of 23 April 2018.

<sup>10</sup> 2019 World Bank Doing Business Report.

<http://www.doingbusiness.org/content/dam/doingBusiness/country/m/morocco/MAR.pdf>.

<sup>11</sup> "Bahrain Introduces New Bankruptcy Law in Legal Reform Push", Arab News <http://www.arabnews.com/node/1382031/business-economy>.

evaluate whether the new 2018 bankruptcy statutes have adequately addressed the main deficiencies of the past laws by i) measuring the laws' consistency with US and international best practices and ii) identifying remaining deficiencies that could be addressed through implementing regulations, or through capacity-building initiatives. This article will focus on many of the elements that are included in the World Bank's methodology:

- whether debtors can file for bankruptcy without being in default;
- whether there is a prioritisation of creditor classes;
- whether debtors can obtain financing during an insolvency proceeding; and
- whether creditors have a sufficient role in the bankruptcy process.

However, in addition to these crucial elements, there are other significant elements that must be incorporated for the restructuring mechanism to be effective, particularly for small businesses, which are the key drivers of economic growth in the region. These elements include:

- whether a debtor can continue to manage its business;
- Whether there are streamlined provisions for small businesses;
- whether there is an immediate and automatic suspension of claims against the debtor;
- whether there is an independent entity to regulate compliance with the law;
- whether there are strict disclosure requirements; and
- whether debts can be discharged following a restructuring.

## 2. Bankruptcy eligibility

The ability of a debtor to file for bankruptcy without being “balance sheet” insolvent or in default is critical for maximising the benefits of a restructuring mechanism. The importance of this element lies in the nature of creditor rights and specifically the right of a creditor to foreclose on debtor assets, or to repossess its security when companies face temporary cash-flow problems. By enabling debtors to commence insolvency proceedings prior to a default, countries are giving companies the ability to organise their affairs and make the changes needed to pay their debts without being impaired by litigation or the sudden loss of assets or securities.

Prior to the new statute, Moroccan debtors could not file for bankruptcy unless they were in default.<sup>12</sup> However, the new Moroccan Bankruptcy law, the Regulations of Corporation Difficulties 73.17, created a new mechanism called the “rescue procedure”, which only requires that the company be facing “insurmountable difficulties” that could potentially lead to a default.<sup>13</sup> This flexible language is more consistent with US and international best practices, which encourage debtors to access the bankruptcy protections in order to prevent a default. However, the Moroccan law has kept the default requirement for the judicial settlement procedure, which includes greater creditor participation and protections than the rescue procedure.<sup>14</sup> Moreover, the Moroccan law requires that the court determine that the business is not “irrevocably compromised”, in order to start the judicial settlement procedure. The court can decide on its own or based on a motion from the creditors or public prosecutor, to convert the settlement or rescue procedure to a liquidation if such a finding of “irrevocably compromised” is made. This language as written will likely result in funnelling failing companies into the rescue procedure, which may be good for debtors but not creditors. If the courts' implementation of the rescue-procedure does not include

<sup>12</sup> Commercial Laws of Morocco 2013, EBRD - at p 34.

<sup>13</sup> Moroccan Bankruptcy Law, art 561: The Rescue Procedure “may be started upon request of corporation without being in default when it faces insurmountable difficulties which may cause it to default in the short term.”

<sup>14</sup> *Idem*, art 575: Judicial settlement procedures “apply to any corporation proved to be in payment default; art 583: “the court must ascertain that corporation situation is not irrevocably undermined.”

sufficient creditor participation, credit markets and the investment climate will be detrimentally affected.

Similar to the rescue procedure under the Moroccan law, the Bahraini Bankruptcy Law allows for companies to file for bankruptcy protection prior to a default.<sup>15</sup> The previous 1987 Bahrain Bankruptcy and Composition law also required that debtors be in a state of non-payment or default on financial obligations in order to file for either the liquidation or the scheme of arrangement procedures.<sup>16</sup> The new Bahrain Bankruptcy Law also allows the judge to issue a temporary order approving the initiation of bankruptcy proceedings based on a showing that the person meets the basic criteria.<sup>17</sup>

### 3. Debtor-in-possession and creditor committee

One of the most important assumptions of modern insolvency laws, is that businesses are more valuable as going concerns than they are as the sum of their individual components.<sup>18</sup> This does not mean that all failing businesses are capable of being restructured, but rather that by giving companies the time needed to attempt a restructuring process, companies will have a greater chance of maintaining their value for a potential sale or, ideally, to survive the bankruptcy and become profitable. When liquidation is the only option – which has historically been the case in much of the Middle East and North Africa (MENA) region<sup>19</sup> – failing companies that are unable to renegotiate their debts with creditors are auctioned off in pieces, thereby losing any potential value as a going concern. There are two main approaches to the management of a failing business during the restructuring process. The United Kingdom's approach, which is perhaps the most prevalent around the world, involves the appointment of an administrator or a trustee to manage the affairs of the business during the restructuring process.<sup>20</sup> However, the US bankruptcy code makes the appointment of the trustee an exception rather than a rule for reorganisations and creates a creditors' committee<sup>21</sup> to minimise the risk of improper management by the debtor.<sup>22</sup> Despite the differences, both approaches agree that the objective of the entity managing the restructuring is to keep the business operating.<sup>23</sup>

Bahrain's Reorganisation and Bankruptcy Law seems to take the US approach by preserving debtor-in-possession as the default option. Debtors are allowed to remain in possession of the business as long as their activities are in the "ordinary course of

<sup>15</sup> Bahrain Law of Reorganisation and Bankruptcy, art 6(a) (1) "If he failed to cover his debt within thirty days of its due date, or will fail to cover his debt on its due date. 2) Or if his debts owed exceed the value of his assets."

<sup>16</sup> Leonard, B, *Getting the Deal Through, Restructuring and Insolvency 2017*, The International Insolvency Institute, 2017 at 43.

<sup>17</sup> Bahrain Law of Reorganisation and Bankruptcy, art 7(b).

<sup>18</sup> Bracewell & Giuliani, *Chapter 11 of the United States Bankruptcy Code Background and Summary 2012*, at 3, "The general purpose of Chapter 11 is to provide a meaningful opportunity to preserve the debtor's business as a going concern by restructuring its debt and equity interests to better reflect the actual ability of the business to service debt", available at [www.insol.org/files/Fellowship\\_2015/Session\\_3/Chapter\\_11\\_Overview.pdf](http://www.insol.org/files/Fellowship_2015/Session_3/Chapter_11_Overview.pdf).

<sup>19</sup> While Morocco has had a restructuring provision, restructurings are rare and liquidation becomes the primary method of approaching a failing company.

<http://country.eiu.com/article.aspx?articleid=1344074918&Country=Morocco&topic=Economy&subtopic=Forecast&subsubtopic=Policy+trends&u=1&pid=1101794494&oid=1101794494>.

<sup>20</sup> Kelly, S *et al*, "A practical guide to UK insolvency proceedings", [www.squirepattonboggs.com/~media/files/insights/publications/2011/04/a-practical-guide-to-uk-insolvency-proceedings/files/eur6182-girr--squire-sanders/fileattachment/eur6182-girr--squire-sanders.pdf](http://www.squirepattonboggs.com/~media/files/insights/publications/2011/04/a-practical-guide-to-uk-insolvency-proceedings/files/eur6182-girr--squire-sanders/fileattachment/eur6182-girr--squire-sanders.pdf).

<sup>21</sup> Bracewell & Giuliani, *supra* n 18, at 6. At the beginning of a Chapter 11 case, the US Trustee's office will appoint a committee of creditors holding unsecured credit which monitors the debtor's ongoing operations, consults with the debtor and can be "very influential in the case."

<sup>22</sup> Creditors' Committee: A creditors' committee can be an important safeguard to the proper management of the business by the debtor in possession. <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-13-bankruptcy-basics>.

<sup>23</sup> Kelly, S *et al*, *supra* n 20, at 1, "The primary objective of an administration is to rescue the company as a going concern."



business”, unless a court rules otherwise.<sup>24</sup> The law does not include operation of the business as an explicit task of the trustee.<sup>25</sup> Furthermore, the law reiterates the preference for the debtor to remain in possession in both the reorganisation chapter<sup>26</sup> and the “pre-packaged” reorganisation chapter.<sup>27</sup> Importantly, the law creates a creditors’ committee, which is to be constituted at the beginning of a reorganisation procedure, similar to the US system. The creditors’ committee also plays a supervisory role over the debtor while it maintains possession of the business and can even participate in the nomination of a trustee.<sup>28</sup>

Under Morocco’s previous bankruptcy statute, creditors lacked substantial opportunities to participate in the bankruptcy process.<sup>29</sup> However the new Moroccan bankruptcy law, creates a new creditor “association”, which is convened at the outset of every judicial settlement procedure and has significant authority to supervise the debtor.<sup>30</sup> In terms of possession of the business, the new Moroccan bankruptcy law contains two different approaches to the debtor-in-possession question for each of its restructuring provisions, the rescue procedure and the judicial settlement. The “rescue procedure” was designed to enable a business to overcome its difficulties and “guarantee continued operation.”<sup>31</sup> The default structure of the rescue procedure is for the debtor to operate the business under the supervision of the trustee<sup>32</sup> and does not mention any authority of the trustee to manage the business. However, in contrast with the rescue procedure the judicial settlement procedure includes a more empowered role for the trustee. While the procedure allows for the debtor to remain in possession,<sup>33</sup> the provision gives explicit authority to the trustee to assist the debtor with operation or to “fully or partially manage the business on their own.”<sup>34</sup> The law also allows the trustee to manage the debtor’s bank accounts<sup>35</sup> with explicit authority given to the court to determine the exact role of the trustee.

#### 4. Automatic suspension of claims

In order to give the debtor the crucial time needed to develop their plans and negotiate with creditors, an effective restructuring mechanism needs to be supported by a suspension of claims provision. Under the US Bankruptcy Code, the filing of a bankruptcy case by a debtor immediately results in the suspension of claims against it, which is referred to as an “automatic stay”.<sup>36</sup>

<sup>24</sup> Bahrain Reorganisation and Bankruptcy Law, art 11: “Filing lawsuit of bankruptcy or the approval of opening bankruptcy procedures shall not prevent the debtor from managing its business, operating its facilities, using its funds and performing the necessary transactions if they are in line with the ordinary course of business, unless the court otherwise resolves.”

<sup>25</sup> *Idem*, art 40, “Tasks and duties of bankruptcy trustee”.

<sup>26</sup> *Idem*, art.98, “Debtor to remain in possession unless court rules otherwise”.

<sup>27</sup> *Idem*, art 133, “A debtor may continue to operate its business per usual provided that the pre-approved plan does not stipulate otherwise.”

<sup>28</sup> *Idem*, art 33, “The Court shall... appoint a Bankruptcy Trustee or more on the basis of a nomination by the creditor committee or creditors who own at least 10% of the total unsecured debts.”

<sup>29</sup> Commercial Laws of Morocco, EBRD at 34.

<sup>30</sup> Moroccan Bankruptcy Law, art 606, “A creditor association is to be formed when starting judicial settlement procedures...”

<sup>31</sup> *Idem*, art. 560, Rescue procedure.

<sup>32</sup> *Idem*, art 566 (Rescue Procedure): “The head of the corporation is responsible for everyday operations, he is to submit to the authority of the syndic concerning dispositions and implementation of the rescue plan- syndic reports to the acting judge.

<sup>33</sup> *Idem*, art 586 (Judicial Settlement): corporation resumes operation after issuing the ruling to start judicial settlement.

<sup>34</sup> *Idem*, art 588: “only trustee may request implementation of current contracts through offering the service to the contractor by the corporation; Authorities of Trustee - art 592: “to monitor operation, to assist CEO with operation, to fully or partially manage the corporation on their own - court may at ANY time change the trustee’s role upon request or on its own...”

<sup>35</sup> *Idem*, art 593: “trustee may manage corporation bank accounts in the interest of the business.”

<sup>36</sup> Bracewell & Giuliani, *supra* n 18 at 7.

Unlike under the US code, the suspension under the Bahraini Reorganisation and Bankruptcy Law is not automatic. The US bankruptcy code allows the judge to consider lifting the stay<sup>37</sup> in certain circumstances and based on a motion by one of the interested parties; however, neither a motion nor a judicial order are needed for the stay to take legal effect at the outset. By contrast, the Bahraini law gives the judge the discretion to issue the stay.<sup>38</sup> Such discretion, if interpreted inconsistently, could create uncertainty in the process and discourage failing debtors from utilising the bankruptcy process.

The Moroccan Bankruptcy Law adopts the US approach by giving immediate effect to the suspension during the judicial settlement procedure. Unlike the Bahraini Bankruptcy Law, the relevant Moroccan provision does not mention the need for a judicial order.<sup>39</sup> Moreover, the automatic stay provision under the Moroccan law is included within its section on “Common rules of Rescue, Judicial Settlement and Judicial Liquidation Procedures”,<sup>40</sup> therefore the automatic stay applies to all three procedures. Additionally, the Moroccan law allows for the imposition of a stay during out of court conciliation procedures upon the request of either the conciliator or the debtor.<sup>41</sup>

## 5. Debtor financing

The debtor-in-possession and automatic stay protections are often insufficient to keep the business running unless it can access new funds, especially for viable businesses with temporary cash flow problems. The World Bank Doing Business report rewards countries one point for allowing debtors to access credit after commencing bankruptcy procedures and an additional point for assigning priority to such credit.<sup>42</sup> Under Chapter 11 of the US Bankruptcy Code, debtors can obtain unsecured credit during a restructuring and will be given priority above other unsecured credit as an administrative expense.<sup>43</sup>

The Bahrain Reorganisation and Bankruptcy Law has adopted this best practice by not only allowing for debtors to access credit but also by giving priority status to the unsecured credit.<sup>44</sup> Similarly, the Moroccan law has explicitly allowed for debtors to obtain credit during insolvency proceedings and has given priority to such credit, including trade creditors,<sup>45</sup> for both the rescue and judicial settlement procedures.

<sup>37</sup> 11 USC § 362(c).

<sup>38</sup> Bahrain Reorganisation and Bankruptcy Law, art 16: At the judge's discretion, he may order "Temporary Measures" prior to Bankruptcy Approval. These temporary measures could include:

- 1) An art 51 "stay" (وقف) which bars all claims, legal proceedings, asset transfers, including all proceedings to seize, freeze, or in any way control the bankrupt's assets;
- 2) Impose temporary restrictions on the debtor's activities and discretionary powers.

Lifting stay: Creditors' mechanism for lifting the stay to avoid debtors abusing the stay:

- 1) Art 21: The court may impose penalties against anyone who abuses the bankruptcy proceedings based on a motion from any interested party or *sua sponte*;
- 2) Art 53: The Creditors Council may request that the court lift the stay if there has been a violation of the stay.

<sup>39</sup> Moroccan Bankruptcy Law, art 686: "The ruling to launch procedure suspends or bans every law suit filed by the creditors owning debts incurred prior to this ruling and seeking to 1) order the debtor to pay a sum of money or void a contract for not paying a sum of money." At art 687: current lawsuits or suspended until plaintiff creditor admits his debt.

<sup>40</sup> *Idem*, Part Six - Common Rules.

<sup>41</sup> *Idem*, art 555 – Reconciliation - "conciliator or head of company can decide that a temporary stay of procedure can facilitate an agreement with creditors, CJ can suspend claims until agreement is reached..."; art 559: "During implementation of the agreement, every individual procedure or lawsuit is suspended whether related to corporation property or real estate in order to repay the debts stated in the agreement. This agreement also suspends deadlines given to creditors to get their rights."

<sup>42</sup> World Bank - Resolving Insolvency Indicator - Does the insolvency framework provide for the possibility of the debtor obtaining credit after commencement of insolvency proceedings?

<sup>43</sup> Bracewell & Giuliani, *supra* n 18 at 12.

<sup>44</sup> Bahrain Reorganization and Bankruptcy Law, art 79e - Unsecured credit extended to bankrupt or to the bankruptcy administrator has priority status; art 81: "Post-bankruptcy financing receives super priority status."

<sup>45</sup> Moroccan Bankruptcy Law, art 591: "The corporation may receive new funding to continue operating" and arts 565 and 590: "The debts which legally result from starting rescue procedures and corporation operation must be paid on



## 6. Classification and prioritisation of claims

Credit markets rely heavily on the classification and prioritisation of credit, which determine creditor rights. One of the main objectives of an effective insolvency system should be to “recognize existing creditor rights and respect the priority of claims with a predictable and established process.”<sup>46</sup> Without clear statutory guidance on the priority structure of claims, judicial discretion can lead to inconsistent outcomes, which increases the uncertainty and risk in a country’s credit market. Under the US bankruptcy code, creditors, including service providers, governments and lenders, are classified into groups, which receive distributions based on their level of priority under the restructuring plan.<sup>47</sup> The prioritisation is determined in large part based on public policy concerns to ensure that, for example, taxes and domestic support are paid before secured creditors.

One of the key reforms of the new Bahraini Bankruptcy law is the inclusion of detailed guidance on the prioritisation of creditors under the new bankruptcy procedures.<sup>48</sup> Unlike the US bankruptcy code, the Bahraini Bankruptcy Law gives the highest priority to secured creditors even above trade creditors and governments.<sup>49</sup>

However, the Moroccan law does not include such detailed guidance. The Moroccan law refers to mortgages and privileged creditors, particularly in the context of a liquidation, however there is no reference to classification in the context of a rescue procedure or a judicial settlement procedure. As for prioritisation, debtor financing claims are the only ones with clear priority in a rescue procedure or a judicial settlement. However, there is some guidance as to the priority of claims in the context of liquidation distributions.<sup>50</sup> A detailed hierarchy of creditors is needed for the Moroccan bankruptcy system to assure creditors that their rights will be protected in a consistent and predictable manner.

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time within the resolution period. If such debts can’t be paid on time, they receive priority over all other debts even privileged or guaranteed ones...”

<sup>46</sup> Principles for Effective Insolvency and Creditor/Debtor Regimes

<http://pubdocs.worldbank.org/en/919511468425523509/ICR-Principles-Insolvency-Creditor-Debtor-Regimes-2016.pdf>.

<sup>47</sup> 11 US Code, § 507.

<sup>48</sup> New Bankruptcy Law in Bahrain - characterises creditors based upon the nature of their debts and to ensure that minority non-consenting creditors are subject to a cram-down where the two-thirds of the creditors by value agree to the restructuring proposals; <https://www.lexology.com/library/detail.aspx?q=909a5e6d-8693-4757-8794-bd1135da1b2a>.

<sup>49</sup> Bahrain Reorganization and Bankruptcy Law, art 80(b)-(c) specifies the hierarchy of priority status among creditors and the court’s discretion in altering that hierarchy.

Art. 93:

1) After satisfying the debts of secured creditors from the collateral against which their debts were secured, the priority hierarchy proceeds as follows:

- a. Procedural Claims (المتطلبات الإدارية) stipulated in art 78(d) and art 79 receive first priority;
- b. Procedural Claims (المتطلبات الإدارية) stipulated in art 92 receive second priority;
- c. Claims which arose after the filing, including in order or priority:
  - i. Employee compensation up to BHD 3,000;
  - ii. Commercial agents who purchased goods or services from the debtor up to BHD 1,000 per agent;
  - iii. Bahraini government entities owed taxes or fees up to BHD 10,000 per agency;
- d. Unsecured creditors, including the under-secured debt of secured creditors;
- e. Unsecured creditors who filed after the deadline but before the distribution report was finalised;
- f. Foreign government fees and taxes;
- g. Unsecured creditors’ expenses incurred from delay of payment;
- h. Shareholders and interest holders.

<sup>50</sup> Moroccan Bankruptcy Law, art 663: “If prior to division of property price one or more sums are distributed, privileged creditors and mortgage holders receive amounts proportionate to their total debts.”

After selling property and finally deciding upon the priority of creditors holding official mortgages and privileges, those who occupy a suitable status cannot get the sums appropriate to their mortgage priority in distribution from property price except after deduction of sums already paid.

Regular creditors then benefit from the deducted sums.

## 7. Creditor participation – voting rules for reorganisation plan

The approval process for the reorganisation plan is one of the key mechanisms that can be used to ensure creditor participation and the protection of creditor rights. The World Bank rankings reward countries for ensuring that all creditors can participate, that creditors are divided into their specific classes and that creditors are treated equally within each class.<sup>51</sup> Under the previous Moroccan statute, creditors were not given an opportunity to vote on the reorganisation plan in a judicial reorganisation process.<sup>52</sup> Under the US Bankruptcy Code, creditor participation refers only to classes of creditors who are actually affected by the reorganisation plan are allowed to vote on the plan.<sup>53</sup> All classes must approve the plan and for an entire class of claims to have approved, creditors with two-thirds in amount and more than one-half in number of the claims in the class must approve.

The new Bahraini Bankruptcy law follows the US model very closely. All creditor classes must agree on the plan and approval by a class is obtained by a majority of creditors approving in each class, as long as the majority possesses two-thirds of the unsecured debt.<sup>54</sup> Unaffected creditors are not permitted to vote. A creditors' committee is also established for both reorganisation and liquidation procedures and participates in the development of the reorganisation plan.<sup>55</sup>

In stark contrast to both the World Bank guidance and the US Bankruptcy Code, the new Moroccan Bankruptcy law does not allow creditors to vote on the plan under the rescue procedure. The court has exclusive authority to approve the rescue procedure plan based on a finding that there is a "serious possibility to save the corporation", which is determined based on the trustee's report.<sup>56</sup> However, the judicial settlement procedure includes much more robust creditor participation. A creditor "association" is created at the outset of every judicial settlement procedure,<sup>57</sup> with the stated objective of approving the settlement plan<sup>58</sup> among other tasks. The association also includes the trustee and the debtor with voting rights;<sup>59</sup> however, the reorganisation plan cannot be approved without at least half of the debt being represented.<sup>60</sup> The association meetings must be attended by creditors with at least two thirds of the debt in order to have a valid session,<sup>61</sup> although a plan can be approved with only half of the debt. Therefore, the Moroccan judicial settlement procedure provides less protection to creditors' rights than both the US and Bahraini models. The

<sup>51</sup> World Bank Doing Business Report, Resolving Insolvency.

<sup>52</sup> Leonard, B, Getting the Deal Through, *supra* note 16, at p 43.

<sup>53</sup> Bracewell & Giuliani, *supra* note 18, at p 32. 11 USC, § 1126.

<sup>54</sup> Bahrain Reorganization and Bankruptcy Law, art 114: "Only those debtors with an interest in the plan may vote. All creditor classes must agree on the plan in order for it to be approved. Each creditor class shall vote independently and any creditor class that will receive payment in full or any creditor class that is not affected by the plan shall be considered to have voted in favor of the plan. A creditor class votes in favor of a plan when a majority of its creditors agree to the partial or final settlement of their claims, provided that the majority possess two-thirds of the unsecured debt of that creditor class, and that ratio is based on the total debt of the class less any creditors who do not participate in the voting."

<sup>55</sup> *Idem*, art 103 (reorganisation), art 145 (liquidation).

<sup>56</sup> Moroccan Bankruptcy Law, art 570: court decides to approve the plan if it perceives that there are serious possibilities to save the corporation based on the syndic report.

<sup>57</sup> *Idem*, art 606: "A creditor association is to be formed when starting judicial settlement procedures".

<sup>58</sup> *Idem*, art 607: "The association is convened to Draft settlement plan to maintain corporation operation mentioned in article 595 above:

- Draft settlement plan to maintain corporation operation suggested by creditors as stated in paragraph 3 of article 615 below;
- Modify the objectives and methods of the draft settlement plan to maintain corporation operation while applying article 629 below;
- Request to replace the appointed syndic based on article 677 below;
- Selling one or more of the important assets referred to in article 618 below.

<sup>59</sup> *Idem*, art 608.

<sup>60</sup> *Idem*, art 611: "Association decisions are considered valid when approved by present creditors or their agents who own at least half of the certified debts of present creditors or agents who took part in the vote."

<sup>61</sup> *Ibid.*

inclusion of the creditor association is likely to address some of the past concerns of a lack of creditor participation, but the structure of the new Moroccan rescue procedure will prevent this new framework from fully addressing the past concerns of creditors about their participation in the process.

## 8. Disclosure and compliance

Full and accurate disclosure of the debtor's financial records, assets and liabilities is critical to a successful restructuring process. The World Bank has recently added disclosure requirements to its methodology of measuring countries' bankruptcy systems.<sup>62</sup> One of the main criticisms of the previous Moroccan law, was the inability of creditors to access accurate records of debtors. In the US system, the US Bankruptcy Courts have the authority to subpoena records and witnesses to ensure that creditors are receiving "adequate information" and to uncover fraudulent transfers. The Courts are also supported by the US Trustee Program (USTP), which is an office within the US Department of Justice.<sup>63</sup> The USTP is an invaluable resource for Courts, which often do not have the resources to police the parties and review disclosures to the extent necessary for the many cases that are filed.

Under the new Moroccan Bankruptcy Law's rescue procedure, the debtor is required to disclose detailed financial records.<sup>64</sup> The law also includes a broad obligation for all persons with relevant information to disclose relevant to a trustee or face a fine imposed by a judge.<sup>65</sup> Under the judicial settlement procedure, the trustee is obligated to collect and disclose information about the financial status of the debtor.<sup>66</sup> Creditors also have an affirmative right to access a variety of documents and financial data, either as a member of the creditor association or based on a direct request to the trustee to disclose the documents.<sup>67</sup> The creditor also has a right to appeal any decisions by the trustee refusing to release documents.<sup>68</sup> Additionally, the new Moroccan law empowers the public prosecutor to monitor the disclosure of documents and intervene if disclosures are not

<sup>62</sup> Whether the creditor has a right to request information from insolvency representative (World bank 2019).

<sup>63</sup> White C, "Professional Fees, Corporate Governance, Predictability and Transparency in Chapter 11", AMERICAN BANKRUPTCY INSTITUTE JOURNAL at 3, available at [www.justice.gov/ust/file/849381/download](http://www.justice.gov/ust/file/849381/download).

<sup>64</sup> Moroccan Bankruptcy Law, art 561.

<sup>65</sup> *Idem*, art 568: Anyone in possession of corporation documents or account books must place them with the trustee for study, or else a fine determined by the acting judge may be imposed.

<sup>66</sup> *Idem*, art 612. "The Trustee must provide the following paperwork and documents to creditors starting from the day following the publication of notification until the meeting date:

- If the association is to discuss the draft settlement plan for continued corporation operation or settlement plan suggested by creditors:
- Information related to the financial situation of the corporation including assets and liabilities especially privileged and regular liabilities
- A detailed inventory of corporation assets
- The draft settlement plan stated in article 595 above, suggested by the syndic along with the offers received in case of partial sale mentioned in article 635 below if required
- If necessary, the draft settlement plan suggested by creditors as per paragraph 3 of article 615 below
- If the association meeting is to discuss modifying the goals and methods of the continuity plan as per article 629 below:
  - The continuity plan as approved by court
  - Suggested amendments to the plan including suggested reduction rates
  - The syndic report as per paragraph one of article 629 below
  - Information regarding the financial situation of the corporation
  - If the association meeting is to discuss asset assignment as per article 618 below, a copy of the assignment application and a list of protected assets referred to in the same article

<sup>67</sup> *Ibid*, "Every creditor may review the above-mentioned documents in person or through an agent and receive a copy of them at his own expense."

<sup>68</sup> *Ibid*, "If any creditor is unable to review the above-mentioned documents or the syndic refuses to allow review, he may appeal to the acting judge."

sufficient during any of the bankruptcy procedures governed by this law.<sup>69</sup> However, unlike the US system, the new Moroccan law does not create a separate entity to monitor the compliance of the trustees, courts and parties with the obligations of the bankruptcy statute. The new law relies heavily on the courts, which are tasked with sanctioning debtors that do not comply with the disclosure requirements,<sup>70</sup> and the public prosecutor's office, which retains its authority to subpoena documents directly from debtors.

Under the Bahraini Reorganisation and Bankruptcy law, debtors and creditors are required to make extensive disclosures in order to start a bankruptcy procedure.<sup>71</sup> The new law also gives the court the ability to request documents from both the debtor and the creditor prior to making a determination on whether to open bankruptcy procedures for a debtor.<sup>72</sup> Once a reorganisation procedure has been commenced, trustees are tasked with preparing a report on the financial status of the debtor at the outset of the procedure<sup>73</sup> and to include an additional report through a "statement of disclosure" to the creditors along with the reorganisation plan.<sup>74</sup> The trustee is also required to maintain records on the financial status of the debtor during the bankruptcy itself<sup>75</sup> and to provide regular reports to the courts.<sup>76</sup> The creditors' committee is also given the explicit task of monitoring and investigating the financial status of the debtor but without the subpoena power of a court.<sup>77</sup> In terms of compliance with the disclosure requirements, the new Bahraini law gives the court the authority to impose fines on parties for submitting false or incomplete claims to open bankruptcy procedures.<sup>78</sup>

However, the new Bahraini law stops short of the Moroccan and US models of creating explicit rights and mechanisms for creditors to the disclosure of pertinent information, especially during the bankruptcy process. Also, like the Moroccan law, the Bahraini law does not create a separate institution to support the courts in monitoring compliance with disclosure requirements, nor does it provide explicit guidance or authority for law enforcement, such as a public prosecutor, to intervene in bankruptcy cases.

Given the critical importance of accurate disclosures, the lack of sufficient authorities and resources to ensure compliance may seriously undermine the new Bahraini and Moroccan statutes. As the courts begin to apply these new statutes, there is a serious risk that there will not be sufficient resources for the courts to police the disclosure process. The Moroccan law invokes the power of the public prosecutor's office, which could be an effective solution if sufficient resources are allocated by that office to monitor the bankruptcy process. However, a specialised office or task force would be better suited to ensure compliance given the complex and extensive nature of bankruptcy disclosures.

<sup>69</sup> *Idem*, art 760: The public prosecution may order the syndic to give up all documents and contracts in his possession. (Article located within section of provisions that applies to the entire bankruptcy chapter.)

<sup>70</sup> *Idem*, art 745: "The court must be involved in all stages of the settlement or judicial liquidation procedure in order to issue a ruling if necessary to invalidate the commercial competence of any merchant proven to have committed any of the following acts... (2) Neglect to provide legal accounts or conceal some or all of account documents."

<sup>71</sup> Bahrain Reorganization and Bankruptcy Law, arts 12(debtor) and 13 (creditor).

<sup>72</sup> *Ibid.*

<sup>73</sup> *Idem*, art 40 (1): prepare a report upon his appointment about the debtor's assets and business and all circumstances affecting the financial position of the debtor and the expected developments.

<sup>74</sup> *Idem*, art 112.

<sup>75</sup> *Idem*, art 41.

<sup>76</sup> *Idem*, art 42.

<sup>77</sup> *Idem*, art 103, Creditor Committee provisions - (reorganization); art 145 (liquidation).

<sup>78</sup> *Idem*, art 21: "The Court may, on its own or at the request of any concerned person, impose a fine not exceeding twenty thousand Dinars on the person that submits a statement of claim or request hereunder with the aim of obstructing or delaying bankruptcy procedures without justification..."



## 9. Special provisions for small and micro debtors and discharge

As both Morocco and Bahrain seek to develop their economies, there is increasing focus on the needs of small and micro businesses given their crucial role in economic growth.<sup>79</sup> The high failure rate of these businesses also makes it important for countries to have bankruptcy procedures that are conducive for these businesses.<sup>80</sup> According to a recent report by the World Bank, two of the primary methods of supporting distressed small businesses are to create streamlined procedures with limited roles for courts and to ensure the full discharge of debtors from their debt obligations following a liquidation.<sup>81</sup> Prior to the new 2018 statutes, debtors in Morocco and Bahrain were not able to fully discharge their debts following a bankruptcy, even after agreeing to a scheme of arrangement settlement under the Bahraini law.<sup>82</sup>

### 9.1 Streamlined procedures

Under the US Bankruptcy Code, consumer debtors have an alternative procedure<sup>83</sup> to the lengthy Chapter 11 reorganisation processes, a Chapter 13 filing, that enables the debtors to develop a repayment plan that is submitted to a Court for approval. The procedure includes many of the principles of a Chapter 11 including the automatic stay and strict disclosure requirements;<sup>84</sup> however, the process is fast-tracked to put in place the repayment plan. While still a “court-based” approach, the World Bank considers this procedure to be an exceptional model in its success, crediting this success to the specialised US Bankruptcy Courts and the extensive infrastructure in place to process these claims.<sup>85</sup> The recommended approach of the World Bank is to limit the role of the courts in the case of countries that “lack the robust and insolvency-focused institutional structure to bear these burdens.”<sup>86</sup> The World Bank’s research has found that the formality of a court-led structure results in the preservation of less enterprise value.<sup>87</sup> Morocco and Bahrain would qualify as countries that lack an extensive institutional structure for insolvency, given how recently their modern statutes were ratified.

The new Bahraini Reorganisation and Bankruptcy Law contains a provision that allows courts to fast track the reorganisation or liquidation of debtors with less than BHD 10,000 of debt based on its own discretion.<sup>88</sup> The streamlined procedures in the reorganisation procedure remove the requirements of appointing trustees, considering appeals and appointing a panel of creditors and enables the court to have a plan approved with only a majority of all creditors in number and value instead of a the two-thirds majority of each

<sup>79</sup> *Saving Entrepreneurs, Saving Enterprises: Proposals on the Treatment of MSME Insolvency* (2018) The World Bank Group at V. <http://documents.worldbank.org/curated/en/989581537265261393/pdf/129977-WP-PUBLIC-DOCDATE-91-18-17-9-2018-10-31-20-TaskForceSavingEntrepreneursSavingEnterprisesMSMEInsolvency.pdf>.

<sup>80</sup> *Saving Entrepreneurs, Saving Enterprises: Proposals on the Treatment of MSME Insolvency* (2018) The World Bank Group, at 1.

<sup>81</sup> *Ibid.* “... a necessary step to allow such individuals to become economically productive again. Securing voluntary release of this debt, even in part, has proven to be an all but insurmountable challenge for individual MSME operators.”

<sup>82</sup> Legislative Decree No. 11 of 1987, Promulgating the Bankruptcy and Composition Law, art 211: “The scheme may provide for allowing the debtor periods of time for repayment of the debts. It may also provide for discharging the debtor of part of the debt; however the debtor shall remain liable for this discharged part as natural debt.”

<sup>83</sup> 11 USC, § 1322, <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-13-bankruptcy-basics>.

<sup>84</sup> *Ibid.* One of the features is an opportunity for creditors to interview the debtor under oath.

<sup>85</sup> *Saving Entrepreneurs, Saving Enterprises: Proposals on the Treatment of MSME Insolvency* (2018) The World Bank Group, at 17.

<sup>86</sup> *Ibid.*

<sup>87</sup> *Ibid.*

<sup>88</sup> Bahrain Reorganization and Bankruptcy Law, art 190: Special provisions for the bankruptcy of small debtors.



class required by the reorganisation chapter.<sup>89</sup> The liquidation provision limits distributions to one distribution.<sup>90</sup>

The Moroccan Bankruptcy Law does not include special procedures for debtors based on the size of debts. However, the law does contain two flexible mechanisms, an external prevention procedure and a reconciliation mechanism, that empower the Chief Justice of the court to stay foreclosures and repossessions while also appointing a conciliator to negotiate a mutually accepted resolution between the debtor and creditors.<sup>91</sup>

## 9.2 Discharge

The liquidation procedure of the US Bankruptcy Code includes a full discharge from debts after the assets are liquidated.<sup>92</sup> For reorganisations, the plan itself results in the discharge of non-plan debts.<sup>93</sup>

Consistent with the US Bankruptcy Code, the new Bahraini Bankruptcy Law provides a complete discharge for debtors after a liquidation, while also discharging debtors from debts that are not part of the approved reorganisation plan.<sup>94</sup> In contrast, the Moroccan law is not explicit on the question of discharge. The rescue, judicial settlement and liquidation procedures do not include explicit language about the status of debts following the implementation of the procedure. In order for the Moroccan law to effectively serve the needs of businesses, it is critical that a provision be added to discharge the debts of debtors after liquidation.

## 10. Conclusion

The 2018 Moroccan and Bahraini bankruptcy statutes have addressed many of the weaknesses of past legislation that have deterred investment and discouraged risk-taking by small businesses. Morocco and Bahrain are signalling a major shift in their legal frameworks by adopting these new laws and the international best practices that are incorporated in their provisions.

For Morocco, the fortification of its disclosure requirements and the inclusion of creditor voting in its judicial settlement procedure will greatly reduce creditor concerns and encourage investment. However, the bankruptcy process, particularly for small businesses, would be further strengthened by:

- a clearly defined priority structure for creditors;

<sup>89</sup> *Ibid.*

<sup>90</sup> *Ibid.*

<sup>91</sup> Moroccan Bankruptcy Law, arts 549 (External prevention), art 551 (Reconciliation).

<sup>92</sup> One of the primary purposes of bankruptcy is to discharge certain debts to give an honest individual debtor a “fresh start.”; <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics>. Although an individual Ch 7 case usually results in a discharge of debts, the right to a discharge is not absolute and some types of debts are not discharged.

<sup>93</sup> USC 11, § 1141(d)(1) generally provides that confirmation of a plan discharges a debtor from any debt that arose before the date of confirmation. After the plan is confirmed, the debtor is required to make plan payments and is bound by the provisions of the plan of reorganisation. The confirmed plan creates new contractual rights, replacing or superseding pre-bankruptcy contracts.

<sup>94</sup> Bahrain Reorganization and Bankruptcy Law, art 116: If the plan is certified and does not mention discharge of debt, then any remaining debt not specifically addressed in the plan is discharged (with some exceptions). Article 150 (regarding Liquidation): Debt is discharged as long as the debtor 1) is not a fictitious entity; 2) is insolvent; 3) cooperates with liquidation administrator; 4) has committed no fraud in the four years prior to bankruptcy. Debts cannot be discharged that are 1) art 4 debts; 2) debts resulting from fraud; 3) debts accrued intentionally to harm another; 4) debts related to criminal activity; 5) marital or familial debts.

- the creation of a specialised institution to support the courts and the public prosecutor's office in monitoring the parties' compliance with disclosure requirements and other obligations;
- the inclusion of a provision requiring creditor approval or participation in the approval of a rescue plan;
- the inclusion of small business provisions in its regulations that streamline the reorganisation process; and
- the addition of a complete discharge of debt liability for liquidated debtors.

For Bahrain, the creation of a new reorganisation process, the inclusion of streamlined procedures for small debtors, the discharge of liquidated debtors and the removal of the punitive provisions, will encourage greater risk-taking and entrepreneurship. However, all of the bankruptcy procedures would be significantly improved by:

- the inclusion of an automatic suspension of claims; and
- the creation of a specialised institution to support the courts and the public prosecutor's office in monitoring the parties' compliance with disclosure requirements and other obligations.



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