Critical Analysis of Commencement Requirements of Bahraini Reorganisation Law: A Comparative Perspective

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Abstract

In 2018, Bahrain enacted the Reorganization and Bankruptcy Law (RBL 2018), aligning with its 2030 Economic Vision and drawing inspiration from US Chapter 11 legislation and supra-national recommendations. Despite its potential significance, RBL 2018 has received limited attention in academic literature. This article aims to address this gap by critically analysing the commencement requirements of RBL 2018 through a comparative analysis with Chapter 11 and various UK reorganisation regimes. This study focuses on three commencement tests: the viability test, the good faith test, and the insolvency test.

The critique centers on the justification for the insolvency test as a prerequisite for initiating reorganisation proceedings under RBL 2018. The analysis reveals that the insolvency test, which requires debtors to prove their financial distress, significantly impedes early rescue attempts and burdens businesses with extensive evidentiary obligations. Furthermore, within the context of RBL 2018, the insolvency test lacks justification due to the stringent good faith test and high court involvement, both of which provide strong safeguards against misuse. Additionally, the absence of alternative formal reorganisation mechanisms in Bahrain and the contradiction with supra-national recommendations further undermine the necessity of the insolvency test.

Consequently, the article suggests omitting the insolvency test -while maintaining the stringent application of the good faith test- in favour of a more lenient approach: the financial difficulty test. This approach would allow for earlier interventions and make reorganisation proceedings more accessible. The study concludes with recommendations for potential

future reforms to enhance the efficiency and effectiveness of Bahrain's insolvency regime.

Keywords: Insolvency, Bankruptcy, Reorganisation, Restructuring, Bahrain, UK, US.

ملخص

في عام ٢٠١٨، اتخذت مملكة البحرين خطوة مهمة نحو تعزيز ثقافة إنقاذ الأعمال، من خلال سنّ قانون إعادة التنظيم والإفلاس لسنة ٢٠١٨، الذي يتماشى مع رؤية البحرين الاقتصادية ٢٠٣٠، مستمدًا أحكامه من قانون الإفلاس الأمريكي (الفصل الحادي عشر) وكذلك التوصيات الدولية للأونسيترال. على الرغم من أهمية دور هذا القانون في تنمية الاقتصاد الوطني، لم يحظَ بكثير من الاهتمام على الصعيد الأكاديمي. تهدف الورقة البحثية الماثلة إلى سدّ هذه الفجوة من خلال التركيز على التحليل النقدي لمتطلبات بدء إجراءات إعادة التنظيم في ظل قانون إعادة التنظيم والإفلاس لسنة ٢٠١٨، وذلك من خلال تحليل مقارن مع أحكام الفصل الحادي عشر وأنظمة إعادة التنظيم المتعددة في المملكة المتحدة، مع التركيز على ثلاثة شروط رئيسة: شرط إمكانية الاستمرار، شرط حسن النية، شرط الإعسار.

تتركز أبرز أهداف هذا البحث على التحليل النقدي لمسوّغات شرط الإعسار بوصفه شرطًا أساسيًّا لبدء إجراءات إعادة التنظيم بموجب قانون الإفلاس البحريني. توصلت نتائج البحث إلى أنَّ شرط الإعسار الذي يتطلّب من المدين إثبات ضائقته المالية وتوقفه عن الدفع، يعيق بشكل كبير المحاولات المبكرة لإنقاذ الشركات، ويثقل كاهل المدين بعبء إثبات إعساره. علاوة على ذلك - في سياق قانون الإفلاس البحريني - يفتقر شرط الإعسار إلى المسوّغ بسبب وجود شرط حسن النية الصارم، وكذلك سلطة المحكمة في إدارة دعوى الافلاس، اللذين يوفران ضمانات قوية ضد سوء استخدام أو استغلال إجراءات إعادة التنظيم. بالإضافة إلى ذلك، فإن غياب آليات إعادة تنظيم رسمية بديلة في البحرين وتعارض شرط الإعسار مع التوصيات الدولية، يضعفان الحجة الداعية لتبني شرط الإعسار.

وبناءً على ذلك، يقترح المقال حذف شرط الإعسار مع استمرار تطبيق شرط حسن النية، واعتماد نهج أكثر مرونة: اختبار الاضطراب المالي. سيسمح هذا النهج بالتدخل المبكر قبل الوصول إلى مرحلة الإعسار مما يزيد فرص نجاح إعادة التنظيم، ويجعل اللجوء إلى إجراءات إعادة التنظيم يسيرًا، مما يعزِّز كفاءة نظام الإفلاس وفعّاليَّته في المملكة.

Introduction

1.1 Background

In the dynamic realm of modern business, corporate reorganisation and rescue mechanisms are pivotal in maintaining economic stability and ensuring the sustainability of businesses facing financial distress. These mechanisms provide a framework for distressed businesses to restructure their operations, debts, and assets, allowing them to regain their footing and contribute to the preservation of employment opportunities and the enhancement of the national economic framework.[1] Such socio-economic benefits of enacting rescue-oriented insolvency laws are actively promoted by international organisations, such as the United Nations Commission on International Trade Law (UNCITRAL), which consider offering both a formal restructuring framework and liquidation procedures crucial for maintaining a nation's international reputation in terms of insolvency regulations.[2]

Chapter 11 of the US Bankruptcy Code 1978, which embodies a comprehensive and flexible framework that allows debtors to restructure their debts, operations, and assets while preserving value for all stakeholders, is at the global forefront of corporate reorganisation processes. It is widely regarded as the 'golden standard' in reorganisation procedures,[3] and its impact transcends borders and influences reorganisation regimes worldwide.[4]

1. H.R. REP. No. 595, 95th Cong., 1st Sess. 220 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6179; Charles J Tabb, 'The Future of Chapter 11' (1992) 44 SC L Rev 791, 792; Rasha Mustafa Abu Al-Gheit, 'Restructuring Troubled Projects as a Mechanism to Prevent Bankruptcy: In Accordance with the Provisions of Law No. 11 Of 2018 Regarding the Organization of Restructuring, Preventive Composition and Bankruptcy' (Arabic) (2020) 6(2) Sadat City University, Faculty of Law 3, 12; Ibrahim Sabri Al-Arnaout, 'The Regular Reorganization Plan to Save Troubled Economic Projects According to The Jordanian Insolvency Law (A Comparative Study)' (Arabic) (2020) 47(3) Derasat 152, 154.

2. Faisal Ibrahim F Alfawzan, 'Critical Examination of Saudi Restructuring Law in the Light of United Kingdom and United States Experiences' (PhD thesis, University of Leeds, January 2022) 25.

3. Nigel J. Isherwood, 'Coronavirus and Corporate Insolvency: A Comparative Analysis of the Corporate Insolvency and Governance Act 2020' (2022) 11 Aberdeen Student L Rev 100, 130.

4. See, e.g. Spanish Law 382011/ of October 2011; German insolvency Code 1999 (Insolvenzordnung); Saudi Bankruptcy Law 2018; Jay Lawrence Westbrook, 'The Globalisation of Insolvency Reform' (1999) 1999 NZ L Rev 401, 401.

Within the United Kingdom, the recommendations of the Cork Report,[5] regarded as the cornerstone upon which contemporary corporate insolvency frameworks are built,[6] spurred a significant transformation in the landscape of English corporate insolvency. The Cork Report's suggestions laid the groundwork for fostering a 'rescue culture' emphasising the necessity of modern insolvency laws to preserve viable businesses that contribute to the economy.[7] In reaction to the Cork Report, the Insolvency Act of 1986 (IA 1986) implemented reorganisation procedures, such as Administration and the Company Voluntary Arrangement (CVA). Moreover, the Enterprise Act 2002 represents a significant reform in the insolvency framework of the UK. Later, the Companies Act 2006 (CA 2006) introduced the Scheme of Arrangement (SoA), and the most recent reform, the Corporate Insolvency and Governance Act 2020 (CIGA), introduced a stand-alone moratorium procedure and a restructuring plan mechanism (Part 26A scheme). Each of these mechanisms is tailored to a specific scenario and offers a range of options for companies in financial distress to reorganise and recover.

Bahrain, a key player in the context of the Gulf Cooperation Council countries, enacted the Reorganization and Bankruptcy Law 2018 (RBL 2018),[8] implemented in tandem with Bahrain's ambitious 2030 Economic Vision.[9] Together, these comprise a significant step towards modernising the country's business landscape. RBL 2018 seeks to establish a

5. Kenneth Cork, Insolvency Law and Practice: Report of the Review Committee (HM Stationery Office 1982).

6. Vanessa Finch and David Milman, Corporate Insolvency Law: Perspectives and Principles (3rd edn, Cambridge University Press 2017) 15.

7. ibid 202.

8. Reorganization and Bankruptcy Law 2018 (RBL 2018).

9. --, 'Bahrain Economic Vision 2030'(Kingdom of Bahrain's National Portal, 18 July 2021) <https://www.bahrain.bh/wps/portal/en/!ut/p/z1/lVLLUsIwFP0VN12W3DbQRneVQZCRwQFKIRsmhfShbVJCbPXvDcMKFYrZJXNe9-QiilaIClbnKdO5FKww9zX1NqMpeI5L3DHBIYZg6vVn9wNwhtBD0TkAMB4cAf6rv7x3PQKI3sIHd9J3nruGP5kABORx9rJ46gMM8Y38Cydo9V8iimi1zXdojRPHT3q9xHZ9wu2ux8AmMYtt4ntu4hDCux4-ordCVzpDa57KupJKs2LDlAUFE7tcpHcVS_nBgphliuXCBQw_S_qdgl6fITrattR80rjSY5vJ2oT0L4Y0ClGd8waFQqrSbMb8n8WNAI3bPsNsW_6239PAlCyF5p8arW5v2cinhYxPWxuIGJMUUcUTrrjqfCjznGldHR4ssKBpmk4qZVrwzlaWFvxFyeTB-J8j0ZwpVJVhGJYEf9nvM9Iskqyoy4ho8g1roKJ3/dz/d5/L0lHSkpZQSEhL3dMTUFIa0FFa0EhIS80TlZFL2Vu/> accessed 27 July 2023; Foutoun Hajjar and Siddharth Goud, 'Bahrain Introduces New Insolvency Regime' (Lexology, 28 February 2019) <https://www.lexology.com/library/detail.aspx?g=efa7bea9-a1994-fd01-9504-c3c392f2047 > accessed 28 July 2023.

comprehensive framework for corporate reorganisation, aligning Bahrain with international best practices in the realm of insolvency laws, drawing inspiration from the renowned Chapter 11, and building on recommendations from UNCITRAL.[10]

Prior to the enactment of RBL 2018, the only formal option for distressed debtors to avoid bankruptcy was under the repealed Bankruptcy and Composition Law 1987 (BCL 1987). In that legal framework, debtors sought a settlement with their creditors, overseen by the court,[11] to avoid the bankruptcy stigma and harsh consequences of being declared bankrupt. These consequences encompassed the curtailment of various civil and political rights of the bankrupt debtor, such as the rights to vote, stand for public office, and engage in public employment.[12]

This article seeks to critically analyse the commencement requirements of the Reorganization and Bankruptcy Law 2018 (RBL 2018) concerning the initiation of reorganisation proceedings. Assessing these conditions is crucial as it determines the accessibility and effectiveness of the Law, which is essential for the successful resolution of corporate insolvency. Comparisons will be drawn with the commencement requirements under the insolvency laws of the United Kingdom and the United States, specifically Chapter 11 of the US Bankruptcy Code and various UK insolvency frameworks.

1.2 Justification

The enactment of RBL 2018 represents a significant step into corporate rescue in Bahrain's landscape. Despite its potential significance, RBL 2018 remains understudied in academic literature. Only limited assessments have been implemented, primarily shortly after its passage, which lack

10. Buthaina Amin and David Billington, 'Bahrain's New Bankruptcy Law' (2019) 9 Emerging Markets Restructuring Journal 1,1; Ronald Langat and Maryam Alhashemi, 'Black is the new black, Bahrain's bankruptcy regime at a glance' (Al Doseri Law, 1 Dec 2021) < https://www.aldoserilaw.com/black-is-the-new-black-bahrains-bankruptcy-regime-at-a-glance/ > accessed 28 July 2023; --, 'Continuous development is necessary to improve the law. 'House of Merchants': No cases of bankruptcy law exploitation were discovered.' (Alayam, 3 April 2023) < https://alay.am/p/6xn4> accessed 26 July 2023.

11. Farooq Ahmed Zaher, The Bankruptcy System in Egyptian Law Between the Old and New Trade legislations (Arabic) (Dar Al-Nahda Al-Arabia 2003) 277.

12. Saeed Abdullah Al-Hamidi, Explanation of Bahrain Bankruptcy Law (Arabic) (1st edn, Modern Arab Office 2010) 9.

attention to evolving court practices. This article seeks to fill that void by critically analysing RBL 2018 six years after its enactment, considering new case law and updated insights. The current practice of RBL 2018 has raised concerns. The challenges in initiating reorganisation proceedings have frequently unfolded in court, leading to notable case dismissals. These concerns form focal points for the subsequent sections, which aim to advance comprehension in the realm of corporate insolvency and furnish pragmatic insights for policymakers, legal practitioners, and scholars alike.

1.2 Objectives

This article seeks to scrutinise the effectiveness and ease of the commencement requirements inherent in RBL 2018's reorganisation proceedings, considering practices in the US and UK. Central to this analysis are three pivotal commencement tests: the viability test, the good faith test, and notably, the insolvency test.

The viability test evaluates whether a debtor can realistically continue its operations post-restructuring, thereby ensuring that reorganisation efforts are economically feasible and likely to succeed. In contrast, the good faith test examines the sincerity of the debtor's intentions in proposing a reorganisation plan, safeguarding against abusive or fraudulent practices. However, the focus of critique within this article revolves around the justification for the insolvency test as a prerequisite for initiating reorganisation proceedings under RBL 2018.

1.3 Methodology

The research primarily adopts a doctrinal methodology to assess and analyse RBL 2018. This approach involves a comprehensive examination of legal sources, including legislation, case law, scholarly articles, and government reports.[13] Such a method allows for a thorough examination of the key features of the legislation and case law. Relevant components are subsequently carefully merged or synthesised to make a thorough and correct legal assertion on the subject matter.[14]

13. Jadesola Tiwalola Faseluka, 'A Critical Analysis of The Effectiveness of Corporate Rescue in Retail Sector Insolvency Cases' (PhD thesis, University of Leeds, March 2022) 8.

14. Dawn Watkins and Mandy Burton (eds), Research Methods in Law (2nd edn, Routledge 2017) 13.

Furthermore, this study embraces a comparative methodology by comparing RBL 2018 to the reorganisation regimes of the UK and US. This comparative aspect is pivotal to evaluating the efficacy of RBL 2018 in furnishing effective reorganisation mechanisms for distressed debtors. The provisions of RBL 2018 are largely influenced by US Chapter 11, rendering a comparative analysis with it instrumental in comprehending and assessing RBL 2018's provisions. Additionally, the established and well-tested nature of both the UK and US reorganisation regimes offers insights to address any deficiencies and enhance the effectiveness of RBL 2018. Moreover, the diverse solutions provided by the various reorganisation frameworks in the UK offer strategies to navigate legal challenges. Lastly, the pro-debtor nature of Chapter 11, in contrast with the pro-creditor UK regimes,[15] provides a notable contrast that deepens the analysis of RBL 2018.

Finally, this article also employs an empirical methodology in certain sections, incorporating a quantitative approach. This involves analysing 66 bankruptcy cases to understand the reasons behind their dismissals. By examining these cases, the study provides valuable insights into how the law is applied in practice,[16] highlighting patterns and potential areas for improvement. This empirical analysis not only supports the theoretical arguments presented but also offers practical guidance for refining the legal framework to better serve debtors and creditors. Through this comprehensive approach, the article aims to bridge the gap between theory and practice, ensuring that the recommendations are grounded in real-world evidence.

1.4 Research Outline

This article is structured into five sections. Section 1 presents an introductory overview of the research subject, including the research justification, methodology, objectives, and an outline of the forthcoming sections. Section 2 provides an overview of the prerequisites for commencing reorganisation proceedings under RBL 2018, US Chapter 11,

15. Alfawzan (n 2) 32; Gerrard McCormack, 'Corporate Rescue Law in Singapore and the Appropriateness of Chapter 11 of the US Bankruptcy Code as a Model' (2008) 20 SAcLJ 396,406.

16. C.E. Koops, 'Contemplating compliance: European compliance mechanisms in international perspective' (PhD thesis, Amsterdam Center for International Law, March 2014) 65.

and various UK reorganisation mechanisms. Section 3 critically analyses the three pivotal commencement tests under RBL 2018: the viability test, the good faith test, and the insolvency test, in comparison with US and UK bankruptcy legislation. Section 4 suggests adopting a more lenient approach for RBL 2018, advocating for the Financial Difficulty approach instead of the insolvency test. Lastly, Section 5 provides a conclusion to the research, encapsulating the principal findings and recommendations generated by the study.

2. Commencement of Reorganisation Proceedings: An Overview

To assess the success of reorganisation processes, it is critical to determine their accessibility and investigate the commencement requirements for such procedures. As an overall concept, it is preferable that the commencement requirement be transparent and certain, permitting accessible, cost-effective, and timely access to insolvency proceedings to encourage financially troubled or insolvent enterprises to voluntarily initiate proceedings.[17] Meanwhile, Accessibility must be matched with appropriate protections to prevent improper use of proceedings.[18] Thus, a balance is needed between the commencement requirements.

The following section delves into the specific requirements outlined in RBL 2018 for commencing reorganisation proceedings and compare them to the corresponding provisions in US and UK laws. This allows it to obtain a full insight of RBL 2018's strengths and limitations, as well as identify potential areas for improvement.

The section begins by providing an overview of the reorganisation regimes in the UK and US, highlighting their commencement requirements.

2.1 UK perspective

The UK offers a variety of reorganisation regimes designed to address the financial difficulties of businesses, including the Company Voluntary Arrangements (CVAs), Scheme of Arrangement (SoA), Part 26A scheme, Stand-Alone Moratorium, and the Administration process.

17. UNCITRAL, Legislative Guide on Insolvency Law (United Nations 2005) 45.
18. ibid.

2.1.1 Administration

Administration in the UK is a legal process that facilitates the reorganisation of a company or the realisation of its assets.[19] It serves as a gateway to various routes that a distressed company can take rather than being a stand-alone reorganisation procedure.[20] When corporate restructuring appears feasible, the appointed administrator may propose a Company Voluntary Arrangement (CVA) under Part 1 of the Insolvency Act 1986, a scheme of arrangement under Part 26 of the Companies Act 2006, or a restructuring plan under Part 26A of the Companies Act 2006.[21]

Upon entering administration, an insolvency practitioner is appointed as the administrator, taking over control of the company's business and assets from the directors. The administrator's role is to achieve one of the statutory objectives of administration. The primary goal is to rescue the company as a going concern. If this is not practicable, the secondary objective is to achieve a better outcome for creditors than would be possible through liquidation. The third objective, pursued only if the first two are unattainable, is to realise the company's property to make a distribution to secured or preferential creditors.[22]

2.1.1.1 Commencement requirements

A company can enter administration either through a court order or by filing documents at court, known as the out-of-court route. The court route involves a formal application and an open hearing, while the out-of-court route can be initiated by the company, its directors, or the holder of a

19. Practical Law Restructuring and Insolvency, 'Adminstration' (Practical Law UK) <https://mail.google.com/mail/u/2/#inboxhttps://uk.practicallaw.thomsonreuters.com/Document/I3351a6fee8da11e398db8b09b4f043e0/View/FullText.html?navigationPath=Search%2Fv12%Fresults%2Fnavigation%2Fi0ad7401200000190bbb11284b83f10c73%Fppcid%3D159592272a8145a9b0e5385f984f01b726%Nav%3DKNOWHOW_UK%26fragmentIdentifier%3DI3351a6fee8da11e398db8b09b4f043e026%parentRank%3D026%startIndex%3D126%contextData%3D%2528sc.Search%252926%transitionType%3DSearchItem&listSource=Search&listPageSource=87021b9d45648aeec472bef424ec08e6&list=KNOWHOW_UK&rank=1&sessionScopeId=d6f4ab8b728c354ab26b58009942b8f7f0921fba5f2f1cbf0132aabd91403b13&ppcid=159592272a8145a9b0e5385f984f01b7&originationContext=Search%20Result&transitionType=SearchItem&contextData=(sc.Search)&comp=pluk > accessed 1 July 2024

20. Alfawzan (n 2) 90.

21. ibid.

22. Practical Law Restructuring and Insolvency (n 19); Insolvency Act 1986 (IA 1986) paragraph 3(1), Schedule B1.

qualifying floating charge over the company's assets.[23] The out-of-court appointment of an administrator has become the predominant method since the enactment of the Enterprise Act 2002.[24]

For the court to grant an administration order, it must be satisfied that the company is unable or likely to become unable to pay its debts (insolvency test), and that the administration is reasonably likely to achieve its purpose.[25] The insolvency test includes the cash flow test where the debtor is 'unable to pay its debts as they fall due'[26]. And the balance sheet test, when 'the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities'.[27]

2.1.2 Company Voluntary Arrangements (CVAs)

Company Voluntary Arrangements (CVAs) provide an alternative path for companies experiencing financial difficulties. Established under the Insolvency Act 1986, CVAs were designed to offer companies a chance to initiate rescue efforts before becoming insolvent.[28] The primary purpose of a CVA is to facilitate the recovery of a company, often in conjunction with other mechanisms such as administration.[29]

CVAs allow companies to negotiate the composition of their debts with creditors. For instance, a company might agree to pay 59 pence on the pound of its debts.[30] Additionally, a CVA can involve a scheme of arrangement where creditors are paid a portion of what is owed, but not necessarily immediately.[31] The compromise reached through a CVA binds all creditors who were entitled to vote at the meeting approving the arrangement, including those who would have been entitled to vote if they had received notice of the meeting.[32]

One of the distinctive features of a CVA, compared to administration, is that the company's management retains control over the business operations. This control is exercised under the supervision and guidance

23. Practical Law Restructuring and Insolvency (n 19).
24. Alfawzan (n 2) 91.
25. IA 1986 Schedule B1 , para 11; Alfawzan (n 2) 91.
26. IA 1986, s 123(1)(e).
27. IA 1986, s 123(2).
28. John Paul Tribe, 'Company Voluntary Arrangements and Rescue: A New Hope and a Tudor Orthodoxy' (January 15, 2009) Journal of Business Law, Forthcoming1,9.
29. ibid 10.
30. ibid.
31. ibid.
32. Alfawzan (n 2) 95.

of a proposed nominee, who assists in implementing the arrangement.[33]

2.1.2.1 Commencement requirements

Unlike Administration, a company who apply for a CVA does not need to be insolvent or unable to pay its debts,[34] making it a flexible option for businesses seeking to restructure their obligations and achieve financial stability. Despite this advantage, it is important to note that CVAs do not include a moratorium on creditor actions, which means that while the arrangement is being proposed and negotiated, creditors are not prevented from taking enforcement actions against the company. However, a moratorium can be obtained by combining CVAs with other restructuring routes, such as administration or the stand-alone moratorium.[35]

2.1.3 Stand-Alone Moratorium

Stand-Alone Moratorium is a relatively new addition to the UK's restructuring toolkit, introduced by the Corporate Insolvency and Governance Act 2020 (CIGA 2020). It allows financially distressed companies to obtain an initial 20-business-day moratorium period which can be extended, during which they are protected from creditor actions.[36] This restructuring moratorium operates as a stand-alone mechanism and is not a preliminary step to an insolvency process, although it can be used alongside various restructuring mechanisms including schemes of arrangement and CVAs. [37]

2.1.3.1 Commencement requirements

To initiate the Stand-Alone Moratorium proceedings, two key conditions must be met: the company must pass an eligibility test and demonstrate viability.

All companies are eligible for the standalone moratorium, except those explicitly excluded under Schedule ZA1.[38] This exclusion list covers business types such as banks, insurance companies, investment

33. ibid.
34. ibid.
35. ibid.
36. IA 1986, part A9 (2).
37. Jennifer Payne, 'An Assessment of the UK Restructuring Moratorium' (SSRN, January 2021) <https://ssrn.com/abstract=3759730 or http://dx.doi.org/10.2139/ssrn.3759730> accessed 2 July 2024, 463.
38. IA 1986, Sch ZA1.

exchanges, and securitisation companies.[39]

The viability test stands for that ‘it is likely that a moratorium for the company would result in the rescue of the company as a going concern’.[40] To meet this requirement, the proposed monitor must state confidently that the moratorium will indeed facilitate the company’s rescue as a going concern.[41]

2.1.4 Scheme of Arrangements

A Scheme of Arrangement (SoA) is a legal mechanism under the Companies Act 2006 (CA 2006) in UK, used to restructure a company’s debts or make other significant changes to its corporate structure. It involves a formal agreement between the company and its creditors or shareholders, requiring court approval and the agreement of a specified majority of stakeholders. This process provides a structured and legally binding framework for companies to reorganise their affairs, often as part of a broader insolvency or restructuring strategy.

2.1.4.1 Commencement requirements

The application of SoA can be applied by the company itself, any creditor or member of the company, the liquidator, or the administrator if the company is in administration or liquidation.[42]

One distinct feature of SoA that it is open for both solvent and insolvent companies,[43] meaning that the scheme can be filed and approved whether the company is in actual or imminent insolvency.[44] Nevertheless, SoA itself does not inherently include a moratorium. As a result, during the duration of the scheme’s initial application, until it becomes effective and accepted, any creditor has the right to exercise all of his rights and remedies against the company.[45] To obtain such moratorium, the company has to accordingly pair the scheme with administration or the stand-alone mortarium process.

39. Alfawzan (n 2) 101.
40. IA 1986, pt A1, ch 2, s A6.
41. Alfawzan (n 2) 102.
42. Company Act 2006 (CA 2006) s 896(2).
43. Finch and Milman (n 6) 411.
44. Alfawzan (n 2).
45. Finch and Milman (n 6) 414.

2.1.5 Part 26A scheme

A Part 26A Scheme of Arrangement, newly introduced under CIGA 2020, is a legal mechanism used to restructure a company's debts or make significant changes to its corporate structure. This new procedure is codified in Part 26A, which was added to the Companies Act 2006. The Part 26A scheme and SoA generally share common procedures and features.

2.1.5.1 Commencement requirements

Similarly, to SoA, Part 26A scheme does not require to be in insolvency or imminent insolvency. However, a company would be eligible for applying such a scheme if two conditions were met:

(A) the company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern;

(B) the purpose of the plan is to eliminate, reduce, prevent or mitigate the impact of those financial difficulties.[46]

Despite the 'financial difficulties' term is mentioned in both conditions, it is not defined. It is most likely derived from the first condition, which is any difficulties affecting the business's ability to carry on business as a going concern.[47] In Re DeepOcean,[48] the court emphasised, in determining whether condition A was met, that the current or expected financial difficulties must be 'sufficiently serious' to give rise to the likelihood that the company will be unable to continue operations as a going concern.[49] In such a case, the applicant companies argued that severe financial underperformance had led them to rely on continuous funding from their parent company, DeepOcean Group. However, the parent company faced constraints that made it unable to sustain this financing without risking its own financial stability, making it unlikely to continue providing the necessary funds. As a result, the court concluded that condition A was satisfied because the underperformance causing the applicant companies' financial difficulties had jeopardised their ability to operate as a going concern.[50]

46. CA 2006, s 901A.
47. Riz Mokal, 'The difficulties with "financial difficulties": the threshold conditions for the new Pt 26A process' (2020) 35(10) BJIB&FL 662, 662.
48. In Re DeepOcean [2020] EWHC 3549 (Ch).
49. ibid (39).
50. Alfawzan (n 2) 106.

In Re Virgin Atlantic Airways Ltd,[51] the court examined the satisfaction of condition A by concluding that if the restructuring plan is not sanctioned, the most likely alternative is an administration of the company resulting in liquidation.[52]
condition B can be satisfied if the restructuring plan aims to reduce the impact of the financial difficulties whether towards some or all creditors or even the company itself.[53] In other words, Condition B is met even if the restructuring plan does not seek to restore a company's full financial capability.[54] This leniency appears to lower the entry threshold for debt restructuring.[55]

2.2 US Chapter 11 perspective

The success and robustness of the US bankruptcy regime rely significantly on its comprehensive structure, which includes Chapter 7 liquidation bankruptcy, Chapter 11 reorganisation bankruptcy, and Chapter 15 cross-border bankruptcy.56 Among these, Chapter 11 is often regarded as the gold standard for managing corporate reorganisation due to its structured approach, judicial oversight, and ability to balance the interests of various stakeholders.[57]
Chapter 11 of the US Bankruptcy Code, enacted as part of the Bankruptcy Reform Act of 1978 , stands as one of the extraordinary laws that have profoundly shaped the American economy and society.[58] Its influence has resonated globally, making Chapter 11 a prominent model in commercial law reform worldwide.[59]
At its core, Chapter 11 is based on the idea that a failing business can be reshaped into a successful operation through reorganisation.[60] It 'provide[s] a debtor with legal protection in order to give it the opportunity to reorganize, and thereby to provide creditors with going-concern

51.[2020] BCC 997.
52. ibid [23]; Alfawzan (n 2) 106.
53. Isherwood (n 3) 116.
54. ibid.
55. Alfawzan (n 2) 106.
56. Isherwood (n 3) 130.
57. Payne, 'An Assessment of the UK Restructuring Moratorium' (n 37) 457.
58. Elizabeth Warren and Jay L. Westbrook, 'The Success of Chapter 11: A Challenge to the Critics'(2009) 107 MICH. L. REV. 603, 604.
59. ibid.
60. ibid.

value rather than the possibility of a more meager satisfaction through liquidation'[61]

2.2.1 Commencement requirements

A Chapter 11 restructuring petition is usually initiated voluntarily at the request of the company. In exceptional cases, the restructuring petition might be filed involuntarily against the company's willingness, namely by its creditors.

There is no requirement that the debtor be insolvent or near insolvency in order to apply for Chapter 11 protection.[62] As a result, Strategic bankruptcies have become prominent feature of the US regime. In simple terms, companies may claim the protective shroud of Chapter 11 for a variety of reasons other than pure insolvency,[63] including lowering employee costs and resolving potential tort liability.[64] In re Manville [65] is an excellent example of employing Chapter 11 for non-insolvency issues. In 1982, Johns-Manville Corporation filed for Chapter 11 bankruptcy to address a significant problem caused by an unmanageable surge in asbestos litigation made against it as a result of its long-term use of asbestos-containing products, which caused health problems.[66] The court ruled that a business, even if foreseeing insolvency, need not wait until it becomes unable to pay debts before initiating Chapter 11 proceedings. In addition to the voluntary Chapter 11 filing, the debtor company may be compelled to take part in the Chapter 11 proceedings. If the debtor company has at least 12 creditors, three of whom have unsecured non-contingent, undisputed claims totalling more than $10,000, the creditors can file an involuntary petition against the company, and if the company 'generally fails to pay debts as they become due unless such debts are the subject of a bona fide dispute'.[67] If the company has less than 12 creditors, the proceedings can be initiated by one of its creditors.[68] If the involuntary petition did not meet the aforementioned conditions or

61. In re the Gibson Group, Inc, 66 F3d 1436, 1442 (6th Cir 1995); Alfawzan (n 2) 109.
62. Isherwood (n 3) 131.
63. McCormack (n 15) 406.
64. Alfawzan (n 2) 110.
65. ibid; In re Johns-Manville Corp, 36 BR 727 (Bankr S D N Y 1984).
66. Alfawzan (n 2) 110.
67. ibid 407.
68. Alfawzan (n 2) 112.

was filed in bad faith, the debtor company may recover the proceeding expenses from the petitioning creditors and seek redress.[69] However, Involuntary reorganisation petitions are extremely uncommon. In fact, creditors' involuntary petitions currently account for fewer than 0.05 percent of all petitions.[70]

2.3 Bahrain Perspective

The Reorgnization and Bankruptcy Law of 2018 (RBL 2018) marks a significant milestone in the legal landscape of Bahrain, positioning the country as a pioneer among GCC states in adopting a comprehensive reorganisation process under Chapter 3. Inspired by the principles of US Chapter 11 bankruptcy and the United Nations Commission on International Trade Law (UNCITRAL) recommendations, RBL 2018 introduces an effective framework for reorganisation and bankruptcy proceedings.

The objectives of the RBL 2018 are multifaceted.[71] Primarily, the law seeks to preserve and protect the bankruptcy estate, ensuring that the assets of a distressed company are safeguarded and managed effectively. By maximising the value of the bankruptcy estate, the law also aims to provide the best possible outcome for all stakeholders involved. The law also emphasises the importance of integrity and transparency in bankruptcy proceedings, ensuring that all matters are handled in an orderly and expeditious manner.

Another critical goal of RBL 2018 is to reorganise the debtor, thereby avoiding liquidation wherever reasonably possible. This approach not only helps to preserve the business but also protects the interests of employees, creditors, and other stakeholders. The law provides for the fair distribution to creditors and ensures equal treatment of creditors with similar claims. It also strives to offer fair treatment to all persons having an interest in the bankruptcy proceedings, thereby upholding principles of justice and equity.

69. McCormack (n 15) 407.
70. Richard M. Hynes and Steven D. Walt, 'Revitalizing Involuntary Bankruptcy' (2020) 105 Iowa L Rev 1127,1128.
71. RBL 2018 , art 2.

2.3.1 Scope

The scope of RBL 2018 provisions is limited exclusively to merchants, encompassing both natural persons and juridical entities, such as commercial companies.[72] Notably, RBL 2018 does not extend its application to banks and other financial institutions regulated by the Central Bank of Bahrain, including insurance companies.[73] The reorganisation of such institutions remains within the jurisdiction of the Central Bank and is governed by the Financial Institutions Law 2006.[74] The exclusion of banks and other financial institutions from the RBL 2018's scope seems to be due to their unique nature and critical role in the financial system. These institutions are regulated by the CBB, which ensures their stability and soundness through stringent regulatory and supervisory frameworks. Financial institutions, including banks and insurance companies, have specific operational, risk management, and solvency requirements that differ significantly from those of other businesses. The legislative history of RBL 2018 supports this justification. During the deliberations on enacting RBL 2018 in the Shura Council, the Minister of Justice stated that 'these types of institutions are regulated by the Central Bank of Bahrain, which can intervene with specific procedures that do not fall under this Law [referring to RBL 2018]'.[75]

Furthermore, the scope of the RBL 2018 does not encompass foreign companies or their affiliates operating within Bahrain. Article 3 explicitly states that the law shall apply to 'commercial companies incorporated in the Kingdom'. This limitation is reinforced by judicial application.

72. Ibid, art 3 (A).
73. Ibid, art 3 (C)(1)
74. Financial Institutions Law 2006; Patrick Gearon and William Reichert, 'Notable Changes to Insolvency Legislation in the GCC' (Charles Russell Speechlys, 15 April 2021) <https://www.charlesrussellspeechlys.com/en/news-and-insights/insights/corporate/2021/notable-changes-to-insolvency-legislation-in-the-gcc/> accessed 29 July 2023; Noor Radhi, Noora Janahi, Mohamed Altraif, 'Bahrain: Law and Practice' in Paul Leake (ed), Insolvency (Chambers and Partners 2022) 96.
75. Shura Council, 'Rules of 28th session- 4th Legislative Chapter' (Shura Council, 29 April 2018) <https://councilsessions-s3-bucket.s3.me-south-1.amazonaws.com/_28_pdf-1704976865799.pdf?X-Amz-Algorithm=AWS4-HMAC-SHA256&X-Amz-Credential=AKIA4XAHVY3LHQ7YI5EO%2F202407172%Fme-south-12%Fs32%Faws4_request&X-Amz-Date=20240717T120432Z&X-Amz-Expires=900&X-Amz-Signature=102149aa5257c61ec8109a2c691bf545af96ef8b5fdaf2f0e60394be18a6655a&X-Amz-SignedHeaders=host> accessed 10 July 2024

For instance, in cases number 029/05922/2020/ and 021/125/2021/, [76] petitions for bankruptcy were made by affiliates of foreign companies, Emirati and Cypriot entities. The court rejected these petitions, stating that 'from reviewing the commercial register certificate of the plaintiff and the extract from its commercial register, it is evident that the company is a branch of an Emirati company established in the United Arab Emirates. Consequently, it is a subsidiary of that company and not a company incorporated in the Kingdom of Bahrain to which the Reorganisation and Bankruptcy Law applies. Therefore, as a foreign company (Emirati), it falls outside the scope of the applicable Reorganisation and Bankruptcy Law. Thus, its request to initiate bankruptcy (liquidation) proceedings is not supported by the law and must be dismissed.'[77]

This judicial interpretation underscores the clear jurisdictional boundaries set by the RBL 2018. The law is designed to regulate insolvency and reorganisation within the Bahraini jurisdiction, ensuring it effectively addresses the specific needs and challenges of businesses incorporated in Bahrain. While despite the court in the previous cases not elaborating on the justification for excluding foreign companies from the scope of the RBL 2018, it is evident that extending its scope to include foreign companies would complicate enforcement and administration due to jurisdictional challenges and potential conflicts with the laws of other countries.

2.3.2 Commencement requirements

Under RBL 2018, the initiation of both reorganisation and liquidation proceedings is contingent upon filing of a bankruptcy case with the court. Within this bankruptcy case, the debtor must distinctly specify whether they seek to commence reorganisation or liquidation processes.[78]

The bankruptcy proceedings, encompassing reorganisation and liquidation proceedings, can be initiated either voluntarily by the debtor or involuntarily through a creditor's petition. In cases where the claim exceeds BD 20,000, a single creditor can initiate the petition; however, when the claim is less, at least three creditors are required for such initiation.[79]

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76. Case number 022020) 9/05922/2020/); Case number 022021) 1/125/2021/).
77. Case number 022020) 9/05922/2020/);
78. RBL 2018, art 6, 8.
79. RBL 2018, art 8 (A), (C); Case number 022021) 3/5775/2021/).

Under RBL 2018, the reorganisation proceedings cannot be commenced unless the court is satisfied three pivotal conditions are met: the good faith test, insolvency test,[80] and viability test.

After furnishing a general outline of the overarching provisions of RBL 2018, the following section engages in a comprehensive comparative analysis of the commencement requirements: the good faith test, insolvency test, and viability test as stipulated by RBL 2018.

3. Analysing Commencement Requirements of RBL 2018

This section critically delves into the specific requirements outlined in RBL 2018 for commencing reorganisation proceedings and compares them to corresponding provisions in US and UK laws where relevant. This provides full insight into RBL 2018's strengths and limitations and identifies potential areas for improvement.

As discussed earlier, Under RBL 2018, the initiation of reorganisation proceedings is subject to three pivotal conditions: the good faith test, insolvency test, and viability test.

3.2 Viability Test

The viability test pertains to the debtor's capacity to effectively address their financial distress and reach a satisfactory settlement with their creditors within a reasonable timeframe.81 This test is satisfied when there are 'economic reasons for the debtor to resume his business'.[82] In Case number 022/00563/2019/ (GARMCO),[83] the first successful – and most important[84] – reorganisation case in Bahrain, with debts reaching USD 81,000,000, the court appointed a temporary reorganisation trustee solely for the purpose of satisfying this test. The trustee's report concluded with the possibility of pursuing the path of reorganisation as a means

80. ibid art 6 (A)(1); Hisham Almansoor, 'An Overview of Bahrain's Bankruptcy Framework' (Mondaq, 13 April 2022) <https://www.mondaq.com/insolvencybankruptcy/1182506/an-overview-of-bahrains-bankruptcy-framework> accessed 15 June 2024; Amin and Billington (n 10).

81. Alfawzan (n 2) 118.

82. RBL 2018, art 17.

83. Case number 022019) 2/00563/2019/) (GARMCO).

84. GARMCO is considered a significant case due to its substantial debt and its impact on Bahrain's economy. Furthermore, it is the only reorganisation case in which the judgment and case documents have been published.

for the debtor to continue its activities and fulfil its debts.[85] Conversely, in case number 027/6322/2022/,[86] the trustee stated in his report that he was unable to reach a professional conviction supporting the viability of the plaintiffs continuing in a reorganisation process. He highlighted the reasons for his conclusion, citing the impossibility of generating financial returns from the company and the high value of the company's debts compared to its assets. Consequently, the court dismissed the reorganisation petition.

The viability test is crucial for several reasons. Primarily, it determines if a company can realistically continue operating, ensuring that restructuring efforts are not wasted on businesses with no chance of recovery. It has been argued that the viability test prevents 'zombie' companies from seeking the benefits of reorganisation proceedings.[87] A zombie company is defined as a business that consistently fails to generate sufficient profits and exhibits poor expected future growth potential, making them financially unsustainable in the long term[88] and have no chance to be rescued.[89] Moreover, the viability test aligns with the goals set out in RBL 2018, particularly the objective of 'Reorganizing the Debtor and avoiding liquidation wherever reasonably possible'.[90] The test ensures that reorganisation efforts are pursued only when there is a realistic chance of achieving this objective. By allowing only those companies with a genuine potential for recovery to enter reorganisation. This approach ensures that resources are effectively utilised, and that the reorganisation process remains focused on viable outcomes.

The next section undertakes a comprehensive analysis of the other two prerequisites for initiating the commencement of reorganisation proceedings under RBL 2018. The analysis draws insights from the reorganisation regimes in both the US and UK to provide a comparative perspective where relevant.

85. GARMCO (n 83) 2.
86. Case number 022022) 7/6322/2022/).
87. Alfawzan (n 2) 102.
88. Ryan Banerjee and Boris Hofmann, 'Corporate zombies: Anatomy and life cycle' (2020) Bank for International Settlements working paper 882 1,3.
89. Alfawzan (n 2) 102.
90. RBL 2018, art 3.

3.3 Good Faith Test

The good faith test is a pivotal principle in bankruptcy proceedings, ensuring that the debtor's intentions are genuine and honest when filing for reorganisation or bankruptcy. The good faith test scrutinises the motivations and behaviour of the debtor. This test aims to prevent the misuse of the bankruptcy process by ensuring it is accessed only by those who sincerely seek financial rehabilitation.

As bankruptcy courts function as courts of equity, they are not intended to be used as a 'sword against creditors'.[91] Therefore, a debtor should not be allowed to file for reorganisation with the sole purpose of obstructing a creditor's attempts to enforce their rights under bankruptcy law.

The rationale for this test stems from the fact that reorganisation is a process that aims to help the troubled debtor get out of their crisis and prevent collapsing and a cessation of activity. This benefit should only be granted to traders whose acts are marked by honesty and integrity.[92] It inhibits the abuse of the reorganisation law's protection.

The good faith test has been fairly assessed under RBL 2018 and US Chapter 11, as discussed below.

3.2.1 US Perspective

Chapter 11 bankruptcy proceedings include an implicit requirement of good faith, which, though not explicitly stated in the code, is a well-established principle in judicial practice and legal commentary.[93] To obtain a successful petition for restructuring under Chapter 11, a fundamental condition must be met: the requirement of good faith.[94]

Courts have developed various interpretations and tests to assess whether this condition is met, with one notable example being the objective–

91. Carlos J. Cuevas, 'Good Faith and Chapter 11: Standard That Should Be Employed to Dismiss Bad Fait Chapter 11 Cases' (1993) 60 Tenn L Rev 525, 531

92. Salem bin Salam bin Humaid Al-Faliti, 'The Role of Restructuring in Saving Projects and Commercial Companies in The Omani Bankruptcy Law: An Analytical Study' (Arabic) (2019) Journal of the College of Law for Legal and Economic Research-Alexandria University 2 1127,1208.

93. Cuevas (n 91) 525; Diane B. McColl, 'Good Faith in Chapter Eleven Reorganizations' (1984) 35 S C L Rev 333, 333.

94. McCormack, 'Corporate Rescue Law in Singapore and the Appropriateness of Chapter 11 of the US Bankruptcy Code as a Model' (n 15); Ali M. M. Mojdehi & Janet Dean Gertz, 'The Implicit Good Faith Requirement in Chapter 11 Liquidations: A Rule in Search of a Rationale' (2006) 14 Am Bankr Inst L Rev 143, 144.

subjective test used in the case of Carolin Corp. v. Miller,[95] which evaluates whether the specific reorganisation case's goals align with the principles underlying Chapter 11.[96]

The objective–subjective test comprises two key components. The objective part evaluates the debtor's ability to reorganise effectively.[97] This means that the court examines whether there is a reasonable likelihood that the debtor can successfully restructure its obligations and continue operations. For instance, the court assesses the debtor's financial situation, the viability of its business model, and the feasibility of its proposed reorganisation plan. If the debtor lacks a genuine ability to reorganise, it may be deemed to have filed in bad faith, as the filing would appear to be a strategic move to delay creditors or gain an unfair advantage rather than a sincere effort to reorganise.

The subjective part of the test focuses on the intentions behind the filing.[98] This component seeks to prevent the abuse of Chapter 11 by ensuring that the debtor's motives align with the fundamental purposes of the bankruptcy code. The court examines the debtor's conduct and intentions to evaluate whether the filing is intended to achieve a genuine reorganisation or is a tactical manoeuvre to impede creditors, avoid obligations, or pursue a hidden purpose. Overall, the subjective test examines the debtor's honesty and ability to reorganise, ensuring that the filing is not a mere façade for improper purposes.[99]

The court in Carolin Corp emphasised the objective–subjective test effectively balanced the competing interests of debtor rehabilitation and creditor protection, ensuring that a debtor's opportunity to reorganise was not prematurely jeopardised.[100]

Another notable case exemplifying these principles is SGL Carbon Corporation[101]. In this case, the court dismissed SGL Carbon Corporation's Chapter 11 petition, concluding that the company lacked a 'genuine reorganizational purpose'. The court found that the filing was not driven by the need to restructure its business operations and financial obligations but

95. 886 F.2d 693 (4th Cir. 1989).
96. Cuevas (n 91) 530.
97. Cuevas (n 91) 530.
98. ibid.
99. ibid.
100. ibid 531.
101. 200 F3d 154 (3rd Cir 1999).

was instead a strategic move to gain leverage in pending antitrust litigation. This decision highlighted the court's commitment to maintaining the integrity of the bankruptcy process by ensuring that Chapter 11 petitions are filed in good faith, with an honest intent to reorganise.
Additionally, in In re Little Creek Dev. Co.,[102] where the court emphasised that bankruptcy courts must consider whether the debtor's filing is an honest attempt to reorganise or merely an attempt to delay and manipulate the legal process
US Bankruptcy courts also have often dismissed cases for lack of good faith when the debtor is not an ongoing business. Chapter 11's primary purpose is to rehabilitate troubled businesses.[103] Therefore, reorganisation proceedings are unnecessary if there is no viable business to protect. In addition, another factor bankruptcy courts consider is the debtor's conduct. For instance, in In re Andrews[104] the court found the debtor lacked 'that candor, frankness, sincerity and willingness to do equity which are the indicia of good faith'.[105] Moreover, evidence of bad faith includes false statements to the court, failure to maintain books or records, unexplained absences from court hearings.[106] Furthermore, filings that lack good faith typically include organisations with no employees, little or no cash flow, and no available sources of income to support a reorganisation plan.[107]
In summary, the implicit good faith requirement in Chapter 11 bankruptcy ensures that filings are made with genuine intent to reorganise viable businesses, preventing misuse of the bankruptcy process for dishonest purposes.

3.2.2 Bahrain perspective

One notable requirement of RBL 2018 is that it requires the reorganisation petition be filed in good faith. While despite the word good faith is not explicitly mentioned in RBL 2018, The good faith requirement is clearly integrated in many in RBL 2018 articles.,

102. In re Little Creek Dev. Co., 779 F.2d 1068, 5th Cir. 1986.
103. McColl (n 93) 345.
104. 17 B.R. 515 (Bankr. C.D. Cal. 1982).
105. McColl (n 93) 346.
106. In re Verrazzano Towers, Inc., 10 B.R. 387 (Bankr. E.D.N.Y. 1981); In re Pappas, 17 B.R. 662, 667 (Bankr. D. Mass. 1982); McColl (n 93) 346.
107. In re Little Creek Dev. Co. (n 102).

For example, Article 31 (A-2) grants the insolvency court the authority to decline a reorganisation case if it lacks a 'lawful purpose for bankruptcy', a principle seems to be derived from the US perspective of good faith requirement as discussed above. Article 2 exemplifies the 'lawful purpose', emphasising integrity, transparency, and efficiency in utilising bankruptcy proceedings. Additionally, Article 23 (E) empowers the court to prevent abusive exploitation of bankruptcy proceedings.

To uphold the principle of good faith in the proceedings, RBL 2018 implements stringent punitive measures to prevent abuse of the bankruptcy process. Parties may face fines of up to BD 100,000 and a maximum imprisonment term of two years If found to have filed the bankruptcy petition with any of the following.[108]

1. Deliberately conceals of all or part of his property or exaggerates its value in order to be entitled to a procedure under the Bankruptcy Proceedings;
2. Deliberately allows a creditor who is untrue, or not permitted to participate in the Bankruptcy Proceedings or exaggerates his debts to participate in the deliberations and voting or deliberately allows him to take part;
3. Deliberately omits a creditor from the list of creditors;
4. Deliberately exaggerates his debts;
5. Participates in the Reorganisation deliberations or voting knowing he is legally prohibited from doing so;
6. Knowingly concludes a secret contract granting him special privileges to the prejudice of other creditors;
7. Is not a creditor and knowingly participates in Bankruptcy Proceedings as a creditor;
8. Pays debts to some creditors or provides them with a security right with the intention of causing prejudice to others and as a consequence becomes unable to settle their debts in full;
9. Fraudulently increases the Debtor's liabilities or decreases the value of his estate;
10. Knowingly submits to the Court or the Bankruptcy Trustee false or misleading information;
11. Deliberately conceals from the Court or the Bankruptcy Trustee any

108. RBL 2018, art 19293-.

data, information, registers or documents that must be presented to them or deliberately prevents them from having access to the said information and documents;

12. Knowingly presents an untrue claim against the Debtor or fraudulently exaggerates the value of his claim;

Many of the behaviours mentioned above serve as indicators of bad faith that debtors or other parties may exhibit during bankruptcy proceedings. RBL 2018 addresses such conduct with strict punitive measures aimed at preventing the abuse of the bankruptcy process.

Moreover, the bankruptcy court can impose fines up to BD 20,000 on the party who presented a petition with the intention 'of obstructing or delaying the Bankruptcy Proceedings without lawful justification, for an illegal purpose, deliberate fabrication of bankruptcy… or exploiting the bankruptcy proceedings in an abusive manner'.[109] These provisions underscore the importance of good faith and discourage misuse of the reorganisation process.

3.2.2.1 Good Faith in Judicial Application

Good faith requirement has been fairly tested in Bahraini courts through various cases, demonstrating the judiciary's commitment to upholding the integrity of bankruptcy proceedings. This section will discuss such cases, illustrating how the courts have interpreted and applied the principle of good faith within the framework RBL 2018

3.2.2.1.1 Lawful Purpose Test

Bankruptcy courts have applied the 'lawful purpose' test to determine whether the bankruptcy petition is filed with good faith. for instance, in case number 022/16940/22023/, the debtor sought the protection of RBL 2018 by filing a reorganisation petition stating that his debts exceed BHD 4,000,000. The court, however, before ruling on the plaintiff's request to initiate bankruptcy proceedings, decided to appoint a temporary bankruptcy trustee. In his report, the trustee reached several conclusions, one of which was that the plaintiff company was 'not serious about filing for bankruptcy'. This assessment was based on the company's failure to provide the necessary documents, an accurate list of creditors and debtors,

109. RBL 2018, art 21.

and a complete overview of its assets and liabilities. Consequently, the trustee and the court were unable to accurately determine the company's true financial status and decide whether to initiate the proceedings.
Furthermore, the trustee noted inconsistencies in the statements made during a meeting attended by the company's owners. In this meeting, the partners revealed that the company had no operational activities and had laid off all its employees in 2021. Based on these findings, the trustee recommended rejecting the bankruptcy petition, asserting that it was filed in violation of Article 12 and Article 31 of RBL 2018, as it did not serve a legitimate purpose for bankruptcy. The court, satisfied with the trustee's report findings, ruled to dismiss the case.
In similar case, 027/6322/2022/, the bankruptcy trustee recommended dismissing the case for several reasons, one of which is the debtors' lack of transparency and cooperation with the trustee and the court, as it as it did not serve a legitimate purpose for bankruptcy.

3.2.2.1.2 Subjective Test

A notable case, 025/03954/2019/, has implemented the subjective test, which focuses on the debtor's intentions. In such a case, two creditor field a motion to the court requesting the imposition of a fine on the debtor and the publication of this fine for 'intentionally' fabricating a state of bankruptcy' based on Article 21 which stipulates:
The Court at its own motion or upon the request of any interested Person shall be entitled to fine a sum up to twenty thousand Bahraini Dinars on the party who presented a petition or a demand in accordance with this Law with the intention of obstructing or delaying the Bankruptcy Proceedings without lawful justification, for an illegal purpose, deliberate fabrication of bankruptcy, harming the Debtor's reputation or exploiting the Bankruptcy Proceedings in an abusive manner. The Court shall be entitled to order the publication of the fining decision at the expense of the convicted party in one or more daily newspaper of wide circulation in or outside the Kingdom, in Arabic or in a foreign language.
The court in determining the bad intention of the debtor used a subjective test referring to the general principle of the Civil Law 2001[110] in exercising rights. Article 28 of Civil Law 2001 states that the exercise of a right in

110. Civil Law 2001.

a lawful manner does not entail liability, even if it causes harm to others. However, the exercise of a right is considered unlawful in certain cases, such as when the sole intention is to harm others, or when the interests sought to be achieved are of little importance compared to the harm caused to others, or when the interests or benefits sought to be achieved are unlawful.

The Court also referred to the Court of Cassation ruling that the right to litigate is one of the legitimate rights that should be protected for everyone. Therefore, a person who seeks justice in court for a legitimate right should not be questioned, unless it is proven that they have deviated from the legitimate right to engage in malicious litigation, seeking to harm the opponent. The court's assessment of abuse and excess in the exercise of one's right is a matter within the court's discretion.[111]

Considering the above, the court applied such principles applying to RBL 2018, requires the presence of an 'unlawful motive and cause' in the debtor's lawsuit, along with the establishment of 'bad faith' by the debtor. This bad faith leads to deviating from the legitimate right and entering the realm of abuse of rights. However, the court concluded that the debtor filed his bankruptcy lawsuit believing in its validity, based on the documents he had available and included in his lawsuit. The court used its authority to investigate this matter and ultimately rejected his bankruptcy petition. Therefore, there is no evidence that the debtor had the 'intent to harm' or 'abuse the interveners or to engage in malicious litigation against creditors', which would justify imposing the prescribed fine on him. Consequently, the court decided to reject creditors request to impose the fine against the debtor.

The cases discussed above clearly demonstrate that filing a reorganisation petition with indicators of bad faith can lead to the dismissal of the bankruptcy petition. Key indicators of bad faith include a lack of transparency and cooperation, dishonesty, malicious intent, false statements, the absence of employees, and minimal or no cash flow.

3.2.2.2 Comparative analysis

The good faith requirement in RBL 2018 closely parallels the principles observed in US Chapter 11 bankruptcy proceedings. Both jurisdictions

111. Cassation number 2522010) 2010/)

emphasise the necessity of genuine intent and honesty in bankruptcy filings to prevent manipulative abuses of the process. In Chapter 11, the good faith test, illustrated by cases such as Carolin Corp. v. Miller, includes both objective and subjective assessments to evaluate the debtor's true intent to reorganise. This involves examining whether the debtor has a reasonable likelihood of successfully restructuring and whether their filing aligns with the fundamental purposes of the bankruptcy code. Similarly, Bahrain's RBL 2018, while not explicitly mentioning 'good faith', integrates this requirement implicitly through various articles as discussed.

For instance, Article 31 (A-2) of RBL 2018 empowers the court to dismiss reorganisation cases lacking a 'lawful purpose for bankruptcy', reflecting a similar judicial oversight to that in the Chapter 11, where courts assess the sincerity and legitimacy of bankruptcy petitions. Furthermore, stringent punitive measures in Bahrain for bad faith actions, such as fines up to BD 100,000 and imprisonment for up to two years for deceptive practices, align with the U.S. approach to maintaining the integrity of bankruptcy proceedings. Furthermore, in In re Andrews, the US court identified bad faith through indicators such as false statements and failure to maintain accurate records, leading to dismissal of the bankruptcy case. Bahrain's RBL 2018 similarly addresses such conduct, with strict penalties for actions like concealing property, exaggerating debts, or submitting false information, thereby reinforcing the necessity of good faith.

Moreover, Bahrain's judicial application of the lawful purpose test to determine good faith in bankruptcy petitions, as seen in cases like 022/16940/22023/, demonstrates a parallel to the US application of subjective tests. This ensures that debtors' filings are sincere attempts at reorganisation rather than strategic moves to delay creditors or gain unfair advantages. In both jurisdictions, the courts scrutinise the debtor's conduct and intentions, emphasising the need for honesty and genuine reorganisation efforts to uphold the integrity and fairness of the bankruptcy process.

Overall, both Bahrain and the US prioritise the principles of integrity, transparency, and genuine intent in their bankruptcy proceedings, ensuring that the protections of Chapter 11 and RBL 2018 are reserved for those with legitimate needs and purposes. This alignment reflects

a shared commitment to preventing the abuse of bankruptcy laws and ensuring that debtors seeking reorganisation are doing so with honest intentions and a realistic plan for financial recovery.

The good faith perquisite is also fundamental in the assessment of the insolvency test, discussed in the following section. In summary, the adoption of the good faith requirement under RBL 2018 is justified.

3.3 Insolvency Test

The requirement of insolvency as a prerequisite for utilising such procedures is an important issue to consider while investigating the commencement of reorganisation proceedings. The RBL 2018 interconnection of reorganisation procedures and the bankruptcy petition, as discussed earlier, exemplifies the mandate for the debtor's insolvency condition as a prerequisite to commence bankruptcy proceedings and trigger reorganisation measures, including the moratorium. As such, reorganisation proceedings cannot be commenced unless the court is satisfied that the debtor is currently or potentially insolvent. A debtor is considered insolvent under the following conditions:

1. Where the Debtor fails to pay his debts within thirty days from the date his debts are due or will be unable to pay on the maturity dates;
2. Where the value of the financial liabilities exceeds the value of assets.[112]

It is evident from this article that RBL 2018 requires both a 'cash flow' and a 'balance sheet' test[113] to deem the debtor insolvent. The cash flow test assesses the debtor's ability to meet its current financial obligations as they come.[114] Conversely, the balance sheet test evaluates the overall financial health by comparing total liabilities to total assets.115 If liabilities exceed assets, the debtor is considered insolvent, providing a longer-term perspective on the debtor's financial stability.

In both tests, debtors are declared unable to pay their debts when they fail to pay on the due date and the entire debt is not subject to a lawful dispute

112. RBL 2018, art 6 (A)(1)(2).

113. Finch and Milman (n 6) 119; UNCITRAL (n 17) 5960-; Abdulrahim Khalaf-Allah Mohamed Ali, The Saudi Bankruptcy System: An Analytical Study Compared to The Bankruptcy Systems in The United States, England, and European Union (Arabic) (Law and Economic Library 2023) 47.

114. M. P. Ram Mohan, 'The Role of Insolvency Tests: Implications for Indian Insolvency Law' (2021) IIMA working paper 1,2.

115. ibid.

prior to filing for bankruptcy or subject to a set-off for the amount of the alleged debt.[116]

3.3.1 Assessing the Insolvency Test Requirement

3.3.1.1 Comparative Perspective

From a comparative standpoint, the insolvency test requirement in RBL 2018 appears to be consistent with the UK administration process that requires the debtor to be insolvent.[117] However, it diverges from other UK reorganisation regimes, namely SoA, CVAs, Part 26A scheme and Stand-Alone moratorium which all do not mandate an insolvency test, as has been discussed earlier in Section 2.[118]

While despite being inspired by the US Chapter 11 provisions, the RBL 2018 adoption of insolvency test perquisite contrasts with Chapter 11 approach. Chapter 11 does not require that the debtor be insolvent or near insolvency to apply for protection.[119] Chapter 11 proceedings primarily serve as a tool for debtor relief rather than a remedy for creditors.[120] As has been discussed in the previous section, instead of an insolvency test, Chapter 11 safeguards against misuse through the dismissal of filings made in 'bad faith'.[121] Thus, a debtor must pass a good faith test to commence the proceedings.

3.3.1.2 Analysing the Insolvency Test

When evaluating the rationale behind mandating an insolvency test, it becomes evident that the primary argument for this approach is to prevent the improper use of reorganisation proceedings.[122] This refers to situations where a financially stable debtor may file a reorganisation petition solely to exploit existing legal protections, particularly the moratorium. However, such justification is inadequate, as demonstrated by US Chapter 11, which safeguards creditors from such improper use by

116. RBL 2018, art 6 (B).
117. IA 1986, s 123.
118. Finch and Milman (n 6) 411; Jennifer Payne, Schemes of Arrangement: Theory, Structure and Operation (Cambridge University Press 2014) 196.
119. Isherwood (n 3) 131.
120. ibid.
121. Jay Lawrence Westbrook, Charles D. Booth, Christoph G. Paulus, Harry Rajak, A Global View of Business Insolvency Systems (Martinus Nijhoff Publishers 2010) 66.
122. UNCITRAL (n 17).

employing the good faith test to prevent such unfair practices.

Conversely, this approach entails several significant disadvantages. A significant critique of imposing the insolvency requirement in restructuring processes is that it impedes early attempts to rescue distressed businesses.[123] This imposition is argued to hinder companies from initiating rehabilitation procedures until the possibility of successful rescue is no longer feasible.[124] Early engagement in seeking rehabilitation during the initial stages of financial difficulties is crucial for the success of the rehabilitation process. However, the insolvency test may hinder such early rescue attempts.[125] As professor Westbrook noted, the criteria for commencing insolvency proceedings should facilitate convenient, cost-effective, and expeditious access to the laws.[126] If debtors willingly acknowledge their need for legal protection due to their financial condition or imminent financial failure, it remains uncertain whether the delays and expenses associated with an insolvency test will yield a commensurate benefit.[127] Such delays often lead to value erosion for both the debtor and its creditors, increasing the likelihood that a proposed rescue will culminate in liquidation.[128] Furthermore, creditors may anticipate a bankruptcy test if they become aware of the debtor's insolvency susceptibility. As a result, creditors may take steps to protect assets that would be allocated in an orderly and equitable manner in the case of bankruptcy.[129]

Considering the severe consequences associated with requiring an insolvency test, it is imperative to carefully evaluate this approach when contemplating reorganisation proceedings. Alfawzan argues that such an approach finds justification within the framework of the UK administration process, primarily due to the minimal court involvement in the administration procedure, which necessitates the imposition of the insolvency requirement to counter potential abusive use of the procedures.[130]

123. Gerard McCormack, Corporate Rescue Law: An Anglo-American Perspective (Edward Elgar 2008) 119.

124. Alfawzan (n 2) 115; Colin Anderson and David Morrison, 'The Commencement of the Company Rescue: How and When Does It Start?' in Paul J Omar (ed), International Insolvency Law: Themes and Perspectives (Ashgate Publishing Limited 2008) 92.

125. Alfawzan (n 2) 115.

126. Westbrook and others, A Global View of Business Insolvency Systems (n 121).

127. ibid.

128. ibid.

129. Anderson and Morrison (n 124).

130. Alfawzan (n 2) 116.

This minimal court involvement is represented in the Enterprise Act 2002, where various routes into administration were introduced. [131] Pursuant to the Enterprise Act 2002, the appointment of an administrator is now permissible either by the company itself or by a qualified floating charge holder outside the court process,[132] which minimises the court's authority over the reorganisation process. Conversely, Alfawzan also observes that such an approach may not be necessary under US Chapter 11, given the court-based nature of the proceedings and the judicial safeguard represented by the good faith requirement.[133] Moreover, one potential mitigating factor for the drawbacks associated with the insolvency test requirement under the UK administration regime lies in the existence of alternative formal restructuring procedures that do not require an 'insolvency test', notably the CVAs , SoA, Part 26A scheme and the Stand-Alone Moratorium, despite of their drawbacks.[134]
The aforementioned argument finds relevance within the Bahraini context as well, as discussed below:

3.3.1.1.1 Robust Safeguards Against Misuse

RBL 2018 offers substantial protection against the misuse of the reorganisation process through its stringent good faith requirements, and extensive court involvement, ensuring the integrity and effectiveness of the restructuring framework in Bahrain.

3.3.1.1.1.1 Good Faith Test

As has been previously discussed, RBL 2018 incorporates a stringent good faith requirement for the reorganisation process, serving as a robust safeguard against any potential improper use of the reorganisation proceedings. Notably, RBL 2018 enforces the good faith criterion more rigorously than does US Chapter 11. This rigorous enforcement is evidenced by the imposition of substantial punitive fines and other consequences by Bahraini courts, forming a strong deterrent against disingenuous debtors attempting to exploit the reorganisation process.
The RBL 2018's emphasis on good faith serves a dual purpose. Firstly,

131. McCormack, Corporate Rescue Law: An Anglo-American Perspective (n 123) 119.
132. ibid.
133. Alfawzan (n 2) 116.
134. ibid 117.

it ensures that only those debtors who genuinely seek to reorganize their businesses and meet their obligations are allowed to utilise the reorganisation process. This requirement acts as a filter to weed out any attempts to misuse the system for purposes such as delaying creditor actions or evading liabilities without a genuine intention to restructure. Secondly, it provides a level of protection and assurance to creditors, who can trust that the reorganisation process is being used appropriately and that their interests are being considered.

Unlike the RBL 2018, the US Chapter 11 bankruptcy code does not require an insolvency test for a debtor to initiate reorganisation proceedings. Instead, it relies on a good faith requirement, similar to the RBL 2018. This comparison underscores the sufficiency of the good faith test as a safeguard. The US experience demonstrates that rigorous enforcement of the good faith criterion can effectively prevent abuse without the need for an additional insolvency test.

Introducing an insolvency test on top of the good faith requirement could impose further hardship on debtors. The insolvency test requires a detailed assessment of the debtor's financial status, which can be time-consuming and resource-intensive. For debtors already in distress, meeting this additional criterion could delay access to the reorganisation process, potentially exacerbating their financial difficulties. Moreover, the insolvency test could create an unnecessary barrier for debtors who are on the verge of insolvency but still have a viable path to reorganisation if allowed to proceed promptly.

In contrast, the good faith requirement focuses on the debtor's intentions and plans for reorganisation rather than their current financial state. This approach allows for a more dynamic and responsive process, where the primary concern is whether the debtor genuinely intends to use the reorganisation process to address their financial issues and develop a feasible plan for recovery. By ensuring that the reorganisation process is reserved for those with legitimate intentions, the good faith test effectively protects against misuse without adding undue burden to the debtor.

overall, the rigorous enforcement of the good faith requirement under the RBL 2018 provides a robust safeguard against improper use of the reorganisation process. It ensures that only genuine and well-intentioned debtors can access the benefits of reorganisation, protecting creditors

and maintaining the integrity of the process. The comparison with the US Chapter 11 system further illustrates that a good faith test, when rigorously enforced, is sufficient to prevent abuse, making an additional insolvency test unnecessary and potentially counterproductive.

3.3.1.1.2 Court Involvement

Additionally, the reorganisation process under RBL 2018 is characterised by a profound reliance on court involvement, requiring court approval at almost every stage,[135] from the initiation of the proceedings to the final ratification of the reorganisation plan. This heightened level of court supervision acts as a deterrent against any misuse of the reorganisation process.[136] Under the RBL 2018, for example, the moratorium is not automatically triggered upon the filing of the reorganisation petition. Instead, the court must first evaluate all the prerequisites for opening the bankruptcy proceedings, including the moratorium. Only after this assessment can the moratorium take effect. This rigorous judicial supervision ensures that the debtor cannot easily manipulate the reorganisation process, as they must meet every court-mandated requirement.

3.3.1.2 Lack of Alternative Reorganisation Mechanism

Another factor supporting the argument against imposing the insolvency test is the lack of alternative formal reorganisation mechanisms in the Bahraini insolvency framework. Unlike the UK regime which offers procedures do not require the debtor to be insolvent such as the Company Voluntary Arrangement (CVA), Scheme of Arrangement (SoA), Part 26A scheme and the Stand-Alone moratorium. Consequently, distressed debtors in Bahrain have only one formal recourse: seeking protection under the reorganisation process governed by the RBL 2018.

While it can be argued that the RBL 2018 includes provisions allowing debtors to file a pre-packaged reorganisation petition without initiating bankruptcy proceedings, there are significant limitations. Firstly, the pre-packaged reorganisation still requires the debtor to be insolvent,

135. The sole exception to court approval arises when the insolvency trustee performs their mission within the ordinary course of business. See RBL 2018, art 23, 25.

136. RBL 2018, art 2324-.

either by ceasing to pay or having liabilities that exceed their assets.[137] Additionally, the pre-packaged reorganisation process heavily relies on creditors' willingness to voluntarily participate in the voting process, which is challenging to achieve, especially when dealing with multiple creditors.

Furthermore, this mechanism lacks a moratorium during the negotiation process, meaning that creditors can continue to take actions against the debtor while negotiations are ongoing. As a result, it is not surprising that the pre-packaged reorganisation mechanism has yet to be tested in Bahraini courts.

In comparison to the UK insolvency framework, the limitations of the Bahraini system are evident. The absence of multiple reorganisation options means that debtors have less flexibility in addressing their financial distress and ultimately must be insolvent to seek protection under RBL 2018. In the UK, however, the diverse reorganisation mechanisms provide a range of tools that can be tailored to the specific circumstances of the debtor. This offers a more nuanced approach to insolvency and mitigates the consequences of requiring an insolvency test in the UK Administration process.

3.3.1.3 Harmonising with Supranational Recommendations

Imposing the insolvency test in the reorganisation process is contrary to supranational recommendations, notably those from UNCITRAL and the International Monetary Fund (IMF). Although RBL 2018 is based on UNCITRAL principles, it diverges from these recommendations by maintaining the insolvency test for the commencement of reorganisation proceedings.

The UNCITRAL recommendations emphasise that the reorganisation process should enable debtors to address financial difficulties at an early stage.[138] To this end, the commencement process should be more flexible than that of liquidation, allowing debtors to seek protection before they reach the point of actual cessation of payments.[139] Additionally, UNCITRAL stresses the importance of focusing on discouraging improper use of reorganisation proceedings rather than making the commencement

137. RBL 2018, art 124.
138. UNCITRAL (n 14) 53.
139. ibid.

process more burdensome.[140] This objective can be achieved by granting the relevant court the power to deny any petition conducted with the intention of improper use, which aligns with the good faith test imposed in RBL 2018.[141]

Additionally, the International Monetary Fund (IMF) emphasises that the primary economic objective of reorganisation procedures is to transform financially distressed enterprises into competitive and productive participants in the economy, benefiting all stakeholders involved. To achieve this, the features of these procedures must be sufficiently attractive to encourage debtors to initiate proceedings early in their financial difficulties, thereby increasing the chances of successful rehabilitation. In consistent with this objective, the IMF recommends that is appropriate to design a commencement criterion that does not require the debtor to wait until it has ceased making payments (i.e., until it is illiquid) before starting rehabilitation proceedings.[142] Many countries have recognised the value of this approach, though they implement it in different ways.
The IMF recommendations further elaborate on this point, noting that a more relaxed commencement criterion could potentially be misused by debtors. However, the potential for such abuse largely depends on the design of other elements within the rehabilitation procedure.
Despite these international guidelines, the Bahraini insolvency framework imposes an insolvency test, which requires debtors to demonstrate insolvency before they can seek reorganisation under RBL 2018. This requirement stands in contrast to the flexible and preventive approach recommended by UNCITRAL and the IMF. By insisting on the insolvency test, the Bahraini framework potentially delays the initiation of reorganisation proceedings, thereby reducing the chances of successful rehabilitation and increasing the likelihood of liquidation.
UNCITRAL's recommendations suggest that insolvency laws should concentrate on discouraging improper use of reorganisation proceedings. This can be effectively achieved by empowering the courts to reject petitions made in bad faith. The good faith requirement in RBL 2018

140. ibid 54.
141. ibid.
142. IMF, Orderly & Effective Insolvency Procedures (International Monetary Fund 1999).

serves this purpose well, acting as a robust safeguard against the improper use of reorganisation proceedings. However, retaining the insolvency test contradicts the overarching goal of facilitating early intervention and flexible access to reorganisation, as emphasised by UNCITRAL and the IMF.

In summary, while RBL 2018 incorporates significant safeguards to prevent the misuse of reorganisation proceedings, its insistence on an insolvency test diverges from supranational recommendations. To better align with UNCITRAL and IMF guidelines, the Bahraini insolvency framework could benefit from eliminating the insolvency test and focusing instead on ensuring that reorganisation proceedings are initiated in good faith. This would enhance the flexibility and effectiveness of the reorganisation process, ultimately improving the prospects for the successful rehabilitation of financially distressed companies.

3.3.1.4 Excessive Burdensome

Another significant concern supporting the argument for the exclusion of the insolvency test within the framework of RBL 2018 pertains to the excessively high burden of proof it places on the debtor. Article 12(A) and judicial application mandates that the debtor furnish a substantial amount of evidence to meet the requirements for opening bankruptcy proceedings. These requirements encompass:

1. Financial statements/reports of the claimant company, or commercial ledgers, or any documentation proving activity for the three years preceding the filing date of the bankruptcy petition, in addition to the year in which the petition was filed up to the filing date.
2. Audited reports based on sound accounting principles must be submitted; internal reports are not accepted.[143]
3. Financial reports for each branch of the company/institution must be provided, as the cease of payment or distress of one branch does not necessarily mean the cease of payment or distress of the other branches. Moreover, the activity and revenue of any branch will reflect on the entire group, especially if the branches engage in diverse and different activities rather than a single field.[144]

143. Case number 022021)7/11296/2021/); Case number 022021)4/10045/2021/).

144. Case number 022021) 6/12974/2021/).

4. Bank statements for all company accounts with banks for the three years preceding the petition and for all branches of the company/ institution.
5. A list detailing the types of debts (commercial, personal, secured, unsecured) and the due date for each debt.
6. A list of the company's owned assets and funds (cash, real estate, movable assets such as company furniture, etc.) and a report containing information about these assets, their nature, and their valuation.[145]
7. A list of assets excluded from the bankruptcy estate.
8. Documentation indicating the company's cessation or inability to pay within 30 days from the due date, or that it will be unable to pay, or that its financial obligations exceed its assets according to Article 6, and the date of the last payment made to each creditor.
9. Any documents showing the company's activity and contracts for the three years preceding the filing of the petition or cessation of activity.
10. A list detailing the names of creditors, including their email addresses and phone numbers, the total amount owed to each, the due date, and the nature of the debt (secured or unsecured, mortgaged, guaranteed, or privileged if applicable).
11. A list of the names of the company's debtors, their email addresses, and phone numbers if available, the total amount owed by each, the due date, and the nature of the debt (secured or unsecured, mortgaged, guaranteed, or privileged if applicable).
12. A list of all current and former employees, the amounts due to them if any, the total amount due to all employees, and their identification numbers.[146]
13. Translation of all documents into Arabic.

This requirement for extensive evidence has proven problematic, As evidenced by the rigid approach adopted by the courts in cases where the prescribed documents were not satisfactorily presented to meet all requirements.

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145. Case number 022021) 5/18461/2021/).
146. Case number 022023) 6/5577/2023/).

As seen above, court applications have developed more rigid requirements, such as the submission of comprehensive audited financial reports and bank statements for all branches of the parent company, even those not involved in the bankruptcy case. The same applies to all branches of individual establishments, regardless of their direct involvement in the bankruptcy proceedings. These requirements are not only exhaustive but also exceptionally expensive and burdensome for the debtor.

Despite RBL 2018 permits the court a level of authority to initiate bankruptcy proceedings even without meeting the document requirements.[147] However, the courts have applied a very rigid approach, rarely exercising this discretionary power.

In fact, this research included an empirical study involving quantitative analysis of 66 published bankruptcy cases.[148] The findings revealed that 87% of these cases were rejected. Of these rejected cases, 78% were due to the failure to submit all required documents and the inability to prove the insolvency status necessary for commencing bankruptcy proceedings, whether through liquidation or reorganisation.[149] This highlights

147. RBL 2018, art 7: 'If the court decides not to meet the requirements stipulated in paragraph (A) of this article, it must notify the plaintiff of the deficiencies and provide a reasonable opportunity to correct or complete them. Otherwise, the court may dismiss the claim, proceed with the case as filed, or issue the decision it deems appropriate.'

148. According to published bankruptcy cases from the Ministry of Justice and the Supreme Judicial Council. See --, 'Bankruptcy Cases' (Ministry of Justice, Islamic affairs and Waqf) <https://www.moj.gov.bh/ar/communication-guide-arb-6> accessed 15 June 2024; --, 'Judgments of Lawsuits in Commercial Disputes' (Supreme Judicial Council, 2024) < https://ahkamtejaria.sjc.bh/ > accessed 15 June 2024.

149. See. e.g. case number 022019) 1/06095/2019/); case number 022019) 8/10764/2019/); case number 022019) 9/14061/2019/); case number 022019) 8/16113/2019/); case number 022020) 8/03064/2020/); case number 022020) 8/06305/2020/); case number 029/12434/2020/2020)); case number 022020)1/5362/2020/); case number 022020) 1/6415/2020/); case number 022021)4/10045/2021/); case number 022021) 6/12974/2021/); case number 025/17004/2021/2021)); case number 022021) 5/18461/2021/); case number 022021) 3/18462/2021/); case number 022021) 1/19452/2021/); case number 022021) 7/19494/2021/); case number 022022) 8/12421/2022/); case number 022022) 9/18239/2022/); case number 029/20511/2022/2022)); case number 022022) 3/20692/2022/); case number 022022) 2/21012/2022/); case number 022022) 8/21586/2022/); case number 022022) 4/5097/2022/); case number 022022) 9/8522/2022/); case number 022022) 9/9430/2022/); case number 029/0203/2023/2023)); case number 022023) 9/04328/2023/); case number 022023) 6/5577/2023/); Case number 92023) 02/2023/10010/); Case number 82023) 02/2023/08042/); Case number 22023) 02/2023/9664/); Case number 82023) 02/2023/17534/); Case number 502/2024/1369/2024)).

the excessive burden placed on debtors to provide comprehensive evidence, often leading to the rejection of their petitions. In fact, only two reorganisation petitions being approved for the commencement of bankruptcy proceedings,[150] despite RBL 2018 having existed for more than six years.

While some of these required documents are crucial for determining various tests imposed by RBL 2018, such as the good faith test, viability test, the idea here is not to challenge the validity of all these documentation requirements. Rather, the argument is that imposing an insolvency test and its burden on top of this excessive burden significantly hinders debtors. As discussed above, the insolvency test prevents early reorganisation attempts, lacks justification within Bahrain's insolvency framework, and contradicts supranational recommendations. Consequently, the necessity to prove insolvency, coupled with the demand for extensive documentation, creates an almost insurmountable barrier for debtors seeking relief through reorganisation proceedings, making the process overly complex and inaccessible. Moreover, the exclusion of the insolvency test would also reduce the heavy burden on debtors, especially those required to provide audited financial reports for the entire corporate group, including all branches. This change would streamline the process, allowing for earlier and more effective intervention in financial distress cases, aligning Bahrain's insolvency framework more closely with international best practices.

It could be argued that the RBL 2018 considers a debtor insolvent if he is 'unable to pay on the maturity dates'. However, this potential insolvency test has not yet been tested in courts. Given the rigid application of the law by the courts, as discussed above, it is neither promising nor clear how the courts will interpret this concept.

Based on the aforementioned arguments, it can be deduced that the 'insolvency' requirement stipulated in RBL 2018 functions as a severe impediment to debtors seeking protection through reorganisation proceedings. This hindrance prevents early rescue attempts and imposes additional burdens, making the reorganisation process unattractive for

150. GARMCO (n 83); case number 022019) 9/03349/2019/).

businesses.[151] Moreover, the insolvency requirement lacks justification within the framework of RBL 2018, given the court-based nature of the proceedings, and the robust good faith test, both of which adequately safeguard against any potential improper use. In addition, the requirement of the insolvency test contradicts supranational recommendations, which promote a more lenient requirement than liquidation. This requirement also puts a heavy burden on debtors, further complicating their efforts to seek relief through reorganisation proceedings. Consequently, the author consequently recommends a more lenient approach to the commencement of reorganisation processes under RBL 2018, with the exclusion of the insolvency test.

4. A Lenient Approach: Financial Difficulty Approach

A question may arise regarding what alternative approach could be used instead of the insolvency test. By considering the comparative aspect of this research, which entailed observing UK and US reorganisation mechanisms, the Bahraini insolvency framework could benefit from these systems. RBL 2018, as discussed earlier, is similar to the US Chapter 11 approach in imposing the good faith test, which serves as a robust guard against any misuse of the reorganisation process.

From the UK perspective, which includes various reorganisation regimes that do not require insolvency status, such as the CVAs, SoA, Part 26A scheme, and the Stand-Alone Moratorium, one mechanism stands out: the Part 26A scheme. This scheme includes a ‘financial difficulty’ approach rather than a ‘financial distress’ approach.

Financial difficulty refers to a situation where a company is experiencing problems with its finances, such as reduced cash flow and increased debt. It is often a preliminary stage and can be manageable with corrective actions such as reorganisation. On the other hand, financial distress is a more severe condition where a company is struggling to meet its financial obligations and is at risk of defaulting on its debt, which is essentially the insolvency status.

151. Aurelio Gurrea-Martínez, ‘Insolvency Law in Emerging Markets’ (2020) Ibero-American Institute for Law and Finance working paper 312 ,2020/ <https://ssrn.com/abstract=3606395> accessed 1 July 2024.

Financial difficulties can be identified through several key indicators that align with international accounting standards,[152] beyond the traditional insolvency tests such as the payment cease and balance sheet test. Firstly, a significant increase or decrease in the project's debt ratio signals potential financial difficulty. This can be accompanied by a continuous reliance on short-term financing to cover commercial expenditures, highlighting a shortfall in the project's ability to manage its finances sustainably. Additionally, if the project frequently resorts to debt rescheduling and extends repayment periods multiple times, this indicates ongoing financial challenges. Another critical indicator is a consistent rise in inventory levels, which may suggest sales decline. A substantial drop in company sales and a decrease in overall project profitability are also clear signs of financial strain. Moreover, signs of weakened management capability to adapt to different economic conditions further exacerbate the financial difficulties faced by the project.[153]

As seen in Re DeepOcean, the UK court provided a significant precedent for assessing the 'financial difficulty' approach. The court emphasised that for condition A to be met, the current or expected financial difficulties must be 'sufficiently serious' to give rise to the likelihood that the company will be unable to continue operations as a going concern. This standard ensures that only those companies facing genuinely severe financial distress, which threatens their ongoing viability, are eligible for reorganisation protection.

In this particular case, despite the parent company not being in a state of ceased payments nor its affiliates (the applicant companies), it faced financial constraints that jeopardised its ability to continue providing the necessary support without risking its own financial stability. The court found that the financial difficulties of the applicant companies, exacerbated by the parent company's inability to sustain financing, sufficiently demonstrated a threat to their ability to operate as a going concern. Consequently, the court concluded that condition A was satisfied, allowing the companies to benefit from the reorganisation process.

152. Hayam Abdulghani Yousif Mohamed, 'Restructuring of Troubled Commercial Projects' (Arabic) (2023) 42 Legal & Scholar Research Journal 753,7634-.
153. ibid.

This approach highlights the flexibility and practicality of assessing financial difficulty rather than strictly requiring insolvency. By focusing on the seriousness of financial distress and its impact on a company's viability, the court enabled companies that had not yet ceased payments to access the reorganisation process. This proactive stance allows for earlier intervention, potentially preventing liquidation and preserving value.

Adopting a similar 'financial difficulty' approach within Bahrain's RBL 2018 could offer substantial benefits. Currently, RBL 2018's requirement for demonstrating insolvency imposes a significant burden on debtors, often delaying intervention until the financial situation has deteriorated to a critical point. This delay can lead to value erosion, as will be seen in the case of Awal Gulf Manufacturing (AGM), where the requirement to prove insolvency before seeking protection contributed to the company's eventual liquidation.

4.1 A Working Example: Awal Gulf Manufacturing (AGM)

A notable example supporting the 'financial difficulty' approach as an alternative to the insolvency test within the framework of RBL 2018 is the current situation of Awal Gulf Manufacturing (AGM). AGM is a leading HVACR manufacturing company based in the Kingdom of Bahrain since 1970, serving customers in more than 40 countries globally. Recently, AGM announced that it has filed a lawsuit before the Bahraini courts for the liquidation and bankruptcy of the company and its complete closure.[154] AGM stated that the decision to liquidate and completely close the company came against the backdrop of 'financial difficulties' the company started facing with local banks since 2018, due to debts amounting to approximately 49 million Bahraini dinars. Despite AGM reaching a settlement regarding its debts with creditor banks, the company was forced into liquidation and closure after local banks reneged on the previously agreed-upon debt reduction. consequently, AGM has announced the layoff of more than 760 employees.

The situation of AGM exemplifies the potential benefits of adopting a 'financial difficulty' approach instead of an insolvency test within the framework of RBL

154. Tamam Abu-Safi,'"Awal Al Khaleej" is heading towards liquidation and complete closureTop of Form Bottom of Form' (Alayam, 1 Feb 2024) <https://alay.am/p/7ux3> accessed 1 July 2024.

2018. If the RBL 2018 had included provisions to protect companies experiencing financial hardship before reaching insolvency, AGM might have had the opportunity to implement a formal reorganisation process, rather than being forced into liquidation.

AGM needed official legal protection to facilitate its out-of-court settlement and ensure that the agreements made with creditors were enforceable. The financial difficulties that AGM experienced with local banks since 2018 indicate that the company was facing financial difficulties long before it filed for liquidation and become insolvent. However, without a legal framework that recognises financial difficulty as a valid criterion for initiating reorganisation, AGM had no formal means to seek protection and restructure its debts under Bahraini law. The requirement to prove insolvency as a precondition for reorganisation effectively barred AGM from accessing the necessary legal mechanisms to resolve its financial distress. Eventually, the delays and expenses associated with the insolvency prerequisite led to value erosion for AGM and resulted in its liquidation.

Had there been a formal reorganisation process available to AGM under RBL 2018, the company could have sought court approval for a reorganisation plan at an earlier stage, even before reaching the point of insolvency. This legal protection would have allowed AGM to negotiate with creditors under the supervision of the court, ensuring that the agreements reached were binding and could not be unilaterally altered by the banks. The enforcement of a reorganisation plan through the court would have provided AGM with the necessary breathing space to restructure its operations, reduce its debt burden, and avoid liquidation.

Moreover, the inclusion of a 'financial difficulty' criterion would align RBL 2018 with international best practices, as recommended by supranational bodies like UNCITRAL and the IMF. These organisations advocate for a flexible approach to reorganisation that allows companies to address financial difficulties early on, thereby increasing the chances of successful rehabilitation and minimising the need for liquidation. The insistence on an insolvency test not only contradicts these recommendations but also fails to provide a practical solution for companies like AGM that are struggling but not yet insolvent.

Regionally, the concept of 'financial difficulty' as a criterion for initiating reorganisation processes is increasingly being recognised as a practical and effective approach within the legal frameworks of Arab countries. This is evident in the Egyptian Restructuring, Preventive Composition and Bankruptcy Law 2018, and the Omani Bankruptcy Law 2019 which both have adopted 'financial difficulty' approach, facilitating earlier intervention before the status of insolvency and increasing the chances of successful rehabilitation.[155]

To sum up, Bahrain's RBL 2018 could significantly enhance its effectiveness by revisiting its insolvency requirement and considering the adoption of a 'financial difficulty' criterion. This change would not only align Bahrain's framework with aligning with international best practices and supranational recommendations and regional advancements but also improve the prospects for successful rehabilitation of distressed companies, thereby supporting economic stability and growth.

Conclusion

In conclusion, this article has delved into the commencement requirements for reorganisation proceedings under the RBL 2018, comparing them with counterparts in the US and UK legal frameworks. The primary focus has been on the insolvency test, a pivotal condition for initiating reorganisation proceedings in Bahrain. While the RBL 2018's good faith requirement and court-centric nature offer commendable safeguards against misuse, the imposition of the insolvency test has been scrutinised for its drawbacks.

The analysis has highlighted that the insolvency test, requiring debtors to prove their financial distress, poses significant impediments to early rescue attempts, burdens businesses with extensive evidentiary obligations, and, in practice, has led to a limited number of approved reorganisation petitions. This raises concerns about the test's relevance within the Bahraini context. Despite the insolvency test's potential relevance in UK administration proceedings, it is essential to note that the UK benefits from having multiple formal reorganisation mechanisms. Bahrain, however,

155.Al-Faliti (n 92) 1211; Ibrahim Ahmed El-Bastawisi, 'Restructuring According to Law No. 11 of 2018 Regulating Restructuring, Protective Composition and Bankruptcy "A Comparative Study with Some Arab Laws"' (Arabic) (2022) 25(2) Tfhna Al-Ashraf Law College Journal 975,10023-.

lacks any alternative formal reorganisation frameworks, making the insolvency test's application even more problematic.

Moreover, the imposition of the insolvency test in Bahrain contradicts supranational recommendations, which advocate for more flexible and debtor-friendly approaches to reorganisation. The rigid requirement to prove insolvency not only hampers the potential for early intervention but also places an undue burden on debtors, thereby reducing the likelihood of successful reorganisation attempts. This misalignment with international best practices suggests the need for a reassessment of the current legal framework.

Drawing parallels with the US Chapter 11 system, which relies on a good faith test rather than an insolvency test, this article argues for a more lenient approach to the commencement of reorganisation processes under RBL 2018. The recommendation is to omit the insolvency test while ensuring the rigorous application of the good faith standard. Such an adjustment would strike a balance between protecting debtors and preventing misuse, ultimately enhancing the efficiency and accessibility of reorganisation proceedings in Bahrain.

Furthermore, the article suggests adopting a financial difficulty test as an alternative to the insolvency test. This approach, already utilised in jurisdictions like UK, Egypt and Oman, would allow companies facing significant financial challenges to seek reorganisation without the onerous requirement of proving insolvency. Implementing a financial difficulty test would provide a more realistic and practical threshold for reorganisation, promoting early intervention and increasing the chances of successful business rescues.

In summary, the article advocates for a nuanced re-evaluation of the insolvency test within the RBL 2018 framework to better align with the unique features of the Bahraini legal landscape and foster a more robust and equitable insolvency regime. By adopting a financial difficulty approach, Bahrain can create a more supportive environment for struggling businesses, encouraging early reorganisation efforts and ultimately contributing to the country's economic stability and growth.

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