THE JUDICIAL AUTHORITY OF THE DUBAI INTERNATIONAL FINANCIAL CENTRE

In the name of His Highness Sheikh Mohammad Bin Rashid Al Maktoum, Ruler of Dubai

IN THE COURT OF FIRST INSTANCE

IN THE MATTER OF THE DIFC INSOLVENCY LAW NO. 7 OF 2004

BEFORE HIS HONOUR JUSTICE MICHAEL HWANG

FORSYTH PARTNERS GLOBAL DISTRIBUTORS LIMITED,

-and-

FORSYTH PARTNERS GROUP HOLDINGS LIMITED

-and-

FORSYTH PARTNERS (MIDDLE EAST) LIMITED

22 November and 25 November 2007

Judgment reserved

Judgment : [30 January 2007]

JUDGMENT

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1. There were three separate petitions before this Court pursuant to Article 71 of the Insolvency Law (DIFC Law No. 7 of 2004) ("Insolvency Law") by the joint liquidators, Mr. David John Dunckley and Mr. Stephen John Akers ("the Liquidators"), of Forsyth Partners Global Distributors Limited, Forsyth Partners Group Holdings Limited ("Forsyth") and Forsyth Partners (Middle East) Limited ("Forsyth Middle East') (collectively "the Petitioners" or "the Companies") seeking directions as to which debts of the respective Companies, if any, should be treated as preferential debts for the purposes of Article 67 of the Insolvency Law ("the Petitions"). In particular, the Liquidators sought the Court's directions in the context of various claims that had been lodged with the Court by former employees of the respective Companies.

2. In the respective Petitions filed by the Liquidators on behalf of the Petitioners on 20 November 2007, the Petitioners seek the direction of the Court, in connection with Article 67 of the Insolvency Law, as to whether any or all of:

(i) certain wage related claims (as set out in paragraph 9 of Schedule 6 of the English Insolvency Act 1986 ("Insolvency Act"));

(ii) certain claims for holiday pay (as set out in paragraph 10 of Schedule 6 of the Insolvency Act);
(iii) payments in lieu of notice; and
(iv) redundancy pay
can be deemed preferential debts for the purposes of Article 67 of the Insolvency Law (set out at paragraph 10).

3. It is clear that the Petitioners' employee claims are framed based on English insolvency law.

Background

4. The Petitioners are all companies registered in the DIFC and incorporated on 5 July 2005 under the Companies Law (DIFC Law No. 3 of 2006). Forsyth Partners Global Distributors Limited is a subsidiary of Forsyth. Mr. Paul Graham Forsyth is a director of all three Companies.

5. The Petitioners were carrying on financial services activities in Dubai. Forsyth and Forsyth Middle East both held financial services licences issued by the Dubai Financial Services Authority ("DFSA") as "Category 4" companies. These financial services licences authorised Forsyth and Forsyth Middle East to arrange credit or deal in investments and to advise on financial products or credit. According to the DFSA, Forsyth had failed to meet the applicable regulatory capital requirements as a "Category 4" company pursuant to the DFSA Rules. The DFSA issued a show cause notice to Forsyth on 22 August 2007 and directed it to cease the carrying on of any financial service or other activity that would prejudice the clients or creditors of the firm, until further notice. Forsyth was given until 26 August 2007 to show cause why its licence to provide financial services in the DIFC should not be withdrawn, but was unable to demonstrate a capacity to remedy the breach of the capital requirements in question. The DFSA therefore withdrew the licence of Forsyth and Forsyth Middle East.

6. Shortly after the withdrawal of the financial services licences, the boards of directors of the Companies passed separate resolutions at board meetings held on 13 September 2007 to liquidate the Companies pursuant to Article 50(a) of the Insolvency Law, and appoint the Liquidators as joint liquidators for the purposes of the winding-up ("the Resolutions"). The Companies applied to the Court on 18 September 2007 for Winding Up Orders pursuant to the Insolvency Law on the basis of the Resolutions. The Companies also asked that the Court exercise its discretion to excuse the Companies from the obligation under Regulation 5.3 of the DIFC Insolvency Regulations to advertise the petitions in a newspaper circulating in the DIFC.

Petitions for winding up orders

7. Counsel for the Liquidators came before the Honourable Chief Justice Sir Anthony Evans on 19 September 2007, when he issued Winding Up Orders in respect of the three separate petitions directing that the Companies be wound up under the provisions of the Insolvency Law. He also directed that Mr. Akers and Mr. Dunckley were to be appointed as joint liquidators in respect of the Companies pursuant to Article 58 of the Insolvency Law, and that the Companies were excused from any obligation under Regulation 5.3 of the Insolvency Regulations to advertise the petitions. The Orders also stated that all creditors of the Companies had liberty to apply to the Court within seven days for the terms of the Winding Up Orders to be varied.

8. The Liquidators (on behalf of the Companies) then applied to the Court for directions pursuant to Article 71 of the Insolvency Law seeking directions as to which debts of the Companies, if any, should be treated as preferential debts for the purposes of Article 67 of the Insolvency Law.

Relevant laws

9. Article 71 of the Insolvency Law provides that:

"***71. Reference of questions to Court***

(1) The liquidator or any shareholder or other person liable to contribute to the assets of the Company or creditor may apply to the Court to determine any question arising in the winding up of a Company by the Court.

(2) The liquidator or any aggrieved person may apply to the Court for an order in relation to the exercise of the powers or functions of the liquidator.
(3) The Court may make such order on an application under this Article as it thinks just, including where appropriate an order enforcing or setting aside any direction given or requirement made by the liquidator to or of a person."

10. Article 67 of the Insolvency Law provides that:

"***67. Preferential debts***

(1) Subject to the application of any other laws as described in Article 101, in a winding up the Company's preferential debts shall be paid in priority to all other debts.
(2) The Board of Directors of the [Dubai International Financial Centre Authority] may make such Regulations as it sees fit to designate certain types of claim on a Company as preferential debts and to prescribe any priorities as to their payment."

11. It was common ground that there are no other DIFC Laws as described in Article 101(1) of the Insolvency Law that are applicable to a DIFC company's preferential debts in a winding up. Article 101 provides that:

"***101. Application of other laws in relation to receivership and winding up***

(1) The provisions of this Law and Regulations relating to the powers of a receiver, administrative receiver, provisional liquidator and
liquidator to get in, secure, realise and distribute property of a Company are subject to the application of other DIFC Laws and rules and regulations made under those laws which may be inconsistent with or otherwise extend, exclude, modify, or waive the application of provisions of this Law and Regulations in particular cases or classes of case.
(2) In particular, and without limiting the generality of Article 101(1), such other laws, rules or regulations may provide for the orderly conduct of affairs or winding up of a Company which is licensed as an Authorised Firm or Authorised Market Institution under the Regulatory Law, in relation to which the legislation may prescribe procedures and priorities for the dealing with assets of the Company or other persons in the event of pending or actual insolvency or other default."

12. In the Petitions, Counsel for the Liquidators stated that the Dubai International Financial Centre Authority ("DIFCA") had not promulgated any Regulations in respect of preferential debts in the DIFC pursuant to Article 67(2) of the Insolvency Law. This was confirmed in a letter dated 19 November 2007 from Mr. Dean Ferris, the Registrar of Companies, written on behalf of the DIFCA. This letter also confirmed that the DIFCA had no objection to the Liquidators of the Companies currently under liquidation from making an application to the DIFC Courts to seek directions on what might constitute preferential debts for the purposes of Article 67 of the Insolvency Law.

13. Article 8 of the Law on the Application of Civil and Commercial Laws in the DIFC (DIFC Law No.3 of 2004) ("DIFC Law No. 3") provides that:

"***8. Application***

(1) Since by virtue of Article 3 of Federal Law No.8 of 2004, DIFC Law is able to apply in the DIFC notwithstanding any Federal Law on civil or commercial matters, the rights and liabilities between persons in any civil or commercial matter are to be determined according to the laws for the time being in force in the Jurisdiction chosen in accordance with paragraph (2).
(2) The relevant jurisdiction is to be the one first ascertained under the following paragraphs:
(a) so far as there is a regulatory content, the DIFC Law or any other law in force in the DIFC; failing which,
(b) the law of any Jurisdiction other than that of the DIFC expressly chosen by any DIFC Law; failing which,
(c) the laws of a Jurisdiction as agreed between all the relevant persons concerned in the matter; failing which,

(d) the laws of any Jurisdiction which appears to the Court or Arbitrator to be the one most closely related to the facts of and the persons concerned in the matter; failing which,

(e) the laws of England and Wales."

Petitions pursuant to Article 71 of the Insolvency Law

14. The hearing of the three Petitions took place on 22 and 25 November 2007. During the hearing, I explained to Counsel for the Liquidators that I had three choices:

(a) to follow English law;
(b) to defer the hearing until the DIFCA promulgated the appropriate regulations in respect of preferential debts; or
(c) to declare that there was no regime of preferential debts until the DIFCA's promulgation.

15. Counsel then explored a fourth possibility, i.e. the applicability of United Arab Emirates law ("UAE law"). Counsel submitted that UAE Law could be applicable by virtue of Article 8(2)(d) of DIFC Law No. 3 (set out above at paragraph 13), as UAE law are "the laws of a Jurisdiction which appears to the Court . to be one most closely related to the facts of and the persons concerned in the matter". If Article 8(2)(d) applied, UAE law would take priority over English law as the default law, assuming no other law having priority applied.

16. Following this, I directed Counsel to submit an independent legal opinion from Dubai qualified lawyers on the issue of how employee claims for unpaid salary and benefits (including wages, holiday pay, pay for leave in lieu of notice, and redundancy pay, (or equivalent)) are treated in an insolvency under UAE law.

17. Counsel therefore filed further written submissions, and exhibited a legal opinion on UAE Law by Habib Al Mulla & Company, Advocates & Legal Consultants, based in Dubai, in support of the Petitions on 17 December 2007 ("the Legal Opinion").

18. As the Legal Opinion did not deal with the position of holiday pay under UAE law, I sought clarification on this issue, and the Counsel for the Liquidators submitted a supplementary Legal Opinion addressing this point on 7 January 2008 ("Supplemental Opinion").

Arguments

19. Counsel's arguments proceed on the premise that there are no Regulations promulgated by the DIFCA pursuant to Article 67(2) of the Insolvency Law, and that there are no other relevant DIFC laws on preferential debts pursuant to Article 101 of the Insolvency Law. Counsel put forward two arguments as follows.

(i) UAE law on preferential debts is most closely related to the facts and the persons concerned in the present case pursuant to Article 8(2)(d) of DIFC Law No. 3.

(ii) In the alternative, English law on preferential debts applies as the default law pursuant to Article 8(2)(e) of DIFC Law No.3.

(i) UAE law on preferential debts

20. Counsel for the Liquidators submits that, applying Article 8(2)(d) of DIFC Law No. 3, UAE Law is the law of a jurisdiction that would appear to the Court to be the one most closely related to the facts and the persons concerned in the present case. Counsel argues that, following this, UAE insolvency law relating to preferential debts can be applied to define what constitutes "preferential debts" in the DIFC.

21. Based on the Legal Opinion, Counsel submits that Article 713 of the UAE Federal Law No. 18 of 1993 (as amended) (the "Commercial Code") is the relevant provision governing preferential debts in the UAE. This provision (as translated from Arabic) reads as follows.

> "*1 - After obtaining the permission from the judge of bankruptcy, the trustee of bankruptcy, within ten days from the issuance of the judgment declaring bankruptcy, shall pay the wages and salaries, (monthly Remuneration as per the Labor Law), of the workers and employees due prior to issuance of the judgment declaring bankruptcy, for a period of thirty days, from any monies of the bankruptcy under his hand, regardless of any other debts. However, if the trustee of the bankruptcy has no sufficient money for settling the said debts, the first amounts of money that comes into the bankruptcy shall be used for payments regardless of any other debts that are of higher level of privilege.*
>
> *2 - The amount due for the said categories of workers exceeding those indicated in the preceding paragraph shall be treated pursuant to the laws related to privileges.*"

22. Article 713(2) of the Commercial Code refers to the laws related to privileges. According to Counsel for the Liquidators, this is in effect Article 4 of the UAE Federal Law No. 9 of 1980 (as amended) (the "Labour Law"). Article 4 states that:

> "*Any amounts due to an employee or his beneficiaries pursuant to the Labor Law shall have privilege over all the employer's moveable and immovable property and shall be paid immediately upon settlement of any legal expenses, sums due to the public treasury and Sharia alimony awarded under Islamic Law to the wife and children.*"

23. The Legal Opinion assumes that the Companies are entities that undertake "commercial business" as a "trader" within the meaning of Articles 4 and 11 of the Commercial Code respectively.

24. Counsel for the Liquidators submits that Article 713 only covers employees who were still listed as employees of the relevant company as at the date of appointment of the trustee in bankruptcy. Any employee who resigned or was terminated prior to this date, whether or not pursuant to the insolvency, will not be entitled to the wages and salaries payable as entitlements under Article 713.

25. Counsel further argues that Article 713 of the Commercial Code entitles these employees that are still listed (to the extent that they have not already been paid this amount) to an amount equivalent to 30 days of their usual monthly salary and benefits (which would include base salary and all contractual allowances and benefits that are ordinarily paid monthly, but not end of service benefit). These payments are made in priority to all other creditor claims. Any remaining employee related claims are considered to be of equal validity as between each other and are to be treated as privileged claims payable in accordance with Article 4 of the Labour Law from funds that remain after payment of the Article 713 entitlements. Only legal expenses (i.e. judicial court expenses), sums due to the public treasury and Sharia alimony awarded under Islamic Law to the wife and children are paid in priority to the employee related claims.

26. The Supplemental Opinion points out that "holidays" are preferred debts and are subject to Article 713-2 of the Commercial Code, which refers indirectly to Article 4 of the Labour Law, since holidays are not part of the "salary" referred to under Article 713-1 of the Commercial Code read with Article 1 of the Labour Law.

27. Counsel for the Liquidators also points out that the Commercial Code and the Labour Law do not recognise the concept of redundancy pay in the same way as the English Insolvency Act.

(ii) English law on preferential debts

28. In the alternative, Counsel for the Liquidators submits that the English law on preferential debts could apply as the default position pursuant to Article 8(2)(e) of DIFC Law No. 3.

29. The English law relating to preferential debts is set out in Section 386 and Schedule 6 of the English Insolvency Act. These provisions set out the categories of preferential debts that would apply in a winding up in England.

30. Section 386 of the Insolvency Act provides that:

"***386 Categories of preferential debts***

> *(1) A reference in this act to the preferential debts of a company or an individual is to the debts listed in Schedule 6 to this Act [(contributions to occupational pension schemes; remuneration, &c. of employees; levies on coal and steel production)]; and reference to preferential creditors are to be read accordingly.*
>
> *(2) In that Schedule "the debtor" means the company or the individual concerned.*
> *(3) Schedule 6 is to be read with [Schedule 4 to the Pension Schemes Act 1993] (occupational pension scheme contributions).*"

31. Counsel submits that Category 5 (Remuneration, etc., of employees) of Schedule 6 is relevant as the likely preferential claims of the employees of the Companies under the Insolvency Act would be for (i) wage related claims as set out in paragraph 9 read with paragraphs 13-14 of Schedule 6 and (ii) claims for holiday pay as set out in paragraph 10 read with paragraphs 13-14 of Schedule 6. According to Section 387(3)(ba) of the Insolvency Act, these claims are payable from the date of the passing of the resolution for the winding up of the debtor company for the purposes of determining the existence and amount of preferential debts.

32. A person who is or has been an employee of a debtor company is entitled to remuneration (payable as wages or salaries) from the debtor company, subject to a prescribed limit.

33. If a person's employment were terminated by the debtor company before the passing of the resolution of the debtor company, that person would be entitled to accrued holiday remuneration which would not be subject to any prescribed limit.

34. Counsel for the Liquidators submits that there are certain employee claims that would be settled in part or in full by the Redundancy Payments Office ("RPO") irrespective of whether they would be afforded preferential status. These sums are paid out by the RPO from a statutory fund (the National Insurance Fund) under the Employment Rights Act 1996, which covers (i) pay in lieu of notice, and (ii) redundancy pay. Counsel for the Liquidators submits that these employees' claims are unsecured and not preferential (subject to Schedule 6 of the Insolvency Act). However, Counsel submits that, to the extent that these claims are protected under English law, but for a duty to mitigate notice pay, they are payable in full out of the statutory fund established for such purpose.

Discussion

35. Article 8(2) of DIFC Law No. 3 (set out above at paragraph 13) provides a framework for determining the applicable law in specific situations, and provides that English law applies in a default position. The applicable laws are set out in descending order of applicability.

36. It is clear that, pursuant to Article 8(2)(a) of DIFC Law No. 3, the relevant "regulatory content" in the DIFC Law or any other law in force in the DIFC on preferential debts will take priority over all other laws. I will return to the applicability of this provision later.

37. There is no applicable law of a jurisdiction other than that of the DIFC that was expressly chosen by any DIFC Law. Accordingly, Article 8(2)(b) of DIFC Law No. 3 does not apply.

38. Article 8(2)(c) of DIFC Law No. 3 is also inapplicable as there was no evidence adduced of any agreement between the Liquidators (and other relevant persons concerned in the Petitions) as to the applicable law of a Jurisdiction.

39. Accordingly, the only other serious candidates under Article 8(2) of DIFC Law No.3 appear to be (i) UAE Law (applying Article 8(2)(d)), or (ii) English law (applying Article 8(2)(e)).

40. It is worthwhile to note, however, that the starting point in this analysis is that each scheme for preferential debts derives from the priorities and social conditions existing in the relevant country. There is therefore no presumption that the principles of insolvency are universal, and certainly no natural presumption that UAE law or English law was intended to apply in the DIFC.

41. Bearing this in mind, I note that there are factors in both the UAE and English laws on preferential debts that militate against the applicability of either law in the DIFC.

42. In my view, UAE law is not applicable in the present case as there are other factors in UAE insolvency law that may be influenced by priorities and social conditions in the UAE. For instance, Sharia alimony awarded under Islamic law to an employee's wife and children takes priority over any amounts due to the employee under Article 4 of the Labour Law. The recognition of Islamic law may not necessarily be a relevant consideration in the DIFC, as DIFC laws do not envisage the direct application of Islamic law. The preferential status of payments due to the public treasury over employee claims under Article 4 of the Labour Law is also likely to be influenced by priorities and economic considerations in the UAE.

43. Likewise, English law is not applicable in the present case as there are factors in English insolvency law that are influenced by the priorities and social conditions in England and Wales that do not necessarily apply in the DIFC. For example, the concept of "redundancy" and "occupational pension schemes" are both peculiar to the English common law and do not apply to the DIFC. The preferential status accorded to coal and steel productions under Section 386(1) of the Insolvency Act also demonstrates that preferential debts in England and Wales are driven by national

economic interests that are not necessarily relevant to the DIFC. As the 1982 UK Report of the Insolvency Law Review Committee on Insolvency Law and Practice (Cork Report) points out (at paragraph 1428), "*[preferential debts were] introduced in an effort to ease the financial hardship caused to a relatively poor and defenceless section of the community by the insolvency of the employer*" at a time when "*there was no welfare state and wages were low*".

44. The English legislative history on preferential debts also buttresses my view that preferential status was accorded to certain types of claims that were clearly influenced by the social conditions of England and Wales. The wages and salaries of clerks, servants, labourers and workmen were first given preferential status under the English Companies Act 1883, which formed the basis of the Insolvency Act. This was clearly a social effort to ease the financial hardship amongst certain poorer sections of the community.

45. Taking into account all these factors, it is my view that the legislature of the DIFC intended to have its own law regarding preferential debts. Even though there is not yet any pronouncement from the DIFCA as to which debts are preferential, this does not mean that UAE law or English law applies in default.

46. Since the position is that the DIFC Insolvency Law envisages that there will be regulations on preferential debts specified by the DIFCA, the conclusion that I draw is that the legislature wished a regime of preferential debts to be established under local law, and not by reference to another system of law. In effect, what the legislature has said is that DIFC will have its own regime on preferential debts and not rely on default provisions or English or UAE law as submitted by Counsel for the Liquidators. Accordingly, the legislature has preempted the applicability of any other laws in favour of DIFC law on preferential debts even though there is as yet no DIFCA promulgated list of preferential debts until such promulgation is made.

47. Accordingly, until such promulgation is made, there are presently no preferential debts in any insolvencies carried on under the DIFC Insolvency Law (DIFC Law No. 7 of 2004) in the DIFC.

48. I therefore give my directions pursuant to Article 71(1) of the Insolvency Law as follows.

In connection with Article 67 of the Insolvency Law,

(i) certain wage related claims (as set out in paragraph 9 of Schedule 6 of the English Insolvency Act);
(ii) certain claims for holiday pay (as set out in paragraph 10 of Schedule 6 of the English Insolvency Act);
(iii) payments in lieu of notice; and
(iv) redundancy pay cannot presently be deemed preferential debts for the purposes of Article 67 of the Insolvency Law.

MICHAEL HWANG

Judge

Date of issue: 30 January 2008