THE REGULATION OF FUNDING TROUBLED PROJECTS

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ABSTRACT

Objectives: A project may suffer a financial crisis; the project management shall seek to provide the necessary financial liquidity to overcome the state of default that has affected this project. Therefore, companies resort to seeking financing sources. However, the search for financing sources under the description of the project as Troubled is a very difficult task. How can a financier be convinced to finance a Troubled project?

Methods/Approach: the study followed the descriptive analytical comparative approach. The descriptive approach will be used to address the means of recovering the projects from the difficulties, and to analyze the legal articles governing this financing, and thus to address its controls, the comparative approach will be relied upon, where the financing of Troubled projects in the American Bankruptcy Law will be addressed, and thus the comparative approach will be used.

Results: the study addressed the concept of a Troubled project, the regulations for granting guaranteed financing, in addition to cross-collateralization. Considering that guarantees are the basis of financing, a lender will not finance without guarantees, especially if the project to which the loan is being provided is a Troubled project.

Conclusions: The study reached several recommendations, including the establishment of a Troubled projects support fund, which would be funded by contributions from the companies themselves and would be under the authority of the government. In addition, establishing a government fund to support Troubled projects, with financing priorities divided according to the importance of the project to the economy. These loans would be interest-free.

Keywords: Troubled projects, Stalled Project, Funding Project, Cross-Collateralization, Funding Guaranteed

JEL classification: K2; K4; O57; P5

Paper type: Research article


INTRODUCTION

There is no doubt that business transactions are based on forward transactions, meaning that the seller gives the buyer a grace period to pay for the goods, as the buyer rarely pay the full price for the goods in cash immediately. Forward transactions rely on trust between traders regardless of the guarantees that will be provided to accept these forward transactions. Accepting forward transactions is credit, and the credit is the trust that the creditor gives to the debtor. The laws governing business transactions in all countries seek to protect this trust and prevent anything that disturbs it. Efforts to preserve that trust come as a result not of protecting trust itself, but because the debtor's creditor is a debtor to another creditor and so on. This is the pattern of business life. Business transactions between traders are compared to rings, each relationship between a creditor and a debtor forms a ring, and each ring is intertwined with the other because every creditor is a debtor and every debtor is a creditor. Therefore, the default of any debtor from fulfilling his obligations will
inevitably lead to the default of his creditor in fulfilling his obligations because his creditor is a debtor to another creditor and so on, the business life will be completely paralyzed. Therefore, bankruptcy was found as a means to remove the debtor from the circle of business transactions with the least losses by liquidating all of his assets and distributing the proceeds of the sale among the creditors. Certainly, the creditors will not get their full debts, but a part of them, because if the creditors get their rights in full, why did the debtor stop fulfilling his debts and his debts exceeded his assets.

Therefore, one of the most dangerous situations that a company can go through is a financial crisis. It raises the interest of the owners, creditors, and all stakeholders associated with the company. The financial difficulties will not be overcome except by the combined efforts of all stakeholders who are keen on the company continues. Undoubtedly, a troubled company faces many challenges, the most important of which is providing the necessary financial liquidity to overcome the state of irregularity in paying off its debts in order to get out of its crises and rebalances its books. To manage the necessary liquidity in the face of this crisis that may lead to the bankruptcy of the company if it is not dealt with competently, companies resort to looking for financing sources. Definitely, it is difficult to obtain financing for economically strong projects due to the multiplicity of financing requirements. Therefore, it becomes more difficult to the point of impossibility if the applicant for financing is a Troubled project. It is difficult to convince a lender to finance a Troubled project and the difficulty of obtaining his money that he will provide as a debt for this project. Studies that have addressed the financing of Troubled projects, including the study of (Carapeto, 1999), indicate that new financing for borrowers from troubled companies undergoing restructuring provides greater opportunities for successful restructuring.

Elayan and Thomas (2001) also analyzed the response of stock and bond prices to the announcement of Dubai Investments Park (DIP) that it received financing. It was noted that new financing in the case of financial default is appropriate and leads to positive results that affect stock and bond prices.

The United Nations Commission on International Trade Law (UNCITRAL) has paid great attention to the stalling of projects and ways to provide the means that would help to save projects from their difficulties. Its efforts resulted in the issuance of the UNCITRAL Model Law on Insolvency. In the guide issued on this law in 2009, the Commission pointed to the importance of providing access to financing for troubled companies. Based on this, countries have sought to strengthen their commercial and economic legislative systems with means to support Troubled projects, in order to save them recover. This resulted in the transformation of laws governing the failure of merchants into means of assistance and support for Troubled projects, and not legislation for the purpose of removing the trader and the Troubled project from the business life. The Saudi legislator followed this approach and issued a New Bankruptcy Law in 2018. The Saudi legislator used preventive settlement, financial rehabilitation, and liquidation as means of support for Troubled projects. Chapter (10) regulated the financing of Troubled projects. Based on this Chapter, it regulated how the Troubled project obtains financing, and defined the types of financing, and the court's authority to approve or not approve
the financing, so, the troubled project can request a Loan even during preventive settlement, financial rehabilitation.

Therefore, the study will focus on financing Troubled project, as it is a fundamental means to recover Troubled business projects, or in other words, to revive them and restore confidence in them again, and to reintegrate them into the economic system.

STUDY PROBLEM
The study problem consists of two problems; First Problem, is that financing a non-Troubled project is not easy, so it is natural that financing a Troubled project is more difficult and may reach the point of impossibility. Therefore, the first problem is financing a Troubled project. Second Problem, is that despite the existence of a legislative regulation for funding troubled projects in the Kingdom of Saudi Arabia since 2018, there are no judicial rulings that have addressed the financing of a Troubled project. The lack of judicial applications (published) deepens the problem even more.

METHODOLOGY
The study followed the descriptive analytical comparative approach. The descriptive approach will be used to address the means of recovering the projects from the difficulties, and in particular their financing, and to analyze the legal texts governing this financing, and thus to address its controls. Due to the novelty of the regulation in Saudi law, and the absence of judicial rulings through which the problems of application can be extrapolated, the comparative approach will be relied upon, where the financing of Troubled projects in the American Bankruptcy Law will be addressed, and thus the comparative approach will be used.

DISCUSSION
1. What is the Troubled project?
The business project is considered to be a Troubled project if it faces temporary circumstances that have affected its results, but it has the potential to reform its course and recover from its difficulties if the necessary financial reasons and resources are available (Havelka et al., 2006). Some have defined troubled companies as companies that are unable to meet their debt obligations at their inception (Mba, 2019). Others have defined financial distress as a decrease in revenue flow, and the possibility that the owners of the business project will be unable to pay its expenses, especially its debt burdens. If these qualities are present in a project, it can be described as a Troubled project (Gordon, 1971). Financial distress of the project may be caused by a number of financial reasons, such as an imbalance in the balance between the financial investments of the company that runs the project and the paid-up capital, which leads the company to borrow at high interest rates to cover the shortage of financial liquidity for the Troubled business project (Sidak et. al. 2020). The cost of administrative expenses for the business project may also increase, which is due to the increase in salaries and wages for workers in the business project (Gordon, 1971).

It is worth noting that UNCITRAL has been extremely thoughtful in the failure of projects and the ways of providing the means that would help projects to recover from their hardship, and this is evident from its issuance of the UNCITRAL Model Law on Insolvency (UNCITRAL, 2009). In the UNCITRAL Practice
Guide on Cross-Border Insolvency Cooperation 2009, it referred to the importance of providing troubled companies with financing, as it expressed it as follows: “Access to funds to enable them to continue to pay for essential supplies of goods and services, including labour costs, insurance, rent, property maintenance, contracts, and other operating expenses, as well as costs associated with maintaining the value of their assets.” (UNCITRAL, 2009)


The mere fact that a project has fallen into financial difficulty does not mean that it will be liquidated immediately. On the contrary, comparative legislations seek to grant Troubled projects the opportunity to reorganize their affairs in order to continue their calculated presence in the market (Sidak et. al., 2023). Therefore, any project enters into any of the bankruptcy procedures requires the appointment of an administrator for this procedure, as stated by the Saudi Bankruptcy Law, for example. This administrator is allowed by law to continue managing the project and making its commercial decisions. In this regard, he enjoys the rights and powers of a guardian under the Bankruptcy Law. Therefore, the debtor and the procedure officer shall try to continue the activity of the project, and it may be necessary to arrange for financial liquidity in order to continue the productivity of the project, especially if the project is expected to exit its financial crisis through the reorganization of its financial and operational matters (Triantis, 1993). In this case, the debtor proceeds to obtain financing, he shall either obtain the approval of the creditors or obtain the permission of the court for this financing, after verifying that the creditors’ debts will not be negatively affected by the required financing (Dolny, 2023) (Triantis, 1993). The competent court is responsible for assessing the suitability of the proposal submitted by the debtor (Norley et al., 2001) (Iheme, 2020).

The American Bankruptcy Code, Chapter (11), addresses the means by which Troubled projects can be saved from their difficulties in order to protect them from bankruptcy. This is done by enabling the Troubled project to reorganize its financial situation in a way that allows the project to overcome the difficulties that have affected it.

Some (Bowles et al., 1997) have argued that Chapter (11) is the best that comparative legislation has achieved in terms of supporting Troubled projects. The basis for these means provided for in Chapter (11) is that the value of a Troubled business project can sometimes be greater after it has been reorganized and removed from its Troubled state than it would be if it were sold as separate assets. For this reason, the aforementioned law has granted a set of mechanisms that enable troubled projects to overcome their troubled state.

By examining the paragraph 5 of Article 1123 of Chapter 11 of the American Bankruptcy Code, it can be concluded that the American legislator has provided all the appropriate ways that enable the troubled project to overcome the difficulties that have affected it, such as transferring all or any part of the project’s assets to

\[\text{(5) provide adequate means for the plan’s implementation, such as—}
\]
\[(A)\text{retention by the debtor of all or any part of the property of the estate;}
\]
\[(B)\text{transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;}
\]
one or more entities, merging the debtor with one or more persons, modifying any lien, modifying or terminating any contract that the Troubled project has previously entered into, extending due dates or modifying interest rates.

On the other hand, the Saudi legislator has introduced a mechanism within the mechanisms for protecting Troubled business projects from bankruptcy. According to Article 182 and 183 of the Bankruptcy Law, the legislator has allowed Troubled business projects to request new financing, despite their troubled financial position. This is on the basis that securing the necessary liquidity for the project through new financing will help it to continue its operations.

3. Banking and non-banking financing and its role in recovering the Troubled project.

The regulation of the financing of Troubled projects is a relatively new, especially in Saudi law. Article 182 and 183 of the Bankruptcy Law allows Troubled projects to request new financing, despite their Troubled financial position. Some believe that the purpose of this regulation is to enable the debtor to offer incentives to lenders in the form of a high priority, which would otherwise prevent lenders from providing their financial support (Triantis, 1993).

New financing can be obtained internally or externally. Internal sources of new financing include capital contributions from current shareholders, the disposal of assets or the withdrawal of investments, loans from shareholders, or even through funds contributed by the company, represented by the reserves that the company has accumulated over time from its profits. At the external level, troubled borrowers may issue shares, obtain loans, issue bonds or other forms of debt instruments (Mba, 2019), also the partnership between public-private is important for funding troubled projects (Avena & Grasis, 2023) (Dolny, 2023). The principle of a socially responsible state entails the obligation to formulate sustainable and balanced policies that promote public welfare while considering the interests of both the public and private sectors (Palkova & Abuseridze, 2020). Based on these principles, countries are more likely to thrive in a rules-based, rather than power-based system, which increases the possibility of financing projects in general (Abuseridze, 2023).

Some banks are reluctant to provide the necessary Loan for troubled projects due to the state of distress in which the project is found. However, financial institutions have expanded their financing of Troubled projects, and a large number of banks now have specialized departments for financing companies in bankruptcy. (Triantis, 1993; Mba, 2019) The studies show that several crowdfunding projects successfully collect money even if the expected interest is low (Avena & Grasis, 2023) Studies indicate that Chemical Bank, which merged with Manufacturers Hanover, is one of the entities that have specialized in this area of financing (Moore, 1990).

(C) merger or consolidation of the debtor with one or more persons;
(D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate;
(E) satisfaction or modification of any lien;
(F) cancellation or modification of any indenture or similar instrument;
(G) curing or waiving of any default;
(H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;
(I) amendment of the debtor’s charter; or
(J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose;
If Troubled projects resort to offering shares, if the company allows it, to increase its capital through subscription to additional shares of the company, the company will face a problem that the market value of the company's shares has decreased due to the company's financial situation. Therefore, financing with shares may not achieve the goal that the Troubled project aspires to achieve (Lewis, 1994; 2004). However, pumping new financing for the Troubled project in shares can provide the money that Troubled projects need. It is worth noting that new shares enjoy an important advantage as a source of financing for troubled businesses, as the new funds that enter the capital structure of troubled businesses as equity do not require the payment of interest, as is the case with loans (Sidak et. al., 2023). The borrower is not obliged to pay loan service payments and the debt that will be provided against the loan is usually higher to reflect the risks of lending, a situation that can make the borrower more vulnerable to bankruptcy (Collard, 1994).

Despite the possibility of increasing liquidity through capital subscription, especially in the case of subscription by the company's shareholders or owners of shares therein, shareholders or owners of shares may resort to lending the company, because the legal position of the lender is different from the legal position of the shareholder (Engert, 2004), especially if the shareholder lender -in the form of subscription to bonds-provided a secured loan from the debtor (Dolny, 2023).

The British and American courts have considered the extent to which it is permissible for the chairman of the board of directors of a troubled company to lend the company in a dispute that was heard by the British courts Matthew Ellis & Co. Ltd. [1933] 458, the facts of which are summarized in the lender (the chairman of the board of directors of the debtor) granting a loan to the debtor to purchase goods and taking a floating charge on the debtor’s assets. The English court in this case decided that no fault in the granting loan also from the court point of view the security interest held by the chairman of the board was not flawed. Note that although this issue was recognized as an area for reform by the Cork Commission (Britain et al., 1982; Mba, 2019) (Alshammari & Sadeq, 2023).

In the case of Taylor v. Standard Gas v. Electric Co. (Deep Rock), the court developed the equitable principle that became known as the “Deep Rock doctrine.” This doctrine, in its entirety, requires a controlling shareholder to provide credit to the debtor on the basis that the debtor's insolvency arose from a lack of capital and mismanagement by the controlling shareholder (Mba, 2019).

In the same context mentioned in the case of Taylor v. Standard Gas v. Electric Co. (Deep Rock), the US Supreme Court explained the basis of subordination leading to the idea of being obliged to provide credit to the debtor in the case of Pepper v. Litton, where it went on to say that even in the absence of fraud, shareholder/debtor control, or lack of capital, the company's claim may be subordinated if the shareholder breaches the fiduciary duty owed to the shareholders and other creditors) (Mba, 2019).

However, this approach is difficult to accept under Saudi Companies Law. Either the controlling party mismanages the company and bears personal liability, or the opposite, and the company therefore is responsible for its debts because the source of the obligation to provide credit is the contract.

In Bankruptcy Law, the Saudi legislator adopts three basic means to deal with troubled and bankrupt projects which are preventive settlement, financial reorganization, and liquidation. In turn, the aforementioned law differentiates in dealing with debtors between large debtors and small debtors. The three means indicated herein were divided into seven means due to dividing debtors into large and small debtors. Therefore, the means adopted by the Saudi legislator to deal with troubled projects are divided, concerning the debtor, into seven means. These are preventive settlement, preventive settlement for small debtors, financial reorganization, financial reorganization for small debtors, liquidation and liquidation for small debtors, and administrative liquidation.

Article 182 of the Saudi Bankruptcy Law explains the mechanism of dealing with troubled projects that need financing to be covered. The financing was divided into three sections, prevention and permission by type of financing and type of procedure. The aforementioned Article stipulates that:

I. The Debtor shall not obtain secured financing after commencing any of the bankruptcy proceedings except after the Court's approval in accordance with the provisions of the Law.

II. Unsecured financing shall not be obtained after the commencement of the liquidation or liquidation procedures for small debtors except after the approval of the Court in accordance with the provisions of the Law.

III. Secured or unsecured financing shall not be obtained after the commencement of the administrative liquidation procedure."

Based on the foregoing, financing for troubled projects is divided into two types, secured financing and unsecured financing. For Secured Financing, the approval of the competent Court is required as long as the project has opened one of the following six procedures against it, except with the approval of the Court. These procedures are preventive settlement, preventive settlement for small debtors, financial reorganization, financial reorganization for small debtors, and liquidation and liquidation for small debtors. Secured or unsecured financing shall not be requested in the event of administrative liquidation according to the provision of the Article 182 (3).

For Unsecured Financing, the approval of the Court is not required if the project initiation to any of the following procedures (preventive settlement, preventive settlement for small debtors, financial reorganization, and financial reorganization for small debtors). Therefore, unsecured financing in the event of liquidation or liquidation procedures for small debtors requires the approval of the competent Court.

On the other hand, Article 364 (c) of the United States Bankruptcy Code allows the court to allow "access to credit or incurring debts" by the court if the debtor is unable to obtain unsecured credit. This paragraph

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1 The Bankruptcy Committee defined the status of a small debtor as “if the debtor’s total debts do not exceed two million riyals, he is considered a small debtor and has the right to initiate this procedure.” [https://bankruptcy.gov.sa/ar/Knowledge Center/FAQ/Pages/debtor.aspx?qid=q-14](https://bankruptcy.gov.sa/ar/Knowledge Center/FAQ/Pages/debtor.aspx?qid=q-14)
permits obtaining credit or incurring debt under one of three terms: (1) Post-petition credit or debit shall have priority over other administrative expenses; (2) Post-petition credit or debit is secured by a lien on unpledged property; or (3) the post-petition credit or debit is secured by a small lien on the pledged property. If the debtors are unable to secure credit under (c), the Bankruptcy Court may authorize them to obtain credit or assume a debt of older or equal lien on the pledged property if the lien holder on the property is adequately protected.\textsuperscript{1} Article 364 (e) of the U.S. Bankruptcy Code prohibits challenging the refinancing plan. Therefore, if the refinancing plan is approved as part of the financial restructuring of the project, the financing plan shall not be appealed, as American judgments have established that “Articles 364 (c) & (d) permit only certain types of procedures or liens to obtain post-petition credit or financing and Article 364 (e) only protects the validity of a lender's post-petition debt and/ or certain priorities and liens. Therefore, before this court decides that Article 364 (a) prohibits refinancing plan appeals, it must decide whether the terms of the refinancing plan are permissible under Article 364 (c) and/ or (d).”\textsuperscript{2}

5. The legal system for secured financing of Troubled projects.

The motivation for providing new financing on a secured basis to a troubled company is essentially the same reason for which a lender provides secured lending to healthy and untroubled companies. Security interests primarily ensure the priority of repayment to the lender in respect of certain assets of the debtor over the assets of other creditors (Baird et al., 2004). The studies show that several crowdfunding projects successfully collect money even if the expected interest is low (Avena & Grasis, 2023).

The priority of the secured creditor over other financial creditors can be justified on the basis that unsecured creditors grant a loan knowing that some assets are subject to security interests or may be subject to security interests without their permission. If certain creditors do not tolerate other creditors with security interests in the borrower's assets, they can refuse to make a loan or only provide it if the borrower agrees not to subject its assets to any security interests (Leebron, 1991).

It should be noted that for approval of secured financing, the debtor requesting financing shall prove the inability to obtain unsecured financing. The US judiciary has established that "the trustee or debtor in possession shall prove his inability to obtain the necessary credit in any way other than obtaining this credit secured by an older or equal lien on the previously pledged property.”\textsuperscript{3}

5.1. Nature of Secured Financing

Originally "all the debtor's property is a security for the payment of his debts, and all creditors are equal in this security, and no one of them has priority except by a statutory provision".\textsuperscript{4} However, such equality may result in damage to creditors if the debtor deliberately arranges debts in his financial disclosure greater than his


\textsuperscript{4} Article 181 of the Saudi Civil Transactions Law
secured funds, which results in the bankruptcy of the project. Article 1 of the Bankruptcy Law defines a Bankrupt as "A debtor whose debts have consumed all of his assets." Therefore, the debtor may have financial assets greater than the debt at the time of borrowing from the creditor, but during the period between the arise of the debt and its maturity, the debtor created several obligations in his financial liability that exceeded in total the value of his financial assets. In that case, the creditor only recovers part of his debt as a result of distributing the debtor’s assets to all creditors, each of them according to the proportion of his debt. Therefore, to achieve the safety of creditors, Saudi law allows the allocation of a certain amount of the debtor's funds to meet a debt owed by no one.

The security interest is based on the idea of assigning a specific property, whether real or movable, as security for a specific debt. This means that if the debtor voluntarily failed to pay off this debt, the creditor may enforce the security property without fear that it may have been removed from the debtor's ownership in the period between the creation of the debt and the taking of enforcement measures, and without fear of being crowded out by other creditors in the enforcement of the security property (Peltoniemi et al., 2013).

Paragraph 1 in Article 182 of the Saudi Bankruptcy Law stipulates that "Secured financing shall not be obtained by the debtor after the initiation of any of the bankruptcy procedures except upon the court's approval, in accordance with this Law.”

Regarding the scope of secured financing, Article 183 of the Saudi Bankruptcy Law stipulates that “In a protective settlement procedure, small debtors' protective settlement procedure, financial restructuring procedure, and small debtors' financial restructuring procedure, a debtor may, after the initiation of the procedure, file a petition with the court for the approval of the secured financing, provided the petition is supported by an expert report. The court shall approve the petition if it is necessary for the continuation of the debtor’s business, or for the protection of the bankruptcy assets during such procedure.”

In order to overcome the frequency status of funding troubled projects, guarantees contribute to promoting Lenders to fund debtors, because professional lenders will not fund a project, especially if it is troubled or bankrupt, unless the availability of guarantees provides sufficient security for the Lender (Tabb, 1986). Occasionally, a troubled company could lack the available assets through which it can arrange a guarantee for a new Lender. This is conceivable when the Lender is overindebted. When there are no assets available, the Lender shall provide secured loans to new Lenders. The new Lender may remain interested to provide financing as a result of the higher interest rates obtained by this lending. This lending is highly profitable for the Lender in terms of higher interest rates and charged fees compared to normal lending to non-troubled companies (Qi, 2006).

Article 364 of the United States Bankruptcy Code stipulates that the Troubled project obtain financing. Whereas, an unsecured financing mentioned in paragraphs "A" and "B", while a secured financing mentioned in paragraphs "C" and "D". Originally, Article No. 364 stipulates that the financing is unsecured; this is evidenced by reading part of paragraph "C" of the aforementioned Article. However, the aforementioned
Article required the Court’s approval of the secured financing after notice and a hearing. This financing accorded to priority for administrative expenses or super-priority (Triantis, 1993).

5.2. Conditions to consider the financing secured.

Article 184 of the Saudi Bankruptcy Law stipulates that “Financing shall be deemed secured if:

a. It has priority over unsecured debts at the time of filing the petition for financing.

b. It is secured by pledging a debtor’s asset that is not encumbered by another pledge.

c. It is secured by pledging a debtor’s asset that is encumbered by another pledge of a higher priority.

d. It is secured by pledging a debtor’s asset that is with a higher or equal priority to another pledge if the court establishes that the rights of the pledgee holding the existing pledge are not affected, or if the pledgee consents to the existence of another pledge of a higher or equivalent priority. The debtor must ensure the protection of the pledgee’s rights in the existing pledge to ensure the satisfaction of the pledgee’s rights from the pledged property, including protection from a decrease in the value of the pledged property, the pledging to others of assets subject of the existing pledge, or the debtor's use, sale, or lease of the pledged asset while pledged.

Paragraphs "C" and "D" of Article 364 of the United States Bankruptcy Code stipulates that the guarantees that can be provided to fund the Troubled project, which are:

(c) If the trustee is unable to obtain unsecured credit allowable under section 503(b)(1) of this title as an administrative expense, the Court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt.

(1) With priority over any or all administrative expenses of the kind specified in section 503(b) or 507(b) of this title.

(2) Secured by a lien on property of the estate that is not otherwise subject to a lien; or

(3) Secured by a junior lien on property of the estate that is subject to a lien.

(d)

(1) The Court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien only if—

(A) The trustee is unable to obtain such credit otherwise.

(B) There is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted.

(2) In any hearing under this subsection, the trustee has the burden of proof on the issue of adequate protection."

It is argued that the Court may authorize the Debtor to issue a debt secured by an equal or higher lien on the pledged assets. When all of the debtor's assets are pledged, this arrangement is typically proposed by debtors in possession. However, this is frequently opposed by the impacted secured creditors. As well as the debtor shall prove that the project is unable to obtain credit in any other way, (Dolny, 2023) in addition to that the interest of the creditors exists and is preserved despite this required credit (Triantis, 1993). This opinion is
consistent with Paragraph's "D" content of Article 184 of the Saudi Bankruptcy Law. In order to arranging a guarantee equal to or higher than previous pledges, the debtor shall prove to the Court that the pledgee’s rights in the current pledge will not be affected. It is an almost impossible hypothesis for the debtor because the imposition is that the debtor creates a new guarantee on its money that it previously provided as a guarantee for previous debts. Therefore, the previous creditor will be affected by the priority of the new creditor. Unless the debtor has other money that is not pledged for creditors, it has pledged money for a debt and the financing provider has decided that its debt shall be pledged with the money previously pledged. In order to achieve security for the first creditor in fulfilling its debt with the same priority that was available to him, the debtor can prove to the Court that the first creditor has priority in transferring another money. The only thing that will be transferred to another money with the same priority is its guarantee. There is another hypothesis addressed in Paragraph "D" of Article No. 184 of the Saudi Bankruptcy Law, which is that the creditor in the current pledge (i.e., the first) agrees to the existence of a pledge with a higher priority or equivalent to its priority over its pledge.

5.3. Secured Financing Are Being Applied to the Judiciary.

Article 183 of the Saudi Bankruptcy Law stipulates that “In a protective settlement procedure, small debtors' protective settlement procedure, financial restructuring procedure, and small debtors' financial restructuring procedure, a debtor may, after the initiation of the procedure, file a petition with the court for….”. It is clear from the previous text that the Competent Court shall approve secured financing. It also stipulates that the Court shall accept the request, therefore, the request shall include a report from an expert approved by the Court, in addition to the necessity of the invocation that the financing is necessary for the continuation of the debtor’s procedures or the preservation of the bankruptcy assets.

Section 364 of the United States Bankruptcy Code stipulates that in order to provide financing to Troubled projects. Additionally, it stipulates that the Bankruptcy Courts shall investigate the relationship between financing patterns and investment incentives. The Court will examine an important matter, which is the impact on the troubled company of both the high investment incentives and the lack of investment. The Court will examine an important matter, which is the impact on the troubled company of both the high investment incentives and the lack of investment (Triantis, 1993). The Troubled project will seek to provide investment incentives to attract financing, these incentives may affect the creditors rights. Therefore, the Court shall verify the impact of new investments on the rights of previous creditors. In order to prioritize project lenders after difficulty as a method of incentive, Courts shall be able to distinguish between financing solutions provided by the debtor in possession that enhance the value of the business and those that redistribute project assets across classes of investors and stakeholders.
Paragraph "C" of Section 510 of the United States Bankruptcy Code stipulates that "the Competent Court shall be entitled to hear bankruptcy disputes of the authority, to rearrange the liens on the debtor’s funds."\(^1\) Thereafter, according to the aforementioned text, the Court can cancel the creditor's lien and assign it to the general guarantee of the creditors.

The Competent Court to consider the financing request shall determine if the debtor's financing is effective and leads to maximizing the value of the company, or if the debtor's requested financing will not lead to maximizing the value of the company. The court shall verify whether the project faces a problem of lack or increase in investments and investments’ level. In other words, the court shall verify whether the project has investments or not. If the project does not have investments, investment incentives shall also be provided to attract investors. If the project has investments and yet the project troubled, these elements shall be evaluated through the following factors: the level of difficulty (i.e., the difference between liabilities and assets), the risks of the projects available to the company, whether the lender was the same before or after bankruptcy and whether the company intended to give the lender a high priority (Triantis, 1993). Using crowdfunding as a funding tool can support the projects (Avena & Grasis, 2023).

6. Cross-Guarantees in the United States Judiciary to rescue Troubled Projects:

The study targets Saudi law - which is somewhat modern - in providing the methods that enable Troubled projects to obtain financing. However, this modernity affected the practical applications of the Saudi Bankruptcy Law's provisions regulating the financing of Troubled projects. Whereas, the researchers searched at all 2213 rulings that are published on the Saudi Ministry of Justice's website\(^2\) on the application of Bankruptcy Laws. They failed to find any ruling that deals with a Bankruptcy Court's review of a financing request for a Troubled project. Accordingly, to support the comparative aspect of the study and to maximize its results, we discuss cross-guarantees and their applications in the United States judiciary, considering that they are considered a close application of the text of Paragraph "D" of Article 184 of the Saudi Bankruptcy Law.

The cross-guarantees are defined as the process of using an asset that represents guarantee for a loan as guarantee for a second loan. If the debtor is unable to pay the scheduled instalments of either loan on time, the affected lenders can eventually be forced to liquidate the asset and use the proceeds for repayment (Dingová et al., 2014). The other argued that the use of cross-collateralization to obtain financing after bankruptcy led to the creation of a disagreement between the judicial rulings and jurisprudence in their notes that are related to rulings. Some Courts approved financing orders based on cross-guarantees (Bohm, 1985). The Eleventh Circuit Court of Appeals in the United States of America ruled in the Adams Apple\(^3\) case that credit is extended

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\(^1\) (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or all or part of an allowed interest to all or part of another allowed interest; or (2) order that any lien securing such a subordinated claim be transferred to the estate.

\(^2\) https://www.moj.gov.sa/ar/Ministry/Departments/ResearchCenter/Pages/Alaf LarsCourtDoc.aspx

during the debtor’s appeal in compliance with the cross-guarantees provided by the Bankruptcy Court under Article 10.

One American judgment stated that “cross-guarantees” is a term that describes the process whereby a lender providing funds to a bankrupt debtor obtains a security interest over all of the debtor’s assets, whether for the new funds provided or the lender’s prior indebtedness. In other words, “cross-guarantees” means that the debtor’s equity in the pre-petition assets is used to secure the post-petition obligation to the creditor, and the debtor’s equity in the post-petition assets is used to secure the pre-petition obligation to the creditor. In the event of liquidation and it follows, both prior and subsequent obligations are paid before the unsecured debts.¹

On the other hand, in a judgment by the Second Circuit Court of Appeals², the court criticized the “cross-guarantees” in the Texlon case. But the court stopped short of banning this practice completely. At issue was the Bankruptcy Court’s unilateral financing order granting the lender a security interest in the debtor’s property to secure pre-petition and post-petition debts. The court concluded, “However, in order to decide this issue, we are not obligated to say that under no conceivable circumstances can ‘cross-guarantees’ be permitted.” Suffice it to say that...the financing scheme is completely inconsistent with the spirit of the Bankruptcy Law, as it shall not be granted by a unilateral order, as the Bankruptcy Court relies only on the declarations of the debtor who possesses that necessary credit. It is worth noting that the approach taken by the court in the aforementioned case was in light of the previous American bankruptcy law, which expired on October 1, 1974 AD, which is the date on which the new American Bankruptcy Code entered into force.

It is worth noting that the judicial judgements provided a definition of “cross-guarantees”, as one of the judgements states that “cross-guarantees” are “in exchange for providing new loans to a debtor in possession under Chapter 11, the financing institution obtains a security interest on all of the debtor’s assets, whether those existing at the date of the order or those established during Chapter 11 procedures, not only on new loans whose authenticity is undisputed, but also on its existing indebtedness”⁴. In another recent judgement, the Court defined “cross-guarantees” as “The practice of securing a pre-petition debt through a post-petition loan to the debtor is known as “cross-guarantees”⁴.

In this sense, “cross-guarantees” are considered a great incentive for previous creditors to provide new financing to the debtor, especially since the creditors shall be granted a lien on all of the debtor’s funds, and in application of this in a case whose facts are that Saybrook Manufacturing Co., Inc., and related companies (the Debtors), They commenced proceedings to obtain financing under Chapter 11 of the Bankruptcy Law on December 22, 1988. On December 23, 1988, the Debtors filed a motion to use cash collateral and to authorize the use of secured debt. The Bankruptcy Court issued an emergency financing order on the same day. At the


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time of the bankruptcy petition, the debtors owed Manufacturers Hanover approximately $34 million. However, the value of the guarantees for this debt was less than $10 million. Under the order, Manufacturers Hanover agreed to loan the debtors an additional $3 million to facilitate their reorganization. In exchange, Manufacturers Hanover obtained a security interest in all of the debtors’ property—both properties owned before the bankruptcy petition was filed and those acquired later. This security interest not only protected $3 million of post-petition credit, but also secured the Manufacturers Hanover’ $34 million pre-petition debt.1

The Georgia District Court judgement2 states that there are at least two types of cross-guarantees (1) pre-debt cross-guarantees with post-petition assets, also known as “forward cross-guarantees”, and (2) cross-guarantees of post-petition debt with pre-petition assets. The first type of cross-guarantees is strongly criticized as preferential if the claim of the advance lender obtaining the forward cross-guarantees is unsecured. The second type of cross-guarantees is entirely appropriate in the context of a post-petition loan as long as any existing creditor whose collateral is pledged by an equal or significant lien in favor of the lender is adequately protected as required under Article 364 (d)(b) of the Bankruptcy Law. Regarding the suitability of a pre-petition creditor to make a post-petition loan and guarantee the new loan with pre-petition and post-petition assets, this type of cross-guarantees is authorized under Article 364 (c)(2) and (d)(1) because these sections allow a lien on “property of the estate” to secure a post-petition loan. In Section 541 (a)(1) and (7), the law defines estate ownership “to include all legal and equitable interests of the debtor in the property as of the commencement of the case and any interest in the property acquired by the estate after the commencement of the case.”

The effect of forward cross-guarantees is to transfer post-petition assets that may be available for payment to ordinary unsecured creditors.3

The financing granted under Article 364 represents an important guarantee for the lender, as it enables it to recover its debt from the guarantees provided with priority over other creditors, as it was stated in a judgement issued by the Middle District Court in the State of Florida that “The Southpoint financing order also granted South Point a superior priority administrative claim under Law No.11 US Law 364(c)(1):

The Debtor's obligations to repay [South Point] the Financing Amount shall be granted "super-priority administrative expense status" under Article 364(c)(1) of the Bankruptcy Law, and trump any other claims under Article 364(c)(1) of the Bankruptcy Law, priority over all other claims against the Debtor, now existing or hereafter arising, of any kind, including, but not limited to, all administrative expenses of the kind specified in Sections 503(b) and 507(b) of the Bankruptcy Law (“Priority Claim”), without any proof of claim having to be filed. The Priority Claim filed by [South Point] shall be entitled to the full protection of Article 364(e) of the Bankruptcy Law if this Order is reversed or any provision thereof or modified, on appeal or otherwise.4

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The judiciary’s judgements on the priority system in demanding debt recovery commented that it constitutes a cornerstone in the practice and organization of financial reorganization.¹

7. Evaluating the effectiveness of funding troubled projects in the Saudi Bankruptcy Law

There is no doubt that funding troubled projects in the Saudi Bankruptcy Law is a good regulation, as it provides a legal basis for lenders to provide their financing to troubled companies. However, from the researchers’ point of view, this regulation needs some improvements to reach the results it aims to achieve, because, basically, obtaining financing for a non-faltering project is not an easy matter and undoubtedly requires guarantees from the proposal, and the loan provider shall verify the availability of internal resources for the project capable of servicing the loan, considering that the guarantee provided to secure the loan is a reserve guarantee, while the basis is for the project to generate self-resources that enable it to service the loan and fulfil its obligations.

If this is the case for a non-Troubled project, how it would be for a Troubled project, which suffers from a lack of trust from his clients' mistrust and inability to meet its debts; By extension, there is a lack of cash, so it is almost impossible. This is evidenced by the fact that Saudi judicial judgements published over four years did not refer to an application for financing to the Bankruptcy Court and at our discretion, if we recognize the importance of cash liquidity for any project, as well the financing is one of the means of achieving that liquidity, However, it is inconceivable that legislative regulation shall solve unilaterally the crisis of project financing in general and the financing of Troubled projects in particular. Because if we are looking for a solution to a Troubled project to manage liquidity for its revival, it is first and foremost one project and it is not logical to introduce a financed project to finance an unthinkable project so that ultimately the result is that we are in front of both a lender and a borrower that are struggling. There shall therefore be an increasing cycle of project default and bankruptcy, which is not targeted by the project, and the solution in our estimation lies in two things:

First: Establishing a fund to support Troubled projects, which shall be as close as possible to social security, so that it is received from contributions paid by the companies themselves, under the authority of the Ministry of Commerce and the Ministry of Finance, and if any project providing financing from this fund is hindered. When the project is liquidated, the project receives a sum from the fund from which it shall pay its financial obligations.

Second: The State shall provide initiatives to finance Troubled projects so that the State directly intervenes in the dismissal of the troubles of Troubled projects and provides them with the necessary financing to dismiss them. The State may intervene as a partner in the project or provide the necessary financing to provide them with the necessary liquidity for the project. In fact, Saudi Arabia has some programs and initiatives that concern

https://casetext.com/case/czyzewski-v-jevic-holding-corp
the financing of Troubled projects, especially in the agricultural, health and education sectors. Some of these programs and initiatives are:

- **Addressing Troubled projects**: is a program provided by the Agricultural Development Fund in cooperation with the Ministry of Environment, Water and Agriculture and investors wishing to invest in Troubled agricultural projects. The program provides financial, technical and administrative solutions to restart these projects and improve their productivity and quality.

- **Project Support Fund**: An initiative by the Ministry of Finance through the National Development Fund to finance Troubled projects in the health and education sectors. The initiative aims to stimulate investment in these sectors and provide quality health and education services to citizens.

**CONCLUSION**

This study deals with the financing of Troubled projects in Saudi Bankruptcy Law by indicating the rules governing this means of rescuing the struggling debtor and returning him to his normal economic activity as he was before. The study compared with the United States Bankruptcy Law as one of the old laws that dealt with this method, and there were many judicial judgements applying that method. The study found several conclusions, most notably:

- **First**: Business Troubled project as a business facing incidental circumstances that has influenced the results of its work, but has the potential to reform its progress and improve its troubles if there are reasons and financial resources to do so.

- **Second**: The UNCITRAL at the United Nations was interested in providing the troubled companies with access to funds, as confirmed by the UNESTRAL Model Law on Insolvency.

- **Third**: It does not mean that the project suffered financial hardship resulting in its stumbling over or bankruptcy that the project shall be liquidated immediately, on the contrary, comparative legislation seeks to give Troubled projects the possibility to make amends with continue its influential position in the market.

- **Fourth**: The financing of Troubled projects is one of the most important means by which projects can get out their difficulties. If the debtor obtains the financing, either the creditor's consent or the court's authorization for such financing shall be obtained after the creditors have ascertained that their debts will not be adversely affected by the required financing.

- **Fifth**: Regulating the financing of Troubled projects aims not only to legitimize the financing of such projects, but also to enable the debtor to provide incentives to lenders in the form of high priority, without which lenders are unable to make their financial claims to lenders.

- **Sixth**: New financing can be obtained internally or externally. The internal sources of the new financing are current equity shareholders' contributions, disposal of assets or divestment, shareholder loans, or even through the funds contributed by companies to the company’s cumulative profit reserves over time.

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1. [https://adf.gov.sa/ar/CreditServices/TroubledProjects/Pages/default.aspx](https://adf.gov.sa/ar/CreditServices/TroubledProjects/Pages/default.aspx)
2. [https://www.mof.gov.sa/PSF/Pages/Apply.aspx](https://www.mof.gov.sa/PSF/Pages/Apply.aspx)
external level, troubled borrowers may issue shares, obtain loans, issue bonds or other forms of debt instruments.

**Seventh:** Some judgements issued by the British and American judiciary are required by the controlling shareholder of the Troubled project to provide credit to the project, considering that it is the cause of the troubles. However, that trend is difficult to accept in Saudi Companies Law either the controlling party abuses the management of the company and assigns its personal responsibility or vice versa, and the company therefore is responsible for its debts because the source of the obligation to provide credit is the contract.

**Eighth:** Guarantees play a pivotal role in incentivizing lenders to finance debtors in order to overcome the hesitancy surrounding the financing of Troubled projects, since professional lenders shall not provide financing for a private project and it is Troubled or bankrupt unless there are sufficient guarantees for the lender's security.

**Ninth:** paragraph (d) in Article 184 of the Saudi Bankruptcy Law represents the basis for funding troubled projects due to their organization priorities over the pledged money However, the hypothesis of the practical application here question remains to be considered as a result of the debtor's difficulty in proving to the court that the rights of the existing pledge holder shall not be affected by the new pledge, This shall be achieved only if the old pledge is transferred to new money on the basis of the imposition of new, unpledged money.

**Tenth:** The Bankruptcy Court's authority to consider the application is not discretionary for three conditions; I) Do not prejudice the existing or core creditor that seeks to arrange a higher or equal priority right for the debtor, II) Submit a report from a court-certified expert, III) It shall be shown that the financing is necessary for the debtor's continued activity or the preservation of bankruptcy assets.

**Eleventh:** Cross-Guarantees in US Code is a practical application of the text of the paragraph (d) in Article 184 of the Saudi Bankruptcy Law, and the problems encountered by the United States judiciary in applying cross-guarantees shall be the same as those that will be brought before the Saudi judiciary. However, the problem in applying the text of the Saudi judiciary remains that the previous priorities established by the debtor over its funds and related to the rights of creditors shall be respected. Otherwise, any legal value of legal guarantees and prioritization would be lost.

**Recommendations:**

**First:** The study recommends establishing a fund to support Troubled projects, to be derived from contributions paid by the companies themselves in the same way as Social Security, under the authority of the Ministry of Commerce and the Ministry of Finance, and if any project providing financing from this fund is hindered. When the project is liquidated, the project receives an amount from the fund from which it shall pay its financial obligations.

**Second:** The study recommends establishing a government fund to support Troubled projects, dividing financing priorities according to the project's relevance to the national economy, and these loans are of no interest.
Third: The study recommends adding an article of the Saudi Bankruptcy Law whereby the State will forfeit its debts for Troubled projects provided that the financial restructuring plan or the bankruptcy settlement is successful.

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Court Judgments:


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