INSOL International

Module 5C

Guidance Text

Cayman Islands

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INSOL INTERNATIONAL
FOUNDATION
CERTIFICATE
in INTERNATIONAL INSOLVENCY LAW

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1. INTRODUCTION TO INTERNATIONAL INSOLVENCY LAW IN THE CAYMAN ISLANDS

Welcome to **Module 5C**, dealing with the insolvency system of the **Cayman Islands**. This Module is one of the elective module choices for the Foundation Certificate. The purpose of this guidance text is to provide:

- a general overview, including the background and history, of Cayman's insolvency laws;
- a relatively detailed overview of Cayman's insolvency system, dealing with both corporate and consumer insolvency; and
- a relatively detailed overview of the rules relating to international insolvency and how they are dealt with in the context of the Cayman Islands.

This guidance text is all that is required to be consulted for the completion of the assessment for this module. You are not required to look beyond the guidance text for the answers to the assessment questions, although bonus marks will be awarded if you do refer to materials beyond this guidance text when submitting your assessment.

Please note that the formal assessment for this module must be submitted by **11 pm (23:00) BST on 31 July 2021**. Please consult the web pages for the Foundation Certificate in International Insolvency Law for both the assessment and the instructions for submitting the assessment. Please note that no extensions for the submission of assessments beyond 31 July 2021 will be considered.

For general guidance on what is expected of you on the course generally, and more specifically in respect of each module, please consult the course handbook which you will find on the web pages for the Foundation Certificate in International Insolvency Law on the INSOL International website.

2. AIMS AND OUTCOMES OF THIS MODULE

After having completed this module you should have a good understanding of the following aspects of insolvency law in the Cayman Islands:

- the background and historical development of the Cayman Islands insolvency law;
- the various pieces of primary and secondary legislation governing Cayman insolvency law;
- the operation of the primary legislation in regard to liquidation and corporate rescue;
- the operation of the primary and other legislation in regard to corporate debtors;
- the rules of international insolvency law as they apply in the Cayman Islands;
- the rules relating to the recognition of foreign judgments in the Cayman Islands.

After having completed this module you should be able to:

- answer direct and multiple-choice type questions relating to the content of this module;
- be able to write an essay on any aspect of Cayman insolvency law; and
- be able to answer questions based on a set of facts relating to Cayman insolvency law.

Throughout the guidance text you will find a number of self-assessment questions. These are designed to assist you in ensuring that you understand the work being covered as you progress through the text. In order to assist you further, the suggested answers to the self-assessment questions are provided to you in Appendix A.

3. AN INTRODUCTION TO THE CAYMAN ISLANDS

The Cayman Islands is located in the western Caribbean Sea to the south of Cuba and Miami. The territory comprises three islands: Grand Cayman, Cayman Brac and Little Cayman.

Grand Cayman is by far the largest and most populous of the three islands and is where all of the Islands' financial services industry is based. The total population of the three islands is approximately 60,000.

3.1 Government

The Cayman Islands is a British Overseas Territory.

England took formal control of the Cayman Islands, along with Jamaica, as a result of the Treaty of Madrid of 1670. The islands continued to be governed as part of the Colony of Jamaica until 1962 when Jamaica became independent of England.

Since 1962 the Islands have been directly overseen by the UK. The UK Foreign and Commonwealth Office appoints a Governor. The Governor has responsibility for matters such as National Security, Foreign Affairs, Police and Immigration.

For all matters not falling within the province of the Governor, the Cayman Islands has a democratically elected local government. The insolvency laws of the Cayman Islands are within the remit of the local government. The local government works closely with the private sector and judiciary to ensure such laws serve the needs of the Cayman Islands financial services industry and the local population.

3.2 Tax and financial services

The Cayman Islands has always been a tax-exempt jurisdiction and has never levied income tax, capital gains tax, or any wealth tax.

This tax "neutrality", coupled with business friendly laws and a wealth of experienced professionals practicing in Grand Cayman, has been largely credited with helping the Islands to become a thriving offshore financial centre.

At the time of writing there are some 100,000 companies registered in the Cayman Islands including more than 280 banks, 700 insurers, and 10,500 mutual funds. The Cayman Islands also has its own stock exchange which was opened in 1997.

The US remains the largest source of foreign direct investment followed by Hong Kong, Europe and Brazil. There has also been a substantial increase in investment from Japan in recent years.

Outward direct investment from the Cayman Islands goes to Luxemburg, the US, Hong Kong, Europe and the People's Republic of China.

3.3 Tourism

The pristine beaches and coral reefs mean that tourism is the second pillar of the Cayman Islands economy. The tourist industry is aimed at the luxury market and caters mainly to visitors from North America.

The Cayman Islands offers the highest standard of living in the Caribbean (reputedly comparable to that of Switzerland).

4. LEGAL SYSTEM AND INSTITUTIONAL FRAMEWORK

4.1 Legal system

As mentioned above, the Cayman Islands has been controlled by England since the 17th century. The Cayman Islands legal system is therefore based on the English model.

In terms of the laws which are in force in the Cayman Islands, the English common law applies save to the extent that it has been modified by Cayman Islands statute.

Although the insolvency laws of the Cayman Islands have been placed on a statutory footing, the legislation is largely inspired by UK legislation with the common law of England filling in any gaps in the law.

Since the same basic principles as those underlying the insolvency regime in the United Kingdom apply, the Cayman Islands system will be quite familiar to English and other commonwealth practitioners.

The doctrine of judicial precedent applies in the Cayman Islands and so case law is important. The similarities between the Cayman Islands and English laws mean that decisions from English courts and other Commonwealth countries, while not binding, are frequently cited and are of persuasive authority.

4.2 Institutional Framework

4.2.1 Tiered court system

The Cayman Islands court system is split into three tiers at a local level: the Summary Court, the Grand Court and the Court of Appeal.

Minor civil and criminal matters are tried by professional magistrates sitting in the Summary Court. The Summary Court is not relevant for the purposes of this course.

The Grand Court, on the other hand, is the court of most relevance to the insolvency practitioner. It is a superior court of record (with powers equivalent to the High Court of England and Wales) and it is where insolvency proceedings are initiated.

The Grand Court administers locally enacted laws, the common law and the law of equity of England as well as any imperial legislation which may be passed in London from time to time (although the latter is rare).

The Grand Court has five divisions to manage cases:

- Admiralty;
- Civil;
- Criminal;
- Family; and
- Financial Services Divisions.

It is the Financial Services Division (FSD) that deals with insolvency proceedings.

4.2.2 Substantive law

Until 2008, the law relating to corporate insolvency was derived from three basic sources, namely:

- Part V of the (Cayman Islands) Companies Law (as revised);
- the English Insolvency rules 1986; and
- local case law

Part V of the Companies Law was a direct reproduction of the English Companies Act 1862 (as re-enacted in 1962).

In 2008, following a review of the law by the Cayman Islands Law Reform Commission in 2006 (in conjunction with the private sector), the law was substantially overhauled to bring it up to speed with the demands of a modern, international business centre and to serve the needs of the financial services industry.

The substantive law is now contained largely in the Companies Law (2018 Revision), the Exempted Limited Partnerships Law (2018 Revision) and case law. The relevant sections of these laws will be dealt with below.

4.2.3 Procedural rules

Proceedings in the Grand Court generally are governed by the Grand Court Rules (as revised). These rules contain requirements of general application, for example, the rules for lawful service of documents, the filing of affidavit evidence and so forth.

Proceedings relating to the winding up of companies, however, are specifically governed by the Companies Winding Up Rules (2018) (CWR) and certain judge issued practice directions.

4.2.4 FSD

The dedicated Financial Services Division of the Grand Court opened in November 2009. The FSD has greatly enhanced the Cayman Islands as a forum for international litigation and dispute resolution and has resulted in the expedited resolution of complex commercial disputes.

4.2.5 Appeal

Appeals from the Grand Court lie to the Cayman Islands Court of Appeal in the first instance.

Further appeal lies, as appropriate, to the Judicial Committee of the Privy Council in London.

There is also a right of petition to the European Court of Human Rights once all other domestic legal remedies have been exhausted.

4.2.6 Case law and precedent

Some decisions of the Grand Court and all decisions of the Court of Appeal and the Privy Council on appeals from the Cayman Islands, are reported in the Cayman Islands Law Reports (CILR). These reports are not yet freely available to the public; however, local practitioners receive automatic access to the CILR upon payment of their annual practicing certificates.

Decisions of the Cayman Islands Court of Appeal and decisions of the Privy Council which arise from appeals originating in the Cayman Islands are binding on the Grand Court. Decisions of the Courts of England and Wales and in appropriate cases other Commonwealth or common law jurisdictions are highly persuasive. Decisions handed down from the higher courts in the United Kingdom, other Commonwealth countries and the Privy Council are therefore cited frequently.

4.2.7 Judges

The Grand Court judiciary consists of the Chief Justice and five other full-time judges supplemented by acting, visiting judges from overseas as the need arises. Specialist commercial judges sit in the FSD.

4.2.8 Informal restructuring

There is no requirement in the Cayman Islands insolvency legislation for consensual restructuring negotiations to take place before the commencement of the statutory process (indeed the legislation is silent on the matter).

Such negotiations do take place, however, not least because company management and lenders are commonly situated onshore, meaning that contemporary onshore practices influence the offshore strategy.

It is also helpful to be able to demonstrate to the Cayman court, when making an application for restructuring (such as a scheme of arrangement coupled with an order for provisional liquidation), that positive, consensual restructuring discussions have been taking place prior to the application being made.

4.2.9 Moratorium

If an entity requires protection from creditor enforcement (for example, in order to negotiate a scheme of arrangement), it will need to place the entity into provisional liquidation in order to trigger a stay. This requires the appointment of a provisional liquidator and an explanation, to the Grand Court, as to why the directors believe that the company's affairs can be turned around by such a scheme. This process is dealt with in detail under paragraph 6.5 below.

4.2.10 Secured creditors

A creditor with security over an asset of a company is entitled to enforce its security even after the company is placed into official liquidation or provisional liquidation. The secured creditor may do so without the leave of the Grand Court and without any reference to the company's liquidator.[1]

A secured creditor whose debt is more than the value of his security may prove in the liquidation for the unsecured balance. In such circumstances, the proof of debt submitted by the secured creditor must state particulars of the security and the value which he or she places on the security.

For more on this topic, see paragraph 5 below.

4.2.11 Unsecured creditors

An unsecured creditor has the right to file a winding-up petition in respect of a debtor company.

4.2.12 No insolvency regulator

The Cayman Islands does not have an insolvency regulator.

It should be noted, however, that the Cayman Islands Monetary Authority (CIMA) has powers to appoint Controllers over any of the entities it is charged with licensing and supervising (such as banks, trust companies, regulated mutual funds). This includes the power to take control of the entity at board level and apply for the winding-up or reorganisation.

Self-Assessment Exercise 1

Question 1

On which legal system is the Cayman Islands system loosely based?

Question 2

To which court or courts may a litigant appeal following receipt of an adverse decision at first instance?

[1] CWR, O.17.

Question 3

Which law or laws govern insolvency in the Cayman Islands?

For commentary and feedback on self-assessment exercise 1, please see APPENDIX A

5. SECURITY

In the Cayman Islands, security may be taken over immovable and movable assets.

Pursuant to section 142 of the Companies Law, notwithstanding that a winding-up order has been made, a creditor that has security (over the whole or part of the assets of a company) is entitled to enforce its security without the leave of the Court and without reference to the liquidator. There is no stay on enforcement by secured creditors similar to Chapter 11 proceedings in the USA.

5.1 Immovable property

The following are the most common forms of security rights which may be granted over immovable property:

5.1.1 Mortgage

Security over real property (freehold or leasehold) is usually granted by mortgage. There are two different types of mortgage:

5.1.1.1 Legal mortgage

This is where the lender (mortgagee) holds legal title to the property as security for a debt. The debtor / borrower (mortgagor) retains possession of the property and recovers legal ownership once the secured debt is discharged. If the debtor defaults, the secured creditor will be permitted to take possession and exercise its power of sale with respect to the property, or appoint a receiver to realise the real property.

Legal mortgages over certain types of property must be created by deed and validly executed. The Register of Lands must be updated.

5.1.1.2 Equitable mortgage

This is where the debtor / borrower (mortgagor) transfers the beneficial or equitable interest in the property to the lender (mortgagee) while retaining possession and legal interest in the property.

Generally, the mortgagee does not have a right to take possession of the collateral; however, the mortgage agreement may contain a power of attorney in favour of the secured creditor permitting it to execute a transfer of land document to transfer the property into its name upon default.

In the absence of a power of attorney provision, the secured creditor will need to apply to court for specific performance. The court may then convert the equitable mortgage into a legal mortgage conferring associated rights and powers.

An equitable mortgage does not take priority over a third party who has no notice of the security interest and who acquires legal title to the property in good faith and for value (a *bona fide* purchaser). It is therefore a weaker form of security compared to a legal mortgage.

Equitable mortgages can be in writing and are usually created by deed.

5.1.2 Fixed charge

A fixed charge gives the creditor the right to take possession of the charged property (and sell it) if the borrower defaults.

Once the property is sold, the creditor may apply the proceeds of sale to the debt owed to it.

The charged property is not deemed to be an asset of the debtor in the event of insolvency.

The debtor cannot sell the charged property without the creditor's consent.

Fixed charges must be in writing and are typically created by deed.

5.2 Movable property

The most common forms of security taken over movable property are:

5.2.1 Mortgage

Mortgages are commonly used as security over ships and aircraft. Such mortgages need to be registered on the respective vessel or aircraft registry.

Mortgages over shares are also common in the Cayman Islands. This is achieved by an agreement to create a mortgage, the entry of the secured creditor's name into the register of members as the holder of the shares and the deposit of the relevant share certificate, if any, with the secured creditor.

5.2.2 Fixed charge

See the explanation of fixed charges over immovable property above.

5.2.3 Floating charge

A floating charge is typically taken over a class of assets that change from day to day. Often, a secured creditor will take fixed charge over specific assets together with a floating charge over all other assets not covered by the fixed charge. Both types of charge are created by contract (or by operation of law).

The floating charge does not attach to a particular asset, but hovers over one or more assets. Such a charge is usually taken over a debtor's inventory or its entire business.

Unlike the fixed charge, the debtor can deal with its charged assets, subject to the terms of the charge, without the creditor's consent.

Upon the occurrence of a specified event of default, the floating charge "crystallises" and converts into a fixed charge which then attaches to the debtor's specific assets at that point in time.

If for any reason the floating charge has not crystallised at the commencement of the liquidation of the debtor, the assets continue to be assets of the debtor for the purposes of the liquidation. The chargee's claim, however, will have priority over the claims of any unsecured creditors.

5.2.4 Pledge (also known as bailment)

A pledge is a legal form of security which is created by contract and perfected through by delivery of possession of the asset to the secured creditor. Such delivery can be actual or constructive.

An asset may be pledged as security for a loan. In the event of default on the loan, the lender has the right to take possession of the pledged asset and sell it.

The requirement for delivery means that this is only used for movable assets.

5.2.5 Lien

This is similar to a pledge; however, a lien gives a creditor the right to keep possession of an asset that belongs to the debtor until the debt is paid. The creditor is only entitled to retain the asset in its possession; it is not entitled to sell the asset if the debtor defaults. Liens are created by contract, common law and / or statute.

5.3 Registering security

The Cayman Islands does have ownership registers for real estate,[2] ships,[3] aircraft,[4] motor vehicles and intellectual property.[5] These registers are centrally maintained and mortgages and charges can be registered. A third-party purchaser of those assets will be deemed to have notice of any such interest and will therefore acquire the asset subject to the secured creditor's interest.

There is no public security registration regime in the Cayman Islands for other assets. A creditor must therefore take adequate steps to ensure that it has sufficient control over an asset to prevent a third party from purchasing it. Any creditor should therefore review a company's register of mortgages and charges prior to making a loan (see below).

Section 54 of the Companies Law requires that security interests be entered in the register of mortgages and charges of the debtor company. The register must be maintained by the company at its registered office in the Cayman Islands. Failure of a company to update the register of mortgages and charges does not, in and of itself, invalidate any security interests.

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2 Registered Land Law.
3 Maritime Authority Law.
4 Civil Aviation Authority Law and Mortgaging of Aircraft Regulations.
5 https://www.ciipo.ky/laws/.

Registering a security interest in the company's register of mortgages and charges does not create priority. However, the register is open for inspection by any member of the company or creditor and therefore registration does put third parties on notice of the existence of a security.

Under Cayman Islands conflict of laws rules, the relevant law governing the priority and perfection of security interests will be determined by the location of the asset.

Self-Assessment Exercise 2

Question 1

Name the common forms of security in the Cayman Islands for immovable property.

Question 2

Name the common forms of security in the Cayman Islands for movable property.

Question 3

How can a lender ensure that other people have notice of its secured position?

For commentary and feedback on self-assessment exercise 2, please see APPENDIX A

6. INSOLVENCY SYSTEM

6.1 General

The Cayman Islands has a fragmented insolvency system in that different laws must be consulted depending on whether one is dealing with a personal or corporate debtor.

Personal Insolvency is governed by:

- The Bankruptcy Law (Cap 7) (1997 Revision); and
- The Grand Court (Bankruptcy) Rules 1977, as amended.

Corporate Insolvency in the Cayman Islands is regulated by:

- The Companies Law (2018 Revision);
- The Companies Winding Up Rules, 2018;
- The Insolvency Practitioners' Regulations 2018; and
- The Foreign Bankruptcy Proceedings (International Cooperation) Rules 2018.

The Cayman Islands is regarded as a creditor-friendly jurisdiction. Creditors are not treated differently based on whether they are based in the Cayman Islands or elsewhere. The Cayman Islands has taken a conscious decision to remain creditor-friendly in order to continue to attract international business.

6.2 Personal / consumer bankruptcy

Personal bankruptcy is virtually unheard of in the Cayman Islands, which no doubt accounts for the rather outdated legislation in this regard in the Cayman Islands.

6.2.1 Legislation

As stated above, individual insolvency is governed by:

- The Bankruptcy Law (Cap 7) (1997 Revision); and
- The Grand Court (Bankruptcy) Rules 1977, as amended.

6.2.2 Court

The Grand Court is the Chief Court of Bankruptcy, which hears all applications for personal bankruptcy.[6]

6.2.3 Who qualifies as a "debtor"

Section 2 of the Bankruptcy Law defines a "debtor" so as to include any person who at the time when any act of bankruptcy was done or suffered by him –

- was personally present in the Islands;
- ordinarily resided in, or had a place of residence in, the Islands;
- was carrying on business in the Islands, personally or by means of an agent or manager; or
- was a member of a firm or partnership which carried on business in the Islands.

6.2.4 Commencement of proceedings

Proceedings may be commenced by filing a petition with the Grand Court.[7] A debtor may present a bankruptcy petition against himself and a single creditor, or two or more creditors, may present a bankruptcy petition to the Court against a debtor, provided the aggregate amounts of debt owing are not less than KYD 40.

6.2.4.1 Grounds for petition (Acts of Bankruptcy)

A debtor may present a bankruptcy petition against himself without alleging any grounds.[8] However, the petition must be accompanied by a statement setting out details of the debtor's financial affairs.[9]

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6 Bankruptcy Law, s 3(1).
7 *Idem*, s 4.
8 *Idem*, s 15.
9 *Idem*, s 17.

Creditors applying for the bankruptcy of a debtor must allege at least one "act of bankruptcy" from the following list:[10]

(a) that the debtor has, in the Islands or elsewhere, made a conveyance or assignment of his property to a trustee or trustees for the benefit of his creditors;

(b) that the debtor has, in the Islands or elsewhere, made a fraudulent conveyance, gift, delivery or transfer of his property or any part thereof;

(c) that the debtor has, with intent to defeat or delay his creditors, departed out of the Islands, departed from his dwelling-house, otherwise absented himself, begun to keep house or begun to sell his stock-in-trade at an under-value;

(d) that the debtor has, by any act, declared himself unable to meet his engagements;

(e) that the debtor has presented a bankruptcy petition against himself;

(f) that execution issued in the Islands against the debtor on any legal process for the obtaining of payment of any sum of money has been levied by seizure and sale of his goods, or enforced by delivery of his goods;

(g) that the creditor has served on the debtor a summons in an action in the Grand Court wherein the creditor claims payment of a liquidated sum of not less than KYD 40;

(h) that the creditor presenting the petition has obtained final judgment against the debtor for not less than KYD 40 and has served on the debtor in the Islands a bankruptcy notice in writing and the debtor has not, within seven days after the service of notice, paid such amount;

(i) that the debtor has not paid an obligation of not less than KYD 40 upon a negotiable security within 14 days;

(j) that the debtor has, in the Islands or elsewhere, made any conveyance or transfer of his property which would be void as a fraudulent preference if he were adjudged bankrupt;

(k) that the debtor has, in the Gazette and in a newspaper circulated in the Islands, given notice of his intention to convey, assign or transfer his stock-in-trade, debts or things in action relating to his business to any other person; and that the creditor, having a demand against the debtor of not less than KYD 40, has served on the debtor in the Islands a bankruptcy notice in writing, and that the debtor has not, within seven days after the service of such notice, paid such amount.

(l) that the debtor has paid money to or given or delivered any satisfaction or security for the debt of a petitioning creditor, or any part thereof, after such creditor has presented a bankruptcy petition against him:

[10] *Idem*, s 14.

In addition to establishing one of the above acts:

- the alleged act of bankruptcy must have occurred within six months before the presentation of the petition; and

- the debt of the petitioning creditor must be a liquidated sum due, or growing due at law or in equity, and must not be a secured debt.

6.2.4.2 Provisional order

After the presentation of a petition, if the court is satisfied of the evidence of the creditor's debt, the court will make a provisional order that the affairs of the debtor shall be wound up and his property administered under the law.[11]

6.2.4.3 Service and notice to show cause

The provisional order is served on the debtor, together with a notice that within a specified number of days the debtor may show cause why the provisional order should be revoked.[12]

6.2.4.4 Revocation of provisional order

If the debtor, within the time appointed, shows to the satisfaction of the Court that either the proof of the petitioning creditors debt, or of the act of bankruptcy, is insufficient, the Court must revoke the provisional order and, unless it sees good cause to the contrary, will order costs to be paid to the debtor.[13]

6.2.4.5 Statement of affairs

If the debtor does not show cause why the provisional order must be revoked, an order is served on the debtor requiring him to file, within the specified number of days, a statement of his affairs.[14]

6.2.4.6 Absolute order

If the debtor fails to comply with the order to file his statement of affairs, or to show a sufficient excuse for not having complied with it, the Court may, on the application of any creditor, make an absolute order for bankruptcy against the debtor.[15]

6.2.5 Stay

All proceedings to recover debts are stayed upon the making of a provisional or absolute order[16] unless leave of the Court is obtained.[17]

The effect of the provisional order is retroactive (to the date of the proven "act of bankruptcy").[18]

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11 *Idem*, s 29.
12 *Idem*, s 30.
13 *Idem*, s 31.
14 *Idem*, s 32.
15 *Idem*, s 33.
16 *Idem*, s 34(1).
17 *Idem*, s 35(2).
18 *Idem*, s 35.

Secured creditors: This stay does not affect the power of any secured creditor to realise or otherwise deal with his security in the same manner as he could have done prior to the making of the provisional or absolute order.[19] Secured creditors may appoint receivers to enforce security rights (see below).

6.2.6 *Property vests in Trustee in Bankruptcy*

Upon a provisional or absolute order being made, the property of the debtor immediately passes to, and vests in, the Trustee in Bankruptcy (Trustee).[20]

The Trustee is attached to the Court. It administers the estates of debtors in bankruptcy subject to the Bankruptcy Law.

6.2.7 *Powers and duties of Trustee*

Until the provisional order is made absolute, it is the duty of the Trustee to preserve the property such that it may be returned to the debtor in the event the provisional order is revoked.[21]

The Trustee may carry on the trade of the debtor so far as may be necessary or expedient for the beneficial winding up or sale of the business.[22]

The Trustee may bring, institute or defend any legal proceedings relating to the property of the debtor.[23]

The Trustee must receive and decide on the proof of debts.[24] The manner in which proof of debts must be filed is set out in the Grand Court (Bankruptcy) Rules 1977.

Once an absolute order has been made, the Trustee must proceed to administer the debtor's estate for the benefit of the creditors.[25]

6.2.8 *Allowances to debtor for support*

The Trustee may, from time to time, make such allowances as he thinks just to the debtor out of the debtor's property for the support of the debtor and his family, or in consideration of the debtor's services if he is engaged in the winding up of his own estate.[26]

6.2.9 *Onerous and unprofitable property*

The Trustee may disclaim onerous and unprofitable property in certain prescribed circumstances. These circumstances, and the effects of such disclaimer, are set out in section 105 of the Bankruptcy Law.

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19 *Idem*, s 34(3).
20 *Idem*, s 37.
21 *Idem*, s 38.
22 *Idem*, s 79.
23 *Idem*, s 80.
24 *Idem*, s 87.
25 *Idem*, s 65.
26 *Idem*, s 137.

6.2.10 Duty to aid Trustee

The debtor has a duty to aid the Trustee in the realisation of his property and the distribution of the property among his creditors.[27] Failure to do so amounts to contempt.[28]

6.2.11 Meetings of creditors

The Court must, as soon as practicable after the provisional order, summon a general meeting of the creditors of the debtor. Such a meeting will not take place if an absolute order has been made.[29]

Various rules, which are beyond the scope of this module, govern such meetings. These rules include:

- A person is not entitled to vote at such a meeting unless he has, in the prescribed manner, proved a debt that is due to him; and
- A secured creditor will only be deemed to be a creditor for the purposes of voting in respect of any balance due to him.

At the meeting the creditors may, by the votes of a majority in value of the creditors present, personally or by proxy,[30] resolve:

- the petition be stayed, the affairs of the debtor wound up and his property administered under a "deed of arrangement"; or
- that adjudication of bankruptcy be made.

6.2.12 Deed of arrangement

A deed of arrangement may be entered into between a debtor and his creditors,[31] provided the deed is assented to by a majority in number (that is, 50%) representing 75% in value of the creditors of the debtor who have proved their debt.

The deed of arrangement must be taken into consideration by the court, but before the deed is considered by the court the debtor must submit himself to the public examination of the Court and the Trustee must make a report to the Court under section 67 of the Bankruptcy Law.[32]

The court will confirm the deed if it appears to be in the interest of the creditors generally that it should be so confirmed. Only then will the deed become binding on all creditors and the debtor.

If a deed is so approved, the terms of the deed will provide for the date and circumstances in which the debtor will ultimately be discharged.[33]

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27 *Idem*, s 39.
28 *Idem*, s 40.
29 *Idem*, s 41.
30 *Idem*, s 44.
31 *Idem*, s 48.
32 *Idem*, s 50.
33 *Idem*, s 55.

6.2.13 Absolute orders

When an absolute order for bankruptcy has been made against a debtor, a public examination of the affairs of the debtor must take place. The debtor must attend and submit to examination.[34]

If it appears to the Court that the debtor has failed to keep proper books of account or that he has incurred debt by breach of trust or without having had any reasonable expectation of being able to repay such debt, the Court has the discretion to imprison him.[35]

6.2.14 Trustees report

It is the duty of the Trustee, as soon as possible after the close of the public examination of the debtor, to make a report as to the state of the debtor's affairs and as to the conduct of the debtor before and during the bankruptcy.[36]

In particular, the Trustee is required to note in his report any matters which might constitute offences under the Bankruptcy Law and / or which would justify the Court refusing, suspending or qualifying an order for the debtor's discharge.

6.2.15 Divisible property

When a provisional order has been made against a debtor, his property becomes divisible between his creditors in proportion to the debts owed.

The property of the debtor divisible amongst his creditors and vesting in the Trustee will be comprised of:[37]

(a) all such property as may belong to, or be vested in, the debtor at the commencement of the bankruptcy or which may be acquired by, or devolve on, him at any time previous to his discharge;

(b) the capacity to exercise, and to take proceedings for exercising, all such powers in, or over, or in respect of, property as might have been exercised by the debtor;

(c) all goods and chattels being at the commencement of the bankruptcy in the possession of the debtor.

6.2.16 Non-divisible property

The following property of the debtor is not available to satisfy claims:[38]

(a) property held by the debtor on trust for any other person; or

(b) the tools, if any, of his trade, the clothes and bedding of himself, his wife and children to a value not exceeding KYD 60 in the whole.

In addition, marital property may be exempt depending on the date and circumstances of its settlement.

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34 *Idem*, s 62.
35 *Idem*, s 64.
36 *Idem*, s 67.
37 *Idem*, s 100.
38 *Idem*, s 100(i-ii).

6.2.17 Secured creditors

A secured creditor may on giving up his security prove for his whole debt, or he may prove for any balance due to him after realising or giving credit for the value of his security.

6.2.18 Priority creditors

The following debts are paid in priority to all other debts:[39]

(a) all public taxes imposed by law due from the debtor at the date of the provisional order not exceeding in the whole one year's taxes;

(b) all wages or salary of any clerk or servant in respect of services rendered to the debtor for four months next preceding the date of the provisional order, not exceeding KYD 100; and

(c) all wages of any labourer or workman in respect of services rendered to the debtor for four months next preceding the date of the provisional order.

These debts rank equally and must be paid in full unless the property of the bankrupt is insufficient to meet them.

6.2.19 Preferences and void payments

Such payments are governed by Part XVII of the Bankruptcy Law.

Any conveyance, transfer, charge or payment made by a debtor in favour of any creditor, with a view of giving such creditor a preference over the other creditors, must, if a provisional order takes effect within six months, be deemed fraudulent and void as against the Trustee.

Any disposition, made by any trader unable to pay his debts, of his stock-in-trade or things in action relating to his business, otherwise than in the ordinary course of business, shall, if a provisional order or an absolute order takes effect within six months, be deemed fraudulent and void as against the Trustee, except in the following circumstances:

(a) if the dispositions were made and executed with the assent of 75% in number and value of the creditors;

(b) the same were made and executed after not less than 21 days' notice in the Gazette and in a newspaper circulated in the Islands of the intention of the trader to make such disposition.

6.2.20 Bailiff[40]

When the goods of a debtor have been taken in execution in respect of a judgment and sold, the bailiff must, if he has notice of a petition filed against the debtor, hold the balance of the proceeds of the sale, after deducting expenses, upon trust to pay the same to the Trustee.

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39 *Idem*, s 135.
40 *Idem*, s 114-115.

When the goods of a debtor have been taken in execution in respect of a judgment and not sold before the bailiff or officer executing the process receives notice of the appointment of a receiver or Trustee under a bankruptcy petition, the bailiff after receipt of the notice, must deliver up such goods to the receiver or Trustee.

6.2.21 Creditor that has executed on property

A creditor who has levied execution on the property of a debtor, or has made an attachment thereof, is not entitled to retain the benefit of such execution or attachment unless and except insofar as he has, before the filing of a petition against or by such debtor, enforced such execution by sale of the property seized, or enforced such attachment by actual possession of the moneys attached or, as the case may be, by sale of the property attached.[41]

6.2.22 Landlord

A landlord to whom any rent is due from the debtor may, at any time, either before or after the commencement of the bankruptcy, distrain upon the goods or effects of the debtor for the rent due to him.[42]

If such distress for rent is levied after the commencement of the bankruptcy, it will be available only for one year's rent accrued due prior to the date of the provisional order.

After notice received by the person making the distress of the appointment of the Trustee or receiver, no sale may be made of the goods distrained, unless the Court otherwise orders, except by the Trustee or receiver.

6.2.23 Netting-off

Where there have been mutual credits, mutual debts or other mutual dealings, between the debtor and any person having a debt provable under the bankruptcy petition, netting-off is allowed.[43]

6.2.24 Debtor's discharge

The debtor may, at any time after the filing of such report, apply for an order of discharge.[44]

The Trustee or any creditor may oppose the discharge and may show cause why it should be refused, postponed or made subject to conditions.[45]

The Court may grant the discharge unconditionally or conditionally or it may suspend or refuse the discharge.[46]

The discharge, if made, releases the debtor from his debts (subject to any conditions set out by the Court and subject to the *caveat* that it shall not release a bankrupt form any liability incurred by means of fraud).[47]

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41 *Idem*, s 116.
42 *Idem*, s 117.
43 *Idem*, s 127.
44 *Idem*, s 68(1).
45 *Idem*, s 68(2).
46 *Idem*, ss 68 and 70.
47 *Idem*, s 71.

Self-Assessment Exercise 3

Question 1

Which law governs personal bankruptcy in the Cayman Islands?

Question 2

Which debtors may be subject to the jurisdiction of the bankruptcy court?

Question 3

Name 5 acts or defaults which can be alleged by a petitioner as the grounds of a personal bankruptcy petition?

Question 4

Is all of the debtors property available to creditors?

For commentary and feedback on self-assessment exercise 3, please see APPENDIX A

6.3 Corporate liquidation

6.3.1 Introduction

In addition to personal bankruptcy matters, the Grand Court of the Cayman Islands also has jurisdiction over corporate liquidations and restructurings.

The Grand Court has jurisdiction[48] to make (winding up) orders in respect of companies which are either:

(a) incorporated in the Cayman Islands;

(b) incorporated elsewhere but subsequently registered in the Cayman Islands; or

(c) in respect of a foreign company which –

(i) has property located in the Islands;

(ii) is carrying on business in the Islands;

(iii) is the general partner of a limited partnership; or

(iv) is registered under Part IX (a so-called "overseas company").

[48] *Idem*, s 91.

6.3.2 Types of corporate liquidation

The Cayman Islands Companies Law (Part V) provides for three types of corporate liquidations:

(a) voluntary liquidations;

(b) provisional liquidations; and

(c) official liquidations.

Schemes of arrangement are also available (see 6.5); however, they are not, strictly speaking, a liquidation procedure unless coupled with one of the above. Receivers may also be appointed in certain situations (see 6.4).

6.3.2.1 Voluntary liquidation

Introduction

A company may be wound up voluntarily.[49]

Voluntary liquidation is governed primarily by sections 116-130 of the Companies Law. In a voluntary liquidation, the affairs of the company are wound up and creditors are paid. Any excess assets after payment of creditors are distributed to the shareholders.

Generally, in a voluntary liquidation, the company must cease trading except where it is necessary and beneficial to the liquidation.[50]

Circumstances that may initiate a voluntary liquidation

A company may be wound up voluntarily[51] if:

(a) the company by special resolution resolves that it be wound up voluntarily;

(b) if the company by ordinary resolution resolves that it be wound up voluntarily as a result of the inability to pay its debts as they fall due;

(c) where the duration of the company as fixed by its memorandum or articles of association has expired;

(d) if an event occurs which the memorandum or articles provide is to trigger the company's winding-up.

Commencement

A voluntary liquidation is deemed to commence at the time of the passing of the resolution for winding-up, or on the expiry of the period or the occurrence of the event specified in the company's memorandum or articles.[52]

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49 *Idem*, s 90(b).
50 *Idem*, s 118.
51 *Idem*, s 116.
52 *Idem*, s 117.

Role of voluntary liquidator

There are no qualification requirements for the role of a voluntary liquidator[53] and no authorisation is required from the Grand Court for a voluntary liquidator to exercise his powers.

As such, directors may be appointed as voluntary liquidators. In the event a voluntary liquidator who is not a director is appointed, the directors are displaced by the voluntary liquidator.

Applications to Grand Court

A voluntary liquidator may apply to the Grand Court to determine any issue that arises during the winding-up process, or for an order that the liquidation continues under the Court's supervision.[54]

Declaration of solvency

A company may only be wound up outside the court process if it is solvent.[55] A voluntary liquidator is required to apply to the Grand Court for an order that the liquidation be carried out under the Grand Court's supervision unless the directors sign a declaration that the company will be able to meet its debts in full within a period not longer than 12 months from the commencement of the voluntary liquidation.[56] This is known as a "declaration of solvency". The declaration must be signed within 28 days of the initiation of the voluntary liquidation.

Application for court supervision

Even after a declaration of solvency has been made by the directors, the voluntary liquidator, any creditor or shareholder can apply to bring the liquidation under the Grand Court's supervision on the following grounds:[57]

(a) the company is, or is likely to become, insolvent; or

(b) court supervision will facilitate a more effective, economic or expeditious liquidation of the company in the interests of the shareholders and creditors.

If a voluntary liquidation is brought under the supervision of the Grand Court, then it continues as an official liquidation (see below). Indeed, the effect of the supervision order is to place the company into official liquidation with retroactive effect from the commencement of its voluntary liquidation.

No moratorium

There is no protection from the company's creditors during a voluntary liquidation. Debts must be paid as they fall due. If they are not paid, secured creditors can enforce their security or unsecured creditors can initiate winding-up proceedings against the company.

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53 *Idem*, s 120.
54 *Idem*, s 129. Winding-up subject to the supervision of the Court is governed by ss 131-133.
55 Companies Law section 116.
56 *Idem*, s 124.
57 *Idem*, s 131.

No set-off or net-off

The voluntary liquidator is required to pay claims in full and there is no statutory set-off or netting-off that applies during a voluntary liquidation.

No adjudication process

There is also no process for adjudicating creditors' actual or contingent claims. Any disputes need to be determined by whichever court has jurisdiction over the claim.

No power to disclaim onerous contracts

The voluntary liquidator has no statutory power to disclaim onerous contracts. The normal rules governing breach of contract therefore apply.

Liquidators reports

A voluntary liquidator is required and expected to provide reports and accounts to the company's shareholders. Reporting should also be provided on request to creditors who have not been paid in full.

Reporting is done in connection with each annual general meeting and the final meeting in the voluntary liquidation, or whenever the voluntary liquidator thinks appropriate.

Rights to information

Aside from the above liquidators reports, shareholders and creditors have no other statutory rights to information during a voluntary liquidation.

Timeframe

Voluntary liquidations are generally quicker than official liquidations; however, the duration of a voluntary liquidation is largely determined by the complexity of the winding-up process.

The law contemplates that all creditors in a voluntary liquidation will be paid in full within 12 months. It imposes an obligation on the voluntary liquidator to apply to bring the liquidation under the Grand Court's supervision unless all the directors swear a statutory declaration of their belief that the company will be able to comply with this timeline.

General meeting

After the business of the company is wound up, the liquidator must call a general meeting of the company to present his account of the voluntary liquidation and then file a return with the registrar of companies.[58]

Dissolution

The company is deemed to have been dissolved three months after the return's registration date.[59]

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58 *Idem*, s 127.
59 *Idem*, s 151.

6.3.2.2 Provisional Liquidation

Entities that are covered

As with other kinds of liquidation (voluntary and official), provisional liquidation is available to any company liable to be wound up under the Companies Law.[60]

Uses

Provisional liquidation is mainly used to preserve and protect a company's assets until the appointment of official liquidators. It is often used to facilitate a compromise or arrangement with the company's shareholders (see scheme of arrangement below) or in support of foreign restructuring proceedings such as Chapter 11 in the United States.

Standing to apply

Applications to appoint provisional liquidators may be made by creditors, shareholders or the Cayman Islands Monetary Authority (CIMA).[61]

A company can also apply for the appointment of provisional liquidators in order to present a compromise or arrangement to creditors.[62] As discussed below, this gives the company the protection of an automatic stay.[63]

Grounds for application

Per section 104 (2) of the Companies Law, creditors, shareholders or CIMA may make an application (usually *ex-parte* or without notice to the company) on the grounds that:

(a) There is a *prima facie* case for a making a winding up order;[64] and

(b) The appointment of a provisional liquidator is necessary to:

  (i) preserve and protect the company's assets;

  (ii) prevent the oppression of minority shareholders; or

  (iii) prevent mismanagement of the company's affairs by the directors.

Per section 104(3) of the Companies Law, the company itself may make an *ex parte* application for provisional liquidation on the grounds that:

(a) the company is, or is likely to become, unable to pay its debts within the meaning of section 93;

(b) the company intends to present a compromise or arrangement to its creditors (that is, a scheme of arrangement under section 86).

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60 *Idem*, s 91.
61 *Idem*, s 104(2).
62 *Idem*, s 104(3).
63 *Idem*, s 97.
64 See Official Liquidation below.

Definition of "unable to pay its debts"

Under section 93, a company is deemed unable to pay its debts if:

(a) a creditor to whom the company is indebted in a sum exceeding KYD 100 then due, has served on the company a demand requiring the company to pay the sum so due, and the company has for the space of three weeks succeeding the service of such demand, neglected to pay such sum, or to secure or compound for the same to the satisfaction of the creditor; or

(b) execution of other process issued on a judgment, decree or order obtained in the Court in favour of any creditor in any proceedings instituted by such creditor against the company, is returned unsatisfied in whole or in part; or

(c) it is proved "to the satisfaction of the Court" that the company is unable to pay its debts.

Section 93 (c) means the Court will apply the cash flow test.

Appointment and powers of the joint provisional liquidators (JPLs)

The JPLs will be appointed by the Court but, since the application for provisional liquidation is often made *ex parte*, the JPL will normally be nominated by the applicant who files the petition.

The powers and duties (including reporting obligations) of the provisional liquidators are given to them in the appointment order. The extent of the powers depends on the reason for their appointment.

Management participation

In the case of "light touch" provisional liquidations, existing management is allowed to continue in control of the company but subject to the supervision of the provisional liquidator and the Grand Court. In other cases, the provisional liquidator's powers replace those of the directors. This will all depend on the facts of the case.

Provisional liquidation committee

At times, the Grand Court may direct that a provisional liquidation committee be established. The committee's mandate will be to assist and act as a sounding board for the provisional liquidators. The committee will also monitor the JPL's fees.

Statutory moratorium

Pursuant to Section 97 of the Companies Law, once a provisional liquidator is appointed, no action or proceeding may be commenced or continued against the company without the leave of the Grand Court. This is a key feature of the provisional liquidation process.

The stay does not prevent secured creditors from enforcing their security.

Adjudication of claims

There is no statutory mechanism for the adjudication of creditors' claims during a provisional liquidation.

If the provisional liquidation is being pursued for the purpose of a scheme of arrangement, then the terms of the scheme will address the process for adjudicating claims.

If, on the other hand, the provisional liquidation is being used to protect assets pursuant to a winding-up, claims will be submitted and adjudicated as part of the ensuing official liquidation.

Onerous contracts

Provisional liquidators have no statutory power to disclaim onerous contracts. Failure to comply with any such contracts will therefore have the usual consequences for breach of contract.

Essential contracts / supply of utilities

If a request is made by a liquidator or provisional liquidator for the continued provision (after the date of the appointment of the provisional liquidator or date on which the winding up order was made) of electricity, water or telecommunications, the relevant utility supplier may make it a condition of the provision of such supply that the liquidator personally guarantees the payment of any charges in respect of that supply.

The supplier may not, however, make it a condition of the supply that any outstanding charges (which pre-date the appointment of the liquidator / winding up order) are paid.[65]

Timeframe

The time taken to complete a provisional liquidation depends on a number of factors, including its purpose.

If the purpose of the provisional liquidation is to preserve the assets until the hearing of a winding-up petition, the duration is typically short. The Grand Court attempts to hear winding-up petitions within four to six weeks of the petition being filed.

If the purpose of the provisional liquidation is to enable a scheme of arrangement, the winding-up petition is listed for a hearing within one to three months. This is intended to allow adequate time for the preliminary assessment of the viability of the proposed restructuring.

If the proposed scheme of arrangement does not appear to be viable, the company will be ordered to wind up at the first hearing.

If the scheme appears to be viable, the petition is adjourned for a period of time to allow for the scheme of arrangement to be implemented.

[65] Companies Law, s 148.

Conclusion of a provisional liquidation

An application for provisional liquidation may be concluded in the following circumstances:

- A winding-up order is made at the first hearing (that is, the company enters official liquidation meaning the company will be dissolved at the end of a liquidation process); or
- A winding-up petition is dismissed; or
- The provisional liquidator, the company, a creditor or a shareholder applies for an early termination of the provisional liquidators' appointment and such application is granted; or
- An appeal against the provisional liquidator's appointment succeeds.

6.3.2.3 Official liquidation

The purpose of an official liquidation is to wind up the company and distribute its assets to its creditors and shareholders.

The court is central to the process. It decides to appoint official liquidators, considers whether to approve certain actions of the liquidators (sale of assets, leave to commence litigation, compromising of claims) and sanctions payment of the liquidators' remuneration and expenses.

Entities that may be officially liquidated

As with voluntary liquidations and provisional liquidations, official liquidations are available to:[66]

(a) companies incorporated and registered under the Companies Law;

(b) bodies incorporated elsewhere but registered in the Cayman Islands; and

(c) foreign companies which:

(i) carry on business or have property located in the Cayman Islands;

(ii) are the general partner of a limited partnership registered in the Cayman Islands; or

(iii) are registered under Part IX of the Companies Law (so-called "overseas companies").

Functions of the official liquidator(s)

The functions of official liquidators are:[67]

(a) to collect, realise and distribute the assets of the company to its creditors and, if there is a surplus, to the persons entitled to it; and

[66] *Idem*, s 91.
[67] *Idem*, s 110.

(b) to report to the company's creditors and contributories upon the affairs of the company and the manner in which it has been wound up.

Standing to present a petition

Section 94 of the Companies Law states that an application to the Court for the winding-up of a company must be by petition presented either by:

(a) the company;

(b) any creditor;

(c) any shareholder of the company; or

(d) the Cayman Islands Monetary Authority (which is the financial services regulator).[68]

The right to present a petition is, however, subject to any contractually binding non-petition clauses.

A company can only file a winding up petition if the directors have obtained a shareholder resolution authorising them to do so, or they are duly authorised to do so in the company's articles of association.[69]

Grounds upon which an entity may be wound up

A company may be wound up by the Grand Court if any of the following apply:[70]

(a) the company passes a special resolution requiring it to be wound up by the court;

(b) the company does not commence business within a year of incorporation;

(c) the company suspends its business for a whole year;

(d) the period fixed by the company's articles for the company's duration expires, or an event occurs which, under the articles, triggers the company's winding-up;

(e) the company is unable to pay its debts;

(f) the Grand Court decides that it is "just and equitable" for the company to be wound up;

(g) the company is carrying on a regulated business in the Cayman Islands and is not duly licensed or registered to do so;

(h) certain other grounds specified in regulatory and other laws (for example, where a company is operating without the necessary regulatory licence).

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68 There have been several high-profile applications by CIMA in recent years concerning regulated entities (banking, securities, insurance) such as *In the matter of OneTradex* and also *In the matter of Caledonian Bank Limited*. A petition is often preceded by the appointment by CIMA of one or more insolvency practitioners to relieve incumbent directors of command.

69 *Re Emmadart* [1979] 1 All ER 599.

70 *Idem*, s 92.

"Unable to pay its debts"

A company is deemed to be unable to pay its debts if:[71]

(a) a creditor to whom the company owes a sum exceeding KYD 100 has served on the company a demand requiring the company to pay the sum due and the company has not been paid for 21 days after the demand;[72]

(b) execution of other process issued on a judgment, decree or order obtained in the Court in favour of any creditor in any proceedings instituted by such creditor against the company, is returned unsatisfied in whole or in part; or

(c) it is proved to the satisfaction of the Court that the company is unable to pay its debts.

Normally it is creditors that bring such applications. As a general rule, shareholders cannot apply on this basis because, if the company is insolvent, such shareholders will no longer have an economic interest in the company.

The onus is on the party petitioning for the winding up of the company to prove that it is insolvent, not on the company to prove its solvency.

The normal test for whether the company can pay its debts[73] is calculated on a cash-flow basis; however, various authorities in recent years have suggested that future cash flow may be considered.[74]

Cayman Islands law contains no "balance sheet test"; however, the company's general financial position may be relevant to the question of whether it is just and equitable to wind up a company (see below).

"Just and equitable"

Although the categories of "just and equitable" ground are not closed, commonly petitions under this heading rely upon the following bases:

- loss of substratum;
- deadlock;
- mismanagement; and / or
- exclusion from mismanagement.

Such petitions are normally brought by minority shareholders. The court has the power to make alternative orders (such as orders regulating the management going forward, or orders that the minority shareholders be bought out at a fair price) instead of resorting to liquidation of the company and it will often do so.

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71 *Idem*, s 93.
72 If the company is disputing the debt claimed on substantial grounds, then the debt cannot form the basis of a winding-up petition.
73 *Idem*, s 93(c).
74 *Re Weavering Macro Fixed Income Fund Ltd (in Liquidation)* [2016 (2) CILR 514].

Moreover, such applications will rarely be brought in respect of an insolvency company (and are therefore outside the focus of this module). This is because a petitioning shareholder will need to demonstrate to the court that it has standing to advance a winding up petition (by demonstrating that it has an economic interest in the company) and it will only be able to do so where there will be surplus of assets after the company's debts and the expenses of the winding-up have been paid.

Groups of companies

Insolvency proceedings relating to each company in a group must be commenced by a separate petition; however, the Grand Court can (and does) take a pragmatic approach and will sometimes co-ordinate liquidation proceedings in respect of several group companies in the interests of efficiency.

Where appropriate, the Grand Court may order the pooling of assets and liabilities of group companies. This may happen where there are good reasons for piercing the corporate veil,[75] or where the affairs of the separate companies are so interwoven and improperly or inadequately accounted for, that it would be impractical to treat the companies as distinct entities for the purpose of effecting the liquidations.

Alternatively, there may have been a vote from a sufficient majority of creditors in each company by which they agree to a scheme of arrangement that provides for the pooling of assets or a compromise agreement from the liquidators of each company, in relation to cross-claims between group entities.

To achieve such a consolidation, the Grand Court would need to be persuaded to use its discretion with reference to the required majorities being met and there being sufficient benefit to the entities concerned.

In addition, whilst there are no formal provisions for co-operation between liquidators of different companies within a group, there may be circumstances which merit such co-operation. The Grand Court may, therefore, appoint the same liquidators over more than one entity within the group. This will be entirely fact dependent and will involve consideration of the potential benefit to creditors and the risk of any conflict of interest existing or arising.

Liquidators qualifications

Official Liquidators (OLs) must be resident in the Cayman Islands or be foreign practitioners appointed jointly with a resident qualified insolvency practitioner.[76] They must also be qualified insolvency practitioners (IPs).

It is common for the Court to appoint joint liquidators (for example, one IP from the Cayman Islands together with one from the US, England or Hong Kong), particularly where the work will be substantially undertaken in the US, UK or Asia.

Displacement of board

Once appointed, the OLs displace the company's directors and control the company's affairs, subject to the Grand Court's supervision. The directors may still

[75] See *Prest v Petrodel Resources Ltd*, 2013, UKSC 34.
[76] Companies Law, s 108.

be required to assist the liquidator and can be ordered to provide information and deliver up assets or records (see below).[77]

Liquidators powers of investigation

Upon taking office, the liquidators are responsible for realising and distributing the assets of the company to the unsecured creditors but they are also given wide-ranging powers, including power to require directors, professional service providers or employees to provide statements of the company's affairs supported by affidavit[78] and, with leave of the Court, to compel certain persons (such as former directors) to submit to oral examination.[79]

More on duties of liquidators

The official liquidator is an officer of the court. He is required to make "himself thoroughly acquainted with the affairs of the company; and to suppress nothing, and to conceal nothing, which has come to his knowledge in the course of his investigation, which is material to ascertain the exact truth in every case before the Court".[80]

He may sell assets with sanction of the court:

> "The primary duty of a liquidator when selling the assets of a company is to take reasonable care to obtain the best price available in the circumstances... taking into account the nature of the business to be sold, the relevant market, the steps taken to market and to sell the assets and the urgency of the sale."[81]

Liquidation committee

A liquidation committee must be established unless the Grand Court orders otherwise.[82] It is a body representative of the company's stakeholders formed to consult with the liquidators. The liquidation committee acts as a sounding board for the official liquidators and also reviews their fees. The committee consists of not less than three and no more than five members (six in circumstances of doubtful solvency) and the eligibility requirements for the nature of the interest of committee members is contingent on the solvency determination made by the official liquidators.[83]

Automatic stay

On the making of a winding-up order, an automatic stay comes into effect which prohibits the commencement or continuation of any action against the company without the leave of the Grand Court.[84]

The automatic stay does not prohibit secured creditors from enforcing their security.[85]

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77 *Idem*, s 103.
78 *Idem*, s 101.
79 *Idem*, s 103.
80 *Gooch's Case* 1872, 7 Ch App 207.
81 *Trident Microsystems (Far East) Limited* (2012 (1) CILR 424).
82 Companies Winding Up Rules (2018 Revision), Order 9, r (1)(1).
83 *Idem*, Order 9, r (1)(3) – (6).
84 *Idem*, s 97.
85 *Idem*, s 142.

Provable debts

All debts payable on a contingency and all claims against the company, whether present or future, certain or contingent, ascertained or sounding only in damages, are admissible to proof against the company.

The official liquidator must make a just estimate so far as is possible of the value of all such debts or claims.[86]

There are special rules in relation to the admissibility to proof of foreign taxes, fines and penalties.

Proofs of debt

Creditors must submit a proof of debt for review by the official liquidator. The proof of debt contains details of the amount and interest owed, including the basis for the debt.

The official liquidator can accept, reject or request further evidence in relation to a claim.

Creditors can appeal the decision taken by the official liquidator in relation to a proof of claim.

Trades, assignments and transfers

Creditors can trade or assign their claims without seeking the leave of the Court (although they will need to give notice to the company of any assignment). Shareholders require both the leave of the Court and consent of the official liquidator to transfer their shareholding.[87]

Onerous contracts

Official liquidators have no statutory power to disclaim onerous contracts. The usual rules in relation to breach of contract apply.

Duty to report

Official liquidators have a duty to report to the Grand Court, liquidation committee, creditors and shareholders.

Rights of inspection

Pursuant to section 114 of the Companies Law, at any time after making a winding-up order, the Court may make such orders as it thinks fit for the inspection of the company's documents by creditors and contributories.

The Court may also order the preparation of reports by the official liquidator and the provision of such reports to the company's creditors and contributories.

If, however, the liquidation file contains confidential documents the disclosure of which may be prejudicial to the economic interests of the parties, the official liquidator

86 *Idem*, s 139.
87 *Idem*, s 99.

can apply to the Grand Court for the file / documents to be sealed (so they are not available for inspection).

Distribution of the company's property

The basic rule is that property of the company must be applied in satisfaction of its liabilities *pari passu*, following which it must be distributed amongst the members according to their rights and interests.[88]

This rule is subject to the very significant *caveat* that effect must first be given to the rights of preferred and secured creditors AND subject to any agreement between the company and any creditors that the claims of such creditors shall be subordinated AND any contractual rights of set-off[89] or netting of claims.[90]

Order of priorities

A secured creditor's rights in a liquidation are superior to the rights of all other parties and sit above the order of priorities listed immediately below.

The order of priorities in an official liquidation is as follows:

(a) liquidation expenses;

(b) preferential debts, comprising:

  (i) sums due to employees;

  (ii) taxes due to the Cayman Islands government;

  (iii) sums due to depositors (if the company is a bank);

  (iv) unsecured debts which are not subject to subordination agreements;

(c) amounts due to preferred shareholders;

(d) debts incurred by the company in respect of the redemption or purchase of its own shares; and

(e) any surplus remaining after payment of the above amounts is returned to the shareholders of the company in accordance with its articles or any shareholders' agreement.

"Preferential debts"

Per section 141 of the Companies Law, in the case of an insolvent company the following debts are paid in priority to all other debts:[91]

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88 *Idem*, s 140(1).

89 Creditors are able to exercise common law and contractual rights of set-off and netting against a company following the commencement of liquidation. Save where the creditor had notice (at the time the debt fell due for payment) that liquidation proceedings had been initiated, set-off will be automatic absent any contractual arrangement to disapply it. Where set-off applies, an account will be taken of what the company owes to the creditor and *vice versa* (calculated at the commencement of the liquidation) and the balance after the set-off will be paid to the party to whom it is due.

90 Companies Law, s 140(2).

91 *Idem*, Sch 2, "Categories of Preferred Debts".

(a) sums due to employees;

(b) taxes due to the Cayman Islands government;

(c) sums due to depositors (if the company is a bank);

(d) unsecured debts which are not subject to subordination agreements.

These preferential debts rank equally. If available funds are insufficient to satisfy them in full, they abate in equal proportions.

Preferential charge on good distrained

In the event of a landlord (or other person entitled to receive rent) distraining or having distrained on any goods or effects of the company within three months preceding the date of the winding-up order, the debts to which priority is given by section 141 must be a first charge on the goods or effects so distrained on or the proceeds of sale thereof.[92]

Effect of execution or attachment

Subject to certain qualifications, where a creditor has issued execution against the goods or land of a company, or has attached any debt due to it and the company is subsequently wound up, the creditor is not entitled to retain the benefit of the execution or attachment against the liquidator unless the creditor has completed the execution or attachment before the commencement of the winding up.[93]

Avoidance of property dispositions

Section 99 of the Companies Law states that any dispositions of a company's property made after the deemed commencement of the winding-up will be void in the event that a winding-up order is subsequently made (unless validated by the Grand Court).[94]

The liquidator is entitled to apply for appropriate relief to require the repayment of the funds or the return of the asset.

In this regard, it is important to remember that the commencement date will be deemed to be the date on which the petition was filed rather than the date on which the order is made.

The court does have the power to validate post-petition grants of security (retrospectively or prospectively), therefore a company should seek validation orders (for example, in relation to the grant of security in exchange for new money).

The court normally will validate such arrangements if the company is clearly solvent and provided it is satisfied that an "intelligent and honest" director acting reasonably would come to that decision.[95]

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92 *Idem*, s 143.
93 *Idem*, s 144.
94 This provision is in the same terms as section 127 of the UK's Insolvency Act 1986 therefore decisions of the courts of England and Wales are treated as persuasive authority.
95 *In the matter of Fortuna Development Corporation [2004-05] CILR 533.*

The court is unlikely to endorse such an arrangement where the company is insolvent, unless it can be shown that the grant of security has corresponding benefit to the company and enhances the value for creditors as a whole.

Where no petition has yet been filed, any such transaction is not caught by section 99 however it may be subject to other claw-back mechanisms set out immediately below.

Voidable preference

According to Section 145 of the Companies Law, any payment or disposal of property to a creditor constitutes a voidable preference if:

- it occurs in the six months before the deemed commencement of the company's liquidation and at a time when it is unable to pay its debts; and
- the dominant intention of the company's directors was to give the applicable creditor a preference over other creditors.

In *re Weavering Macro Fixed Income Fund Ltd (in Liquidation)*[96] the Cayman Islands Court of Appeal considered in detail each stage of the test to be applied in identifying voidable preferences under section 145(1).

Giving a preference over other creditors means putting that creditor in a better position than it otherwise would have been.[97] A dominant intention may be inferred by the court from the available evidence. If the company's dominant intention in making the payment or granting the security was to achieve a different purpose (for example, in good faith to pay an essential service provider) it might not be classed as a voidable transaction even if the collateral effect is to prefer the creditor in question.

Importantly, a disposition made to a "related party" of the company (such as a person who has the ability to control the company or exercise significant influence) will be deemed to have been made with a view to giving a preference.[98]

A disposition that is set aside as a preference is void and the liquidator may apply to the Grand Court to order the creditor to return the asset and prove in the liquidation for the amount of its claim.

Avoidance of dispositions made at an undervalue

Section 146 of the Companies Law provides that a transaction in which property:

- is disposed of at an undervalue; and
- with the intention of wilfully defeating an obligation owed to a creditor (that is, an intent to defraud)

is voidable on application of the liquidator.

96 [2016 (2) CILR 514].
97 *Weavering* [2019] UKPC 36.
98 Companies Law, s 145 (2) and (3).

"Undervalue" is defined to mean the provision of no consideration or a consideration which in money or money's worth is significantly less than the value of the property. The burden of proof is on the creditor or liquidator (seeking to have the disposition set aside) to establish an intent to defraud.

The application must be brought within six years of the disposal.

Fraudulent trading

Section 147 of the Companies Law deals with fraudulent trading.

If the business of a company was carried on with intent to defraud creditors, or for any fraudulent purpose, a liquidator may apply for an order requiring any persons who were knowingly parties to such conduct to make such contributions to the company's assets as the Court thinks proper.

Obligation to file for insolvency

There is no statutory obligation to file for insolvency and the Companies Law does not contain a prohibition on wrongful trading (that is, continuing to trade whilst insolvent).

Directors can, however, be made personally liable to the company for any losses which they cause to the company if they act in breach of their fiduciary duty to act in the best interests of the company.

In *Prospect Properties v McNeill*[99] the Grand Court held that where a company is insolvent, the directors' duty to act in the best interests of the company requires them to have regard to the interests of its creditors. It is in the interest of the creditors to be paid and it is in the interest of the company to be safeguarded against being put in a position where it is unable to pay.

When a company is in official liquidation, the official liquidator can pursue claims against the directors on behalf of the company (in the company's name) for breach of their fiduciary duty.

Time frame for completion

There is no set time period within which a liquidation must be completed. The time taken to complete a liquidation depends on a number of factors including, but not limited to, the complexity of the issues and the nature and size of the assets.

Dissolution

At the completion of the winding up of the affairs of the company, the official liquidator applies to the Grand Court for an order that the company be dissolved.[100]

The company cannot be reinstated after dissolution.

[99] [1990-91 CILR 171].
[100] Companies Law, s 152.

Self-Assessment Exercise 4

Question 1

Name the three types of liquidation in the Cayman Islands.

Question 2

Over which companies does the Cayman Islands Grand Court have jurisdiction?

Question 3

How can a company achieve a stay against creditor action?

Question 4

Under what circumstances may a voluntary liquidation come under court supervision?

Question 5

In what circumstances may a company be wound up by the Court?

Question 6

How does the automatic stay affect secured creditors?

Question 7

Describe the main avoidance of property provisions in the Cayman Islands.

For commentary and feedback on self-assessment exercise 4, please see APPENDIX A

6.4 Receivership

6.4.1 Grand Court Rules

Receivers are not explicitly mentioned in the statutory provisions dealing specifically with insolvency (namely the Companies Law and CWR); however, the Grand Court Rules (GCR) do contemplate that receivers may be appointed by the Court for the purposes of collecting money (for example, rents) or to carry out some other act (for example, the execution of a contract or a document of title).

Order 30 GCR governs the appointment and duties of receivers generally.

Order 45 GCR (which deals with enforcement of judgments and orders generally) states that receivers may be appointed to enforce court orders for the payment of money.

Order 51 GCR also provides for the appointment of receivers by way of equitable execution. [101]

6.4.2 Segregated Portfolio Companies (SPCs)

Receivers and receivership orders are specifically provided for by statute in respect of a particular type of Cayman Islands legal entity, namely the Segregated Portfolio Company.

An SPC is essentially a regular company which remains a single entity but which is permitted to create separate portfolios for different assets and liabilities. Each portfolio is ring-fenced (by statute) from the assets and liabilities contained in other portfolios.[102] These companies are easily identified by the words "Segregated Portfolio" or "SP" after their name.

If the Grand Court is satisfied that the SP's assets attributable to a particular portfolio of the company are likely to be insufficient to discharge the claims of creditors in respect of that portfolio, it may make a receivership order in respect of that portfolio.[103]

A receivership order must direct that the the business and segregated portfolio assets of, or attributable to, a segregated portfolio must be managed by a receiver specified in the order for the purposes of:

(a) the orderly closing down of the business of, or attributable to, the segregated portfolio; and

(b) the distribution of the segregated portfolio assets attributable to the segregated portfolio to those entitled to have recourse thereto.[104]

A receivership order:

(a) may not be made if the segregated portfolio company is in the process of being wound-up; and

(b) shall cease to be of effect upon commencement of the winding-up of the segregated portfolio company, but without prejudice to prior acts of the receiver or his agents.[105]

When an application has been made for (and during the period of operation of) a receivership order, no suit, action or other proceedings may be instituted against the segregated portfolio company in relation to the segregated portfolio in respect of which the receivership order was made, except by leave of the Court (which may be conditional or unconditional).[106]

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[101] This power derives from section 11(1) of the Grand Court Law (which states that the Grand Court shall possess like jurisdiction within the islands which is vested in the High Court of England) read in conjunction with Section 37(1) of the Senior Courts Act 1981 (England) which states the High Court may appoint a receiver in all cases in which it appears just and convenient to do so. See also *TMSF v Merrill Lynch Bank and Trust Company (Cayman) Ltd* [2011] (1) CILR and *Y v R* (Jan 2018).

[102] Companies Law, s 216.

[103] *Idem*, s 224(1).

[104] *Idem*, s 224(3).

[105] *Idem*, s 224(4).

[106] *Idem*, s 226(5).

During the period of a receivership order, the receiver relieves the directors of their functions and powers in respect of the business of the SP.[107]

6.4.3 Use by creditors

The main relevance of receivers in an insolvency context, is that receivership may offer an alternative course of action for certain creditors.

Receivers can be appointed without any court involvement pursuant to rights in a security instrument. For example, a holder of a fixed or floating charge can, if the charging document specifically provides for it, appoint a receiver over the company's charged assets if a debtor defaults.

The receiver will act under the powers set out in the charge document, which will typically include a right of sale. The receiver will generally realise the value of the charged asset and repay the creditor the amount of its unpaid debt.

In this scenario, the receiver is not supervised by the court and usually owes its duties to the creditor rather than the debtor company.

6.5 Corporate rescue

6.5.1 Introduction

Due to the nature of informal work-outs, these are not addressed in the Cayman Islands legislative framework; however, they are used in practice when there is requisite support from affected parties.

The Cayman Islands legislative framework does not contain a regime equivalent to the US Chapter 11 or the UK's administration procedure.

Notwithstanding the absence of these legislative frameworks, the Cayman Islands has managed to earn a reputation as a leading restructuring jurisdiction. Its success is due in large part to the ingenuity of local practitioners and the judiciary.

The main technique used to achieve some breathing space for the debtor is to obtain a moratorium against any proceedings continuing or being commenced against a company by putting the debtor into provisional liquidation pursuant to Section 104(3) of the Companies Law.

At the time of making the application, the applicant will explain to the court the purpose of the application, which will be the appointment of JPLs in order to allow for the negotiation and promotion of a compromise or arrangement with its creditors or members.

It is therefore common to see provisional liquidation used in conjunction with a scheme, although this is not always the case.

6.5.2 Schemes of arrangement

A scheme of arrangement ("scheme") is a court approved compromise or arrangement entered into between a company and its creditors or members or any

[107] *Idem*, s 226(6).

classes of them. This will be familiar to students with knowledge of English schemes of arrangement.

The power to "scheme" a company derives from section 86 of the Companies Law (as revised).

6.5.2.1 Some or all creditors of members

Such a compromise or arrangement may be proposed and agreed between a company and its creditors or any class of creditors, or between the company and its members or any class of members.

A scheme may, for example:

(a) restructure liabilities;

(b) reorganise share capital; and / or

(c) alter shareholders and creditors' distribution rights.

Debt for equity swaps are common. Pre-packaged sales are also possible but are less common in practice.

6.5.2.2 Who may commence the scheme?

The company, a creditor or a shareholder can commence scheme proceedings; however, scheme proceedings that are commenced by a creditor or shareholder require the company's consent.

6.5.2.3 Provisional liquidation and the moratorium

As stated elsewhere, in the Cayman Islands it is only possible to obtain a court ordered stay if the company is in liquidation (which includes provisional liquidation).

This means that if breathing space from creditors is required to effect the scheme, the company will need to present a winding-up petition to the Grand Court and apply for an order appointing provisional liquidators prior to filing the scheme petition.

An application under section 104(3) can be made by the company on an *ex parte* basis on the ground that the company is or is likely to become unable to pay its debts as they fall due[108] and the company intends to present a compromise or arrangement.[109]

6.5.2.4 Company management

If the company is not in provisional liquidation, existing management will continue to manage the company.

[108] That is, cash flow test (which includes debts currently due plus debts that will become payable in the reasonably near future).

[109] If the court grants the application *ex parte,* it will usually require an *inter partes* date shortly thereafter to ensure that creditors have the opportunity to be heard.

Upon the appointment of provisional liquidators, the Grand Court will determine which powers will remain with the directors and which will be vested in the provisional liquidators. Sometimes directors may be relieved of control entirely.

When the powers remain largely with the directors, this process is referred locally as "light touch".

6.5.2.5 Approval procedure

The procedure for obtaining approval for a scheme of arrangement is governed by Order 102, rule 20 of the Grand Court Rules (GCR) and Practice Direction 2/2010.

After the filing of a scheme petition, there is a three-stage process for schemes:

(a) An application must be made to the Grand Court for an order that meetings of creditors or members be convened for the purpose of approving the scheme (the "convening hearing");

(b) The scheme proposals are discussed at meetings held in accordance with the convening hearing order and are either approved or rejected (the "scheme meetings");

(c) If approved at the scheme meetings, an application is then made to the Grand Court to obtain approval / sanction of the scheme (the "sanction hearing").

The detailed scheme documentation is distributed to all scheme participants and may also be advertised, depending on the circumstances.

The documentation will typically contain a mechanism for determining claims, post-sanction of the scheme, for distribution purposes.

6.5.2.6 Convening hearing

At this hearing, the Court will be concerned with issues of class composition, any jurisdictional issues, the adequacy of the scheme documentation and notice.

The Grand Court must be satisfied that the scheme document and supporting explanatory statement contain all the information reasonably necessary to enable the scheme creditors (and / or shareholders, as applicable) to make an informed decision about the proposed scheme.

6.5.2.7 Scheme meetings

In order for a proposed scheme to be approved, a majority in number (that is, over 50%) representing over 75% in value of the creditors (or class of creditors, or members or class of members, as the case may be), present and voting either in person or by proxy at the meeting, must agree to the compromise or arrangement.

If the necessary majorities are obtained, the scheme can proceed to the sanction hearing (see below).

In this way, a debtor can "cram down" creditors (force dissenting creditors to accept the scheme of arrangement) within an accepting class, provided the threshold is reached.

It also follows, however, that a scheme creditor or group of creditors may be able to block a scheme if they command a sufficient number of votes.

6.5.2.8 Cross- / intra-class cramdown

At the convening hearing, the court may have placed creditors into different classes.

In the Cayman Islands, all classes must vote to accept the scheme of arrangement in order for it to be sanctioned by the court.

In other words, in each and every class, more than 50% representing 75% in value of the creditors (or members) of that class must vote in favour of the scheme.

Therefore, there is no "cramdown" of the proposed restructuring on a dissenting class.

This lack of cross-class cramdown normally does not present a problem as, unlike the case in Chapter 11 proceedings, the majority of schemes in the Cayman Islands have very few (and often only one) classes of creditors. In addition, secured creditors are generally treated as being outside the scheme since they have the ability to exercise their security rights at any time.

6.5.2.9 Court sanction

If it has the necessary creditor support, the compromise or arrangement must still be sanctioned by the Court before it is binding on all the creditors (or the class of creditors, or on the members of class of members, as the case may be), the company and its contributories.[110]

A dissentient creditor (or shareholder) has the right to oppose the scheme at the sanction stage, although its options will be limited at that point.

The Court will be concerned with compliance with the convening orders, whether the majority fairly represent the class, whether the arrangement (having regard to the alternatives) is such that an intelligent, honest member of the class convened, acting in his own interest, might reasonably approve it.

6.5.2.10 Timeframe

Typically, it takes between 10 to 12 weeks from the filing of the petition to the approval of the scheme. In addition, prior to the filing of the petition, time may be spent negotiating the scheme with creditors and preparing documentation.

6.5.2.11 Trading claims

There is no statutory prohibition on the trading of creditor claims. Notice of the assignment would need to be given to the company.

6.5.2.12 Groups

As discussed above in relation to provisional and official insolvency, the Grand Court is able to take a pragmatic view in relation to group companies. In the restructuring

[110] *Idem*, s 86(2).

context, therefore, schemes of arrangement may be co-ordinated to ensure efficiency and cost effectiveness.

6.5.2.13 Disposal of assets

If the company is in provisional liquidation, the disposal of assets must be subject to Grand Court approval.

If the company is not in provisional liquidation, the disposal of assets will be carried out by the directors and there are no restrictions to the use or sale of the company's assets (save for any applicable contractual restrictions).

Creditors may bid for the assets. There are no specific rules that govern bids by creditors; however, if the company is in provisional liquidation, the sale must be approved by the Grand Court.

6.5.2.14 Funding a scheme

The process is funded from the company's assets and / or from any new money (sometimes referred to as debtor-in-possession or DIP financing) invested by way of debt or equity.

If the company is being schemed without recourse to provisional liquidation, there is no statutory protection / priority afforded to rescue financing.

Similarly, if the company is being schemed during a provisional liquidation, there will be no statutory protection / priority in the event the company emerges from provisional liquidation but subsequently fails.

If, on the other hand, rescue financing is provided during a provisional liquidation and the company is subsequently wound up without having emerged from the provisional liquidation process (because no restructuring was approved), then the rescue financing is likely to constitute an expense of the provisional liquidation, thereby taking priority over the majority of official liquidation expenses and all unsecured creditors' claims.

It is noteworthy that any such priority does not trump any pre-existing security which had been taken over an asset (see commentary on the status of secured assets above).

6.5.2.15 Conclusion of scheme

The Grand Court must approve the terms of the scheme before it becomes effective and will not do so unless satisfied that it is fair.

A scheme of arrangement concludes after all the terms to which it relates have been complied with.

Self-Assessment Exercise 5

Question 1

What is a scheme of arrangement?

Question 2

Is it possible for management to stay in place during a scheme?

Question 3

Is it possible to cram down dissenting shareholders?

For commentary and feedback on self-assessment exercise 5, please see APPENDIX A

7. CROSS-BORDER INSOLVENCY LAW

The Cayman Islands has positioned itself as a leading financial centre for international business. It is home to some 100,000 companies, many of which conduct their business exclusively outside the Cayman Islands. As a result, the vast majority of liquidations involve cross-border issues.

7.1 The Court's powers

The Grand Court's powers to make orders in support of foreign insolvency proceedings, are provided for in Part XVII of the Companies Law.

7.2 UNCITRAL Model Law on Cross-Border Insolvency

The Cayman Islands has not implemented the UNCITRAL Model Law on Cross-Border Insolvency, although most of the principles are followed (in the interests of comity).

7.3 European Union legislation

The Cayman Islands, despite being a British Overseas Territory, is not a member of the EU and therefore EU legislation does not apply.

7.4 Discretion

In the Cayman Islands, there are no threshold tests for the grant of assistance, nor are there automatic rights based on the centre of main interests (COMI) of the debtor.

Instead, foreign representatives must satisfy the Cayman court that it is appropriate for the court to exercise its discretion by granting the relief sought in the foreign representative's application.

7.5 Foreign bankruptcy proceeding

A foreign bankruptcy proceeding includes proceedings for the purpose of reorganising or rehabilitating an insolvent debtor.[111]

7.6 Ancillary orders

The Grand Court can provide the following forms of ancillary relief:[112]

(a) recognising the right of a foreign representative to act in the Islands on behalf of, or in the name of, a debtor;

(b) enjoining the commencement or staying the continuation of legal proceedings against a debtor;

(c) staying the enforcement of any judgment against a debtor;

(d) requiring a person in possession of information relating to the business or affairs of a debtor to be examined by and to produce documents to its foreign representative; and

(e) ordering the hand-over – to a foreign representative- of any property belonging to a debtor.

7.7 Criteria upon which the Court's discretion must be exercised

In determining whether to make these ancillary orders, the Grand Court is guided by matters which will best assure an economic and expeditious administration of the debtor's estate, consistent with:[113]

(a) the just treatment of all holders of claims, wherever they are domiciled, in accordance with established principles of natural justice;

(b) the protection of claim holders in the Cayman Islands against prejudice and inconvenience in the processing of claims in foreign proceedings;

(c) the prevention of preferential or fraudulent dispositions of property in the debtor's estate;

(d) the distribution of the estate among creditors substantially in accordance with the statutory order of priority;

(e) the recognition and enforcement of security interests created by the debtor;

(f) the non-enforcement of foreign taxes, fines and penalties;

(g) comity (mutual recognition and co-operation concerning legal decisions).

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111 *Idem*, s 240.
112 *Idem*, s 241.
113 *Idem*, s 242.

7.8 Treatment of creditors

The Cayman Islands is decidedly creditor-friendly. It takes a universalist rather than a territorial approach to cross-border issues.

In many countries, insolvency law is heavily influenced by the desire to prevent unemployment (meaning that the interests of creditors are often subordinated). In other countries, insolvency laws give local creditors preferential treatment at the expense of foreigners.

In contrast, Cayman Islands insolvency law focuses upon the rights of creditors (and all such creditors are treated equally regardless of where they are domiciled).

This informal policy allows for a huge volume of capital markets and financial asset finance business to be placed through the Cayman Islands.

7.9 Protocols

Cayman Islands legislation does not provide for protocols between the Grand Court and foreign courts.

However, the law does make provision for Cayman official liquidators to enter into international protocols with foreign officeholders to promote:

(a) the orderly administration of an estate of a company in official liquidation;

(b) the avoidance of duplication of work; and

(c) the avoidance of conflict between the official liquidator and the foreign officeholder.

Such protocols may allocate responsibilities between the Cayman liquidator and foreign officeholder in relation to, *inter alia* the:

(a) preservation and realisation of assets;

(b) pursuit of causes of action;

(c) exchange of information;

(d) procedures for the administration of the estate and reporting;

(e) adjudication of claims; and

(f) distribution of assets.

Relevant provisions include:

- the Companies Law Part XVII (International Co-Operation);
- the Companies Winding Up Rules O.21 (International Protocols);

- the Grand Court Law, section11A (Interim relief in the absence of substantive proceedings in the Islands); and

- the Grand Court's Practice Direction 1 of 2018.

International protocols agreed between a Cayman liquidator and a foreign officeholder must be approved by both the Grand Court and the appropriate foreign court or authority.

Self-Assessment Exercise 6

Question 1

How will the Grand Court decide whether or not to grant assistance to overseas insolvency proceedings (and liquidators)?

Question 2

Are protocols used? Are there any legal requirements?

For commentary and feedback on self-assessment exercise 6, please see APPENDIX A

8. RECOGNITION OF FOREIGN JUDGMENTS

In cross-border cases, the Grand Court adopts a co-operative approach to ensure an effective winding-up and the protection of the interests of its creditors, wherever those creditors are situated.

8.1 Treaties

The Cayman Islands has not entered into any international treaties for the reciprocal recognition or enforcement of foreign judgments, neither has the UK extended its ratification of any such treaties to the Cayman Islands by Order in Council (save for the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards).[114]

The Cayman Islands is not a signatory to the Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters.

8.2 Statute

The Foreign Judgments Reciprocal Enforcement Law (1996 Revision) does provide a statutory scheme for recognition and enforcement of foreign judgments in circumstances where the country from which the judgment originates assures substantial reciprocity of treatment regarding the enforcement of Cayman Islands Judgments.[115] However, to date the provisions of the Law have only been extended

[114] The UK has the power to extend treaties because the Cayman Islands is a British Overseas Territory.
[115] Foreign Judgments Reciprocal Enforcement Law (1996 Revision), s 3(1).

to judgments from the Superior Courts of Australia. This procedure is governed by Order 71 of the Grand Court Rules.

In order to be enforceable, the foreign judgment must be:

(a) final;

(b) a money judgment; and

(c) made after the 1996 Law was extended to the relevant foreign country.

8.3 Common law

Given the limited application of the Foreign Judgments Reciprocal Enforcement Law (1996 Revision), the enforcement of foreign judgments is usually achieved by commencing a new action in the Cayman Islands based upon the foreign judgment as an unsatisfied debt or other obligation.

Such actions are conducted under the regular procedural regime for litigation in the Cayman Islands (that is, The Grand Court Rules).

Money and non-money judgments (including declaratory judgments) are enforceable at common law.[116]

The mandatory requirements for enforcement of a foreign judgment at common law are:

(a) the judgment is final;

(b) the foreign court had jurisdiction over the debtor;

(c) the foreign judgment was not obtained by fraud;

(d) the foreign judgment is not contrary to public policy of the Cayman Islands; and

(e) the foreign judgment was not obtained contrary to the rules of natural justice.

Once a local judgment has been obtained, the full range of domestic enforcement remedies are available.[117]

8.4 Limitation

A six-year limitation period applies both for common law enforcement and under the 1996 Law.

The period runs from the date of the judgment or, when there have been appeals, the date of the last judgment.

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[116] *Bandone v Sol Properties* 2008 CILR 301. The case confirmed that *in personam* judgments may be recognised and enforced through equitable remedies or, if required, under the principle of comity. The Court will have regard to the principles of fairness, mutuality and public policy.

[117] Iincluding the appointment of receivers under O.45 of the Grand Court Rules.

Self-Assessment Exercise 7

How can one enforce a foreign judgement in the Cayman Islands?

For commentary and feedback on self-assessment exercise 7, please see APPENDIX A

9. INSOLVENCY LAW REFORM

9.1 Insolvency Rules Committee

The Insolvency Rules Committee is established by section 154 of the Companies Law (as revised). It is responsible for making rules that may be necessary to give effect to the substantive law.

The Committee is comprised of the Chief Justice, the Attorney General and several respected practitioners in private practice. The Committee is therefore a useful tool in developing procedural change.

In addition, insolvency practitioners in private practice are instrumental in liaising with the legislature and recommending reforms to government.

Other developments in the law are judge-led (in keeping with the common law tradition of the islands).

9.2 The Companies Winding Up Rules 2018

Effective February 1, 2018, amendments were made to the CWR. Amongst other things, a new Part V was inserted into Companies Winding Up Rules 2018. Order 3 enhances the ability of a company to present a petition for its own winding-up.

9.3 Foreign Bankruptcy Proceedings (International Cooperation) Rules 2018 (the FBPR 2018)

Changes were introduced in February 2018. The FBPR 2018 is concerned with the procedures by which a foreign representative can be recognised in the Cayman Islands and seek the assistance of the Grand Court. The FBPR has been revised to provide greater clarity on these procedures.

9.4 Restructuring officers

The Cayman Islands insolvency and restructuring professionals are currently discussing revisions of the Companies Law, which would have the effect of introducing restructuring officers. A further announcement is expected in the first half of 2021.

9.5 Judicial Insolvency Network (JIN)

The Cayman Islands is a member of JIN and has adopted the JIN Guidelines for Cooperation in Cross-Border Insolvency Matters (JIN Guidelines). See Practice

Direction No. 1 of 2018 (PD 1/2018). Such guidelines have been designed to enhance communication between courts, insolvency representatives and other parties.

10. USEFUL INFORMATION

- Cayman islands legislation: https://legislation.gov.ky/cms/;
- Cayman Islands Judicial and Legal Website: https://www.judicial.ky/;
- Cayman Islands Monetary Authority: https://www.cima.ky/;
- Cayman Islands Restructuring and Insolvency Association: http://risa.ky/;
- Cayman Islands Law Reform Commission: http://www.lawreformcommission.gov.ky/portal/page/portal/lrchome;
- Cayman Finance (a private association tasked with promoting the financial services industry): https://www.cayman.finance/.

APPENDIX A: COMMENTARY AND FEEDBACK ON SELF-ASSESSMENT EXERCISES

Self-Assessment Exercise 1

Question 1

On which legal system is the Cayman Islands system loosely based?

Question 2

To which court or courts may a litigant appeal following an adverse decision at first instance?

Question 3

Which law or laws contains govern insolvency?

Commentary and Feedback on Self-Assessment Exercise 1

Question 1

England.

Question 2

The Cayman Islands Court of Appeal, the Judicial Committee of the Privy Council in London and (in rare instances) the European Court in Strasbourg.

Question 3

The Companies Law (as revised), The Companies Winding Up Rules (as revised).

Self-Assessment Exercise 2

Question 1

Name the common forms of security in the Cayman Islands for immovable property.

Question 2

Name the common forms of security in the Cayman Islands for movable property.

Question 3

How can a lender ensure that other people have notice of its secured position?

Commentary and Feedback on Self-Assessment Exercise 2

Question 1

Mortgage (legal or equitable), fixed charge

Question 2

Mortgage (legal or equitable, fixed charge, floating charged, pledge, lien

Question 3

File notice of the security with the centrally maintained registers if the property in question is land, a ship, an aircraft or a motor vehicle. For all other types of property, ensure that the Register of Mortgages for the debtor is clear before making the loan and updated with details of the charge after the granting of the loan.

Self-Assessment Exercise 3

Question 1

Which law governs personal bankruptcy in the Cayman Islands?

Question 2

Which debtors may be subject to the jurisdiction of the bankruptcy court?

Question 3

Name 5 acts or defaults which can be alleged by a petitioner as the grounds of a personal bankruptcy petition?

Question 4

Is all of the debtors property available to creditors?

Commentary and feedback on Self-Assessment 3

Question 1

The Bankruptcy Law (Cap 7) (1997 Revision).

Question 2

See section 2 of the law – persons present, resident, having a place of residence, carrying on business in the Cayman Islands.

Question 3

There are 12 acts of bankruptcy set out in the legislation.

Question 4

No, there are exceptions for the support of the debtors family (see sections 100 and 137, for example).

Self-Assessment Exercise 4

Question 1

Name the three types of liquidation in the Cayman Islands.

Question 2

Over which companies does the Cayman Islands Grand Court have jurisdiction?

Question 3

How can a company achieve a stay against creditor action?

Question 4

Under what circumstances may a voluntary liquidation come under court supervision?

Question 5

In what circumstances may a company by wound up by the Court?

Question 6

How does the automatic stay affect secured creditors?

Question 7

Describe the main avoidance of property provisions in the Cayman Islands.

Commentary and Feedback on Self-Assessment Exercise 4

Question 1

Voluntary liquidation, provisional liquidation and official liquidation.

Question 2

The Grand Court has jurisdiction to make (winding up) orders in respect of companies which are either:

(a) incorporated in the Cayman Islands;
(b) incorporated elsewhere but subsequently registered in the Cayman Islands; or
(c) in respect of a foreign company which –
- has property located in the Islands;
- is carrying on business in the Islands;
- is the general partner of a limited partnership; or
- is registered under Part IX (a so-called "overseas company").

See section 91 of the Companies Law.

Question 3

A company can only obtain a stay against creditor action if it has been placed into liquidation (which includes provisional liquidation) by the Court.

Section 96 of the Companies Law states:

"At any time after the presentation of a winding up petition and before a winding up order has been made, the company or any creditor or contributory may-

(a) where any action or proceeding against the company, including a criminal proceeding, is pending in a summary court, the Court, the Court of Appeal or the Privy Council, apply to the court in which the action or proceeding is pending for a stay of proceedings therein; and
(b) where any action or proceeding is pending against the company in a foreign court, apply to the Court for an injunction to restrain further proceedings therein."

Section 97 of the Companies Law states:

(1) "When a winding up order is made or a provisional liquidator is appointed, no suit, action or other proceedings, including criminal proceedings, shall be proceeded with or commenced against the company except with the leave of the Court and subject to such terms as the Court may impose.
(2) When a winding up order has been made, any attachment, distress or execution put in force against the estate or effects of the company after the commencement of the winding up is void."

Question 4

Section 131 of the Companies Law states:

"When a resolution has been passed by a company to wind up voluntarily, the liquidator or any contributory or creditor may apply to the Court for an order for the continuation of the winding up under the supervision of the Court, notwithstanding that the declaration of solvency has been made in accordance with section 124, on the grounds that-

(a) the company is or is likely to become insolvent; or
(b) the supervision of the Court will facilitate a more effective economic or expeditious liquidation of the company in the interests of the contributories and creditors."

Question 5

Section 92 of the Companies Law states:

"A company may be wound up by the Court if-

(a) the company has passed a special resolution requiring the company to be wound up by the Court;
(b) the company does not commence its business within a year from its incorporation, or suspends its business for a whole year;
(c) the period, if any, fixed for the duration of the company by the articles of association expires, or whenever the event, if any, occurs, upon the occurrence of which it is provided by the articles of association that the company is to be wound up;
(d) the company is unable to pay its debts; or
(e) the Court is of the opinion that it is just and equitable that the company should be wound up."

Question 6

Secured creditors are not prohibited from enforcing their security (Section 142 of the Companies Law).

Question 7

Section 99 (dispositions of property post-commencement), section 145 (voidable preference), section 146 (dispositions at an undervalue), section 147 (fraudulent trading) and common law breach of fiduciary duty.

Self-Assessment Exercise 5

Question 1

What is a scheme of arrangement?

Question 2

Is it possible for management to stay in place during a scheme?

Question 3

Is it possible to cram down dissenting shareholders?

Commentary and feedback on Self-Assessment Exercise 5

Question 1

A scheme is a court approved compromise or arrangement entered into between a company and its creditors or members. The power derives from section 86 of the Companies Law.

Question 2

If the company remains out of liquidation, the management stay in control. If the scheme is placed into provisional liquidation (normally with a view to securing breathing room from creditors) management may remain in control subject to oversight by the provisional liquidations. This is called a “light touch” provisional liquidation.

Question 3

It is possible for the majority of shareholders in a class to outvote dissenters within that class, but it is not possible for a majority of classes to outvote a dissenting class. In other words, there is no cross-class cramdown available.

Self-Assessment Exercise 6

Question 1

How will the Grand Court decide whether or not to grant assistance to overseas insolvency proceedings (and liquidators)?

Question 2

Are protocols used? Are there any legal requirements?

Commentary and Feedback on Self-Assessment Exercise 6

Question 1

The Cayman Islands has not implemented the UNCITRAL Model Law, although regard is had to the principles. The criteria upon which the Court’s discretion will be exercised is set out at section 242 of the Companies Law.

Question 2

There is no legislation governing protocols between courts. However, there is law on protocols between officeholders. These must be approved by the Grand Court.

Self-Assessment Exercise 7

How can one enforce a foreign judgement in the Cayman Islands?

Commentary and feedback on self-assessment exercise 7

At common law there are 5 requirements:

(1) the judgment is final;
(2) the foreign court had jurisdiction over the debtor;
(3) the foreign judgment was not obtained by fraud;
(4) the foreign judgment is not contrary to public policy of the Cayman Islands; and
(5) the foreign judgment was not obtained contrary to the rules of natural justice.

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