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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 5A**

**BERMUDA**

This is the **summative (formal) assessment** for **Module 5A** of this course and is compulsory for all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 5A**. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentID.assessment5A]**. An example would be something along the following lines: 202122-336.assessment5A. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **7 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

When is a Bermuda company deemed to be unable to pay its debts under section 161 and section 162 of the Companies Act 1981?

1. Only when it is balance sheet insolvent.
2. Only when it is cash flow insolvent.
3. When it is balance sheet insolvent and cash flow insolvent.
4. When it is either balance sheet insolvent, or cash flow insolvent, or a valid statutory demand has not been satisfied within a period of three weeks after service on the company’s registered office, or if a judgment in favour of a creditor remains unsatisfied.

**Question 1.2**

**Who may appoint** a Provisional Liquidator over a Bermuda company?

1. A secured creditor.
2. An unsecured creditor.
3. The company itself (whether acting by its directors or its shareholders).
4. The Supreme Court of Bermuda.

**Question 1.3**

**In what order** are the following paid in a compulsory liquidation under Bermuda law?

a) Preferential creditors; b) unsecured creditors; c) costs and expenses of the liquidation procedure; d) floating charge holders.

1. a, b, c, d
2. c, d, a, b
3. c, a, d, b
4. a, c, d, b

**Question 1.4**

**What percentage** of unsecured creditors must vote in favour of a creditors’ Scheme of Arrangement for it to be approved?

1. Over 50% in value.
2. 50% or more in value.
3. Over 75% in value.
4. A majority of each class of creditors present and voting, representing 75% or more in value.

**Question 1.5**

What is the **clawback period** for fraudulent preferences under section 237 of the Companies Act 1981?

1. Two (2) years.
2. One (1) month.
3. Twelve (12) months.
4. Six (6) months.

**Question 1.6**

What types of transactions are reviewable in the event of an insolvent liquidation?

1. Only fraudulent conveyances.
2. Only floating charges.
3. Only post-petition dispositions.
4. All of the above.

**Question 1.7**

How many insurance policyholders are required to present a petition for the winding up of an insolvent insurance company under section 34 of the Insurance Act 1978?

1. At least five (5).
2. One (1) is sufficient.
3. At least 10 or more owning policies of an aggregate value of not less than BMD 50,000.
4. At least 10.

**Question 1.8**

Where do secured creditors rank in a liquidation?

1. Behind unsecured creditors.
2. Behind preferential creditors.
3. Behind the costs and expenses of liquidation.
4. In priority to all other creditors, since they can enforce their security outside of the liquidation.

**Question 1.9**

Summary proceedings against a company’s directors for breach of duty (or misfeasance) may be brought by a liquidator under which provision of the Companies Act?

1. Section 237 of the Companies Act 1981.
2. Section 238 of the Companies Act 1981.
3. Section 247 of the Companies Act 1981.
4. Section 158 of the Companies Act 1981.

**Question 1.10**

What is a segregated account representative of an insolvent Segregated Accounts Company required to do under section 10 of the Segregated Accounts Companies Act 2000?

1. Resign immediately.
2. File a Suspicious Transaction Report forthwith.
3. Make a written report to the Registrar of Companies within 30 days of reaching the view that there is a reasonable likelihood of a segregated account or the general account becoming insolvent.
4. Notify the directors, creditors and account owners within 28 days.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 4 marks]**

In what circumstances may be a Provisional Liquidator be appointed?

A Provisional Liquidator (“PL”) may be appointed pursuant to Section 170(2) of the Companies Act 1981 during the time which the winding up petition is made and the final hearing for winding up order is granted. Such powers to appoint a PL is only conferred to the court. If the court deems that an urgent appointment of PL is for the benefit of creditors and circumstances warrants the appointment of PL. Such circumstances typically involve risk of dissipation of assets in a short span of time and a probable scenario of a successful restructuring be completed, through a soft-touch provisional liquidation, with the appointment of PL, given the stay of other legal actions.

**Question 2.2 [maximum 2 marks]**

When can rights of set-off be exercised after the commencement of a liquidation of a Bermuda company?

The transactions subject to set-off must be genuine and not subject to fraudulent preference or fraudulent conveyance. The parties entering into these transactions must be relating to the same type of contract, playing the same role eg. providing same service / goods in the relevant transactions. These transactions must have been entered into prior to commencement of liquidation and the debts must have fallen due or become due and payable.

**Question 2.3 [maximum 4 marks]**

Describe **three possible ways** of taking security over assets under Bermuda law?

1. A legal mortgage – in exchange for a debt, the debtor may transfer the legal title of an asset to a creditor. While the debtor retains the possession of the asset, the legal title of the asset is transferred to the creditor and the creditor retains the legal title until such time the debts have been fully satisfied.
2. Fixed charge – A creditor may also obtain a fixed charge against an asset that gives them the right to take possession and sell the asset in the event of default by debtor. A fixed charge secured creditor may sell the asset without any notice to other creditors and apply the proceed of sale towards payment of the debts due to them. During such time the asset is subject to a fixed charge, the debtor may not deal with the asset without consent by the fixed charge holder.
3. Floating charge – for movable assets and or some intangible property, a creditor may take a floating charge security. Such floating charge only crystallises upon an event of default and converts to a fixed charge attached to the balance of these assets on the date of default. Prior to which, the debtor may deal with the asset as they deem fit, without consulting or getting approval from the creditor.

It is important to note that any security agreement that is entered into should also be filed as soon as practicable with the Registrar of Companies in Bermuda. This is to ensure that the security interests are perfected and those security that are registered with the Registrar will have priority over any security interests that are not registered or subsequently registered. This registration with the Registrar also serves as notice to third party as the register is publicly available.

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1** **[maximum 8 marks**]

Write a brief essay on the basis upon which foreign liquidators are granted recognition and assistance in Bermuda.

There is currently no statutory law that legislates the recognition and assistance granted by Bermuda courts to foreign liquidators. In the case of *Cambridge Gas Transportation Corp v Navigator Holdings plc,* the Privy Council held that as a matter of common law, the Supreme Court of Bermuda can recognize liquidators appointed by a foreign court and the winding up order. The Bermuda courts have discretion to grant such recognition and assistance to the foreign liquidation which would have been allowed if the winding up had taken place in Bermuda or as allowed for by Bermuda laws. The scope that such recognition and assistance may be granted is subject to discussions and has been highlighted in the recent cases in *Singularis Holdings Limited v PricewaterhouseCoopers* and *PricewaterhouseCoopers v Saad Investments Company Limited.* In these cases, the Privy Council held that the assistance that may be granted should be only those that are available in the foreign jurisdiction and in Bermuda locally and must also not be contrary to public policy.

Summarily, recognition and assistance are most likely to be granted / provided to foreign liquidators by the Bermuda Court when the following conditions are met:

1. There is an established nexus between the foreign entity and the foreign court that makes the foreign court the most suitable forum for an order granting the appointment of foreign liquidator be made.
2. The foreign entity conducts its affairs in Bermuda and has documents, properties or debts in Bermuda. The foreign entity has conducted business via its officers and agents in Bermuda and is required to be a party to ongoing proceedings within Bermuda; and
3. Providing assistance does not contravene any public policy.

The privy council has raised the issue of the extent that common law allows assistance to foreign liquidators is on a case-by-case basis and type of assistance that is being sought. The power of the Bermuda court to grant an order for the production of documents is limited to cases where it is deemed essential to support the foreign liquidator. The Bermuda court is not able to assist with voluntary liquidations, which are deemed to be an informal agreement. If the foreign court does not allow for the order to be granted, the Bermuda court will not be able to grant such order. Any orders made by the Bermuda courts must be consistent law in Bermuda and public policy.

It is common for Bermuda exempted companies to do business in foreign countries, be listed in foreign exchange and be subject to foreign insolvency regulations. If winding up proceeding is not taking place in Bermuda, typically, there will be supplementary liquidation proceedings in Bermuda in parallel or judicial recognition and aid from the Bermuda Supreme Court will be sought by the foreign liquidator.

**Question 3.2 [maximum 7 marks]**

Write a brief essay on the circumstances in which a foreign Court judgment **will not be** registered or enforced in Bermuda. Also consider and address the question as to whether a foreign Court-sanctioned Scheme of Arrangement might be registered or enforced in Bermuda.

There are steps required for a foreign Court judgment to be enforceable in Bermuda. Depending on the type of judgment, one may rely on statutory and/or common law to decide how to take such steps for enforcement or registration. Generally, the following applies for the registration and enforcement of various types of judgements:

1. Judgments (Reciprocal Enforcement) Act 1958 (the “1958 Act”) applies to final money judgments in superior courts from UK and certain commonwealth countries and for final money judgments from other countries not listed, common laws apply.
2. Maintenance Orders (Reciprocal Enforcement) Act 1974 (the “1974 Act”) applies to foreign maintenance orders made by courts of reciprocating countries
3. Recognition of foreign judgments in Bermuda proceedings is governed by both statutory and common law rules. They determine the applicability of foreign judgments as a defense against a claim or as conclusive evidence for ongoing disputes within the Bermuda proceedings.
4. Statutory regulations apply to recognition of divorces and legal separations.

Other statutory or common law regulation applies to other types of judgements eg. Arbitration awards, etc. Foreign money judgment that is not defined in the 1958 Act or the common law may not be registered or enforced by application to Bermuda courts.

The 1958 Act also allows for UK judgments granted by superior courts be registered in Bermuda as if it was an order granted locally. This is also extended to Commonwealth countries as set out in Appendix II of the 1958 Act.

A foreign judgment registered under the 1958 Act can be set aside if it fulfils the following criterion:

1. It is not defined in the 1958 Act or was registered contrary to the 1958 Act
2. The foreign court was not the appropriate forum to grant such order due to lack of jurisdiction
3. Notice was not given or insufficient time was provided for defendant to respond and defendant did not appear at the hearing where judgment was made
4. It was obtained by deception
5. The party making the application had no right to such claims

A registration may be set aside if the Bermuda court takes the view that the issue had already been dealt with at the appropriate forum prior to the date of such foreign judgment being made. The courts of Bermuda may not set aside the registration of foreign judgment solely due to the reason that it is not just and equitable or it is contrary to public policy for such registration or enforcement to take place.

Foreign judgments that are not defined under the 1958 Act is governed by the common law, which deems it as an evidence of debt and requires separate legal actions be commenced.

Pursuant to common law, a foreign money judgment will be registered and enforced if:

1. it is legally binding and conclusive
2. foreign court had jurisdiction and was the appropriate forum
3. it was not obtained by act of deceit
4. it does not pertain to taxes, fines or penalties, i.e. sums due to the foreign country
5. it is not contrary to public policy
6. principles of natural justice was upheld

In general, any judgment that deviates from or fails to adhere to the principles of common law in England regarding the recognition and enforcement of foreign judgments will not be successful.

A final and conclusive foreign judgment granted by a foreign court with jurisdiction may be registered pursuant to common law and can be used as evidence in other legal cases in Bermuda. If a judgment is granted in favour of one party by foreign court, said party is not allowed to commence the same proceeding in Bermuda, unless such foreign judgment cannot be registered or enforced in Bermuda.

In the case of *Stephen John Hunt v Transworld Payment Solutions UK Limited*, the Supreme Court of Bermuda did not recognise the appointment of a foreign liquidator from UK as no active assistance had been sought and such assistance if sought would be rejected, given that there are proceedings in England and Wales and other methods available to the parties to gather more information.

The recognition and enforcement of foreign Schemes of Arrangement in Bermuda under common law is uncertain. While the Bermuda courts have recognized foreign court orders approving such schemes, it is unclear what position the courts will take in the event of disputes.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

ELBOW LIMITED (“the Company”) was incorporated in 2019 as an exempt Bermuda company, as the parent company in a group of companies, with a direct subsidiary incorporated in the British Virgin Islands, and with indirect subsidiaries incorporated in Hong Kong and with offices and a substantial business presence in Hong Kong. The Company was formed with the intention of investing, through subsidiaries, in illiquid assets in the form of litigation funding loans and distressed debt in Asian markets.

Having funded, through one of its subsidiaries, a hopeless court case in Hong Kong against VICTORY LIMITED, a costs order was made by the Hong Kong Court against ELBOW LIMITED in favour of VICTORY LIMITED in the sum of USD 2 million, payable in full within 14 days.

At the due date for payment of the costs order to VICTORY LIMITED, ELBOW LIMITED’s assets were fully invested and its investments, although illiquid, were valued in the aggregate sum of USD 10 million.

The Company’s directors decided that it was in the best interests of ELBOW LIMITED and its shareholders not to satisfy the Hong Kong Court judgment and not to liquidate any of its assets to cash given the risk that an urgent “fire-sale” would completely destroy the value of those assets, and in circumstances where ELBOW LIMITED did not consider that the Hong Kong Court judgment would be enforceable against it in Bermuda.

The Company’s directors subsequently borrowed an additional USD 5 million from its bank, LENDBANK, secured by way of a floating charge against all of its shares and the assets of its subsidiaries. Out of the USD 5 million received from LENDBANK, ELBOW LIMITED’s directors immediately paid themselves a bonus payment of USD 2 million and they also paid a dividend to the Company’s shareholders in the sum of USD 3 million.

VICTORY LIMITED only found out about these transactions two weeks later, through a report received from a disgruntled former employee of ELBOW LIMITED.

**Using the facts above, answer the questions that follow**.

**Question 4.1 [maximum 7 marks]**

What actions could VICTORY LIMITED take to try to recover its cost order against ELBOW LIMITED? Please consider (a) the jurisdictions in which it could take such action, bearing in mind the potential need for enforcement; (b) the defendants against whom it could take such action; (c) the pros and cons of litigation as opposed to insolvency proceedings; and (d) the causes of action that may be available against the various potential defendants.

1. Possible Jurisdictions to take action – Hong Kong, Bermuda, BVI

Practically, it may be easiest for Victory Limited (“**VL**”) to commence action in Hong Kong, where assets of Elbow Limited (“**EL**”) are located and can be easily enforced against. However, the claim of VL is against EL, which is incorporated in Bermuda and EL may not have a direct connection to the assets in Hong Kong. It is more likely for VL to get a successful order in favour in Bermuda courts and then to subsequently seek recoveries in BVI via the direct subsidiary and indirect subsidiaries in Hong Kong.

1. & (d) defendants and causes of action against potential defendants – directors of EL, shareholders of EL, EL directly, subsidiary in BVI, indirect subsidiaries in Hong Kong

Directors of EL – breach of duty of care - for failing to make payment on time pursuant to the Hong Kong judgment and subsequently charging the assets to Lendbank for additional financing and making bonus payments of USD2m to directors and USD3m of dividends to shareholders when EL may be insolvent or would have become insolvent as a result.

Shareholders of EL – for receipt of unlawful dividend when EL is insolvent or may have become insolvent as a result of the dividend payment.

EL – for default in making payment as required by the order

Subsidiary in BVI – to seek remedy of cost order against EL’s assets, including its subsidiary in BVI

Indirect subsidiaries in Hong Kong – to seek remedy of cost order against EL’s assets, including its indirect subsidiaries in Hong Kong

1. Pros and cons of litigation as opposed to insolvency proceedings

Litigation may be a long-drawn process and can take significant time to conclude, which may end up being very costly. Insolvency proceedings are relatively more straightforward and can be concluded in a shorter timeframe and thus cost less.

Litigation outcomes may be uncertain and unpredictable, depending on the matters that come to light during the process and dependant on the judge’s view. It can however result in settlement being made if both parties do not want to incur additional costs to conclude the dispute.

As EL is not balance sheet insolvent (total assets is valued at USD10m and only USD2m is owed to VL), it may be difficult to wind up EL as there is no basis to do so. A winding up proceeding may be utilized and commenced by VL as leverage to facilitate negotiations with EL.

It is noted however that EL’s assets are illiquid and if there are news of winding up proceedings being commenced, it may result in significant discount being applied to the assets held by EL and adversely affect the recoveries of VL. Hence, insolvency proceedings should only be commenced if discussions fall through, and likelihood of recoveries or settlement is low.

**Question 4.2 [maximum 8 marks]**

To what extent would it be open to ELBOW LIMITED to try to take steps to restructure its debt obligations? How and where would it do so? Consider whether it would be more appropriate to take steps before the Hong Kong courts, the Bermuda courts, or both and, if so, why? Also consider whether it would make any difference if the debt restructuring involved a “debt-for-equity” swap, i.e. the creditors of ELBOW LIMITED would be issued new shares in the Company in exchange for cancellation of their debt, with existing shareholders’ shares in the Company being cancelled.

Bermuda restructuring

Directors of EL may wish to restructure through an informal work out and discussion with creditors but this requires all creditors consent and during such time EL will be subject to enforcement actions by creditors. While it is the directors’ duty to take steps to rehabilitate the company by taking steps to restructure, it may be more effective to conduct such restructuring by way of a soft-touch provisional liquidation. Directors may choose to appoint a provisional liquidator, to allow Elbow Limited (“EL”) the benefit of the automatic stay of proceedings for companies in provisional liquidation while a scheme of arrangement is being worked out to prevent any creditor from disrupting the process by commencing litigation and/or winding up proceedings. Noting that EL has business dealings in other jurisdictions, it is likely that EL may be subject to other enforcement proceedings in foreign jurisdictions, which may disrupt the restructuring process. Hence, a soft-touch provisional liquidation is required to offer protection against further enforcement actions.

A Scheme of Arrangement can be adopted to implement a debt-to-equity swap as it is a procedure designed to allow an entity to restructure its debt and equity. A scheme requires consent from majority in number representing at least 75% in value of each class of creditors and/or members. The Bermuda court has jurisdiction to sanction such a scheme.

Any transfer of shares of a Bermuda exempt company, which EL is, will require approval of the Bermuda Monetary Authority. Hence, the scheme will also require the approval of the Bermuda Monetary Authority for the cancellation of existing shareholders’ shares and issuance of new shares (swapping of debt to equity).

Hong Kong restructuring

It can be argued that EL’s centre of main interest is in Hong Kong, where its assets are in and where EL conducts its business.

There is no formal restructuring procedure available under Hong Kong law. However, it is possible to negotiate an informal work-out. Similar to Bermuda law, this will require consent of all creditors. Pursuant to the directive of the Hong Kong Association of Banks and the Hong Kong Monetary Authority, lenders are generally encouraged to discuss restructuring options with borrowers. Without co-operation from all creditors, a scheme of arrangement may be more effective to drive a successful restructuring that is binding on all creditors.

Pursuant to Division 2 of Part 13 of the Companies Ordinance (Cap. 622 of the laws of Hong Kong), a scheme of arrangement requires approval from majority in number and at least 75% in value of each class creditors or members present and voting. The scheme will become binding on all such classes once approved by court, including dissenting creditors and members. The Hong Kong courts have discretion on the decision to sanction any scheme. Factors that the courts will consider include: (i) if statutory requirements have been complied with, (ii) whether there is fair representation of each class acting in good faith voting in favour, and (iii) whether the interest of all classes of creditors / members are not prejudiced. Where creditors / members have varying / conflicting interests, they should be split into different classes and be required to vote separately and have separate discussion on any proposed scheme.

Similar to the Bermuda scheme of arrangement, no protection is provided against enforcement actions by creditors and a provisional liquidator may have to be appointed to protect EL from such enforcement actions.

The recognition and enforcement of foreign Schemes of Arrangement in Bermuda under common law is uncertain. While the Bermuda courts have recognized foreign court orders approving such schemes, it is unclear what position the courts will take in the event of disputes.

Hence, it is more advisable to proceed with the restructuring process directly in Bermuda, or if there requires a proceeding in Hong Kong, the proceeding in Hong Kong should be conducted in parallel to that in Bermuda.

**\* End of Assessment \***