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

**CAYMAN ISLANDS**

This is the **summative (formal) assessment** for **Module 5C** of this course and must be submitted by 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 5C**. 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.assessment5C]**. An example would be something along the following lines: 202223-336.assessment5C. **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 “studentID” 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 2024**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2024**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

**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**

Select the **correct answer**.

Once an application for a restructuring officer is filed:

1. No action may be commenced against the company without permission of the court.
2. No action may be continued against the company without permission of the provisional liquidator.
3. No action may be continued against the company without permission of the restructuring officer.
4. No action may be commenced against the company.

**Question 1.2**

Which of the following is **not** available to a corporate debtor in the Cayman Islands?

1. Appointment of a receiver.
2. Court-supervised liquidation.
3. Official liquidation.
4. Deed of Company Arrangement.

**Question 1.3**

Select the **correct answer**.

In a voluntary liquidation:

1. The company may cease trading where it is necessary and beneficial to the liquidation.
2. The company must cease trading except where it is necessary and beneficial to the liquidation.
3. The company must cease trading if it is necessary and beneficial to the liquidation.
4. The company may cease trading unless it is necessary and beneficial to the liquidation.

**Question 1.4**

Select the **correct answer**.

The Grand Court of the Cayman Islands has jurisdiction to make winding up orders in respect of:

1. A company incorporated in the Cayman Islands.
2. A company with property located in the Cayman Islands.
3. A company carrying on business in the Cayman Islands.
4. Any of the above.

**Question 1.5**

Select the **correct answer**.

In a provisional liquidation, the existing management:

1. Continues to be in control of the company.
2. Continues to be in control of the company subject to supervision by the court and the provisional liquidator.
3. May continue to be in control of the company subject to supervision by the provisional liquidator and the court.
4. Are prohibited from having any control of the company.

**Question 1.6**

Select the **correct answer**.

When a winding up order has been made, a secured creditor:

1. May enforce their security with leave of the court.
2. May enforce their security without leave of the court.
3. May enforce their security with leave of the court provided the liquidator is on notice of the application.
4. May not enforce their security until the liquidator has adjudicated on the proofs of debt.

**Question 1.7**

Select the **correct answer**.

Any payment or disposal of property to a creditor constitutes a voidable preference if:

1. 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.
2. It occurs in the six months before the deemed commencement of the company’s liquidation, or 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.
3. 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, or the dominant intention of the company’s directors was to give the applicable creditor a preference over other creditors.
4. It occurs in the six months before the deemed commencement of the company’s liquidation, or at a time when it is unable to pay its debts, or the dominant intention of the company’s directors was to give the applicable creditor a preference over other creditors.

**Question 1.8**

Which of the following **is not** a preferential debt ranking equally with the other four?

1. Sums due to company employees.
2. Taxes due to the Cayman Islands government.
3. Sums due to depositors (if the company is a bank).
4. Unsecured debts which are not subject to subordination agreements.
5. Amounts due to preferred shareholders.

**Question 1.9**

Select the **incorrect statement**.

A company may be wound up by the Grand Court if:

1. The company passes a special resolution requiring it to be wound up.
2. The company is unable to pay its debts.
3. The company is carrying on regulated business in the Cayman Islands without a license.
4. The company does not commence business within six months of incorporation.

**Question 1.10**

Select the **correct answer**.

In order for a proposed creditor scheme of arrangement to be approved:

1. 50% or more in number representing 75% or more in value of the creditors must agree.
2. More than 50% in number representing 75% or more in value of the creditors must agree.
3. 50% or more in number representing more than 75% of the creditors must agree.
4. More than 50% in number representing more than 75% of the creditors must agree.

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

**Question 2.1 [maximum 4 marks]**

Does the Cayman Islands Grand Court have the power to assist foreign bankruptcy proceedings? If so, what is the source of that power and in what circumstances may it exercise it?

Although the Cayman Islands has not implemented the UNCITRAL Model Rules on Cross-Border Insolvency and is not a member of the EU, the Cayman Islands Grand Court does have the power to assist foreign bankruptcy proceedings, as provided in Part XVII of the Companies Act. There are no threshold requirements in order to provide assistance and there is no automatic right based on the COMI of the Debtor. Instead, foreign professionals must apply to the Court and request that the Court exercise its discretion in granting the relief requested.

Some examples of relief that can be granted are (1) recognizing the right of a foreign representative to act on behalf of a Debtor in the islands; (2) preventing commencement or staying continuation of legal proceedings; (3) preventing judgment enforcement against a Debtor; (4) requiring examination of a person having information on a Debtor’s affairs and/or production of documents; and (5) turnover of property owned by a Debtor to the foreign representative.

The Court’s discretion to grant the above forms of relief is based on the economic and efficient administration of the Debtor’s estate, so as to provide just treatment of claims, protection of Cayman Island claim holders from administration of their claims in a foreign proceeding, prevention of preferential or fraudulent transfers, equitable distribution to creditors in accordance with the Cayman Islands priority structure, recognition and enforcement of security interests, non-enforcement of foreign taxes, fines and penalties and mutual cooperation and recognition between regions.

**Question 2.2 [maximum 3 marks]**

Outline the legal framework for the recognition of foreign judgements in the Cayman Islands.

The legal framework for recognition of foreign judgments in the Cayman Islands is based on a cooperative approach with an aim towards effective winding up and protection of Cayman Islands creditors. There are no international treaties that apply to recognition of foreign judgments, the UK has not ratified any treaties to the Cayman Islands by Order of Council and the Cayman Islands is not a signatory to the Hague Convention.

The Foreign Judgments Reciprocal Enforcement Act (1996 Revision) does provide a statutory basis for recognition and enforcement of foreign judgments, but only if the country from which the judgment originates gives reciprocity to the Cayman Islands. As of this point in time, the only country meeting this requirement is Australia. Even then, the foreign judgment must be final, a money judgment and made after the 1996 Act was extended to the applicable country.

As a result of the limited application, most creditors having a foreign judgment are required to commence a new action in the Cayman Islands in order to obtain enforcement. These actions are conducted pursuant to the Grand Court Rules and common law. Once the local judgment has been obtained, it is entitled to full enforcement remedies subject to a six year limitation period.

**Question 2.3 [maximum 3 marks]**

Is it possible for a creditor to register its security over an asset in the Cayman Islands? If so, how, and what is the effect of it doing so, if any?

There is no required statutory regime in the Cayman Islands for perfection of security interests. If there is a security interest granted in the pertinent documents, it is enforceable unless otherwise voidable. There are, however, ownership registers for real estate, ships, aircraft, motor vehicles and intellectual property. Registration ensures that the secured creditor takes priority over a bona fide purchaser and establishes priority over other non-registered secured creditors. For other categories of assets other than those noted above, there is no public security registration. Thus, a creditor must take adequate measure to investigate whether an asset is encumbered prior to granting a lien. Also, a Debtor is required to maintain a register of mortgages (although there is no meaningful penalty for failure to comply to the Debtor or the omitted creditor and so this is often not done). In any event, a creditor should also review the Debtor company’s register of mortgages as part of its investigation.

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

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**Question 3.1 [maximum 6 marks]**

Receivers have no role to play in a Cayman Islands insolvency scenario. Discuss.

Receivers do not necessarily play a role in an insolvency per se, but they are a often used remedy for secured creditors There are two types of receiverships: private and court appointed.

A private receiver is one appointed by a secured creditor pursuant to their contractual provisions in their security documents. The receiver in this instance is concerned only with the particular collateral noted in the agreement and the primary duty is to the secured creditor.

In contrast, a court appointed receiver can be appointed whenever justice requires it, such as to safeguard assets pending resolution of a dispute or to liquidate assets and distribute the proceeds to creditors and shareholders. The Court’s power to appoint a receiver derives from section 11(1) of the Grand Court Act, which models court appointed receiverships after those occurring in the High Court of England (section 37(1) of the Senior Courts Act 1981). The most common forms of receivership are to preserve status quo as to assets pending litigation or to sell assets so as to collect on a monetary judgment. These types of receivers can play a very similar role to that of a professional insolvency practitioner in an insolvency scenario (and indeed many insolvency practitioners also serve as receivers).

One other type of receivership is provided specifically by statute and is very similar to an insolvency proceeding. This is the Segregated Portfolio Company receivership. An SPC company can go through an official liquidation or, alternatively can have a receiver appointed. The receivership order can be sought by the SPC itself, a creditor, a shareholder or the Cayman Islands Monetary Authority (CIMA) when the SPC is licensed under the regulatory laws. During the period of the receivership order, the receiver takes over the operations of the particular portfolio to which he/she has been appointed and the directors are divested of their powers and functions. Thus, again, the receiver’s role is similar to a liquidator.

**Question 3.2 [maximum 9 marks]**

In the absence of a statutory prohibition on insolvent trading, is it possible for court appointed liquidators of an insolvent company, or creditors of such a company, to hold its former directors accountable by either seeking financial damages against those directors and / or by seeking to “claw back” any payments that those directors should not have made? If so, please explain the possible options.

Yes the official liquidator may bring this type of action for transfers prior to the official liquidation. Directors can be personally liable to the company for losses they cause the company to incur if they have not acted in the best interests of the company such that they have breached their fiduciary duty. The seminal case on this is Prospect Properties v. McNeill, where the Grand Court held that a directors is required to act in the best interests of the company’s creditors when the company is insolvent. This is part of the directors’ duty to act in the best interests of the company and includes safeguarding the company against being in the position of not being able to pay its creditors.

The official liquidator of an official liquidation may pursue claims on behalf of the company against the directors for breach of fiduciary duty in situations such as outlined above. However, there is no statutory obligation for an insolvent company to file for insolvency and the Companies Act does not contain a prohibition on wrongful trading (in other words, a company can continue to trade when insolvent). So, it appears to be a matter of discretion for the official liquidator and the Court.

Also, the official liquidator has the power to claw back any dispositions of the company’s property under Section 99 of the Companies Act. Any asset dispositions after commencement of the wind up but before the winding up order is made can be voided by the official liquidator. In such case, the official liquidator will be able to either recover the asset or the funds. Sometimes, alternatively, these dispositions can be ratified by the Court. However, when the company is insolvent, the Court is unlikely to ratify the dispositions unless it can be shown that the disposition benefitted the company and the creditors as a whole.

In addition, the liquidator can seek to claw back, or void, certain transactions. One such transaction is known as a preference to a creditor. Under Section 145 of the Companies Act, a payment to a creditor is a preference if (1) it was made within six months of the deemed commencement of the liquidation and when the company was insolvent (2) the dominant intention of the directors was to give the creditor a preference over other creditors. The dominant intention can be inferred from the evidence.

Another claw back statute is contained in Section 146 of the Companies Act which allows the liquidator and/or creditor to apply to the Court in order to claw back (or deem voidable) a disposition made at under value. In order for this type of transaction to be avoided, there has to be an intent to defraud. The action must be brought within six years of the disposition and the burden of proof to establish intent to defraud is on the liquidator or creditor.

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

Punk Lizard is a company registered in the Cayman Islands. It operates liveaboard diving cruises across the Caribbean. Punk Lizard was founded by the Kraken family over 70 years ago. The family continues to own and manage the business.

Punk Lizard’s revenues are down in recent years, due to some well publicised safety issues. The business has only managed to stay afloat with the assistance of a very large loan from Turtle National Bank (TNB). TNB has lent Punk Lizard USD 900 million (USD 450 million of which is secured by a mortgage over half of Punk Lizard’s fleet).

The market for liveaboard diving remains strong, and financial forecast for Punk Lizard is relatively bright, however Punk Lizard has immediate solvency issues. It cannot afford to pay the ongoing costs associated with maintaining its fleet (electricity, maintenance, insurance, staff costs, rum etcetera) and it has fallen behind on the monthly repayments to TNB.

To make matters worse, Punk Lizard commissioned Harland & Wolff (H&W) to build five more dive boats shortly before the (lack of) safety issue hit the news. Punk Lizard has failed to pay for the H&W boats. H&W has secured an arbitration judgment from the ICC in London for USD 150 million. The award is payable within 28 days.

You are a Cayman Islands-based insolvency professional and have been approached to provide advice on the following:

1. What action can TNB take to protect its interests? (2 marks)

TNB has a mortgage against half of Punk Lizard’s fleet. Since Punk Lizard has fallen behind on its monthly repayments, TNB may proceed may proceed to take possession of its collateral and exercise its power of sale according to its loan documents and/or may appoint a receiver. Secured creditors rank highest in priority over all creditors and can proceed with enforcement actions without regard to whether a windup is commenced. There is no stay on enforcement that applies to a secured creditor. TNB could also have the liquidator (if one is appointed) sell the assets, in which case the costs associated with the sale are recoverable with a higher priority to the secured creditor.

It is unclear from the hypothetical as to whether TNB is oversecured or undersecured but ½ of the Punk Lizard’s fleet is not subject to the mortgage. If TNB is undersecured, it may want to take additional action, such as entering into a scheme of arrangement (eg receiving turnover of additional funds and/or boats in exchange for its unsecured indebtedness). Or, perhaps negotiating with the company to start a restructuring petition if there is a meaningful likelihood that the company could come out of it as a solvent company. Alternatively, TNB could file an application for a provisional liquidation and have a liquidator appointed if continuation of the company is not feasible.

1. What action can H&W take to protect its interests? (2 marks)

It is possible that H&W would want to file a application for a provisional liquidator if there is no chance that the company could regain solvency. Section 104(2) provides that a provisional liquidator can be appointed (1) if the creditor can pass to Prima Facie hurdle (ie it being more likely than not that a wind up order will be granted) and (2) the appointment is necessary to prevent dissipation of assets or to prevent misconduct of directors. In this case, H&W should be able to satisfy the Prima Facie hurdle because it has a judgment (ie, its debt is no longer in dispute) as long as it can also prove that Punk Lizard is not paying its debts within the meaning of Section 93 of the Companies Act. As to necessity, H&W would need to prove by clear and strong evidence that a provisional liquidator is necessary in order to prevent dissipation of assets.

H&W may also want to enter into a scheme of arrangement or informal workout wherein the company could agree to turnover some of its unliened fleet to H&W in exchange for retirement of the debt. Again, we do not have information as to the value of the fleet or whether this would be possible given TNB’s lien.

Lastly, since H&W is an unsecured creditor, it may be best off cooperating in a corporate rescue, since apparently the future market for Punk Lizard is possibly brighter than a liquidation would yield.

Or, H&W assumedly could acquire a judgment lien against the unliened fleet and appoint a receiver to potentially take control of these assets and sell for the benefit of H&W. Or, if H&W could negotiate to obtain a consensual lien on the unliened fleet perhaps in exchange for a reduction of the amount owed, this would likely be the best option available to H&W so that it could then pursue collection without regard for any insolvency proceeding that might thereafter be filed.

1. What action can the unpaid employees take against Punk Lizard? (3 marks)

It would seem that the unpaid employees would have two options: either to commence an application for provisional liquidation and/or windup petition (based on their creditor status from not having been paid) or to cooperate in a corporate rescue by the company. Pursuant to Section 141 of the Companies Act, employees are included in the preferential debt category for priority for payment of their claims in a liquidation. However, this only means that they share on an equal basis with any taxes due to the Caymanian government and/or with unsecured claims, which in this case would include the $150 million judgment of H&W. And they come behind any expenses of the liquidation. As such, a liquidation may not provide much of an option for the employees and they likely would lose their jobs (the company uses ceases to exist)

If a liquidation is not commenced of the company, the employees would likely be able to negotiate a scheme of arrangement (Section 86 of the Companies Act) or informal workout so that they could keep their jobs and get paid for their past work, in order to continue the business during a corporate rescue. On august 31, 2022, Part V of the Companies Act was amended so as to allow a restructuring alternative. Essentially, then, parties negotiate a scheme of arrangement within the restructuring proceedings. Alternatively, they may be able to work with any receiver or restructuring officer appointed, in order to keep the business going and be paid as part of the receiver’s efforts to liquidate the assets and/or as part of the restructuring process.

1. Does the Cayman Islands Court have jurisdiction over Punk Lizard? (1.5 marks)

Punk Lizard is registered in the Cayman Islands. As such, the Grand Court of the Cayman Islands has jurisdiction.

1. Is there a legal route via which Punk Lizard can protect itself and seek to restructure? (3 marks)

Prior to 2022, Cayman legislation did not allow for a corporate restructure (except by initiating provisional liquidations and/or schemes of arrangement). However, on August 31, 2022, Part V of the Companies Act was substantially amended to introduce a restructure process similar to Chapter 11 of the United States Bankruptcy Code.

Corporate rescue now includes informal workouts, provisional liquidation, restructuring officer appointments and schemes of arrangement. With the application for a restructuring officer, a moratorium immediately occurs. Thus, Punk Lizard could avoid an appointment of a receiver by H&W in connection with a judgment lien. However, the application for a restructuring officer would not prevent TNB from collecting on its lien by exercising its power of sale with respect to the ½ of the fleet to which its mortgage applies. Still, if TNB is undersecured, it may be willing to forego collection if the prospects for recovery on any unsecured portion of its debt is more likely in a restructure.

Under Section 91B(1) of the Companies Act, Punk Lizard could commence an application for a restructuring officer on the grounds that it is unable to pay its debts and intends to present a compromise or arrangement to its creditors. The grounds for appointment of a restructuring officer are the same as those required to appoint a provisional liquidator under 104(3) of the Companies Act. And, in fact, the Court can now appoint a provisional liquidator in any case where the Court deems it appropriate to do so. There is no prima facie or necessity test, as there is for creditor provisional liquidator applications. The only evidence required is that the directors consider the provisional liquidator and/or restructuring officer to be in the best interests of the company.

1. Following on from (e) above, can the Kraken family continue play a part in running Punk Lizard during any restructuring process? (1 mark)

Possibly yes. A provisional liquidation order and/or a restructuring officer order can provide for continuing power and authority of the company’s board of directors. The order itself will detail the powers and authority which the board of directors remain authorized to exercise and any limitations of such power and authority. The Court has discretion as to the terms and provisions of the order. When a board of directors stays involved notwithstanding the appointment of a restructuring officer or provisional liquidator, this is known as a “light touch”.

1. What factors will the Cayman Islands court take into consideration before approving any proposed restructuring? (2.5 marks)

Initially when the Court convenes a hearing in a restructuring process, the Court will be concerned primarily with class composition, jurisdiction, the adequacy of the scheme documentation and whether appropriate notice has been provided. Any creditor or stakeholder may appear at the hearing and to object to any orders requested. The Court must be satisfied that the scheme document contains all necessary information such that the scheme creditors can make an informed decision about the proposed scheme.

Then, if the scheme obtains the necessary creditor support, the Court must still sanction the scheme before it is binding on all creditors. At the Sanction hearing the Court considers whether (1) the scheme is reasonable; (2) each class was fairly represented at the Scheme meeting; (3) the majority acted bona fide; (4) all notice periods were met; and (5) the requisite percentages were obtained for the voting resolutions.

In totality, the Court requires the following to occur in order for a Scheme to be approved:

1. Petition is filed with supporting evidence and summons;
2. Evidence has all information that a party could reasonably require to make an informed decision on voting;
3. Stakeholders separated into classes commensurate with their respective rights;
4. Any objections are considered as to the documents, classes, meetings etc;
5. The company strictly complies with the required procedure set out in orders made the Convening Hearing;
6. All classes approve the Scheme, with the required majorities;
7. The Chairman must report to the Court;
8. The Court makes the orders sanctioning the Scheme, after considering the objections;
9. The company must fulfil all conditions in the Scheme; and
10. The Scheme becomes effective when the order is filed at the Registrar of Companies

**\* End of Assessment \***