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

**BERMUDA**

This is the **summative (formal) assessment for Module 5A** 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 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: 202223-336.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 “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.

7. Prior to being populated with your answers, this assessment consists of **10 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**

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 1.2**

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 1.3**

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

1. Preferential creditors.
2. Unsecured creditors.
3. Costs and expenses of the liquidation procedure.
4. Floating charge holders.

Choose the **correct answer**:

1. Order (i), (ii), (iii) and (iv).
2. Order (iii), (iv), (i) and (ii).
3. Order (iii), (i), (iv) and (ii).
4. Order (i), (iii), (iv) and (ii).

**Question 1.4**

**Who may appoint** a provisional liquidator over a Bermuda company?

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

**Question 1.5**

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 1.6**

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.
2. One 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 1.7**

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 1.8**

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

1. Two years.
2. One month.
3. Twelve months.
4. Six months.

**Question 1.9**

**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 1.10**

Summary proceedings against a company’s directors for **breach of duty** (or misfeasance) may be brought by a liquidator under the following provision of the Companies Act 1981:

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 2 (direct questions) [10 marks in total]**

**Question 2.1 [maximum 2 marks]**

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

Set-off is governed by section 37 of the Bankruptcy Act 1989. It can be exercised after the start of a liquidation if:

* The debts that are to be set off were incurred before the start of the liquidation and are monetary payment liabilities;
* The transactions relating to the incurring of the debts were not fraudulent preferences or fraudulent conveyances; or
* The dealings between the parties were mutual.

**Question 2.2 [maximum 4 marks]**

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

Security can be taken over assets under Bermuda law in various ways. The nature of security interest will depend on (1) the agreement between the parties as set out in applicable security document; (2) what type of assets are being used as security and being secure and (3) the type of interest the debtor as in the assets being secured.

Possible ways include but are not limited to:

1. Legal mortgage – the legal title of the property of the debtor is transferred to the creditor as security; in this case, the debtor retains possession of the property and can regain legal title once the applicable debt has been repaid
2. A pledge – in this case the creditor takes delivery or possession (actual or constructive) of the debtors and retains this until the debt has been settled or discharged;
3. Equitable mortgage – here the debtor retains legal title and possession of the asset but the beneficial interest is transferred to the creditor. Should a 3rd party acquire legal title to the property in good faith, the equitable mortgage does not take priority to the new owner.

**Question 2.3 [maximum 4 marks]**

In what circumstances may be a provisional liquidator be appointed?

The courts of Bermuda are granted the power to appoint liquidators under section 170 of the Companies Act. This includes the ability to appoint provisional liquidators to oversee restructuring purposes. The petition to appoint the provisional liquidator can be made by various interested parties in the company including creditors, shareholders, directors etc.

The appointment of the provisional liquidator adjourns the hearing of the winding up petition and provides an automatic stay of legal proceedings against the company. This provides the company the ability to continue trading and allows the directors and provisional liquidators the formulate and implement the restructuring plan. If the restructuring is implemented successfully, the winding up petition will be dismissed. If not, the hearing can be restored and the company may be wound up.

Provisional liquidators may be appointed by the courts under the following circumstances:

* Where the court is satisfied that a plausible and viable rescue plan is achievable and that, where a scheme will be necessary to implement it, a sufficient majority of creditors are likely to vote in favour of it.
* Between the presentation of a winding-up petition and its final hearing if it is appropriate and in the best interest of the creditors. Circumstances such as if there is a potential risk of company assets being dissipated.
* Where the company is in the process of an informal restructuring and there is a potential risk of certain creditors wanting to enforce their debt through legal proceedings, the appointment of the provisional liquidator will protect the process of restructuring
* Where the company applies for provisional liquidation and the appointment of a provisional liquidator to allow for the implementation of a scheme of arrangement

**QUESTION 3 (essay-type question) [15 marks]**

**Question 3.1 [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.

In Bermuda, an order or judgement made by a foreign court has no legal impact and is not automatically enforceable in Bermuda. For the judgement to be enforceable in Bermuda, a number of steps need to be taken.

The judgement would need to meet various statutory or common law rules to be recognised or enforced. The applicable rules will depend on the nature of the judgement seeking recognition and the place where the foreign judgement was made.

These rules include (but are not limited to):

* The statutory rules applicable to the registration and enforcement of final money judgements of the superior courts in the UK and certain Commonwealth countries under the Judgements (Reciprocal Enforcement) Act 1958 (the 1958 Act”);
* The common law rules applicable to the enforcement of final money judgements of foreign courts in the rest of the world;
* Statutory and common law rules which apply to the recognition of foreign judgements either as a defence to a claim or as conclusive of an in issue in the Bermuda proceedings.

The courts of Bermuda will recognise and enforce a foreign money judgement which falls within the scope of the 1958 Act or a common law rule which allows the recognition and enforcement. The 1958 Act details a procedure which allows for the registration and enforcement of a judgement rendered in the superior courts of the UK to be given effect upon its registration as though the judgement was made by a Bermuda court. The 1958 Act may also be applied to judgements made in various Commonwealth countries as detailed.

As relates foreign court-sanctioned scheme of arrangement, this would be a money judgement and would need to be registered under the applicable statutory or common law rules in Bermuda to allow enforcement in Bermuda.

There are numerous circumstances which could result in a foreign court judgement **not** being registered or enforced in Bermuda. If a judgement is registered under the 1958 Act, any party against whom the judgment may be enforced may apply to the courts to have it set aside. The Supreme Court must set the judgment aside if it has been satisfied that:

* It does not fall within the ambit of the 1958 Act or was registered in contravention of the 1958 Act;
* The foreign court did not have the jurisdiction in the circumstances of the case;
* The defendant did not receive notice of the proceedings underway in the foreign jurisdiction in tie to allow defence against the proceedings and did not appear;
* The judgement was obtained fraudulently;
* The rights under the judgement are not vested in the person by whom he application for registration made;
* If the foreign judgement conflicts with another prior and inconsistent judgement from another court with competent jurisdiction;
* If the judgement is not final and conclusive;
* If the judgement was obtained in a court of law which did not have jurisdiction of the judgement debtor;
* The judgement relates to taxes, fines or penalties;
* The judgement would contravene Bermuda’s public policy or
* Rules of natural justice were not observed in the foreign proceedings.

To ensure that foreign court judgements are registered and enforced, the applicants must ensure that all rules are followed.

**Question 3.2 [maximum 8 marks]**

Write a brief essay on the basis upon which foreign liquidators are granted recognition and assistance in Bermuda. Also consider the circumstances in which foreign liquidators might not be granted recognition and assistance.

Bermuda has no statutory provisions around the granting of recognition and assistance of foreign corporate liquidators in Bermuda. Under common law, the Supreme Court of Bermuda could recognise foreign corporate liquidators who have been appointed in the company’s domicile and also the impact of any winding up orders made by the relevant court. The Bermuda courts do usually recognise the foreign liquidators.

The Bermuda courts also have discretion to assist the main liquidation court by doing what it could have done if the case was a domestic insolvency. The extent and scope of the common law powers of the Bermudian Courts’ assistance to foreign liquidators has been debated extensively in recent court judgements in Bermuda. Two judgments by the Privy Council have provided some guidance. These cases are *Singularis Holdings Limited v PricewaterhouseCoopers* and *PricewaterhouseCoopers v Saad Investments Company Limited*.

Subject to the facts relating to the case before the courts, the Bermuda Court will likely recognise the winding-up order of foreign courts and assist foreign liquidators as far as is practicable in the following circumstances:

* There is “sufficient connection” between the jurisdiction of the foreign court and the foreign company making it the most appropriate, or the “most convenient” jurisdiction made the order for the winding up of the company and the appointment if the foreign liquidators;
* The foreign company has documents, assets or liabilities within the jurisdiction of Bermuda, or the foreign entity has conducted business within or from the jurisdiction of Bermuda (directly or indirectly through agents or by branches), or the foreign company has former directors, officers, managers agents or service providers within Bermuda, and/or the foreign entity properly need to be involved in litigation or arbitration within Bermuda, and
* There is no public policy reason under Bermudian Law to the contrary.

It is noted that the Court does not have the powers to assist foreign liquidators in doing something that they could not do under the law of the country in which they were appointed and the Court’s exercise of power must be in line with public policy and substantive law of the assisting court in Bermuda,

There may circumstances under which the foreign liquidator may not be given recognition and/or assistance by the Bermuda Court.

These may include:

* Where no active assistance has been requested by the foreign liquidator;
* If there is pending litigation in the country in which the foreign liquidator has been appointed;
* Where there are other mechanisms available to the foreign liquidator that does not require the recognition of the foreign liquidator
* If it would be against public policy to do so.

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

Mudatea Limited (the Company) was incorporated in 2020 as an exempt Bermuda company; as the parent company in a group of companies with a direct subsidiary incorporated in the British Virgin Islands; with indirect trading subsidiaries incorporated in the People’s Republic of China (PRC); and with offices and a substantial business presence in Hong Kong. The Company’s trading operations in the PRC involves tea shops and other retail businesses associated with tea and hot drinks.

The Company issued a number of bonds to creditors based in the United States (US) with the face value of USD 500 million, with a view to raising additional capital (by way of debt funding) to fund the expansion of its business activities in the PRC (which had previously been funded with the benefit of shareholders’ capital contributions).

It was subsequently disclosed that the Company had fraudulently misrepresented its financial performance in the offering documents associated with the bonds, with the consequence that the US bondholders were entitled to demand immediate repayment by the Company of the sum of USD 500 million, even though that money had already been transferred to the Company’s indirect subsidiaries in the PRC, and was incapable of being returned due to local currency control restrictions and associated Chinese legal issues.

The US bondholders served a statutory demand on the Company in Bermuda, demanding repayment of the sum of USD 500 million within 21 days.

The Company’s directors decided, however, that it was in the best interests of Mudatea Limited and its shareholders to not satisfy the statutory demand but to ignore it for the time being, having regard also to the Chinese legal position, and with a view to trading through the Company’s financial difficulties.

The Company’s directors subsequently borrowed an additional USD 50 million from its bank, Berbank, which loan is secured by way of a floating charge against all of the Company’s shares and the assets of its subsidiaries. Out of the USD 50 million received from Berbank, Mudatea Limited’s directors immediately paid themselves a bonus of USD 20 million and they also paid a dividend to the Company’s shareholders in the sum of USD 30 million.

The US bondholders only found out about these transactions two weeks later, through a report received from a disgruntled former employee of Mudatea Limited.

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

**Question 4.1 [maximum 7 marks]**

What actions could the US bondholders take in order to try to recover some or all of the sum of USD 500 million from the Company or other parties? Please consider (a) the jurisdictions in which they could take such action, bearing in mind the potential need for enforcement; (b) the defendants against whom they 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.

In the above case, the US bondholders are creditors to the Bermuda registered exempt company. As creditors of the Company, the bondholders are able to apply to the Supreme Court of Bermuda for the compulsory liquidation of Mudatea Limited. Under section 161 of the Companies Act 1981, the court may wind up the Company if it is unable to pay its debt (pursuant to section 162). A compulsory liquidation will give the creditors the opportunity to have a court supervised process undertaken, it provides a compulsory moratorium of actions against the Company (potentially there are other creditors who may perfect security or pursue amounts due) and also allows for the review and setting aside of certain transactions.

What is evident from the above set of facts is that the directors of Mudatea have not acted in the best interests of the Company and given that the company has financial constraints, the directors should also have been cognisant of their duty to act in the best interests of creditors.

It would be prudent for the bond holders to commence simultaneous liquidation applications in the USA, PRC and Bermuda. The action in the USA is because of the creditors being located in this jurisdiction and potentially having the bonds covered by USA law (unclear from the facts); as the funds were deployed to operations conducted by a legal entity in PRC, it would be important to commence proceedings there as this is potentially where significant assets are located that could be attached and used as settlement of debts and proceedings in Bermuda are required as this is where the entity which raised the funds is domiciled and where the directors are potentially located.

In the above case, the bondholders would be able to institute action against Mudatea as the borrowing entity as well as the directors of Mudatea. The directors can be held personally liable in this case under the following provisions of the Companies Act 1981:

* *Fraudulent trading* – under section 246, if a director knowingly caused or allowed the company to carry on business with the intent to defraud creditors may be found personally liable for any or all of the debt or other liability as decided by the court. Should the directors allow the business to continue trading while knowingly insolvent, this would also be considered fraudulent trading. The above facts state that the offering documents contained fraudulent financial information. The directors of Mudatea committed fraud by publishing false information and also continue to allow the business to trade despite the cleat financial constraints. The bondholders can institute legal action against the directors in their personal capacity in order to recover some of the funds.
* *Breach of fiduciary duty and failure to exercise reasonable skill and care* – under section 97 and common law, directors owe a duty of care and to act honestly and in the interest of the company (and creditors where the company is or may become insolvent). Directors who fail to comply with these obligations, may be held personally liable for losses incurred by affected stakeholders. The bond holders again can institute legal action against the directors for the losses incurred.
* *Unlawful return of capital* – section 54 of the Companies Act states that a company shall not declare or pay a dividend if there are reasonable grounds to believe that the company is or will be unable to pay its debts as they become due (cash flow insolvent) or the value of the liabilities will exceed the net realisable of the assets (balance sheet insolvent). Again the bondholders can pursue action against the directors for the declaration and payment of the dividends while knowling that the business was unable to settle its debts.
* The above actions against the directors can be pursued by the bond holders outside of formal insolvency proceedings.

Given that their may be other creditors owed funds (including Berbank), it would be prudent for the bondholders to apply for a provisional winding up of Mudatea. This will provide a moratorium on further legal action by other creditors and stakeholders. It also allows the bondholders to potentially control the liquidation by appointing the provisional liquidator of their choice under the supervision of the courts. This is a useful mechanism in a cross border case such as Mudatea.

Should the bondholders look at litigation, they would lose control of the process and allow for other parties to potentially apply for a provisional or compulsory liquidation. Litigation is a costly and drawn out process which may result in the final liquidation of the company with little or no recovery of the amounts owed.

Also, within a Court sanctioned liquidation, the floating charge created by the directors would be a reviewable transaction under section 239 of the Companies Act as it would have been created within 12 months of the winding up order. The entire transction would be deemed invalid and the foating charge would be cancelled.

**Question 4.2 [maximum 8 marks]**

To what extent would it be open to Mudatea Limited to try to take steps to restructure its debt obligations, and how and where could 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, (that is, if the US bondholders would be issued new shares in the Company in exchange for cancellation of their debt, with existing shareholders’ shares in the Company being cancelled).

It would be a possibility for Mudatea to restructure its current debt obligations. The most prudent way of doing this would by way of a scheme of arrangement. A scheme of arrangement is a formal procedure that can be used to restructure a business while it continues to trade and is the only formal rescue procedure set out in the Companies Act.

In this case, the directors of Mudatea could place the company into a voluntary liquidation and have the Courts appoint a provisional liquidator that could oversee the implementation of the scheme of arrangement under the sanction of the Court. The provisional liquidation provides some protection against litigation from other creditors and impacted stakeholders and also allows for the management to direct the operations.

Given that there are likely to be creditors of the greater business in both Hong Kong and Bermuda, the provisional liquidation and scheme of arrangement should be petitioned for in Bermuda on a primary basis with an application to be made in Hong Kong for recognition of the Bermuda proceedings. This is a more cost effective process than running parallel proceedings in both jurisdictions.

The scheme of arrangement requires the support of 75% of the class of creditor being impacted. Should there be other creditors that make up a value of debt that results in less than 75% being in favour of the scheme, the court would not be able to sanction the arrangement.

However, if the scheme related only to the restructure of the debt relating to the bonds in the “debt for equity” swap and all bond holders agree, the scheme is likely to be approved by the Court. In this case there would be no need for applications to be made in Hong Kong. It would be prudent to apply for recognition of the scheme under US laws as the bonds may be issued under US laws as they were issued to US holders.

**\* End of Assessment \***