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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**.

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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?

Yes, the Grand Court of the Cayman Islands (the **GC**) does have the power to assist foreign bankruptcy proceedings.

The source of that power is derived from Part XVII of the Cayman Islands' Companies Act (2023 Revision) (the **CA**) which relates to international co-operation.

Pursuant to section 241 of the CA, the GC may upon the application of a foreign representative make orders ancillary to a foreign bankruptcy proceeding for the purposes of:

1. *recognising the right of a foreign representative to act in the Islands on behalf of or in the name of a debtor;*
2. *enjoining the commencement or staying the continuation of legal proceedings against a debtor;*
3. *staying the enforcement of any judgment against a debtor;*
4. *requiring a person in possession of information relating to the business or affairs of a debtor to be examined by and produce documents to its foreign representative; and*
5. *ordering the turnover to a foreign representative of any property belonging to a debtor.[[1]](#footnote-1)*

It is worth noting that the Cayman Islands has not implemented the UNCITRAL Model Law on Cross-Border Insolvency, nor is it a member of the European Union despite being a British Overseas Territory.

Ultimately the Grand Court has discretion to grant relief sought in a foreign representative’s application and make ancillary orders if it is satisfied that it is appropriate to do so, and in doing so it required to take into account the criteria in section 242 of the CA (which are designed to assure an economic and expeditious administration of the debtor’s estate):

1. *the just treatment of all holders of claims against or interests in a debtor’s estate wherever they may be domiciled;*
2. *the protection of claim holders in the Islands against prejudice and inconvenience in the processing of claims in the foreign bankruptcy proceeding;*
3. *the prevention of preferential or fraudulent dispositions of property comprised in the debtor’s estate;*
4. *the distribution of the debtor’s estate amongst creditors substantially in accordance with the order prescribed by Part V;*
5. *the recognition and enforcement of security interests created by the debtor;*
6. *the non-enforcement of foreign taxes, fines and penalties; and*
7. *comity.[[2]](#footnote-2)*

If the debtor is a foreign company which is registered under part IX of the CA (being an overseas company that does business in the Cayman Islands)[[3]](#footnote-3) then the Court cannot make an ancillary order under section 241 without also considering whether it should make a winding up order under Part V of the CA in respect of that foreign company's local branch.[[4]](#footnote-4)

**Question 2.2 [maximum 3 marks]**

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

In circumstances where the Cayman Islands (i) has not entered into any international treaties for the reciprocal recognition or enforcement of foreign judgments; (ii) is not a signatory to the Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters and (iii) The Foreign Judgments Reciprocal Enforcement Act (1996 Revision) (the **1996 Act**) currently has limited application because it only applies to judgments from the Superior Courts of Australia, the enforcement of foreign judgments is typically achieved by way of the common law and by commencing new proceedings in the Cayman Islands based upon the foreign judgment as an unsatisfied debt or other obligation.[[5]](#footnote-5) Both money and non-monetary foreign judgments are enforceable at common law.[[6]](#footnote-6)

The Grand Court Act (2015 Revision) and specifically the Grand Court Rules (2023 Revision) (the **GCR**) regulate the procedure for such proceedings in the Cayman Islands. In addition, order 45 of the GCR sets out the rules that apply to the enforcement of judgments and orders in general.

There are some mandatory requirements that must be met in order to enforce a foreign judgment at common law in the Cayman Islands, including that the

1. *judgment is final;*
2. *foreign court had jurisdiction over the debtor;*
3. *foreign judgment was not obtained by fraud;*
4. *foreign judgment is not contrary to public policy of the Cayman Islands; and*
5. *foreign judgment was not obtained contrary to the rules of natural justice.*[[7]](#footnote-7)

Once a foreign judgment has been recognised under either the 1996 Act or pursuant to the common law by way of a new proceeding, there is a six-year period within which the judgment can be enforced and that time starts to run from the date of the judgment or, when there have been appeals, the date of the last judgment.[[8]](#footnote-8)

**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?

It is possible for a creditor to register a mortgage or charge over real estate, ships, aircraft, motor vehicles and intellectual property on the specific ownership registers that exist in the Cayman Islands for these kinds of assets. The effect of registration means that any third-party purchaser of the asset will be deemed to have notice of the security interest and will acquire the asset subject to the secured creditor's interest in the asset.[[9]](#footnote-9) In a liquidation scenario, registration gives the secured and registered creditor priority over non-registered creditors.

There is no security registration regime in the Cayman Islands for other types of assets outside of those mentioned above. In those circumstances, it is up to the creditor to take steps to investigate whether a particular asset is already encumbered.

With respect to companies, section 54 of the CA requires that security interests are entered in the register of mortgages and charges of the debtor company and that such register must be maintained by the company at its registered office in the Cayman Islands. The reality is that not all companies comply with this obligation and any failure of a company to update the register of mortgages and charges does not, in and of itself, invalidate any security interests that are not recorded.[[10]](#footnote-10)

In addition, there is no statutory regime in the Cayman Islands that requires perfection of security interests. As such, as long as the security interest that is granted in the relevant contract is valid, and not voidable for any other reason, it will be enforceable.[[11]](#footnote-11) Being a secured creditor in a liquidation context has the benefit that their claims will rank in priority to all other creditors and they can realise their security outside of the liquidation / restructuring process as they see fit. The only exception is that preferred creditors (for example, employees, the Cayman Islands Government with respect to taxes and banks) rank ahead of secured creditors where the secured creditor’s security is in the form of a floating charge.

This means that secured creditors can proceed with any enforcement actions against the secured asset as soon as there is event of default. The commencement of liquidation proceedings in the Cayman Islands does not place any stay on the action of secured creditors.

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

**Question 3.1 [maximum 6 marks]**

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

The suggestion that receivers have no role to play in a Cayman Islands insolvency scenario is false, on the contrary receivers play a range of roles following private and Court appointments including with respect to segregated portfolio companies (**SPCs**). This short essay discusses examples of the more specific roles that receivers can play in each of these contexts.

With respect to private receivership, a secured creditor may appoint a receiver pursuant to their contractual rights in the relevant security documentation and typically the receiver's role is to take custody and control of, collect income from, and (if necessary) sell, the asset over which the secured creditor has taken security. In a scenario where a Cayman Islands based debtor becomes insolvent and defaults on their payment obligations, a secured creditor's privately appointed receiver may take steps to realise the debt that they are owed (outside of any formal liquidation with respect to the debtor) with respect to the specific assets over which their receivership relates. This can involve selling the secured assets and taking all steps to ensure that the best price is obtained.

With respect to real estate, a secured creditor has a statutory right under sections 72 and 73 of the Registered Land Act (2018 Revision) to appoint a receiver in relation to their secured interest in the property.

Turning to court-appointed receiverships, the GC has the power to appoint a receiver *“in all cases in which it appears to the Court to be just and convenient to do so”*. The source of this power is section 11(1) of the Grand Court Act, which states that the Grand Court shall possess like jurisdiction within the Cayman Islands which is vested in England and in England, section 37(1) of the Senior Courts Act 1981 states that the High Court may appoint a receiver in all cases in which it appears just and convenient to do so.[[12]](#footnote-12) When a receiver is appointed the Court will describe the powers that they have in the order that appoints them, as such, it is important for the applicant to have a clear understanding of what the receiver will be required to do so that can be encompassed by the summons the order.

Although it's certainly not the only use, a common application for the appointment of receivers in the Cayman Islands, arises in an insolvency context of a freezing injunction to preserve assets which are at risk of dissipation and receivers are appointed to take control of those assets and preserve them pending resolution of the insolvency proceedings. Receivers can also be used where a monetary judgment has been issued and steps are being taken to enforce it, however, in this scenario the Court will consider whether the cost of doing so is proportionate in keeping with the amount of the judgment.[[13]](#footnote-13) In this situation, the receiver is appointed and takes possession of the judgment debtor’s property and sells it to satisfy the judgment.

In the insolvency context, commonly the receivers that are appointed are professional insolvency practitioners. The receiver's remuneration will be authorised by the Court, much like it is for official liquidators, and in fact the Court will have regard to the Insolvency Practitioners’ Regulations as to what is appropriate as was the case in *Lea Lilly Perry v Lopag Trust Reg* (Grand Court, 20 April 2020, Unreported).

The GC also has the power to appoint receivers in respect of an SPC and the process is regulated by the CA in relation to particular kinds of SPCs. Such an application may be made by the SPC itself, its directors, a creditor or shareholder of the SPC or whether the SPC is licensed and regulated, the Cayman Islands Monetary Authority (**CIMA**).[[14]](#footnote-14) Pursuant to the CA, the Court may make a receivership order if it is satisfied that (a) the SPC’s assets are or are likely to be insufficient to discharge the claims of the SPC’s creditors;[[15]](#footnote-15) and the making of a receivership order would achieve the orderly closing down of the SPC’s business and the distribution of the SPC’s assets to the persons so entitled.[[16]](#footnote-16)

The appointment of receivers in respect of an SPC is particularly important in an insolvency scenario because while an SPC can be wound up in accordance with the general winding up process set out in the CA, the official liquidator of an SPC may only deal with the SPC’s assets in a manner that is consistent with the structure of the segregated portfolio. In other words, the liquidator can only deal with the assets and liabilities of each portfolio within the SPC as each is established and ring-fenced by statute. The liquidator can't deal with the SPC and all of its portfolios as a whole, the ring fencing must be respected. In this scenario, receivers may be a useful tool and the statute sets out a process for this. In particular, if the GC is satisfied that the SPC’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.[[17]](#footnote-17) This role essentially fulfils that of a liquidator.

The GC has considered the question of when a SPC’s assets are or are likely to be insufficient to discharge the claims of the SPC’s creditors in *In re Obelisk Global Fund SPC* (Grand Court, 12 August 2021, Unreported) (***Obelisk***) and *In re Green Asia Restructure Fund SPC* (Grand Court, 3 August 2022, Unreported) and determined that it requires the use of a flexible balance sheet test. In *Obelisk*, the GC said that the Court must make *“a determination on the available evidence of whether the assets are sufficient now, or are likely to be in the reasonably near future, when assessed against its liabilities (as well as its prospective and contingent liabilities), and are held in a form where they may be used to pay the claims of creditors”.* The GC rejected a contention that section 224(1)(a) created a cashflow insolvency test as used for winding up companies.

If an application for a receivership order is made with respect to a SPC, there is a stay on proceedings against the SPC in relation to the segregated portfolio that the receivership order applies to. The only exception is if leave of the Court is granted.[[18]](#footnote-18) The Court will discharge the receivership order once its purposes have been achieved or become incapable of being achieved.[[19]](#footnote-19) Similarly, a receivership order will cease to have effect if a winding up order is made in respect of the SPC.[[20]](#footnote-20)

As is demonstrated by the above examples, receivers have varied and important roles to play in an insolvency scenario in the Cayman Islands. Parties and the Courts have a wide discretion as to their use and the CA solidifies their importance with respect to SPCs.

**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.

Although the CA does contain a statutory prohibition on insolvent trading, there are ways for Court appointed liquidators of an insolvent company, or creditors of an insolvent company, to hold its former directors accountable and / or by seeking to “claw-back” any payments that those directors should not have made. The main avenues to achieve this in the Cayman Islands are summarised below.

Breach of fiduciary duty

Directors have a fiduciary duty to act in the best interests of the company. If a director is found to have breached their fiduciary duty to act in the best interests of the company, then they can be made personally liable for any losses which they have caused. If a company is in official liquidation and liquidators have been appointed, then those liquidators could bring a claim for breach of fiduciary duty in the name of the insolvent company if they consider that the directors haven’t acted in the best interests of the company by making payments during the period that the company has been insolvent. When considering whether to bring the claim, the liquidators will need to assess the value of the payments that have been made against the potential cost of the litigation to assess whether it should be brought and has the potential to allow for greater returns to the company's creditors.

The GC held in the case *Prospect Properties v McNeill* [1990-91 CILR 171] that where a company is insolvent, a directors’ duty to act in the best interests of the company extends to requiring them to have regard to the interests of its creditors and it is clearly in interest of creditors to be paid. The recent UK Supreme Court decision in *BTI v Sequana* [2022] UKSC 25 also relates to the question of when directors are required to consider the interests of creditors in an insolvency context and in circumstances where Cayman follows English law, this case will also be of relevance in the Cayman Islands.

Winding-up proceedings

A creditor of an insolvent company can petition the GC to wind the company up on the grounds that it is insolvent. Section 92 of the CA sets out the groups upon which a company may be wound up and one of those reasons includes that the company is unable to pay its debts.[[21]](#footnote-21) A company will be deemed unable to pay its debts as per section 93 of the CA if:

*"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 (and the debt is not disputed on substantial grounds);*

*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."*[[22]](#footnote-22)

Once winding-up proceedings are on foot, there are further tools that are available with respect to payments / property dispositions that have been made.

*Avoidance of property dispositions*

In particular, liquidators or creditors may utilise section 99 of the CA. Section 99 states that any dispositions of a company’s property made after the deemed commencement of the winding-up (the date on which the winding-up petition was filed) will be void if a winding-up order is subsequently made, unless those dispositions are validated by the Grand Court. Validation applications are not uncommon, and can relate to past transactions or future transactions, but they require evidence and can be challenged. If a company is insolvent, the Court is unlikely to grant the validation orders sought unless it can be shown that the disposition has a corresponding benefit to the company and enhances the value for creditors as a whole.[[23]](#footnote-23)

If no petition has been filed yet, the relevant transactions are not caught by section 99, however, there are other claw-back mechanisms that are available, and these are explained below.

*Voidable preferences*

Section 145 of the CA sets out the circumstances in which a payment or disposal of property to a creditor constitutes a voidable preference, specifically 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
2. the dominant intention of the company’s directors was to give the applicable creditor apreference over other creditors.

The test to determine whether there has been a voidable preference under s 145(1) of the CA was considered by the Cayman Islands Court of Appeal and Judicial Committee of the Privy Council (the **PC**) in *re Weavering Macro Fixed Income Fund Ltd (in Liquidation)*.[[24]](#footnote-24) The PC held that giving a preference over other creditors means putting that creditor in a better position than it otherwise would have been. It is important that in order for the payment to be a voidable preference, the company’s dominant intention in making the payment or granting the security was to achieve a different purpose (for example, a good faith payment to an essential service provider) then it might not be classed as a voidable transaction. It is also possible that a payment to a related party of the company will be deemed to have been made with a view to giving a preference. The Court will assess and infer the company's dominant intention in payment the payment from the available evidence.[[25]](#footnote-25)

*Avoidance of dispositions made at an undervalue*

Similar to section 145, section 146 of the CA 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 (i.e. an intent to defraud) is voidable on application of the liquidator. As such, the official liquidators of an insolvent company will consider if there has been any property which have been disposed of for either no consideration or consideration which is significantly less than the value of the property and if there is evidence that the relevant disposition has been made with an intent to defraud, then they will apply to the Court to have that disposition set aside. In this scenario it is up to the liquidator to prove that the debtor held the relevant intention to defraud.

*Fraudulent trading*

On the topic of fraudulent activities, section 147 of the CA provides another protection for creditors in that if any business of a company as carried on with an intent to defraud creditors or for any fraudulent purpose, then a liquidator has recourse and can apply to the Court for an order requiring any persons who were knowingly parties to that fraudulent activity to make contributions to the company's assets.[[26]](#footnote-26) This is important because the greater the company's assets the greater the return to creditors will be when it finally comes time for distribution in accordance with the order of priorities set by section 140 of the CA.

*Restructure*

There is one further scenario that is worth mentioning where an official liquidator may be in a position to claw-back any preference payments made to creditors and that is in the context of a restructure. Where a restructuring officer has been appointed, but the restructure is unsuccessful and the company is subsequently wound up, the official liquidator will be able to claw back any preferences that are deemed to have been made within the six months immediately preceding the presentation of the Restructuring Petition.[[27]](#footnote-27)

As it can be seen, although the Cayman Islands' CA does not in and of itself prohibit insolvent trading (a stark difference to other countries), the recourse that is available to creditors / liquidators in their efforts to realise assets for creditors are quite far reaching and the Court has a lot of flexibility to deal with differing scenarios.

**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 lent Punk Lizard (**PL**) USD 900 million. Half of that amount, USD 450 million, is secured by a mortgage over half of PL's boats. We understand that the remaining $450 million is unsecured. PL has fallen behind on its monthly repayments to TNB constituting a default. In the circumstances and as a secured creditor with a mortgage over half of PL's boats, TNB could take possession of those boats and exercise its power of sale with respect to the property to satisfy its debt, or alternatively appoint a receiver to realise the property.

Assuming that PL continues to be unable to make the repayments on the loan, TNB's most powerful tool with respect to the unsecured amount would be to apply to wind up PL on the basis that it is unable to pay its debts. The first step for TNB would be to issue a statutory demand for the outstanding amounts and if PL does not pay for 21 days, that is grounds to issue a creditor's winding up petition seeking a winding up order on the basis that PL is unable to pay its debts.

In order to succeed on the petition, TNB would need to prove that PL is insolvent. The normal test is whether PL can pay its debts and the fact of the unsatisfied statutory demand would indicate that it cannot. The outstanding ICC award would also be evidence that PL cannot pay its debts, particularly if that award has been recognised in the Cayman Islands (see below). However, it is noteworthy that the market for PL's activities remains strong and it has a reasonably positive financial future. The common law in the Cayman Islands suggests that future cash flow can be considered when determining whether a company can pay its debts. As such, if PL can demonstrate that it will be able to satisfy the outstanding amounts based on future expected cash flows, then the Cayman Court may not be satisfied that it is insolvent. Other major factors that would support TNB's case would be the fact that its fleet is reduced following the sale of any boats to satisfy the secured portion of the debt, the bad media and the safety concerns which exist. We are also told that PL cannot currently afford to pay the ongoing costs associated with maintaining its fleet (electricity, maintenance, insurance, staff costs, rum etcetera).

A challenge for TNB in respect of the unsecured portion of its loan is that if there are any other creditors of PL, and we know that at least H&W has an unsatisfied debt and there are likely others given that it hasn’t been paying electricity, maintenance, insurance, staff costs, rum etc, then those creditors would also be entitled to share in any funds that are realised in the liquidation and TNB would be paid in accordance with the order of priorities and on a *parri passu* basis. Given that there are sums owed to employees, those sums would be considered preferential debts under s 141 of the CA and they would be paid out first before the remaining unsecured debts.

The upshot of all of this is that TNB is unlikely to recover all of the $450 million that is unsecured, however, it is will be able to recover the secured $450 million and do so outside of any liquidation as long as the secured assets are sufficient to satisfy this amount (or the amount of the debt).

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

In circumstances where H&W has a foreign judgment from the ICC in London for PL to pay it USD $150 million dollars, H&W's priority will be to enforce that judgment against PL in the Cayman Islands where PL is registered.

H&W's first step would likely be to write to PL to seek payment of the ICC award, however, given PL's bad financial circumstances and the fact that it has fallen behind on its loan payments to TNB, this seems highly unlikely to eventuate.

In circumstances where the judgment is made by the ICC in London, it will not be recognised under the Foreign Judgments Reciprocal Enforcement Act (1996 Revision) which currently only applies to judgments from the superior Courts of Australia.

In addition, 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 which it has the power to do in circumstances where the Cayman Islands is a British Overseas Territory.

As such, in order for H&W to enforce its judgment, its best option is to commence a new action in the Cayman Islands based on the ICC's judgment as an unsatisfied debt in accordance with the common law. In order to satisfy the Cayman Islands Court that the ICC's award can be enforced in Cayman at common law, H&W will need to prove that (i) the ICC's award is final (i.e., it can't be appealed), (ii) the ICC had jurisdiction over PL, (iii) the ICC award was not obtained by fraud; (iv) the ICC award is not contrary to public policy of the Cayman Islands; and (v) the ICC award was not obtained contrary to the rules of natural justice.

In order to properly advise on the above, the Cayman Islands-based insolvency professional would likely need legal advice. In particular, there is a question regarding whether the ICC had jurisdiction over PL considering that it is a Cayman registered company. It may be that H&W is a UK company and this is the reason that the ICC felt it had jurisdiction to determine a dispute regarding PLs failure to pay for the new dive boats, however, more information is required to make a proper assessment. There are no indications that the other mandatory criteria wouldn’t be met.

If H&W is able to get the ICC's award recognised in the Cayman Islands under the common law and a local judgment is issued against PL, then H&W may start taking advantage of the full range of domestic enforcement remedies. For example, H&W may issue a statutory demand and upon non-payment commence winding up proceedings on the basis that PL is unable to pay its debts. Or it may seek to appoint receivers or provisional liquidators over PL to ensure that its assets are protected pending such a liquidation. It may also apply to appoint receivers in aid of the enforcement which would entail receivers taking possession of PL's property and selling it to satisfy the $150 million dollar judgment.

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

As mentioned above, any amounts owed by PL to its employees would be treated as preferred debts in a liquidation context. This means that aside from any liquidation expenses which can include the petitioner's cost, the costs of any restructuring officer and the official liquidator's fees and expenses, any amounts owed to PL's employees would be paid out as preferential debts pursuant to section 141 of the Companies Act. The statute thereby provides additional protection to employees meaning that they would be paid out ahead of other unsecured creditors such as TNB (with respect to the $450 million) and H&W.

However, we know that PL is a family owned and operated business having been founded by the Kraken family over 70 years ago and the family members continue to own and manage the business. If the unpaid employees as are family members, they will likely have an interest in seeing PL continue to operate as opposed to being would up. In those circumstances, in their position as PL's owners they may take steps to restructure PL's debts. This could include taking steps informally out of Court through an informal creditor workout or potentially by way of a more formal process such as via the new restructuring officer regime and/or a scheme of arrangement. It's worth mentioning that provisional liquidation can also be used to achieve restricting goals depending on the circumstances.

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

The Cayman Islands Court does have jurisdiction over PL because it is registered in the Cayman Islands. We aren’t told where it is incorporated, but even if it is incorporated elsewhere, by the fact that it is registered in Cayman it falls within the Cayman Court's jurisdiction.[[28]](#footnote-28) Even if it wasn’t registered in the Cayman Islands and is a foreign company, the fact that it has property on the Cayman Islands and is carrying on a business in the Cayman Islands means that it falls within the Cayman Islands' Court's jurisdiction.[[29]](#footnote-29)

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

PL may seek to protect itself by taking advantage of the legal route that is available under sections 91A to 91J of the CA and the Companies Winding Up Rules (as revised) (the **CWR**) and petition the Court to appoint a restructuring officer (the **RO Regime**).

This is a relatively new regime which was only introduced in 2022 and provides another option to a company who wishes to restructure instead of provisional liquidation.

Upon filing of the restructuring petition, an automatic stay preventing the commencement of any other proceedings against PL (without the leave of the Court) will come into effect. This is a powerful tool for PL because it could prevent the commencement of liquidation proceedings by any of the known creditors mentioned above unless the Court grants leave.

Pursuant to section 91B(1) of the Companies Act, PL would be entitled to present a petition seeking the appointment of a restructuring officer on the grounds that it is (a) is or is likely to become unable to pay its debts, or (b) intends to present a compromise or arrangement to its creditors (Restructuring Petition).

On the basis that PL has already fallen behind on its payments to TNB it seems that it would easily meet the requirements of (a). In addition, if it has formulated a new plan that it wishes to present to its creditors which provides a compromise or a new arrangement for its creditors then it may satisfy (b). A benefit of the RO Regime is that PL can present a compromise or a scheme or arrangement to its creditors within the content of the Restructuring Petition. In essence a scheme or arrangement is intended to revitalise and restructure a company at a time of financial distress.

If PL intends to present a compromise or arrangement to its creditors by way of a Restructuring Petition, then such an application must be supported by:

(a) an affidavit sworn by or on the authority of PL board of directors containing, amongst other things:

(i) a statement that, having made due enquiries and taken appropriate advice, the board believes that PL is or is likely to become unable to pay its debts (and the reason for the stated belief). This would likely encompass an explanation of the safety issues, the drop in business, the default on the bank loans and the money owed to H&W.

(ii) a statement of PL's financial position specifying details regarding PL's assets and liabilities (including contingent and prospective liabilities) and an explanation of how the company will be funded in the event and during the restructuring period; and

(iii) a statement of why the directors believe that the appointment of a restructuring officer and the mortarium will be in the bests interest of the company and if relevant, its creditors. This may include an explanation that it will allow the company time to reorganise itself and the expected bright future which will result in a better outcome for creditors as opposed to liquidation which will result in creditors receiving less than what they are owed;[[30]](#footnote-30) and

(b) an affidavit sworn by the person or persons nominated for the appointment as restructuring officer containing matters which are specified in Order 3, rule 4 of the CWR, which relates to an official liquidator’s consent to act.

There are further requirements that need to be followed, for example the Restructuring Petition has to be advertised in the Cayman Islands and in the countries where the petition will come to the attention of PL's creditors.[[31]](#footnote-31) Based on the facts this would include other countries in the Caribbean and most likely the UK if that is where H&W is based. The advertisement also needs to occur with 7 days of the petition being filed and no less than 7 days before the hearing to ensure than interested stakeholders have proper notice and can participate.

At the hearing of the Restructuring Petition, the Court will either order the appointment of the Restructuring Officer (the **RO**), adjourn the hearing, dismiss the petition, or make any other order that the Court sees fit (aside from a winding up order). It is noteworthy that the Court can grant leave for a winding-up petition and then hear that petition and the Restructuring Petition at the same time.[[32]](#footnote-32)

It is also noteworthy that the requirements for the appointment of restructuring officers are the same as the former requirements for the appointment of a provisional liquidator under section 104 (3) prior to the law being amended in 2022. As a result, the case law on the appointment of provisional liquidators will likely inform the Court’s approach to the appointment of RO's.

In addition, RO regime, it is still available to PL to apply to appoint provisional liquidators for the purpose of presenting a restructuring proposal to its creditors or members. Section 104(3) of the CA simply provides that the Court may appoint a provisional liquidator if the Court considers it appropriate to do so. In view of this broad drafting, PL may take advantage of this route too in order to restructure its affairs. There is a school of thought in the Cayman Islands that appointing a provisional liquidator may make it easier when it comes to seeking recognition of that insolvency professional overseas as opposed to seeking recognition of a restructuring officer. This could be important for PL if it needs the Cayman Court's order / appointment to be recognised in other countries for the purpose of its restructuring plan.

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

If an RO has been appointed by the Court, in the context of making that appointment, the Court will have determined what powers are to be retained by the directors (if any). If the Court has allowed the Kraken family to continue managing PL's affairs simultaneously with the restructuring appointment, then this is referred to as “light touch". The Court's decision will likely depend on the proposals and the Court's confidence in the family's abilities based on the evidence.

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

Before approving any proposed restructuring of PL, the Court will consider whether:

1. The statutory notice and advertising periods were met;
2. Each class of creditors was fairly represented at the Scheme Meeting(s);
3. There is support for the restructuring from all creditors / any opposition;
4. The restructuring is in the best interests of the PL and its stakeholders;
5. The restructuring plan is viable and PL's business exists (in this case we know that there is a viable business for PL as the market for liveaboard diving remains strong, and financial forecast is relatively bright);
6. The resolutions were passed by the required majorities and that the majority acted bona fide; and
7. That approval of the Scheme was reasonable (in other words, whether an intelligent, honest member of the class convened, acting in his own interest, might reasonably have approved the Scheme).[[33]](#footnote-33)

**\* End of Assessment \***

1. CA, section 241. [↑](#footnote-ref-1)
2. CA, section 242. [↑](#footnote-ref-2)
3. CA, section 183. [↑](#footnote-ref-3)
4. CA, section 242(2). [↑](#footnote-ref-4)
5. Module 5C Guidance Text, Cayman Islands 2023 / 2024 (**Guidance Text**), section 8, pages 69 – 71. [↑](#footnote-ref-5)
6. *Bandone v Sol Properties* 2008 CILR 301. [↑](#footnote-ref-6)
7. Guidance Text, section 8.3, pages 70 – 71. [↑](#footnote-ref-7)
8. Guidance Text, section 8.4, page 71. [↑](#footnote-ref-8)
9. Guidance Text, section 5.3.3, page 11. [↑](#footnote-ref-9)
10. Ibid. [↑](#footnote-ref-10)
11. Ibid. [↑](#footnote-ref-11)
12. Guidance Text, Section 6.4.1.2, page 45. [↑](#footnote-ref-12)
13. GCR, Order 51, rule 1. [↑](#footnote-ref-13)
14. CA, Section 225(1). [↑](#footnote-ref-14)
15. CA, Section s 224(1). [↑](#footnote-ref-15)
16. CA, Section s 224(3). [↑](#footnote-ref-16)
17. CA, Section s 224(1). [↑](#footnote-ref-17)
18. CA, Section s 226(6). [↑](#footnote-ref-18)
19. CA, Section s 227(1). [↑](#footnote-ref-19)
20. CA, Section s 224(4)(b). [↑](#footnote-ref-20)
21. CA, Section 92(e). [↑](#footnote-ref-21)
22. Guidance Text, Section 6.3.2.3, page 34. [↑](#footnote-ref-22)
23. *Tianrui (International) Holding Company Limited* [2020 (1) CILR 417]; *In the Matter of Torchlight Fund LP* [2018 (1) CILR 290. [↑](#footnote-ref-23)
24. [2016 (2) CILR 514]; [2019 (2) CILR 245]; [2019 (2) CILR 245]. [↑](#footnote-ref-24)
25. Guidance Text, section 6.3.2.3, page 42. [↑](#footnote-ref-25)
26. CA, Section 147; Guidance Text, section 6.3.2.3, page 43. [↑](#footnote-ref-26)
27. Guidance Text, Section 6.5.4.6. [↑](#footnote-ref-27)
28. CA, Section 91. [↑](#footnote-ref-28)
29. CA, Section 91(d). [↑](#footnote-ref-29)
30. CWR, O 1A, r 2(2). [↑](#footnote-ref-30)
31. CWR, O 1A, r 1. [↑](#footnote-ref-31)
32. CWR, O 1A, r 5. [↑](#footnote-ref-32)
33. Guidance Text, page 63. [↑](#footnote-ref-33)