



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 5A

BERMUDA

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

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

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

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

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentnumber.assessment5A]**. An example would be something along the following lines: 202021IFU-314.assessment5A. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **7 pages**.

ANSWER ALL THE QUESTIONS

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

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

Question 1.1

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

- (a) Only when it is balance sheet insolvent.
- (b) Only when it is cash flow insolvent.
- (c) When it is balance sheet insolvent and cash flow insolvent.
- (d) When it is either balance sheet insolvent, or cash flow insolvent, or a valid statutory demand has not been satisfied within a period of three weeks after service on the company's registered office, or if a judgment in favour of a creditor remains unsatisfied.**

Question 1.2

Who may appoint a Provisional Liquidator over a Bermuda company?

- (a) A secured creditor.
- (b) An unsecured creditor.
- (c) The company itself (whether acting by its directors or its shareholders).
- (d) The Supreme Court of Bermuda.**

Question 1.3

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

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

- (a) a, b, c, d
- (b) c, d, a, b
- (c) c, a, d, b**
- (d) a, c, d, b

Question 1.4

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

- (a) Over 50% in value.
- (b) 50% or more in value.
- (c) Over 75% in value.
- (d) A majority of each class of creditors present and voting, representing 75% or more in value.

Question 1.5

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

- (a) Two (2) years.
- (b) One (1) month.
- (c) Twelve (12) months.
- (d) Six (6) months.

Question 1.6

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

- (a) Only fraudulent conveyances.
- (b) Only floating charges.
- (c) Only post-petition dispositions.
- (d) All of the above.

Question 1.7

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

- (a) At least five (5).
- (b) One (1) is sufficient.
- (c) At least 10 or more owning policies of an aggregate value of not less than BMD 50,000.
- (d) At least 10.

Question 1.8

Where do secured creditors rank in a liquidation?

- (a) Behind unsecured creditors.
- (b) Behind preferential creditors.
- (c) Behind the costs and expenses of liquidation.
- (d) In priority to all other creditors, since they can enforce their security outside of the liquidation.

Question 1.9

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

- (a) Section 237 of the Companies Act 1981.
- (b) Section 238 of the Companies Act 1981.
- (c) Section 247 of the Companies Act 1981.
- (d) Section 158 of the Companies Act 1981.

Question 1.10

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

- (a) Resign immediately.
- (b) File a Suspicious Transaction Report forthwith.
- (c) 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.
- (d) Notify the directors, creditors and account owners within 28 days.

CORRECT – 10 MARKS.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 4 marks]

In what circumstances may a Provisional Liquidator be appointed?

A provisional liquidator may be appointed over a company following the presentation of a petition to wind the company up, and prior to the hearing of the petition.

As per the case of *Re Stewardship Credit Arbitrage Fund Ltd* [2008] Bda LR 67, such appointment is commonly made where there is a risk of dissipation of assets, or the need for

independent supervision and control over the company. In such cases creditors would usually apply for the appointment of the provisional liquidator.

Provisional Liquidators may also be appointed upon the application of the company, usually where the company is contemplating a restructuring. The benefit of doing so includes the fact that an application may then be made for a statutory stay of all proceedings against the company while a work-out process is underway (informally or through a Scheme of Arrangement). In certain cases, the provisional liquidator may be appointed on a 'soft touch' basis to allow that board of directors to retain control of the company and to work alongside the provisional liquidator.

Also the Official Receiver may be appointed as the provisional liquidator of a company in compulsory liquidation. This is usually on a default basis in the event that no commercial insolvency practitioner is willing and able to accept office.

CORRECT – 4 MARKS.

Question 2.2 [maximum 2 marks]

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

Rights of set-off are to be exercised after the commencement of a company liquidation where:

- The debts giving rise to the set-off were incurred prior to the commencement of liquidation and have crystallized a monetary payment liabilities
- The transaction giving rise to the debts was not a fraudulent preference or a fraudulent conveyance
- The dealings between the parties were mutual

Also a person is not entitled to claim the benefit of set off in any case where he had, at the time of giving creditor to the debtor, notice of an act of insolvency committed by the debtor and available against him.

CORRECT – 2 MARKS

Question 2.3 [maximum 4 marks]

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

1. Security may be taken over immovable, movable and certain intellectual property by way of a legal mortgage, by which the legal title of the debtor's property is transferred to the creditor as security for the debt. In such case the debtor remains in possession of the property and may regain possession of legal title upon satisfaction of the debt and re-conveyance of legal title by the creditor.
2. Security may also be taken over immovable, movable and certain intellectual property by way of an equitable mortgage, under which the debtor retains legal title (and possession of) the property but transfers the beneficial interest in the property to the creditor. In this case the equitable mortgage does not take priority over a third party who, without notice of the creditor's beneficial interest acquires the legal title to the property in good faith and for value. As such it may be regarded as a less desirable form of mortgage for the creditor.

3. Security may also be taken over immovable, movable and certain intellectual property by way of a fixed charge. Such charge does not result in the transfer of legal or beneficial ownership, but gives the creditor a right to take possession of the property with a right of sale, in the event of default by the debtor. Thereafter the debtor may not deal with any property that is subject to the fixed charge without the consent of the creditor. Upon exercise of the power of sale, the proceeds of sale may be applied by the creditor toward payment of the debt in priority to and without reference to other unsecured creditors.

In addition to the above mentioned forms of security over immovable, movable and certain intellectual property, security may be taken over movable and certain intangible property by way of a floating charge, pledge or lien.

Where a company grants security, the secured creditor should file details of the security with the Registrar or Companies.

CORRECT – 4 MARKS

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

Question 3.1 [maximum 8 marks]

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

Foreign liquidators may be granted recognition and assistance in Bermuda, as a matter of common law. Unlike in some other jurisdictions, Bermuda has no statutory provisions governing the recognition of foreign liquidators (with a limited exception relating to the UK, as below), including because Bermuda has not implemented the UNCITRAL Model Law on Cross-Border Insolvency.

As per the decision of the Privy Council in *Cambridge Gas Transportation Corp v Navigator Holdings plc*, the Supreme Court of Bermuda has the power to recognise liquidators appointed by the court of the company's domicile and the effects of a winding up order made by that court. Furthermore, the Supreme Court has a discretion to assist the primary liquidation court through making available to insolvency tools which would usually be available in a domestic liquidation. The extent to which the Supreme Court will so recognise and assist foreign liquidators has been the subject of some debate in the authorities, including (i) *Singularis Holdings Limited v Pricewaterhouse Coopers* and (ii) *PricewaterhouseCoopers v Saad Investments Company Limited*.

The Privy Council has made clear that the recognition and assistance of foreign liquidators will be case specific, turning on the relevant facts. The Court does not have the power to assist a foreign liquidator to do something which they could not do under the law of the jurisdiction in which they were appointed. Furthermore, in general the Court's exercise of its discretion to assist and recognise foreign liquidators must be consistent with Bermudan law and public policy.

In summary, and subject to fact specific issues, the courts of Bermuda are likely to recognise the winding-up order of foreign courts, and to assist foreign liquidators to the fullest extent possible where:

1. There is a sufficient connection between the foreign court's jurisdiction and the company in question. As such the jurisdiction in which the winding-up order was made

must have been the most appropriate or most convenient jurisdiction to have made the order and appointed and appointed the office holder.

2. There is sufficient connection between the company and the jurisdiction of Bermuda, for example by:
 - a. The presence of documents, assets or liabilities of the foreign company within Bermuda
 - b. The foreign company having conducted business or operations within or from Bermuda
 - c. The foreign company having former directors, officers, managers, agents or service providers within Bermuda
 - d. The foreign company properly needing to be involved in litigation or arbitration within Bermuda
3. There is no public policy reason under Bermudan law that the foreign liquidator should not be recognised / assisted (for example there would be prejudice caused to local Bermudan creditors).

With regard to schemes of arrangement or related proceedings, the Bermudan courts had shown themselves willing to recognise foreign court orders approving foreign schemes. However, the situation regarding a contested scheme is yet to be determined.

Finally, there are special rules relating to the assistance which will be granted by the Bermudan courts to the courts of the UK with regard to personal bankruptcy cases, under s. 144 of the Bankruptcy Act 1989.

CORRECT – 8 MARKS.

Question 3.2 [maximum 7 marks]

Write a brief essay on the circumstances in which a foreign Court judgment **will not be** registered or enforced in Bermuda.

A foreign judgment has no direct legal effect in Bermuda *per se*. Therefore active steps are required in order to achieve the recognition and enforcement of a foreign judgement. A foreign judgment may be recognised and enforced in Bermuda pursuant to certain statutory rules and/or as a matter of common law, depending on the nature of the judgment and jurisdiction in which it was made.

Under the Judgments (Reciprocal Enforcement) Act 1958 (as amended) and regulations made thereunder, the courts of Bermuda will recognise and enforce foreign final money judgments from certain jurisdictions (the courts of England & Wales and the courts of certain other commonwealth jurisdictions). However, a foreign judgment recognised under the 1958 Act may be set aside upon application of a party against whom the registered foreign judgment may be enforced, if the Supreme Court is satisfied of any of the following:

1. It was obtained by fraud
2. The rights under it are not vested in the personal by whom the application for registration was made
3. The defendant did not receive notice of the proceedings in the foreign jurisdiction in sufficient time to enable him to defend the proceedings and did not appear
4. The foreign court had no jurisdiction in the circumstances of the case
5. It is not covered by the 1958 Act or was registered in contravention of the 1958 Act

6. The matter in dispute giving rise to the registered foreign judgment had, previously to the sate of such judgment, been the subject of a final and conclusive judgment by a court of competent jurisdiction

As per the case of Masri v Consolidated Contractors International Company [2009] Bda LR 12, the fact that it is not just and convenient to enforce the judgment or that it would run contrary to public policy do not constitute sufficient grounds to set aside registration of a foreign judgment under the 1958 Act.

Judgments from foreign courts which do not fall within the ambit of the 1958 Act may be recognised and enforced under Common law. The criteria which such a judgment must meet in order to be so recognised and enforced is as follows:

1. The judgment is final and conclusive in the foreign court
2. The foreign court was of competent jurisdiction
3. The judgment was not obtained by fraud
4. The judgment was not in respect of taxes, fines or penalties
5. The enforcement of the judgment would not be contrary to Bermudan public policy
6. The rules of natural justice were observed in the proceedings before the foreign court

We can see therefore, that there are less obstacles to enforcing a judgment under the 1958 than under to common law because whilst the factors to be taken account mirror each other in both cases to a large extent, there is no public policy obstacle to blocking recognition of a judgment under the 1958 Act.

It is also interesting to note that foreign default judgments (where the defendant did not engage to defend the proceedings) are capable of enforcement in Bermuda unlike in some other jurisdictions (as long as the defendant received proper notice of the foreign proceedings).

CORRECT – 7 MARKS.

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

ELBOW LIMITED (“the Company”) was incorporated in 2019 as an exempt Bermuda company, with offices and a substantial business presence in Hong Kong. The Company was formed with the intention of investing in illiquid assets in the form of litigation funding loans and distressed debt in Asian markets.

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

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

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

The Company’s directors subsequently borrowed an additional USD 5 million from its bank, LENDBANK, secured by way of a floating charge against all of its illiquid assets. Out of the USD 5 million received from LENDBANK, ELBOW LIMITED’s directors immediately paid

themselves a bonus payment of USD 2 million and they also paid a dividend to the Company's shareholders in the sum of USD 3 million.

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

Using the facts above, answer the questions that follow.

Question 4.1 [maximum 7 marks]

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

Victory Ltd ("Victory") essentially has three options: (i) seek to agree an informal work-out with the Company for payment of the debt, (ii) petition to wind-up the Company and prove in the liquidation or (iii) seek recognition and enforcement of the Hong Kong judgment against the Company. It may also be possible for action to be taken against the directors of the Company (and potentially the shareholders) personally (i) by Victory and/or (ii) by an appointed liquidator.

Turning to the specific considerations:

(a) the jurisdictions in which it could take such action, bearing in mind the potential need for enforcement

Victory may consider taking steps to wind-up the Company or to enforce its judgment debt against the company either in Bermuda or in Hong Kong. Advice on Hong Kong law would be required to definitively advise.

It may be that if the Company, for example, owns assets of value in Hong Kong, that there are various options in Hong Kong to directly enforce the judgment debt there, notwithstanding that the Company is incorporated in Bermuda.

Should Victory successfully apply in Hong Kong to wind-up the Company, again it may be possible for a liquidator to collect in and distribute to creditors any assets in Hong Kong. However, if an HK appointed liquidator wishes to take any steps in Bermuda, they would need to seek recognition and assistance from the Bermudan courts. The factors which the Bermudan courts would take into account are detailed in the answer to question 3.1 above.

Depending on the Company's asset position, those steps to wind-up the Company or enforce the judgment debt may also be taken in Bermuda. The HK judgment does not have effect in Bermuda, and so steps would need to be taken for its recognitions and enforcement (under common law assuming the 1958 Act has not been extended to Hong Kong). If the judgment is so recognised, enforcement action could be taken in Hong Kong to enforce the judgment debt. Again, depending on the asset position, Victory may seek to present a winding-up petition to the Supreme Court of Bermuda, in order to wind-up the Company and prove in the liquidation.

(b) the defendants against whom it could take such action;

Victory may seek to enforce the judgment against the Company or to wind-up the Company. As such, the Company would be the defendant in either of those proceedings.

There is also a prima-facie case that the Company's directors have acted in breach of their fiduciary duties to the Company through their action in paying the proceeds of the LendBank loan to themselves and the Company's shareholders. In circumstances where those duties were owed to the company, the proper plaintiffs to sue the directors would be liquidators appointed to wind-up the company.

However, it is also notable that under Bermudan law, where a company enters the zone of insolvency, the directors must act in the best interests of creditors. On our facts, it appears that the Company is balance sheet solvent but cash flow insolvent. For the purpose of s 161 of the Companies Act a company may be deemed insolvent under either test. Therefore, there would appear to be good arguments that the Company's directors owed duties to the Company's creditors at the time they paid the proceeds of the LendBank loan to the directors and shareholders of the Company. In such case, Victory may seek to bring claims against the directors personally.

A liquidator, if so appointed, could seek to avoid the payments made by the company to the directors and shareholders.

With regard to the shareholders, Victory may seek to bring claims in the economic torts such as unjust enrichment (noting that the specifics of such claims are not dealt with in this module).

(c) the pros and cons of litigation as opposed to insolvency proceedings;

Whether insolvency proceedings or litigation are the best course for Victory may depend on what other creditors / debts Elbow has. Victory will rank as an ordinary unsecured creditor in the liquidation. If Elbow has granted security over its assets and / or has other debts in excess of its assets, winding-up Elbow would not be in Victory's best interests as it may not recover the full amount of the judgment debt. In such circumstances, litigation would be a better option. Winding-up Elbow would also cause Victory to lose control of the enforcement process to some extent, as this would be done by the liquidators; and it may take more time for the liquidators to gather in Elbow's assets to pay creditors.

On the other hand if Victory can successfully apply to have the judgment debt recognised in Bermuda, it could then avail itself of enforcement options such as a garnishee or charging order, without regard to other creditors of Elbow limited. This is likely to be a quicker process to recover the debt.

One advantage of insolvency proceedings is that this could allow the a liquidator to bring avoidance actions against the directors and shareholders (Victory could not bring avoidance actions as such in ordinary litigation)

(d) the causes of action that may be available against the various potential defendants.

Victory's cause of action may include:

- Claims against Elbow's directors for fraudulent trading (s.236 of the Companies Act 1981)
- Claims in unjust enrichment or other economic torts against the Elbow's directors and shareholders
- Claims against Elbow's directors for breaches of fiduciary duties (if the court is satisfied that Elbow was insolvent when payments were made out of the company)
- A debt claim against Elbow
- Enforcement action against Elbow, including to seek garnishee or charging Orders
- Presentation of a winding-up petition against Elbow

- Enforcement action in Hong Kong for breach of the costs order

GOOD ANSWER – 7 MARKS

Question 4.2 [maximum 8 marks]

To what extent would it be open to ELBOW LIMITED to try to take steps to restructure its debt obligations? How and where would it do so? Please consider whether it would be more appropriate to take steps before the Hong Kong courts, the Bermuda courts, or both and, if so, why?

Elbow could seek to restructure its debt obligations in Bermuda by an informal work out or a scheme of arrangement under sections 99 and 100 of the Companies Act 1981.

To undertake a formal scheme of arrangement (outside of a liquidation) the company would apply to the court providing a draft of the formal Scheme of Arrangement, together with its Explanatory Statement. If the Court approves the scheme, the company (or its provisional liquidators – see below) convene a scheme meeting to allow the stakeholders to vote on the proposed scheme. The proposed scheme must be approved by a majority in number representing 75% in value of each class of stakeholder attending and voting at the meeting. The terms of the scheme will become binding on the company and all members of the relevant classes once the necessary statutory majorities are achieved. If the scheme is passed, the Court then needs to sanction it. One benefit of the scheme procedure is that it allows for a 'cram down' of dissenting stakeholders.

In the present case it is notable that the directors have undertaken serious mismanagement of the company, in breach of their fiduciary duties, by paying the LendBank loan out to themselves and shareholders at a time when the company was cash-flow insolvent. Accordingly, it seems unlikely that the Court would sanction a scheme formulated and implemented by the directors. Instead, the company could seek to be placed into provisional liquidation by which a winding-up petition is presented, and application is made to stay the winding up petition and have PLs appointed. One advantage of doing so is that an application can then be made for a stay of proceedings against the company in order to allow for breathing space from creditor claims in which to negotiate the restructuring. That would be done according to the aforementioned scheme procedure or informally. It is possible in certain cases for "soft-touch" PLs to work alongside the board of directors in implementing a restructuring. However, again in view of the directors' mismanagement of the company, it is unlikely that the Court would sanction such an arrangement.

Whether any corporate rescue proceedings should be commenced in Hong Kong will turn on Hong Kong law, and the company should take local law advice in that regard. It may be possible for the company to also enter into a scheme of arrangement in Hong Kong

Per the *Titan Petrochemicals* decision, the Bermudian Court has recognised that it frequently approves parallel scheme of arrangement, including to link Hong Kong and Bermudian schemes. However, there is some uncertainty whether a foreign scheme of arrangement or other corporate rescue scheme can be recognised in Bermuda as a matter of common law, in the absence of a local scheme of arrangement in parallel. It is generally thought that such a scheme may be recognised if it is not opposed, but it is less clear what would happen if the

foreign scheme is opposed. On that basis, if the company is seeking to restructure its debts, it is advisable for it to take steps in Bermuda as well as any steps it is advised to take as a matter of Hong Kong law in Hong Kong.

GOOD ANSWER – 8 MARKS

TOTAL – 50 OUT OF 50.

*** End of Assessment ***