



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: **[studentnumber.assessment5C]**. An example would be something along the following lines: 202021IFU-314.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 “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) BST (GMT +1) 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

Select the **correct answer**.

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

- (a) a company incorporated in the Cayman Islands.
- (b) a company with property located in the Cayman Islands.
- (c) a company carrying on business in the Cayman Islands.

(d) any of the above.

Commented [BT1]: Correct. 1 mark

Question 1.2

Which of the following is **not** available in the Cayman Islands?

- (a) Appointment of a receiver.
- (b) Court-supervised liquidation.**
- (c) Official liquidation.
- (d) Deed of Company Arrangement.

Commented [BT2]: Incorrect. The answer was 'd'.

Question 1.3

In a voluntary liquidation:

- (a) the company may cease trading where it is necessary and beneficial to the liquidation.
- (b) the company must cease trading except where it is necessary and beneficial to the liquidation.**
- (c) the company must cease trading if it is necessary and beneficial to the liquidation.
- (d) the company may cease trading unless it is necessary and beneficial to the liquidation.

Commented [BT3]: Correct. 1 mark

Question 1.4

Select the **correct answer**.

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

- (a) may enforce their security with leave of the court.
- (b) may enforce their security with leave of the court provided the liquidator is on notice of the application.
- (c) may enforce their security without leave of the court.
- (d) may not enforce their security until the liquidator has adjudicated on the proofs of debt.

Commented [BT4]: Correct. 1 mark

Question 1.5

Select the **correct answer**.

In a provisional liquidation, the existing management:

- (a) continues to be in control of the company.
- (b) continues to be in control of the company subject to supervision by the court and the provisional liquidator.
- (c) may continue to be in control of the company subject to supervision by the provisional liquidator and the court.
- (d) is not permitted to remain in control of the company.

Commented [BT5]: Correct. 1 mark

Question 1.6

Select the **correct answer**.

Once a provisional liquidator is appointed:

- (a) no action may be commenced against the company without leave of the court.
- (b) no existing action may be continued against the company without permission of the provisional liquidator.
- (c) legal proceedings may be commenced or continued against the company without leave of the court.
- (d) no action may be commenced against the company.

Commented [BT6]: Correct. 1 mark

Question 1.7

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

- (a) Sums due to company employees.
- (b) Taxes due to the Cayman Islands government.

(c) Amounts due to preferred shareholders.

Commented [BT7]: Correct. 1 mark

(d) Sums due to depositors (if the company is a bank).

(e) Unsecured debts which are not subject to subordination agreements.

Question 1.8

Select the **correct answer**.

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

(a) 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.

(b) 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.

Commented [BT8]: Correct. 1 mark

(c) 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.

(d) 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 1.9

Select the **correct answer**.

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

(a) 50% or more representing 75% or more in value of the creditors must agree.

Commented [BT9]: Incorrect. The correct answer was 'd'

(b) 50% or more representing more than 75% of the creditors must agree.

(c) more than 50% representing more than 75% of the creditors must agree.

(d) more than 50% representing 75% or more in value of the creditors must agree.

Question 1.10

Select the **incorrect statement**.

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

(a) company passes a special resolution requiring it to be wound up.

(b) company does not commence business within a year of incorporation.

(c) company is unable to pay its debts.

(d) board of directors decides it is "just and equitable" for the company to be wound up,

Commented [BT10]: Correct. 1 mark

(e) company is carrying on regulated business in the Cayman Islands without a license.

Commented [BT11]: 8/10 for question 1.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

Explain the extent to which it is possible to register security over an asset in the Cayman Islands.

[In the first instance, there are no public security registers nor public searchable registers in the Cayman Islands.]

Commented [BT12]: 2 marks. Candidate displays some understanding but not a complete grasp of the topic. Suggest re-reading Guidance Text.

However, pursuant to section 54 of the Companies Law¹, the details of a security interest (regardless of where the security is located) must be recorded in the company's register of mortgages at its registered office. Other than the particulars of the security agreement, there is no statutory requirement to file transaction documents relative to the security.

The validity of a security is not affected if a company fails to register the security in its register of mortgages and charges. However, "under Cayman Islands conflict of law rules, the relevant law governing the priority and perfection of security interests will be determined by the location of the asset."^{2]}

Question 2.2 [maximum 4 marks]

Explain the legal basis for the Cayman Islands Grand Court's power to assist foreign bankruptcy proceedings and the circumstances in which such powers may be exercised.

[Although the Cayman Islands has not adopted the MLCBI³, many of its principles are applied to insolvency matters involving cross-border circumstances and this is evidenced in Part XVII (seventeen) of the Company Law which addresses the concept of "International Co-operation".]

Commented [BT13]: 4 marks

Section 241 of the Companies Law gives the Grand Court the authority to make ancillary orders with respect to specific forms of ancillary relief required by foreign bankruptcy proceeding.

Section 242 of the Companies Law contains a set of criteria by which the Grand Court is guided when making ancillary orders. It should be noted that the premise of these criteria is consistent with assuring an economic and efficient administration of the debtor's estate⁴. Pursuant to the relative section these are:

- (a) the just treatment of all holders of claims against or interests in a debtor's estate wherever they may be domiciled;

¹ Cayman Islands Company Law - Companies Law (2018 Revision).

² Tonner QC, Benjamin; Module Author, INSOL International, Modul 5C, Guidance Text Cayman Islands (2020/2021), section 5.3 (Registering security), p.9. Hereinafter referred to as "the Guidance Text".

³ The United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency ("MLCBI").

⁴ This is also in line with the objectives set out in the preamble of the MLCBI; "Fair and efficient administration of cross-border insolvencies...Protection and maximization of the value of the debtor's assets".

- (b) the protection of claim holders in the Islands against prejudice and inconvenience in the processing of claims in the foreign bankruptcy proceeding;
- (c) the prevention of preferential or fraudulent dispositions of property comprised in the debtor's estate;
- (d) the distribution of the debtor's estate amongst creditors substantially in accordance with the order prescribed by Part V;
- (e) the recognition and enforcement of security interests created by the debtor;
- (f) the non-enforcement of foreign taxes, fines and penalties; and
- (g) comity.]

Question 2.3 [maximum 3 marks]

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

[The Foreign Judgements Reciprocal Enforcement Law⁵ (1996 Revision) ("FJREL") provides the legal framework for the recognition of foreign judgements in the Cayman Islands. The three (3) basic principles for the enforcement of a foreign judgement are outlined in Order 71 of the Grand Court Rules:

1. The order must be final and conclusive;
2. The order must be a monetary judgement; and
3. The order must have been made after the FJREL was extended to the relevant jurisdiction.

Currently, the FJREL has only been extended to foreign judgements within the jurisdiction of Australia. It is on this premise that the recognition and enforcement of foreign judgements are determined according to the following common law principles⁶:

- (a) the judgment is final;
- (b) the foreign court had jurisdiction over the debtor;
- (c) the foreign judgment was not obtained by fraud;
- (d) the foreign judgment is not contrary to public policy of the Cayman Islands; and
- (e) the foreign judgment was not obtained contrary to the rules of natural justice.]

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

Question 3.1 [maximum 9 marks]

In the absence of a statutory prohibition on insolvent trading, the Cayman Islands is ill-equipped to deal with directors who wilfully disregard the interests of creditors.

Critically discuss this statement and indicate whether you agree or disagree with it, providing reasons for your answer.

[Directors whose actions cause a company to continue trading during a state of insolvency can be made personally liable to the company for any losses. It is an established point of view in the Cayman Islands, that the duties of a director are owed to the company over and above the direct interests of creditors. However, in the case of insolvency, Cayman Islands law mandate that directors must take into consideration the creditors' interests as part of their duty to act in the best interest of the company⁷. Despite this position, to agree or disagree that the

⁵ The Guidance Text, section 8.2 (Recognition of Foreign Judgements – Statute), p.46

⁶ Ibid, p.47

⁷ This duty was demonstrated in the Cayman Islands decision, Hutchinson Limited, Crain Creek Limited Mountain Dew Limited and Forum Limited v. Cititrust (Cayman) Limited and Ten Others (1998) CILR 43 where

Commented [BT14]: 3 marks

Cayman Islands is ill-equipped to deal with directors who willfully disregard the interests of creditors, one must first objectively consider the definition of 'insolvent trading', within the context of the fiduciary duties of a director.

Directors always have a fiduciary duty to act in the best interest of the company. It is therefore on this premise, the duties of a director may, involve making decisions in circumstances where the company is experiencing financial challenges. If a company is at risk of becoming insolvent, directors will need to make 'hard and fast' decisions on whether there is a reasonable prospect, of the company 'trading out' of an insolvent state, and whether this action could alleviate any pressures that the company may be experiencing. This was a point of contention that was addressed in the Prospect Properties v McNeill matter where it was held, "where a company is insolvent or of doubtful solvency, the directors duty to act in the best interest of the company requires them to have regard to the interests of its creditors"⁸. In simple terms, some decisions made by directors in best interest of the company may involve implementing certain measures that could mitigate the company's inability to meet financial obligations. This includes to a great degree, the interest of the creditors to be paid.

In summary, if it is the intention of the directors to use insolvent trading as a means of financial recovery to the company, it is my belief that this action cannot be regarded as a 'willful disregard' to the interest of creditors and neither should this action be considered as a liability to a director for a breach of their fiduciary duty to the company. Directors have a duty to exercise powers for a proper purpose⁹.

In conclusion, although there are no statutory provisions that prohibit insolvent trading, the actions of directors are governed by the Companies Law. Furthermore, the Cayman Islands is regarded as a creditor-friendly jurisdiction and emphasis of company law principles, to protect the rights of creditors as key stakeholders in the company, is significant. It can therefore be concluded that the Cayman Islands is equipped to deal with directors who willfully disregard the interests of [creditors].

Question 3.2 [maximum 6 marks]

Receivers have a limited role to play in a Cayman Islands insolvency scenario. Discuss.

[As it relates to the insolvency laws of the Cayman Islands, receiverships are not specifically provided for under The Companies Winding Up Rules 2013. Nevertheless, receiverships are regarded as an alternative method of recovery in the formal insolvency scenario in the Cayman Islands. Outside of this scope, the appointment of receivers and the issuance of receivership orders are specifically provided for under the relevant statute dealing with segregated portfolio companies¹⁰.

Receiverships are generally utilized by secured lenders in circumstances where a debtor has defaulted on a contractual agreement. The COVID-19 pandemic has had a negative impact on the business operations worldwide, and by extension corporate entities that are either incorporated in the Cayman Islands or have assets located in relevant jurisdictions may potentially be exposed to some form of receivership. Given the Cayman Islands is regarded

it was held that, "It is settled law in the Cayman Islands and England that when a company is insolvent or doubtfully solvent it is incumbent upon its Directors to keep its assets inviolate for its creditors. If directors fail to perform this duty they will be in breach of their fiduciary duties ..."

⁸ Insert Prospect v McNeill judgement here.

⁹ This duty was confirmed in the Cayman Islands decision in Argentine Holdings (Cayman) Limited v. Buenos Aires Hotel Corporation S.A. (1997), CLR 90.

¹⁰ The Guidance Text, section 6.4.2 (Segregated Portfolio Companies), p.37.

Commented [BT15]: 7 marks. Some good points here. Specific reference might also have been made to sections 99, 135, 145, 146, 147 Companies Act.

Commented [BT16]: 6 marks

as a creditor-friendly jurisdiction¹¹, secured lenders in pursuit of recovering outstanding funds owed to them have used the option of receivership appointments to manage and execute recovery efforts. The advantage to creditors is that receivers may be appointed without court involvement in respect of the provisions contained in the security agreement¹².

A receiver may also be appointed by the Grand Court in the Cayman Islands by way of a court petition by a secured creditor. This provision is governed by Order 30, r.1 of the Grand Court Rules (Application for receiver and injunction). Furthermore, section 11A of the Grand Court Law confirms the Grand Court's power to, by order, appoint a receiver in relation to foreign proceedings (essentially cross-border proceedings). It should be noted that the Grand Court's power to appoint receivers is separate from an appointment by a lender in the debtor's default in a loan or mortgage agreement. In circumstances where the enforcement of security has been unsuccessful, the appointment of receivers by way of equitable execution is possible where a judgement creditor petitions a court application¹³.

Receivers do have a limited role to play in a Cayman Islands insolvency scenario, particularly since the main objective of secured lenders with a judgement debt is to quickly secure assets, to prevent asset devaluation.]

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

Black Pearl Ltd is a company registered in the Cayman Islands. It operates a fleet of pirate-themed cruise ships across the Caribbean. It was founded by the wealthy Sparrow family over 75 years ago. The family continues to own and manage the business.

In recent years, Black Pearl has been rapidly expanding its cruise ship operations. However, the unexpected slump in worldwide tourism at the start of 2020 due to Covid-19 has badly affected Black Pearl's revenues.

Within weeks Black Pearl is going to default on its loan repayments to Monster Mortgage (Monster). Monster has lent Black Pearl USD 100 million (USD 40 million of which is secured by a mortgage over four of Black Pearl's cruise ships).

Black Pearl has already failed to pay various service providers for several months (tender vessels, food and beverage suppliers, utilities, engineers and mechanics). The payment of utilities is particularly important to the ongoing repair and maintenance of the fleet of vessels at Black Pearl's dry dock facility in Little Cayman.

To make matters worse, Black Pearl has recently lost arbitration proceedings in London in relation to the construction of a new fleet of ships and been ordered to pay damages of USD 50 million to Jolly Roger Inc. It will not be able to satisfy that award.

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

- (a) What action can Monster take to protect itself?
- (b) What action can Jolly Roger Inc take against Black Pearl?

¹¹ Idem, section 6.1 (Insolvency System – General), p.11.

¹² Idem, section 6.4.3, p.38.

¹³ Smith, Paul and Pearson, Katie; Harneys (Cayman Islands), "Corporate Receivership Applications – Fighting back – Receivership is an important weapon in the arsenal of any commercial litigator".

- (c) What action can the unsecured trade creditors take against Black Pearl?
- (d) Does the Cayman Islands Court have jurisdiction over Black Pearl?
- (e) Is there a legal route via which Black Pearl can protect itself and seek to restructure?
- (f) Following on from (e) above and assuming there is a legal route via which Black Pearl can protect itself and seek to restructure, can the Sparrow family continue to run Black Pearl during this process?
- (g) Assuming that the Cayman Islands Court has jurisdiction, what factors will the court take into consideration before approving any proposed restructuring?

What action can Monster take to protect itself?

[Since Black Pearl has not yet entered liquidation proceedings and neither has an event of default occurred, Monster as a secured lender should begin reviewing the options available for the recovery of the outstanding funds owed to them.

Monster has a mortgage security over certain assets of Black Pearl (namely, four (4) of its cruise ships) and Monster is therefore considered a secured lender of Black Pearl. Although there is no specific mention of the principle amount remaining to be settled with respect to the loan agreement, the debt owed outweighs the value of the security. However, it is likely the security is secured by a fixed charge over certain assets. This gives Monster the right to take possession of the cruise ships, sell them and apply the proceeds to the debt owed by Black Pearl. This can be achieved by an out-of-court appointment of a receiver, in respect of the provisions contained in the mortgage agreement.

In the event liquidation proceedings are commenced to wind-up the business of Black Pearl, the debt owed to Monster is more than the value of its security. Therefore, Monster may prove in the liquidation for the unsecured balance. The proof of debt submitted by Monster must include details of the security and the value. Order 17 of The Companies Winding Up Rules gives guidance on this process.

Commented [BT17]: 2 marks

What action can Jolly Rodger Inc. take against Black Pearl?

The enforcement of foreign arbitral awards in the Cayman Islands are governed by The Arbitration Act, 2012¹⁴ ("the Act") and the Foreign Arbitral Awards Enforcement Act (1997 Revision).

Pursuant to section 72 of the Act, an arbitral award made by the arbitration proceedings in London, may with leave of the court, be enforced in the same manner as a domestic judgement or order of the court, regardless of the jurisdiction in which the award was made.

Jolly Rodger may make an application for leave of the court to enforce the arbitral award by filing an *ex parte*¹⁵ originating summons along with an affidavit containing exhibits of certified copies of the original award and the original arbitration agreement. Black Pearl has 14 days from the date of service to make application to set aside the order for leave. Grounds for a rejection of a foreign arbitral award are minimal but if recognised by the court the award can be enforced in like manner as with a foreign judgement.

Commented [BT18]: 2 marks

¹⁴ Global Legal Insights, International Arbitration 2021 (Cayman Islands) at << <https://www.globallegalinsights.com/practice-areas/international-arbitration-laws-and-regulations/cayman-islands>>> accessed on 23 July 2021. This Act is modelled on the UK's Arbitration Act 1996 as well as the provisions of the UNCITRAL Model Law on International Commercial Arbitration (1985), with amendments as adopted in 2006.

¹⁵ One or more parties are being served.

What action can the unsecured trade creditors take against Black Pearl?

[Under Cayman Islands law, an unsecured creditor has a right to file a winding up petition against Black Pearl. It should be noted that should Black Pearl enter provisional liquidation proceedings, an automatic stay on claims is triggered.]

Commented [BT19]: 2 marks

Does the Cayman Islands Court have jurisdiction over Black Pearl?

[Black Pearl is a company that is registered in the Cayman Islands; therefore, the Grand Court has jurisdiction to make (winding up) orders in respect of companies which are incorporated elsewhere but subsequently registered in the Cayman Islands.]

Commented [BT20]: 1 mark

"Under Cayman Islands conflict of law rules, the relevant law governing the priority and perfection of security interests will be determined by the location of the asset."^{16]}

Is there a legal route via which Black Pearl can protect itself and seek to restructure?

[Yes, pursuant to section 86 of the Companies Law, Black Pearl does have legal recourse to protect itself and seek to restructure. This can be through a scheme of arrangement between Black Pearl and its creditors (or any class of creditors). The power derives from section 86 of the Companies Law.]

Commented [BT21]: 1.5 marks. Yes, but the key is to combine it with PL under 104(3) to secure the moratorium under section 97.

A scheme of arrangement to restructure liabilities of Black Pearl may be most appropriate in this case and a debt for equity swap could be arranged between Black Pearl and its creditors.]

Following on from (e) and assuming there is a legal route via which Black Pearl can protect itself and seek to restructure, can the Sparrow family continue to run Black Pearl during the process?

[Yes, as long as Black Pearl remains out of liquidation, the Sparrow family may continue to run Black Pearl during this process. However, if the scheme is placed into a provisional liquidation, the Sparrow family may continue in control of Black Pearl, but this is subject to supervision by a provisional liquidator and the Grand Court.^{17]}

Commented [BT22]: 1 mark

Assuming that the Cayman Islands Court has jurisdiction, what factors will the court take into consideration before approving any proposed restructuring?

[Firstly, the legislation under Cayman Islands law, that governs the approval procedure for Black Pearl's proposed scheme of arrangement is Order 102, rule 20 of the Grand Court Rules and Practice Direction 2/2010.

The filing of a scheme petition involves a three-stage process involving an application to the Grand Court, discussions regarding scheme proposals with concerned parties and once approved an application to the Grand Court to sanction the scheme.

During a sanction hearing the court will consider the following factors:

1. Jurisdictional issues and whether Black Pearl's COMI exist in the Cayman Islands and there was no recent shift of the company's COMI- this will avoid objections from a dissenting creditor or the Court.
2. Issues with the composition of and class of creditors.
3. The feasibility of the scheme documentation, whether all scheme participants have been appropriately notified and privy to the document.]

Commented [BT23]: 2 marks

Commented [BT24]: 11.5 for question 4.

* End of Assessment *

Commented [BT25]: Total marks for this candidate = 41.5

¹⁶ The Guidance Text p.10

¹⁷ The Guidance Text, p.24 – Also referred to as "light touch" provisional liquidations.