



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: 202122-336.assessment5C. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words "studentID" with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. 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 **8 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**.

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 [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]: Correct. 1 mark.

Question 1.3

Select the **correct answer**.

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**.

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 [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**.

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 [BT6]: Correct. 1 mark.

Question 1.7

Select the **correct answer**.

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

- (a) 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.
- (b) 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.
- (c) 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.
- (d) 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.

Commented [BT7]: Correct. 1 mark.

Question 1.8

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.
- (d) Sums due to depositors (if the company is a bank).
- (e) Unsecured debts which are not subject to subordination agreements.

Commented [BT8]: Correct. 1 mark.

Question 1.9

Select the **incorrect statement**.

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

- (a) The company passes a special resolution requiring it to be wound up.
- (b) The company does not commence business within a year of incorporation.
- (c) The company is unable to pay its debts.
- (d) The board of directors decides it is "just and equitable" for the company to be wound up.
- (e) The company is carrying on regulated business in the Cayman Islands without a license.

Commented [BT9]: Correct. 1 mark.

Question 1.10

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.
- (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.

Commented [BT10]: Correct. 1 mark.

Commented [BT11]: 10/10 for this section

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [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 its security (mortgages and security) over an asset in Cayman Islands if the asset is either real estate, ship, aircraft, motor vehicle or intellectual property since there is a public central proprietorship registration system for said assets in Cayman Islands, and security interest (charges, mortgages) over such assets are also considered as assets that can be registered. The effect of doing so is third-party buyer will be considered to have constructive notice of such security interest over said assets and the third-party buyer only purchase the said assets subject to secured creditor's registered security interest.

Commented [BT12]: Correct but further reference should have been made to the Register of Mortgages system and its effect/limitations. 2 marks.

Question 2.2 [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?

Cayman Islands Grand Court have discretion powers to issue ancillary orders to assist foreign bankruptcy proceedings under Part XVII of the Companies Act. In order to achieve the best effective and speedy administration of the debtor's estate, the Cayman Islands Grand Court may exercise said discretion powers to issue ancillary reliefs if such reliefs are consistent with following circumstances :

- (1) the international comity which refers to reciprocal recognition and cooperation regarding decisions between the courts;
- (2) the recognition and enforcement of security interest granted by the debtor;
- (3) the non-enforcement of taxes, fines and penalties levied by foreign jurisdictions or authorities;
- (4) the fair treatment of all claimholders under the principle of natural justice, no matter where they are resided;
- (5) the protection of holders of claims in Cayman Islands from coming across prejudice and inconvenience in foreign legal process;
- (6) the prevention of fraudulent transaction or preferential disposal of debtor's assets;
- (7) the allocation of insolvency estate among creditors mainly according to legal order of priority.

Commented [BT13]: 3 marks. The examiner was looking for the candidate to make reference to s. 242 and the statutory test therein for full marks.

Question 2.3 [maximum 3 marks]

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

Legal framework for the recognition of foreign judgements in the Cayman Islands include the statutory framework: Foreign Judgements Reciprocal Enforcement Act (1996 Revision) ("FJREA"), and Common law. Under FJREA, Cayman Islands courts recognise and enforce the judgements of foreign country if the said foreign country also provide equal treatment of judgements of Cayman Islands courts. So far, the FJREA only recognise and enforce the judgements of Superior Courts in Australia. Therefore, most foreign judgments are enforced as unpaid debt via bringing new legal action under Common law in the Cayman Islands courts. The conditions for enforcement of foreign judgment under Common law are the foreign judgment is: (1) not got by fraud or in breach of natural justice; (2) not against the public policy of Cayman Islands; (3) final and the foreign court from which the judgment originates has jurisdiction over the debtor.

Commented [BT14]: 3 marks (although the examiner suggests the candidate thinks of these conceptually as 5 mandatory requirements not 3).

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, 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.

As per **Prospect Properties v McNeill**[1990-91 CILR 171], the Cayman Grand Court held that if the company is insolvent, the fiduciary duty of the directors is to act in the best interest of the company which include to regard the interest of creditors. To protect the interest of creditors, the directors shall act to prevent creditors' debts being unpaid. Inference from the said case authority, if the insolvent trading led to the company unable to pay the debts of creditors, such trading adversely affected the interest of creditors, the directors was in breach of their fiduciary duties. If the company is in liquidation, the liquidators can hold the former directors accountable by seeking financial damages against those directors for their breach of fiduciary duties.

If the insolvent trading led to a payment or disposition of company's asset to a creditor, and the said trading takes place in the six months prior to the deemed commencement (the date of filing the liquidation petition with Grand Court) of the company's liquidation and at such time the company is unable to pay its debts, and the paramount intention of the directors of the company was to provide said creditor with a preference over other creditors, the said insolvent trading amount to voidable preference under Section 145 of the Companies Act. Providing certain creditor with preference indicate that as a result of trading certain creditor get an advantageous position otherwise than he would have. In order to decide whether the directors have said paramount intention, the court may decide it by inference from the evidence. If there is disposal of company's asset to creditor who is related party simultaneously, such disposal is considered as preference. Such transaction shall be set aside as void, and the liquidator is entitled to apply to the Cayman Islands Grand Court for an order to claw back any payments paid to said creditor.

If the insolvent trading led to a company's asset to be sold at an undervalue with the wilful intention to defeat the creditors' debts owed by the company, under Section 146 the liquidator may apply to the Cayman Islands Grant Court to set aside the transaction within 6 years from the date of transaction.

As the intention in said undervalue transaction is to defeat creditor's debts, it is also a kind of intention to deceive creditors, so the said insolvent trading at undervalue is also subject to Section 147 of the Companies Act. As per 147, the liquidator may apply to the Cayman Islands Grand Court for an order to make knowingly parties (may include directors, fraudulent creditor) to such transaction to make contributions to company's asset as the court thinks proper.

Commented [BT15]: 7 marks. Candidate might have added a little more detail (eg. referred to sections 99 and 135)

Question 3.2 [maximum 6 marks]

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

Although appointment of receivers has not expressly mentioned in the insolvency-related legislation of Cayman Islands (e.g., Companies Act), as per Scotiabank (Cayman Islands) Limited v Treasure Island Resort (Cayman) Limited [2004=2005 CILR 423], Section 11(1) of the Grand Court Law provides the Cayman Islands Grand Court shall have same jurisdiction that is vested in High Court of England, and as per Section 37(1) of England Senior Court Act 1981, High Court of England may appoint receiver in cases if it seems just and convenient to do so. Thus, the Grand Court Rules provide the appointment of receivers for equitable execution and receivers may also be appointed to enforce court orders for the payment of money.

Moreover, if the Cayman Islands Grand Court consider it is possible that the property ascribable to specific portfolio of Segregated Portfolio Company ("SPC") is not enough to repay the debts in respect of such specific portfolio whereas the SPC is not in the winding-up process, the Court may issue a receivership order for the said specific portfolio.

Under receivership order, a receiver (equivalent to liquidator) is appointed to take over the powers of directors for the business of specific portfolio. Receiver is authorised under the said order to manage the business and property ascribable to specific portfolio, so that the business of specific portfolio can be closed down orderly, and the property of specific portfolio can be distributed to the persons who have legal right to claim. Within the time of receivership order, no legal action can be brought against the SPC regarding its said specific portfolio, unless the plaintiff has obtained leave of the Court. During receivership, if SPC is in the winding-up process, the effect of receivership order will come to an end when the winding-up process of SPC commence, but the effect of receiver's previous act during receivership is still valid.

Commented [BT16]: Good. 5 marks.

Last but not the least, in Cayman Islands secured creditor can make use of receivers for the sale of secured property outside the court if the security document has already provided the relevant provision.

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

Skull & Crossbones Inc (S & C) is a company registered in the Cayman Islands. It operates a fleet of pirate-themed party ships across central America and the Caribbean. It was founded by the wealthy Rackham family over 50 years ago. The family continues to own and manage the business.

Between 2015 and 2019, S & C had been rapidly expanding its operations. However, the unexpected slump in worldwide tourism at the start of 2020 due to COVID-19 adversely affected S & C's revenues.

S & C has only managed to stay afloat for the past 2 years with the assistance of a very large loan from Sparrow's Treasure Bank (Sparrow). Sparrow has lent S & C USD 200 million (USD 80 million of which is secured by a mortgage over four of S & C's largest party boats). The

loan facility has now been exhausted. S & C has also fallen behind on the monthly repayments to Sparrow.

There are early signs that the tourism market is starting to pick up again; however, S & C cannot afford to pay the ongoing costs associated with maintaining its fleet of ships (which include electricity and water costs for its huge dry dock facility, ongoing engineering and mechanical costs and also wages, pension and health insurance for its reduced team of employees) let alone find enough money to buy the vast quantities of top-shelf rum it will need for its forthcoming booze cruises.

To make matters worse, S & C commissioned Roger Jolly to build 10 more oversized party boats only a few months before the pandemic struck. S & C attempted to wriggle out of the contract but, by virtue of an arbitration clause, the dispute was referred to the ICC sitting in London. Earlier this month, the ICC ruled that S & C must pay damages of USD 50 million to Roger Jolly by mid-February 2022. S & C has no prospect of being 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 Sparrow take to protect its interests?
- (b) What action can Roger Jolly take to protect its interests?
- (c) What action can the unpaid employees take against S & C?
- (d) Does the Cayman Islands Court have jurisdiction over S & C?
- (e) Is there a legal route via which S & C can protect itself and seek to restructure?
- (f) Following on from (e) above, can the Rackham family continue play a part in running S & C during any restructuring process?
- (g) What factors will the Cayman Islands court take into consideration before approving any proposed restructuring?

(a) Among Sparrow's USD 200 million loans, USD 80 million of them is secured debt as it is secured by a mortgage over four of S & C's largest party boats. Even S & C is in liquidation, Sparrow can enforce the said mortgage over the said ships for the amount of USD 80 million without the leave of the Grand Court or taking liquidator into account, as secured debt are paid in priority over other preferential debts and unsecured debt in the process of liquidation.

Regarding the balance USD 120 million, they are unsecured debt. As per Section 92 of the Companies Act, Grand Court may wind up a company if it is unable to pay its debts. As per Section 93 of the Companies Act, a company is considered as unable to pay its debts if it is proved to the satisfaction of the Court that the company is unable to pay its debts, and as per Section 93(c), whether a company is unable to pay its debts depend on cash-flow test. As S & C has also fallen behind on the monthly repayments to Sparrow, and besides S & C also cannot afford to pay the ongoing costs associated with maintaining its fleet of ships, it submits that S & C is unable to pay its debt on cash-flow basis. Therefore, Sparrow can file a winding-up petition with the Grand Court for legal liquidation of S & C, so that legal liquidator can be appointed under court order to wind up S & C and distribute its property to creditors and shareholders. Alternatively, Sparrow can make an ex-parte application to the Grand Court under Section 104(2) for provisional liquidation of S & C in order to protect the asset of S & C

and prevent mismanagement of S & C by its existing directors until the appointment of official liquidator.

(b) As Roger Jolly has obtained foreign judgement (ICC decision in London) for the award of damages of USD 50 million, if S & C did not pay the said damages by the mid Feb 2022, such foreign judgments can be enforced as unpaid debt (USD 50 million) via bringing new legal action under Common law in the Cayman Islands courts within six years limitation period from the date of said ICC decision. The conditions for enforcement of Roger Jolly's foreign judgment under Common law are the said ICC decision is: (1) not obtained by fraud or in breach of natural justice; (2) not against the public policy of Cayman Islands; (3) final and the ICC has jurisdiction over the debtor (S & C). If Roger Jolly's said legal action under Common law is successful in Cayman Islands courts, full range of enforcement remedies in Cayman Islands are available to Roger to enforce his judgement.

(c) The unpaid employees are also a kind of creditors of S & C, like Sparrow, under Section 92, unpaid employee can file a winding-up petition with the Grand Court for legal liquidation of S & C on the ground that S & C is unable to pay its debt (wages), so that legal liquidator can be appointed under court order to wind up S & C and distribute its property to creditors and shareholders. As per Section 141, unpaid employees' wages are one of the preferential debts which are paid in priority to other debts except secured debts.

(d) The Cayman Islands Court has jurisdiction over the matter of corporate restructuring or liquidation of S & C, since S & C is registered in the Cayman Islands.

(e) S & C itself can make an ex-parte application to the Grand Court for provisional liquidation under Section 104(3) for the reason that S & C is or is likely to be unable to pay its debt; and S & C wants to have a scheme of arrangement with its creditors under Section 86. If the Grand Court approve S & C's application and grant provisional liquidation to it, during the period of provisional liquidation there is an automatic stay on legal action against S & C, and S & C can make use of that to negotiate with creditors and work out a scheme of arrangement with the creditors.

(f) If S & C only file a scheme of arrangement petition with the Grand Court without making an ex-parte application to the Grand Court for provisional liquidation in the first place, during restructuring process the Rackham family can continue to play a part in running S & C. But if there is no provisional liquidation, there is also no automatic stay on legal action against S & C during restructuring process. If there is a provisional liquidation accompanying with S & C's restructuring process, the Grand Court must decide which power shall be exercised by the provisional liquidator, and which power shall be retained by Rackham family (as existing management). If Grand Court decide that Rackham family retain most of its existing power, it is a light-touch restructuring. But it is also possible for the Grand Court to authorize provisional liquidator to take over all of the power from Rackham family over the management of S & C during the restructuring process.

(g) Cayman Islands court take into account following factors into consideration before approving proposed restructuring: (1) whether court's order for meetings of creditors/members be convened for approving the scheme is in compliance or not; (2) during convening hearing whether the class is fairly composed of and the scheme document fully include necessary information for creditors or members to make informed decision on the scheme proposal; (3) during scheme meetings whether the majority fairly represent over 50% in numbers and also at least 75% of value of the creditors present and voting in person or in proxy; and (4) whether the scheme of arrangement itself can let a clever and truthful convened member reasonably approve the scheme for his own interest.

*** End of Assessment ***

Commented [BT17]: Pretty good answer overall. 2 marks. Examiner was looking for candidate to reference ability of secured creditor to enforce its security (which should be centrally registered given it concerns vessels) outside of liquidation proceedings and without leave of the court (s.142). Also, that S&C cannot pay its debts (s.92 and 93) such that Sparrow has standing as an unsecured creditor to petition to wind up S&C. Sparrow may therefore choose to help S&C restructure via a work out or alternatively as part of a court supervised process depending on its view of the likely recovery in each scenario.

Commented [BT18]: 1.5 marks. RJ can apply for recognition and enforcement of the arbitral award since the New York Convention has been extended to the Cayman Islands. The key point is that RJ has to apply to have the judgment recognised in the Cayman Islands. Once it does so, a range of enforcement remedies become available to it, including a charging order, writ of execution, examination of judgment debtor, attachment of earnings, garnishee proceedings and the ability to petition to wind up S&C (since RJ will be an unsecured creditor). If winding up petition has already been filed, there may be a moratorium preventing JR from taking any of the enforcement actions mentioned above in which case it will be left to file a proof of debt for its US\$50m as part of the official liquidation.

Commented [BT19]: 2 marks. The unpaid employees can sue S&C for the unpaid debts (provided a winding up petition has not yet been filed). Alternatively, they can apply to wind up under section 92 - 94 Companies Act or apply to apply to appoint provisional liquidators under 104 (if they are concerned about mismanagement or wish to support a court-supervised restructuring). If an order is made that S&C be liquidated, the sums due to the employees rank as preferential debts (section 141) ahead of certain other creditors.

Commented [BT20]: 1 mark.

Commented [BT21]: 3.5 marks

Commented [BT22]: 1 mark

Commented [BT23]: 2.5 marks. Factors include:

1. The meeting was properly convened (in accordance with the court's initial order)
2. Proposal approved by over 50% in number representing 75% or more in value of the creditors (or class of creditors) present and voting
3. whether the majority of Stakeholders voting acted in good faith, were a fair representation of the relevant Class
4. that the Scheme is better than the result would be if the company were wound up, and
5. that an intelligent and honest member of the Class would agree that the Scheme should be approved.

Commented [BT24]: Total mark 43.5/50