



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.**
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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]: Incorrect. D.

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?

Yes, however in the Cayman Islands, there is no public security registration scheme available to creditors nor is there ownership registers for certain assets including real estate, ships, aircraft, motor vehicles or intellectual property. It is the responsibility of the creditor to ensure that they have taken the necessary steps to take control of the asset.

However, all security interests must be entered into the Company's register of mortgages and charges of the debtor company. If a creditor fails to register their security interest, their interest will not be made void, however in registering the security, the third party that may be interested in purchasing the asset, will be put on notice as to the existence of a security. These steps are deemed necessary to avoid a third party from stepping in and simply purchasing the assets.

Commented [BT12]: The candidate has misunderstood the position in relation to real estate, ships, aircraft etc. 1 mark is given, however, for the candidates reference to the register of mortgages and charges.

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?

Yes, the process includes the approval of Ancillary Relief, which includes the reorganisation or rehabilitation on an insolvent debtor.

As per Section 241 and 242 of the Companies Act, the Court may grant ancillary relief in the following situations:

- To recognise the right of a foreign representative to act in the Cayman Islands on behalf of or in the name of a debtor.
- To enjoy the commencements or stay of a continuation of legal proceedings against the debtor
- To stay the enforcement of any judgement against a debtor
- To require a person that is possession of information relating to the business or affairs of the debtor to be examined or be ordered to produce documents to the foreign representative.
- To order any individual to handover any property belonging to the debtor to the foreign representative.

Commented [BT13]: 4 marks

However, there are certain criteria that should be adhered to before the ancillary order can be approved, the matters to be considered should be consistent as follows:

- All claim holders should have equal and just treatment in accordance with natural justice;
- All claim holders should be protected against prejudice and inconvenience in the processing of claims in foreign proceedings;
- Preferential of fraudulent disposal of property in the debtor estates should be prevented;
- Any distribution should be conducted in accordance with statutory order of priority;
- Any security interest created by the debtor should be recognised and enforced;
- Foreign taxes, fines and penalties should not be enforced;
- Legal decisions should be mutually recognised.

Question 2.3 [maximum 3 marks]

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

The legal framework for recognition of foreign judgments in the Cayman Islands is The Foreign Judgments Reciprocal Enforcement Act (1996 Revision). However, this judgement only applies to enforcement of Australian judgements and provides a statutory scheme for recognition and enforcement. However, in order for the judgement to be enforceable, it must have 3 characteristics, it must be final, it must be a money judgment and it should have been made after the 1996 Act was extended.

The legal framework for the enforcement of money and non-money foreign judgements for all other countries other than Australia, is usually done by commencing a new action in the Cayman Islands and will be conducted under the Grand Court Rules and are enforceable at common law. However, in order for a foreign judgment to be enforceable in respect to common law, it must be final, it must be from a foreign court that has jurisdiction over the debtor, it must not have been obtained fraudulently, it must not be contrary to the public policy of the Cayman Islands, and it must not have been obtained contrary to the rules of natural justice.

Commented [BT14]: 3 marks

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.

Although there is no statutory prohibition, directors can still be liable for any losses they have caused the Company. Directors owe the Company, its shareholders and its creditors a duty of care and diligence under Common law, a fiduciary duty to be honest and act in good faith and also a statutory duty.

When Companies are wound up, if there has been any determination of fraud, the Judge can order those parties who defrauded the Company to contribute to the assets of the Company, including directors of the Company.

As per Section 99 of Companies Act, any dispositions that are made after the Company has been wound up will be void, which is usually from the date that the petition was filed. It will be within the rights of the Liquidator to apply for all relevant transactions, or payments made from

the assets to be repaid or the actual return of a physical asset. If the petition is not filed, the respective transactions cannot be covered under this Section.

However, it is possible that it is covered under Section 145 of the Companies Act. This section covers voidable preferences to payment or disposals of Company property that has occurred 6 months before the commencement of liquidation proceedings or in the instance where certain creditors were given preference over others. In order to prove that certain creditors were given preference, the liquidator would have to show that those creditors were placed in a better position than they initially would have been. Voidable preference can also be evidenced in making payments to a related party of the Company. All instances of voidable preference can be brought before the Grand Court and those parties can be ordered to return any physical assets or repay any amounts to the Liquidator.

Section 146 of the Companies Act covers the avoidance of dispositions made at an undervalue and are covered under this section once it is proven that the asset was disposed of undervalue and it was done with the intent to defraud a creditor. All applications brought under this section, must be done within 6 years of the disposition occurring.

Section 147 of the Companies Act covers Companies that are victims of fraudulent trading. Under this section, if it can be proven that a Company remained active with the intention of defrauding its creditors, the Liquidator can request an Order from the Grand Court ordering all individuals who were aware of the situation to make contributions to the Companies assets as appropriate.

Question 3.2 [maximum 6 marks]

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

This statement is not quite true, Receivers do have a role to play in a Cayman Islands insolvency scenario. Receivers are mainly appointed over Segregated Portfolio Companies (SPC), which are regular companies which remains a single entity permitted to create separate portfolios for assets and liabilities. However, Receivers can only be appointed over insolvent portfolios to realise and distribute the assets, and on the other hand, official liquidators can only be appointed over the entire SPC.

There have been doubts in the powers/role of a Receiver and it has been noted that "the role of the Receiver is analogous to a liquidator", meaning that they can perform the same tasks. However, Receivers do not have to be appointed by the Court and can be appointed pursuant to a security instrument and will carry out its duties as set out in the charge document without any involvement from the court.

In the Matter of *JP SPC 11 and JP SPC 4*, the Court sought to remove those doubts by making a decision detailing the powers available to the Receiver and the powers and duties of a Liquidator in the Cayman Islands. Although those powers are alike, the Receivers role is distinct in that they are appointed over SPC's to realise and distribute assets and can exercise any additional powers to fulfil their duties including any powers that would have been exercised by an official liquidator.

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.

Commented [BT15]: Good. 7 1/2 marks. Might also have discussed Prospect Properties and section 135.

Commented [BT16]: 4.5 marks. Good on SPCs but don't forget GCRs and contractual appointment.

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?

Skull & Crossbones Inc (S & C) has undoubtedly run into a bit of trouble and as an Insolvency Professional, advice to Sparrow, who is a secured creditor can open liquidation proceedings against S & C. The same advice will be given to Roger Jolly and the unpaid employees, who are both unsecured creditors and have the ability to file a winding up petition in respect of S&C. However, regardless of whether Sparrow open proceedings against S&C or not before the unsecured creditors, they still have a right to enforce their security after S&C is placed into official liquidation. Roger Jolly may also have an unsecured aspect of their claim, in the amount of the excess of the debt against the value of their security.

Sparrow as a secured creditor ranks above all other parties following which the liquidation expenses, preferential debts, amounts due to preferred shareholders, debt incurred by the company in respect of redemption or purchase of shares and payment to shareholders follow. As per 141 of the Companies Act, preferential debts are paid in priority of all other debts as follows:

Commented [BT17]: 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]: .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]: 1 mark.

Commented [BT20]: General comment - Question 4 calls for an answer to each part (a)-(g), which the candidate has failed to appreciate. Regrettably, this has negatively impacted the candidates marks.

Commented [BT21]: .5 mark

Commented [BT22]: 1 mark

- Sums due to employees
- Taxes due to the Cayman Islands government
- Sums due to depositors
- Unsecured debts which are not subject to subordination agreements

However, these debts rank equally.

Roger Jolly, Sparrow or the unpaid employees can rightfully be listed as the petitioning creditor for the application. A petitioner of a winding up application can either be the Company, a creditor, any shareholder of the Company or the Cayman Islands Monetary Authority as per Section 94 of the Companies Act. Therefore, one out of the three creditors who are all owed money from the Company and would like to take the appropriate action against the Company can thus be the petitioning creditor. It is not unusual for a creditor to open liquidation proceedings against a Company and in most cases, it definitely is the creditors who do so.

As per Section 91 of the Companies Act, the Cayman Islands Grand Court will make an order to wind up a Company once it satisfies one of the following requirements:

- Incorporated in the Cayman Islands
- Incorporated else by registered in the Cayman Islands or
- In respect of a foreign Company, has property in the Cayman Islands, is carrying our business in the Cayman Islands, is the general partner of a limited partnership or is registered as a overseas company in the Cayman Islands.

S & C is registered in the Cayman Islands, and therefore can be officially liquidated in the Cayman Islands as this is one of the requirements for companies to be liquidated in the jurisdiction. The purpose and one of the functions of the official liquidation would be to wind up the Company and distribute its assets to the creditors of the Company, those creditors being Sparrow, the unpaid employees, Roger Jolly and any other creditors that may come forward when the notice of winding up is advertised. The assets of the Company are likely to be listed as the various party boats that the Company are in possession of.

The application for winding up must be satisfied with appropriate grounds for winding up in that the Company including being unable to pay the debts of the Company, of which S & C has been unable to do. A Company unable to pay its debt is described such as according to Section 93 of the Company Act, "if it is proved to the satisfaction of the court that the Company is unable to pay its debt". Sparrow, as petitioning creditor will have no issues demonstrating to the Court that the Company is unable to pay their debts as they have fallen behind on monthly repayments after haven exhausted their loan facility and the Company was unable to pay for maintenance of their fleet and wages, pension and health insurance for their employees.

All creditors including the secured creditor must submit a proof of debt form in the liquidation describing the amount and interest that is due. All distributions made by the Company must done *pari passu* in order of priorities as detailed above.

There is a legal route that S & C can use to protect the Company, the Company can be placed in provisional liquidation pursuant to Section 104(3) of the Companies Act. This process will allow for the negotiations and compromises between the Company and the creditors and members. According to the Guidance Text, it is not unusual for a provisional liquidation to be used in conjunction with a Scheme of Arrangements.

A Scheme of Arrangement is approved by the Court and is an arrangement between the Company and its creditors or members or any class of them. A scheme can be commenced by a creditor, shareholders or the Company, however if the scheme is commenced by the creditor or shareholder, the Company's consent is required.

The Rackham family can continue to play a role in running S & C once the Company is in an approved Scheme of Arrangement once the company is not in provisional liquidation, unless

Commented [BT23]: 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 [BT24]: 2 marks. The Court may, at any time after the presentation of a winding up petition but before making a winding up order, appoint provisional liquidators (PLs). An application may be made *ex parte* by the company (S&C) on the grounds that it is, or is likely to become, unable to pay its debts and intends to present a compromise or arrangement to its creditors in accordance with section 104(3) of the CICA. In the event that a winding up petition is presented by a creditor, S&C could respond by seeking to appoint provisional liquidators. The appointment of PLs would ensure that no action or proceedings may be commenced or continued against the S&C without the leave of the Court as per Section 97 of the CICA (statutory moratorium). Under the supervision of the Court and the JPLs, S&C could then explore a restructuring.

the proceedings are light touch insolvency proceedings. In light touch provisional liquidations, the directors will be supervised by the provisional liquidator and the Grand Court, but this can also depend on the severity of the case.

There is an approval procedure for Scheme of Arrangements, and the following three stage process must be achieved as follows which is governed by Order 102, Rule 20 of the Grand Court Rules and Practice Direction 2/2010:

1. The application must be made to the Grand Court for an order that meeting of creditors or members be convened for the purpose of approving the scheme. This meeting should consist of a majority in number representing at least 75% in value of creditors present and voting in person or by proxy who must agree to the compromise or arrangement.
2. The proposals in the Scheme should be discussed at meetings held in accordance with the convened hearing order and either approved or rejected.
3. If the Scheme is approved at the hearing, an application can then be made to the Grand Court to obtain approval or sanction of the said Scheme. The process normally takes 10 to 12 weeks from the filing stage to be approved and will only approve a Scheme that is considered "fair".

The approved Scheme of Arrangement can then be advertised.

In a Scheme of Arrangement, if the Company is not in provisional liquidation the disposal of the assets will be executed by the directors of the Company and creditors may bid for the assets and there are no specific rules governing bids by creditors. Scheme of Arrangements are funded by the assets of the Company or from any new funds obtained through investments.

*** End of Assessment ***

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Commented [BT25]: 1/2 mark. It depends on the terms of the PL order. As per provisions of section 104(1)(4) of the Companies Act, once appointed by the court a provisional liquidator will carry out only such functions as the Court may confer on him/her and will exercise such powers as may be conferred by the order of appointment.

Commented [BT26]: 2 marks. Factors include the court will consider when decided to sanction 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.