



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).
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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]: 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?

In the Cayman Islands, there is no public registration regime for security (save for registers relating to land, ship, aircraft, motor vehicles, and intellectual property)¹. Although there is no public register for security interests in the Cayman Islands, section 54 of the Companies Act (Revision 2020) (CA (Revision 2020)) expressly mandates Cayman companies to maintain a register of charges and mortgages at their registered office². Thus, if a security interest, by way of example, charge, pledge, or encumbrance, is created over the assets of a Cayman company, such charge must be duly recorded on its register of charges and mortgages. The register must include: (a) a short description of the property mortgaged or charged; (b) the amount of the charge created; and (c) the names of the mortgagee or persons entitled to such charge³. Notably absent from the above requirements is that there is, in fact, no statutory requirement to file the security document with the company's registered office. If a company fails or neglects to update and/or maintain the register of mortgages and charges, each director, manager, or officer of the company is liable to a statutory fine⁴.

Commented [BT12]: 3 marks

Registration of a security interest in the company's register does not create a statutory priority. Nor is registration necessary for the holder of the security interest to 'perfect' a security interest. Nevertheless, the register of mortgages and charges puts any third party who has inspected or been provided with a copy of the register on 'actual notice' of the existence of a charge over an asset⁵. As there is no statutory priority for security interests under Cayman law, priority over such interests is determined by common law choice of law principles⁶.

¹ Module at [5.3]

² S. 54 of CA (2020 Revision).

³ S. 54(1) CA (2020 Revision).

⁴ S.54(2) CA (2020 Revision).

⁵ Module at [5.3].

⁶ Ibid.

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?

Whilst the Cayman Islands have yet to enact the UNICTRAL Model Law on Cross-Border Insolvency (**Model Law**), the Grand Court of Cayman Islands (**Grand Court**) has both a statutory power as well as common law comity principles at its disposal to assist in foreign bankruptcy proceedings.

Section 241 of the CA (Revision 2020) confers standing to a “foreign representative” (i.e., a trustee, liquidator, or other insolvency practitioners) approved over a foreign company to make an application to the Grand Court for orders ancillary to a “foreign insolvency proceeding” (as that term is defined in section 240 of the CA (Revision 2020)⁷). Such relief includes:

- (1) Recognizing the right of a foreign representative to act in the Cayman Islands on behalf of or in the name of the debtor⁸;
- (2) Staying the commencement or continuation of proceedings⁹ or the enforcement of judgments against the debtor in the Cayman Islands¹⁰;
- (3) Requiring a person or persons with information relating to the business or affairs of a debtor to be examined by and provide documents to its foreign representative¹¹; and/or
- (4) Ordering the turnover of property belonging to the debtor to the foreign representative¹².

Section 240 defines a debtor for the purposes of s. 240 of the CA (Revision 2020) as a “foreign corporation” or other “foreign legal entity” subject to a foreign bankruptcy proceeding¹³. Thus, the ancillary relief available under s.241 applies to companies registered/incorporated outside the Cayman Islands. If the company is a Cayman Islands company, it will be necessary for the foreign representative to seek the recognition or assistance of the Grand Court under common law principles. For a foreign representative to obtain the benefit of the insolvency protections under the CA (Revision 2020), the representative generally must bring parallel insolvency proceedings in the Cayman Islands. It is important to note that this is not a hard and fast rule, and the Grand Court has granted such relief in the absence of Cayman insolvency proceedings. In the case of *In the Matter of China Agrotech Holdings Ltd* (FSD 157 of 2017 (NSJ)), the Grand Court recognized the court’s jurisdiction to grant common law recognition and assistance to a foreign liquidator without Cayman insolvency proceedings being afoot in the Cayman¹⁴.

Commented [BT13]: 3 marks. The circumstances are contained in the statutory test at s.242.

Question 2.3 [maximum 3 marks]

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

⁷ S.240 CA (Revision 2020).

⁸ S.241(1)(a) CA (Revision 2020).

⁹ S.241(1)(b) CA (Revision 2020).

¹⁰ S.241(1)(c) CA (Revision 2020).

¹¹ S.241(1)(d) CA (Revision 2020).

¹² S.241(1)(e) CA (Revision 2020).

¹³ S.240 CA (Revision 2020).

¹⁴ <https://www.ogier.com/publications/cayman-court-grants-recognition-and-assistance-to-foreign-liquidators-appointed-over-a-cayman-company>

The Cayman Islands have not entered into any bilateral or multilateral treaties for the reciprocal recognition and enforcement of foreign judgments. As such, there are two regimes available for enforcement.

Statutory Regime

The Foreign Judgments Reciprocal Enforcement Act (1996 Revision) (**Enforcement Act**) applies to judgments issued by foreign courts expressly set out in the Enforcement Act. The Enforcement Act has only been extended to the Superior Courts of Australia and its external Territories. Namely:

- High Court of Australia;
- Federal Court of Australia;
- Family Court of Australia;
- Family Court of Western Australia;
- Supreme Court of New South Wales;
- Supreme Court of Victoria;
- Supreme Court of Queensland;
- Supreme Court of Western Australia;
- Supreme Court of South Australia;
- Supreme Court of Tasmania;
- Supreme Court of the Northern Territory;
- Supreme Court of Australia Capital Territory; and
- Supreme Court of Norfolk Island.

Upon recognition, upon a judgment of one of the foreign courts listed above, the foreign judgment shall have the same force and effect as a judgment given by the Grand Court for the purposes of enforcement¹⁵.

For the Enforcement Act to apply, said judgment (1) must be final and conclusive between the parties¹⁶; (2) is for a sum of money (not a penalty or taxes)¹⁷; and (3) such judgment was given after the Enforcement Act had been extended to the foreign country. Under the Enforcement Act, a judgment will be deemed final, notwithstanding that the judgment is subject to an appeal in the foreign court¹⁸.

Common law regime

For all other foreign judgments, the common law regime rules apply. Prior to 2008, both regimes only applied to monetary judgments. Under the common law regime, the Grand Court has extended the ability to enforce non-monetary judgments, where the principles of private international law and comity require¹⁹. A foreign judgment will be capable of recognition by the Grand Court provided that:

- The foreign court had jurisdiction over the debtor in accordance with Cayman conflict of law principles;
- The judgment is final; and

¹⁵ S. 4(2) Enforcement Act

¹⁶ S. 4(2)(a) Enforcement Act

¹⁷ S. 4(2)(b) Enforcement Act

¹⁸ S.3(3) Enforcement Act.

¹⁹ *Bandone v Sol Properties Incorporated* [2008] CILR 301 at [60] to [64]

- The judgment has not been obtained by fraud or contrary to the rules of natural justice²⁰

Procedure

A party seeking to enforce a foreign judgment must apply to the Grand Court by Originating Summons supported by an affidavit²¹. This affidavit must state to the best of the deponent's knowledge and belief:

- The full name and address of the debtor/creditor
- Exhibit a copy of the judgment;
- That the judgment creditor is entitled to enforce the judgment; and
- That at the date of the application, the judgment remains unsatisfied.

Upon the Grand Court recognizing the foreign judgment, enforcement of the judgment may not commence until the set-aside period has expired. Upon the expiration, the foreign judgment has the same effect as a judgment of the Cayman Court and may be enforced by any or all of the methods available for domestic judgments (e.g., Appointment of a Receiver; Writ of Execution; Committal Proceedings; Charging Orders or a Garnishee order).

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.

The director of an insolvent company or a company in the "zone of insolvency" owes a fiduciary duty to act in the best interests of the company's creditors. Where such a director acts in breach of such duties, he/she may be liable for:

- Fraudulent trading;
- Avoidance of dispositions
- Avoidance of dispositions made at an undervalue; or
- Voidable preferences;

Regarding fraudulent trading, section 147 of the CA (Revision 2020) confers standing on the liquidator to apply to the Grand Court for a declaration that any person or persons are liable to contribute to the company's assets²². To bring such an application, a liquidator must establish that under the direction of the company's directors/officers, the company's business was carried out with the intent to defraud creditors or for any fraudulent purpose²³. If the Grand Court is satisfied that the company carried out its business to defraud creditors, it may make such director liable to contribute to the assets of the company's assets in the amount that the court thinks proper²⁴.

²⁰ Module at [8.3].

²¹ Grand Court Law (1995 Revision) Order 71, r 2-3

²² S.147(2) CA (Revision 2020).

²³ S.147(1) CA (Revision 2020).

²⁴ S.147(2) CA (Revision 2020).

As regards avoidance of property dispositions, antecedent dispositions made after the commencement date of the winding up petition (i.e., the date of filing of the petition²⁵) is liable to be set aside. Section 99 of the CA (Revision 2020) provides that:

“When a winding up order has been made, any disposition of the company’s property and any transfer of shares or alteration in the status of the company’s members made after the commencement of the winding up is, unless the Court orders otherwise, void²⁶.”

Thus, upon the making of a winding up order, any disposition of the (i) company’s property; (ii) transfer of shares; and/or (iii) alteration in the status of the company’s shareholders made after the commencement date may be set aside on the insistence of the liquidator. The company can avoid the effect of s.99 by applying to the court for a validation order. Such application may be made prospectively (the prudent approach for a company to adopt) or retrospectively. Still, the company runs the risk of the court not granting a validation order for retrospective validation²⁷.

Under section 99, the Court has the power to require the payment of funds to the company or the return of the asset²⁸. Further to section 99, this relief is only available to a liquidator for dispositions after the presentation of a winding-up petition.

As regards transactions at an undervalue, such transaction may be set aside under s.146 of the CA (Revision 2020).

Section 146 confers standing on a liquidator to make an application to set aside a transaction at an undervalue where company property is disposed of:

- At an undervalue²⁹. For the purposes of this section, undervalue means “no consideration” or “consideration of money or money’s worth significantly less than the value of the property³⁰”; and
- Such property is disposed of with the intent to defraud creditors of the company³¹.

For the purpose of this section, the liquidator bears the burden on such application to establish that the questionable disposition was carried out with the intent to defraud the company’s creditors³². Moreover, the look-back period concerns dispositions of the company made in the six years prior to the commencement of the liquidation³³.

If the court is satisfied that the transaction was carried out at an undervalue and with the intent to defraud creditors, the liquidator may seek either a declaration that such transaction is void or order for restitution. However, where a disposition is set-aside under section 146, if the Court determines that the recipient of such disposition has acted in good faith, the recipient will have a first-ranking charge over the property. Such charge will include the property’s costs and the costs properly incurred by the recipient in defending the proceedings³⁴.

²⁵ S.100(2) CA (Revision 2020).

²⁶ S.99 CA (Revision 2020).

²⁷ Module at [39].

²⁸ Module at [39]

²⁹ Section. 146(2) CA (Revision 2020)

³⁰ Section 146(1) CA (Revision 2020)

³¹ Section 146(2) CA (Revision 2020); Module [39].

³² Section 146(3) CA (Revision 2020)

³³ Section 146(4) CA (Revision 2020)

³⁴ Section 146(5) CA (Revision 2020)

As regards voidable preferences, section 145 of the CA (Revision 2020) confers standing on the liquidator to apply to the Grand Court for an order under this section. If the Grand Court is satisfied that such transfer of property or payment is a preference, it may declare the transaction void and order the return of the property/payment to the company.

Under section 145 a transaction will be a preference provided that:

- The person who received the preference was a creditor of the company;
- The effect of the preference is to put the creditor in a better position over the other creditors of the company if the company was to enter into the liquidation process;
- The preference was given in the period ending with the onset of the commencement of liquidation; and
- At the time of the preference, the company was unable to pay its debts within the meaning of s.93³⁵ of the CA (Revision 2020)³⁶.

Moreover, a transfer of property or payment to a related party of the company, such transfer/payment is deemed to have been made with the intent to prefer the related party over the other creditors of the company³⁷.

Commented [BT15]: 8 1/2 marks

Question 3.2 [maximum 6 marks]

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

Under the Cayman insolvency regime, a company may be wound up by:

- Voluntary liquidation;
- Provisional liquidation; or
- Official liquidation.

In the Cayman Islands, there is no administrative procedure equivalent to the procedure in England and Wales under the Insolvency Act 1986. Nevertheless, in the insolvency context 'receivers' have been appointed in the Cayman Islands in the following circumstances:

- By secured creditors under the express terms of a security instrument;
- By the Grand Court in relation to Segregated Portfolio Companies; and/or
- Generally, by the Grand Court where it is "just and expedient" to do so³⁸.

In the insolvency context, points (1) and (2) will be discussed below.

Receivers

If a corporate borrower is in financial difficulties, in addition to the insolvency procedures set out above, a secured creditor may enforce its security over an asset by the appointment of a

³⁵ S. 93: "A company shall be deemed to be unable to pay its debts if – (a) a creditor by assignment or otherwise to whom the company is indebted at law or in equity in a sum exceeding one hundred dollars then due, has served on the company by leaving at its registered office a demand under that person's hand requiring the company to pay the sum due, and the company has for the space of three weeks succeeding the service of such demand, neglected to pay such sum or to secure or compound for the same to the satisfaction of the creditor; (b) execution of other process issued on a judgment, decree or order obtained in the Court in favour of any creditor at law or in equity in any proceedings instituted by such creditor against the company, is returned unsatisfied in whole or in part; or (c) it is proved to the satisfaction of the Court that the company is unable to pay its debts."

³⁶ S. 145(1) CA (Revision 2020)

³⁷ S. 145(2) CA (Revision 2020)

³⁸ Module at [42] to [44].

receiver. This method of enforcement is an “out of court” procedure outside the court-supervised liquidation. The appointment of a receiver is only available to a secured creditor if it is expressly provided for in the security instrument.

Following a contractual event of default, a secured creditor may appoint a receiver to enforce its security with a view to selling the asset. In general terms, a security instrument will confer the power to the receiver to (i) take possession of the charged asset; (ii) manage the secured asset; (iii) execute voting rights in respect of the charged asset; (iv) receive and retain all dividends and/or interest accrued; and (v) sell the asset³⁹. Upon the appointment, a receiver owes its primary duty to the secured creditor but must exercise the same in good faith and in accordance with the express terms of the security instrument⁴⁰.

Segregated Portfolio Companies

The Grand Court may wind up a segregated portfolio company (SPC). However, due to the segregated nature of these entities, liquidators may only be appointed over the entire portfolio. Where an individual portfolio is insolvent, the Grand Court has the power to appoint a receiver of the individual portfolio to realize the assets of the portfolio and distribute its assets to creditors. The Court of Appeal confirmed this in *ABC Company SPC v JH & Co Ltd*, where it was accepted on appeal that: (1) the court has no jurisdiction under the Companies Law to wind up an individual portfolio; and (2) the appointment of a receiver over an individual portfolio was only available if the assets of the portfolio are insufficient to meet the claims of the creditors.

Upon making a Receivership order, an automatic stay of proceedings against the SPC takes effect, preventing creditors from bringing individual suits or claims against the SPC⁴¹. Similar to a court-ordered winding up, during the period of receivership, the board of directors is displaced and the receiver shall be responsible for all functions and duties of the directors in respect of the segregated portfolio⁴².

Commented [BT16]: 6 marks

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.

³⁹ [https://www.walkersglobal.com/images/Publications/Articles 2019/January/SGP-IDR-Article-International Corporate Rescue Secured Rights and Receiverships Windfalls and Pitfalls – 22 Jan 2019.pdf](https://www.walkersglobal.com/images/Publications/Articles%202019/January/SGP-IDR-Article-International%20Corporate%20Rescue%20Secured%20Rights%20and%20Receiverships%20Windfalls%20and%20Pitfalls%20-%2022%20Jan%202019.pdf)

⁴⁰ Module at [44].

⁴¹ S.226(5) CA (Revision 2020).

⁴² S.226(6) CA (Revision 2020).

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?

4(a)

Sparrow Treasure Bank (**Sparrow**), both a secured and unsecured creditor of Skull & Crossbones (**S&C**), has two options to protect its interest. Subject to the express terms of the security instrument, Sparrow as a secured creditor, is entitled to enforce its security against the vessels. This is so even where another creditor of S&C has filed a petition to wind up S&C, and the Grand Court subsequently makes a winding up order under s.142 of the CA (Revision 2020). Specifically, s.142 of the CA (Revision 2020) provides that:

“(1) Notwithstanding that a winding up order has been made, a creditor who has security over the whole or part of the assets of a company is entitled to enforce a person’s security without the leave of the Court and without reference to the liquidator.”

Thus, the commencement of liquidation proceedings does not affect Sparrow’s contractual rights, nor does the automatic stay prevent Sparrow’s ability to enforce its security. If S&C has entered the insolvency process and the liquidator sells the vessels, Sparrow is entitled to be paid in full after the liquidator’s costs have been satisfied⁴³.

As to the part of the unsecured loan (being \$120m), again, subject to the terms of the security instrument, Sparrow may take the following steps to enforce its rights. First, provided that Sparrow has *locus standi* to present a winding up petition, it may present a petition to seek an

⁴³ s. 142(2) CA (Revision 2020)

order that the Grand Court winds up S&C. In that regard, s.94 of the CA (Revision 2020) provides that a winding up petition may be presented by:

- (a) the company;*
- (b) any **creditor or creditors or prospective creditor or creditors;***
- (c) any contributory or contributories; or*
- (d) the Authority pursuant to the regulatory laws⁴⁴ⁿ (emphasis my own)*

Accordingly, Sparrow, as a creditor of S&C, has standing to present a winding up petition to the Grand Court. The Grand Court has the statutory power to make a winding up order against S&C if it is satisfied that S&C is “unable to pay its debts⁴⁵.” Section 93, in relevant part, states that a company shall be unable to pay its debts if:

“(1) a creditor who is owed a sum exceeding \$100 serves a statutory demand on the company and the company fails to satisfy the statutory demand within 21 days after service of the statutory demand⁴⁶; or

(2) it is proved by the creditor that the company is unable to pay its debts.”

Therefore, it is open to Sparrow to either serve a statutory demand seeking repayment of the \$120m and, if not paid, present an application on deemed insolvency or bring an application relying on the grounds that the company is unable to pay its debts. If Sparrow wishes to bring an application on the grounds that S&C is unable to pay its debts, the Grand Court will apply a cash flow test. In this respect, the Grand Court will consider whether Sparrow is unable to pay its debts as they fall due. In the present case, Sparrow should be in a position to satisfy the Grand Court that S&C is cash flow insolvent by relying on the fact that S&C has fallen behind its monthly repayments to Sparrow.

In the alternative, and as discussed above, Sparrow could serve a statutory demand for repayment. It should be noted, however, that in statutory demand cases, a court will not grant a winding up order if the debt is *bona fide* disputed on substantial grounds. It is well established by the authorities that the threshold of what constitutes a disputed debt is not a high one. In *Tallington Lakes v Keveten District Council* [2012] EWCA Civ 433, Etherton LJ explained that the threshold may be reached “even if, on an application for summary judgment, the defence could be regarded as shadowy.”

In the circumstances, if Sparrow can establish that S&C is unable to pay its debts, the application should be made on these grounds.

4(b)

As a foreign creditor, Roger Jolly (RJ) must apply to the Grand Court for recognition and enforcement before it may take steps in the Cayman Islands to recover the judgment debt. There are two separate statutory frameworks for arbitral awards in the Cayman Islands. The Foreign Arbitral Awards Enforcement Act (1997 Revision) gives domestic effect to the New York Convention. In 2012, the Cayman Islands enacted the Arbitration Law 2012, which extended the Grand Court’s jurisdiction to enforce arbitral awards from any foreign state.

As discussed above, RJ must make an application seeking leave from the Grand Court to enforce the foreign arbitral award. The application must be supported by affidavit evidence that exhibits the arbitration agreement and arbitral award. If leave to enforce the award is

⁴⁴ S 94(a) to (d) CA (Revision 2020)

⁴⁵ S 92(d) CA (Revision 2020)

⁴⁶ S 93(a) CA (Revision 2020)

Commented [BT17]: Good. 2 marks. Don't forget that it might be more beneficial to Sparrow to rescue the company inside or outside of court proceedings - maybe there will be a better recovery for Sparrow if S&C is allowed to continue to operate the secured assets...

Commented [BT18]: 2 marks

granted, the order must be served on S&C. Once service has been effected, S&C will have a 14-day period to apply to set aside the order. The foreign arbitral award is not capable of enforcement until the expiry of this period.

Upon recognition of the award, RJ may enforce the award in the Cayman Islands by using any or all of the relevant enforcement methods, taking into account the facts of this case, as follows:

Appointment of Receivers

Under Order 51 of the Grand Court Law (1995 Revision), the Court has the power to appoint a receiver by equitable execution over S&C's assets where it appears to the Court to be "just and convenient" to do so. Such applications are to be made in accordance with Order 31 rule 1 of the Grand Court Law.

Writ of Sequestration

If S&C fails to comply with a judgment of the Court (i.e., the recognized foreign arbitral awards), with leave, RJ may apply under Order 46, rule 5 of the Grand Court Law to have a sequester appointed to seize the assets of S&C up to the value of the judgment.

Charging Orders

Another method of enforcement available to RJ is a charging order. This method of enforcement may be deployed where a judgment debt has a beneficial interest in certain types of property, including, but not limited to, land or securities. Such applications may be made under Order 50 of the Grand Court Law. In practical terms, the effect of such an order creates a charge over the assets, which permits the judgment creditor (i.e., RJ) to obtain an order for sale to satisfy all or part of the judgment debt out of the proceeds of sale.

4(c)

In the event that S&C enters formal or informal insolvency proceedings, the employees may have various claims against S&C. In particular, these claims include:

- (1) Unpaid salary accrued during the 4 months preceding the commencement of liquidation⁴⁷;
- (2) Benefits, including any sum payable by S&C on behalf of an employee for medical health insurance premiums or pension fund contributions⁴⁸;
- (3) If the employee's contract of employment has been terminated due to S&C entering liquidation, any sums due for severance pay and earned vacation leave⁴⁹; and/or
- (4) Claims against S&C for breach of contract and/or tort⁵⁰.

The employees have three potential routes to recover any of the above sums due and owing. Specifically, the options available to the employees include:

- Claim in S&C's liquidation;
- If a winding-up order has been made, seek the court's permission to continue or bring proceedings against S&C; or
- Sell and assign their claim.

⁴⁷ Schedule 2(1) of the CA (Revision 2020)

⁴⁸ Schedule 2(2) of the CA (Revision 2020)

⁴⁹ Schedule 2(3) of the CA (Revision 2020)

⁵⁰ Schedule 2(5) of the CA (Revision 2020)

These options will be discussed in turn below.

The employees may claim in S&C's liquidation as a creditor of S&C. The priority for the payment of debts out of assets of the insolvency estate is mandated by statute. It is important to bear this in mind when considering the appropriate approach to adopt. First, any creditor who has security over the whole or any part of the assets (e.g., Sparrow over 4 vessels of S&C) is entitled to enforce that security without leave of the Court or reference to the liquidator⁵¹. Thus, these assets will not be available to satisfy the debts of S&C's unsecured creditors. Second, the liquidator's expenses incurred in the winding up are payable out of the company's assets in priority to all other claims⁵². After the payment of a liquidator's expenses, s. 141 of the CA (Revision 2020) provides that the debts due to employees are treated as preferential debts and are to be paid in priority to (i) taxes due to the Cayman government; (ii) sums due to depositors; (iii) unsecured creditors; (iv) any amounts due to preferred shareholders; (v) debts incurred by the company redeeming or purchasing its own shares; and (vi) any available surplus due to the shareholders of the company⁵³.

Section 141(2)(a) provides that preferential debts shall:

"rank equally amongst themselves and be paid in full unless the assets available...are insufficient to meet them, in which case they shall abate in equal proportions."

In other words, if the company has sufficient assets available after the payment of liquidation expenses, employees of S&C will be paid in full, otherwise, the employees should expect to receive pennies of every dollar owed to them under a liquidation scenario.

If a winding-up petition has not been presented to the Grand Court, the employees may issue proceedings against S&C. In circumstances where a winding-up order has been made against S&C, no legal proceedings may be commenced or continued against the company without the permission of the Grand Court⁵⁴.

Consideration must be given as to whether there are sufficient assets of the company and the likelihood a petition will be presented to justify the expense of issuing, or if a winding up order has been made, continuing proceedings against S&C. As *Re Exchange Securities & Commodities Ltd* [1983] BCLC 186 makes clear, the employee will have to demonstrate to the court on an application for leave to continue proceedings why it is necessary to bring proceedings rather than claim a debt in insolvency. Based on the available facts, the sensible approach for the employees is to prove in S&C's liquidation.

A final route available to the employees to recover part of any debts owing would be for the employee to sell their claim and assign it to a third party. Permission from the Court is not required; however, notice of such assignment must be given to the company or where liquidators have been appointed to the liquidators on behalf of the company. Unless the company is going to have sufficient assets to satisfy its debts to the employees in a liquidation scenario, the assignment of their claims will allow the employees to recover something without incurring the further expense or participating in S&C's liquidation.

4(d)

Commented [BT20]: 1 mark.

⁵¹ Section 142(1) of the CA (Revision 2020)

⁵² Section 109(1) of the CA (Revision 2020)

⁵³ Section 141 of the CA (Revision 2020); see also Schedule 2(1) of the CA (Revision 2020).

⁵⁴ Section 97 of the CA (Revision 2020)

The short answer is that the Grand Court has jurisdiction over S&C. The basis for this jurisdiction is grounded on the fact that S&C is a company registered under the laws of the Cayman Islands. For the purposes of insolvency proceedings, the Grand Court will have jurisdiction to make a winding up order in respect of:

- An existing company⁵⁵;
- A company incorporated and registered under the laws of the Cayman Islands⁵⁶.

Even if S&C was not a Cayman-registered company, S&C would still be subject to the winding up jurisdiction of the Grand Court:

- S&C has property located in the Cayman⁵⁷; or
- S&C is carrying on business in the Cayman⁵⁸.

Based on the available facts, S&C operates its “pirate-themed party ships” in the Caribbean. While it is not readily apparent from the factual matrix of this case – it’s reasonable to infer that S&C either (i) has property within the Cayman; and/or (ii) carrying on business in the Cayman Islands.

4(e) |

Commented [BT21]: 3.5 marks

Under the Cayman insolvency regime, provisional liquidators (PLs) may be appointed upon an application of a creditor or contributory of the company (s. 104(2) of the CA (Revision 2020)) or the company pursuant to s. 104(3) of the CA (Revision 2020). For completeness, the purpose of an application for the appointment of PLs by a creditor or contributory is to preserve and/or protect the assets of the company pending the making of a winding up order⁵⁹ and/or displace the board of directors to prevent the mismanagement or misconduct on the part of the directors of the company⁶⁰.

Where a company is in financial distress (i.e., insolvent and/or in the ‘zone of insolvency’) the CA (Revision 2020) provides for the appointment of PLs on a “soft touch” basis to afford the company an opportunity to implement a formal restructuring of the company’s debts. The appointment of PLs will trigger a statutory moratorium to prevent the company’s creditors, without the leave of the Grand Court, from enforcing its debts against the company. During the moratorium, the distressed company, under the supervision of court-appointed officers (i.e., PLs), can negotiate and hopefully present a scheme to the Grand Court for its approval.

Section 104(3) of the CA (Revision 2020) provides that:

“(3) An application for the appointment of a provisional liquidator may be made under sub-section (1) by the company ex parte on the grounds that –

(a) the company is or is likely to be unable to pay its debts within the meaning of s. 93⁶¹; and

⁵⁵ S. 91(a) of the CA (Revision 2020)

⁵⁶ S. 91(b) of the CA (Revision 2020)

⁵⁷ S.91(d)(i) of the CA (Revision 2020)

⁵⁸ S.91(d)(ii) of the CA (Revision 2020)

⁵⁹ S. 104(2)(b)(i) of the CA (Revision 2020)

⁶⁰ S. 104(2)(b)(iii) of the CA (Revision 2020)

⁶¹ S. 93: *“A company shall be deemed to be unable to pay its debts if – (a) a creditor by assignment or otherwise to whom the company is indebted at law or in equity in a sum exceeding one hundred dollars then due, has served on the company by leaving at its registered office a demand under that person’s hand requiring the company to pay the sum due, and the company has for the space of three weeks succeeding the service of such demand, neglected to pay such sum or to secure or compound for the same to the satisfaction of the creditor;*

(b) the company intends to present a compromise or arrangement to its creditors.”

Thus, following the presentation of a winding up petition by a creditor or contributory of S&C, under s. 104(3) of the CA (Revision 2020), S&C may make an application for the appointment of PLs. As it appears from the available facts, S&C has reasonable prospects of satisfying s.104(3)(a) on the grounds that: (i) it is unable to meet its ongoing expenses to maintain its fleet of ships and has fallen behind on its monthly payments to Sparrow. As a consequence, if S&C wishes to continue its business as the world comes out of the global pandemic - S&C should present a compromise or arrangement to its creditors.

In *Sun Cheong Creative Development Holdings* [2020] CIGC J1020-1, the Grand Court confirmed that the court has an ‘extensive discretionary power’ for the appointment of provisional liquidators to enable the rescue of a company where it is just to do so. Having reviewed the authorities, the Court considered the matters which the Court should have regard to:

- the express wishes of the creditors;
- whether the refinancing is likely to be more beneficial than a winding up order;
- there is a real prospect of refinancing and/or sale as a going concern being effected for the benefit of the general body of creditors; and
- the considered views of the board as the best way forward⁶².

If S&C enters into the provisional liquidation process under Cayman law, upon a successful restructure, S&C would not be wound up and will continue as a going concern. However, if an agreement cannot be reached with S&C’s creditors, then a winding-up order will be made, and S&C will be dissolved.

4(f)

The Rackham family may continue to play a part in S&C provided that the Grand Court appoints PLs on a “soft touch” basis. In a ‘soft touch’ liquidation⁶³, the directors of the S&C remain in day-to-day control of the company. The extent of the directors’ powers, as well as the powers of the PLs, will be provided for in the Order appointing the PLs. It should be noted, however, that if the creditors of S&C are of the view that there has been mismanagement of the company and/or dissipation of the company’s assets – it is likely the Grand Court would appoint PLs and displace the current directors of S&C⁶⁴.

Commented [BT22]: 1 mark

4(g)

If S&C’s scheme has the requisite support of the creditors (over 50% of the creditors representing at least 75% in value⁶⁵), the scheme must be presented to the Grand Court for approval.

Commented [BT23]: 3 marks

(b) execution of other process issued on a judgment, decree or order obtained in the Court in favour of any creditor at law or in equity in any proceedings instituted by such creditor against the company, is returned unsatisfied in whole or in part; or (c) it is proved to the satisfaction of the Court that the company is unable to pay its debts.”

⁶² At [36]–[37]

⁶³ Module at [6.5.2.4]

⁶⁴ Cayman Restructuring Toolkit: Exploring the Flexible Restructuring Options on Offer in the Cayman Islands

⁶⁵ S. 86(2) CA (Revision 2020)

The principles to be applied by the Grand Court considering an application to sanction a scheme were recently reviewed and considered by Doyle J in *Bestway Global Holdings Inc* (FSD 208 of 2021 – unreported). In *Bestway*, the Grand Court sanctioned the scheme, being satisfied that:

- “The proposed scheme was a scheme of arrangement within the meaning of s.86 of the CA (Revision 2020) – noting *Re SIIC Medical Science and Technology Group Ltd 2003*; *Euro Bank Corporation (In Liquidation) 2003 CILR 205*;
- The scheme document provided all the material information reasonably required to enable the scheme shareholders to come to an informed view on the merits of the scheme (as required by Order 102 rule 21(4)(e) of the Grand Court Rules, Practice Direction No 2 of 2010 at [3.7] and *Re XL Capital Limited 2010 Vol 1 CILR 52*.
- The Court meeting was properly held, and the statutory majorities were achieved;
- There was no reason to believe that the views of the overwhelming majority of those who voted in favour of the scheme did not fairly represent the views of the scheme shareholders as a whole, that they were not acting *bona fide*, or that they were subject to coercion;
- The arrangement scheme was fair because an intelligent and honest person acting in respect of his relevant interest might reasonably approve it. Those voting are the best judges of their own commercial interest and reasonableness of the terms of the scheme of arrangement. Being fully informed, an overwhelming majority had voted in favour of the scheme at the Court meeting. In commercial matters, members and creditors are generally much better judges of their own interest than the courts; and
- There was no good reason for the court to exercise its residual discretion not to sanction the scheme. The Court should give due recognition to the commercial judgment of others directly involved in the scheme and that the details of the scheme are not a matter for the court provided the scheme as a whole is found to be fair⁶⁶.”

*** End of Assessment ***

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⁶⁶ *Bestway Global Holdings Inc: A Summary of the Principles Applied When Considering Applications For Schemes of Arrangement and Capital Reductions: Ms Sarah McLennan.*