



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: 202223-336.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 2023. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2023. 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 9 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 an application for a restructuring officer is filed:

- (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]: Incorrect. Answer was (a)

Question 1.2

Which of the following is not available to a debtor company in the Cayman Islands?

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

Commented [BT2]: Incorrect. Answer was (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.***

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.***

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.***

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.

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.

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.

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.

Question 1.10

Select the correct answer.

In order for a proposed creditor 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 [BT3]: 8/10

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?

Mortgages or charges over aircraft, ships and legal mortgages over property, (but not equitable mortgages) must be registered on the Shipping, Aircraft or Land Registries. Charges can also be registered over motor vehicles and intellectual property.

When a security is registered it is deemed that third parties have notice of the security and that any acquisition of the asset will be subject to the secured creditor's interest. Registration gives the secured creditor priority over unsecured and non-registered creditors.

There is no regime that permits or requires the registration of a security over other assets. Section 54 of the Companies Act does require companies to maintain a register of mortgages and charges but this does not create a priority for the creditor.

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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?

The Grand Court has the power to assist foreign proceedings under Part XVII of the Cayman Islands Companies Act (the "Act"). The foreign representative must make an application to the Court and under section 241 the Court may make orders in support of the foreign proceedings. When considering whether to make an order the Court will look at matters that will assist in an economic and efficient administration of the estate. The matters list in section 242 are:

- *The just treatment of creditors and stakeholders*
- *The prevention of any unfair treatment of Cayman Islands (the "Islands") creditors*
- *The prevention of dispositions of the debtor's property that are fraudulent or preferential*
- *The distribution to creditors in the priorities set out in Part V of the Act*
- *The recognition and enforcement of the interests of secured creditors*
- *Foreign taxes, fine and penalties will not be enforced by the Grand Court*
- *The mutual recognition and co-operation of the laws and customs of other nations (comity)*

Commented [BT5]: 4 marks

Where the foreign company has a local branch and is therefore registered in the Islands under Part IX of the Act, the Court must first consider whether to make a winding up order against that branch.

Question 2.3 [maximum 3 marks]

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

There is a statutory regime for the recognition of foreign judgements in the Foreign Judgements Reciprocal Enforcement Act (1996 Revision) (the "Reciprocal Act"). The judgement creditor can apply to register the judgement in the Islands under section 4 of the Reciprocal Act and Order 71 of the Grand Court Rules ("GCR"). If accepted the judgement has the same effect and force as if it had been made by the Grand Court.

However the Islands have not entered into any treaties for reciprocal recognition and the provisions of the Reciprocal Act have only been extended to the Superior Courts of Australia and its External Territories.

Commented [BT6]: Common law? 1.5 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 on trading the company while it is insolvent, directors must carefully consider their actions and ensure that act in the best interest of the company and its creditors.

The court appointed Official Liquidator ("OL") can pursue claims against directors if they have failed in their fiduciary duties. That is to act Bona Fides (sincerely in the belief) in the best interest of the company, using their powers for the proper purpose as set out in the memorandum & articles and without conflict of interest or fettered discretion.

The directors' primary duty is to the company but when a company becomes insolvent or potentially insolvent, the directors must also have regard to the creditors' interests. In Prospect Properties v McNeill (1990-91 CILR 171) the court held that the circumstances of the company and the consequences of director's actions "made it a vital part of the directors' duty to the company to consider the interests of its creditors."

The articles of association will tend to have a clause indemnifying the directors against losses but they can be disqualified from this indemnification. In Prospect Properties v McNeill the court also found the directors guilty of wilful neglect or default in their duty and stated that they could not claim the protection of the indemnification. The court made an award against the directors to put the company back into the position it would have been if their actions had not caused the wrong and that the sum be paid to the company with interest.

Fraudulent trading on the other hand is covered by the Act in section 147. If, in the course of winding up a company, it appears to the liquidator that any company business may have been carried out with the intention to defraud creditors he may apply to the court to declare that anyone knowingly carrying out the fraudulent business must make contributions to the company's assets.

There are other courses of action the liquidator can take to "claw back" assets (or at least their value) that were not dealt with in the best interests of the company or its creditors and those are avoidable property dispositions, voidable preferences and dispositions made at under value.

When a winding up order has been made, any dispositions of property, transfer of shares or changes in the members' status are void under section 99 of the Act, if made after the commencement of the winding up. Except for certain circumstances listed in section 100, that section states that the commencement of the winding up will be the time of the presentation of the petition. This section will therefore not apply for voluntary liquidations where a petition has not also been presented.

The Court may order the transaction to not be void but this is unlikely unless the company can show it was solvent, it was a reasonable action to take or there is a benefit to the company and its creditors. In the matter of Fortuna Development Corporation (CILR 533), before granting a validation order, the court had to be satisfied that the directors had the powers to make the disposition, they could show they believed the transaction to be necessary, they had acted in good faith and that the decision for the transaction and the associated terms were reasonable.

Voidable preferences are transactions that the company entered into within 6 months prior to the commencement of the liquidation, at a time when it was insolvent (or became insolvent because of the transaction) and done with an intention of preferring the creditor (putting it in a better position than it would have been otherwise).

Section 145 of the Act states that if the transaction is shown to meet the above tests then it shall be invalid. It also says that if the transaction is to a related party then it is deemed to have been made with the intention of preferring the creditor.

*The intention to prefer can often be a difficult one to show but in *Weaving Macro Fixed Income Fund Ltd* the Islands Court of Appeal and later the Judicial Committee of the Privy Council concluded that the emails from the Company's director to the creditor showed clear intent of a preference. The courts also considered in detail the timing test and the solvency test and found the transaction to be both within the 6 months and that the company was insolvent at the time. The judgement against the directors awarded the company UD\$111m.*

Dispositions at undervalue are ones that have been made for no consideration or for a value significantly lower than the property's value and with a wilful intent to defraud. The transaction shall be void on the application of the Official Liquidator under section

146, the application must be made within 6 years of the disposition and the burden of establishing the intent to defraud is on the Official Liquidator.

The voluntary liquidator, Official Liquidator, or a creditor may also apply to the Court to declare that a person, who was consciously involved in company business carried out with the intention to defraud, be liable to make contributions to the company's assets. There is no time limitation on this offence.

Prior to liquidation the creditors themselves could also apply to court for an order to take control or seize goods or land of the debtor by execution or attachment. The creditor will only be entitled to retain the benefit from either if the action is completed before the commencement of the winding up. Section 144 of the Act defines what completed means for execution against goods, securities or land and for attachment of a debt. For the purposes of that section the commencement of a voluntary winding up is the date the creditor receives notice of the meeting to resolve to wind up the company and that the creditor could apply to the court to retain the benefit over the liquidator if completion had not occurred.

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Question 3.2 [maximum 6 marks]

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

Receivers do have a role to play in an Islands insolvency scenario; that of the insolvency of one or more portfolios of a Segregated Portfolio Company (an "SPC"). Under section 224 of the Act the Court may appoint a receiver to manage the business and assets of the portfolio if it is satisfied that:

- The portfolio assets are (or are likely) to be insufficient to discharge it's creditors' claims,**
- The receivership order will achieve the orderly closing down of the portfolio's business and the distribution of it's assets to it's rightful creditors or stakeholders, and**
- There is no current winding up of the SPC.**

Under section 226 the receiver shall have all the powers of the directors of the portfolio and may do all things necessary to achieve the orderly closing down and the distribution.

The receivership order shall direct that the purpose of the management by a receiver is to close down the portfolio's business in an orderly manner and to distribute the assets to those entitled to receive them.

The order cannot be made if the portfolio is already in winding up and ceases to have effect upon the commencement of winding up. The company can only resolve to voluntarily wind up the portfolio subject to a receivership order with the permission of

the court. The order can also be discharged by order of the Court if its purpose has been achieved, substantially achieved or it is shown to the Court that it is unachievable.

Receivers can also be appointed by a secured creditor and without the Court's involvement if the charge document granting the security provides for the appointment. The charge document will also set out the powers of the receiver who will owe his duty to the appointing creditor. The powers will normally include the right to sell the charged property and repay the debt due to the creditor.

Where the security is a floating charge, section 141 allows for the preferential creditors (as listed in Schedule 2 of the Act) to be paid in priority of the secured creditor where the company's other assets are insufficient to meet the preferential claims in full.

The GCR also allows for the appointment of receivers. Order 30 allows for the application to appoint a receiver and the duties of that receiver. Order 45 states that one of the means of enforcing a judgement or order for money is the appointment of a receiver. And Order 51 covers the appointment of a receiver by way of equitable execution with the application of that appointment being governed by Order 30.

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

Vegan Patty Inc (VP) is a company registered in the Cayman Islands. It operates a fleet of party boats cross central America and the Caribbean. It was founded by the wealthy Rackham family over 40 years ago. The family continues to own and manage the business.

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

VP has only managed to stay afloat for the past three years with the assistance of a very large loan from Blue Iguana Treasure Bank (BITB). BITB has lent VP USD 300 million (USD 180 million of which is secured by a mortgage over four of VP's largest party boats). The loan facility has now been exhausted. VP has also fallen behind on the monthly repayments to BITB.

This year, the tourism market picked up again; however, VP 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 rum it needs to keep the tourist customers suitably refreshed.

To make matters worse, VP commissioned Johnson & Boris Ltd (JoBo) to build seven more oversized party boats only a few months before the pandemic struck. VP 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 VP must pay damages of USD 50 million to JoBo within 45 days. VP 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 BITB take to protect its interests?**
- (b) What action can JoBo take to protect its interests?**
- (c) What action can the unpaid employees take against VP?**
- (d) Does the Cayman Islands Court have jurisdiction over VP?**
- (e) Is there a legal route via which VP can protect itself and seek to restructure?**
- (f) Following on from (e) above, can the Rackham family continue play a part in running VP during any restructuring process?**
- (g) What factors will the Cayman Islands court take into consideration before approving any proposed restructuring?**

(a) Under the mortgage that BITB holds over the four largest party boats it could take possession of the boats and exercise its right to sell or may appoint a receiver to do this on its behalf. Any shortfall following the sale will rank as an unsecured debt in any subsequent insolvency proceedings. The mortgage should be registered on the Cayman Islands Shipping Registry which has the effect of third parties being deemed to have notice of the mortgage and ensures the priority of the secured debt. Although the lack of registration may not render the security void, I would be advising BITB to ensure that registration has been completed in order to avoid any risk that it may not be bidding on VP or that a third party could purchase one or more of the boats free of the security or acquire a higher ranking security over the boats.

(b) The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention") was extended to the Islands by the UK government in 1980 and has been embraced by the jurisdiction as an efficient and cost-effective alternative to legislation. Domestic effect of the New York Convention is given by the Arbitration Law (2012 revision) (the "AL") and the Foreign Arbitral Awards Enforcement Law (1997 Revision) (the "FAAEL"). JoBo could apply to the Court under section 72 of the AL to have the arbitration agreement enforced in the Islands in the same manner as a judgement or order of the Court. Section 6 of the FAAEL sets out the evidence JoBo will be required

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to produce, namely the arbitration agreement and award, and section 7 set out the very narrow set of circumstances which may allow the enforcement to be refused. JoBo will then have to serve on VP the order giving leave to enforce the award and allow them 14 days to apply to set it aside, following which (assuming it is not set aside) JoBo can enforce the requirements set out in the arbitration award. JoBo will want to make sure that completion of the enforcement (as described under section 144 of the Act) by way of seizure and sale of the goods is carried out before the commencement of any liquidation.

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(c) As creditors, the employees could petition for the winding up of VP under section 94 of the Act and Order 3 of the Company Winding Up Rules (the "CWR"). They may also have labour protections in the jurisdiction they are working. If the company goes into liquidation via any route the employees will have priority over other creditors as laid out in schedule 2 of the Act. This right of priority is regardless of where the employee of the company is working and covers salaries, wages and gratuities accrued over the 4 months prior to the commencement of the winding up. It also covers any amount due by the company for medical health insurance premiums and pension fund contributions. The employment contracts may be terminated as a consequence of the liquidation and if this happens any sum due for severance pay and earned vacation leave are also preferred debts. They may also claim as ordinary creditors for any sums due over & above the preferred debts.

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(d) Under section 91 of the Act the Court has jurisdiction over companies registered under the Act, whether incorporated in the Islands or under any other law. VP is registered in the Islands so the Court has jurisdiction over the company.

Commented [BT12]: 1.5

(e) Since 30 August 2022 new legislation came into force that would allow VP to petition for the appointment of a Restructuring Officer ("RO") on the grounds that it is or likely to become unable to pay its debts and it intends a restructure. Upon the filing of the petition an automatic stay of proceedings is triggered under section 91G of the Act which would protect the company from actions against it, including those in foreign countries, without leave of the court. If VP were particularly concerned over the urgency of the situation they could apply for an Interim RO to be appointed under section 91C. The powers of the RO, interim or otherwise, are set out in the term of the order of appointment but will not affect the rights of a secured creditor to enforce their security. Following the appointment of the RO the company can use the moratorium to give them time to propose a compromise or arrangement with the creditors or classes of creditors under section 86 and 91I of the Act.

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(f) Under section 91B (5) (b) the order appointing the RO will also set out the manner and extent to which the RO's powers and functions will affect the directors' powers and functions so it could be possible that the Rackham family could remain involved in running VP in some capacity allowed by the Court. It is expected that the Court make the same considerations on the directors' remaining powers and functions as they did under the restructuring proposals made under the appointment of provision liquidators.

Commented [BT14]: 1

(g) Practice Direction 2 of 2010 covers what the Court will consider in Schemes of Arrangement and Compromise under section 86 of the Act and Order 102 of the GCR covers applications under the Act. The court will consider:

- a. Whether it is appropriate to convene meetings of creditors and, if so, the composition of the creditor classes*
- b. Any potential jurisdictional and other issues that may cause the Court to refuse the sanction of the scheme*
- c. Whether the time and place proposed for the meetings of creditors allows them sufficient time to consider the scheme documentation and make an informed decision*

At the hearing of the petition where the results of the creditors' meeting votes are reported to the Court the Court will also consider any matters raised by those who voted on the scheme.

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* End of Assessment *

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