



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 5A

BERMUDA

This is the summative (formal) assessment for Module 5A ***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 5A. ***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.assessment5A]. An example would be something along the following lines: 202223-336.assessment5A. 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 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

When is a Bermuda company deemed to be unable to pay its debts under section 161 and section 162 of the Companies Act 1981?

- (a) Only when it is balance sheet insolvent.
- (b) Only when it is cash flow insolvent.
- (c) When it is balance sheet insolvent and cash flow insolvent.
- (d) When it is either balance sheet insolvent, or cash flow insolvent, or a valid statutory demand has not been satisfied within a period of three weeks after service on the company's registered office, or if a judgment in favour of a creditor remains unsatisfied.**

Correct

Question 1.2

Who may appoint a provisional liquidator over a Bermuda company?

- (a) A secured creditor.
- (b) A contributory.
- (c) The company itself (whether acting by its directors or its shareholders).
- (d) The Supreme Court of Bermuda.**

Correct

Question 1.3

In what order are the following paid in a compulsory liquidation under Bermuda law?

- (i) Preferential creditors.**
- (ii) Unsecured creditors.**
- (iii) Costs and expenses of the liquidation procedure.**
- (iv) Floating charge holders.**

Incorrect

Choose the correct answer:

- (a) Order (i), (ii), (iii) and (iv).**
- (b) Order (iii), (iv), (i) and (ii).**
- (c) Order (iii), (i), (iv) and (ii).**
- (d) Order (i), (iii), (iv) and (ii).**

Correct

Question 1.4

What percentage of unsecured creditors must vote in favour of a creditors' scheme of arrangement for it to be approved?

- (a) Over 50% in value.**
- (b) 50% or more in value.**
- (c) Over 75% in value.**
- (d) A majority of each class of creditors present and voting, representing 75% or more in value.**

Correct

Question 1.5

What is the clawback period for fraudulent preferences under section 237 of the Companies Act 1981?

- (a) Two years.**

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(b) One month.

(c) Twelve months.

(d) Six months.

Correct

Question 1.6

What types of transactions are reviewable in the event of an insolvent liquidation?

(a) Only fraudulent conveyances.

(b) Only floating charges.

(c) Only post-petition dispositions.

(d) All of the above.

Correct

Question 1.7

How many insurance policyholders are required to present a petition for the winding-up of an insolvent insurance company under section 34 of the Insurance Act 1978?

(a) At least five.

(b) One is sufficient.

(c) At least 10 or more owning policies of an aggregate value of not less than BMD 50,000.

(d) At least 10.

Correct

Question 1.8

Where do secured creditors rank in a liquidation?

(a) Behind unsecured creditors.

(b) Behind preferential creditors.

(c) Behind the costs and expenses of liquidation.

(d) In priority to all other creditors, since they can enforce their security outside of the liquidation.

Correct

Question 1.9

Summary proceedings against a company's directors for breach of duty (or misfeasance) may be brought by a liquidator under the following provision of the Companies Act 1981:

(a) Section 237 of the Companies Act 1981.

(b) Section 238 of the Companies Act 1981.

(c) Section 247 of the Companies Act 1981.

(d) Section 158 of the Companies Act 1981.

Correct

Question 1.10

What is a segregated account representative of an insolvent Segregated Accounts Company required to do under section 10 of the Segregated Accounts Companies Act 2000?

(a) Resign immediately.

(b) File a Suspicious Transaction Report forthwith.

(c) Make a written report to the Registrar of Companies within 30 days of reaching the view that there is a reasonable likelihood of a segregated account or the general account becoming insolvent.

(d) Notify the directors, creditors and account owners within 28 days.

Correct

9 out of 10

QUESTION 2 (direct questions) [10 marks in total]

Question 2.1 [maximum 4 marks]

In what circumstances may be a provisional liquidator be appointed?

Under s 170(2) of the Bermuda Companies Act 1981 (the "CA"), the court may, on the presentation of a winding-up petition or at any time thereafter and before the first appointment of a liquidator, appoint a provisional liquidator who may be the Official Receiver or any other fit person.

A provisional liquidator can be appointed prior to the final hearing of a compulsory winding-up petition if there is at least a good prima facie case for saying that a winding-up order will be made. (Re Stewardship Credit Fund Ltd [2008] Bda LR 67 ("Re Stewardship") at [35], citing with approval the case of Discover Reinsurance Company v PEG Reinsurance Co Ltd [2006] Bda LR 88, which in turn quoted the English position set out in Re Highfield Commodities Ltd [1984] 3 All ER 884 at 892-893).

Once that hurdle has been cleared, the court must consider whether in the circumstances of the case, it is right that provisional liquidators should be appointed. In this regard, s 170 of the CA does not restrict the power of the court to appoint provisional liquidators to certain category of cases (Re Stewardship at [36]).

The appointment of a provisional liquidator would be appropriate where: (a) there is a risk of dissipation of the company's assets between the presentation of a winding-up petition and the final hearing of the winding-up petition; or (b) there is a need for independent supervision and control of the company, for instance, where a restructuring is capable of being achieved under the supervision of an independent court officer with the benefit of a stay of other legal proceedings (since, pursuant to s 167(4) of the CA, when a winding-up order has been made or a provisional liquidator has been appointed, no action or proceeding shall be proceeded with or commenced against the company except by leave of the court and subject to such terms as the court may impose).

Correct - 4 marks

Question 2.2 [maximum 2 marks]

When can rights of set-off be exercised after the commencement of a liquidation of a Bermuda company?

Rights of set-off can only be exercised after the commencement of a liquidation of a Bermuda company if: (a) the debts giving rise to the set-off were incurred prior to the commencement of liquidation and have crystallised as monetary payment liabilities; (b) the transaction giving rise to the debts was not a fraudulent preference or a fraudulent conveyance; or (c) the dealings between the parties were mutual (i.e, the parties giving rise to the debt are identical to the parties giving rise to the credit, and the parties have contracted with each other in the same capacity).

Correct - 2 marks

Question 2.3 [maximum 4 marks]

Describe three possible ways of taking security over assets under Bermuda law.

Three possible methods of taking security over assets under Bermuda Law include: (1) mortgages; (2) charges; and (3) pledges.

Mortgages may either be legal or equitable. In a legal mortgage, legal title in the debtor's property is transferred to the creditor as security for a debt. The debtor retains possession of the mortgaged property but only regains legal title upon payment and satisfaction of the debt and reconveyance of legal title by the creditor to the debtor. Conversely, in an equitable mortgage, the debtor retains legal title to, and possession of, the mortgaged property but transfers the beneficial interest in the mortgaged property to the creditor. However, an equitable mortgage does not take priority over a third party who has acquired legal title to the mortgaged property in good faith and for value, without notice of the equitable creditor's beneficial interest.

Charges may either be fixed or floating. In the case of fixed charges, creditors take a fixed charge over property that does not result in legal or beneficial ownership being transferred to the creditor, but are given a right to take possession of the property with a right of sale in the event of a default by the debtor. Upon exercise of the power of sale, the proceeds may be applied by the creditor towards payment of the debt in priority to and without reference to other unsecured creditors. Additionally, the debtor cannot deal with property subject to a fixed charge without the consent of the creditor. As for floating charges, the creditor is given a charge not over a particular, but which "floats" over a variety of assets. The debtor can sell or dispose of property subject to a floating charge without the creditor's consent. In the event of default by the debtor, the floating charge will "crystallise" and convert into a fixed charge that attaches to specific assets remaining at that date. Property secured by a floating charge forms part of the debtor's general assets in the event of the debtor's insolvency.

In the case of a pledge, the creditor takes actual or constructive delivery or possession of the debtor's assets until the debt is repaid or discharged.

Correct - 4 marks

10 out of 10

QUESTION 3 (essay-type question) [15 marks]

Question 3.1 [maximum 8 marks]

Write a brief essay on the basis upon which foreign liquidators are granted recognition and assistance in Bermuda. Also consider the circumstances in which foreign liquidators might not be granted recognition and assistance.

*Although Bermuda has not statutorily implemented the UNCITRAL Model Law on Cross-Border Insolvency, the Supreme Court of Bermuda has confirmed, following the Privy Council decision in *Cambridge Gas Transportation Corp v Navigator Holdings plc* [2007] 1 AC 508 that as a matter of common law, the Supreme Court of Bermuda may recognise liquidators appointed by the foreign court of the debtor-company's domicile and the effects of a winding-up order made by that foreign court. The basis of the Bermudian courts' common law power to grant recognition and assistance foreign liquidators has been discussed in two judgments of the Privy Council, on appeal from the Court of Appeal of Bermuda, in *Singularis Holdings Limited v PricewaterhouseCoopers* [2015] 2 WLR 971; [2014] UKPC 36 ("*Singularis*") and *PricewaterhouseCoopers v Saad Investments Company Limited* [2014] 1 WLR 4482; [2014] UKPC 35.*

*In *Singularis*, Lord Collins of Maplesbury of the Privy Council observed that there is a principle of the common law that the court has the power to recognise and grant assistance to foreign insolvency proceedings. Moreover, that power is primarily exercised through the existing powers of the court, and can be extended or developed from existing powers through the traditional judicial law-making techniques of the common law. Furthermore, the limited application of legislation by analogy does not allow the judiciary to extend the scope of insolvency legislation to cases where it does not apply. Finally, those powers do not extend to the application, by analogy "as if" the foreign insolvency were a domestic insolvency, of statutory powers which do not actually apply in the instant case: see *Singularis* at [38].*

In gist, the Bermuda Court is likely to recognise the winding-up orders of foreign courts, and to assist foreign liquidators to the fullest extent possible, where the following are satisfied:

- (1) There must be a "sufficient connection" between the foreign court's jurisdiction and the foreign debtor-company making the foreign jurisdiction the most appropriate or convenient jurisdiction to have made an order for the winding-up of the company and the appointment of foreign liquidators.*
- (2) There are documents, assets or liabilities of the foreign debtor-company within the jurisdiction of Bermuda; the foreign company has conducted business or operations within, or from the jurisdiction of Bermuda, whether directly or by agents or by branches; the foreign debtor-company has former directors, officers, managers, agents or service providers within the jurisdiction of Bermuda; and/or the foreign debtor-company properly needs to be involved in litigation or arbitration within the jurisdiction of Bermuda.*
- (3) There is no public policy under Bermuda that is contrary to such recognition and assistance. For instance, there cannot be unfairness or prejudice to local Bermudian creditors.*

However, the question of how far it is appropriate to develop the common law in order to assist foreign liquidations depends on the facts of each case and the nature of the power that the Bermuda Court is being asked to exercise. For instance, the Lord Sumption of the Privy Council in *Singularis* held that there is a power at common law to assist a foreign court of insolvency jurisdiction by ordering the production of information in oral or documentary form which is necessary for the administration of a foreign winding up. The Privy Council cautioned against encouraging the “promiscuous creation of other common law powers to compel the production of information”, observing that the limits of such a power are implicit in the reasons for recognising its existence. Such a power is only available to assist the officers of a foreign court of insolvency jurisdiction or equivalent public officers, and would not be available to assist a voluntary winding up, which is essentially a private arrangement. Moreover, the Bermuda Court’s power to assist exists for the purpose of enabling foreign courts to surmount the problems posed for a worldwide winding up of the company’s affairs by the territorial limits of each court’s powers. It is not therefore available to enable foreign liquidators to do something which they could not do even under the law by which they were appointed. Thirdly, it is available only when it is necessary for the performance of the liquidator’s functions. Finally, the power is subject to the limitation that any assistance must be consistent with the substantive law and public policy of Bermuda, as mentioned above: see *Singularis* at [25].

Foreign liquidators may also not be granted assistance where no active assistance has yet been requested, and any such potential assistance would probably have been refused, in light of pending litigation in the foreign jurisdiction and other information-gathering mechanisms available to the parties.

In the Bermuda Supreme Court case of *Stephen John Hunt v Transworld Payment Solutions UK Limited* [2020] SC Bda 14 Com (*Transworld*), the court declined to grant recognition in Bermuda of a liquidator’s appointment pursuant to a winding up order made in the High Court of England and Wales. Among other reasons, the court observed that common law powers to recognise foreign liquidators cannot be used to obtain material for use in actual or anticipated foreign litigation (at [36] and [44], referring to *Singularis* at [25]). The Bermuda Supreme Court observed that it was clear that the sole purpose of the application for recognition was to clothe the liquidator with the authority of the Bermuda court in order obtain information and evidence for use in contemplated proceedings in England (*Transworld* at [43]). The use of a recognition order to obtain evidence to be used in contemplated foreign proceedings was held to be an illegitimate use of the procedure (*Transworld* at [44]).

Correct - a good and complete answer - 8 marks

Question 3.2 [maximum 7 marks]

Write a brief essay on the circumstances in which a foreign court judgment will not be registered or enforced in Bermuda. Also consider and address the question as to

whether a foreign court-sanctioned scheme of arrangement might be registered or enforced in Bermuda.

Under the common law generally, a foreign money judgment will not be recognised and enforced as a debt against the judgment debtor where any of the following applies, and the registration may thus be set aside:

- (1) The foreign judgment was not final and conclusive in the foreign court;*
- (2) the foreign judgment was not obtained in a court of law which had jurisdiction over the judgment debtor;*
- (3) the foreign judgment was obtained by fraud;*
- (4) the foreign judgment was in respect of taxes, fines or penalties;*
- (5) the enforcement of the foreign judgment would contravene the public policy of Bermuda;*
- (6) the rules of natural justice were not observed in the foreign proceedings; and/or*
- (7) the foreign judgment conflicts with another prior, inconsistent judgment from another court with competent jurisdiction.*

*In relation to the fifth mentioned ground, ie, where the enforcement of the judgment would contravene the public policy of Bermuda, an exception arises in relation to the Judgments (Reciprocal Enforcement) Act 1958 (the "REA"). In particular, the Supreme Court of Bermuda in *Masri v Consolidated Contractors International Company* [2009] Bda LR 12 that despite the wording of Rule 12 of the Judgments (Reciprocal Enforcement) Rules 1976, the Supreme Court of Bermuda is not entitled to set aside the registration of a foreign judgment merely on the grounds that it is not "just or convenient to enforce the foreign judgment in Bermuda, or on "public policy" grounds.*

Furthermore, the registration of a foreign judgment may be set aside if the Supreme Court of Bermuda is satisfied that the matter in dispute in the proceedings giving rise to the registered judgment had, previously to the date of such judgment, been the subject of a final and conclusive judgment by a court having jurisdiction in the matter.

Additionally, a foreign judgment which has been registered under the REA may be set aside on the application of any party against whom a registered judgment may be enforced, if the Bermuda Supreme Court is satisfied of any of the following:

- (1) the foreign judgment is not covered by the REA or was registered in contravention of the REA;*
- (2) the foreign court had no jurisdiction in the circumstances of the case;*
- (3) the debtor did not receive notice of the proceedings in the foreign jurisdiction in sufficient time to enable him to defend the proceedings and thus did not appear;*
- (4) the foreign judgment was obtained by fraud;*
- (5) the rights under the foreign judgment are not vested in the person by whom the application for registration was made; and/or*

The Supreme Court of Bermuda has confirmed that the court has jurisdiction to recognise a foreign court-sanctioned scheme of arrangement. In *Re C&J Energy Services Ltd* [2017] Bda LR 22, the Bermuda Supreme Court summarised the legal position at [16], observing that the court may recognise and enforce (by way of a stay of proceedings or otherwise in accordance with local law) a foreign restructuring order extinguishing claims against an insolvent Bermudian company. However, the court may only properly do so as against parties who have submitted to the personal jurisdiction of the foreign court and/or as regards property which (by reason of its *situs*) is subject to the *in rem* jurisdiction of the foreign court. The Court has the common law power to assist a foreign insolvency court as much as it can unless there are good reasons for not doing so. In *Re Seadrill Limited* [2018] Bda LR 39, the Bermuda Supreme Court confirmed that the court had the jurisdiction to recognise a reorganisation plan under Chapter 11 of the United States Bankruptcy Code (at [12]). In *Re Energy XXI* [2016] Bda LR 90, the Bermuda Supreme Court similarly granted recognition of a restructuring plan sanctioned by the court in Texas. The court observed at [27] that the recognition order being sought in Bermuda was being sought on the basis of traditional recognition principles against a background of parallel insolvency proceedings in which there was no or no serious challenge to the proposition that the US proceedings should be regarded as the primary proceedings.

It is, however, uncertain whether a foreign scheme of arrangement or related procedure can be recognised and enforced in Bermuda as a matter of common law, in the absence of a local scheme of arrangement implemented in parallel. While the Supreme Court of Bermuda appears willing to recognise foreign court orders approving foreign schemes in the absence of opposition, it is unclear what the court's position is where there are contentions arising against the scheme.

In *Re C&J Energy Services Ltd* [2017] Bda LR 22, the Bermuda Supreme Court observed at [14] that doubts exist about the jurisdiction of the Bermuda court to recognise and assist foreign insolvency courts by implementing a foreign restructuring in relation to a Bermudian company without implementing a parallel scheme of arrangement under Bermudian law. A Bermuda scheme was observed to be the "safest means of avoiding dissenting creditors attempting an 'end run' on a foreign proceeding where they can successfully argue that they are not bound by the foreign court's orders".

Similarly, in *Re Energy XXI* [2016] Bda LR 90, the Bermuda Supreme Court observed at [10] that there is always a risk that a creditor or shareholder who is not party to or otherwise bound by the foreign restructuring proceeding might, absent a Bermudian parallel scheme, have standing to contend that the foreign court's order approving the foreign plan or scheme of arrangement ought not to be recognised as binding on the dissenting party under Bermudian law.

Correct - a good and complete - answer - 7 marks

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

Bercoffee Limited (the Company) was incorporated in 2019 as an exempt Bermuda company; as the parent company in a group of companies with a direct subsidiary incorporated in the British Virgin Islands; with indirect trading subsidiaries incorporated in the People's Republic of China (PRC); and with offices and a substantial business presence in Hong Kong. The Company's trading operations in the PRC involves coffee shops and other retail businesses associated with coffee and hot drinks.

The Company issued a number of bonds to creditors based in the United States (US) with the face value of USD 500 million, with a view to raising additional capital (by way of debt funding) to fund the expansion of its business activities in the PRC (which had previously been funded with the benefit of shareholders' capital contributions).

It was subsequently disclosed that the Company had fraudulently misrepresented its financial performance in the offering documents associated with the bonds, with the consequence that the US bondholders were entitled to demand immediate repayment by the Company of the sum of USD 500 million, even though that money had already been transferred to the Company's indirect subsidiaries in the PRC, and was incapable of being returned due to local currency control restrictions and associated Chinese legal issues.

The US bondholders served a statutory demand on the Company in Bermuda, demanding repayment of the sum of USD 500 million within 21 days.

The Company's directors decided, however, that it was in the best interests of Bercoffee Limited and its shareholders to not satisfy the statutory demand but to ignore it for the time being, having regard also to the Chinese legal position, and with a view to trading through the Company's financial difficulties.

The Company's directors subsequently borrowed an additional USD 50 million from its bank, Lendbank, which loan is secured by way of a floating charge against all of the Company's shares and the assets of its subsidiaries. Out of the USD 50 million received from Lendbank, Bercoffee Limited's directors immediately paid themselves a bonus of USD 20 million and they also paid a dividend to the Company's shareholders in the sum of USD 30 million.

The US bondholders only found out about these transactions two weeks later, through a report received from a disgruntled former employee of Bercoffee Limited.

Using the facts above, answer the questions that follow:

Question 4.1 [maximum 7 marks]

What actions could the US bondholders take in order to try to recover some or all of the sum of USD 500 million from the Company or other parties? Please consider (a) the

jurisdictions in which they could take such action, bearing in mind the potential need for enforcement; (b) the defendants against whom they could take such action; (c) the pros and cons of litigation as opposed to insolvency proceedings; and (d) the causes of action that may be available against the various potential defendants.

The US bondholders may commence winding up proceedings against the Company in the jurisdiction of Bermuda to recover some of the USD 500 million. Pursuant to s 161(e) of the Bermuda Companies Act 1981 (the "Companies Act"), a company may be compulsorily wound up by the court where the company is unable to pay its debts. Further, pursuant to s 162, a company is deemed unable to pay its debts for the purposes of s 161(e) if a creditor, by assignment or otherwise, to whom the company is indebted in a sum exceeding five hundred dollars then due has served on the company, by leaving it at the registered office of the company, a demand requiring the company to pay the sum so due and the company has for three weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor. In the present case, the Company would be liable to be compulsorily wound up since the US bondholders had served a statutory demand on the Company in Bermuda, demanding repayment of the sum of USD 500 million within 21 days, and the Company's directors decided not to satisfy the statutory demand.

Once the Company is placed into winding up, the liquidator may take the following actions which would increase the assets of the Company available for distribution to the Company's creditors, which includes the US bondholders.

*First, the liquidator may seek to enforce the winding up order obtained in Bermuda in other jurisdictions such as: (a) the PRC so as to prevent the Company from dissipating the USD 500 million which is currently held by its subsidiaries incorporated in the PRC; or (b) Hong Kong, where the Company has a business presence, to prevent the company from dissipating its other assets. In this respect, the Supreme Court of Bermuda has issued letters of request to foreign courts asking for foreign court recognition of, and assistance to, Bermudian liquidators of Bermudian companies. The jurisdiction to issue such letters of request has developed as a matter of common law and the court's inherent jurisdiction, since there is no Bermudian legislation or rules of court specifically governing the process. Provisional liquidators may also be granted recognition by the Hong Kong court (see *Re Hsin Chong Group Holdings* [2019] HKCFI 805). However, it is important to note that following the decision of the Privy Council in *PricewaterhouseCoopers v Saad Investments Company Limited* [2014] 1 WLR 4482; [2014] UKPC 35, it is clear that the Bermuda Supreme Court has no jurisdiction to wind up overseas companies that have not been granted a permit by the Minister of Finance to carry on business in Bermuda. Thus, the Bermuda Supreme Court cannot directly wind up the overseas subsidiaries or businesses of the Company in Hong Kong or China.*

Second, pursuant to s 239 of the Companies Act, where a company is being wound up, a floating charge on the undertaking or property of the company created within twelve

months of the commencement of the winding up shall, unless it is proved that the company immediately after the creation of the charge was solvent, be invalid, except to the amount of any cash paid to the company at the time of or subsequently to the creation of, and in consideration for, the charge, together with interest on that amount at the statutory rate fixed under the Interest and Credit Charges (Regulation) Act 1975. In the present case, the liquidator could apply to set aside the floating charge granted in favour of Lendbank over the Company's shares and the assets of its subsidiaries. If it can be established that: (a) the Company was insolvent after the creation of the floating charge; and (b) the floating charge was created within 12 months of the commencement of the Company's winding up, the liquidator would likely succeed in setting aside the floating charge.

Third, following the commencement of winding up proceedings, the liquidator may pursue the following claims against the directors of the Company.

Pursuant to s 246(1) of the Companies Act, if in the course of the winding up of a company it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the court, on the application of the Official Receiver, or the liquidator or any creditor or contributory of the company, may, if it thinks proper so to do, declare that any persons who were knowingly parties to the carrying on of the business in manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liability of the company as the court may direct. In the present case, the Company had fraudulently misrepresented its financial performance in the offering documents associated with the bonds issued to the US bondholders. Thus, it is likely that the directors may be held personally liable for the return of the USD 500 million to the US bondholders, having deliberately defrauded the US bondholders into purchasing the bonds. The advantage of relying on s 246(1) of the Companies Act is that there is no limit on the amounts that the directors may be held liable to repay to the US bondholders.

Next, pursuant to s 247(1) of the Companies Act, if in the course of winding up a company it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager or liquidator, or any officer of the company, has misapplied or retained or become liable or accountable for any money or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the court may, on the application of the Official Receiver, or of the liquidator, or of any creditor or contributor, examine the conduct of the promoter, director, manager, liquidator or officer, and compel him to repay or restore the money or property or any part thereof respectively with interest at such rate as the court thinks just, or to contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust as the court thinks just. In the present case, the directors had paid themselves a bonus of USD 20 million from the USD 50 million borrowed from Lendbank. This would constitute a misapplication of the assets of the Company since the company was, at that point in time, facing a statutory demand of USD 500 million from the US

bondholders and it is unclear if there is any basis for the payment of the bonus. The US bondholders may therefore seek the return of the USD 20 million paid to the directors as bonus.

Alternatively, the US bondholders may choose to commence litigation against the Company itself for claims in misrepresentation or fraud. The US bondholders may consider litigation against the directors personally as well. However, the disadvantage in commencing an action directly against the directors is that the directors may not have sufficient assets or funds to repay the entire sum of USD 500 million to the US bondholders. In particular, it may be argued that the directors have breached their fiduciary duties. Pursuant to s 54(1) of the Companies Act, a company shall not declare or pay a dividend or make a distribution out of contributed surplus, if there are reasonable grounds for believing that: (a) the company is, or would after the payment, be unable to pay its liabilities as they become due; or (b) the realisable value of the company's assets would thereby be less than its liabilities. In the present case, the directors had caused the company to declare a dividend of USD 30 million to the shareholders of the Company even though the company was facing a statutory demand of USD 500 million from the US bondholders. Accordingly, it is likely that the declaration of the dividend would be contrary to s 54 of the Companies Act. The US bondholders may thus argue that the directors' declaration of the dividends in breach of s 54 of the Companies Act constitutes a breach of the directors' fiduciary duties, and seek equitable compensation on that basis. However, it might be difficult for the US bondholders to show that they are the proper plaintiffs in such an action since the company would arguably be the rightful claimant in an action for breach of fiduciary duties.

There are several key disadvantages to commencing winding up proceedings against the Company (as opposed to litigation). In the absence of any facts to the contrary, it would appear that the US bondholders would be in the position of unsecured creditors. This is significant because the Company's directors had borrowed USD 50 million from Lendbank, which was secured by a floating charge against all of the Company's shares and the assets of its subsidiaries. Thus, Lendbank would rank higher in priority than the US bondholders in the Company's insolvency. Given that the USD 500 million had already been transferred to the Company's indirect subsidiaries in the PRC and is incapable of being returned due to local current control restrictions and Chinese legal issues, it is likely that the assets of the company would not be sufficient to repay the USD 50 million loan from Lendbank. Thus, it is likely that the sums that the US bondholders may recover as an unsecured creditor would not be substantial.

On the flipside, an advantage of commencing winding up proceedings against the Company is that pursuant to s 170(2) of the Companies Act, the court may appoint a provisional liquidator between the presentation of the winding-up petition and its final hearing. The appointment of a provisional liquidator would allow the US bondholders to expeditiously prevent the dissipation of the Company's assets in China

and/or Hong Kong in the interim period between the presentation of the winding up petition and the hearing of the petition.

On the whole, it is submitted that commencing insolvency proceedings against the Company would be more efficient than commencing litigation. That is because if the Company is unable to satisfy any judgment debt given to the US Bondholders in litigation, the Company would ultimately still go into insolvency proceedings. Thus, it would be faster and more cost-efficient to directly commence insolvency proceedings against the company.

Correct - a good and complete answer - 7 marks.

Question 4.2 [maximum 8 marks]

To what extent would it be open to Bercoffee Limited to try to take steps to restructure its debt obligations, and how and where could it do so? Consider whether it would be more appropriate to take steps before the Hong Kong courts, the Bermuda courts, or both and, if so, why? Also consider whether it would make any difference if the debt restructuring involved a “debt-for-equity” swap, (that is, if the US bondholders would be issued new shares in the Company in exchange for cancellation of their debt, with existing shareholders’ shares in the Company being cancelled).

Bercoffee Limited (the “Company”) may seek a scheme of arrangement before the Bermuda court. Pursuant to s 99(1) of the Bermuda Companies Act 1981 (the “Companies Act”), where a compromise or arrangement is proposed between a company and its creditors or any class of them, the court may, on the application of any creditor of the company, or, in the case of a company being wound up, of the liquidator, order a meeting of the creditors or class of creditors to be summoned in such manner as the court directs. Pursuant to s 99(2) of the Companies Act, if a majority in number representing three-fourths in value of the creditors or class of creditors present and voting either in person or by proxy at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall if sanctioned by the court, be binding on all the creditors or the class of creditors and also on the company or, in the case of a company in the course of being wound up, on the liquidator and contributories of the company.

The Company may also seek a scheme of arrangement in Hong Kong and apply to have it recognised by the Bermuda court. It is uncertain whether a foreign scheme of arrangement can be recognised and enforced in Bermuda as a matter of common law in the absence of a local scheme of arrangement implemented in parallel (*Re C&J Energy Services Ltd* [2017] Bda LR 22; *Re Energy XXI* [2016] Bda LR 90; *Re Seadrill Limited* [2018] Bda LR 39). In *Re Titan Petrochemicals Group* [2014] Bda LR 90, the Bermuda court observed that it often approves parallel schemes linking Bermuda and Hoing Kong. Therefore, it would be more appropriate to seek parallel schemes of arrangement in both Bermuda and Hong Kong.

Courts have emphasised in this regard that it is desirable for relative advantages and disadvantages, and potential costs and expenses, of parallel schemes of arrangement to be considered in light of the facts and circumstances of any particular restructuring, having regard to the rule in *Gibbs* (as formulated in the English Court of Appeal decision in *Antony Gibbs & Sons v La Societe et Commerciale de Metaux* (1890) LR 25 QBD 398). The Rule in *Gibbs* provides that unless a creditor submits to a foreign proceeding or debt restructuring, a foreign proceeding designed to bring about the discharge of a debtor's obligations will discharge only those liabilities governed by the law of the country in which that proceeding took place.

If the debt restructuring involves a debt-for-equity swap, it might not be open for the Company to implement parallel debt restructurings in Bermuda and Hong Kong due to the Rule in *Gibbs*. In particular, under the Rule in *Gibbs*, a debt can only be validly discharged under the provisions of its governing law, unless the relevant creditor(s) submits to a foreign debt restructuring.

In the presently contemplated scenario, a debt-for-equity swap would involve the issuance of new shares in the Company to the US Bondholders, in exchange for the cancellation of the Company's debts. There are two possibilities that follow.

- (a) First, if a debt restructuring involving a debt-for-equity swap is commenced in Bermuda, that debt restructuring would only validly discharge the Company's debts if the Company's debts are governed by Bermuda law. This is unless the creditors of the Company (*ie*, the US bondholders) submit to the Bermuda debt restructuring.
- (b) Second, if a debt restructuring involving a debt-for-equity swap is commenced in Hong Kong, that debt restructuring would only validly discharge the Company's debts if the Company's debts are governed by Hong Kong law. This is unless the US Bondholders submit to the Hong Kong debt restructuring.

Therefore, if the restructuring plan involved a debt-for-equity swap, it would be most practical to commence debt restructuring only in the jurisdiction whose laws govern the debt of the Company. However, parallel debt restructurings involving a debt-for-equity swap may nevertheless be commenced in both Bermuda and Hong Kong if the US Bondholder submit to the debt restructuring in the other jurisdiction whose laws do not govern the debt of the Company, as the case may be.

Correct - a good and complete answer - 8 marks.

Total: 49 out of 50 marks

* End of Assessment *