



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 - incomplete answer**

**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.**

(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**

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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**

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

Question 2.1 [maximum 4 marks]

**In what circumstances may a provisional liquidator be appointed?**



Under s 170(2) of the Companies Act 1981, the court may appoint a provisional liquidator between the presentation of a winding-up petition and its final hearing. The relevant test is that the applicant must "at least make out a good prima facie case that a winding-up order will be made" (*Re Stewardship Credit Arbitrage Fund Ltd* [2008] Bda LR 67 ("*SCAF*") at [36]). The Court then considers whether, in the circumstances of the case, it is "right" that a provisional liquidator should be appointed (*SCAF* at [36]).

The position in Bermuda is effectively identical to the position in England (*Discovery Reinsurance Company v PEG Reinsurance Co Ltd* [2006] Bda LR 88 at [17]), where the following dictum of Sir Robert Megarry (VC) in *Re Highfiled Commodities Ltd* [1984] 3 All ER 884 at 892-893 was affirmed (see also *SCAF* at [35]):

No doubt a provisional liquidator can properly be appointed if the company is obviously insolvent or the assets are in jeopardy but I do not think that the cases show that in no other case can a provisional liquidator be appointed over the company's objection. As the judge said, s 238 [of the English Companies Act 1948, which is the statutory equivalent of s 170(2) of the Companies Act 1981,] is in quite general terms. I can see no hint in it that it is to be restricted to certain categories of cases. The section confers on the court a discretionary power, and that power must obviously be exercised in a proper judicial manner. The exercise of that power may have serious consequences for the company, and so a need for the exercise of the power must overtop those consequences." [emphasis added]

The general rule, therefore, is that there are no strict categories of cases where the power to appoint provisional liquidators should be exercised, and the discretion remains broad.

Nonetheless, some circumstances where a provisional liquidator may (and have been) be appointed include where there is a risk of dissipation of assets (in which case, an urgent application may be made), or the need for independent supervision and control. For instance, the court in *SCAF* appointed provisional liquidators arising from the latter circumstance. Having found that there was a good prima facie case for the winding up order to be made against the subject, it noted at [80] that the company in question did not "[act] as one might expect a company in its position to act". This included failures to communicate a "highly critical development" to key investors in the company (at [80]), and having made poor decisions such as to "favour its own continued existence rather than the discharge of its obligations" to said key investors (at [84]). For this, and other reasons, Geoffrey Bell (acting as Puisne Judge) held at [86] that the company "need[ed] to be under the control of joint provisional liquidators who are officers of the Court, rather than under the control of the present board of directors."

**Correct**

Question 2.2 [maximum 2 marks]

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

*Section 37 of the Bankruptcy Act 1989 provides for mandatory set-offs in the event of a liquidation in Bermuda. However, set-off can only be exercised after the commencement of liquidation if (a) the debts giving rise to the set-off were incurred prior to the commencement of liquidation and have crystallized 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 (Guidance Text at p 11).*

Correct

Question 2.3 [maximum 4 marks]

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

*Generally, the exact nature and manner in which security is taken is subject to the terms of the relevant security documents; the nature of the property, and the nature of the debtor's interest. To name three forms of security (amongst others), security over assets may be taken by way of (a) legal mortgage; (b) equitable mortgage; and (c) fixed charges.*

*A creditor may take security over property by way of legal mortgage through the transfer of legal title of the debtor's property to the creditor as security for a debt. While the debtor remains in possession of the property, legal title will only be reconveyed to the debtor upon payment and satisfaction of the debt to the creditor.*

*Where an equitable mortgage is concerned, the debtor retains legal title to and possession of the property, but transfers the beneficial interest in the property to the creditor. Notably, an equitable mortgage does not take priority over third party who acquires, without notice of the creditor's beneficial interest, legal title to the property in good faith and for value.*

*Fixed charges give creditors the right to take possession of the property with a right of sale in the event of a default by the debtor. They do not result in the transfer of legal or beneficial ownership. Upon sale, the proceeds of sale may be applied by the creditor towards payment of the debt in priority to and without reference to other unsecured creditors. Depending on the precise terms of the parties' agreement, the debtor generally may not deal with any property subject to a fixed charge without the creditor's consent.*

*The creditor should also file details of the security (as well as either an original or certified copy of the security document) with the Registrar of Companies in Bermuda. The effect of registration is that these secured assets will have priority over any security interests which are not registered or which are subsequently registered in the Register of Charges. Further (and this is relevant in the case of equitable mortgages), registration in this manner provides constructive notice of the existence of the security to third parties.*

**Correct**

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.***

*The recognition and assistance of foreign liquidators take place under the common law in Bermuda. Unlike other jurisdictions such as the UK, Bermuda has not enacted local legislation incorporating the centre of main interest test set out in the UNCITRAL Model Law on Cross Border Insolvency, nor does Bermuda have any statutory analogue to Chapter 15 of the US's Bankruptcy Code, or the UK's Cross-Border Insolvency Regulations 2006. Notwithstanding this, the court has indicated its willingness to take into account all the circumstances of the case (including concepts such as the company's COMI) in addressing the question (*Re C&J Energy Services Ltd* [2017] Bda LR 22. Similarly, following the Privy Council decision *Cambridge Gas Transportation Corp v Navigator Holdings plc* [2007] 1 AC 508, it has been held that as a matter of common law, the Supreme Court of Bermuda may recognise liquidators appointed by the court of the company's domicile and the effects of a winding up order made by that court, and has a discretion pursuant to such recognition to assist the primary liquidation court by doing what ever it could have done in the case of a domestic insolvency.*

***The Bermuda Court is likely to recognise the winding-up orders of foreign courts and to assist foreign liquidators to the fullest extent in circumstances where:***

- (1) There is a "sufficient connection" between the foreign court's jurisdiction and the foreign company making it the most appropriate, or the "most convenient" jurisdiction to have made an order for the winding-up of the company and appointment of foreign liquidators;***
- (2) There are documents, assets, or liabilities of the foreign 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 company has former directors, officers, managers within the jurisdiction of Bermuda; and /or the foreign company properly needs to be involved in litigation or arbitration within the jurisdiction of Bermuda; and

(3) There is no public policy reason under Bermudian law to the contrary such as unfairness or prejudice to local Bermudian creditors.

Foreign liquidators should also pay heed to the Practice Directions issued by the Supreme Court of Bermuda, which have set out guidelines applicable to court-to-court communications in cross-border cases. This is because court-to-court cooperation is necessary in the event of parallel liquidations, which is oft the case with companies incorporated in Bermuda that engage in business activities in foreign jurisdictions.

In terms of the extent of the power of assistance by the Bermudan court, the general position is that the court is limited to granting assistance to the extent that such assistance is both available from the Bermuda court and the foreign Court, and consistent with public policy (*PwC v Saad* [2014] UKPC 35; *Singularis v PwC* [2014] UKPC 36).

Correct - 8 marks

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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.**

The starting point is to consider that the judgment of a foreign court has no direct legal effect in Bermuda (*Holborn Oil Company Ltd v Tesora Petroleum Corporation*, Civil Jurisdiction 1990: No 273, 20 August 1990). Instead, foreign judgments may be recognised in Bermuda pursuant to various statutory or common law rules. It would follow that, generally speaking, failure to apply the relevant rules would be one circumstance in which foreign court judgments would not be registered nor enforced. The applicable rules (which stem either from statute or common law) depend on the nature of the foreign judgment. For instance:

- The Judgments (Reciprocal Enforcement) Act 1958 (the "1958 Act") (and the regulations made thereunder) govern the registration and enforcement of final money judgments of superior courts in the UK and certain Commonwealth countries. Under the 1958 Act, a judgment rendered in the superior courts of the UK (and the commonwealth countries listed in Appendix II of the act) may be registered in Bermuda and given effect upon registration as though it were a judgment entered in Bermuda. Judgments of inferior courts cannot be

registered or enforced under the 1958 Act, even if they have been transferred to the relevant superior court ( *Crossborder Capital Ltd v Overseas Partners Re Ltd* 2[004] Bda LR 17). Further, the 1958 Act excludes the bringing of an action at common law upon a judgment capable of registration (see s 6 of the 1958 Act; *Young et al v GNI Fund Management (Bermuda) Limited* [2001] Bda LR 70 (" *Young*"); and the bullet point below). As such, one circumstance by which a foreign judgment will not be enforced may be where an application that could have been made under the 1958 Act was brought at common law (see the *Young* case).

- This is supplemented by common law rules which are applicable to the enforcement of final money judgments of foreign courts in the rest of the world. These judgments may be enforced by way of a separate action on the basis that the foreign judgment is treated as *evidence* of debt;
- The Maintenance Orders (Reciprocal Enforcement) Act 1974 (and the regulations made thereunder) govern the registration and enforcement of maintenance orders made by foreign courts of reciprocating countries;
- Statutory and common law rules applicable to the recognition of foreign judgments, either as a defence to a claim or as conclusive of an issue in the Bermuda proceedings;
- The Recognition of Divorces and Legal Separations Act, which apply to the recognition of divorces and legal separations; and
- Various other statutory and common law rules that apply to foreign arbitration awards, etc.

To elaborate on the 1958 Act (per bullet point 1), another circumstance where foreign judgments would not be registered or enforced (in a final sense) would be where an opponent successfully sets the registered judgment. A foreign judgment registered under the 1958 Act can be set aside on an application of the party against which judgment may be enforced. The grounds under which the Supreme Court must set the registration order aside are:

- Where the judgment was registered in contravention of the 1958 Act, or if it does not fall within the ambit of the act;
- Where the foreign court had no jurisdiction in the circumstances;
- Where the defendant did not receive notice of the proceedings in the foreign jurisdiction in sufficient time to enable him to defend proceedings and did not appear;
- It was obtained by fraud; and
- The rights under it are not vested in the person by whom the application for registration was made.

The Court may set the order aside if it is satisfied that the matter in dispute in the proceedings giving rise to the registered judgment had, prior to the date of judgment, been the subject of a final and conclusive judgment by a court having jurisdiction of the matter. However, the Court 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, or on public policy grounds (*Masri v Consolidated Contractors*

*International Company* [2009] Bda LR 12; despite the wording of rule 12 of the Judgments (Reciprocal Enforcement) Rules 1976).

To elaborate on the applicable common law rules (per bullet point 2), foreign money judgments will be recognised and enforced as a debt against the judgment debtor where:

- The judgment is final and conclusive in the foreign court;
- The judgment was obtained in a court of law which had jurisdiction over the judgment debtor;
- The judgment was not obtained by fraud;
- The judgment was not in respect of taxes, fines or penalties;
- The enforcement of the judgment would not contravene the public policy of Bermuda (save for in the case of the 1958 Act per *Masri*); and
- The rules of natural justice were observed in the foreign proceedings.

Conversely, where the above rules are not met, the foreign judgment may not be recognised. For instance, in *Laep Investments Ltd v Emerging Markets Special Situations 3 Ltd* [2015] CA (BDA) 10 Civ (Laep), the Bermuda Court of Appeal held that a stay order issued by the Brazilian courts meant that a Brazilian arbitration award was not final and conclusive for enforcements purposes, thus refusing to recognise the award.

#### Foreign Court-Sanctioned Scheme

In terms of whether a foreign scheme of arrangement may be recognised and enforced in Bermuda under the common law, the position is still uncertain, though it is noted that there have been examples where the Bermuda Courts have been willing to recognise the scheme of arrangement order (see the *MPF Limited* case; Guidance Text at p 46).

#### Correct

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.**

Jurisdictions in which action could be taken

**The Company is a Bermuda exempt company and carries international business. As such, it is not only subject to the winding-up jurisdiction of the Supreme Court of Bermuda, but also the courts of the foreign jurisdictions it operates in (through its various subsidiaries in the PRC and its substantial operations in HK). As a result, the bondholders could take (a) action against the Company's indirect trading subsidiaries in the PRC; (b) in Hong Kong where the Company has a substantial business presence; and/or (c) action against the Company in Bermuda. It should also be noted that such**

action may also be commenced on a *simultaneous* basis, *ie*, in one or more jurisdictions simultaneously. In such a situation, one of the courts will be recognised as the primary court, while the others are deemed “ancillary” courts. This will in turn be determined (insofar as the Supreme Court of Bermuda is concerned) by the court’s assessment of all the circumstances of the case (*including* concepts such as the company’s centre of main interest) (*Re C&J Energy Services Ltd* [2017] Bda LR 22).

#### Defendants

The bondholders may take action against (a) the Company; (b) its directors; (c) the business entities/subsidiaries the Company has in Hong Kong and (d) in China.

#### Litigation v Insolvency Proceedings

The advantage of instituting insolvency proceedings in the present context is that a stay on enforcement of the Company’s debt comes into force upon commencement of those proceedings. This, together with the claims process that follows and that is facilitated by the relevant insolvency office holder appointed, allows a more orderly and co-ordinated claim against the Company, as opposed to each individual creditor taking action against the Company in ‘a race to the bottom’ scramble for assets, be it in Bermuda or elsewhere (of course, it could be that all the bondholders are joined as plaintiffs in a single action against the Company).

Litigation, however, may have the advantage of being a more ‘direct’ approach to a claim on debt, particularly where there is clear evidence of said debt. From a more self-centred perspective, it could also allow the bondholders to recuperate a larger sum from the Company as judgment debt (rather than to have to share in a *pari passu* distribution of the remainder of the Company’s estate after the secured/preferential creditors have been satisfied). However, what weighs against this is that the Company would also have to spend money to defend itself in such a claim; in which case the overall value of the estate will be eroded as well. Litigation may also drag on for far longer than envisaged. Instituting insolvency proceedings may thus be the most appropriate solution moving forward.

#### Causes of Action

##### *Winding-Up Proceedings in Bermuda*

The US bondholders may apply for the Company to be compulsorily wound by the court under s 161(e) of the Companies Act 1981, *ie*, that it is unable to pay its debts. A company is deemed unable to pay its debts pursuant to s 162(a) of the Companies Act 1981 if a creditor serves a statutory demand (for a sum exceeding five hundred dollars) on the company’s registered office which has been neglected or unsatisfied for a period of three weeks. In the present case, it would appear that this statutory timeline of three weeks would be met within 7 days of the Company’s continued ignorance of the statutory demand. The US bondholders could also prove that the



*Company is unable to pay its debts demonstrating that the “contingent and prospective liabilities” of the Company are so large that it fails the cash flow insolvency or balance sheet insolvency tests (s 162(c) of the Companies Act 1981.*

*Alternatively, the US bondholders may also make an application under s 161(g) of the Companies Act 1981, which provides that the court may wind up a company if the court is of the opinion that it would be “just and equitable” to do so. Examples of such circumstances would be where there is a “lack of probity on the part of the company’s directors” (Guidance Text at p 17), which the US bondholders may arguably succeed in proving given the board’s election to ignore the statutory demand for a substantial sum, and its decision to incur *even* more debt from Lendbank and to make personal payments out of that latter sum.*

*The making of a winding-up order has the useful effect of bringing about a statutory moratorium on proceedings against the company, though this does not prevent secured creditors from enforcing their security in a self-help manner.*

*More importantly, however, it allows the US bondholders to ‘reach’ into the entirety of the Company’s assets (i.e, whatever moneys may be in HK or the PRC)*

*Discrete causes of action*

*Under Bermuda law, it would be also possible to ‘attack’ or claw back the transactions entered into by the Company after the statutory demand was served, i.e, the additional 50m loan from Lendbank (and the payments made from that sum). Under s 239 of the Companies Act 1981, a floating charge on the property of a company (as is the case here) created within 12 months of the commencement of the winding-up shall be invalid, unless it is proved that the company immediately after the creation of the charge was solvent and to the extent of any cash paid to the company at the time of or subsequently to the creation of, and in consideration for, the charge (which, in this case is USD50m). Should the Company’s shares and assets of its subsidiaries (the assets to which the floating charge was declared) exceed 50m, then any further amount may be clawed back under this section for the *pari passu* distribution amongst the bondholders.*

*Action may also be taken directly against the directors for breach of their fiduciary or statutory duties, for instance:*

- Under s 247 of the Companies Act, the directors bear personal liability if they have misapplied or retained, or become liable or accountable for any money or property of the company, or if they have been guilty of any misfeasance or breach of trust in relation to the company. Here, the board’s decision to make payment to themselves and wilfully ignore the statutory demand may strongly suggest such misfeasance.*
- Similarly, liability may arise in terms of the directors’ common law/statutory duties to the Company to exercise reasonable skill and care (see s 97 of the Companies Act).*

- Under s 54 of the Companies Act, a company shall not declare a dividend if there are reasonable grounds to believe that the company is unable to pay its liabilities. To this extent, the directors may be liable for having declared the dividend despite clear knowledge of the company's insolvency.
- Finally, to the extent that the mental element can be proven, the directors of the Company may be liable under s 246 of the Companies Act 1981, which provides that directors who knowingly cause or allow a company to carry on business with the intent to defraud creditors of the company (which in this case may be the bondholder).

**A thorough and thoughtful answer.**

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).**

*The Company could consider the appointment of a provisional liquidator in Bermuda. This would avail the Company the 'cloak' of a statutory moratorium on creditor enforcement action, thus shielding the Company from proceedings by creditors and giving it breathing room while it explores restructuring options. Such an approach is known as "soft touch" provisional liquidation. Under s 170(2) of the Companies Act 1981, the court may appoint a provisional liquidator between the presentation of a winding-up petition and its final hearing. The relevant test is that the applicant must "at least make out a good prima facie case that a winding-up order will be made" (*Re Stewardship Credit Arbitrage Fund Ltd* [2008] Bda LR 67 ("*SCAF*") at [36]). The Court then considers whether, in the circumstances of the case, it is "right" that a provisional liquidator should be appointed (*SCAF* at [36]). The Company may therefore present a petition for winding-up, and the provisional liquidator once appointed may then apply for a statutory stay of all proceedings while the work-out process (whether formally or informally) continues with the Board at the helm and under the supervision of the provisional liquidator. Should the negotiations for restructuring be successful, the winding-up petition may be dismissed.*

**Restructuring in Bermuda**

*In terms of the restructuring efforts proper, the Company could commence a scheme of arrangement ("*SOA*") under the Companies Act 1981. An *SOA* is a formal procedure which may be used to restructure its debt obligations with a view to its continued trading. Under an *SOA*, all of the Company's debts (or certain classes of debt) may be*

*adjusted or compromised. SOAs may also be used to implement a debt-for-equity swap.*

*In order for the SOA to be binding, the approval of a majority within each class of creditors present and voting (including by proxy) at the meeting of that class, representing 75% by value of that class, must vote in favour of the scheme. Upon court approval, the SOA is then binding on all creditors. A successful SOA may thus involve a cram down of a minority of dissenting creditors. That said, court approval remains a discretionary matter, and the court must be satisfied that the statutory requirements have been met (including the holding of requisite class meetings and approval of necessary majorities), that each class was fairly represented at each meeting, and that the SOA is generally fair to creditors and that the majority has not taken unfair advantage of its position (Guidance Text at p 25). Procedurally speaking, the SOA is not effective until a copy of the sanction order from the court is delivered to the Registrar of the Companies.*

*Those voting at the SOA meetings may even include persons beneficially interested in the company's debt, as may be the case for the US Bonds (Guidance Text at p 24). The meeting may be called for upon the direction of the court, and the creditors summoned by notice.*

*In terms of funding the procedures of the SOA, should the Company be unable to use its own assets to facilitate the process, it is possible for the company or its liquidators to enter into funding arrangements with those interested in the outcome of the procedures (such as creditors) if such would be beneficial for the winding-up of the company. Funding liabilities would be expected to be re-paid by the company or by the liquidator prior to the repayment of unsecured creditors. In this vein, it is possible to secure priority treatment for rescue financing (and is a possible option the Company may consider in order to fuel its restructuring efforts).*

*Aside from the formal SOA procedure, the Company could also engage in informal 'work-outs' with the consent of all relevant creditors; though a cram down of dissenting creditors is not an option available in the absence of a formal restructuring process.*

*The Bermuda liquidator may also apply for recognition of the SOA under Chapter 15 of the US Bankruptcy Code (of which there are, notably, successful precedents - see *In re Board of Directors of Hopewell Intl Ins Ltd* 275 BR 699 (SDNY 2022)).*

#### *Restructuring in HK*

*The Company should also consider engaging in a parallel SOA in Hong Kong at the same time (ie, an application to both HK and Bermuda). There has been a favourable precedent in this regard in *Re Titan Petrochemicals Group* [2014] Bda LR 90, where the Bermudian Court recognised that it frequently approves parallel schemes linking Bermuda and Hong Kong (amongst others).*

*This would be the safest way of ensuring the control in the overall scheme and the management of creditor action in both jurisdictions, especially since Bermuda does not have enacted local legislation incorporating the centre of main interest test set out in the UNCITRAL Model Law on Cross Border Insolvency, nor does Bermuda have any statutory analogue to Chapter 15 of the US's Bankruptcy Code, or the UK's Cross-Border Insolvency Regulations 2006.*

*This must of course be balanced against the potential costs and expenses, and the advantages and disadvantages of engaging in such parallel schemes. Regard must be had to the rule in *Antony Gibbs & Sons v La Societe Industrielle et Commerciale de Metaux* (1890) IR 25 QBD 398: a debt can only be validly discharged under the provisions of its governing law unless the relevant creditors submit to a foreign debt restructuring. This will have implications in the context of the cross-border nature of the proposed parallel scheme.*

*In this regard, another alternative (to beginning a parallel SOA in HK) is to simply apply for the recognition and enforcement of the Bermudian SOA in HK (see *Re China Oil/ Gangran Energy Group Holdings Limited* [2021] HKCFI 1592, where it was observed that the fact a soft-touch liquidation is not permissible in Hong Kong does not prevent the Hong Kong Court from recognising foreign soft-touch provisional liquidation).*

#### *Debt-to-equity Swap*

*If a debt-to-equity swap were proposed, it would be relevant to consider that under Bermuda law, a Bermuda company that is not in liquidation cannot lawfully return capital to its shareholders except by way of an approved reduction of capital or repurchase. It would thus be necessary to engage in a formal insolvency procedure (i.e. liquidation) and engage in the formal SOA process in Bermuda in order to enact the debt-to-equity swap.*

*The rule in *Gibbs*, i.e. that a debt is treated as discharged if compromised in accordance with the law of the jurisdiction which governed the instrument giving rise to the debt, is also relevant to the extent it is good law in Bermuda and Hong Kong. Here, depending on whether the governing law allows for debt-to-equity swaps, it may be that such an arrangement will not be recognised as a valid discharge of debt in Bermuda/ Hong Kong.*

*This is a thorough and complete answer, save only that the first paragraph under the debt for equity swap discussion is a little bit confused, since this would not be a case of a return of capital.*

7 marks

TOTAL: 48 out of 50 marks.

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\* End of Assessment \*