

Equity Derivatives

Contributing editors

John M Brandow, Ray Ibrahim and Mark M Mendez



2017

GETTING THE
DEAL THROUGH 

GETTING THE
DEAL THROUGH 

Equity Derivatives 2017

Contributing editors

John M Brandow, Ray Ibrahim and Mark M Mendez
Davis Polk & Wardwell LLP

Publisher
Gideon Robertson
gideon.roberton@lbresearch.com

Subscriptions
Sophie Pallier
subscriptions@gettingthedealthrough.com

Senior business development managers
Alan Lee
alan.lee@gettingthedealthrough.com

Adam Sargent
adam.sargent@gettingthedealthrough.com

Dan White
dan.white@gettingthedealthrough.com



Published by
Law Business Research Ltd
87 Lancaster Road
London, W11 1QQ, UK
Tel: +44 20 3708 4199
Fax: +44 20 7229 6910

© Law Business Research Ltd 2017
No photocopying without a CLA licence.
First published 2016
Second edition
ISSN 2397-7906

The information provided in this publication is general and may not apply in a specific situation. Legal advice should always be sought before taking any legal action based on the information provided. This information is not intended to create, nor does receipt of it constitute, a lawyer-client relationship. The publishers and authors accept no responsibility for any acts or omissions contained herein. The information provided was verified between March and April 2017. Be advised that this is a developing area.

Printed and distributed by
Encompass Print Solutions
Tel: 0844 2480 112



CONTENTS

| | | | |
|--|-----------|---|-----------|
| Introduction | 5 | Japan | 46 |
| John M Brandow, Ray Ibrahim and Mark M Mendez Davis Polk & Wardwell LLP | | Kentaro Nakanishi and Akihiro Tsukamoto TMI Associates | |
| Brazil | 6 | Mexico | 50 |
| Carlos Fernando Siqueira Castro and Guilherme Dantas Siqueira Castro – Advogados | | Pablo Perezalonso Ritch, Mueller, Heather y Nicolau SC | |
| Canada | 10 | Norway | 56 |
| William A Scott, Jonathan Willson and François Gilbert Stikeman Elliott LLP | | Per Morten Christiansen and Christoffer Norén Advokatfirmaet Selmer DA | |
| Cayman Islands | 17 | Portugal | 61 |
| Philip Paschalides and Paul Osborne Walkers | | André Figueiredo and Luis Miguel Vasconcelos PLMJ – Sociedade de Advogados, RL | |
| China | 22 | Spain | 68 |
| Chin Chong Liew, Simon Zhang, Stephen Song and Ying Zhou Linklaters | | Gonzalo García-Fuertes Garrigues | |
| Germany | 27 | Switzerland | 74 |
| Christian Storck Linklaters LLP | | Patrick Hünerwadel, Patrick Schleiffer and Olivier Stahler Lenz & Staehelin | |
| Hong Kong | 33 | United Kingdom | 81 |
| Bronwen May and Ka Yin Au Yeung Hogan Lovells | | Jason Brooks and James Parkes CMS Cameron McKenna LLP | |
| Italy | 39 | United States | 86 |
| Carmelo Raimondo, Antonella Brambilla and Alessandra Pagliari Chiomenti Studio Legale | | John M Brandow, Ray Ibrahim and Mark M Mendez Davis Polk & Wardwell LLP | |

Cayman Islands

Philip Paschalides and Paul Osborne

Walkers

1 Other than transactions between dealers, what are the most typical types of over-the-counter (OTC) equity derivatives transactions and what are the common uses of these transactions?

The OTC equity derivatives transactions that we have seen most frequently over the past two to three years (other than between dealers) include:

- margin loans used to finance or leverage shareholdings (this is often used by British Virgin Islands companies in respect of shares in Cayman Islands companies);
- zero strike call options, prepaid forward transactions or share loans between an issuer and an underwriter or its affiliates to facilitate the hedging by investors of the issuer's convertible debt;
- call spreads used by the issuer to raise the effective strike price of its convertible debt;
- prepaid forward contracts to monetise shareholdings; and
- total return swaps to provide the swap buyer with investment exposure to the underlying shares.

The answers to the questions below focus on shares issued by Cayman Islands companies, but not those companies listed on the Cayman Islands Stock Exchange (CSX), irrespective of whether the shares are also listed and traded on a stock exchange in a similar jurisdiction. It is not typical to see OTC equity derivatives transactions written over shares that are listed on the CSX. At the time of writing, there are seven companies that have shares listed in the equity section of the Official List of the CSX. Accordingly, the Listing Rules of the CSX or any other rules, regulations or codes issued by the CSX, are not considered in this chapter.

2 May market participants borrow shares and sell them short in the local market? If so, what rules govern short selling?

As a matter of Cayman Islands law, it is permissible for Cayman entities to borrow shares and sell them short in the local market. There are no rules in the Cayman Islands that govern short selling.

3 Describe the primary laws and regulations surrounding OTC equity derivatives transactions between dealers. What regulatory authorities are primarily responsible for administering those rules?

There are no laws or regulations in the Cayman Islands that specifically regulate OTC equity derivatives transactions between dealers, nor is there a regulatory authority specifically responsible for such regulation.

The Securities Investment Business Law (2015 Revision) of the Cayman Islands (SIBL) specifically provides that the activities of a person dealing in securities as principal for their own account should not constitute securities investment business under SIBL, provided that they do not solicit members of the public to deal in securities nor hold themselves out as willing to deal in securities at prices determined by them generally and continuously or as engaging in the business of underwriting securities. The SIBL lays down a licensing regime for any company, foreign company or partnership incorporated or registered in the Cayman Islands that carries on securities investment business anywhere in the world or any entity that has a place of business in the Cayman Islands through which securities investment business is

carried on. The term 'securities' is widely defined and includes shares, partnership interests, trust units, debt instruments, warrants, options, futures and contracts for differences.

4 In addition to dealers, what types of entities may enter into OTC equity derivatives transactions?

Cayman Islands law does not restrict the types of entities that may enter into OTC equity derivative transactions.

5 Describe the primary laws and regulations surrounding OTC equity derivatives transactions between a dealer and an eligible counterparty that is not the issuer of the underlying shares or an affiliate of the issuer. What regulatory authorities are primarily responsible for administering those rules?

There are no laws or regulations in the Cayman Islands that specifically regulate OTC equity derivatives transactions between a dealer and an eligible counterparty that is not the issuer of the underlying shares or an affiliate of the issuer. There is no regulatory authority specifically responsible for the regulation of such transactions.

EU regulations and directives, such as the Markets in Financial Instruments Directive (MiFID), do not apply in the Cayman Islands. The Cayman Islands does not have a concept of 'eligible counterparty' such as that which applies under the MiFID.

6 Do securities registration issues arise if the issuer of the underlying shares or an affiliate of the issuer sells the issuer's shares via an OTC equity derivative?

There are no securities registration requirements under Cayman Islands law.

A Cayman Islands exempted company that is not listed on the CSX is prohibited from making any invitation to the public in the Cayman Islands to subscribe for any of its securities.

7 May issuers repurchase their shares directly or via a derivative?

The Companies Law (amended 2016 Revision) of the Cayman Islands (the Companies Law) permits a Cayman Islands company limited by shares or by guarantee and with a share capital, if authorised by its articles of association, to purchase its own shares, subject to certain restrictions to protect creditors and shareholders. A company may not purchase any of its shares that are not fully paid or if, as a result of the repurchase, it would no longer have any shares in issue other than treasury shares.

A company's purchase of its own shares must be in the manner and on the terms authorised by its articles of association or by a shareholder resolution (if the articles are silent on manner and terms) or, if the board is authorised by the articles or a shareholder resolution to do so, in the manner and on terms determined by the board of directors.

Under the Companies Law, payments by a company to purchase its shares may only be made from its profits, the proceeds of a fresh issue of shares, the share premium account or out of capital. If a payment is made from the company's share premium account or out of its capital, a statutory solvency test must be satisfied, such that immediately following the date of the payment the company must be able to pay its debts as they fall due in the ordinary course of business. There are significant

criminal penalties for knowingly or wilfully making payments out of the share premium account or capital in breach of this solvency test.

Although the Companies Law does not lay down a solvency test for payments out of profits, the view is held that the fiduciary duties owed to the company by its directors (including acting in the company's best interests and not acting imprudently) mean that in the context of a share repurchase out of profits, the company's directors must be able to conclude reasonably that, following the payment for the shares, the company would be able to continue to meet its debts as they fall due.

More generally, the issuer's directors will also need to be confident that any share repurchase and its terms are in the best interests of the company.

The Cayman Islands does not specifically prohibit a company from giving financial assistance for the purchase of its shares. However, under the common law's maintenance of capital rule, a transaction whereby a company returns capital to its shareholders in whatever form and under whatever label, and whether directly or indirectly, cannot be ratified by the shareholders and is void unless it has been sanctioned by the courts or by statute. In assessing whether there has been an unlawful return of capital, the courts will focus on the substance over the form of a transaction.

Provided that the shares are not listed on the CSX, a purchase by a Cayman Islands company of its own shares would not be subject to any Cayman Islands laws or regulations directed to addressing market manipulation.

8 What types of risks do dealers face in the event of a bankruptcy or insolvency of the counterparty? Do any special bankruptcy or insolvency rules apply if the counterparty is the issuer or an affiliate of the issuer?

Cayman Islands counterparty insolvency risks – general

A particular feature of the official liquidation process in the Cayman Islands can lead to uncertainty for those facing a Cayman Islands counterparty in an insolvency scenario. Official liquidation of a Cayman Islands company is commenced by the court making a winding up order. The court process is initiated by the filing of a winding up petition. If a winding up order is made, the liquidation is deemed to have commenced on the date the winding up petition was filed. This is important because any disposition of the company's property, any transfer of shares and any alteration in the status of the company's shareholders purportedly made after the deemed commencement of winding up is void unless the court orders otherwise. This means that there will be uncertainty between the date upon which a winding up petition is filed and the date of the hearing at which the court will determine whether the company is to be wound up. It would be possible to apply to court for an order to validate any transaction that involves the disposition of the Cayman Islands company's property or, where it is also the issuer, any transfer of shares in the counterparty issuer or alteration in the status of its shareholders. However, there can be no guarantee that the court would validate a particular transaction as there would be a number of factors to be considered (eg, the solvency of the company). Of course, if no winding up order were to be made, then the company would be able to perform the transaction as contemplated by its terms.

When a liquidator has been appointed in respect of a Cayman Islands company, there are different proceedings that the liquidator may bring to challenge transactions of the company, which are outlined below:

Voidable preference

A transaction that constitutes a voidable preference is invalid and will be reversed such that the parties will, to the extent able, be put back into the position they were in prior to entry into the transaction. A transaction that involves or consists of a transfer of property or payment obligation will be a voidable preference where the transaction was made:

- by a Cayman Islands company in favour of a creditor within six months immediately preceding the commencement of the liquidation of the company;
- at a time when the company was unable to pay its debts on a cash-flow basis; and
- with a view to giving the creditor a preference over other creditors. English judicial authority (which is persuasive although not technically binding in the Cayman Islands) indicates that acting 'with a view' to preferring one creditor over another means that it is the company's dominant intention to do so.

Fraudulent disposition or disposition at an undervalue

Any disposition of property made at an undervalue (which means for no consideration or for consideration the value of which is significantly less than the value of the property disposed of) by or on behalf of a company with the intention of defrauding its creditors (which means an intention wilfully to defeat an obligation owed to a creditor that existed on or prior to the date of the disposition) is voidable at the instance of the company's official liquidator. If these elements are present, the transaction is also voidable at the instance of a creditor that is prejudiced by it (although such a claim can be made outside of the company's liquidation). However, such action by a liquidator or creditor cannot be commenced more than six years after the relevant disposition. If a transaction is set aside on this ground then if the court is satisfied that the transferee has not acted in bad faith, the transferee will have a first and paramount charge over the property that is the subject of the disposition in an amount equal to the costs properly incurred by the transferee in defending the proceedings, and the disposition will be set aside subject to the proper fees, costs, pre-existing rights, claims and interests of the transferee.

Fraudulent trading

This statutory cause of action requires the liquidator to establish that certain business of the company has been carried on with intent to defraud creditors of the company or of any other person or for any fraudulent purpose. The court may declare that any person who was knowingly party to carrying on the company's business in such manner is liable to make such contributions to the company's assets as the court deems proper. This power is very wide, allowing a liquidator to seek redress from any such knowing party to the fraudulent trading. There is no limitation period for fraudulent trading actions brought by a liquidator.

Constructive trust

A liquidator may bring proceedings against the directors of the company in liquidation for breach of their fiduciary duties owed to the company, for example, where the company (by its directors) knowingly divests itself of an asset at an undervalue in breach of the directors' duty to act in the best interests of the company. If the recipient of the property 'knew' that it was receiving the property as a result of a breach of fiduciary duty, the liquidator may seek, as part of its relief, a declaration that the recipient is holding the property on constructive trust for the company. Based on English judicial authority (which is persuasive although not technically binding in the Cayman Islands), the test for the required level of knowledge is whether the recipient knew enough of the facts surrounding the breach of fiduciary duty to make it unconscionable for it to retain the benefit received.

It should be noted that constructive trust claims are not exclusively available to a liquidator and may arise pre-insolvency. However, a claim based on a breach of fiduciary duty is a claim of the company. As a practical matter, it may be unlikely that the company's directors would cause the company to commence proceedings against themselves. A shareholder derivative action may be possible with the leave of the court but dissatisfied creditors would have no standing to make a claim of this kind. The creditors' remedy in that situation, if the company is on the brink of insolvency or is insolvent, would be to petition for the winding up of the company and to seek the company's liquidator to pursue any claims against the directors.

Insolvency risks – where the counterparty is the issuer

Where the counterparty is the issuer of shares that are the subject of an OTC equity derivatives transaction, the transaction is one that is in respect of the counterparty's shares rather than its assets.

As noted in the first paragraph above, any transfer of shares in a Cayman Islands company and any alteration in the status of the company's shareholders purportedly made after the commencement of a winding up of the company is void unless the court orders otherwise.

To the extent that the issuer will, or may, acquire its own shares under an OTC equity derivatives transaction, the share purchase regime under the Companies Law would apply in respect of the transaction. As indicated in question 7, it is important that the issuer is solvent at the time that it makes any payment to acquire its own shares and continues to be solvent immediately following any such payment.

Under the share purchase regime of the Companies Law, if at the commencement of the winding up of a Cayman Islands company any of its shares that it agreed to purchase have not been purchased, the purchase agreement may be enforced against the company unless either:

- the purchase was to take place on a date later than the commencement of the winding up; or
- in the period from the agreed purchase date to the commencement of the winding up, the company could not, at any time, have made a distribution equal to the purchase price because immediately following the date of such distribution it would not have been able to pay its debts in the ordinary course of business.

Another important consequence of the liquidation of the counterparty issuer is that any claim for the payment of share purchase monies would be subordinated. If a shareholder is able to enforce the share purchase agreement with the issuer (as described in the previous paragraph), such amount would be subordinated to all other debts and liabilities of the company (other than any due to shareholders in their character as such), and any amount due to satisfy any preferential rights of other classes of shares of the issuer. More generally, in a liquidation of a Cayman Islands company, the claims of shareholders against the company are subordinated to the claims of unsecured creditors.

In the context of an OTC equity derivatives transaction, the risk of not being able to enforce the obligations of an issuer to pay for its shares when that issuer is in liquidation may be mitigated if certain termination or settlement provisions are structured into the transactions, the effect of which may be to change the overall nature of the characterisation of the transaction.

Many OTC equity derivatives transactions are structured so that the only payments to be made by the issuer are at inception, in circumstances where the issuer's solvency at such time can be determined, so as to reduce further the potentially adverse consequences.

9 What types of reporting obligations does an issuer or a shareholder face when entering into an OTC equity derivatives transaction on the issuer's shares?

Provided that no shares of the issuer are listed on the CSX, neither the issuer nor any of its affiliate shareholders would have any reporting obligations under Cayman Islands law in respect of their entering into an OTC equity derivatives transaction over the issuer's shares.

There are certain reporting obligations under the Listing Rules of the CSX, the Code on Takeovers and Mergers and the Rules Governing Substantial Acquisitions of Shares issued by the CSX that apply to companies whose shares are listed on the CSX.

10 Are counterparties restricted from entering into OTC equity derivatives transactions during certain periods? What other rules apply to OTC equity derivatives transactions that address insider trading?

Provided that the shares that are the subject of an OTC equity derivatives transaction are not listed on the CSX, and outside of an insolvency scenario (see question 8), Cayman Islands law does not restrict counterparties from entering into OTC derivatives transactions during particular periods.

The criminal offences of insider dealing and creating a false or misleading market created under the SIBL apply only in respect of securities listed on the CSX.

The Listing Rules of the CSX and the Code on Takeovers and Mergers also contain rules and restrictions that are directed at addressing insider trading. In view of the small number of issuers that are listed on the CSX (as opposed to other exchanges) these rules are not material for the purposes of the present discussion.

11 What additional legal issues arise if a counterparty to an OTC equity derivatives transaction is the issuer of the underlying shares or an affiliate of the issuer?

See questions 7 and 8.

12 What types of taxation issues arise in issuer OTC equity derivatives transactions and third-party OTC equity derivatives transactions?

The Cayman Islands currently have no form of income, corporate or capital gains tax and no estate duty, inheritance tax or gift tax. Payments under an issuer OTC equity derivative transaction or a third-party OTC derivative transaction would not be subject to taxation in the Cayman Islands and no withholding would be required on any such payments under Cayman Islands law, nor would any gains derived from the disposal of the underlying shares be subject to Cayman Islands income or corporation tax.

Stamp duty in the Cayman Islands arises where the relevant instrument is executed in or physically brought into the Cayman Islands after execution or sought to be produced before a Cayman Islands court.

13 Describe the liability regime related to OTC equity derivatives transactions. What transaction participants are subject to liability?

There is no specific liability regime under Cayman Islands law related to OTC equity derivatives transactions.

14 What stock exchange filings must be made in connection with OTC equity derivatives transactions?

Provided that the shares that are the subject of an OTC equity derivatives transaction are not listed on the CSX, there are no stock exchange filings that are required to be made in connection with OTC derivatives transactions.

The Listing Rules of the CSX do not contain any provisions specifically dealing with OTC equity derivative transactions, although depending on the particular facts, an OTC equity derivatives transaction written over shares listed on the CSX may trigger certain general filing requirements.

15 What types of documents are typical in an OTC equity derivatives transaction?

Typically, OTC derivatives transactions involving Cayman Islands counterparties, or that are in respect of shares issued by Cayman Islands companies, are documented under ISDA documentation governed by New York law or English law.

In the case of prepaid forward transactions used to monetise a shareholding, where the shares in question are held with a custodian, it would be typical to see a non-ISDA security document given in respect of the custodied shares or the counterparty's rights against the custodian. If it is a Cayman Islands custodian or the custodial account is located in the Cayman Islands, the security documents may also include a security agreement governed by Cayman Islands law.

Margin loans in respect of shares in a Cayman Islands company are typically documented as a loan agreement together with a non-ISDA security given over the shares, either directly or following a similar arrangement to that described above, where the shares are held by a custodian.

16 For what types of OTC equity derivatives transactions are legal opinions typically given?

Legal opinions would typically be given regarding all the OTC equity derivatives transactions noted in question 1.

Admittedly, it is not necessarily the case that Cayman Islands counsel will be asked to advise on every OTC equity derivatives transaction involving a Cayman Islands counterparty. For instance, the counterparties to a particular transaction may have an existing trading relationship, which means that the non-Cayman Islands counterparty may be sufficiently comfortable, and perhaps familiar with the jurisdiction, not to need a Cayman Islands legal opinion as to the existence, capacity and authority of its Cayman Islands counterparty. In such circumstances, the ISDA market opinions or a legal opinion on enforceability from the jurisdiction of the governing law of the transaction may be sufficient, although many parties will consult with Cayman Islands counsel:

- if they consider bespoke aspects of a particular transaction may remove that transaction from the coverage of the ISDA market opinions;

- if the particular transaction concerns shares issued by the counterparty itself; and
- where the counterparty is of a legal form that warrants special considerations (eg, segregated portfolio companies, trusts, STAR trusts, unit trusts and exempted limited partnerships).

17 May an issuer lend its shares or enter into a repurchase transaction with respect to its shares to support hedging activities by third parties in the issuer's shares?

Assuming that the directors of the issuer would be confident that in authorising such transactions they would be acting in the best interests of the issuer and otherwise in accordance with their fiduciary duties, and that such transactions are permitted by the issuer's articles of association, an issuer should, in principle, be able to lend its shares or enter into a repurchase transaction with respect to its shares to support hedging activities by third parties in the issuer's shares. (See question 7 in relation to other requirements in respect of an issuer's acquisition of its own shares and question 8 in relation to insolvency risks.)

For an issuer that is a Cayman Islands company, a share loan or a repurchase transaction would involve two distinct stages.

With regard to a share loan, the initial 'loan' of the shares would involve the issuance of new shares by the issuer to the share borrower, with the issuer entering the borrower into its internal share register as holder of the relevant shares. At maturity, the only material obligation to be performed would be the borrower's delivery to the issuer equivalent shares (which presumably would also be shares in the issuer) to those initially issued to the borrower. No payment would be required from the issuer at maturity. Depending on the terms of the share loan, the delivery of the equivalent shares at maturity could be seen as a purchase of its shares by the issuer for no further cash consideration or by way of surrender of the shares for no consideration by the borrower. In either case, the requirement under the Companies Law that the shares must be fully paid up to their par or nominal value could be achieved by ensuring that the borrower made a cash payment at inception, which the issuer applies to pay the new shares.

For a repurchase transaction, the initial sale leg would also involve the issuance of new shares by the issuer as 'seller' with the buyer paying the purchase price to it in return. The purchase price should be applied to pay the shares fully as to their par or nominal value and the issuer would enter the buyer into its internal share register as holder of the shares. At maturity, the 'repurchase' leg of the transaction would involve a purchase by the issuer of its shares equivalent to those initially issued to the buyer at the pre-agreed repurchase price. The purchase would need to comply with the share purchase regime under the Companies Law.

For both a share loan and a repurchase transaction, the articles of association of the issuer should be reviewed to confirm that they permit the issuer to purchase its own shares or, in the case of a share loan, accept the surrender of its shares for no consideration.

18 What securities registration or other issues arise if a borrower pledges restricted or controlling shareholdings to secure a margin loan or a collar loan?

The Cayman Islands does not have a generally applicable concept of restricted shareholdings, although the articles of association of a Cayman Islands company may always impose specific restrictions upon shares or a particular class of shares.

There are no registration requirements under Cayman Islands law.

Provided that the shares were not listed on the CSX, the granting of security by a borrower would give rise to any particular issues that particularly differed from taking security over shares in a Cayman Islands company in general.

19 If a borrower in a margin loan files for bankruptcy protection, can the lender seize and sell the pledged shares without interference from the bankruptcy court or any other creditors of the borrower? If not, what techniques are used to reduce the lender's risk that the borrower will file for bankruptcy or to prevent the bankruptcy court from staying enforcement of the lender's remedies?

The Cayman Islands do not have formal corporate rehabilitation regime akin to administration in England and Wales or Chapter 11 in the US pursuant to which a Cayman Islands company may benefit from an automatic 'stay' or 'moratorium' that would prevent creditors

taking steps to enforce their security or recover their debts through the commencement of legal proceedings, upon the commencement of insolvency proceedings by the Cayman company. Notwithstanding the lack of a formal restructuring regime, corporate rehabilitation in the Cayman Islands can be achieved through the Cayman Court appointment of provisional liquidators pursuant to section 104(3) of the Companies Law coupled with a Cayman Court request for a moratorium pursuant to section 97(1) of the Companies Law. With the benefit of the Cayman Court ordered moratorium, the provisional liquidators can present a compromise or arrangement to the company's creditors and/or stakeholders.

Assuming that the security interest of the lender in the secured shares is valid, binding and enforceable (in accordance with all applicable laws) and that it gives the lender the power to seize and sell the secured shares, the secured creditor would be able to enforce its security without the leave of the Cayman Court or the permission of a liquidator (including a provisional liquidator) pursuant to section 142 of the Companies Law. This right subsists irrespective of whether the company is insolvent as a matter of Cayman Islands law (ie, unable to pay its debts) or whether it has initiated a formal insolvency process (including a provisional liquidation).

20 What is the structure of the market for listed equity options?

There are no equity options and no derivative warrants listed on the CSX at the time of writing. Derivative warrants are defined under the Listing Rules of the CSX as specialist securities that give the holder the right, but not the obligation, to buy from or sell to the issuer a specified number of securities issued by an entity other than the issuer or any other assets, indices or specified variables or to receive a cash payment by reference to the value of any of the foregoing.

21 Describe the rules governing the trading of listed equity options.

See question 20.

The CSX has not promulgated rules for the trading of listed equity options.

Under the Listing Rules of the CSX, equity options fall within the definition of equity securities. Chapter 2 (General Listing Requirements) and Chapter 6 (Equity Securities) of the Listing Rules provide for certain continuing obligations that apply in relation to listed equity securities generally. There are no continuing obligations in these chapters that specifically apply to listed equity options.

22 What categories of equity derivatives transactions must be centrally cleared and what rules govern clearing?

There are no requirements under Cayman Islands law or regulations for the central clearing of any categories of equity derivatives transactions, although Cayman Islands entities may, depending on the circumstances and their activities, be subject to rules or regulations of other jurisdictions that require central clearing.

23 What categories of equity derivatives must be exchange-traded and what rules govern trading?

There are no requirements under Cayman Islands law or regulations that make any provision for any categories of equity derivatives transactions to be exchange traded.

24 Describe common collateral arrangements for listed, cleared and uncleared equity derivatives transactions.

Not applicable. See questions 22 and 23.

25 Must counterparties exchange collateral for some categories of equity derivatives transactions?

There are no requirements under Cayman Islands law or regulations for counterparties to exchange collateral for equity derivatives transactions.

26 What is the territorial scope of the laws and regulations governing listed, cleared and uncleared equity derivatives transactions?

Not applicable. See questions 22 and 23.

27 What registration or authorisation requirements apply to market participants that deal or invest in equity derivatives, and what are the implications of registration?

There are no registration or authorisation requirements under Cayman Islands law, or regulations that apply to market participants that deal or invest in equity derivatives provided that such activities of the relevant market participant do not constitute securities investment business under SIBL (see question 3).

28 What reporting requirements apply to market participants that deal or invest in equity derivatives?

There are no reporting requirements under Cayman Islands law or regulations that apply to market participants solely by dealing or investing in equity securities.

29 What legal issues arise in the design and issuance of structured products linked to an unaffiliated third party's shares or to a basket or index of third-party shares? What additional disclosure and other legal issues arise if the structured product is linked to a proprietary index?

There are no securities registration requirements under Cayman Islands law in respect of the issuance of structured products, whether linked to an unaffiliated third party's shares or a basket or index of third-party shares or to a proprietary index.

Provided that the structured products in question are not listed on the CSX, there would be no disclosure requirements whether they were linked to an unaffiliated third party's shares or a basket or index of third-party shares or to a proprietary index.

There may be filings and registrations for the issuing entity pursuant to the Foreign Account Tax Compliance Act (FATCA) and other tax information sharing legislation depending on the classification of the entity. The Cayman Islands is a party to numerous tax information exchange agreements and subject to both the US and UK FATCAs, as well as the Common Reporting Standard. Reporting entities incorporated or formed in the Cayman Islands will, therefore, be bound to provide information regarding their investors to the Cayman Islands Tax Information Authority as and when required by law.

Other than as stated in the foregoing paragraph and, potentially in relation to stamp duty, there should be no Cayman Islands tax issues that arise from equity-linked structured products. See question 12.

If the issuer of the structured products is a Cayman Islands exempted company that is not listed on the CSX, it is prohibited under the Companies Law from making any invitation to the Cayman Islands' public to subscribe for any of its securities.

30 Describe the liability regime related to the issuance of structured products.

There is no specific liability regime under Cayman Islands law related to the issuance of structured products.

31 What registration, disclosure, tax and other legal issues arise when an issuer sells a security that is convertible for shares of the same issuer?

Provided that no shares of the issuer, or convertible securities, are listed on the CSX, there should be no disclosure issues where an issuer sells a security that is convertible for shares in the same issuer. There may potentially be filings and registrations for the issuing entity pursuant to FATCA and other tax information sharing legislation depending on the classification of the issuer. See question 6.

There should be no Cayman Islands tax issues that arise from equity-linked structured products, with the possible exception of stamp duty. See question 12.

The board of directors of the issuer would need to be confident that the transaction was in the best interests of the issuer, particularly where it was also entering into OTC equity derivative transactions in connection with the issuance of its convertible securities. The issuer would also need to ensure that it would, at all relevant times, have sufficient authorised but unissued share capital to enable it to issue the required number of shares pursuant to the proposed conversion of the securities by investors, to the extent that it could not obtain sufficient numbers of its issued shares from the market.

32 What registration, disclosure, tax and other legal issues arise when an issuer sells a security that is exchangeable for shares of a third party? Does it matter whether the third party is an affiliate of the issuer?

Provided that no shares of the issuer, exchangeable securities, are listed on the CSX, there should be no disclosure issues where an issuer sells a security that is exchangeable for shares in a third party, regardless of whether the third party is an affiliate of the issuer. There may potentially be filings and registrations for the issuing entity pursuant to FATCA and other tax information sharing legislation depending on the classification of the issuer. See question 6.

There should be no Cayman Islands tax issues that arise from equity-linked structured products, with the possible exception of stamp duty. See question 12.

The board of directors of the issuer would need to be confident that the transaction was in the best interests of the issuer.



Philip Paschalides
Paul Osborne

philip.paschalides@walkersglobal.com
paul.osborne@walkersglobal.com

190 Elgin Avenue
George Town
Grand Cayman KY1-9001
Cayman Islands

Tel: +1 345 949 0100
Fax: +1 345 949 7886
www.walkersglobal.com

Getting the Deal Through

Acquisition Finance
Advertising & Marketing
Agribusiness
Air Transport
Anti-Corruption Regulation
Anti-Money Laundering
Arbitration
Asset Recovery
Aviation Finance & Leasing
Banking Regulation
Cartel Regulation
Class Actions
Commercial Contracts
Construction
Copyright
Corporate Governance
Corporate Immigration
Cybersecurity
Data Protection & Privacy
Debt Capital Markets
Dispute Resolution
Distribution & Agency
Domains & Domain Names
Dominance
e-Commerce
Electricity Regulation
Energy Disputes
Enforcement of Foreign Judgments
Environment & Climate Regulation
Equity Derivatives
Executive Compensation & Employee Benefits
Financial Services Litigation
Fintech
Foreign Investment Review
Franchise
Fund Management
Gas Regulation
Government Investigations
Healthcare Enforcement & Litigation
High-Yield Debt
Initial Public Offerings
Insurance & Reinsurance
Insurance Litigation
Intellectual Property & Antitrust
Investment Treaty Arbitration
Islamic Finance & Markets
Labour & Employment
Legal Privilege & Professional Secrecy
Licensing
Life Sciences
Loans & Secured Financing
Mediation
Merger Control
Mergers & Acquisitions
Mining
Oil Regulation
Outsourcing
Patents
Pensions & Retirement Plans
Pharmaceutical Antitrust
Ports & Terminals
Private Antitrust Litigation
Private Banking & Wealth Management
Private Client
Private Equity
Product Liability
Product Recall
Project Finance
Public-Private Partnerships
Public Procurement
Real Estate
Restructuring & Insolvency
Right of Publicity
Securities Finance
Securities Litigation
Shareholder Activism & Engagement
Ship Finance
Shipbuilding
Shipping
State Aid
Structured Finance & Securitisation
Tax Controversy
Tax on Inbound Investment
Telecoms & Media
Trade & Customs
Trademarks
Transfer Pricing
Vertical Agreements

Also available digitally



Online

www.gettingthedealthrough.com



Equity Derivatives
ISSN 2397-7906



THE QUEEN'S AWARDS
FOR ENTERPRISE:
2012



Official Partner of the Latin American
Corporate Counsel Association



Strategic Research Sponsor of the
ABA Section of International Law