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Welcome to Walkers’ first Special Issue of International Corporate Rescue. The analysis provided in the articles in this Special Issue reflects our well-established reputation in the offshore insolvency market across 10 different jurisdictions. We have acted for some of the key players in some of the largest recent offshore insolvencies and restructurings including those involving Saad Investments Company Limited (In Official Liquidation), the Abraaj Group, Ocean Rig UDW Inc., CHC Group, Mongolian Mining Corporation and Constellation Overseas Ltd. to name a few.

Walkers’ global insolvency and dispute resolution group is internationally recognised as having the premier insolvency and corporate recovery team amongst the offshore law firms. With the most ranked offshore restructuring and insolvency lawyers, Walkers frequently plays a leading role in some of the most complex, ground breaking, cross-border cases that involve offshore jurisdictions.

Our dedicated insolvency and restructuring teams across 10 jurisdictions offer Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Irish and Jersey law advice on all aspects of restructuring, insolvency, corporate recovery, litigation and dispute resolution. Our group regularly specialises in complex cross border restructurings, contentious and non-contentious insolvencies, insolvency litigation and distressed situations.

I hope you enjoy this Special Issue. We look forward to working with you in the future in this fast-moving and challenging area.

Colette Wilkins, Partner, and Andrew Gibson, Senior Counsel, Walkers, Cayman Islands

Synopsis

As one of the leading offshore jurisdictions globally for the resolution of complex financial services disputes, expert witnesses are frequently appointed to provide evidence to the Financial Services Division of the Grand Court of the Cayman Islands (the ‘Court’) on a wide array of disciplines. Their role is becoming increasingly important as the financial services industry continues to evolve and gives rise to the emergence of expertise in new categories of disputes, such as shareholder appraisal rights in the context of mergers and fair value petitions where the opinion of an expert can well determine the outcome of the case.

This memorandum focusses on some of the key pre-trial procedural aspects relating to the appointment of experts in the Cayman Islands, including the duties they owe to the Court, the required form and content of their reports, and meetings between party appointed experts.

Directions for the appointment of an expert

Except with the leave of the Court or where all parties agree, expert evidence cannot be adduced. 1 In practice this means that if the parties are unable to agree upon directions for the appointment of one or more experts in a particular discipline (e.g. forensic accountancy, or foreign law), the requesting party must apply to the Court seeking a direction to that effect. Such applications would ordinarily be determined by the Court at a directions hearing or case management conference shortly after the commencement of the proceedings.

The directions available to the parties and the Court vary and will be tailored to the proceedings in hand but common elements are (a) identifying the scope of the expert evidence; (b) the form in which the expert evidence is to be provided (a written report being the default and preferred form); (c) the deadline for filing and exchanging such reports; (d) whether a sole expert may be utilised, or whether the parties may appoint separate experts; (e) the deadline for any meetings between the separate experts in an attempt to narrow the issues in dispute; and (f) the deadline for the filing and exchanging of any reply reports.

The question of determining the appropriate number of experts was considered by the Court in the recent decision of In the Matter of Qunar Cayman Islands Ltd, 2 which concerned a fair value petition under Section 238 of the Cayman Islands Companies Law 3 where there were multiple dissenters. If each dissenter were to be permitted to instruct their own valuation expert, the Court would have needed to hear evidence from five different experts. The Court, pursuant to its case management powers, decided that one expert should be instructed by the dissenters jointly and severally on the basis that their interests ought to be aligned, and that this would not infringe their right to a fair trial.

General requirements of an expert

Paragraph B5.2 of the Second Edition of the Financial Services Division Guide sets out eight general requirements of an expert. Those eight requirements, which are also commonly referred to as the ‘duties’ of an expert, are as follows:

1. It is the duty of an expert to help the Court on the matters within his expertise. This duty is paramount and overrides any obligation to the party from whom the expert has received instructions or by whom he is paid.

2. Expert evidence presented to the Court should be, and should be seen to be, the independent product of the expert uninfluenced by the pressures of litigation or any party.

3. An expert witness should provide independent assistance to the Court by way of objective unbiased

Notes

1 GCR O.38, r.16.


3 Section 238 of the Cayman Islands Companies Law provides minority shareholders who dissent from a statutory merger the right to a court determination as to the fair value of their shareholdings.
opinion in relation to matters within his expertise. An expert witness should never assume the role of an advocate or seek to promote his client’s case.

4. An expert witness should not omit to consider material facts which could detract from his concluding opinion.

5. An expert witness should make it clear when a particular question or issue falls outside his area of expertise.

6. If an expert’s opinion is not properly researched because he considers that insufficient data is available, this must be stated in his report with a clear indication that his opinion is no more than a provisional one.

7. In a case where an expert witness who has prepared a report is unable to confirm that the report contains the truth, the whole truth and nothing but the truth without some qualification, that qualification must be clearly stated in the report.

8. If, after the exchange of reports, an expert witness changes his view on a material matter having read another expert’s report or for any other reason, such changes of view should be communicated in writing (through the party’s attorneys) to the other side without delay, and, when appropriate, to the Court.

The second of these requirements is vital, and is consistent with the finding of Lord Wilberforce in the House of Lords decision of Whitehouse v Jordan, in which he said: ‘While some degree of consultation between experts and legal advisers is entirely proper, it is necessary that expert evidence presented to the court should be, and should be seen to be, the independent product of the expert, uninfluenced as to form or content by the exigencies of litigation. To the extent that it is not, the evidence is likely to be not only incorrect but self-defeating.’

The duties were also considered by the Court in the matter of Al Sadik v Investcorp Bank BSC and Five Others in which the Court was less than impressed by the evidence given by one of the experts. The Honourable Justice Jones held that the evidence of the plaintiff’s expert was largely inadmissible on the basis that the expert had been asked to provide opinions on matters which were irrelevant, outside the expert’s expertise, and on matters of law which were for the Court to decide. It was held that the expert’s reports were adversarial both in tone and content; the terms of reference had encouraged the expert to take a judgmental approach; and the cross-examination of the expert took on the character of a debate in which the expert advocated the plaintiff’s case. Given those findings it was no surprise that the Judge held that the expert had not met the required standards of an expert witness, and as such, the Court approached the evidence provided with a high degree of caution.

**Form and content of expert report**

Expert reports must comply with the following requirements:

1. In stating the substance of all material instructions on the basis of which his report is written an expert witness should state the facts or assumptions upon which his opinion is based.

2. The expert must make it clear which, if any, of the facts stated are within his own direct knowledge and which are not.

3. If a stated assumption is, in the opinion of the expert witness, unreasonable or unlikely he should state that clearly.

4. The expert’s report must be limited to matters relevant to the issue or issues in the list of issues to which the relevant expert evidence relates and for which leave to call such expert evidence has been given by the Court.

To assist the experts in fulfilling the above requirements, the parties might seek to agree in advance a common scope of issues to be determined by them, which can be in the form of a series of questions based on assumed facts.

It is important that these questions are settled between the parties at an early stage in order for the trial to proceed expeditiously. In the recent decision of In the Matter of E-House (China) Holdings Limited, the petitioner sought an order, after exchange of expert reports (together consisting of over 700 pages) and after the experts having discussed the matters on which they are agreed and the differences which remain between them, to permit the experts to ask five further written questions on issues that had not already been dealt with in their reports. This had the potential effect of widening their scope and delaying the trial of the proceedings. The Court, in exercising its case management powers, refused the order drawing particular reference to the fact that the request to vary the consent order in this instance came from the attorneys and not the

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**Notes**

4 [1981] 1 WLR 246, at 256.
6 Paragraph B5.3(a) of the Second Edition of the Financial Services Division Guide.
7 Unreported. 3 November 2017.
experts. The decision also emphasised the substantial authority experts possess in satisfying themselves that they have access to all information they require. The Honourable Justice Mangatal commented:

‘If such a need for further questions exists, the Court should expect an expert to say so plainly and unambiguously, and also to indicate, at least in a general way, what additional matters he wishes to speak about.’

Statement of truth

As is customary throughout most common law jurisdictions, the report must contain a statement of truth, which should include a separate statement to the effect that the expert has read and complied with the eight general requirements set out above.8

Documents referred to in expert report

Unless already disclosed by the parties in the proceedings as part of the ordinary discovery process, any documents relied upon by the expert in their report, as well as copies of any unpublished sources, must be provided at the same time as the report.9

Any requests for inspection of a document referred to in a report should not be made if the document is publically available or can be obtained from an alternative source.10

Although there are no formal requirements for an expert’s letter of instruction to be disclosed, it is common practice for this to be produced so that the Court and opposing party has full visibility on the scope of the instruction and materials that have been provided to the expert.

Meetings between experts

Where there is a direction for separate experts to meet, such meetings would typically take place shortly after the exchange of their respective reports and prior to the commencement of the trial.

The purpose of such meetings is to give the experts the opportunity (a) to discuss the expert issues; and (b) to decide, with the benefit of that discussion, which expert issues they share or can come to share the same expert opinion, and on which expert issues there remains a difference of expert opinion between them (and what that difference is).11

In order to facilitate this, the meetings should be conducted on a without prejudice basis, and neither the parties or their legal representatives should be in attendance.12

Following the meeting, the experts are expected to prepare a joint report.13 The joint report ought to record:

1. the fact that they have met, when and where and that they discussed the expert issues;
2. the issues on which they agree;
3. the issues on which they disagree; and
4. a brief summary of the reasons for any such disagreement.

If experts reach agreement on an issue, that agreement shall not bind the parties unless they expressly agree to be bound by it.14

Conclusion

The importance of experts ensuring compliance with the above duties and requirements cannot be understated. Failure to comply may lead to the Court imposing adverse costs orders, or perhaps even disregarding the expert’s evidence in its entirety.

Parties must also be committed at the outset of the proceedings towards attempting to agree appropriate and proportionate directions particularly in relation to the number of experts to be appointed, and the scope of their instructions, mindful of the Court’s ability to exercise its overarching case management powers.

Walkers acted for the Defendants in Al Sadik v Investcorp Bank BSC and Five Others.

Notes

8 Paragraph B5.4 of the Second Edition of the Financial Services Division Guide.
9 Paragraph B5.7(a) of the Second Edition of the Financial Services Division Guide.
10 Paragraph B5.7(c) of the Second Edition of the Financial Services Division Guide.
11 Paragraph B5.6(a) of the Second Edition of the Financial Services Division Guide.
12 Paragraph B5.6(c) and B5.6(d) of the Second Edition of the Financial Services Division Guide.
13 GCR 0.38, r.18.
14 Paragraph B5.6(e) of the Second Edition of the Financial Services Division Guide.
15 Paragraph B5.6(f) of the Second Edition of the Financial Services Division Guide.
Shining a Light on Validation Orders: An Overview of Validation Orders in Cayman Insolvency Proceedings

Joanne Collett, Partner and Meenaa Azmayesh, Senior Associate, Walkers, Hong Kong and Fiona MacAdam, Senior Counsel, Walkers, Cayman Islands

Synopsis

A recent judgment of the Cayman Islands Court of Appeal has provided certainty for directors, general partners and insolvency practitioners with respect to the principles that the Cayman Islands Courts will take into account in determining whether to grant a validation order in the context of Cayman Islands winding up proceedings. This article provides an overview of validation orders in Cayman Islands insolvency proceedings and a summary of the relevant factors to consider when making an application seeking a validation order.

Introduction

Under Cayman Islands law, if a winding up order is made, the winding up of a company is deemed to commence at the time of the presentation of the winding up petition for an official liquidation or the passing of the members’ resolution in the event that a Court supervised liquidation commenced as a voluntary liquidation.1 There will inevitably be a period of time that passes between the commencement of the winding up and the making of a winding up order. As such, a question often arises as to whether a company that is the subject of winding up proceedings can enter into valid transactions during that intervening period in circumstances where a winding up order is ultimately made by the Grand Court of the Cayman Islands (the ‘Grand Court’).

The answer can be found in section 99 of the Companies Law (2018 Revision) (the ‘Companies Law’), which provides that:

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

The requirements for obtaining a validation order (which can be sought either in advance or retrospectively) were recently considered and reaffirmed by the Cayman Islands Court of Appeal (‘CICA’) in In Re Torchlight Fund L.P. (Unreported, 27 April 2018, CICA). This article provides an overview of validation orders in Cayman Islands insolvency proceedings and summarises the applicable principles that the Grand Court will consider in determining whether to grant a validation order.

Purpose of Section 99

Pursuant to section 99 of the Companies Law, any disposition of the company’s property, effects and things in action, or any transfer of shares held by the company and/or in the company or alteration in the status of the members of the company during the period between the commencement of the winding up and the making of the winding up order is void, unless the Grand Court grants a validation order. It follows that in the event that a winding up petition is dismissed and therefore no winding up order is made, section 99 will not affect a transaction entered into following the presentation of such winding up petition (although noting that the relevant transaction could potentially be successfully challenged by a liquidator in the future pursuant to an alternative antecedent transaction section of the Companies Law should a winding up order be granted on a further winding up petition2).

Section 99 seeks to void any transfer of a company’s property which would have the result of diminishing the ‘pot’ of assets available for distribution to the company’s stakeholders in a liquidation. Section 99 also assists in protecting the fundamental principle of pari passu treatment of all unsecured creditors, that is, the

Notes

1 Section 100 of the Companies Law.
2 Section 145 of the Companies Law (Voidable preferences), section 146 of the Companies Law (Avoidance of dispositions made at an undervalue) and section 147 of the Companies Law (Fraudulent Trading).
principle that all unsecured creditors equally share in any available assets in the insolvent estate according to their rights and interests in the company.

If a transaction is void pursuant to section 99, the liquidator will be entitled to seek appropriate relief for any asset to be returned or repayment of funds for the benefit of the company’s creditors as a whole.

The exception to section 99

The legal rights of a secured creditor will be unaffected by the commencement of winding up proceedings of a company.1 Accordingly, irrespective of the existence of section 99 of the Companies Law and any insolvency proceedings on foot, a secured creditor will retain the ability to enforce its security and sell the charged property to obtain payment of the debt owing without leave of the Grand Court and without reference to any liquidator. If the sale proceeds of the charged asset are insufficient to discharge the debt, a secured creditor can rank as an unsecured creditor in the liquidation in respect of the balance of the debt.

A secured creditor may appoint a receiver over a charged asset for the purpose of enforcing their security rights if permitted by the relevant security document. A receiver is not subject to supervision by the Grand Court and their primary duty will be to the secured creditor, as opposed to the general body of creditors. Despite the fact that a receiver’s primary duty is to the secured creditor appointing it, the receiver is an agent of the company. As such, the receiver also owes duties to the company, in particular, a receiver must act in good faith, must deal fairly and equitably with the company and, if selling an asset, owes a duty to the company to obtain the best price reasonably available in the circumstances.

Should a secured lender enter into a new security arrangement with a company after the commencement of winding up proceedings against such company, that security is likely to be void (if not validated by the Grand Court) where a winding up order is granted. Therefore, prior to taking any security, a secured lender should make certain that no winding up petition has been presented against the company by undertaking a search at the Grand Court. A secured lender should also ensure that an appropriate special resolution placing the company into voluntary liquidation has not been passed by the members in general meeting, and, in respect of a limited duration company, that a triggering event has not occurred: a security document executed by the directors of the company after a voluntary winding up has been commenced without the consent of the liquidators or the members of the company is likely to be void unless ratified.

Transfers of shares pursuant to section 99

Following the decision of Smellie C.J. in In re Bayou Offshore Master Fund Limited [2007 CILR 434], it is typical for applications seeking the validation of a transfer of shares in a Cayman company in liquidation to be dealt with by the Grand Court administratively, that is, without the need to attend an oral hearing before the Grand Court. In Re Bayou, which involved the transfer of shares in a Cayman Islands mutual fund which was in liquidation, Smellie C.J., stated that ‘in order to save the costs of what are anticipated to be routine applications, any such application may be made in writing and may be considered administratively by a judge.’

The historical rationale for the prohibition on a transfer of shares relates to the obligation on the members of a company to contribute to the assets of the company, limited to the par value (particularly in the context of an investment fund). However, it is more common now for shares to be issued as fully paid or with nominal par value. Accordingly, the Grand Court recognises that a transfer of fully paid shares should generally be validated on an administrative basis.4 The Grand Court is also familiar with applications made pursuant to section 99 to facilitate the market for buying and selling shares held in Cayman Islands companies in official liquidation proceedings.

Order 19 of the Companies Winding Up Rules 2018 expressly addresses applications made pursuant to section 99 of the Companies Law seeking a validation order for the transfer of shares in companies in liquidation. It provides that where an application is made pursuant to Section 99 ‘for an order validating the transfer or proposed transfer of any shares of a company may be made by its liquidator or by the transferor or transferee of the shares in question’ and ‘provided that the shares in question are fully paid and the liquidator does not object to the transfer, the application shall be made by a letter addressed to the Judge to whom the proceeding is assigned.’ Such an application ‘shall be supported by an affidavit, confirming that the shares are fully paid and that the liquidator has no objection to the transfer, and a draft of the order sought by the applicant’.

In circumstances where those prerequisites cannot be met, a substantive application would need to be made and heard orally before the assigned judge in the liquidation proceedings.

Notes

3 Section 142 of the Companies Law.
4 Order 19, rules 4 and 5 of the Companies Winding Up Rules 2018.
What will the Grand Court consider on the application for a validation order?

The Companies Law does not prescribe the circumstances in which the Grand Court may validate any particular disposition: the Grand Court’s discretion pursuant to section 99 is unfettered. That said, guidance on the principles to be taken into account by the Grand Court when considering whether to grant a validation order under section 99 can be derived from case law, and different considerations may apply depending on whether the company concerned is solvent or insolvent.

In relation to solvent companies, the recent decision of the CICA in Aurora Funds Management Limited et al v Torchlight GP Limited (Unreported, Morrison JA, 27 April 2018) reaffirmed the principles which the Grand Court will take into account in determining whether to grant a validation order. The CICA cited the dicta of Henderson J. in In Re Fortuna Development Corporation [2004-2005] CILR 533 in which the Grand Court held that ‘there are four elements which must be established before an applicant is entitled to a validation order...’.

These are:
1. the disposition must be within the powers of the directors;
2. there must be evidence to show that the directors believe the disposition is necessary or expedient in the interests of the company;
3. the directors must have reached that decision in good faith; and
4. the reasons for the disposition must be shown to be ones which an intelligent and honest director could reasonably hold.

In In Re Fortuna Development Corporation, Henderson J. added that the test the applicant must satisfy is not high but there must be a body of evidence which, viewed objectively, establishes that the decision is one which a reasonable director, having only the best interests of the company in mind, might endorse.

The CICA also cited In Re Cybervest Fund [2006] CILR 80, in which Smellie C.J. agreed with and adopted the guidelines set out in Re Fortuna Development Corporation, but added that the Grand Court should also consider whether irregularities in the conduct of the affairs of the company can be shown, even if the company is clearly solvent.

In In Re Cybervest Fund, it was alleged that there had been a deliberate attempt by the fund managers to divert the company’s assets for their own purposes and that the substratum of the company had failed. Smellie C.J. declined to make a validation order in that case on the basis that he did not consider that ‘the directors could properly hold that these dispositions are necessary or expedient in the interests of the company at this time’. The Torchlight case also concerned alleged irregularities in the conduct of the affairs of the exempted limited partnership which went to the very heart of the question as to whether a validation order be granted in the circumstances.

In relation to insolvent companies, the principal concern of the Grand Court in considering an application for a validation order will be to seek to avoid prejudice to the interests of unsecured creditors of the company (In the Matter of Freerider Limited [2010 (2) CILR 154, citing the decision of the English Court of Appeal in Denney v John Hudson & Co Ltd [1992] BCC 503). Generally speaking, available assets of an insolvent company will be distributed to unsecured creditors on a pari passu basis, meaning that all creditors will share equally in such assets in proportion to the debt due to each creditor.

In Express Electrical Distributors Ltd v Beavis and others [2016] EWCA Civ 765, the English Court of Appeal considered and reaffirmed the English decision of Re Gray’s Inn Construction Co Ltd [1980] 1 WLR 711 which held that save in exceptional circumstances, a validation order should only be made in respect of an insolvent company if there is some special circumstance which shows that the disposition in question will be (in a prospective application case) or has been (in a retrospective application case) for the benefit of the general body of unsecured creditors, such that it is appropriate to disapply the usual pari passu principle.

The English Court of Appeal in Express Electrical Distributors Ltd however rejected the long held position following Re Gray’s Inn that a disposition carried out in good faith in the ordinary course of business at a time when the parties were unaware that a winding up petition had been presented should normally be validated by the court, noting that validation on such basis could well prejudice the interests of the body of unsecured creditors. The judgment serves as a reminder that those seeking validation orders to continue trading, or for specific creditors to be paid, must produce clear and credible evidence that the payment will, or did, produce a benefit to the general body of creditors. This decision, though not technically binding, would be regarded as persuasive to the Grand Court.

Conclusion

The interests of the creditors of a company in liquidation are paramount. In line with this fundamental principle, section 99 of the Companies Law provides protection for unsecured creditors of a company that is subsequently wound up. It has long been established that, in the case of an insolvent company, a validation order, which will disapply the usual pari passu principle, should only be made in exceptional circumstances which demonstrate that the disposition is of benefit to the general body of creditors. Recent
authorities suggest that it is now no longer sufficient that payments made in good faith and in the ordinary course of business without knowledge of the winding up proceedings will result in a validation order. As such, counterparties should closely monitor trading relationships regularly in an attempt to avoid issues with companies in financial difficulties given the potential for payments needing to be repaid to an insolvent estate in the absence of exceptional circumstances.
Welcome Irish High Court Ruling in Corporate Rescue Case: Clarification on Import and Effect of Undertakings to Discharge Current Revenue Liabilities During Period of Protection Afforded by Examinership

Gavin Smith, Partner, Walkers, Dublin, Ireland

Overview
It has become a frequent feature for Irish companies seeking court protection through examinership to provide a written undertaking at the petition stage that it will discharge in full post-petition taxes to the Irish Revenue Commissioners (the ‘Revenue’) that accrue and fall due during the period of protection. A recent written judgment of the Irish High Court (Ms Justice Baker) in Harley Mechanical Services Ltd & the Companies Act 2014 (the ‘Proceedings’) has provided welcome clarity on the import and effect of such undertakings.

Walkers’ Dublin office acted on behalf of the examiner/liquidator in the Proceedings and was successful in challenging an order which had the effect of deeming unpaid Revenue liabilities as costs in the examinership and thus given special status such that these monies would be unavailable to the liquidator to discharge his own fees and the claims of other creditors.

Examinership
Ireland boasts a powerful, flexible, corporate restructuring process, which international corporates will recognise as similar to the Chapter 11 of the US Bankruptcy Code. Examinership is a court supervised statutory process available to an insolvent company which has a reasonable prospect of survival as a going concern. The procedure is commenced by way of presentation of a petition to the Irish High Court (the ‘Court’) seeking the appointment of an independent office holder called an examiner (invariably an insolvency practitioner) to the company and, if appropriate, related companies. Upon the presentation of the petition, the company is placed under the protection of the Court which affords it extensive protection from enforcement or execution action by its creditors. Usually the petitioner is the company itself. However, other stakeholders, such as directors, creditors and shareholders holding at least 10% of the issued share capital of the company, also have standing to present an examinership petition.

From an EU law perspective, examinership is recognised as a main insolvency proceeding for the purposes of the Recast European Insolvency Regulation (‘EIR Recast’). The company which is the primary subject of the petition must have its centre of main interests (‘COMI’) in Ireland. Companies which are incorporated or registered elsewhere in the EU but have their COMI in Ireland can be the subject of the petition. It is also possible to apply for the appointment of an examiner to a foreign (i.e. non-EU) company, as a related company, if that company may be wound up by the courts of Ireland.

Like Chapter 11, examinership is a debtor-in-possession process whereby (save in exceptional circumstances) the directors retain control and executive power of the company. The Examiner sits along side the directors and management of the company. He or

Notes
2 The legislative code for examinership is set out in Part 10 of the Irish Companies Act 2014 (‘the Act’).
3 Under section 2 of the Act, a related company is broadly defined and includes but is not limited to a holding company or subsidiary; a company or companies entitled to exercise control the exercise of more than one half of the voting power at any general meeting of the first company; where the businesses of the companies have been so carried on that the separate business of each company is not readily identified; or where there is another body corporate to which both companies are related.
4 As per the EIR Recast, a debtor company’s COMI is generally the place where it conducts the administration of its interests of a regular basis as ascertainable by third parties. In most cases there is a rebuttable presumption that a corporate debtor’s COMI is the location of its registered office.
5 Under the Act, a foreign company may be wound up by the Irish High Court if it has a sufficient connection to the State and there is a reasonable possibility that if a winding up order is made, it will be of benefit to those applying for the winding up order. For example, both BVI and Jersey companies have been considered as being liable to be wound up in Ireland in previous cases.
she has a brief period of time (up to 100 days from the date the petition is presented) to put together a restructuring plan to save the company, that is, the scheme of arrangement. This will usually involve sourcing fresh investment and agreeing write-downs with the company’s creditors.

The scheme of arrangement is presented to the company’s creditors and members at duly convened meetings and voted upon. A striking feature of examinership is that only one class of impaired creditors needs to vote in favour of the proposals, by way of simple majority in number and value, before the Court has jurisdiction to consider whether or not to approve the scheme of arrangement.

The threshold for court approval is that the Court must be satisfied that the proposals will, if implemented, have a reasonable prospect of facilitating the survival of the company as a going concern and that the proposals are not unfairly prejudicial to any interested party. Generally speaking, proposals will not be considered unfairly prejudicial if the dividend/outcome for creditors under the scheme of arrangement is more favourable than it would be in a receivership or liquidation.

**The Proceedings**

In the Proceedings, Walkers were initially instructed to represent and advise the proposed examiner, Mr Aengus Burns of Grant Thornton. Mr Burns was appointed as examiner (the ‘Examiner’) on an interim basis on 28 June 2017 and his appointment as Examiner was later confirmed by the Court on 11 July 2017. The petition for Mr Burns to be appointed as Examiner was supported by an affidavit of a director of the company sworn 27 June 2017. The affidavit contained an undertaking on behalf of the company to discharge its Revenue liabilities as they fell due during the period of protection afforded by the examinership process. On 5 September 2017, the Examiner made an application to have the protection of the Court lifted and have the company put into liquidation in circumstances where investment could not ultimately be secured, which investment was needed for the company to have a reasonable prospect of survival. On foot of Mr Burns’ application, the company was wound up by the Court and Mr Burns was appointed as Liquidator to the company (the ‘Liquidator’).

Later in the afternoon of 5 September 2017, after the end of the normal Court day, Counsel on behalf of the Revenue appeared before Ms Justice Baker on an ex parte basis and advised the Court that contrary to the company’s undertaking to discharge its Revenue liabilities as they fell due during the protection period, the company had failed to discharge its tax liabilities for the period 1 July to 31 July 2017, which were due to be discharged on or before 23 August 2017. Counsel for the Revenue sought and was granted an order that the sum due for the said period be treated as a priority expense in the examinership (the ‘Order’), with the result that these monies would not be available to the Liquidator to discharge his own fees and the claims of other creditors. The Liquidator applied to have the Order set aside.

**Liquidator’s application**

An exchange of affidavits ensued between the Liquidator and the Revenue in which both sides alleged a lack of candour or good faith on the part of the other. The Liquidator took issue with the fact that the Revenue did not make the application earlier in the day on 5 September 2017 and the fact that the application was made ex parte. Counsel for the Revenue argued that the Examiner should have alerted the Court immediately once he became aware that the Revenue liability had not been discharged sometime after 23 August 2017. The Court assessed both parties’ allegations and concluded that there was no lack of candour or good faith on the part of either party and proceeded to address the substance of the Liquidator’s application i.e. what was the appropriate result arising from the breach of the undertaking.

It was noted by the Court that undertakings in a form similar to that given by the company in the Proceedings are commonly given by companies seeking to have an examiner appointed. The Court noted that a practice has evolved whereby the Revenue, who can frequently be a significant creditor and thus on notice of a petition to appoint an examiner to a company, will consider taking a neutral position when such an undertaking is given and that the giving of such an undertaking is a factor that will be taken into account in the exercise by the Court of its discretionary power to appoint an examiner. The Court then considered the purpose of the undertaking, to whom the undertaking is given and the effect of a breach of the undertaking.

The Court noted that notwithstanding the import and solemnity of the undertaking, the effect of a breach of the same is not to alter or improve the priority status of the Revenue’s debt. The Court rejected the argument made by the Revenue that the Examiner had breached the undertaking, which was given by and on behalf of the Company. The Court found that the undertaking to discharge the Revenue liabilities was not an undertaking given to the Revenue; but was an undertaking given to the Court and was to be treated for most purposes as being equivalent to a Court order in identical terms. The Court then proceeded to consider the effect of a breach of such an undertaking.

Counsel for the Revenue argued that the Order did no more than give effect to the situation that would have transpired had the company complied with the terms of the undertaking. It was also argued that the Order was an appropriate sanction to the Examiner/Liquidator for his failure to advise the Court immediately upon becoming aware of the breach of the undertaking by the company. The Liquidator argued that the Court...
Welcome Irish High Court Ruling in Corporate Rescue Case

did not have jurisdiction to make the Order as only the Examiner could certify liabilities as being costs of the examinership, albeit subject to Court supervision.

Ultimately, after a careful analysis of the relevant legislation and case law, the Court accepted the argument advanced by the Examiner/Liquidator and set aside the Order.

Case significance

The Proceedings provide welcome clarity to the law on examinership, providing important guidance on the nature and effect of undertakings to discharge Revenue liabilities that arise during the protection period, the potential effect of a breach of the same and clarification on the role of the Court in certifying liabilities as costs in the examinership process.

While examinership did not save the company in this instance, it can often provide a means of survival for certain companies in financial difficulties or those facing insolvency. Directors of such companies would do well to seek professional advice at the earliest available opportunity in order to explore this as a restructuring or rescue option.

Examinership as a cross border restructuring tool

Examinership has been a feature of the Irish corporate restructuring landscape since its inception in 1990 and therefore, as an English speaking common law jurisdiction, it benefits considerably from being administered by a dedicated division of the Irish High Court that has nearly three decades of accumulated knowledge and specialist expertise. Furthermore, in recent years, there have been a number of significant international / cross border restructurings which have utilised examinership successfully, namely the telecommunications group Eircom and the oil and gas group Petroceltic and so complex multi-jurisdictional issues are well-known to the Irish Courts.

In light of the legal uncertainty which Brexit has created, it is possible that Ireland will become a more popular legal jurisdiction for directors of international corporates in difficulties and their advisors to consider. With a legal system closely analogous to the highly respected English system, it benefits from the fact that examinership will be recognised as a main insolvency proceeding in the remaining EU member states and that judgments of the Irish Courts are and will continue to be recognised under Brussels Recast.

Brexit also comes at a time when Europe is embracing Chapter 11 which is the inspiration behind the EU Commission’s proposal for a directive on Insolvency, Restructuring and Second Chance. In this regard, the vast majority of the terms of the proposals envisaged by the EU Commission, as far as corporates are concerned, are already a tried and tested feature of the Irish corporate restructuring legal system through the examinership process. As explained in greater detail earlier in this article, examinership is available to any companies that have their COMI in Ireland.

Notes

6 Eircom Limited & Ors & the Companies (Amendment) Act 1990 Record Number 2012/175COS.
7 Petroceltic International plc & the Companies Act 2014 Record Number 2016/75COS.
8 Walkers acted for and advised key stakeholders in both of these examinerships.
10 Published in November 2016 and currently undergoing the EU legislative procedure.
Synopsis

The purpose of this article is to provide a brief guide as to the use of statutory demands (a ‘Demand’ or collectively ‘Demands’) in both the Cayman Islands and the British Virgin Islands (the ‘BVI’). In particular, this article will seek to summarise the basic statutory requirements of Demands in both the Cayman Islands and the BVI, highlight some key differences between the use of Demands in both jurisdictions and provide an overview as to certain strategic considerations when a creditor is contemplating issuing a Demand or a debtor is responding to a Demand.¹

A. What is a Demand?

In summary, a Demand is a formal written demand served by a creditor on a debtor for payment of a debt. If the debtor fails to:

1. satisfy, secure or compound the debt to the satisfaction of the creditor or reduce the debt to below the minimum statutory requirement (within 21 days from the date of service of the Demand);² or
2. obtain written confirmation from the creditor that the Demand is withdrawn; or
3. apply to the BVI High Court (the ‘BVI Court’) to set aside the Demand within 14 days from the date of service of the Demand (‘Set Aside Application’)³ (applicable in the BVI); or
4. obtain an injunction order from the Grand Court of the Cayman Islands (the ‘Grand Court’ and together with the BVI Court, the ‘Courts’) restraining the creditor from presenting a winding up petition in respect of the debtor (an ‘Injunction’) or an undertaking (an ‘Undertaking’) from the creditor not to present a winding up petition pending resolution of the debtor’s application to restrain the creditor (‘Injunction Application’ and together with the Set Aside Application, the ‘Applications’) within 21 days from the date of service of the Demand (applicable in the Cayman Islands),

it is at risk of having winding up proceedings commenced against it.

In both the Cayman Islands and the BVI, failure to satisfy a Demand: (i) gives rise to a presumption of insolvency;⁴ and (ii) is a ground upon which the Courts⁵ can make a winding up order against the debtor (collectively referred to as the ‘Consequences’).

B. Requirements of a Demand

Table 1 below shows a summary of the key statutory requirements of a Demand in the Cayman Islands and in the BVI.

C. Strategic considerations when contemplating issuing a Demand

If the creditor is confident as to the validity of its debt (which can, from an offshore perspective, often be governed by a foreign law and therefore require foreign legal advice), then, in both jurisdictions, a Demand can be a cost effective and useful precursor to a winding up petition, noting the Consequences that arise if the Demand is left unsatisfied.

Notes

¹ This article only considers Demands in respect of unsecured debt and in the context of corporate debtors (and not individuals). This article is intended for informational purposes only and does not constitute legal or other professional advice or an opinion of any kind.
² Section 155(2)(d) of the BVI Insolvency Act, 2003 (as revised) (the ‘BVI Insolvency Act’); Section 93(a) of the Cayman Islands Companies Law (2018 Revision) (‘Cayman Companies Law’).
³ Section 156 of the BVI Insolvency Act.
⁴ Section 8(1)(a) of the BVI Insolvency Act and Section 93(a) of the Cayman Companies Law.
⁵ Section 162(1)(a) of the BVI Insolvency Act; Section 92(d) of the Cayman Companies Law.
## Table 1.

<table>
<thead>
<tr>
<th>BVI</th>
<th>Cayman Islands</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt due and payable to the demandor at the time of the Demand</td>
<td>Debt due and payable to the demandor at the time of the Demand</td>
</tr>
<tr>
<td>Minimum Debt of USD 2,000</td>
<td>Minimum Debt of CI$ 100</td>
</tr>
<tr>
<td>Demand in writing and specifies the nature of the debt and its amount</td>
<td>Demand in writing in Companies Winding Up Rules Form No. 1, which states the amount, the date on which the debt fell due, the currency of the debt and the consideration for it</td>
</tr>
<tr>
<td>Dated and signed by the creditor or a duly authorised person on behalf of the creditor</td>
<td>Signed by the creditor or, if the creditor is a firm, any partner of the firm or, if the creditor is a body corporate, any director or officer duly authorised to make the Demand. Must also contain the creditor's address (or contact details of the signatory, if not the creditor)</td>
</tr>
<tr>
<td>Require the debtor to pay the debt or to secure or to compound for the debt to the reasonable satisfaction of the creditor within 21 days of the date of service of the Demand</td>
<td>Include a statement that if payment is not made within 21 days of the date upon which it was served on the debtor, the debtor will be deemed to be insolvent and a winding up petition may be presented against the debtor in accordance with section 92(d) of the Cayman Companies Law</td>
</tr>
<tr>
<td>State that if the Demand is not complied with, the creditor may make an application to the BVI Court for the appointment of a liquidator</td>
<td>See above</td>
</tr>
<tr>
<td>Set out the rights of a person to make the Set Aside Application</td>
<td>No equivalent provision as no statutory mechanism available to set aside the Demand</td>
</tr>
<tr>
<td>No equivalent provision as no statutory requirement for information for payment</td>
<td>Contain information about ways in which the debtor may make payment, including details of a bank account to which the amount owing may be wire transferred</td>
</tr>
<tr>
<td>Comply with and be served in accordance with the BVI Rules: in summary, a Demand is validly served when an original hard copy is delivered by hand to the debtor’s registered office.</td>
<td>Comply with and be served in accordance with the Cayman CWR: in summary, a Demand is validly served when an original hard copy is delivered by hand to the debtor’s registered office. Email or Fax alone will not suffice</td>
</tr>
</tbody>
</table>

If the amount claimed includes any charge by way of interest not previously notified to the debtor as included in its liability, or any other charge accruing from time to time, the Demand must state the grounds upon which the debtor is liable to pay such interest or charges and contain particulars of the way in which interest or charges are calculated.

### Notes

6 Section 155(2)(a) of the BVI Insolvency Act.
7 Section 93(a) of the Cayman Companies Law.
8 Rule 149(1) of the Insolvency Rules (Revised 2013) (‘BVI Rules’).
9 Section 93(a) of the Cayman Companies Law.
10 Section 155(2)(b) of the BVI Insolvency Act.
11 Order 2 Rule 2(1) of the Cayman Companies Winding Up Rules, 2018 (‘Cayman CWR’).
12 Order 2 Rule 2(3) of the Cayman CWR.
13 Section 155(2)(c) of the BVI Insolvency Act.
14 Order 2 Rule 2(2) of the Cayman CWR.
15 Order 2 Rule 2(5) of the Cayman CWR.
16 Section 155(2)(d) of the BVI Insolvency Act.
17 Order 2 Rule 2(6) of the Cayman CWR.
18 Section 155(2)(e) of the BVI Insolvency Act.
19 Section 155(2)(f) of the BVI Insolvency Act.
20 Order 2 Rule 2(7) of the Cayman CWR.
21 Section 155(2)(g) of the BVI Insolvency Act.
22 Rule 26(2)(a) of the BVI Rules.
23 Section 93(a) of the Companies Law; Order 2 Rule 3 of the Cayman CWR.
24 Rule 149(2) of the BVI Rules.
25 Order 2 Rule 2(4) of the Cayman CWR.
The primary benefits of issuing and serving a Demand on a debtor are:

1. quick to prepare;
2. out of court;
3. inexpensive;
4. can be withdrawn by the creditor at its own volition (albeit that if it is withdrawn after the Applications have been made, then there are likely to be cost consequences for the creditor);
5. can lead to payment and/or settlement negotiations in and of itself as debtors are often compelled to act (after having ignored the debt previously) given the Consequences that arise if a Demand is left unsatisfied; and
6. the Consequences (on the assumption the Demand is left unsatisfied for the requisite statutory period) facilitate the granting of a winding up order by the Courts.

However, irrespective of the above benefits, a Demand is, as a matter of both Cayman Islands and BVI law, not a necessary precursor to wind up a debtor and, in certain circumstances: it can delay a winding up order being made against a debtor. In summary, this is because the Demand can give the debtor an opportunity to make the Applications (usually on the basis that the debt is disputed – which we examine in greater detail in section D below) which could result in the creditor being stalled by litigation and not being able to progress the winding up proceedings in a timely fashion.

D. Strategic considerations when served with a Demand

As referenced above, upon being served with a Demand (and on the assumption that the creditor does not agree to withdraw the Demand), a debtor broadly has the following options:

1. satisfy, secure or compound the debt to the satisfaction of the creditor or reduce the debt to below the minimum statutory requirement (as detailed in section A); or
2. file the Set Aside Application within 14 days from the date of service of the Demand (BVI); or
3. obtain an Injunction or Undertaking within 21 days from the date of service of the Demand (Cayman Islands).

In the event the debtor pays the debt in its entirety, secures or compounds the debt to the satisfaction of the creditor or reduces the debt below the statutory minimum requirements (as set out above) or obtains written confirmation from the creditor that the Demand is withdrawn, the matter is usually resolved. If the debtor seeks to challenge the Demand, it has the following options:

i. Set Aside Application – BVI

A debtor who wishes to set aside the Demand must, within 14 days from the date of service, apply to the BVI Court for an order setting aside the Demand.26

The Set Aside Application must be supported by an affidavit specifying the date upon which the debtor was served with the Demand and state the grounds upon which the debtor claims that the Demand should be set aside.27

When the Set Aside Application is filed at the BVI Court, the 21-day compliance period ceases to run from the date of filing.28 The BVI Court will set aside a Demand if it is satisfied that:

1. there is a substantial dispute as to whether:
   a. the debt is owing or due; or
   b. a part of the debt (which would reduce the undisputed amount of the debt to less than the statutory minimum amount of USD 2,000) is owing or due;
2. the debtor has a reasonable prospect of establishing set-off, counterclaim or cross-claim in an amount that would reduce the debt to less than USD 2,000; or
3. the creditor holds security for the debt and the unsecured portion of the debt claimed is less than USD 2,000.29

Additionally and in any event, the BVI Court retains discretion to set aside a Demand if it is satisfied that there would be substantial injustice because there is a defect in it or for some other reason.30

ii. Injunction Application – Cayman Islands

The Cayman Islands has no statutory mechanism in which a debtor can apply to set aside a Demand, as in the BVI.

Notes

26 Section 156(2) of the BVI Insolvency Act. Note that this time cannot be extended.
27 Rule 152(1) of the BVI Rules.
28 Section 156(4) of the BVI Insolvency Act.
29 Section 157(1) of the Insolvency Act.
30 Section 157(2) of the Insolvency Act.
Instead, the remedy available to a debtor is to promptly make the Injunction Application and either obtain an Injunction or Undertaking within 21 days from the date of service of the Demand. The Grand Court is likely to grant an Injunction preventing the presentation of a winding up petition if it appears that the debtor is solvent and that one of the following apply:

- the debt is genuinely disputed on substantial grounds;31 or
- the debtor has a cross-claim or right of set-off against the creditor that exceeds the amount claimed in the Demand or reduces the undisputed amount of the debt to less than the statutory minimum amount of CI$ 100; or
- the debtor has a reasonable excuse for not paying the debt claimed.

In essence, the debtor needs to show that the presentation of a winding up petition would be an abuse of process.

iii. Substantial dispute

In both the BVI and the Cayman Islands, the primary basis upon which a debtor seeks to challenge the validity of a Demand is on the basis that the underlying debt is disputed. In both jurisdictions, the debtor must prove that the debt is bona fide disputed on substantial grounds. We briefly set out below the applicable tests in the BVI and the Cayman Islands as to whether or not a debt is bona fide disputed on substantial grounds.

a. BVI

In the BVI the ‘substantial dispute’ test is on a statutory footing. In s. 157 of the BVI Insolvency Act the requirements are:

‘(1) The Court shall set aside a statutory demand if it is satisfied that

(a) there is a substantial dispute as to whether –

(i) the debt; or

(ii) a part of the debt sufficient to reduce the undisputed debt to less than the prescribed minimum, is owing or due;’

The leading case is Sparkasse Bregenz Bank AG and in the Matter of Associated Capital Corporation,32 in which the then Chief Justice said:

‘the dispute must be genuine in both a subjective and objective sense... the reason for not paying the debt must be honestly believed to exist and must be based on substantial or reasonable grounds. Substantial means having substance and not frivolous, which disputes the Court should ignore. There must be so much doubt and question about the liability to pay the debt that the Court sees that there is a question to be decided. The onus is on the company to bring forward a prima facie case which satisfies the Court that there is something which ought to be tried.’

The BVI Court of Appeal in the matter of Jinpeng Group Limited v Peak Hotels and Resorts Limited,33 recently clarified that it will undertake the critical task of considering whether or not there is a substantial and bona fide dispute.

b. Cayman Islands

The position in the Cayman Islands is broadly similar to the BVI: In Re Duet Real Estate Partners I LP (unreported, 7 June 2011), Duet sought a declaration that there was a genuine dispute in relation to its debts and an injunction to restrain the presentation of a winding up petition where the underlying loan agreement contained an arbitration clause and an arbitration had already been commenced. Having considered the evidence presented to the Grand Court, Jones J determined that there was no bona fide dispute of substance and that the arguments made by Duet in that regard were ‘nothing more than a disingenuous delaying tactic’. He therefore refused to grant the declaration and injunction sought. Subsequently, in In re Ebullio Commodity Master Fund LP (unreported, 24 May 2013), Jones J took a similar position determining that the existence of an arbitration agreement and arbitration proceedings being on foot would only be relevant if the Cayman Court determined that the dispute was genuine and on substantial grounds.34

E. Conclusion

The Demand is an inexpensive and useful precursor to winding up proceedings, albeit, not necessary for the purposes of commencing winding up proceedings. However, it is important to be mindful of the tactics which can be employed by both a creditor in issuing a Demand and a debtor in responding to a Demand.

Notes

32 BVICHMAP 2002/0010.
33 BVICHMAP 2014/0025 and BVICHMAP 2015/0003.
Bermuda’s ‘Light-Touch’ Approach to Cross-Border Restructuring

Nicole Tovey, Partner, and Benjamin McCosker, Senior Associate, Walkers, Bermuda

Introduction

Bermuda has no direct equivalent to the statutory moratorium against creditor action that applies to an insolvent English company in administration proceedings pursuant to Schedule B1 to the Insolvency Act 1986, or to an American corporate reorganisation pursuant to Chapter 11 of the United States Bankruptcy Code. This legislative gap has been enthusiastically filled by the Bermuda Supreme Court’s interpretation of the power to appoint liquidators or provisional liquidators under section 170 of the Companies Act 1981 (the ‘Act’) as including the power to appoint provisional liquidators for restructuring purposes. This article explains how for almost twenty years now, de facto debtor-in-possession, management-led restructurings have been facilitated in Bermuda by reference to this bespoke restructuring regime.

‘Light-touch’ provisional liquidation for restructuring purposes

The power of the Bermuda Supreme Court (the ‘Bermuda Court’) to appoint provisional liquidators is typically employed in circumstances where a company’s assets need to be preserved and protected pending the hearing of a winding up petition where there is evidence of actual or potential misapplication or dissipation of company assets. However, this provisional liquidation jurisdiction can also be invoked to assist in the context of cross-border restructurings in circumstances where provisional liquidators are appointed on a ‘light-touch’ basis.

The distinguishing feature of a Bermuda ‘light-touch’ provisional liquidation is that provisional liquidators are appointed – oftentimes on the company’s own petition – to independently oversee a restructuring process, with a focus on protecting creditors’ interests. The ultimate restructuring can manifest itself in various ways, although an equity injection by a ‘white knight’ investor, a purchase of distressed debt by a third party and/or a scheme of arrangement whereby the company makes a compromise or arrangement with its members and/or creditors pursuant to section 99 of the Act are typically involved. Regardless of what form the restructuring ultimately takes, the company has the benefit of a statutory moratorium, or stay, on proceedings being brought against the company which automatically arises upon the appointment of provisional liquidators and continues for as long as the provisional liquidators remain in office. This is a particularly valuable protection for imperilled boards of companies in the zone of insolvency, where creditor threats to commence proceedings against the company can distract from the primary task of implementing a financial or operational restructuring to ensure that the company may continue as a going concern.

It is not the role of the ‘light-touch’ provisional liquidators to ultimately determine whether or not a certain restructuring proposal should be pursued. That is of course a question for the creditors and members of the company.

Typically, evidence should be shown to the Bermuda Court at the appointment stage that there is a viable restructuring proposal and a good prospect that certain creditors of certain value will be either supportive of the proposal or have indicated that they are willing to wait and see what the company will propose and accordingly do not wish for a winding up order to be made immediately. Subsequent to the appointment of the provisional liquidators, if the necessary creditor support cannot be obtained and a satisfactory restructuring proposal cannot be agreed upon, the provisional liquidators would report this to the Bermuda Court and, in most cases, a winding up of the company would ensue.

Jurisdictional foundation for the ‘light-touch’ provisional liquidation regime

The foundation for the provisional liquidation restructuring jurisdiction was set out in the 1999 judgment of Ward CJ (as he then was) in Re ICO Global Communications (Holdings) Ltd as thus:

Notes

1 Note that secured creditors may enforce their security notwithstanding the moratorium, except for in circumstances where a contractual standstill has been negotiated between the relevant secured creditors and the company.
‘I am satisfied that the Court is given a wide discretion and had jurisdiction under section 170 of the Companies Act and Rule 23 of the Companies (Winding-Up) Rules 1982 to make such an Order. Under it the directors of the Company remained in office with continuing management powers subject to the supervision of the joint provisional liquidators and of the Bermuda Court’.2

In the 2006 decision of Discover Reinsurance Co v PEG Reinsurance Co Ltd, Kawaley J (as he then was) characterised the ‘light-touch’ provisional liquidation regime as part of a ‘legal quid pro quo’:

‘[I]n circumstances where no suspicions about the integrity of the directors really exist, the provisional liquidator is appointed as part of legal quid pro quo for receiving the benefit of the stay on proceedings that the appointment guarantees, Bermuda law presently lacking a formal equivalent of the US Chapter 11 regime or the English administration proceedings’.3

Later, in the 2016 decision In the Matter of Up Energy Development Group Limited, Kawaley CJ described the advantages of the Bermuda ‘light-touch’ provisional liquidation regime in the following terms:

‘It is the involvement of JPLs, embedded with the restructuring troops, which relieves this Court of the burden shouldered by US Bankruptcy Court judges of resolving a myriad of disputes between the restructuring protagonists...All conflicts are typically resolved before the scheme document is finalized, out of court, with the JPLs playing a generally unheralded but crucial mediating role. They bring a high degree of efficiency and economy to Bermudian restructuring proceedings which would likely be lost in a proceeding without the usual appointment’.4

Most recently, in another decision of Kawaley CJ In the Matter of Z-Obee Holdings Limited, reference was made to the fact that the Bermuda Court ‘had an established practice of appointing JPLs to manage a restructuring...’, and that ‘it is too well established today for this Court to depart from in the absence of full and compelling arguments for doing so...’. The then Chief Justice concluded with the remark that ‘the winding up jurisdiction is still being used to fulfill the primary purpose of the winding up jurisdiction: protecting the best interests of the general body of unsecured creditors’.5

The ‘light-touch’ provisional liquidation regime in practice

The appointment of ‘light-touch’ provisional liquidators to a Bermuda company is preceded by the presentation of a winding up petition to the Bermuda Court, pursuant to section 163 of the Act. Such petition can be presented by the company itself, or by any creditor or contributory of the company.6 The petitioner will simultaneously make an application by summons for the appointment of provisional liquidators, and will typically by that summons propose a form of order setting out the ‘light-touch’ powers to be granted.

In making its application for the appointment of provisional liquidators, the petitioner will identify its proposed appointees and typically adduce evidence as to their suitability for the role. The Bermuda Court will be astute to ensure that the proposed appointees are not only competent, but are also capable of winning the confidence of both the creditors and the company. As Hellman J observed in In the matter of Opus Offshore Limited:

‘the efficiency of any restructuring within a provisional liquidation depend[s] in large part upon good will and collegiality reigning across the joint provisional liquidator and management restructuring teams’.7

Where there is a conflict between the petitioner (if not the company itself) and the company as to the selection of provisional liquidators, the Bermuda Court will have regard to the nominees’ respective qualifications and experience, as well as the existing relationship (if any) between the nominees and the company and creditors and any potential conflicts which could arise therefrom. In the Up Energy matter, for example,8 concerns were raised by the petitioner as to the independence of the company’s nominee given their prior appointment by the company as independent restructuring advisers. In the event, the Bermuda Court appointed the petitioner’s nominee as the Bermuda-based liquidator, and the company’s nominees as the Hong Kong-based officeholders. This not only ensured that all relevant interests were evenly-represented by the provisional liquidators, but also facilitated the division and delegation of the very significant restructuring work required to be undertaken by the company, which was incorporated in Bermuda but had its operations

Notes

2 [1999] Bda LR 69 at [6].
3 [2006] Bda LR 88 at [20].
4 [2016] SC (Bda) 83 Com (20 September 2016) at [24].
6 Section 163(1) of the Act.
8 Walkers Bermuda acts for the joint provisional liquidators of Up Energy Development Group Ltd.
in mainland China and was listed on the Hong Kong Stock Exchange.

Ultimately, the choice of provisional liquidators is a matter for the Bermuda Court’s discretion, and in exercising its discretion the Bermuda Court will elect the liquidators ‘most likely to command the confidence of a majority of those who will seek to prove in the liquidation’.9

The powers of the provisional liquidator are not circumscribed by statute and instead are expressly set out in the court order appointing the provisional liquidator. Accordingly, there is scope for the provisional liquidation regime to be used with real flexibility in the context of a restructuring and the suite of powers which will be granted to the provisional liquidator will vary on a case-by-case basis depending upon how much control over the process the provisional liquidator is intended to have. Typical powers granted ‘light-touch’ provisional liquidators in aid of a potential restructuring include the powers to:

1. approach, engage, consult and negotiate with third parties, shareholders and/or creditors of the company with a view to obtaining funding for a proposed restructuring;
2. liaise with creditors, management and shareholders of the company, as well as relevant third parties, with a view to implementing a scheme of arrangement to be entered into as between the company and its creditors and/or its members; and
3. make available to relevant third parties certain books and records of the company in order to facilitate a restructuring proposal, subject to acceptable confidentiality arrangements.

Alongside these usual powers will be certain duties owed by the provisional liquidators beyond the ordinary duty of provisional liquidators to preserve the status quo pending a determination by the Bermuda Court as to whether the company should be wound up. For example, the order appointing the provisional liquidators will typically require that the provisional liquidators will consult with the company on an ongoing basis with respect to the restructuring efforts under negotiation and their perceived prospects of success – as Kawaley CJ observed in Up Energy, one of the fundamental roles of the provisional liquidators is to ‘give confidence to both creditors and the Court that the restructuring process which emerges is a credible one’.10

In all cases, the provisional liquidators, as officers of the Bermuda Court, must advise the Bermuda Court if they form the view that the proposed restructuring is no longer viable.

Company management will typically retain some degree of control over the day-to-day administration of the company during the period of provisional liquidation. The precise degree of control will depend upon the petitioner’s desire to see the company’s management remain involved. If there are allegations of fraud or other forms of impropriety on the part of the company’s management, the Bermuda Court will not permit a ‘light-touch’ provisional liquidation to proceed.11

In the event that a successful restructuring is achieved, an order will be sought from the Bermuda Court for the dismissal of the winding up petition and the discharge of the provisional liquidators from office. However, if the restructuring is unsuccessful, the Bermuda Court will make an order for winding up and appoint permanent liquidators over the insolvent company.

Company-driven versus creditor-driven restructuring

A distinguishing feature of Bermuda’s ‘light-touch’ provisional liquidation jurisdiction is that it can be invoked by either creditors or by the company itself, acting by its board of directors.12 Oftentimes a straightforward creditor’s petition will evolve into a company-driven provisional liquidation appointment and restructuring upon the company’s opposition to the petition and demonstration that a viable prospect of restructuring exists which would be in the best interests of the company’s stakeholders, in lieu of a winding up.

The order setting out the provisional liquidators’ powers will necessarily reflect the manner in which they have been appointed and at whose instigation the appointment was made. Some ‘light-touch’ appointments will be ‘lighter’ than others. For example, orders for the appointment of provisional liquidators following the filing of a winding up petition by a creditor of a company will typically provide for comprehensive and low-level access by the provisional liquidators to the company’s books and records, as well as entitling the provisional liquidators to receive advance notice of, be consulted prior to and sometimes attend meetings of the board and of company management.

Notes

9 In the matter of Opus Offshore Limited, above note 7, at [94] per Hellman J.
10 Note 4, above, at paragraph 28.
11 Discover Reinsurance Co. above note 3.
12 Compare the current position in the Cayman Islands, where absent a special resolution passed by shareholders or a specific authorisation in the company’s articles of association, the directors of a company may not petition for the winding up of the company: Re China Shanshui Group Limited [2015] (2) CILR 255; see also In the matter of CHC Group Ltd (Grand Court, unreported, 24 January 2017).
What about foreign restructuring proceedings?

The ‘light-touch’ provisional liquidation regime in Bermuda has evolved alongside and in furtherance of the Bermuda Court’s endorsement of the concept of modified universalism, or the recognition and assistance of foreign insolvency proceedings. In Re ICO Global, Ward CJ (as he then was) was faced with the all-too-familiar situation of an international liquidation with various actions being undertaken in many jurisdictions simultaneously. Speaking in support of the provisional liquidators’ pursuit of a Chapter 11 plan of reorganisation, His Lordship wrote:

‘this Court should co-operate with Courts in other jurisdictions which have the same aim in relation to the affairs of the company. It is not a question of surrendering jurisdiction so much as harmonisation of effort’.

The Bermuda Court’s view on the interaction between local insolvency proceedings and broader global restructuring efforts aligns with the position taken by Lord Sumption in the Privy Council appeal in Singularis Holdings Limited v PricewaterhouseCoopers, namely that the court of the company’s incorporation should recognise that alternative, foreign forums may be most appropriate for orderly insolvency processes, and is at liberty to provide assistance to enable such foreign insolvency processes to continue expeditiously. The Bermuda Court has consistently shown itself willing to make orders for the appointment of ‘light-touch’ provisional liquidators in order to assist the progression of a cross-border restructuring:

1. In Re C & J Energy Service Ltd No. 42239 – The Bermuda Court made orders to effectively ‘short circuit’ the formal winding up process in circumstances where the company’s affairs were being administered, and all known debt and equity interests had been extinguished, in Chapter 11 proceedings in the United States Bankruptcy Court for the Southern District of Texas, Houston (the ‘Texas Court’) and ancillary proceedings under the Canadian Companies Creditors Arrangement Act in Alberta, Canada;

2. In Re Matter of Energy XXI Ltd – The Bermuda Court appointed provisional liquidators and shortly thereafter granted the provisional liquidators’ application for a recognition order in relation to Chapter 11 proceedings underway in the Texas Court; and

3. In Re Z-Obee Holdings Ltd – The Bermuda Court appointed provisional liquidators for restructuring purposes with the same broad powers already conferred upon them by the High Court of the Hong Kong Special Administrative Region.

‘Light-touch’ provisional liquidation restructuring – the Bermuda advantage

The primary purpose of Bermuda’s ‘light-touch’ provisional liquidation regime is to permit a company the time and breathing space to implement a restructuring, under the watchful eyes of the provisional liquidators and the supervision of the Bermuda Court, which may result in the return of the company to solvency and allow it to continue as a going concern for the benefit of all its stakeholders. The availability of this regime is a tremendous asset for companies incorporated in Bermuda and promotes certainty and predictability in cross-border restructuring matters, including in cases where the shares of the company in question are publicly listed or the company has its operations in jurisdictions other than Bermuda.

Notes

13 Above note 2 at [8].
14 [2015] 2 WLRC 971.
17 Above note 5.
A Tale of Two Islands: Recognising and Assisting Foreign Officeholders in Guernsey and the Cayman Islands

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Introduction

In the increasingly internationalised corporate world, complex cross-border structures which include an offshore entity at some level within the structure are an everyday occurrence. However, the territorial limits of a court’s powers can mean that such structures present difficulties for officeholders attempting to conduct an orderly and efficient winding up of a company’s affairs.

In seeking to manage cross-border insolvency, officeholders rely on both statutory and common law powers of assistance, the latter of which have been the subject of much judicial debate since Lord Hoffman’s articulation of the principle of ‘modified universalism’ in Cambridge Gas Transport Corporation v The Official Committee of Unsecured Creditors (of Navigator Holdings Plc and others).

The principle of modified universalism essentially provides that, within the constraints of public policy, courts should co-operate across jurisdictions. Thus, if a court-appointed officeholder operating in one jurisdiction (the ‘home jurisdiction’) requires assistance from the court of a different jurisdiction (the ‘foreign jurisdiction’), the court in that foreign jurisdiction may, as a matter of common law, provide such assistance as that court properly can. Establishing what is proper in a given instance will depend both on the powers available to the court in the home jurisdiction, and also the powers available to the court in the foreign jurisdiction.

While important, the ‘golden thread’ of modified universalism is not a silver bullet to every jurisdictional difficulty faced by officeholders – each jurisdiction interfaces with the principle of modified universalism in its own way, as demonstrated by a comparison of the different approaches adopted in Guernsey and the Cayman Islands. Neither of these offshore jurisdictions is a party to the UNCITRAL Model Law on Cross-Border Insolvency 1997 (the ‘Model Law’) and statutory powers of assistance are only available in certain circumstances, with the result that the approach of each jurisdiction to the principle of modified universalism will often be determinative of assistance that can be provided to a foreign officeholder.

Statutory assistance

Guernsey

As explained above, Guernsey is not a signatory to the Model Law and is not a member of the European Union. As such, a foreign officeholder cannot rely upon the EU Regulation on Insolvency Proceedings or the Model Law to seek recognition and assistance in Guernsey. However, for liquidations occurring in England and Wales, Scotland, Northern Ireland, Jersey or the Isle of Man, section 426 of the English Insolvency Act 1986 (the ‘Insolvency Act’) has been extended to Guernsey by the Insolvency Act 1986 (Guernsey) Order, 1989. As a result, the Royal Court of Guernsey (the ‘Royal Court’) has a statutory power to provide assistance to officeholders appointed in those jurisdictions.

The procedure under section 426 of the Insolvency Act involves the foreign officeholder applying to the court in their home jurisdiction (i.e. England and Wales, Scotland, Northern Ireland, Jersey, or the Isle of Man) for an order that the home court send a letter of request to the Royal Court seeking assistance. Generally, the Royal Court must comply with the request unless it offends public policy or the outcome would be oppressive.

In addition, section 426(5) of the Insolvency Act gives the Royal Court the ability to apply the insolvency law of either Guernsey or the foreign jurisdiction in relation to similar matters falling within its jurisdiction.

Cayman Islands

Companies Law (2018 Revision)

Like Guernsey, the Cayman Islands are not a signatory to the Model Law and prior to 2009, matters relating
to cross-border insolvencies were not addressed in Cayman Islands legislation. The Companies (Amendment) Law 2007, which was brought into force on 1 March 2009, introduced what is now Part XVII of the Companies Law (2018 Revision) (the ‘Companies Law’) which, supplemented by the Foreign Bankruptcy Proceedings (International Cooperation) Rules 2018, sets out a mechanism by which the Grand Court of the Cayman Islands (the ‘Grand Court’) can provide assistance to the representative of a foreign company which is the subject of bankruptcy or insolvency proceedings in its country of incorporation.

Part XVII of the Companies Law gives the Grand Court a discretionary power to provide assistance for the purposes of:

(a) recognising the right of a foreign representative to act in the Cayman Islands on behalf of or in the name of the foreign company;
(b) enjoining the commencement or staying the continuation of legal proceedings against the foreign company;
(c) staying the enforcement of any judgment against the foreign company;
(d) requiring a person in possession of information relating to the business or affairs of the foreign company to be examined by and produce documents to its foreign representative; and
(e) ordering the turnover to the foreign representative of any property belonging to the foreign company.

In determining whether to provide assistance, the Grand Court is to be guided by ‘matters which will best assure an economic and expeditious administration...’ of the foreign company’s estate, consistent with the following Cayman Islands policy objectives:

(a) the just treatment of all holders of claims or interests in the foreign company’s estate wherever they may be domiciled;
(b) the protection of claim holders in the Cayman Islands against prejudice and inconvenience in the processing of claims in the foreign bankruptcy proceeding;
(c) the prevention of preferential or fraudulent dispositions of property comprised in the foreign company’s estate;
(d) the distribution of the foreign company’s estate amongst creditors substantially in accordance with the order prescribed by Part V of the Companies Law (i.e. the order of distribution applicable to a liquidation commenced in the Cayman Islands);
(e) the recognition and enforcement of security interests created by the foreign company;
(f) the non-enforcement of foreign taxes, fines and penalties; and
(g) comity.

As noted by Justice Jones in *Picard and Bernard L. Madoff Investment Securities LLC (in liquidation) v Primeo Fund (in liquidation)*, even if the foreign proceeding is recognised, the Grand Court may decline to provide assistance if the relief sought by the foreign representative would be likely to produce or contribute to an economic result which is inconsistent with the policy objectives of Cayman Islands corporate insolvency law.

The statutory provision reflects the traditional English common law rule that the court will only recognise the authority of a liquidator or trustee appointed under the law of the country of incorporation. This contrasts with the position under the Model Law which recognises the courts of the country in which an entity has its ‘centre of main interests’ (‘COMI’) (which is not necessarily the country in which the company is incorporated) as being competent to exercise bankruptcy jurisdiction.

For the purposes of Part XVII of the Companies Law, ‘debtor’ is defined as a foreign corporation or other foreign legal entity subject to a foreign bankruptcy proceeding in the country in which it is incorporated or established. It does not include a Cayman Islands company which is the subject of a foreign bankruptcy proceeding and therefore it would not be possible, for example, for a trustee appointed in respect of a Cayman Islands company pursuant to Chapter 11 of the United States Bankruptcy Code to seek recognition and assistance from the Grand Court pursuant to Part XVII of the Companies Law. Assistance may, however, be available as a matter of common law (considered in further detail below).

**Companies Winding Up Rules 2018**

Where a Cayman Islands company in liquidation is also the subject of a concurrent bankruptcy proceeding under the law of a foreign country, or where the assets of a Cayman Islands company in liquidation located in a foreign country are the subject of a bankruptcy proceeding or receivership under the law of that country, the Cayman Islands liquidator has a duty under the Companies Winding Up Rules 2018 to consider whether or not it is appropriate to enter into an international protocol with any foreign officeholder. The purpose of an international protocol is to promote the orderly administration of the estate of a Cayman

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**Notes**

2 Section 242 of the Companies Law.
3 [*2013 (1) CILR 164*]
Islands company in liquidation and avoid duplication of work and conflict between the Cayman Islands liquidator and the foreign officeholder.

In *In the matter of Lancelot Investors Fund Limited,* a Cayman Islands open-ended investment fund with both creditors and an investment manager located in the United States had filed for bankruptcy in the United States and a trustee had been appointed under Chapter 7 of the United States Bankruptcy Code. The Chapter 7 trustee claimed to have exclusive jurisdiction over all of the company’s assets however certain investors considered that the company should be wound up in the Cayman Islands and therefore presented a winding up petition to the Grand Court. The Grand Court recognised the United States as the principal place for the liquidation of the company, but noted that investments into the company were made in the Cayman Islands, the arrangements by which investments were made were governed by the laws of the Cayman Islands and therefore any claims that investors may have had against the company would have to be examined and assessed according to the law of the Cayman Islands. Accordingly, the Grand Court considered it appropriate for the company to also be wound up in the Cayman Islands and for a Cayman Islands liquidator to be appointed. However, the Grand Court stayed the winding up order, in accordance with the principles of judicial comity and universalism in corporate insolvency, to give the Cayman Islands liquidator and the Chapter 7 trustee an opportunity to discuss their respective roles and to agree a co-operation protocol for the efficient liquidation of the company, thus avoiding multiple proceedings and the duplication of costs.

**Common law assistance**

*The development of the principle of modified universalism*

The extent of assistance that can be provided to a foreign officeholder as a matter of common law was considered by Lord Hoffman in *Cambridge Gas.* Lord Hoffman stated that:

‘At common law, their Lordships think it is doubtful whether assistance could take the form of applying provisions of the foreign insolvency law which form no part of the domestic system. But the domestic court must at least be able to provide assistance by doing whatever it could have done in the case of a domestic insolvency. The purpose of recognition is to enable the foreign office holder or the creditors to avoid having to start parallel insolvency proceedings and to give them the remedies to which they would have been entitled if the equivalent proceedings had taken place in the domestic forum.’

In *Cambridge Gas,* the Privy Council was faced with a letter of request sent by the Federal Bankruptcy Court for the Southern District of New York (the ‘New York Bankruptcy Court’) to the High Court of Justice of the Isle of Man. The letter of request sought assistance in giving effect to a plan of reorganisation put forward by the creditors of a business pursuant to Chapter 11 of the United States Bankruptcy Code which had been approved by the New York Bankruptcy Court. The plan of reorganisation had the effect of vesting shares in an Isle of Man company which were held by Cambridge Gas Transport Corporation (‘Cambridge Gas’), a Cayman Islands company, in the creditors of the business. It was accepted by the Privy Council that the New York Bankruptcy Court had no personal jurisdiction over Cambridge Gas; the central issue in dispute was whether the order of the New York Bankruptcy Court approving the plan was a judgment *in rem* or a judgment *in personam,* the answer to which would determine whether the order could be enforced against the shares held by Cambridge Gas in the Isle of Man company. The Privy Council held that the order of the New York Bankruptcy Court was neither a judgment *in rem* nor a judgment *in personam,* on the basis that:

‘Judgments in rem and in personam are judicial determinations of the existence of rights: in the one case, rights over property and in the other, rights against a person. When a judgment in rem or in personam is recognised by a foreign court, it is accepted as establishing the right which it purports to have determined, without further inquiry into the grounds upon which it did so. The judgment itself is treated as the source of the right.

The purpose of bankruptcy proceedings, on the other hand, is not to determine or establish the existence of rights, but to provide a mechanism of collective execution against the property of the debtor by creditors whose rights are admitted or established.’

Jurisdiction to provide assistance in *Cambridge Gas* by recognising and enforcing the order of the New York

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**Notes**

4 The Cayman Islands have also recently implemented a new Practice Direction (Practice Direction No: 1 of 2018) which requires officeholders appointed in the Cayman Islands, companies subject to restructuring proceedings supervised by the Grand Court and other interested parties involved in cross-border insolvency cases to consider whether to incorporate all parts of two sets of guidelines for court-to-court communications (the American Law Institute/International Insolvency Institute Guidelines Applicable to Court-to-Court communications in Cross-Border Cases and The Judicial Insolvency Network Guidelines for Communication and Cooperation between Courts in Cross-Border Insolvency Matters).

5 [2009 CILR 7]
Bankruptcy Court was, according to the Privy Council, conferred upon the Manx court by the principle of universality which underlay the common law principles of judicial assistance in international assistance.

In Rubin v Eurofinance, the Supreme Court held that Cambridge Gas was wrongly decided in so far as it held that special rules apply to orders or judgments made within bankruptcy proceedings, with jurisdiction to provide assistance to a foreign officeholder being conferred upon the Manx court by the principle of universality. As stated by Lord Collins, ‘a change in the settled law of the recognition and enforcement of judgments … has all the hallmarks of legislation, and is a matter for the legislature and not for judicial innovation’.

Further guidance as to the extent of assistance that can be provided to a foreign officeholder as a matter of common law was provided by the Privy Council in Singularis Holdings Limited v PricewaterhouseCoopers. In Singularis, liquidators were appointed in the Cayman Islands to Singularis Holdings Limited (‘Singularis’), a company incorporated in the Cayman Islands. The liquidators obtained recognition of their appointment to Singularis from the Bermudian court and then sought production of internal working papers from Singularis’ auditor in Bermuda, PricewaterhouseCoopers (‘PwC’), pursuant to the common law principle of modified universalism. The court in Bermuda made an order recognising the appointment of the liquidators in Bermuda and exercised what was termed a common law power ‘by analogy with the statutory powers contained in section 195 of the Companies Act’ to order PwC to produce documents which they could have been ordered to produce under section 195 of the Bermuda Companies Act 1981. The order was overturned by the Court of Appeal and subsequently appealed to the Privy Council.

Two issues arose for determination by the Privy Council:

(a) whether the Bermuda court had a common law power to assist a foreign liquidator by ordering the production of information in circumstances where:
   i. the Bermuda court had no power to wind up an overseas company such as Singularis; and
   ii. its statutory power to order the production of information was limited to cases where the company was being wound up in Bermuda; and

(b) whether, if such a power existed, it was exercisable in circumstances where an equivalent order could not have been made by the court in which the foreign liquidation was proceeding.

The Privy Council’s decision was not unanimous and was delivered by the members of the Board in five separate judgments. Whilst the Board agreed that the second issue should be determined in the negative, Lord Mance and Lord Neuberger disagreed as to the extent / existence of a common law power of assistance.

In relation to the first issue, Lord Sumption referred to the decision of the Privy Council in Cambridge Gas and stated that Cambridge Gas, if correct, was authority for three propositions:

(a) the first is the principle of modified universalism, namely that the court has a common law power to assist foreign winding up proceedings so far as it properly can;

(b) the second is that this includes doing whatever it could properly have done in a domestic insolvency, subject to its own law and public policy; and

(c) the third (which is implicit) is that this power is itself the source of its jurisdiction over those affected, and that the absence of jurisdiction in rem or in personam according to ordinary common law principles is irrelevant.

Lord Sumption noted that the first proposition had been subjected to ‘fierce academic criticism’ and held by a majority of the Supreme Court in Rubin to be wrong, and the second proposition was weakened by the absence of any explanation as to where the common law power came from. The Board was therefore of the view that the second and third propositions for which Cambridge Gas was authority could not be supported. However, the majority of the Board confirmed that the first proposition, the principle of modified universalism itself, had not been discredited. On the contrary, Lord Sumption noted that the first proposition in Cambridge Gas had been accepted in principle in both HIH Casualty and General Insurance Ltd and in Rubin.

The majority of the Board therefore accepted that the principle of modified universalism is part of the common law. However, it was held that the principle is much more limited in scope than articulated in Cambridge Gas – as stated by Lord Sumption, it is ‘necessary to bear in mind, first, that it is subject to local law and local public policy and, secondly, that the court can only ever act within the limits of its own statutory and common law powers’.

In the absence of a relevant statutory power available to a foreign officeholder, the question becomes how far it is appropriate to develop the common law
to make the power sought by the foreign officeholder available. The majority of the Board was of the view that there is no single universal answer to this question—it very much depends on the nature of the power that the court is being asked to exercise. The fact that a statutory power exists to make a particular order in a domestic insolvency does not mean that a similar power automatically exists at common law. However, the existence of a statutory power does not exclude the possibility of an equivalent power at common law—the majority of the Board held that an implied exclusion of non-statutory remedies arises only where the statutory scheme can be said to occupy the field, which will normally be the case if the subsistence of the common law power would undermine the operation of the statutory one, usually by circumventing limitations or exceptions to the statutory power which are an integral part of the underlying legislative policy.

Lord Sumption stated that the common law power is subject to the following limitations:

(a) it is available only to assist the officers of a foreign court of insolvency jurisdiction or equivalent public officers. It is not, for example, available to assist a voluntary winding up, which is essentially a private arrangement and not conducted by or on behalf of an officer of the court;

(b) it is a power of assistance which exists for the purpose of enabling foreign courts to surmount the problems posed for a world-wide winding up of a company’s affairs by the territorial limits of each court’s powers. It is not, therefore, available to enable a foreign officeholder to do something which they could not do under the law by which they were appointed;

(c) it is available only when it is necessary for the performance of the officeholder’s functions; and

(d) the order sought must be consistent with the substantive law and policy of the assisting court.

The majority of the Board ultimately refused to make the order requested by the liquidators on the basis that the liquidators could not have obtained similar relief in their home jurisdiction and it is ‘not a proper use of the power of assistance to make good a limitation on the powers of the foreign court of insolvency jurisdiction under its own law’.

**How has Singularis been applied in Guernsey?**

In *Brittain v JTC (Guernsey) Limited,* an English trustee in bankruptcy sought an order from the Royal Court recognising her right to examine persons involved in or connected with the bankrupt’s affairs, including persons involved in the management of two Guernsey companies said to be connected to the bankrupt. There was power to seek such an order under section 426 of the Insolvency Act, however such power was not invoked due to concerns regarding delay and risk of tipping off the bankrupt. The Royal Court was therefore required to determine whether it has jurisdiction at common law to order a third party, resident within the jurisdiction of the Royal Court, to provide documents and information to an English trustee in bankruptcy. The trustee believed that the third party in question held information that might assist in the performance of her functions, including tracing assets of the bankrupt and allowing the trustee to understand the relevant affairs of the English bankrupt generally.

The trustee argued that, following the decision in *Singularis,* the issues for the Royal Court to consider were (i) whether or not any local laws would prevent the granting of the assistance sought, and (ii) whether there were any relevant considerations which meant that the granting of the order sought would be contrary to Guernsey public policy. The trustee argued that as there was no local law that prevented the granting of the order, and no relevant public policy considerations, assistance should be provided.

Lieutenant-Bailiff Hazel Marshall (‘LB Marshall’) did not accept this argument. In her view, the starting point was first to determine whether or not there was a power to make the order sought at all. She held that, when considering whether a particular power was common to both jurisdictions, this assessment was more of a procedural question to be addressed and not a part of the test for determining whether that power existed in the first place.

LB Marshall commented that the judicial division among the members of the Board in *Singularis* was on this very point—which or not the common law power existed at all, or if there was in any event an inherent jurisdiction to make the orders sought. She noted that ‘[i]t is very unusual to have a dissenting judgment in the Privy Council, because it is general convention that the Privy Council gives unanimous advice to Her Majesty, and it is therefore to be inferred that this is a difficult legal point.’

LB Marshall went on to note that she preferred the minority view of the Privy Council in *Singularis* to the majority, and was inclined against the existence of a common law power:

‘I would say that, untrammeled by any constraints of binding authority, my judgment would strongly side with the minority judgment in the Privy Council. I would find against the existence of any common law power in this context, i.e. an inherent jurisdiction

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**Notes**

| 9 | [2015]GLR 248 |
to treat a power conferred only by statute as being available in a case which is not within the statute, relying on some combination of usefulness, a generous assessment of analogy, and resort to a supposed beneficial principle of “modified universalism” of insolvency law of indefinite and necessarily presupposed extent.’

She was also concerned that a finding that would oblige third parties, possibly under threat of contempt of court, to provide information in respect of the affairs of a third party was ‘draconian’, which one generally saw conferred by way of statute. In any event, LB Marshall noted that the absence of the power to compel third parties in Guernsey as sought by the trustee has actually been dealt with in earlier Guernsey cases, and she did not consider Singularis to overrule the local case law.

LB Marshall also viewed as persuasive the fact that the alternative statutory route was available to the trustee, but that this process had not been pursued when it would have been proper to do so. Accordingly, the Royal Court declined to make the order sought.

In In the Matter of Lee Douglass (In Bankruptcy),\(^\text{10}\) the application of Singularis was further considered from a Guernsey perspective in the context of the interface between foreign insolvency proceedings and the Guernsey customary laws of désastre.

The Norman customary law foundation to the common law in the Bailiwick means that a Guernsey insolvency can look quite different to bankruptcy in other jurisdictions. When a Guernsey person (including a corporate personality) is unable to pay its debts, they are said to be ‘en état de désastre’ – quite literally in a ‘state of disaster’. Historically, désastre had very few rules governing its procedure, but the purpose was to permit creditors to share in proceeds from the sale of a debtor’s personal effects, those assets having been seized by Her Majesty’s Sheriff (as distinct from any real estate, which is dealt with separately). As a matter of law, the declaration that a person is en désastre has no bearing on the future activities of the debtor, but it also does not operate as any sort of discharge from the debtors’ liabilities in the way that a declaration of bankruptcy might.

In Douglass, English trustees in bankruptcy sought, inter alia, an order that would allow them to collect Guernsey funds and assets as part of the English bankruptcy proceedings. Although insolvency proceedings against Mr Douglass were progressing in the English courts, Mr Douglass was also a judgment debtor in Guernsey, being the subject of both saisie (the process by which a creditor pursues the real estate of a debtor) and désastre processes.

Mr Douglass’ creditors in Guernsey (Confiance Ltd) were engaging with both the English bankruptcy proceedings and the Guernsey désastre proceedings. Confiance Ltd opposed the trustees’ application for all Guernsey assets to be turned over to the trustees, insofar as it could apply to funds now held by the Sheriff seized by way of désastre processes. In response, the trustees argued that in seeking to participate in the English bankruptcy proceedings, Confiance Ltd had ‘[overridden] its ongoing use of the désastre process in Guernsey’.

Deputy-Bailiff McMahon did not accept this argument, noting that the désastre process in Guernsey would not necessarily produce the same result as an English bankruptcy and therefore participation in the parallel proceedings was not inconsistent. Further, and importantly from a practical perspective, the assets held by the Sheriff did not form part of the estate of Mr Douglass as a matter of customary law, and therefore could not be affected by any order made for the benefit of the trustees.

Deputy-Bailiff McMahon also noted with apparent approval the views expressed by LB Marshall in Brittain in finding that Guernsey will prefer the minority judgment in Singularis:

‘It is apparent that the courts in a number of jurisdictions have had to grapple with the means by which to provide assistance in cross-border insolvencies and the limitations that may be imposed on the extent of any such assistance. In Guernsey, this was the issue in the Brittain case (supra), in which the Lieutenant-Bailiff, not being bound by the majority decision in the Singularis case, preferred the reasoning of the minority (Lords Neuberger and Mance), rejecting the existence of any inherent jurisdiction to treat a power conferred only by statute as being available in a case which is not within the statute.’

Notwithstanding the view of LB Marshall, Deputy-Bailiff McMahon ultimately found that, at least concerning the recognition of an officeholder and the necessary ancillary powers (as opposed to what Deputy-Bailiff McMahon termed ‘more far-reaching power that has no identifiable equivalent outside a statutory framework’), this recognition could be obtained by way of letter of request under section 426 of the Insolvency Act, or under the customary law. Deputy-Bailiff McMahon went on to draw a further distinction between an application under section 426 of the Insolvency Act where no local processes had been commenced, and circumstances where désastre or other customary law avenues were being pursued, which threw up additional issues concerning the effectiveness of modified universalism.

\(^{10}\) Lee Douglass (in Bankruptcy) v Krasner & Wright (2017) (Unreported, Royal Court, 10th July) (Guernsey Judgment No. 32/2017)
What does this mean for foreign officeholders seeking assistance in Guernsey?

In the light of the decisions in Brittain and Douglass, foreign officeholders may, in certain circumstances, be able to obtain certain orders in the pursuance of foreign insolvency proceedings in reliance on the common law, but this is by no means a carte blanche. In particular, foreign officeholders will need to pay particular attention to any local customary law proceedings on foot and may have difficulty obtaining orders that could be considered beyond the ordinary course.

From the point of view of both foreign creditors and foreign officeholders, such uncertainty is unsatisfactory. However, statutory reform of the Guernsey insolvency regime has been proposed which, if implemented, would provide a statutory basis for foreign officeholders to seek information from third parties in a way not currently allowed, and would provide a significant measure of clarity to the insolvency regime overall.

How has Singularis been applied in the Cayman Islands?

Comparatively, the principle of modified universalism has been expressly affirmed in the Cayman Islands (subject to the limitations on the common law power of assistance identified by Lord Sumption in Singularis).

In Picard and Bernard L. Madoff Investment Securities LLC (in liquidation) v Primeo Fund (in liquidation),11 which was decided after Rubin but before Singularis, the Grand Court held that the Supreme Court in Rubin did not reject the underlying proposition that recognition at common law ‘carries with it the active assistance of the court’. As noted by Justice Jones, the Supreme Court in Rubin confirmed the common law power to recognise and grant assistance to foreign proceedings, and only rejected the proposition that ‘active assistance’ extended to the enforcement of in personam judgments made in bankruptcy proceedings which would not otherwise be enforceable in accordance with established conflict of law rules. Justice Jones considered that the Supreme Court in Rubin did not express a view on the question which he had to decide, which was whether the assistance available to a foreign officeholder at common law extends to providing the foreign officeholder with a ‘direct remedy’, meaning an original cause of action which could be pursued against a person in the Cayman Islands, and that it remained open to him to accept Lord Hoffman’s answer to that question (based on Cambridge Gas). It was held that the scope of assistance available at common law did in fact include the power to apply Cayman Islands statutory provisions (in this instance, avoidance provisions of Cayman Islands insolvency law). However, the Grand Court did not have the ability to apply foreign law statutory provisions in the Cayman Islands.12

More recently, the Grand Court relied upon the decision of the Privy Council in Singularis in finding that assistance could be provided to a foreign officeholder appointed in respect of a Cayman Islands entity as a matter of common law (whilst the Grand Court has a statutory power to provide assistance to a foreign officeholder, such power can only be exercised where a foreign entity is subject to a foreign bankruptcy proceeding in the country in which it is incorporated and therefore the statutory power is of no assistance to a foreign officeholder appointed in respect of a Cayman Islands company).

In In the matter of China Agrotech Ltd.,13 the Hong Kong liquidators of China Agrotech Holdings Limited (‘China Agrotech’), a Cayman Islands company, sought permission from the Grand Court to promote a scheme of arrangement in the Cayman Islands between China Agrotech and its creditors in the Cayman Islands. The scheme of arrangement was part of a corporate rescue of China Agrotech involving a parallel scheme of arrangement in Hong Kong and a restructuring of China Agrotech’s capital. There were no parallel insolvency proceedings in respect of China Agrotech in the Cayman Islands.

The Grand Court’s starting point for the consideration of the nature and scope of its non-statutory jurisdiction to recognise and assist foreign officeholders was the decision of the majority of the Board in Singularis (in particular, the judgment of Lord Sumption). Based on Singularis, Justice Segal made the following points:

(a) the Grand Court is to be treated as having a power to recognise and grant assistance to foreign proceedings and liquidators (at least where those proceedings are commenced in and the liquidators are appointed by the court). If the circumstances justify its use, and subject to the limitations on its use, the power can be exercised by making suitable orders for the purpose of enabling the foreign court and its officeholders to surmount the problems posed for a worldwide winding up of the company’s affairs by the territorial limits of its powers. This is the purpose for which the power can be exercised;

(b) the court’s power is a non-statutory jurisdiction which is based on and justified by the public interests as identified by Lord Sumption in Singularis.

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11 [2013 (1) CILR 164]
12 This decision was appealed to the Cayman Islands Court of Appeal but was not overturned on this point.
13 Unreported, 19 September 2017, Segal J
deciding whether and how to exercise the power, the court has regard to and applies the approach which has been labelled ‘modified universalism’;

(c) suitable orders include any order which the court can make in the circumstances based on and by applying the applicable domestic substantive or procedural law, provided that such law is applicable to the particular case before the court;

(d) the court cannot grant relief by making an order which can only be made in reliance on a domestic statutory provision which, by its terms, does not apply in the circumstances. Nor can the court make an order that grants relief to a foreign liquidator which depends on there being a domestic law right which does not in the circumstances exist;

(e) where the foreign liquidator is appointed in the country of incorporation of the company concerned, the domestic private international law of the requested court will apply so that the liquidator is treated as being entitled to act for and on behalf of the company;

(f) when the foreign liquidator is not appointed in the country of incorporation, he cannot rely on this rule of private international law and instead must invoke the common law power in order to be permitted to act on behalf of the company; and

(g) the limitations on the common law power (both as to its scope and the circumstances in which it will be exercised) are those described by Lord Sumption in Singularis.

The Grand Court held that the common law power could be exercised to provide assistance to the Hong Kong liquidators for a number of reasons:

(a) the issue was who should be entitled to act and bring proceedings for a scheme of arrangement on behalf of China Agrotech. There were no competing claims by creditors which would result in different levels of recovery or returns depending on whether the liquidators were granted the relief they were seeking;

(b) the liquidators simply wished to be able to promote a parallel scheme of arrangement in the Cayman Islands and to prevent any proceedings in the Cayman Islands being litigated in a manner that would disrupt or interfere with the scheme process;

(c) there was no likelihood of an application being made for a winding up order in the Cayman Islands;

(d) China Agrotech had substantial contacts with Hong Kong – its shares were listed in Hong Kong, its business was administered from Hong Kong, it was registered in Hong Kong and the majority of shareholders had addresses in Hong Kong; and

(e) there was no need for or reason why creditors or members would benefit from a Cayman Islands winding up and there were no local reputational, regulatory or policy reasons requiring a Cayman Islands winding up.

Justice Segal noted that China Agrotech’s COMI, as that term is used in the Model Law, was probably in Hong Kong and although that was not determinative (given that the Cayman Islands is not a signatory to the Model Law and there is no concept of COMI in Cayman Islands law), it was a consideration of considerable weight to be taken into account when deciding whether the ‘foreign, non-place of incorporation, liquidation’ should be treated as competent and justifying assistance.

What does this mean for foreign officeholders seeking assistance in the Cayman Islands?

Whilst the assistance that can be provided to a foreign officeholder will depend on the circumstances of each case, the authorities demonstrate that the Cayman Islands courts will adopt a pragmatic approach to a request by a foreign officeholder or foreign court for assistance and endeavour to facilitate the efficient and expeditious liquidation of companies wherever possible.
Recent Irish Supreme Court Decision on Assignment Of Claims, Third Party Litigation Funding and Champerty: A Prelude to Real Progress

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Synopsis

On 31 July 2018, Ireland’s highest court, the Supreme Court, delivered a 5-judge unanimous ruling in SPV Osus Limited v HSBC Institutional Trust Services (Ireland) Limited and Others¹ in a case that examined the assignability of a cause of action under Irish law.

Background

The background to the proceedings has its origins in the Bernard L Madoff Investments LLC (‘Madoff’) Ponzi scheme fraud and the entitlement to make claims in the Madoff bankruptcy. As part of the Madoff bankruptcy, a company known as Optimal Strategic US Equity Limited (‘Optimal’) had a claim in the amount of US$1.5bn which carried with it an entitlement to be paid in priority to the liquidation, as well as an unsecured, non-priority claim in the amount of c. US$1.3bn.

Optimal represented the interests of a group of investors who had invested indirectly in Madoff. Subsequent to the discovery of the Ponzi scheme, a secondary market developed for claims in the Madoff bankruptcy. A procedure for assignment of claims in the Madoff bankruptcy was recognised by the Trustee in Bankruptcy and permitted by the court supervising the bankruptcy. The approved scheme required the assignment of not only the preferential claim in the Madoff bankruptcy but of all related claims by the assignor to the assignee.

Due to the manner in which the Optimal investors held their investments, they could not assign their claims so long as the cause of action remained vested in Optimal. In order to enable the Optimal investors to assign their claims in the Madoff bankruptcy (and all other related claims), Optimal assigned its claims against Madoff to SPV Osus Limited (‘OSUS’), a special purpose vehicle set up specifically for this purpose.

The investors in Optimal were given the opportunity to take up shareholdings in OSUS commensurate with their interests in Madoff held through Optimal. Most of the investors subsequently assigned their claims in the bankruptcy and all related claims to distressed debt investors such that the distressed debt investors ultimately held 93% of the shares in OSUS. Having gained control of the board of OSUS, the distressed debt investors then set about issuing proceedings against inter alia the custodian and administrator appointed by Optimal. As both the custodian and administrator were Irish companies, the proceedings issued in Ireland.

High Court and Court of Appeal

After OSUS issued the proceedings, the custodian and the administrator sought to have the proceedings dismissed on the basis that the assignment of the claims by Optimal to OSUS was ‘contrary to public policy, void and unenforceable as a matter of Irish law’. The Irish High Court held that the assignment was void as comprising inter alia an assignment of a bare right to litigate and the Court of Appeal upheld this decision.

OSUS was granted leave to appeal to the Supreme Court to pursue the following issues:

(a) The circumstances in which, as a matter of Irish law, an assignment of a cause of action will be recognised as valid (insofar as potentially relevant to the circumstances of this case); and

(b) The application of the principles identified in the answer to (a) to the facts of this case for the purposes of determining whether the Court of Appeal was correct to determine that the assignment on which OSUS relies should not be recognised as a matter of Irish law.

Maintenance and champerty

Intertwined with the question as to whether or not there exists a right to assign a bare right to litigate under Irish law are the antiquated doctrines of maintenance

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1  [2018] IESC 44.
and champerty. Unlike in England, where the torts were abolished more than 50 years ago, maintenance and champerty remain torts (and crimes) in Ireland and public policy dictates that effect should not be given to a transaction which constitutes either tort.

Maintenance is the unjustifiable provision of financial support for litigation in which the maintainer has no legitimate interests. Champerty is a particular form of maintenance which involves a person providing financial support for the action in return for a share of the proceeds. Maintenance, champerty and the assignment of a bare right to litigate are closely aligned and have similar public policy considerations underpinning their standing in Irish law.

The case made by the custodian and the administrator (and accepted by the High Court at first instance and the Court of Appeal) was not that OSUS was guilty of the tort of maintenance or champerty but that the assignment by Optimal to OSUS of its claim in the Madoff bankruptcy and all of its related claims, including the right to bring a claim against the custodian and administrator, should be void because it ‘savour of champerty’.

This is the second decision of the Irish Supreme Court within 15 months to examine the impact of the anachronistic torts of maintenance and champerty on modern day litigation. In Persona Digital Telephony Ltd & Anor v The Minister for Public Enterprise & Ors, the Supreme Court, by a majority of 4 to 1, held that a third party professional funding agreement to support a party in legal proceedings amounts to champerty and is prohibited under Irish law. However, in so holding, there were a number of very strong judicial comments to the effect that the legislature and / or the Executive should ensure that these torts did not lead to an impermissible restriction on the constitutionally protected right of access to justice, which right might be said to be restricted if access to the judicial system was effectively denied because of the complexities and expenses involved with modern day litigation. As will be discussed further below, the Chief Justice in SPV Osus took the opportunity to forcefully reiterate some of the comments that he made in Persona.

Decision of the Supreme Court

In deciding whether the assignment of the cause of action from Optimal to OSUS was permissible under Irish law, the Supreme Court undertook a detailed analysis of the case law of England and Wales on the issue, in circumstances where the Irish authorities that were considered by the Court did not deal with the specific issue. Having carried out its analysis, the Supreme Court ultimately endorsed the decision of the English House of Lords in Trendtex Trading Corporation v Credit Suisse. In summary terms, this decision said that an assignment of a right to litigate is unenforceable unless the assignee has a genuine commercial interest in the assignment.

In applying the test set down by the House of Lords in Trendtex and finding that the assignment of the claims from Optimal to OSUS was impermissible under Irish law, the Supreme Court rejected the argument put forward by OSUS that it had a commercial interest in the assignment of the right to litigate these proceedings as a consequence of the assignment of bankruptcy claim (which had been permitted in the US). The decision of the Supreme Court confirms that the assignment of a claim to a party without a legitimate interest in the assigned dispute is unenforceable in Ireland. Notwithstanding the foregoing, the obiter comments of Chief Justice Clarke (discussed below) suggest that change could soon be on the horizon as regards the manner in which litigation in Ireland can be funded.

Political pressure on legislature

While the decision of the Supreme Court was delivered by Mr Justice O’Donnell, the consenting judgment of Chief Justice Clarke is arguably the more noteworthy. Just two pages long, Chief Justice Clarke stated that he agreed fully with the legal analysis of Mr Justice O’Donnell and that the purpose of his judgment was to reiterate comments that he had made in Persona.

In Persona Mr Justice Clarke (as then he was) noted that there was an increasing problem with access to justice as a result of inter alia the increasing complexity and cost of conducting litigation but that the choice of policy solution to this problem was very much a matter for the legislature or the Executive to address and not for the Courts to address by way of case law. Mr Justice Clarke did caveat this by saying that if it transpired that the constitutional right of access to justice was being denied and the legislature and the Executive were failing to act, that the Courts, as guardians of the constitution, might have no option but to ‘take measures which would not otherwise be justified’.

In his concurring judgment in SPV Osus, Chief Justice Clarke stated that he was ‘strongly of the view that it is necessary that some measures be taken to address (the problem with access to justice)’. Chief Justice Clarke stated that he ‘remain(s) very concerned that there are cases where persons or entities have suffered
from wrongdoing but where those persons or entities are unable effectively to vindicate their rights because of the cost of going to court’. The Chief Justice went on to say that ensuring adequate access to justice was an issue to which the ‘legislature should give urgent consideration’.

The Chief Justice was careful not to prescribe the solutions to the problem with access to justice and acknowledged that there may be solutions outside of the liberalisation of the laws relating to maintenance and champerty. The Chief Justice expressed the view that ‘by far the best way of attempting to provide solutions is by means of legislation’ to establish a properly regulated scheme or structure which would ensure that the potential benefits of liberalisation are not outweighed by any disadvantages which might flow from an entirely unregulated commoditisation of litigation. However, he warned that a ‘point might be reached where the courts had no option but to go down (the route of effecting change) if it became clear that no real effort was being made on the part of the legislature to address issues such as those that came into focus on this appeal’.

**Comment**

The Chief Justice’s judgment is unusual in so far as its sole purpose is to reiterate comments made more than a year previously about the perceived issues with access to the Irish legal system which the legislature has failed to address.

While it is evident from the Chief Justice’s judgments in *Persona* (before he was Chief Justice) and in this case that he is conscious of the separation of powers under the Irish constitution, he has stated in unequivocal terms that the Courts will act if the legislature fails to ensure that one’s constitutional right to access to justice is protected. One would hope and assume that the Irish legislature will turn its attention to this issue in the near future in light of the Court’s concerns.

While one can only speculate as to how the legislature will chose to ensure access to justice in a meaningful way, there must be a very real possibility that a decision could be made to reform the existing Irish position on maintenance and champerty, and introduce a statutory code that would permit (within certain parameters) professional third party funding being available in Ireland.
The Cayman Restructuring Toolkit: Exploring the Flexible Restructuring Options on Offer in the Cayman Islands

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Synopsis

The Cayman Islands provisional liquidation regime has proven to be an extremely useful and flexible tool to assist with complex financial restructurings. In circumstances where a Cayman Islands company is insolvent or potentially insolvent, its board of directors must have regard to creditors’ interests as a whole when discharging their fiduciary duties and ideally be engaging with the company’s creditors in order to try and agree upon a consensual restructuring solution. However, such a consensual out-of-court process would typically require unanimous support (or acquiescence) from all of the company’s creditors and therefore the company’s board of directors may wish to consider alternative options to mitigate the risk that a disgruntled creditor may seek to disrupt any restructuring process by commencing proceedings against the company. This article focuses on the provisional liquidation regime in the Cayman Islands and how it can be a useful tool for companies who are facing an imminent debt crisis.

Provisional liquidation in the Cayman Islands – traditional v ‘soft touch’

The traditional purpose of the appointment of provisional liquidators is to preserve and protect a company’s assets pending the hearing of a winding up petition in respect of the company where there is evidence of potential dissipation or misuse of assets. In such circumstances, a creditor can make an application to the Grand Court of the Cayman Islands (the ‘Grand Court’) seeking the appointment of provisional liquidators to a company pursuant to section 104(2) of the Companies Law (2018 Revision) (the ‘Companies Law’).

However, the Cayman Islands provisional liquidation regime offers an alternative route to appointing provisional liquidators in circumstances where a Cayman Islands company intends to implement a financial restructuring. Pursuant to section 104(3) of the Companies Law, provisional liquidators can be appointed on a ‘soft-touch’ basis in order to protect the company from creditor enforcement action or proceedings being commenced or continued without the leave of the Court. The moratorium that is triggered on the appointment of provisional liquidators provides breathing space for a company to negotiate with its stakeholders and propose and implement a restructuring without the risk of the process being derailed by the actions of one or more dissenting creditors. Notably, however, such moratorium does not extend to restrict the rights of secured creditors who may enforce their security notwithstanding the appointment of provisional liquidators. Accordingly, standstill agreements with secured creditors or seeking supporting relief in other relevant jurisdictions (such as Chapter 15 in the United States) may still be necessary.

Pursuant to section 104(3) of the Companies Law, following the presentation of a winding up petition, a company may at the same time make an application seeking the appointment of provisional liquidators where (a) the company is or is likely to become unable to pay its debts; and (b) the company intends to present a compromise or arrangement to its creditors. There is no statutory definition of the terms ‘compromise’ or ‘arrangement’ in the Companies Law. The Grand Court typically construes these terms broadly but they must involve some element of ‘give and take’ on both sides. In practice, this can include a Cayman Islands scheme of arrangement, a Chapter 11 plan or restructuring, or a foreign scheme of arrangement.

Provisional liquidation is available to any company liable to be wound up under the Companies Law following the presentation of a winding up petition against the company. Any creditor, shareholder, the company itself or (in respect of regulated businesses) the Cayman Islands Monetary Authority can apply for the appointment of provisional liquidators between the presentation and the hearing of the winding up petition. However, an application seeking the appointment of ‘soft touch’ provisional liquidators on restructuring grounds pursuant to section 104(3) of the Companies Law (that is, where a company is or is likely to become insolvent or potentially insolvent) must be made prior to the hearing of the winding up petition.

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1 Re XL Capital Ltd (unreported, Smellie CJ, Cause No. FSD 66 of 2010) (5 March 2010).
unable to pay its debts and the company intends to present a compromise or arrangement to its creditors) may only be made by the company itself (if properly authorised). Accordingly, as it stands a creditor can only make an application seeking the appointment of provisional liquidators where there is a genuine need to safeguard the assets of the company pending the hearing of a winding up petition and there are no provisions in the Companies Law which allow creditors to apply for the appointment of ‘soft touch’ provisional liquidators.

Whilst the presentation of a winding up petition is a necessary prerequisite to access the Cayman Islands provisional liquidation regime, ‘soft touch’ provisional liquidation does not necessarily result in the formal winding up of the debtor company. Rather, where a ‘soft touch’ provisional liquidation is used to support a successful financial restructuring where the debtor company survives, the end result is usually that the winding up petition is dismissed and the newly restructured company continues as a going concern. Provisional liquidation when used in a restructuring context in the Cayman Islands is therefore somewhat of a misnomer since the object of the proceedings is to typically rescue the company as a going concern rather than to liquidate and dissolve the company.

Provisional liquidators are officers of the Grand Court and agents of the company to which they owe fiduciary duties to act in good faith and in the interests of the company as a whole. However, the powers of the provisional liquidators are not circumscribed by statute and instead are expressly set out in the court order appointing them. Accordingly, there is scope for the provisional liquidation regime to be used with real flexibility in the context of a restructuring depending upon how much control over the process the provisional liquidators are intended to have.

In a ‘soft touch’ provisional liquidation, the provisional liquidators would typically work alongside the existing directors to develop and propose a restructuring without completely displacing the directors’ powers. Ultimately, the order appointing the provisional liquidators will clearly set out which powers the provisional liquidators are able to exercise (often limited to oversight of the progress of the restructuring and reporting to the Grand Court and the company’s creditors) and which powers will be retained by the directors.

Typically the Grand Court has been flexible in allowing sufficient time for the provisional liquidators to consider whether a restructuring is capable of being agreed and implemented in the circumstances. However, if it is evident to the Grand Court that there is no realistic prospect for a successful restructuring to be implemented and for the company to continue as a going concern, it is likely that the winding up petition will be listed and an order made for the appointment of official liquidators to the company.

Recent restructurings in the Cayman Islands

The Cayman Islands has recently seen a number of large cross-border restructurings in the Grand Court where companies have benefited from the flexibility of the ‘soft touch’ provisional liquidation regime. In June 2018, the Grand Court appointed ‘soft touch’ provisional liquidators to Abraaj Holding (‘Abraaj’), the largest private equity fund in the Middle East, and its wholly owned subsidiary, Abraaj Investment Management Limited (‘AIML’), both of which are Cayman Islands companies.2

One of Abraaj’s creditors, The Public Institution for Social Security in Kuwait (‘PIFSS’), presented a winding up petition in the Grand Court on 25 May 2018 on the grounds that Abraaj had failed to pay an undisputed debt and was therefore unable to pay its debts as they fell due. A week later, another creditor of Abraaj, Auctus Fund Ltd (‘Auctus’), filed an application pursuant to section 104(2) of the Companies Law for the appointment of provisional liquidators to Abraaj and AIML on the grounds that the companies were being mismanaged by the incumbent management team and the appointment of provisional liquidators was necessary to avoid further mismanagement and the potential dissipation of assets. Auctus also presented a winding up petition in relation to AIML. In response to the applications filed by PIFSS and Auctus, Abraaj and AIML respectively filed applications with the Grand Court for the appointment of ‘soft touch’ provisional liquidators which were supported by a number of Abraaj and AIML’s secured creditors.

In reaching its decision to appoint ‘soft touch’ provisional liquidators to Abraaj and AIML, the Grand Court noted that an application for the appointment of ‘soft touch’ provisional liquidators is only available to the company and cannot be made by a creditor under Cayman Islands law. In the circumstances, the Grand Court noted that Auctus’ applications for the appointment of provisional liquidators to Abraaj and AIML, although alleging mismanagement of both companies, had accepted that provisional liquidators needed to be appointed with a mandate to promote a restructuring of Abraaj and AIML.

Whilst the Companies Law is clear on who may present a winding up petition and/or make an application for provisional liquidators to be appointed, the Grand Court has grappled on numerous occasions with the issue of whether or not the directors of a company are authorised to present a winding up petition in circumstances where they are not duly authorised by the

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company’s shareholders. Such issue stems from what is known as the Emmadart principle, which originates from the English case of Re Emmadart Ltd. The effect of Emmadart was that the directors may only present a winding up petition in the name of the company if such action is authorised or ratified by the company’s shareholders at a general meeting. The Emmadart principle has been upheld as applicable in the Cayman Islands, most recently in Re China Shanshui Cement Group Limited where Mangatal J held that a winding up petition presented by the company’s directors was not valid on account of the directors not having been authorised by the shareholders to present the winding up petition. Accordingly, the Grand Court was bound to conclude that the directors’ application to also appoint provisional liquidators must also fail given that the prerequisite winding up petition had not been validly presented.

That requirement for shareholder authorisation is also reflected in the Companies Law which provides that where the company’s articles of association (if the company was incorporated post 1 March 2009) authorise the directors to do so, the directors may present a winding up petition without the sanction of a resolution of the shareholders passed at a general meeting. However, an issue arises in circumstances where the company was either incorporated prior to 1 March 2009 or the articles of association do not, in any event, authorise the directors to present a petition without shareholder authorisation. In a restructuring context, this could be fatal since extracting the necessary authorisation from shareholders who are economically disenfranchised may not be possible. Additionally, where the debtor is listed, extracting the necessary consent from a dispersed group of shareholders may be practically impossible or at least logistically challenging. As such, concern existed that if a company’s directors were unable to present the necessary winding up petition in the name of the company due to a lack of shareholder authorisation, the company could not seek the appointment of ‘soft touch’ provisional liquidators in order to implement a restructuring. That concern has however been abated following the successful Cayman Islands restructuring of CHC Group Ltd (‘CHC’), the world’s largest commercial helicopter services provider, where the Grand Court determined that in certain circumstances, directors of a company can make an application for the appointment of ‘soft touch’ provisional liquidators without the need for a shareholders’ resolution or authorisation in the company’s articles of association.

The CHC restructuring was primarily achieved by way of a Chapter 11 proceeding in the United States Bankruptcy Court for the Northern District of Texas filed by CHC and certain of its subsidiaries.

The CHC restructuring however envisaged a transfer of CHC’s assets to a new Cayman Islands limited liability company which would become the parent company of the restructured group. The method of implementing that transfer involved an asset sale to be completed within the framework of a Cayman Islands provisional liquidation proceeding which required validation by the Grand Court. However, CHC’s articles of association did not authorise the directors of CHC to present a winding up petition without shareholder authorisation.

The solution was for an intra-group creditor to petition for the winding up of CHC, thereby opening the gateway for the company itself to apply for the appointment of ‘soft touch’ provisional liquidators. This caused the Grand Court to consider whether an application to appoint provisional liquidators required shareholder authorisation. The Grand Court found that shareholder authorisation was not required and that the decision in China Shanshui had ‘…no bearing on the situation where there is a separate creditor winding up petition in existence and where in those limited circumstances there [is] an application by the company, through its directors, for the appointment of [joint provisional liquidators]’. The CHC decision is the first time that the Grand Court has provided a judgment confirming the validity of this work around.

Cayman Islands schemes of arrangement

There have been a number of recent high-profile cross-border restructurings in the Cayman Islands, such as Ocean Rig UDW Inc. and Mongolian Mining Corporation where the scheme of arrangement process and ‘soft touch’ provisional liquidation regime were successfully used together to implement their respective debt restructurings. The sophisticated restructuring toolkit on offer has ensured that the Cayman Islands remains at the forefront as one of the premier jurisdictions of choice to implement complex cross-border restructurings.

A Cayman Islands scheme of arrangement is a court approved compromise or arrangement between a company and its creditors or shareholders. A scheme of arrangement is frequently used to implement a restructuring of a company’s financial liabilities by varying or

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3 Re Emmadart Ltd [1979] Ch 540.
6 Ocean Rig UDW Inc., (in provisional liquidation) and others (unreported, Parker J, Cause Nos. FSD 100, 101, 102 and 103 of 2017) (18 September 2017).
cramming in the rights of the relevant creditors and/or shareholders of a company but may also be used to complete corporate transactions such as a group restructuring or reorganisation, acquisitions, mergers and take-private transactions. Accordingly, a scheme is not a formal insolvency process as such and the directors would remain in control of the company whilst formulating the terms of and promoting a scheme outside of a liquidation. It is however usual for a restructuring that is implemented by way of a Cayman Islands scheme of arrangement to be conducted within the framework of a ‘soft touch’ provisional liquidation so as to take advantage of the automatic stay on creditors’ claims whilst the restructuring is ongoing.

A scheme requires the approval of each class of affected stakeholder that is, at least a majority in number representing 75 per cent in value of those actually voting need to vote in favour of the terms of the proposed scheme at the court convened scheme meeting(s). Once the proposed scheme of arrangement has been approved by the relevant stakeholders and sanctioned by the Grand Court, all affected stakeholders will be bound by the terms of the scheme (including any dissenting stakeholders and/or any stakeholders that have not voted).

Proposed reform

It is proposed that a new court supervised restructuring moratorium regime will be in force in the Cayman Islands in the near future. The process would allow a company to petition for the appointment of restructuring officers to obtain a stand-alone restructuring moratorium (separate from the winding up regime) thereby offering companies with more avenues by which to benefit from an automatic stay on claims. In the meantime, ‘soft touch’ provisional liquidation is an extremely helpful tool for any Cayman Islands company that is considering its options in the face of a possible default, and provides a formal Court led process, and statutory protection, in order to effectively restructure its debt and continue as a going concern.
Secured Rights and Receiverships: Windfalls and Pitfalls

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Introduction

Despite the advantages of having security over a company’s assets, there are issues which a secured creditor should take note of, from the point of negotiating the terms of the security instrument through to the point of enforcement. Receiverships are a key method of enforcement and enable secured creditors to realise the secured property and recover the secured debt. This article provides a practical consideration of those matters from an enforcement perspective and discusses the points that a secured lender should be aware of in order to maximise its chances of recovering its debt in full.

The terms of the security instrument

Receivership is a contractual self-help remedy available to secured creditors on the terms set out in the security instrument. The terms of the security instrument will inevitably have an impact on the efficiency (in both practical and cost terms) with which the secured creditor is able to enforce its security and take control of the secured property. If the secured creditor wants to enforce its security by appointing a receiver, the secured creditor will not only want to ensure that the security instrument gives the secured creditor the ability to appoint a receiver but it will also want to make sure that the receiver, once appointed, will have all the powers he or she needs to realise the value of the secured property.

It is not just the terms of the security instrument itself that need careful consideration, the ancillary documents that accompany the security document will also have an impact on how cost-effectively and how quickly, the security can be enforced. The ancillary documents are typically used to transfer power to the secured creditor or to a receiver appointed by the secured creditor to enable the secured creditor to take control of the secured property. Where the secured property is charged shares in a BVI or Cayman Islands company (the ‘Target Company’), the ancillary documents are used to vote the charged shares in order to take control of the Target company at board level.

Where the security is in respect of shares in a BVI or Cayman company the typical ancillary documents one would expect to see would include the following:

(a) A share transfer form in respect of the charged shares;
(b) A letter of instruction from the chargor to the registered agent of the Target Company instructing the registered agent to accept the secured creditor as its new instructing party;
(c) Signed but undated resignations letters from each of the directors of the Target Company;
(d) A letter of authority from each of the resigning directors, authorising the secured creditor to date and submit the resignation letters to the registered agent of the Target Company; and
(e) An irrevocable proxy and/or power of attorney executed by the chargor, appointing the secured creditor as its proxy to vote the chargor’s shares in the Target Company and/or act as its attorney to sign written resolutions of the Target Company on behalf of and in respect of the charged shares.

Registering charges in BVI and Cayman

BVI

After the terms of a charge have been agreed and signed by the parties, it is important promptly to register the charge as this will determine its priority. In the BVI, section 166 of the BVI Business Companies Act 2004 (the ‘BCA’) provides that a registered charge will have priority over a charge that is subsequently registered or that is not registered.¹

A BVI company will have two registers of charges: a register of charges that is for internal purposes and a register of registered charges that is a publicly available document held by the BVI Registry of Corporate Affairs.

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¹ This order of priorities can be varied with the express consent of the holder of the charge that has the priority, or by agreement between the charges: see section 167 of the BVI Business Companies Act 2004.
There is no general central public registry or statutory priority regime in relation to charges created by Cayman Islands’ companies. However, under the Cayman Islands Companies Law (2018 Revision) (the ‘Companies Law’) each company must maintain a register of mortgages and charges at its registered office in the Cayman Islands. Failure to update the register leaves the company and directors liable to a financial penalty but does not invalidate the security itself. Hence, following execution of the security documents, the secured party should ensure that particulars of their security are entered on the register of mortgages and charges of the company granting the security. The secured party will also typically request that the security provider delivers to them a certified copy of the updated register of mortgages and charges on or shortly after the date on which the security documents are entered into. Secured parties should ensure that the security instrument obliges the company granting the security to deliver a certified copy of the updated register of mortgages and charges to its registered office promptly following execution of the security instrument.

The register of mortgages and charges is not a publicly searchable register, although under the Companies Law it is open to inspection by creditors and members at all reasonable times. While no statutory priority is afforded to the security holder by ensuring its security is registered, it does put third parties that are provided with a copy of the register of mortgages and charges on actual notice of the existence of the security. As priority of competing security interests would be determined on the basis of common law principles, it is prudent for creditors taking floating charges to require that brief particulars of any negative pledge given by the exempted company in respect of the secured assets are included in the register of mortgages and charges. Although there is no statutory time limit for completing the registration, it is prudent for secured creditors to ensure security is registered as soon as possible given these potential priority implications.

In addition, where a shareholder of a Cayman Islands exempted company grants security over the shares it holds in that exempted company, it is market practice to include in the security document a requirement that a notation is made on the register of members of the exempted company to the effect that the shares are secured in favour of the relevant creditor. It is not possible to file the annotated register of members on a publicly searchable register in the Cayman Islands. Secured creditors will allow a short period following execution of the relevant share security instrument for the notation on the register of members to be completed and a certified copy of the updated register to be provided to the secured creditor. As with updates to registers of mortgages and charges, it is possible to have the register of members updated quickly (including on the date of execution of the security document), if the registered office of the exempted company is given the required notation wording in advance and time zones permit.

**After registration**

Key amongst the benefits that accrue to the security holder is the protection of that security if the company goes into liquidation. The Companies Law provides that, regardless of any winding up order made in respect of the company, any creditor who has security over the whole or part of the assets of the company is entitled to enforce its security without the leave of the Court and without reference to the liquidator. Similarly, in the BVI, the Insolvency Act 2003 (the ‘IA’) confirms that the commencement of the insolvent liquidation of a BVI company does not affect the right of a secured creditor to take possession of and realise or otherwise deal with the assets of the company over which it has a security interest (which protection also exists in respect of a solvent liquidation).

**Charge in possession or receiver?**

Following an event of default under the security instrument, the secured creditor will need to decide whether or not it is going to take control of the charged shares that are the subject of the security. If it makes the decision to take control of them it will need to decide whether it is going to take control of them in its own right or by appointing a receiver of them. If the secured creditor decides to appoint a receiver, it will usually want to appoint a professional receiver. Appointing a professional receiver of the charged shares has the following advantages and it is the usual step a secured creditor takes:

1. Where the company is a private company and there is no readily available market for selling the charged shares, a professional receiver will have the necessary experience to market those shares with a view to obtaining the best price reasonably obtainable for them.

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**Notes**

2. Section 142 of the Companies Law (2018 Revision).
3. Section 9 of the Insolvency Act 2003 (the ‘IA’) defines a creditor as a ‘secured creditor’ of a debtor if it has an enforceable security interest over an asset of the debtor in respect of their claim.
4. Section 175 of the IA.
5. Section 197 of the BCA provides that although a company may be voluntarily liquidated despite the existence of a charge registered in respect of its property, the liquidator is bound to give effect to the rights and priority of the claims of the company’s secured creditors.
2. If the secured creditor wants to buy the charged shares, it is possible to purchase them from the receiver (it is not possible for the secured creditor to sell the charged shares to itself);

3. The registered agent of the Target Company is more likely to cooperate with a third party professional receiver (that it often knows and trusts) than with a secured creditor directly because it will perceive the professional receiver as being neutral;

4. If the secured creditor takes possession of the charged shares, it is under a duty to the chargor, the company, any sureties and any subsequent holders of security, to safeguard the value of the shares. The secured creditor is also under a duty to account for profits received whilst it is in possession of the charged shares, as well as for profits which would have been received but for any failure by them to exercise due diligence. By appointing a receiver the secured creditor passes these various obligations and duties to the receiver and, in that way, insulates itself from any potential liabilities;

5. Unlike a mortgagee in possession, a receiver acts as agent for the chargor, so it can take enforcement action without first having to secure a change in legal title to the charged shares;

6. Although the receiver is the agent of the chargor, he must exercise his powers in good faith, for a proper purpose and in a manner in which he reasonably believes to be in the best interests the party appointing him, meaning that the receiver looks after the interests of the secured creditor; and

7. Where the charged shares are in the hands of a receiver, they are kept off the secured creditor’s balance sheet.

The rights, powers and duties of the receiver

A receiver is typically appointed out of court by the secured creditor in accordance with the terms of the security instrument following a contractual event of default, although they can also be appointed by the Court.

Cayman

In the Cayman Islands, there is no statutory guidance on the rights, powers and duties of a receiver so the secured creditor must look to the terms of the security instrument and the common law. The powers of the receiver to deal with the secured property should be fully set out in the security instrument and they may only be exercised for the purposes for which they are conferred. Typical powers granted to receivers would include the power to take possession of, sell and/or manage the secured property, the power to exercise all voting rights relating to the secured property, and the power to receive and retain all dividends or interest accruing in respect of the secured property.

The receiver owes his or her primary duties to the secured creditor, with secondary duties owed to the security provider and any other party with an interest in the equity of redemption of the secured property. The receiver must exercise his or her duties in good faith.

The receiver is not obliged to exercise any power of sale or to realise the secured property within a specific period of time following his or her appointment but if and when he or she does decide to exercise a power of sale, they must take steps to obtain the best price reasonably obtainable for the secured property at the time of sale. If, having regard to his or her duties, the receiver decides not to sell the secured property immediately following their appointment, they have a duty to act diligently when exercising the rights in respect of the secured property.

BVI

The IA provides that a receiver has the powers expressly or impliedly conferred on them by the charge or other security instrument pursuant to which they are appointed. The IA also provides that, unless the security instrument expressly provides otherwise, a receiver has the power to (a) demand and recover, by action or otherwise, income of the assets in respect of which he or she is appointed; (b) issue receipts for income recovered; (c) manage, insure, repair and maintain the assets in respect of which they are appointed; and (d) exercise, on behalf of the company, a right to inspect books or documents that relate to the assets in respect of which they were appointed in the possession or under the control of a person other than the company.

Consistent with the common law position, the IA also provides that the primary duty of a receiver is to exercise his or her powers in good faith, for a proper purpose and in a manner they reasonably believe to be in the best interests of the person in whose interest they are appointed. Also, when exercising a power of sale of the secured assets, the IA provides that the receivers owe a duty to the creditors, any sureties, the company

Notes

6 Where a receiver is appointed by the Court, he or she will have the powers granted to them in the Court’s order appointing them: section 127(1) of the IA.
7 Section 127(2) of the IA.
8 Section 128 of the IA.
and to any persons claiming an interest in those assets through the company to obtain the best price reasonably obtainable at the time of sale.\footnote{Section 129 of the IA.}

**Appointing a receiver**

**Cayman**

There are no statutory provisions under Cayman Islands law providing for how a receiver should be appointed and there is no statutory requirement to register the appointment of a receiver. The appointment must simply be made in accordance with the terms of the security instrument, in order to be valid.

**BVI**

The IA provides a statutory procedure for the appointment of a receiver out of Court as follows:

1. The appointment must be made in writing, typically by a deed of appointment, executed by the secured creditor in favour of the receiver, setting out the terms on which the receiver is appointed;\footnote{The appointment of the receiver takes effect from the time the receiver receives the written notice of appointment: Section 139(1) and (2) of the IA.}

2. The appointment of a receiver is not effective unless the receiver accepts his or her written notice of appointment before the end of the next business day following the day on which they receive the notice of appointment;\footnote{Section 139(4) of the IA.}

3. The acceptance of the appointment can be given orally or in writing but if it is given orally, the receiver must confirm their acceptance in writing to the person appointing them, within seven days;\footnote{Section 139(5) of the IA.}

4. A confirmation or written acceptance of appointment must state (a) the time and date of receipt of the notice of appointment; and (b) the time and date of the acceptance of the appointment;\footnote{Section 139(8) of the IA.}

5. A deed of indemnity, indemnifying the receivers for any loss, damage or costs that may be incurred by them during the course of their appointment, is also typically entered into by and between the secured creditor and the receiver; and

6. Forthwith upon his or her appointment, the receiver must send a notice of appointment to the company and file a notice of appointment with the Registrar of Companies and, if the company is or has been a regulated person, with the Financial Services Commission and a receiver who fails to do any of these things commits an offence.\footnote{Section 118 of the IA.}

A potential obstacle that can arise when appointing a receiver to take control of charged shares is when the registered agent of the Target Company refuses to recognise the secured creditor’s authority to act in relation to the charged shares. This issue typically arises where the registered agent’s client of record tells the registered agent that there has not been an event of default under the security instrument and that the secured creditor is therefore not in a position, contractually, to enforce its security interest. In the face of conflicting instructions from the registered agent’s client of record and the secured creditor there is a risk that the registered agent will refuse to act on the instructions of either party and insist on seeing a Court order before acting. In these circumstances, the secured creditor may need to consider changing the registered agent of the Target Company or making an application to the Court to rectify the Target Company’s share register to record it as the legal owner of the Target Company’s shares, and incur the delay and costs associated with that.

However, in January 2016, s.91B of the BCA was brought into force to remedy this as follows (emphasis added):

‘Subject to the memorandum and articles of a company, a registered agent shall (a) act on the instructions of the directors of the company if those instructions are contained in a resolution passed by the directors and a copy of the resolution is made available to the registered agent; and (b) recognise and accept the appointment or removal of a director or directors by members of the company.’

Section 91B(b) is a welcome and significant development, particularly for those secured creditors where time is of the essence because they are under pressure to recover the debt or because there is a concern that whilst the Target Company remains in the hands of the chargor there is a risk that its assets will dissipate or disappear. It is common in such cases for the secured creditor to appoint the receivers as directors of the Target Company, whether alongside or in replacement of the incumbent board, so that they, through the receivers, have direct access to the Target Company’s assets and can exert control over the whole of the Target Company even where, for example, the charge is only

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**Notes**

9 Section 129 of the IA.

10 The appointment of the receiver takes effect from the time the receiver receives the written notice of appointment: Section 139(1) and (2) of the IA.

11 Section 139(4) of the IA.

12 Section 139(5) of the IA.

13 Section 139(8) of the IA.

14 Section 118 of the IA.
over 50% of its shares. Once the secured creditor has direct or indirect (through a receiver) control of the board of the Target Company, the registered agent must (under section 91B(a)) act on the board’s instructions to realise the Target Company’s assets with a view to satisfying the debt owed to the secured creditor. Clearly, the initial cooperation of the registered agent in accepting the appointment of the receivers as directors of the Target Company (and accepting the removal of the incumbent directors) is key.
Acts of Perversity: When a Liquidator’s Decision May Be Overturned in the British Virgin Islands

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Synopsis

The appointment of a liquidator is a significant occurrence in the life of a BVI company. Aside from the obvious implication that the life of the company will ultimately be brought to an end, a significant power shift occurs in the management of the company.

Once appointed, the liquidator assumes control and custody of the assets of the company. The directors, though they remain in office, are divested of their powers and have no powers, functions or duties other than those expressly preserved by the BVI Insolvency Act, 2003 (the ‘Act’). Creditors of the company assume primacy in place of the members and members are prohibited from exercising any of the powers granted to them under the company’s memorandum and articles of association.

In contrast to the limitations imposed on the directors and members of the company, the liquidator is granted very broad powers under schedule 2 of the Act in order to allow him to fulfill the duties imposed upon him by the Act to take possession, protect and realise the company’s assets, to discharge the company’s liabilities and to return any surplus to members.

As would be expected, such a situation is ripe for creating dissatisfaction. In the exercise of his powers a liquidator may find himself at odds with directors, creditors, members and other stakeholders interested in or connected to the company. From time to time, such dissatisfaction reaches a sufficient pitch to cause such aggrieved persons to invoke the assistance of the Court.

A liquidator in the BVI must be the holder of an Insolvency Practitioner’s licence. He is invested by statute with wide powers and duties and is credited with broad discretion to perform his functions. That being so, the case law shows that the Courts are loath to interfere with a liquidator’s exercise of his powers or to act as a review panel in relation to his acts or omissions and, fraud or misconduct aside, will do so only in exceptional circumstances.

Legal framework for challenge

Section 273 of the Act provides the statutory basis for the Court’s jurisdiction to intervene in the exercise by a liquidator of his powers:

‘A person aggrieved by an act, omission or decision of an officer holder may apply to the Court and the Court may confirm, reverse or modify the act, omission or decision of the officer holder.’

The Court also has an inherent jurisdiction to control the conduct of liquidators as officers of the Court.

The precise interplay between the scope of the Court’s inherent jurisdiction and its statutory jurisdiction is not clearly defined. However, a recent decision of the Eastern Caribbean Court of Appeal (on appeal from the Territory of the Virgin Islands) demonstrates that there is little room for the exercise of the inherent jurisdiction where the statutory regime expressly deals with the matter. In Chu Kong v David Yen Ching Wai, Chan Pui Sze, Roy Bailey and John Greenwood as Joint Liquidators of Ocean Sino Limited (In liquidation), Lau Wing Yan BVHCMAP2018/0019 (‘Ocean Sino’) the Eastern Caribbean Court of Appeal considered the circumstances in which the Court will exercise its inherent jurisdiction to supervise its officers where an express statutory regime exists to deal with a particular matter. The Court agreed with the proposition that the inherent jurisdiction is inapplicable where it is inconsistent with a parallel statutory regime, on the basis that it is wrong to use the inherent jurisdiction as a means of adopting a different approach to arrive at a different outcome from that which would result from an application of the statute.

A ‘person aggrieved’

The Eastern Caribbean Supreme Court, Virgin Islands (the ‘BVI Court’) will only exercise its powers, whether under section 273 of the Act or under its inherent jurisdiction, if the applicant has a sufficient interest in the liquidation to afford him locus standi to make the application.
The Act confers standing on a ‘person aggrieved’, a term which, at first glance, appears wide enough to encompass any person who is dissatisfied with a liquidator’s act or omission. However, decisions of the BVI Court have considerably narrowed and clarified the understanding of the term ‘person aggrieved’.

Firstly, an applicant under section 273 must be a proper person to make the application. This does not simply mean that he has an interest in the application or may be affected by its outcome; rather, it means he has a legitimate interest in the relief being sought so that he qualifies as a ‘person aggrieved’.

It has been established, therefore, that a ‘person aggrieved’ must be a contributory, creditor or a third narrow class of persons directly affected by the exercise of power specifically given to liquidators, who would not otherwise have any right to challenge the exercise of that power. An ‘outsider’ to the liquidation or a ‘meddlesome busybody’ will not be permitted to attack the decisions of the liquidator. So, in John Greenwood et al. v FuturesOne Diversified Fund SPC Ltd et al. BVIHCM (COM) 2012/0113, 0116, 0114 and 0115 (‘FuturesOne’), Bannister J sitting in the BVI Commercial Court, held that Brick Kane of Robb Evans and Associates LLC, appointed as equity receiver by the United States District Court, had no standing to bring an application under section 273 of the Act as the liquidators’ appointments had not prejudiced the receiver and had no effect on the property of the funds or its beneficiaries. Though the liquidators’ appointments ensured that the funds had management, which could assert claims to any property which rightfully belonged to the funds and could challenge attacks by the receiver on such property, that did not make the receiver a person aggrieved in the sense in which the term is used in section 273.

Similarly, in Kevin Gerald Stanford v Stephen John Akers and Mark McDonald BVIHCMAP 2017/0019 (‘Stanford’) the Eastern Caribbean Court of Appeal (BVI) held that, as the applicant was a mere shareholder of a shareholder of the insolvent company he did not have a legitimate interest in the relief sought and therefore had no standing to bring an application under section 273. The Court held that, as a general proposition, a court that is asked to exercise a statutory power, or its inherent jurisdiction, will act only on the application of a party with a sufficient interest to make it. An applicant seeking to challenge the exercise by a liquidator of his power must therefore show that he is a proper person to make the application and that he has a legitimate interest in the relief sought since an outsider to a liquidation cannot attack decisions of a liquidator.

However, the mere fact that a person has ‘technical capacity’ (as a creditor or shareholder/contributory) on its own is not sufficient if the circumstances demonstrate that the relief is sought not in that capacity but some other. In UBS AG New York et al. v Kenneth Krys et al. BVIHCMAP 2016/0027 former shareholders of Fairfield Sentry Limited (in liquidation) brought an action, inter alia, under section 273 of the Act seeking to move the BVI Court to restrain the liquidators from bringing proceedings against them (and others) in courts in the United States of America. It was argued on behalf of the applicants, inter alia, that they were ‘alleged debtors’ and therefore had standing to bring the application. However, it was held that the appellants were not invoking section 273 in their capacity as creditors but, in essence, as defendants in the US proceedings. In such a capacity they were strangers to the liquidation and had no legitimate interest in the relief sought.

Likewise, in Gold & Appel Transfer SA Iceberg Transport SA et al. v Meade Malone (In his capacity as Liquidator of Gold & Appel Transfer SA) BVIHCV 2004/0130 (delivered 23 March 2006, unreported) the liquidator was pursuing avoidance actions in the United States of America and the defendants applied under section 273 of the Act to stop those proceedings. Although one of the defendants was a creditor and another a member, it was held that they were not seeking the section 273 remedy in those capacities and were thus held to be ‘outsiders to the liquidation’. Accordingly, Hariprashad Charles J found that they had no standing to make an application under section 273.

**Acts complained of**

Section 273 specifically deals with the BVI Court confirming, reversing or modifying specific acts, omissions or decisions of the liquidator. Accordingly, to found a claim under that section, an aggrieved person must identify and act or decision which the Liquidator has taken or an omission of which he has been guilty. There is no relief available under section 273 for an applicant who is simply aggrieved by the liquidator’s existence. In FuturesOne the BVI Court noted that the applicant was unable to point to any act, or omission of the liquidators by which he was aggrieved. The complaint was in relation to the liquidators’ appointment itself, which the applicant complained was wrong. The BVI Court found that the liquidators had been validly appointed. However, in any event, such a complaint was not in the purview of section 273.

In Ocean Sino the Court held that a stakeholder who believes that liquidators are deliberately stalling or refusing to decide on a proposal put to them for the efficient liquidation of a company might write to the liquidators seeking a reasonable timeframe by which to expect a response and warning that a failure to respond would be met by recourse to the Court. If the liquidators reject the proposal, the stakeholder may move the court under section 273 to reverse that decision. If, after the expiration of a reasonable period, the liquidators have failed to respond, this could be considered an omission for the purposes of section 273.

However, the Court cannot intervene on the basis of section 273 to direct some future action of the
liquidator nor does the inherent jurisdiction assist in such a case. In Ocean Sino the complaint made was that the Liquidators had failed to implement a proposal put forward by the applicant and the Court was invited to direct them accordingly. The Court found that any residuary or complementary jurisdiction that it has to control the conduct of the liquidators, outside the scope of the Act, cannot be invoked to control the future, unknown conduct of the Liquidators.

Accordingly, where there had been no complaint about any specific act, omission or decision of a liquidator, any interference by the Court may be deemed an unwarranted interference with the powers granted to liquidators under the Act.

**Acts of perversity**

The legal test for whether ‘an act, omission or decision of an office holder’ should be set aside under section 273, is commonly referred to as the ‘perversity test’.

As explained by the Court of Appeal in Stanford, aside from bad faith or fraud, a court will only interfere with the actions of a liquidator if he has done something so perverse and manifestly absurd that no reasonable person would have done it.

The threshold is deliberately a high one. In Stanford it was stressed that it is not open to the BVI Court to seek to substitute its opinion for that of the liquidator or to question whether the liquidator has chosen the best approach. The position, as explained in ABN AMRO Fund Services (Isle of Man) 24 Nominees Limited formerly Fortis (Isle of Man) Nominees Limited) and Others v Kenneth Krys et al., BVIHC MAP 11-16, 23-28 of 2016 is that the Court’s role is to prevent a liquidator from taking steps that are so manifestly absurd or perverse that they fall completely outside the permissible range of options. The BVI Court must therefore ascertain whether the decision in question is so absurd that no reasonable liquidator could have arrived at it. It is only then that the BVI Court will intervene.

**Conclusion**

The bar to a successful challenge to a liquidator’s decision has been set deliberately high and the task of overturning the decision of a liquidator is a challenging one. It is not the scheme of the insolvency regime in the BVI to provide a ready channel for that conflict by facilitating Court challenges to a liquidator’s decision other than in an exceptional case. So, not only must a person wishing to challenge the decision of a liquidator satisfy the Court that he has a sufficient interest in the liquidation to qualify him to make such a challenge, he must be able to point to a specific act or omission of the liquidator and to demonstrate that it is so manifestly absurd or perverse that no reasonable liquidator could have acted in that manner. The cases in which a challenge succeeds on that basis will necessarily be, and the cases show that they are, rare.
Introduction

The insolvency regime in Jersey is an interesting mix of English law and Norman customary law influences. Jersey has four principal methods of winding up a company:

1. Summary winding up;
2. Creditors winding up;
3. Just and equitable winding up; and
4. Désastre

Whilst there are limitations to the insolvency options available in Jersey, for example the absence of an administration process, the Royal Court has shown itself to be willing to take a pragmatic approach when dealing with corporate insolvencies to enable the best possible outcomes for creditors.

The two areas in which the Royal Court has most frequently shown its willingness to assist creditors are (i) in relation to the recognition of foreign officeholders and (ii) the use of the just and equitable winding up regime. This article however focuses on the use of just and equitable winding up in Jersey and the flexible approach the Royal Court has adopted to this regime.

Just and equitable winding up – the legal basis

Just and equitable winding up is provided for by Article 155 of the Companies (Jersey) Law 1991 (the ‘Law’) which states that:

(1) A company, not being a company in respect of which a declaration has been made (and not recalled) under the Désastre Law, may be wound up by the court if the court is of the opinion that-
   a. It is just and equitable to do so; or
   b. It is expedient to do so.
(2) ...
(3) ...
(4) If the court orders a company to be wound up under this Article it may-
   a. Appoint a liquidator;
   b. Direct the manner in which the winding-up is to be conducted; and
   c. Make such orders as it sees fit to ensure the winding up is conducted in an orderly manner.

The Royal Court therefore has a broad jurisdiction under Article 155 of the Law and has noted in the case of Re Leveraged Income Fund Limited that whilst Article 155 of the Law is based on a similar provision of the Companies Act 1985 and the English courts have developed certain categories of cases where the court will exercise its power under the just and equitable jurisdiction, the Royal Court is not confined to such categories.

The Royal Court in Re Leveraged Income Fund Limited went on to state that the words ‘just and equitable’ are general words and quoting from Palmers Company Law Vol. 3 said:

‘It has sometimes been suggested that there is an exhaustive list of situations that may fall within the scope of the “just and equitable” clause, but it now seems that although such classification may be convenient for purposes of presentation, the words “just and equitable” require a more flexible interpretation.’

It is therefore clear that the Royal Court has a wide jurisdiction and is able to adopt a flexible approach in such circumstances. The Royal Court summarised its approach to just and equitable winding ups in the unreported case of Jean v Murfitt stating that:

‘We conclude by observing that the words “just and equitable” in Article 155 of the 1991 Law should be given a flexible interpretation. Justice and equity cannot be confined within the four corners of specific instances.’

Notes

2  (Jersey Unreported 11 December 1996).
The scope of just and equitable winding up – three key cases

1. Representation of Poundworld (Jersey) Limited

This is an important case which provides guidance on the exercise of the Royal Court’s jurisdiction to order a just and equitable winding up. Poundworld was a Jersey company which had been trading for many years before it ran into financial difficulties. The Royal Court was satisfied that the company was insolvent applying the relevant test in Jersey, namely that it was not able to pay its debts as they fell due. It should be noted that this test differs from the balance sheet test applied in England and Wales and a number of other common law jurisdictions.

The directors of Poundworld had initially intended to conduct a creditors’ winding up and had given notice of the necessary meetings of creditors and shareholders that were required to take place. In the interim however there were significant developments which caused the directors to change their approach and instead make an application to the Royal Court for a just and equitable winding up, having formed the belief that this approach would be more beneficial for the creditors of the Company.

The crux of the argument put forward by Poundworld’s Counsel was that in the special circumstances of the case the Royal Court should make an order for a just and equitable winding up, rather than leave the creditors’ winding up process to run. This argument was advanced due to the time critical situation facing the company and the delay that would arise from waiting until the scheduled meetings of creditors and shareholders had taken place. Two particular matters were relied upon by counsel to justify the application.

The first matter related to stock held by the shipper Poundworld worked with. The arrangements in place between the shipper and Poundworld provided that much of Poundworld’s stock was held free of charge in the shipper’s warehouse. At the time of the application there was approximately £100,000 of stock at cost price held in the shipper’s warehouse. Poundworld however owed the shipper £28,000 and the shipper was threatening to exercise a lien over the stock and to sell it to recover the sums owed to it. Whilst it was not accepted by Poundworld that the lien claimed was valid, Poundworld was unable to gain access to the stock without legal action or paying the sums owed.

The evidence placed before the Royal Court from the proposed liquidator and one of the directors of the company, in support of the application, identified that if the stock was sold by the shipper it was unlikely to realise enough to clear the debt owed to the shipper and was therefore unlikely to provide a surplus for other creditors. In contrast it was asserted that if the stock could be released and was sold from Poundworld’s shops at retail value the proceeds could, on a conservative estimate, realise £150,000 and possibly as much as £200,000. Due to the historic relationship between Poundworld and the shipper it was thought unlikely that the shipper would agree with the directors to release the stock but if a liquidator was appointed it was felt the shipper may be willing to do so. The importance of the liquidator being seen to be independent and subject to the supervision of the Royal Court was identified as a key reason for this view.

The second matter involved the stock in the four retail outlets of Poundworld. Rent was overdue on three of the premises. One of the landlords was threatening to exercise his customary law rights over the stock held and there was concern that the other landlords would follow suit. As was the case with the shipper any sale by the landlords of the stock was considered likely to only realise a small percentage of the cost price. If however the stock were to be sold at retail prices from the outlets over a reasonable period it was said that there would be a significant uplift on the sums recovered. The value of the stock was estimated to be, at cost price, approximately £80,000. It was again asserted that the creditors, in this case the landlords, would be unlikely to reach an agreement with the directors of Poundworld but would be likely to do so with a liquidator.

The view of the proposed liquidator was that it would be in the best interests of the creditors for the stock held at the shipper’s warehouse and at the retail outlets to be sold at retail prices over a period of six weeks. The key supporting factors identified for this view were:

1. The stock was Poundworld’s only material asset.
2. If sold at retail prices the stock may provide a reasonable prospect that preferred creditors would be paid in full and ordinary creditors would receive a ‘modest dividend’.
3. If the stock were to be sold at wholesale prices in bulk it would be unlikely that there would be anything more than very limited recovery for anyone other than the landlords and possibly the shipper.

The Royal Court was satisfied that if the appointment of a liquidator was to be delayed until the scheduled creditors’ meeting, there was a substantial risk that the interests of the creditors as a whole would suffer a significant negative effect.

The Royal Court challenged counsel by observing that he was asking it to make an unusual order and noting that the Law provided a specific procedure to be used for the winding up of insolvent companies, namely the creditors’ winding up regime. The Royal
Court observed that the creditors’ winding up regime gave creditors a say in the choice of a liquidator and in supervising the conduct of the liquidation through a liquidation committee. As such, the Court questioned whether it was right for it to order the just and equitable winding up of an insolvent company when the creditors’ winding up regime existed.

The Royal Court further stated that it should exercise caution before ordering a just and equitable winding up of an insolvent company, whilst at the same time acknowledging that Article 155 of the Law provided it with a wide jurisdiction to order a just and equitable winding up. In the circumstances of the Poundworld case the Royal Court was satisfied that ‘the best interests of the creditors would undoubtedly be served by Poundworld being able to sell its remaining stock from its outlets at retail prices by continuing to trade for the limited period necessary to achieve this’.

The Royal Court was also satisfied that if it did not order an immediate just and equitable winding up there would be prejudice to the body of creditors as a whole if they were required to wait until the creditors meeting that had been scheduled. The Royal Court further justified authorising the liquidators to secure the stock and continuing to trade at retail prices by concluding that it was clearly in the best interests of the creditors as a whole.

The Court showed that it was alive to the fact that it was making an order for a just and equitable winding up without hearing from the creditors of Poundworld, some of whom may have potentially been prejudiced by its decision, and therefore required that notice be given to creditors without delay and additionally gave permission for any creditor to apply to it to seek to have the order set aside.

2. Re Representation of Collections Group

The second key case is that of Re Representation of Collections Group. The Royal Court was asked for the first time to order a just and equitable winding up in circumstances where the proposed course of action for the liquidators was to enter into an agreement to sell as much of the business and assets of the Collections Group to a new company, in what would be known in England as a ‘pre-packaged sale’. The Court observed that this was something sometimes done by administrators but that in Jersey the concept of administration does not exist. The Royal Court noted that it was clearly established that it had a wide discretion under Article 155 of the Law when considering applications brought for a just and equitable winding up. The Royal Court was satisfied that it had the jurisdiction to make the orders sought in this case and turned to consider the question of whether it should exercise its discretion to do so.

It was acknowledged by the Royal Court that such a sale could sometimes be in the interests of creditors but that due to the potential for abuse the Joint insolvency Committee of England and Wales had issued a Statement of Insolvency Practice (SIP 16) which provided guidance for insolvency practitioners in relation to pre-packaged administrations. The Royal Court made extensive reference to SIP 16 and required that the liquidators pay careful attention to the guidance it provides.

The Collections Group employed some 47 full time staff along with approximately ten seasonal staff and was in a dire financial position. The companies had relatively limited assets in the way of stock and other fixed assets. The proposed liquidator summarised the companies’ position as being that they could not pay their staff, their obligations in respect of their premises or their stock. Consequently it was submitted to the Royal Court that if the order was not made the companies would need to be closed immediately, all of the staff would become unemployed and there would be almost no payment to any creditor.

The proposal put to the Royal Court was that if the companies were free of their historic debt, could be restructured and receive new investment then it would be possible for a significant part of the business to trade successfully and profitably. An investor unconnected with the companies had been identified who was prepared to provide an injection of funds of at least £400,000 if the businesses were acquired by a new company.

The proposed sale agreement that was to be entered into by the liquidator involved the sale of such of the business and assets of the companies as the new company was willing to acquire, with the sum ultimately to be paid equal to 20% of net profits of the business generated within one calendar year of the acquisition. The new company would also pay 25% of any net proceeds of sale if it should dispose of any part of the business within a year of the acquisition. Although the potential sums would not realistically clear all of the debts of the companies there was a reasonable prospect the preferential creditors could be paid in full or in part with little chance that the proceeds would be sufficient to pay ordinary unsecured creditors.

The Royal Court heard a number of reasons from counsel as to why it should order a just and equitable winding up. In summary it was argued that the companies were hopelessly insolvent and would have to cease trading immediately if the Court did not approve the pre-packaged agreement. This would have caused the loss of 47 jobs, have a negative impact on the local retail market and cause there to be no dividend for

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4 [2013]JRC 096.
any creditor. In contrast counsel highlighted that if the Court ordered the just and equitable winding up, around 40 jobs would be saved and there would be a realistic prospect of preferred creditors receiving a dividend within 12 months.

Of significant concern to the Royal Court was ensuring it did not approve a ‘Phoenix’ agreement which resulted in companies with the same or similar beneficial ownership emerging with the assets of the business but without the creditors. The Royal Court was satisfied in the circumstances that this was not the case. Even though a director of the companies was to be involved with the proposed purchaser, he did not own any part of the companies, and it was in the best interests of the creditors for a just and equitable winding up to be ordered, the Royal Court accepting the reasons put forward by counsel.

3. Representation of Julian Charles Tyacke

The third case illustrating the scope of the just and equitable winding up regime in Jersey is Re the Representation of Julian Charles Tyacke. This case related to an application to the Royal Court for an order for a just and equitable winding up in relation to five companies which formed part of a wider corporate structure, including companies incorporated in a number of different jurisdictions across the globe. There were considerable intercompany links within the group and the assets of the Jersey companies were in a number of locations across the globe with the majority in the Middle East. The group of companies of which the Jersey companies were part was operating at a substantial loss and the Jersey companies were cash flow insolvent.

The application made to the Royal Court was part of a wider process involving the other companies in the group structure which was intended to bring the companies to an end in accordance with the relevant processes in each jurisdiction. The Royal Court observed that the corporate structure involved was ‘on any analysis complex’ and that it was apparent that in respect of the winding up there would need to be significant levels of co-operation between the Jersey companies and the other group companies. The assets of the corporate group were spread across some 38 sites located across the world and inevitably co-ordination would be required to secure those assets so that the winding up could be progressed in an orderly manner and avoid the risk of improper preference of certain creditors over other creditors.

As in the two other cases we have looked at, the Royal Court observed that its jurisdiction to order a just and equitable winding up was a broad one. In considering the application the Royal Court stated that it was being asked to exercise its discretion to enable the Jersey companies to be subject to a just and equitable winding up as a result of their insolvency. The Court cited with approval the decision in Poundworld, in which the Royal Court confirmed that it could order a just and equitable winding up where the company to be wound up was insolvent.

The Royal Court determined that a désastre, a form of insolvency procedure open to creditors and debtors where the Viscount (Jersey’s official receiver) is appointed to manage the bankrupt’s affairs, was not appropriate in the circumstances, noting that the Viscount would be unlikely to be in a better position than professional liquidators. The key reasons identified by the Royal Court in reaching this conclusion were:

1. The Jersey companies were part of a very complicated group of companies. The whole insolvency process needed to be effectively co-ordinated and considerable interaction would be required between the insolvency processes in the various jurisdictions, with many of the systems utilised by the Jersey companies in common with companies in the group located elsewhere;

2. Many of the assets of the Jersey Companies were in ‘high risk’ jurisdictions and it was important to act quickly in respect of the assets to ensure that they were secured. The Viscount would not have authority to act in those jurisdictions and would need to take extremely urgent action if she were to be able to take any steps;

3. It was important in the circumstances of this case not to enter into a process by which notice would be given to creditors before they are secured as there was a risk of dissipation.

The Royal Court was also satisfied that a creditors’ winding up was not appropriate in the circumstances due to the concerns that were expressed about notice being given to some creditors who it was thought may pose a risk to the recovery of some of the group’s assets. It is worth noting that a number of the Jersey companies’ major creditors had been given notice of the application and were represented at the hearing and that the majority of the major creditors had approved the approach proposed by the representor. The Viscount also agreed that in the circumstances a just and equitable winding up was more appropriate.

The Court concluded that it was satisfied that the companies were insolvent and a just and equitable winding up was the best means of winding up the Jersey companies given the ‘highly complex Intercompany and Intergroup relationships and the worldwide location of the assets’.

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Conclusion

As the cases considered in this article illustrate the Royal Court has shown it is willing to make full use of its wide jurisdiction to order a just and equitable winding up of a Jersey company. The circumstances in which the Royal Court will order a just and equitable winding are diverse and the Royal Court’s powers have facilitated attempts to realise the best outcome for creditors in difficult circumstances.

The pragmatic approach taken by the Royal Court in relation to applications for a just and equitable winding up is helpful to creditors and practitioners alike. It has been used to help ameliorate the lack of an administration regime in Jersey and deal with complex insolvency situations that can arise in relation to global corporate structures. It is also indicative of the Royal Court’s approach to insolvency situations more generally, to put it simply the Royal Court is focused on facilitating the best outcome for creditors and will use its powers creatively to achieve this aim.
Introduction

The Cayman Islands has long established itself as a leading offshore financial centre which offers a sophisticated and flexible restructuring toolkit by which to implement cross-border restructurings. With a robust common law legal system based on English law (with ultimate recourse to the Privy Council of the United Kingdom) providing legal certainty and predictability, a highly sophisticated, dedicated financial services division of the Grand Court of the Cayman Islands (the ‘Cayman Court’) and an experienced network of judges, practitioners and advisors in the insolvency and restructuring sector, it is not surprising that the jurisdiction has a proven track record for constantly delivering complex and high-value restructurings.

Although the Cayman Islands has no formal rehabilitation process for companies in financial distress similar to US Chapter 11 proceedings or English administration, the Cayman Islands scheme of arrangement is often utilised to deliver not only debt restructurings but also corporate reorganisations, acquisitions, mergers and takeovers in circumstances where it is not possible or practical to obtain the consent from all affected stakeholders. Accordingly, a Cayman Islands scheme of arrangement is not a formal insolvency process as such but where it is utilised in connection with a protective provisional liquidation wrapper or official liquidation, the Cayman Islands scheme company would have the benefit of an automatic stay on any unsecured creditor action.

One aspect of the Cayman Islands’ scheme of arrangement – the headcount test – which is the statutory requirement that a Cayman Islands scheme of arrangement has to be approved by a majority in number in addition to being approved by at least 75% in value of each class of stakeholder present and voting at the court ordered meeting, vote to approve the Cayman Islands scheme. Cayman Islands schemes of arrangement are frequently used to implement cross-border and multi-level debt restructurings by varying or cramming down the rights of the relevant creditors and/or shareholders of a company and have become the restructuring tool of debate. Many commentators query its relevance in the context of modern restructurings.

Whilst originally implemented as a minority protection mechanism aimed at protecting smaller shareholders from decisions pushed through by larger shareholders with more significant stakes (and more significant financial resources), there is an argument that in today’s world, the headcount test is no longer fit for purpose.

This article examines the concerns with respect to the continued application of the headcount test and considers whether, in comparing the approaches taken in certain other jurisdictions, it is now time for reform in the Cayman Islands.

Cayman Islands scheme of arrangement

The Cayman Islands legislation for schemes of arrangement is derived from 19th century English legislation. The concept of the scheme of arrangement (together with the requisite approval thresholds to be attained) was first introduced into the Cayman Islands by the Companies Law in 1961 (replicating Section 206 of the English Companies Act 1948).

A Cayman Islands scheme of arrangement is a court-sanctioned compromise or arrangement between a company and its creditors and/or shareholders (or any class of them) which binds all affected stakeholders (including any dissenting creditors and/or shareholders) provided that: (i) a majority in number; and (ii) 75% in value of each class of stakeholder present and voting at the court ordered meeting, vote to approve the Cayman scheme. Cayman Islands schemes of arrangement are frequently used to implement cross-border and multi-level debt restructurings by varying or cramming down the rights of the relevant creditors and/or shareholders of a company and have become the restructuring tool of...
of choice in the Cayman Islands given its flexibility and predictability.

A Cayman Islands scheme enables a company to enter into a binding compromise or arrangement with its creditors and/or shareholders without the need to enter into an individual and separate contract with each and every affected stakeholder and provides companies with a tried and tested mechanism to implement an arrangement where it is not possible or practical to obtain a fully consensual deal. A Cayman Islands scheme will only become effective in accordance with its terms and binding on the company and all members of the relevant classes (including any dissenting stakeholder and regardless of whether or not they voted) once the Cayman Court has sanctioned the scheme and the court sanction order has been filed with the Cayman Islands Registrar of Companies.

When schemes of arrangement were first introduced in England over 100 years ago, shareholders and creditors typically held their interests both beneficially and legally so there was little difference between the persons whose name was entered onto the register of shareholders (or equivalent) and the person beneficially entitled to those interests. In its historical context, the statutory majority test operated as an appropriate check and balance – the headcount test prevented a minority with a large stake prevailing over a majority with a smaller stake; and the value test prevented a numerical majority with a small stake prevailing over the minority with a large stake. As summarised by Brooking J, the dual majority test ensures that ‘mere numbers on a count of heads will not carry the day at the expense of the amount invested and on the other hand that the weight of invested money may not prevail against the desires of a sizeable number of investors.’

However, this is no longer the case – stakeholders’ interests are now often held beneficially through nominees, custodians (such as The Depositary Trust Company in the United States or HKSCC Nominees Limited in Hong Kong), clearing houses or other third parties (this is often more of an issue with shareholder interests). If only registered legal holders of debt and/or equity of the headcount test, then any headcount is unlikely to be necessary for the purpose of enabling it to determine whether or not the statutory majorities will have been achieved. If all or substantially all of the shares or debt instruments to which the proposed scheme relates are registered in the name of one or more custodians of clearing houses, the [Cayman] Court may direct that ... (b) such custodian or clearing house shall specify the number of votes cast in favour of the scheme and the number of clients or members on whose instructions they are cast and the number of votes cast against the proposed scheme and the number of clients or members on whose instructions they are cast [emphasis added].

Practice Direction 2/2010 sets out the manner in which the votes of shareholders will be counted, and provides that the Cayman Court will ‘look through the register’ for the purposes of determining whether or not the statutory majorities have been met stating that ‘the majority in number will be calculated on the basis of the number of clients or members giving instructions to the custodian or clearing house.’

Until the decision in Little Sheep, the Cayman Court adopted the traditional approach (applied in all

‘Looking through the register’: the Cayman Court’s approach in Little Sheep\(^6\) and Alibaba\(^7\)

Section 86 of the Cayman Islands Companies Law (2018 Revision) (the ‘Companies Law’) is widely drafted and provides that the Cayman Court has the power to order a scheme meeting be carried out in such manner ‘as the Court directs’ including any directions as to how voting is carried out and how votes are to be counted. Importantly, Section 86 does not stipulate the mechanism by which the Cayman Court should determine whether the headcount test has been met; this is ‘a matter for the court to fix the mechanism in accordance with the [Grand Court] Rules, having regard to the circumstances of the case ... ’. The Cayman Court may be guided in this process by the Grand Court Rules and related Practice Directions.

Order 102, rule 20 of the Cayman Islands Grand Court Rules 1995 (Revised Edition) (the ‘Grand Court Rules’) provides that:

‘the [Cayman] Court shall give such directions as may be necessary for the purpose of enabling it to determine whether or not the statutory majorities will have been achieved. If all or substantially all of the shares or debt instruments to which the proposed scheme relates are registered in the name of one or more custodians of clearing houses, the [Cayman] Court may direct that ... (b) such custodian or clearing house shall specify the number of votes cast in favour of the scheme and the number of clients or members on whose instructions they are cast and the number of votes cast against the proposed scheme and the number of clients or members on whose instructions they are cast’ [emphasis added].

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4 ANZ Executors and Trustees Ltd. v Humes Ltd [1990] VR 615 at paragraph 622.
5 Cayman Islands Grand Court Rules 1995 (Revised Edition) (the ‘Grand Court Rules’, Order 102, r.20(6) and see also Practice Direction No. 2 of 2010, paragraph 4.
6 In re Little Sheep (Unreported, Jones J, 20 January 2012).
7 In re Alibaba.com Ltd Unreported, 20 April 2012.
8 See per Jones J in Little Sheep; and approved in Alibaba.
9 See per Jones J in Little Sheep.
common law jurisdictions)\textsuperscript{10} to the position of a custodian. Namely, assuming the custodian is instructed to vote some of the shares it holds on behalf of beneficiaries in favour of the scheme and others against the scheme, to treat the custodian for the headcount test as one vote ‘for’ the scheme and one vote ‘against’ the scheme. The effect being that if the custodian received only one vote to approve the scheme by a shareholder holding a minimal percentage of the shares in the company and a greater number of shareholders holding a far higher percentage of the shares in the company voted against the scheme, the votes counted by the Cayman Court (that is, one vote for and one vote against) would cancel each other out. Following this traditional approach, the registered holders of shares in a Cayman scheme company was relevant for the purposes of the headcount test, not those with the beneficial interest in such shares.

In *Little Sheep* it was argued that, for the purposes of the headcount test, a custodian shareholder should be counted as one person having voted either for or against the scheme depending on its net voting position (i.e. to ensure that only one vote was counted in respect of each custodian). This was ultimately rejected by the Cayman Court which held that treating HKSCC Nominees as one shareholder would be inconsistent with the purpose of Section 86 and Order 102, rule 20(6). Jones J stated that ‘the effect of allowing [HKSCC Nominees] to vote for and against the scheme is that the outcome as regards the “majority in value” will be determined, almost inevitably, by the instructions received from its participants. This is the common sense approach’ and one which produces ‘a commercially acceptable result which will be readily understood by investors’. By contrast, Jones J found that the effect of treating HKSCC Nominees as one shareholder (with one vote) for the purpose of ascertaining the ‘majority in number’ without regard to the number of participants from whom instructions are received is not only ‘inconsistent’ with the purpose of Section 86, but would also be ‘highly artificial’ and could produce a result which is commercially unacceptable.\textsuperscript{11} Jones J also noted that such an approach could ‘make it easier for an opponent of the scheme to defeat it by the simple mechanism of having a nominal number of its shares registered in the names of the requisite number of individuals who agree to vote against it ... it would be possible for someone having a minimal economic interest in the company to hold it to ransom.’

The Cayman Court found that Section 86 (together with Order 20 of the Grand Court Rules) gave the Cayman Court wide discretion; and that for the purposes of the headcount test, it was appropriate to count the parties from whom the clearing house (in that case, HKSCC Nominees) received instructions. Jones J held that a clearing house could be considered a ‘multi headed member’ such that the number of clearing system participants for whom instructions were received (both for and against) would determine the votes attributable to the nominee for the purpose of the headcount test.

The issue of how to count votes later arose in *Alibaba*. In that case, Cresswell J indicated that he ‘would be inclined’ to follow Jones J decision in *Little Sheep*. Cresswell J noted that the decision in *Little Sheep* is consistent with and reflects [Practice Direction] 2/2010’.

Ultimately, Cresswell J did not make any order as to how the votes in the scheme would be counted, but ordered that ‘to the extent that the shares ... are registered in the name of one or more custodians or clearing houses ... such custodian or clearing house ... may cast votes both for and against the proposed scheme in accordance with the instructions of its clients ... shall specify the number of votes cast in favour of the scheme and the number of clients or members on whose instructions they are cast ...’. Given the complex arrangements in which shares and debt instruments are held today (particularly in the case of shares of a listed company which may be traded throughout the scheme process), looking through a single layer of ownership – usually to a custodian or nominee – may not necessarily be sufficient and there have been calls for the practice of ‘looking through the register’ to be re-considered.\textsuperscript{12} Below we consider the criticisms raised regarding the practice of looking through the register and the headcount test more generally.

**The headcount test – no longer fit for purpose?**

The debate regarding the appropriateness of the headcount test centres on the following points:

(1) The headcount test gives minority creditors and/or shareholders too much power to reject a Cayman scheme, whatever its merits.

It is currently the position, as a matter of Cayman Islands law, that within one class of creditors (who must have ‘rights not so dissimilar as to make it impossible for them to consult together with a view to their common
interest to form a class) a few small creditors holding a minimal percentage of the relevant debt could vote against a Cayman Islands scheme of arrangement, causing the scheme to fail (as the relevant headcount test threshold may not be met) and thereby preventing the implementation of an otherwise commercially reasonable scheme of arrangement approved by larger creditors holding a more significant portion of the relevant debt.

It is not clear why minority shareholders and/or creditors with the same rights (forming part of the same class) should be granted additional control over the outcome of any vote which is tantamount to a right of veto.

The circumstances are in direct contrast to the protections afforded to shareholders and/or creditors with different rights who form a separate class – in that scenario, rightly, if the relevant class of shareholders and/or creditors reject the Cayman scheme then the Cayman Court does not have the appropriate jurisdiction to sanction the Cayman scheme and the Cayman scheme will therefore fail.

(2) Minority creditors and/or shareholders are already effectively protected by the statutory process for a Cayman Islands schemes of arrangement.

The Cayman statutory procedure for schemes of arrangement provides minority shareholders and creditors with sufficient protections.

As noted above, at the first court hearing, the Cayman Court will consider whether it is appropriate to convene class meeting(s) at which stakeholders can vote on the proposed scheme and if so, the composition of classes so as to ensure that each meeting consists of the relevant classes of shareholders and/or creditors whose rights against the company are ‘not so dissimilar as to make it impossible for them to consult together with a view to their common interest.’ It is therefore right that shareholders and/or creditors with different rights against a Cayman scheme company should fall into separate classes; such rights may for example be employee incentive rights or interests arising as a result of the relevant shareholder being part of the management of the scheme company contrasted against the rights an ordinary shareholder might have against the same scheme company.

In the context of take private and management buy-out schemes, shareholders who are part of the management or bidding consortium (as appropriate) are highly unlikely to form a single class with independent minority shareholders. Therefore, even in the absence of the headcount test, if the minority shareholders do not vote to approve the Cayman scheme of arrangement, the scheme will not go before the Cayman Court for sanction and the management or bidding consortium are not able to cram-down independent minority shareholders.

Minority shareholders and/or creditors are protected by virtue of the classes formed under Cayman schemes as each class of shareholder and/or creditor must approve the proposed scheme at the scheme meetings in order for the sanction hearing to proceed otherwise the scheme of arrangement will fail.

This is in contrast to the position under US Chapter 11 proceedings, where a reorganisation plan can be confirmed in circumstances where there is a non-accepting class (subject to certain controls, such as the ‘absolute priority’ rule) with the effect of effecting a cross-class cram down. In Cayman Islands schemes of arrangement, there is no ability to cram down dissenting whole classes of shareholders and/or creditors (although it is possible to cram down dissenting creditors within a class).

Additionally, the value threshold for approving the Cayman scheme (being shareholders and/or creditors representing 75% in value of each class) is also higher than under other restructuring proceedings in other jurisdictions. For example, the applicable threshold for approval under US Chapter 11 proceedings a reorganisation plan is 66 2/3%.

Moreover, the Cayman Court has broad discretion to sanction (or not to sanction) a Cayman Islands scheme of arrangement notwithstanding that it has been approved by each class of shareholders and/or creditors. The Cayman Court retains discretion to refuse to sanction any Cayman scheme where there is (or may be) abuse of the minority and furthermore, may even impose conditions on its sanction of the Cayman Islands scheme of arrangement (for example, where it is concerned that the terms of the Cayman scheme are not in the best interests of the shareholders and/or creditors). As noted by Chadwick L.J. in Re Hawk Insurance, ‘the safeguard against minority oppression ... is that the court is not bound by the decision of the [scheme] meeting ...’ and the Cayman Court retains the

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13 Per Bowen L.J in Sovereign Life Assurance Co v Dodd [1892] 2 QB 573; and, in the Cayman Islands, In Re Euro Bank Corporation (In Liquidation) [2003] CLLR 205 adopting the test set out by the Hong Kong Court of Final Appeal in UDL Argos Engr. & Heavy Indus. Co. Ltd v Li Oi Lin. See also the recent Cayman Court case of Oceam Rig UDW Inc. & Others Cause No. FSD 100, 101, 102 and 103 of 2017 per Parker J at paragraph 44: ‘In every case the court will consider whether it is appropriate to convene class meetings and, if so, the composition of the classes so as to ensure that each meeting consists of the shareholders or creditors whose rights against the company which are to be released or varied under the scheme, or the new rights which the scheme gives in their place, are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.’

ultimate discretion as to whether or not to sanction the
Cayman scheme at the sanction or fairness hearing.

The Cayman Court’s approach to sanction was most
recently summarised by Parker J in *Re Ocean Rig UDW Inc.* as follows: the Cayman Court ‘should be slow to differ from the vote [of the scheme creditors] recognising that it is the creditors who are clearly the best judges of what is in their commercial interests’ but that ‘the [Cayman] court is not a rubber stamp ... [and] even where the scheme has the support of an overwhelming majority of the creditors ... the court can differ from the vote, but only if it is satisfied that an honest, intelligent and reasonable member of the class could not have voted for the scheme ...’

Furthermore, dissenting shareholders and/or creditors are further protected by Order 102, rule 20(10) which provides that all affected stakeholders (including any dissenting shareholders) have the right to attend the sanction hearing and have their objections to the Cayman scheme heard by the Cayman Court.

If the headcount test were to be abolished, the Cayman Court may need to take on a more active role in considering the commercial benefits of any Cayman Islands scheme of arrangement as it would not, necessarily, be appropriate to take a view that the majority decision is appropriate in all circumstances.

Furthermore, under Cayman Islands law any person who voted at the scheme meeting(s) or gave voting instructions to a custodian or clearing house to vote at the scheme meeting(s) is entitled to appear and be heard at the sanction hearing. 

This goes further to endorse the Cayman Court’s approach in *Little Sheep* where the majority in ensuring that any person with an economic interest in the relevant Cayman scheme has an opportunity to bring to the Cayman Court’s attention any issue relating to the Cayman scheme.

(3) The headcount test is not line with modern Cayman Islands company law policy/approach to voting.

In the context of shareholdings, Cayman Islands law historically required shareholder decisions to be made by way of numerosity and headcount approvals. However, modern law has moved away from this approach and provides that, subject to a Cayman company’s articles of association, the position in determining any shareholder decision is calculated on a ‘one share one vote’ basis (including, but not limited, to ordinary resolutions and special resolutions, and also, the approvals required for statutory mergers, the winding up of companies and capital regimes as set out under the Companies Law). From a policy perspective, it is not clear why Cayman Islands schemes of arrangement adopt a different approach. No similar comparison can be drawn for creditor decision-making.

(4) The headcount test does not reflect how shares/debt instruments are held in the modern context.

As noted above, whilst historically legal and beneficial interests were not divided, today nominees, custodians and trustees (or other financial institutions or vehicles) may hold debt instruments and intermediaries operating through clearing houses may hold uncertificated shares for a large number of beneficiaries. In many jurisdictions, each nominee, custodian, trustee or intermediary (as applicable) is either treated as a single head for the purposes of the headcount test, or is given a ‘yes’ and a ‘no’ vote which cancel each other out. Such an approach materially fails to reflect the number of persons and value of claims represented.

The Cayman Court’s more nuanced approach in *Little Sheep* sought to adopt a ‘middle ground’ (and in doing so, expressly acknowledged the limitations of the headcount test). However, the approach only goes so far – looking through a single layer of legal ownership to the custodian/nominee does not operate to ensure that votes accurately reflect the views of underlying beneficiaries – this will only count those who hold accounts directly with the relevant stock exchange clearing house, themselves often custodians or brokers who hold shares on account of others. If the Cayman Court were to require a company to look further through the register (that is, to definitively identify the ultimate beneficial owners of a company’s shares), this would place an impossible burden on companies seeking to effect a Cayman Islands scheme of arrangement. This is one of the reasons that, in almost every other shareholder decision context, Cayman Islands companies are only required to be concerned with their shareholders of record.

The Cayman approach has also been challenged on the following grounds: first, neither the chairman of the Cayman scheme meetings nor the Cayman Court is likely to be able to verify the validity of instructions. The approach requires the Cayman company, the chairman of the scheme meeting(s) and the Cayman Court to rely on the nominee for information as to how account holders have voted in connection with the Cayman scheme meeting. Generally, custodians will only provide details of the number of account holders who voted for or against the Cayman scheme, but will not be prepared to disclose copies of voting instructions. As such, it is not possible to independently verify the accuracy or
validity of the votes at the scheme meeting; second, it may be difficult to apply in practice. Looking further through the register to apply the headcount test may require scheme companies to have an impossible level of understanding and knowledge of the structures (and arrangements) in which debt or share instruments are held. It may also cause issues with overseas nominees/custodians who may not be willing to disclose the level of information required (in particular, in the context of listed companies); and third, it is inconsistent (in the context of shares) with the Cayman Islands law approach in determining ownership of shares that is, persons entered onto the register of shareholders being *prima facie* evidence of ownership.18

(5) The headcount test is at risk of manipulation.

Shareholders and/or creditors may split their relevant holding across multiple entities or persons in order to acquire a disproportionate level of influence on the Cayman scheme. This can be very difficult to detect – for example, an objecting party may not have access to the register of shareholders. It is also not clear how far the chairman of a scheme meeting must go to ensure that vote-splitting has not occurred (in such a way as to inappropriately affect the outcome of a scheme meeting).

In the case of notes, ‘splitting’ may be more difficult to achieve. However, the trading of notes until the voting record date is not unusual, it is perfectly acceptable for a particular creditor to seek to acquire a controlling stake in a particular class.

Approaches in other jurisdictions

In some jurisdictions (including New Zealand, Canada, India and South Africa) that have imported the scheme of arrangement from English law, a headcount test is not a requirement for the purposes of shareholders schemes. However, the headcount test (in some form) is incorporated for the purposes of creditor schemes in Singapore, Hong Kong, Australia, BVI, Bermuda and South Africa. We outline below the approach taken in certain jurisdictions which have adopted a modified approach to the headcount test.

**Hong Kong**

In Hong Kong, for takeover offers and general offers, the headcount test was replaced in 2014 by a 10% objection test, which requires the votes cast against a scheme of arrangement to not exceed 10% of the total voting rights attached to all disinterested shares.19 For all other arrangements or compromises, the headcount test is still required but the Hong Kong court has the discretion to dispense with the test.20

**Singapore**

In Singapore, which is a jurisdiction that has in recent years made a number of legal reforms in its bid to become a leading international debt restructuring centre, has also made certain changes to the headcount test for schemes of arrangement. In 2014, the Companies (Amendment) Act was passed in Singapore, modifying the language of the headcount test requirement, which now provides that while a ‘majority in number’ of creditors is required, this is now qualified by the caveat ‘unless the court orders otherwise’.21

**Australia**

Similarly, in Australia, the headcount test has been retained, but the court has discretion to dispense with it. In other words, a scheme must still be approved by 75% of the votes cast on the resolution, but the courts in Australia can order for the majority in numbers of shareholders test to be dispensed with.22

**New Zealand**

As for New Zealand, the judiciary has perhaps been the most radical in terms of the headcount test, which was abolished altogether in 1993. The legislation of New Zealand now does not set out a specific test for approving a scheme of arrangement, and instead the shareholders are only required to approve the proposed arrangement, amalgamation or compromise in such manner and on such terms as the court may specify.23 Although the headcount test was re-introduced in the context of certain listed entities by the 2014

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18 See Section 48 of the Companies Law (2018 Revision) and see also definition of ‘registered shareholder’.
19 Section 673 of the Companies Ordinance No. 28 of 2012.
20 Section 674 of the Companies Ordinance No. 28 of 2012.
21 Section 210 (3AB) of the Companies (Amendment) Act.
23 Section 236 of the Companies Act 1993.
amendment to the Companies Act\textsuperscript{24}, this statutory requirement only applied to ‘code companies’;\textsuperscript{25}

Time for reform?

\textit{England and Wales}

In England and Wales, the question of whether the headcount test should be abolished was twice considered by UK Parliament when preparing the Companies Act 2006. The Company Law Review Steering Group recommended that the headcount test be abolished noting that ‘the requirement for majorities in number as well as three-fourths in value has become irrelevant and burdensome, particularly in relation to shareholders and against the background of increasing use of nominees and possible artificial sub-division of nominal shareholdings to reach the requisite majority in number.’ Parliament however, elected to continue to include the headcount test in the English Companies Act 2006.

On the first attempt, Lord Goldsmith (in his capacity as Attorney General) stated that whilst the proposed changes (to remove the headcount test) ‘would facilitate schemes for companies and large creditors and [shareholders], [but] would do [so] at the expense of the interests of small minority [shareholders] and creditors [and that] therefore, the Government are not persuaded that the amendment strikes the right balance.’\textsuperscript{26} The second attempt was put forward on the basis that ‘the majority in number [test], focusing on a majority of registered holders is an anachronism, now that most retail holders hold through CREST nominees, where one registered holder may represent many thousands of beneficial owners. It is also open to abuse by shareholders who could subdivide their holding thought a number of nominee companies.’\textsuperscript{27} However, the proposal was again rejected this time, largely on the basis that the ‘theoretical possibility’\textsuperscript{28} of potential abuse through share splitting was an inadequate basis for removing the protection.

Given recent attempts at share splitting in \textit{Dee Valley}\textsuperscript{29} and the reported intention (pre-dating Brexit) for radical insolvency reform in England and Wales, the issue may once more be considered.

Conclusion

The Cayman Court’s ability to ‘look through’ the register of shareholders attempts to address the limitations of the headcount test in the context of modern share ownership structures (similar provisions do not apply in the context of creditor schemes).\textsuperscript{30} However, it is akin to going ‘down a rabbit hole’. Whilst arguably the ability to ‘look through’ the register seeks to uncover the intentions (for voting purposes) of those with the ultimate beneficial ownership of the Cayman scheme company’s shares, in reality it only reveals those parties holding accounts with the relevant stock exchange (i.e. custodians, clearing houses and brokers) who, in turn, hold the shares on behalf of others, who potentially may hold on behalf of others, and so on and so forth. Any attempt to look further through the register places the Cayman scheme company under an impossible burden: it would be impractical and unworkable to require the Cayman scheme company (or the chairman of the scheme meeting(s)) to follow each and every rabbit hole through the warren and definitively identify the ultimate beneficial owner of the relevant shares of a Cayman scheme company.

Nevertheless, the Cayman Court is clearly willing, ready and able to take steps to address the problematic issues of determining the intention of underlying beneficiaries (see in particular, the suggestion by Cresswell J in \textit{Alibaba} that the ‘look through’ be re-considered).\textsuperscript{31} The Cayman Court and the jurisdiction’s practitioners

Notes

\begin{itemize}
  \item \textsuperscript{24} Section 236A of the Companies Act 1993.
  \item \textsuperscript{25} Code companies being a listed issuer that has financial products that confer voting rights quoted on a licensed market, or has 50 or more shareholders and 50 or more share parcels (as defined by the Takeovers Act 1993).
  \item \textsuperscript{26} \textit{Per} Lord Goldsmith HL Deb 28 March 2006, GC326.
  \item \textsuperscript{27} HL Deb 16 May 2006, col. 217.
  \item \textsuperscript{28} \textit{Per} Lord Goldsmith HL Deb 16 May 2006, vol. 682, cols. 216-217.
  \item \textsuperscript{29} \textit{Re Dee Valley Group Plc} [2017] EWHC 184 (Ch) – In \textit{Dee Valley a minority stakeholder sought to manipulate the headcount test by using a share splitting strategy to defeat a scheme of arrangement. In that case, a disgruntled employee sought to derail a takeover scheme by transferring single shares to hundreds of people for the purpose of manipulating the ‘no’ votes against the scheme. The company, aware of the changes made, by reference to its company books, sought (and obtained) a court order enabling the chairman of the scheme meetings to reject the votes of any person who acquired shares from the disgruntled employee. See also \textit{Re PCCW Ltd} [2009] HKC 292, a similar case involving share-splitting in Hong Kong. In \textit{Re PCCW a controlling shareholder sought to manipulate the outcome of a takeover (by way of scheme of arrangement) by distributing shares to individuals who would vote in favour of the takeover scheme. The Hong Kong court was not satisfied that the vote was a true reflection of the shareholders’ will. The court disregarded (at the sanction stage) the votes of the shares subject to the share split and, as a result, the scheme failed. Note this decision pre-dates the changes to legislation detailed above.}
  \item \textsuperscript{30} The issues regarding the headcount test are less severe in the case of creditor schemes of arrangement given the accepted approach to treat the beneficial owners of debt as contingent creditors (and therefore entitled to vote in the scheme meeting in their own right).
  \item \textsuperscript{31} See for example, Cresswell J in \textit{Alibaba.com Ltd} Unreported, 20 April 2012 stated (in the context of the practice of ‘looking through the register’: ‘in light of my ruling of 20 April 2012 the opportunity might be taken (if thought appropriate) to confirm or re-consider Practice Direction 2 of 2010.’
\end{itemize}
are committed to ensuring that the laws and the practices adopted in the Cayman Islands reflect best practice and remain so.

A practical compromise would be to remove the headcount test for Cayman shareholder schemes of arrangement, given amongst other things, that the current approach is inconsistent with modern Cayman company law. Shareholders would continue to have sufficient protection through, amongst other things, the Cayman Court’s ultimate discretion to sanction Cayman schemes and the ability for affected shareholders to be heard at the sanction or fairness hearing.

In any event, the issues surrounding the headcount test in schemes of arrangement in the Cayman Islands are not insurmountable. The Cayman Islands scheme of arrangement remains a powerful, flexible and relevant restructuring tool: ensuring that a proper balance is struck between the effective compromise of claims and protection for both majority and minority stakeholders.
Soft Touch Provisional Liquidators in the BVI: Constellation Overseas Ltd, Pointing the Way

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Synopsis

In December 2018, the BVI Commercial Court appointed ‘soft touch’ provisional liquidators to Constellation Overseas Ltd, a BVI incorporated company, and five of its BVI incorporated subsidiaries (the ‘Companies’). Although the practice of appointing provisional liquidators to facilitate cross-border restructuring is well established elsewhere, this was the first occasion on which the BVI Court had made such an Order.

Prior to the Constellation decision, there had been a respectable body of practitioner opinion which held that the unique features of the BVI Insolvency Act 2003 (the ‘BVI Act’) excluded any jurisdiction to appoint provisional liquidators in such circumstances. Although the question as to the existence of the jurisdiction may have been answered in the Constellation decision, questions remain as to the limits of that jurisdiction and the circumstances in which the Court will consider it appropriate to exercise its discretion in favour of an appointment where the purpose is a restructuring. This article seeks to explore these questions and to propose answers to at least some of them.

As a starting point, we look at the factual background against which the applications in Constellation were made and the procedural factors material to the Court’s decision in that case. Against that factual background, we then turn to the legal framework within which the Court reached its decision in Constellation and seek to highlight how the Court dealt with certain legal points which arose in the case and which may arise in future cases on different facts. Lastly, we tentatively suggest some general conclusions which may be drawn from the case.

Background

The Companies were members of a group of companies (the ‘Group’) which had its operational headquarters in Brazil and which, together, carried on the business of offshore drilling for the oil and gas industry. Importantly, at the time of the BVI applications, the Group, and each of the Companies, was already the subject of a Brazilian Judicial Reorganisation (‘RJ’) the object of which was to facilitate the agreement and implementation of a plan for restructuring the Group’s debt. Each of the Companies continued to operate its business under the supervision of the First Business Court of Rio de Janeiro (‘the Brazilian Court’). The Companies considered, and submitted to the BVI Court, that Brazil was the proper forum for its restructuring. Certain companies within the Group, including the Companies, had also commenced proceedings in the US for protection under Chapter 15 of the US Bankruptcy Code seeking the recognition of the RJ as the ‘foreign main proceeding’ of each of the Chapter 15 Debtors. Accordingly, the Companies’ approach to the BVI Court was as ancillary support to the main proceeding in Brazil, facilitated by proceedings in other jurisdictions.

The BVI Court’s statutory jurisdiction to appoint a provisional liquidator arises only where an application for the appointment of a liquidator (called, for convenience in this Article, a ‘petition’) has been filed but not yet determined or withdrawn. In Constellation, each of the six Companies had filed its own petition with the BVI Court seeking the appointment of liquidators on the grounds of insolvency. The nature of the proceedings was therefore domestic: involving applications by BVI companies in which the BVI Court was invited to exercise a jurisdiction conferred upon it by a BVI statute within the context of pending BVI winding

Notes

1 Rosalind Nicholson and Rhonda Brown (Associate) represented Banco Bradesco S.A, the Group’s largest unsecured creditor, at the hearing of the Companies’ applications.
2 Re Constellation Overseas Ltd, Lone Star Offshore Ltd, Gold Star Equities Ltd, Olinda Star Ltd, Snover International Inc and Alpha Star Equities Ltd BVIHC(COM) 2018/0206, 0207, 0208, 02010 and 0212 referred to together as ‘Constellation’.
3 There had been an unreported case in which the BVI Court had declined to make such an appointment – Re Transfield ER Cape Limited BVIHC(COM) 2010/121 (unreported) – further discussed below.
4 S.170(1) of the BVI Act.
5 Under s.162(1)(a) of the BVI Act.
up proceedings in respect of those BVI incorporated companies.

The orders sought from the BVI Court had as their purpose the facilitation of the restructuring of the Companies’ debts while they continued to operate as a going concern. The Companies’ applications for the appointment of the provisional liquidators were supported by creditors holding over US$1 billion of the companies’ debts of US$1.5 billion. The support of a 50% majority of creditors was required to secure the success of the RJ. Accordingly, the Court was able to be satisfied that the restructuring enjoyed reasonable prospects of success.

The Court was also satisfied on the evidence put before it that, whilst the Companies were balance sheet solvent, in the absence of a restructuring, they had insufficient cash to meet forthcoming financial debt obligations and that default on those obligations would trigger additional defaults as a result of cross-default provisions in other financial instruments to which the Companies were party.

In addition, the evidence showed that the realisation of the Group’s assets on a going concern basis was significantly better than on a breakup basis. Accordingly, the Court was satisfied that the appointment of the provisional liquidators to the Companies for the purpose proposed, namely maintaining the going concern value whilst facilitating a restructuring, was liable to maintain the value of the assets for the benefit of their creditors as a whole and, accordingly, that its discretion to make such an appointment was engaged.

As part of the RJ process, proceedings and the enforcement of claims against debtors, including the Companies, had been stayed by the Brazilian Court. Similarly, in the Chapter 15 proceedings, the Companies’ objective was to obtain a stay barring the commencement or continuation of actions against them or their assets. The BVI Act provides for a moratorium on enforcement by creditors only after the point at which the Court makes an order for the company to be wound-up and there is no provision in the BVI Act to protect the company against execution by creditors between the date on which a winding up petition is filed and the date of the winding up order. This means that the appointment of provisional liquidators does not, without more, prevent creditors from executing against the company. However, the BVI Court does have power to stay or restrain Court proceedings pending before the BVI Courts or on appeal from those Courts. Although the Companies were aware of only one, non-material claim, pending in the BVI, on Constellation the Court was invited to, and did, make an order staying such proceedings.

We now turn to the legal framework within which the Court reached its decision in Constellation.

### Power to appoint provisional liquidators

Section 170(4) of the BVI Act confers jurisdiction on the Court to appoint provisional liquidators on ‘such terms as it considers fit’, if an application for the appointment of a liquidator of a company has been filed but not yet determined or withdrawn and:

‘(a) the company, in respect of which the application to appoint a liquidator has been made, consents; or
(b) the Court is satisfied that the appointment of a provisional liquidator
   (i) is necessary for the purpose of maintaining the value of assets owned or managed by the company, or
   (ii) is in the public interest.’

Although, in Constellation, the Companies were themselves were the applicants for an Order appointing liquidators, the power to appoint provisional liquidators is not confined to such a case and arises equally where the applicant is a creditor or a member of the company concerned. The company’s consent is, however, relevant to the application to appoint the provisional liquidators. The consent requirement is clearly satisfied where the company is the applicant (as was the case in both Transfield and Constellation) or where the company confirms its consent to the Court. In such a case, English authority suggests that ‘the appointment is almost a matter of course...’. However, although the two conditions are expressed as alternatives, in practice, the BVI Court has required to be satisfied as to the second limb whether or not the company in fact consents in considering the exercise of its discretion.

Ordinarily, and familiarly, the BVI Court has been accustomed to appoint provisional liquidators where there are allegations of wrongdoing within a company or where steps have to be taken to preserve assets in the face of an imminent threat to their value. However, as the Applicants submitted in Constellation, and the Court accepted, these are not the only circumstances in which
an appointment may be made: the Court has a broad and flexible power to make such an appointment.9

The BVI Court in Constellation concluded that its power to appoint provisional liquidators was one which extends to circumstances where there is a need to protect the company’s assets from creditors pending a restructuring.10 There had been some doubt whether this was the case as a matter of BVI law: Part III of the BVI Act includes provision for the appointment of administrators, similar in material respects to the administration provisions of the English Insolvency Act 1986, whereby a company can be reorganised, restructured or have its assets realised under an Administrator with the protection of a statutory moratorium. Part III has never been (and it is thought unlikely that it will be) brought into force. Prior to the Constellation decision, the fact that the BVI Legislature had enacted, but not brought the administration provisions into force, was taken by some to be an indicator that in enacting the provisions of the BVI Act which allow for the appointment of provisional liquidators, the legislature could not have intended that they be used as a framework for a debtor in possession restructuring.

The BVI Court did not deal with this point directly in its judgment in Constellation. However, it apparently accepted the Companies’ submission by analogy to the judgment of Harman J in Re Anglo American Insurance Co Ltd,11 as applied by Smellie CJ in the Cayman case Re Fruit of the Loom Ltd [2000] CILR Note 7b, to the effect that where there are in force no specific statutory provisions which would enable the Court to appoint an administrator in respect of the particular company, then it was open to the Court to use the broad powers conferred upon it to appoint provisional liquidators.

The question of necessity

The burden of establishing that the appointment of provisional liquidators is necessary for the purpose of maintaining the value of assets owned or managed by the company falls on the applicant. However, the test of ‘necessity’ for this purpose, does not require that it is shown that the proposed restructuring will succeed. Rather, the requirement is that the restructuring has a ‘real prospect’ of success and that the proposed appointment will serve the purpose of maintaining the value of the assets in the meantime.12

In Constellation, the Companies had the advantage of the support of a substantial majority of their creditors. In circumstances where the success of the RJ required the support of a simple majority of creditors, the Companies were therefore readily able to satisfy the Court as to the prospects of the restructuring meeting with success. However, although the Court will consider the view reached by the directors of the company itself as to the likelihood of the restructuring succeeding,13 in the absence of evidence of majority creditor support, it is not clear what will be required in order to satisfy the Court as to the ‘real prospect’ of the restructuring succeeding. In particular, it is not clear whether and to what extent restructuring proposals must have been advanced before the Court will be prepared to conclude that the restructuring has sufficient prospects of success.

Ordinarily, one would expect the Company to have been in negotiations with creditors before the point had been reached where the application had been made and the assumption would be that creditor support had reached a critical mass before the company approached the Court – not least because of the absence of a statutory moratorium on presentation of a petition under BVI law (as discussed further below). That being the case, it is fair to assume the BVI Court may be reluctant to appoint provisional liquidators for the purpose of a restructuring if the company is unable to point to any creditor support, but whether minority support would suffice or whether the support of different classes of creditor might be required on another case remains to be determined.

No moratorium

The BVI Act provides for a moratorium on enforcement by creditors only after the point at which the Court makes an order for the company to be wound-up. There is no provision in the BVI Act to protect the company against execution by creditors between the date on which a petition is filed and the date of the winding up order. The only power which the Court has is to stay or restrain Court proceedings pending before the BVI Courts or on appeal from those Courts. In other words, the appointment of a provisional liquidator would not, without more, prevent creditors from executing against the company. Since the appointment of provisional liquidators is intended as a protective measure, the question therefore arises whether, in the absence of a general moratorium, the appointment could meet its objective.

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9 See, for example, Rimer LJ in Revenue & Customs Commissioners v Rochdale Drinks Distributors Ltd [2011] EWCA Civ 1116, [2012] STC 186, [2012] 1 BCLC 748.
11 [1994] 1 BCLC 649
12 See paragraph 86 of the Constellation judgment.
In Transfield, there were various proceedings pending against the company in jurisdictions outside the BVI. The Court was not satisfied that in the absence of a blanket moratorium, provisional liquidators, if appointed, would be in any better position to secure a stay of those proceedings than the directors would be. It could not, therefore, conclude that the appointment of provisional liquidators was necessary for the purpose of maintaining the value of assets owned or managed by the company.

In Constellation, the Companies were able to point to the moratorium effected as part of the RJ process and to the moratorium within the Chapter 15 proceedings. The Companies did not rely, therefore, on the limited moratorium available to them under an Order of the BVI Court.

This is a potentially important point. Because of the particular facts of Constellation, in particular the fact that the application to the BVI Court was made against the background of an existing moratorium imposed under the RJ, the absence of an automatic moratorium in the BVI proceedings was not an issue. However, it may be that in another case, in particular one where there are pressing creditor claims outside the BVI and no pre-existing or prospective moratorium affecting those claims, the BVI Court would consider the absence of a moratorium a critical point of difference. In such a case, it is not clear whether, absent special circumstances, the BVI Court would conclude that the appointment of the provisional liquidators was ‘necessary for the purpose of maintaining the value’ of the company’s assets or, indeed, that a restructuring had real prospects of succeeding.

**Time limits under the BVI Act**

A further consideration is the fact that, uniquely, the BVI Act requires that a winding up petition be determined within six months of filing. Since the appointment of a ‘soft touch’ provisional liquidator necessarily occurs in the context of an existing winding up petition and the legislation clearly assumes that that petition will be determined within a short period of time, the concern was that this allowed little scope for an extended restructuring under the supervision of a provisional liquidator which might take years to effect an outcome. This was one of the factors which had led the BVI Court to reject an application to appoint soft touch provisional liquidators in the earlier case of Transfield. In Transfield, the Judge was concerned that he was being asked to make an open-ended appointment with the proposed restructuring scheduled to take three years, a position which he considered apparently incompatible with the scheme of the BVI Act.

In Constellation, the specific concern with respect to the abbreviated timescale which the BVI Act contemplates was dealt with by reference to case law in other jurisdictions which recognises the reality that companies which enter provisional liquidation for the purposes of a restructuring will often ultimately not go into liquidation at all: indeed, the objective is that they should not need to go into liquidation. That being the case, it cannot be said that it is a condition precedent for the appointment of provisional liquidators for the purposes of a restructuring that the company concerned will ultimately be wound up. The Judge in Constellation accepted this proposition. He also observed, as is the case, that there is no limitation on the number of times that the Court may extend the initial six month period provided that at the time of the application, the Court is satisfied that special circumstances exist for it to grant such an extension.

It must follow from this line of argument that it is not necessary to show that restructuring plans are so advanced or of such a nature that they can be implemented within a very short timescale. Having said that, for the reasons already given, a mere inchoate hope that a restructuring might occur, as distinct from a proposal, even in outline, which has achieved sufficient form to allow negotiations with creditors to commence, may very well not impress a Court invited to appoint provisional liquidators although that too remains to be seen.

**Part XVIII, common law and comity**

The last point which it is useful to make with regard to the Constellation decision concerns the way in which the Court dealt with the question of Part XVIII of the BVI Act. Part XVIII, which like Part III has never been brought into force, provides a statutory scheme allowing the BVI Court to provide assistance and cooperation in cases of cross-border insolvency, including recognition of foreign main proceedings. If brought into force, Part XVIII would incorporate into BVI law the provisions of the UNCITRAL Model Law on Cross-border Insolvency. In Re C (BVIHC (COM) 0080 of 2013) the BVI Court itself (Bannister J) had held that the common law power to assist representatives from territories which were not designated under Part XIX of the BVI Act had been impliedly excluded by the BVI
Act as inconsistent with the statutory scheme in Parts XVIII and XIX of the Act.

The issue which presented itself to the Court in Constellation was whether, against the statutory background coupled with its own decision in Re C, there could subsist jurisdiction either under the BVI Act itself or at common law to appoint provisional liquidators in support of foreign main proceedings. Indeed, the first question which the Court raised in Constellation was whether, in effect, the application before it was an attempt to obtain by the back door relief which was not available to it by virtue of the fact that Part XVIII is not in force.

In any event, the BVI Court was persuaded that Part XVIII was not in point. Part XVIII is predicated on the recognition by the BVI Court of a foreign insolvency proceeding. By contrast, the jurisdiction invoked in Constellation was entirely domestic in nature: the BVI Court was invited to exercise a jurisdiction conferred upon it by existing provisions of a BVI statute, within the context of a pending BVI winding up proceedings in respect of BVI incorporated companies.

For the same reason, the BVI Court was satisfied that Re C could be distinguished: in that case, the foreign representatives were seeking to invoke the BVI Court’s powers as conferred by Part XIX of the BVI Act and, by way of addition, its common law powers in respect of a foreign insolvency proceeding. Accordingly, Re C was not authority for the proposition that the BVI Act had excluded by implication the common law power to assist a foreign court which, under principles of comity, are of general application.

To this consideration was added the fact in May 2017, the BVI Court had adopted the Guidelines for Communication and Cooperation between Courts in Cross-Border Insolvency Matters, as formulated by the Judicial Insolvency Network. Those guidelines specify that:

‘The overarching objective of these Guidelines is to improve in the interests of all stakeholders the efficiency and effectiveness of cross-border proceedings relating to insolvency or adjustment of debt opened in more than one jurisdiction (“Parallel Proceedings”) by enhancing coordination and cooperation amongst courts under whose supervision such proceedings are being conducted’.

This reflects and acknowledges the broader common law principle, which is part of BVI law, which requires that courts should do all in their own power under their own law to provide assistance to a foreign court (without importing other laws to enable them to do so). It is apparent that the fact that the Court was thereby affording comity or cross-border co-operation to a restructuring attempt in another jurisdiction played a role in supporting the exercise of the Court’s discretion. Accordingly, and, subject to the question of the moratorium as discussed above, the BVI Court clearly has jurisdiction in principle to make an appointment in an appropriate case whether or not there are existing foreign insolvency proceedings on foot.

Conclusion

Constellation is the first case of its type in the BVI and it remains to be seen how precisely the Court will be prepared to exercise its jurisdiction in subsequent cases. However, with the door ajar, we suggest that some principles of general application can be drawn from the decision which may be developed as time goes on. Our suggestions are the following:

a) Although in Constellation the petitions were those of the Companies themselves, this is not a condition to the appointment of ‘soft touch’ provisional liquidators nor is it a requirement that it should be the company itself which applies for the appointment of the provisional liquidators. The Company’s consent will, however, improve the prospects of an order being made and, although not strictly required, given the purpose for which the provisional liquidators are proposed to be a restructuring of the company’s liabilities, it would be an exceptional case were the company itself not to consent. Indeed, in the absence of consent, there must be a question whether the Court could be satisfied that there was a ‘real prospect’ of the restructuring succeeding.

b) In principle, there is no reason in principle why ‘soft touch’ provisional liquidators may not be appointed on an application by the company within the context of a creditors’ petition. Nor is it necessary that the petitioning creditor must support the application. However, if that creditor opposes, or is not supportive of the proposed restructuring, and the company is unable to point to significant

Notes

16 Part XIX of the BVI Act provides for the making of Orders in aid of foreign proceedings. The Part XIX powers are confined to proceedings in specific designated jurisdictions which do not include Brazil.
17 See paragraphs 6-9 of the judgment.
18 Practice Direction No 2 of 2017.
20 See paragraph 89 of the Constellation judgment.
third-party creditor support, then, again, there must be a question whether the Court can conclude that the appointment of provisional liquidators is necessary or the restructuring is liable to succeed.

c) Where the applicant is able to point to substantial creditor support, particularly where that creditor support represents a majority of relevant creditors, then the BVI Court is likely – though not, of course, bound – to accede to an application to appoint provisional liquidators to facilitate a restructuring. It may not be necessary to demonstrate that the supporting creditors represent a majority, however, and it is always open to the Court to appoint provisional liquidators for a limited period to allow the applicant to canvas additional support. Whether the support of different classes of creditor might be required on another case remains to be seen.

d) The Court must be satisfied that the appointment of provisional liquidators to the Companies for the purpose proposed, namely maintaining the going concern value whilst facilitating a restructuring, is liable to maintain the value of the assets for the benefit of their creditors as a whole. Evidence that the realisation of the company’s assets on a going concern basis is significantly better than on a breakup basis will go some way to establishing that. However, the absence of a general moratorium under BVI law needs also to be taken into account. In the absence of a general moratorium, it is not clear that in a case where there are pressing creditor claims outside the BVI and no pre-existing or prospective moratorium which would stay those claims the BVI Court would conclude that the appointment of the provisional liquidators would be capable of maintaining the value of the company’s assets or, indeed, that a restructuring has real prospects of succeeding.

e) It is not necessary for an applicant to show that restructuring plans are so advanced or of such a nature that they can be implemented within a very short timescale. However, it is likely that something more than a mere hope that a restructuring might occur will be required, not least because the BVI Court is likely to need be satisfied that there is at least some creditor support in order to conclude that a restructuring has some prospect of being successful.

We look forward to seeing whether and how these general principles are applied as the jurisprudence in the BVI develops.
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