

# Cayman Islands

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## **1. The legal framework and the effectiveness of court processes/legal remedies**

### **1.1 Describe the nature and effectiveness of the following processes:**

#### **(a) Debt recovery remedies where the creditor has no security**

Where the creditor has no security, the only way of obtaining payment of the debt without recourse to the court is through negotiations with the debtor, possibly with the assistance of attorneys. If this is unsuccessful, creditors must commence a debt action to recover the debt and obtain a judgment. A judgment or order for the payment of money may be enforced by one or more of the following means:

- issuing a writ of *feri facias* directing the bailiff of the Grand Court to levy execution on the judgment debtor's personal goods and chattels;
- obtaining a garnishee order requiring any debtor of the judgment debtor to pay that debt to the judgment creditor;
- obtaining a charging order on the judgment debtor's beneficial interest in any property;
- applying for the appointment of a receiver to receive income due to the judgment debtor from, for example, renting out property;
- applying for an order for committal of the judgment debtor to prison for breach of the judgment or order for the payment of money;
- issuing a writ of sequestration to obtain an order sequestering certain specified assets to be applied to pay the debt. The assets can be sold only pursuant to a further order of the court for their sale and the proceeds of sale are then applied by the court to discharge the judgment debtor's liability; or
- obtaining an attachment of earnings order directing the judgment debtor's employer to all or part of the debtor's wages to the judgment creditor until the judgment is satisfied.

A creditor may at any time, either before or after judgment, present a petition in bankruptcy against an individual or for the winding-up of a company on the grounds of the debtor's inability to pay its debts.

Ancillary to formal debt recovery, a creditor may ask the court to grant an injunction, known as a Mareva injunction, to restrain the debtor from dissipating its assets.

The effectiveness of all these procedures to achieve payment of the debt is dependent upon the debtor having assets in the first place

#### **(b) The enforcement of security**

Mortgages and legal charges over property are enforced usually by sale or through foreclosure; the appointment of a receiver of rents is also possible. Mortgages over chattels are generally enforced by sale.

Debentures are normally enforced by the appointment of a receiver/manager.

The effectiveness of the enforcement of security depends upon the value of the security held and the market for the secured assets at the time of enforcement.

#### **(c) Corporate bankruptcy/liquidation processes**

Corporate creditors are in the same position as individual creditors. Any creditor is entitled to present a petition to wind up a corporate debtor on the ground that it is unable to pay its debts. A company is deemed to be unable to pay its debts if:

- it has neglected to pay, to secure or to compound to the satisfaction of the creditor a debt due in excess of CI\$100 within three weeks of being served at its registered office with a statutory demand for payment of the debt due;
- an execution or other process issued on a judgment, decree or order obtained in the court in favour of the creditor has been returned unsatisfied in whole or part; or
- it is proved to the satisfaction of the court that the company is unable to pay its debts.

As winding-up is effectively a class remedy, it is not necessarily an efficient way for any particular creditor to obtain payment in full or in priority to other creditors.

#### **(d) Formal corporate rescue processes**

Pursuant to Section 86 of the Companies Law (2007 revision), a company and its creditors can enter into a scheme of arrangement. A scheme becomes binding on scheme creditors when:

- a majority in number of those voting, representing at least three-quarters in value of those voting in each class of scheme creditors, vote in person or by proxy in favour of the scheme at a specially convened meeting;
- the Cayman court subsequently makes an order approving the scheme; and
- subject to any other condition precedent in the scheme, a copy of that order is delivered to the registrar of companies for registration.

By its nature, a scheme usually predicts a better outcome for creditors than a winding-up. However, the effectiveness of a scheme is dependent upon the company being able to comply with the terms of the scheme as approved.

In the event that the scheme fails due to a

breach of its terms, formal winding-up generally follows and existing assets of the scheme become available to the liquidator for collection and distribution on a *pari passu* basis among all creditors, including those formerly bound by the scheme.

#### **(e) Informal corporate rescue processes**

A company can always enter into negotiations with its creditors in the hope of agreeing a voluntary compromise which can be made binding by the execution of a deed of arrangement between the company and the relevant creditors, but only if all the creditors affected expressly agree.

#### **1.2 What are the formal processes to effect a liquidation of the company's assets?**

The principal statute governing corporate recovery and insolvency is the Cayman Islands Companies Law. The corporate recovery and winding-up regimes are found in Part 5 of the law. They are:

- provisional liquidation (used where there is a risk of dissipation of assets prior to the hearing of a winding-up petition);
- members' voluntary winding-up;
- compulsory winding-up; and
- winding-up subject to the supervision of the Grand Court.

The English Insolvency Rules are adopted in the Cayman Islands save insofar as they are inconsistent with the Companies Law.

In the Cayman Islands, there is no concept of a creditors' winding-up. Instead, it is usual for an insolvent voluntary winding-up to be taken under the supervision of the Grand Court.

**Provisional liquidation:** Provisional liquidators are usually appointed to preserve the assets of a company following presentation of a petition and pending the making of a winding-up order. However, the Cayman Islands court will appoint provisional liquidators to oversee the affairs of a company during its attempts to refinance and/or reorganise itself so as to continue as a going concern. When appointing the provisional liquidators, the court will order a stay of proceedings against the company to protect the company from its creditors and allow it to explore a refinancing and/or reorganisation.

Provisional liquidators oversee the actions of the directors and review objectively whether the

company's attempts to refinance and reorganise itself as a going concern have a realistic prospect of success and are in the interests of the creditors.

**Voluntary winding-up:** Creditors of a company cannot instigate a voluntary winding-up.

**Compulsory winding-up:** Creditors, but not contingent creditors, have standing to present a winding-up petition in the Cayman Islands. Upon the making of a winding-up order, the winding-up is deemed to commence as of the date of presentation of the winding-up petition. Unless the court otherwise directs, any disposition of the company's property from that time is void *ab initio*.

In Cayman, it is usual for the petitioner to recommend to the court its choice of liquidator(s) – generally two persons acting jointly and severally. These normally are Cayman residents who are either partners in or senior representatives of local firms of accountants.

The grounds for winding up a company in the Cayman Islands are set out in the Companies Law:

- The company has passed a special resolution requiring the company to be wound up by the court;
- The company does not commence its business within a year of incorporation or suspends its business for a whole year;
- The company is unable to pay its debts (the balance-sheet test is actual assets versus actual liabilities – contingent assets and liabilities play no part); and
- The court is of the opinion that it is just and equitable that the company should be wound up.

**Winding-up subject to the supervision of the Grand Court:** Under the Companies Law, where a resolution has been passed by the company for its voluntary winding-up, upon application of the liquidator the court may make an order directing that the voluntary winding-up should continue subject to the supervision of the Grand Court. The effect of such an order is to convert the voluntary winding-up into what is effectively a compulsory winding-up, with the voluntary liquidator having the same powers as an official liquidator.

### **1.3 What is the effect on debt collection and the enforcement of security of:**

#### **(a) An adjudication of corporate bankruptcy/liquidation?**

In a winding-up by the court, all dispositions of the property, effects and things in action of the company made between the commencement of the winding-up and the order for winding-up are void, unless the court otherwise orders. The making of a winding-up order has no effect upon the rights of secured creditors to enforce their security. Secured creditors can enforce their security and still prove in the liquidation for any shortfall. Alternatively, secured creditors can abandon their security for the benefit of the general body of unsecured creditors and prove for their entire debt.

#### **(b) The commencement of a formal corporate rescue process?**

As outlined in section 1.1(d) above, a scheme of arrangement is the only formal corporate rescue process provided for in the Cayman Islands. Pursuant to Section 86 of the Companies Law, a scheme of arrangement does not become binding on creditors of the company until a scheme meeting has been held, the statutory voting requirements have been met and the Cayman court has made an order approving the scheme. Until this time, it is open to any creditor of the company to issue proceedings seeking the recovery of any debt owed by the company or to take steps to enforce any security held.

A company taking steps to prepare and enter into a scheme of arrangement with its creditors does not prevent a creditor from taking steps to collect a debt owed by the company or seeking the enforcement of security until that scheme becomes binding. Section 99 of the Companies Law gives the Grand Court the option of restraining further proceedings against a company upon the presentation of a petition for the winding-up of the company. Therefore, prior to making an application under Section 86 for orders relating to a scheme meeting, a company can present a petition for its winding-up and avail itself of the court's power to grant an injunction pursuant to Section 99.

#### **(c) The initiation of an informal corporate rescue process?**

The initiation of an informal corporate rescue process does not prevent a creditor from initiating proceedings against a company seeking the recovery of a debt or taking steps to enforce security.

**1.4 Are insolvency procedures involving a corporation incorporated in your jurisdiction recognised if they are started in another jurisdiction? In particular, what would be the impact of US bankruptcy proceedings being commenced?**

The Cayman court considers itself to have universal jurisdiction to deal with the affairs of a Cayman incorporated company. It would consider bankruptcy proceedings in any other jurisdiction to be ancillary to any proceedings in the Cayman Islands. US bankruptcy proceedings could not lead to the dissolution of a Cayman company, even if all the company's assets and all the company's creditors were dealt with in those proceedings. At the conclusion of the US bankruptcy proceedings, the company would remain in existence and on the Register of Companies in the Cayman Islands.

Creditors whose debts have been discharged under the terms of any plan of reorganisation pursuant to a Chapter 11 proceeding in the United States will not have standing to petition the Cayman court for a local liquidation if:

- the plan of reorganisation has been successfully concluded and therefore the debts of the creditors bound by the plan are deemed to have been discharged; and
- the substantive obligation has been discharged according to the law by which it was governed as a result of the conclusion of the plan.

**1.5 In what circumstances would the directors or officers of a company in financial difficulties face potential personal liability for continuing to trade? In practice, are any such provisions actually enforced?**

There are no wrongful trading provisions within the Cayman law. However, directors causing a company to continue to trade once they are aware that the company is in financial difficulty are potentially exposing themselves to personal liability if they are acting in breach of their fiduciary duties to the company. Claims against directors for breach of fiduciary duty are not commonplace in Cayman, but are regularly brought by liquidators against overseas directors.

**2. What are the advantages and disadvantages of triggering a formal insolvency or corporate rescue procedure?**

The advantage for creditors of triggering a formal

procedure is that an independent third party can be appointed immediately as a provisional liquidator pending the approval of a scheme of arrangement or the making of a winding-up order which facilitates the protection of assets and enhances the creditors' ability to find out about the true financial position of the company.

**3. What are the practical options for out-of-court restructuring?**

The only option is through negotiation with the aim of reaching agreed, and perhaps separately tailored, compromises. This has the advantage of avoiding court and other professional costs associated with a court-assisted restructuring. It also provides additional flexibility when dealing with creditors having specific requirements.

One major disadvantage is that it is generally necessary to reach a compromise with all creditors to avoid winding-up proceedings from even a small minority of dissatisfied creditors.

**4. What is the effect on the management of a company of:**

**4.1 An adjudication of corporate bankruptcy/liquidation?**

On the making of a winding-up order, the court will appoint a liquidator to take control of the company and its assets and act in the winding up of its affairs. Upon his appointment, the powers of the directors are automatically transferred to the liquidator. Accordingly, the appointment of a liquidator deprives the directors of their powers and they no longer have authority to act on behalf of the company.

**4.2 The commencement of a formal corporate rescue process?**

The presentation of a petition for the court's approval of a compromise or arrangement proposed between a company and its creditors or any class of them has no effect upon the management of the company.

If a petition for the winding-up of the company is presented and a provisional liquidator appointed to procure the benefit of a moratorium while the compromise or arrangement is being negotiated, considered and approved by the creditors, the directors' powers are transferred to the provisional liquidator upon his appointment and the directors cease to have authority to act on behalf of the

company unless the court orders that they may do so subject to the overall supervision of the provisional liquidator.

#### **4.3 The initiation of an informal corporate rescue process?**

The initiation of an out-of-court, non-statutory, corporate rescue process has no effect upon the management of a company.

### **5. Parties in interest/key players**

#### **5.1 Who is responsible for the 'case management' control and administration of a corporate bankruptcy/liquidation, a formal rescue and an informal rescue?**

The liquidator takes control of the company's affairs upon his appointment on the making of a winding-up order. The liquidator is subject to control by the court.

The company, through its directors, will have control if the arrangement or restructuring is not proposed in the context of a provisional liquidation. If a provisional liquidator is appointed, he will work with the company and the process will ultimately be subject to the supervision of the court.

Responsibility for the administration of the arrangement or restructuring, once binding, will rest with those nominated by the scheme documentation.

In an informal rescue process the company's board of directors will act on behalf of the company.

#### **5.2 Who is responsible for preparing the restructuring plan in a formal or informal rescue?**

Usually the company, in relevant cases assisted by any liquidator(s) appointed, draws up a proposal which it then puts to its creditors. The company may seek assistance from any creditors' committee that may exist and consult with creditors, shareholders and other financial institutions or professionals.

#### **5.3 Who are the key players? What are their roles and responsibilities?**

In a liquidation the key player is the liquidator, who is responsible for collecting in and distributing the company's assets and winding up the company's affairs.

The key players in a scheme of arrangement

will usually be nominated by the scheme itself, which will set out in detail their respective roles and responsibilities. In an informal rescue procedure the directors will play a key role, but other parties nominated by them or by the creditors or other interested parties, such as lenders, may also have key roles.

### **6. What financial information is available to creditors?**

In a liquidation, creditors are provided with financial information by the liquidator in the form of reports to the general body of creditors. Such information generally includes:

- extracts from previous audited/unaudited financial statements;
- a statement of affairs as at the date of the appointment of liquidators, including realisable value estimates of existing assets; and
- calculations of anticipated dividends.

Although no specific requirements are laid down in Cayman law, in a scheme of arrangement financial information provided within the scheme proposal document is similar to that applicable in a liquidation. A scheme proposal document will usually also include a comparison section comparing recoveries under the scheme and in a liquidation.

In the case of an informal rescue, financial information is provided purely at the company's discretion.

### **7. Common questions**

#### **7.1 Funding and the priority given to new money**

##### **(a) If an insolvent corporation requires urgent working capital funding, what difficulties are likely to be encountered in the provision of such funding?**

If the funding is provided by way of a loan, rather than as an injection of capital, it may be difficult for security to be given to the provider of the funding as any such security may be vulnerable to attack as a preference. It can be difficult to challenge the giving of security for funds provided in the hope of rescuing the company if it cannot be shown that the motive was other than genuine and, even if it fails, the funds were actually applied for that genuine purpose.

**(b) Are lenders providing new money, or debtor-in-possession financing, given any statutory priority?**

Lenders providing new money and/or debtor-in-possession financing are not given statutory priority. Priority can be obtained only through the granting of security.

**7.2 Ranking of creditors****In what order are creditors paid in a corporate bankruptcy/liquidation?**

Payments are made in the following order:

- fees and expenses of the liquidation, which may include reimbursement of any 'funds' provided by a third party subsequent to the appointment of a liquidator for the initiation or furtherance of recovery litigation or asset realisation;
- fees and expenses properly incurred by the liquidator in winding up the company, including all disbursements and the remuneration of the liquidator's employees;
- taxed costs of the petition;
- *pari passu*:
  - all rates, taxes, assessments or impositions imposed or made under any law applicable to the Cayman Islands and having become due and payable in the 12 months before the relevant date;
  - all wages and salaries of any clerk or servant not exceeding CI\$100 in respect of services rendered to the company in the four months before the relevant date; and
  - all wages of any workman or labourer not exceeding CI\$50 in respect of services rendered to the company in the two months before the relevant date;
- money due to depositors who have deposits with a company which is being wound up and which is incorporated in the islands and holds an 'A' licence issued under the Banks and Trusts Companies Law (2003 revision), subject to certain statutory conditions, provisions and limits; and
- unsecured claims.

In relation to the above, the 'relevant date' means:

- as regards a company ordered to be wound up compulsorily which has not previously commenced to be wound up voluntarily, the

date of the winding-up order; and

- in any other case, the date of commencement of the winding-up.

**7.3 Avoidance of antecedent transactions****Are there any legal provisions that might operate to invalidate the creation of security, the disposal of an asset or the payment of a creditor by a company in financial difficulties?**

Any conveyance, mortgage, delivery of goods, payment, execution or other act relating to property which is deemed a fraudulent preference or a fraudulent conveyance, assignment, transfer of sale or disposition shall be invalid in the event of a company's winding-up.

**7.4 'Cram-downs'****What is the position of both unsecured and secured creditors that vote against, do not agree with or do not consent to either a formal or an informal rescue plan?**

All creditors, whether secured or unsecured, will be bound by a scheme of arrangement if they were scheme creditors and the necessary statutory majorities were obtained at the relevant scheme meetings and the scheme is approved by the court, regardless of how they voted.

Agreement to an informal rescue plan must be unanimous among those creditors whose rights will be affected by the proposal.

**7.5 Creditor protection****What actions can creditors take if they are not satisfied with the conduct of either a formal rescue procedure or a corporate bankruptcy/liquidation?**

If creditors are not satisfied with the conduct of a winding-up, they can ask the court to give directions to the liquidator. The court may direct that meetings of creditors be summoned, held and conducted in such manner as the court directs for the purposes of ascertaining their wishes, and may appoint a chairperson for that meeting for the purpose of directing that person to prepare a report to the court. In some circumstances the creditors can seek to have the liquidator removed by the court and replaced with their own nominee.