



Leave for Cayman derivative actions – international or domestic only?

Overview

The rules of court in the Cayman Islands control shareholders' entitlement to issue proceedings in the name of their company. A recent decision of the Appellate Division of the New York Supreme Court has confirmed that any derivative proceeding issued in New York on behalf of a Cayman-incorporated company without the prior approval of the Cayman court will be dismissed for lack of standing.

The Cayman Grand Court Rules do not expressly deal with the grant of leave to issue derivative proceedings in other jurisdictions, nor has that question been addressed in any reported decision of the Cayman courts. This recent decision of the New York Appellate Division therefore raises a key question: is it possible to obtain approval from the Grand Court of the Cayman Islands to bring derivative proceedings in New York or any other jurisdiction?

Facts of the case

The Plaintiff, Paul Davis, was a significant minority shareholder of a Cayman-incorporated company, Scottish Re Group Limited (the **Company**) who brought proceedings in New York against the Company, its US subsidiary, majority shareholders and directors (the **Investors**). He alleged, amongst other things, that the Investors influenced the Company's Board of Directors causing the Company to enter into an undervalued cash-out merger and to implement a dividend strategy which unfairly prejudiced the minority shareholders.

The Plaintiff's claims were initially dismissed for lack of standing and lack of jurisdiction. He appealed and the Appellate Division affirmed that the dispute was governed by the law of the Cayman Islands pursuant to the internal affairs doctrine (which provides that claims concerning the relationship between a company, its directors and a shareholder are governed by the law of the state or country of the company's incorporation). The Appellate court further affirmed that Order 15 rule 12A of the Cayman Islands Grand Court Rules is a substantive law under the conflict of laws principles and that non-compliance with the rule will result in dismissal of the derivative action for lack of standing.

Cayman law regarding leave to continue derivative actions: Order 15 rule 12A of the Grand Court Rules

In the context of derivative action proceedings commenced in the Cayman court, Order 15 rule 12A (**rule 12A**) provides that within a certain number of days after receiving notice of a defendant's intention to defend the action, the plaintiff *must* apply to the Grand Court for leave to continue the action.

While it is clear that the US courts made the correct decision of finding that the Plaintiff in the New York proceedings did not have the standing to commence a derivative action because the Cayman court had not granted leave for the Plaintiff to do so, what is less clear is whether it is within the jurisdiction of the Grand Court to grant leave to a plaintiff in proceedings outside of Cayman.

Under rule 12A the trigger for an application to seek leave to continue a derivative proceeding is receipt of the defendant's notice of intention to defend the filed proceedings. Both those proceedings and the notice of intention to defend are Cayman-based. That is, Cayman's rules of court do not deal with applications for leave to continue (or issue) derivative proceedings in a foreign jurisdiction.

Although an authority¹ was cited by the New York Appellate Court which confirmed that the New York courts would allow a re-filing of the US proceeding if the Cayman court subsequently granted leave to continue, the difficulty lies in the fact that rule 12A does not expressly provide for or infer availability of such leave for foreign litigants. This question of whether the Cayman Grand Court *could* or *would* grant leave to a plaintiff who intends to commence derivative proceedings in a jurisdiction outside of the Cayman Islands has yet to be addressed in any reported decision of the Grand Court.²

Thus there are two questions as to what the Grand Court of the Cayman Islands will do in a situation where a plaintiff intends to bring proceedings outside of the Cayman Islands but is first seeking leave of the Cayman court pursuant to rule 12A:

- 1) Will the Grand Court allow a plaintiff to apply for leave under rule 12A immediately as a stand-alone application without commencing full proceedings in the Grand Court; and
- 2) Even if an application for leave can only be made after formal commencement of proceedings as implied by rule 12A, can/will the Grand Court grant leave where the proceedings are intended to be continued outside of the Cayman Islands?

Since no reported Cayman Islands decisions address these questions, an alternative solution might be to look at the decisions of courts in other Caribbean, Commonwealth jurisdictions.

BVI law regarding leave to continue derivative actions: Section 184C of the Business Companies Act 2004

Similar to rule 12A under the Cayman Grand Court rules, section 184C of the Business Companies Act 2004 (as amended) provides that a shareholder has no standing to bring a derivative claim on behalf of a BVI Company without first obtaining leave from the BVI court. In 2012 the BVI Commercial Court was met with a case similar to *Davis v Scottish Re Group*. In the BVI case³ the plaintiff had brought derivative proceedings in Delaware on behalf of a BVI-incorporated company and, like Mr Davis, was dismissed (without prejudice to the plaintiff's ability to re-file) for lack of standing because the plaintiff had not first obtained sanction of the BVI court. After the dismissal the plaintiff commenced proceedings in the BVI Commercial Court to obtain sanction and was successful. That decision to grant leave was upheld in the Eastern Caribbean Court of Appeal.⁴

The BVI Commercial Court and the Eastern Caribbean Court of Appeal have therefore established that, where warranted, they can and will grant leave to allow plaintiffs to bring derivative proceedings not only in the BVI courts but also outside of the jurisdiction. The question is, given that leave has been granted in at least one other British Territory, will the Cayman courts do the same or will they be hesitant to grant leave to continue a derivative action outside of their jurisdiction?

Will the Cayman Court grant leave for derivative claims to be brought outside the jurisdiction?

On the one hand since the New York courts have established that the laws of the Cayman Islands govern such cases and will be applied, the Cayman court may ask why the derivative action is not being continued in the Grand Court once leave is granted. The Judges of the Grand Court may consider that it is more appropriate for the plaintiff to continue the proceedings in the country whose laws are applicable and then, if successful, to bring separate enforcement proceedings in the jurisdiction where the assets of the company are located. On the other hand, it would be more efficient (if possible) to commence the proceedings in the jurisdiction where enforcement would eventually be sought.

The question as to whether the Cayman courts will fall in line with the BVI Commercial Court and the Eastern Caribbean Court of Appeal has yet to be determined. Although the decision of the New York Appellate Division seems to be based on the premise that the Cayman courts *could* and *would* grant leave to continue proceedings outside the jurisdiction, this premise remains untested as a matter of Cayman Islands law.

In any event, pending a determination of this important underlying issue, the decision in *Davis v Scottish Re Group* serves as a salutary reminder that derivative actions commenced by shareholders of Cayman Islands companies in the New York Courts or courts in other jurisdictions without leave of the Cayman court under rule 12A will face dismissal for want of standing.

¹ Arc Capital LLC v Kalra 2013 NY Slip Op 3136[U] No 652931/2012

² It is possible that such an application has been brought but has not reached a stage where a reportable judgment was delivered.

³ *Microsoft Corporation v Vadem* BVI HV (COM) 2012/0048

⁴ *Microsoft Corporation v Vadem* BVICVP 2013/0007

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