International Corporate Rescue

Published by:
Chase Cambria Company (Publishing) Ltd
4 Winifred Close
Barnet, Arkley
Hertfordshire EN5 3LR
United Kingdom

www.chasecambria.com

Annual Subscriptions:
Subscription prices 2016 (6 issues)
Print or electronic access:
EUR 730.00 / USD 890.00 / GBP 520.00
VAT will be charged on online subscriptions.
For 'electronic and print' prices or prices for single issues, please contact our sales department at:
+ 44 (0) 207 014 3061 / +44 (0) 7977 003627 or sales@chasecambria.com

International Corporate Rescue is published bimonthly.

ISSN: 1572-4638

ARTICLE

Participation by International Stakeholders in Cayman Islands Insolvencies

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Introduction

Companies incorporated in the Cayman Islands usually conduct operations and hold assets elsewhere than in the Cayman Islands and Cayman Islands corporate insolvencies therefore commonly have a significant international dimension. Corporate insolvencies are conducted under the supervision of the Financial Services Division of the Grand Court of the Cayman Islands and the requirements of Cayman law mean that the insolvency practitioners (the liquidators) require court approval ('sanction' in the language of the statute) before they can take certain significant steps in the liquidation. Those steps include: bringing and defending legal proceedings, carrying on the corporate business, making compromises or arrangements with creditors and compromising claims.[1] Another feature of Cayman corporate insolvencies is the liquidation committee: a committee of creditors must be established in respect of every insolvent company being wound up by the court.[2] The liquidators must report to the members of the committee and when the liquidators require sanction the members of the committee are entitled to be heard on the application for sanction.[3] A recent decision *In the matter of PAC Ltd (in official liquidation)*[4] shows that these features of liquidations in the Cayman Islands can be used to provide an opportunity for creditors based overseas to play an informed and potentially decisive role in important decisions in the liquidation.

The committee's role

Liquidation committees have a role both in solvent and insolvent liquidations. Following their appointment, Cayman liquidators must determine whether the company is solvent, insolvent or of doubtful solvency and call appropriate meetings of creditors (if insolvent), shareholders[5] (if solvent) or both (if of doubtful solvency).[6] At these meetings, the liquidators will seek to form a liquidation committee: a representative body of creditors and/or shareholders (as appropriate depending upon the solvency determination).[7] Where the company is determined to be insolvent only creditors are eligible to serve on the liquidation committee. Following the appointment of a committee, liquidators have limited obligations to continue to report to those who are not on the committee.

The committee on the other hand is entitled to have frequent reports of all such matters as are of concern to the committee with respect to the winding up.[8] The liquidators must also seek the committee's views on their remuneration before applying for court approval[9] and must serve every application for sanction of the exercise of their powers[10] (a 'sanction application') on each member of the committee.[11] In practice therefore, there is usually an ongoing dialogue between the liquidators and the committee, which is provided with information in order to participate in the dialogue on an informed basis.

Notes

1 Companies Law (2013 Revision), section 110 and Schedule 3.
2 Unless the court makes a contrary order: Companies Winding Up Rules 2008 (as amended) Order 9 rule 1(1).
3 Companies Winding Up Rules 2008 (as amended) Order 11 rule 3(4).
4 FSD 71/2012, judgment of 11 December 2015.
5 Technically, the reference is to contributories – every person holding fully paid up shares or liable to contribute to the assets of the company in the event it is wound up.
6 Companies Winding Up Rules 2008 (as amended) Order 8, rule 1.
7 Companies Winding Up Rules 2008 (as amended) Order 9, rule 1(6).
8 Companies Winding Up Rules 2008 (as amended) Order 9, rule 4.
9 Insolvency Practitioners' regulations 2008 (as amended), regulation 12, liquidators are allowed to receive payment of up to eighty percent of the remuneration sought in advance of Court approval, but must repay the balance forthwith if the amount approved is less.
10 including bringing or defending legal proceedings, entering into a compromise with a creditor or debtor of the company, selling the company's property, borrowing money, or engaging attorneys, for a full list, see Schedule 3, Part I, to the Companies Law.
11 Companies Winding Up Rules 2008 (as amended) Order 11, rule 2.

In cases where sanction is needed, the liquidators must serve the sanction application on the committee, but there is no requirement that they must obtain the approval of the committee or even a requirement to engage in consultation with the committee. Nevertheless, as the members of the committee have a collective and individual right to be heard on any sanction application, prudent liquidators will seek to engage with the committee to identify and address concerns and refine the approach to the court. That approach will usually result in the views of the liquidators being aligned with the views of the committee.

A case of conflict

The recent Cayman decision in *PAC Limited* was an unusual situation of conflict between the views of the committee and the liquidators. PAC Limited was in insolvent liquidation and the committee was therefore comprised entirely of creditors. The liquidators had identified a potential claim for USD 44 million based on transactions with related companies entered into three days before the company went into voluntary liquidation. The liquidators' view, based on legal advice, was that the case against these companies to recover the USD 44 million was a strong one. They were unable to obtain funding to pursue the claim. They were, however, able to negotiate a settlement of the claim for a cash payment of USD 2.5 million and certain other terms more fully set out in the judgment of the court, in particular the funding of a claim by the company against another alleged debtor.

The liquidation committee strongly opposed the settlement agreement. They said that with liquidation fees and expenses of over USD 2.3 million the settlement agreement represented no return to them. They said they would prefer to pursue criminal proceedings in Lebanon that would be prejudiced by the settlement. The committee did not initially engage counsel, instead making representations directly to the court and the liquidators' counsel by email. The judge (Justice Foster) adjourned two hearings of the sanction application as a result of these representations, but eventually made a conditional order sanctioning the settlement agreement, but suspended it to give the creditors a last chance to engage Cayman counsel. The creditors took Cayman legal advice, which led to the liquidation committee engaging Cayman counsel as counsel for the committee and with the assistance of committee counsel, one of the members advanced a funding proposal to enable the liquidators to pursue the claim in Lebanon. The liquidators did not believe the funding was sufficient or that the proposed proceedings were credible and so continued to seek the sanction of the settlement agreement as representing the best possible return to the liquidation estate. There was a contested hearing.

In favour of the liquidator was a line of authority that holds that in the ordinary case 'the court will attach considerable weight to the liquidator's views' and that where the liquidator brings a compromise before the court for approval 'the court will not speculate on whether the proposed compromise were the best that could have been obtained' and the decision is 'the proposed compromise or no compromise at all'.[12]

On the other hand, and as the judge found, the payment of USD 2.5 million would enable the liquidators '... to meet their arrears of fees and expenses but little, if anything, more. It will certainly not leave anything at all for the creditors.' The only hope of recovery for the creditors were arrangements under which the other party to the proposed settlement agreement was to pursue proceedings in Paris and another claim on behalf of PAC, which the liquidators hoped might produce recoveries. The court was unconvinced by this argument, finding that the terms of the proposed settlement were such as to amount to a cumulative exclusion of the liquidators from any meaningful participation on behalf of PAC in the Paris proceedings and that no details of the other claim had been provided or of its basis or of what value it may have.

Creditors' interests paramount

The judge decided that in determining whether or not to grant sanction he should treat the interests of those who had a real interest in the assets of the company in liquidation as paramount.[13] In this case, because the company was insolvent and there was no question of any return to shareholders, it was the creditors whose interests were paramount. This had a significant impact on the way that the judge approached the USD 2.5 million cash element of the settlement. He had found that the creditors would see none of it because it would be applied to the fees and expenses of the liquidators leaving little over and nothing for the creditors. It was to the interests of the creditors and not the interests of the liquidator to which the judge was to have regard. It had been submitted to him that the fact that the settlement might confer some benefit on the liquidators personally, was no reason for the court to sanction it. The judge accepted this. The question essentially became whether the interests of the creditors were better served by allowing them to pursue matters in Lebanon

Notes

12 See the decision of the Court of Appeal in England and Wales in *Re Greenhaven Motors Ltd* [1999] 1 BCLC 642.

13 Following a line of Cayman authority applying the decision in *Re Greenhaven Motors Ltd* (above).

or binding the company to the proposed settlement in the hope of recoveries from proceedings in Paris or elsewhere.

Creditors are the best judge of their own interests

The judge accepted that there were uncertainties over the prospects of recovery in Lebanon, but he accepted that he should give weight to the creditors' preference for proceedings there over the alternative. He accepted that the creditors are likely to be good judges of where their own interests lie and he expressed the view that in the circumstances of this case the views of creditors, particularly the views of former employees, who together formed the largest creditor group, carried greater weight than the view of the liquidators.

Conclusions

The creditors' objections to the proposed settlement agreement initially gained little traction because they were not represented by counsel. Their objections were being made by emails sent to the court. The committee members were based in Lebanon and unfamiliar with procedure in the Cayman Islands. The Cayman rules, however, allow the committee to appoint their own counsel and for the legal fees reasonably and properly incurred by the committee to be paid out of the assets of the company as an expense of the liquidation. As we have noted, it is common for Cayman liquidations to have a significant international component and not unusual for the stakeholders to have little familiarity with the process in Cayman. The ability to appoint counsel and defray the cost from the assets of the company provides a valuable adjunct to the committee's right to receive information and be served with notice of sanction applications. Together they allow stakeholders in international insolvencies to have a real influence in the conduct of Cayman liquidations.[14]

Notes

14 The authors were the advocates for the liquidation committee at the hearing before Foster J.

International Corporate Rescue

International Corporate Rescue addresses the most relevant issues in the topical area of insolvency and corporate rescue law and practice. The journal encompasses within its scope banking and financial services, company and insolvency law from an international perspective. It is broad enough to cover industry perspectives, yet specialized enough to provide in-depth analysis to practitioners facing these issues on a day-to-day basis. The coverage and analysis published in the journal is truly international and reaches the key jurisdictions where there is corporate rescue activity within core regions of North and South America, UK, Europe Austral Asia and Asia.

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