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**CORPORATE RECOVERY AND INSOLVENCY IN  
THE CAYMAN ISLANDS**

**Introduction**

This document provides an introductory guide to the principal statutory, regulatory and practical requirements of Cayman Islands corporate recovery and insolvency law and practice.

The principal statute governing the Cayman Islands corporate recovery and insolvency law is the Cayman Islands Companies Law (the "Companies Law"). The Corporate Recovery and Winding-up regimes are to be found in Part 5 of the Companies Law. They are:

1. Provisional liquidation and court ordered stay of proceedings - used in the context of assisting a distressed company to reconstruct or refinance itself as a going concern in the interests of the creditors
2. Compulsory winding –up:
3. Members' voluntary winding-up
4. Winding-up subject to the supervision of the Grand Court

## **THE CAYMAN ISLANDS LEGAL SYSTEM**

Cayman Islands law derives principally from English common law and Cayman Islands legislation. The Companies Law is based upon the English Companies Acts with various specialised amendments. The Cayman Islands courts system is also well developed and, in the context of corporate recovery and insolvency cases, the Cayman Islands judiciary has extensive knowledge and depth of understanding of the corporate and commercial issues that arise. The Grand Court of the Cayman Islands is the court of first instance. In addition to the Chief Justice there are currently two permanent and one temporary Judges. All have practised in England or other Commonwealth jurisdictions before their appointment in the Cayman Islands' court. The procedural rules of the Grand Court are based largely upon the previous English Rules of the Supreme Court ("The White Book"). The first appellate court is the Cayman Islands' Court of Appeal with appeals thereafter to the Privy Council in London.

## STATUTORY REGIMES

### THE USE OF PROVISIONAL LIQUIDATION TO ASSIST IN THE REFINANCING AND/OR REORGANISATION OF A CAYMAN ISLANDS COMPANY AS A GOING CONCERN

Following the practice in England to appoint provisional liquidators over distressed insurance companies, the Cayman Islands courts will appoint provisional liquidators to assist and 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. If the relief is required in order to assist US Chapter 11 “debtor in possession” proceedings the Grand Court has, historically, allowed the directors to retain certain residual powers to conduct the business of the company in so far as they are required to complete a successful refinancing or reorganisation as a going concern. Provisional liquidators oversee the actions of the directors in this regard 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. It is the use of the stay of proceedings that protects the company in the meantime from its creditors and allows it to explore a refinancing and/or reorganisation.

The wide jurisdiction provided to the Grand Court under the Companies Law to appoint provisional liquidators has been used to great effect in such recent major cross-border corporate recovery cases such as ICO Global Communications and Fruit of the Loom. The ICO Global Communications case also involved co-ordination of the Cayman Islands' proceedings with similar provisional liquidation proceedings in Bermuda and Chapter 11 proceedings in Delaware. As a result of the schemes and the plans the ICO Group was able to avoid a winding-up and exit the process successfully as a going concern.

The negotiation of cross-border protocols between the Grand Court and courts in other jurisdictions is commonplace to enable co-ordination and to avoid duplication in the jurisdictions concerned.

## **MEMBERS' VOLUNTARY WINDING-UP**

A Cayman company may be wound up voluntarily: -

- (a) if the company's shareholders have passed a special resolution (being greater than a two-thirds majority or such greater majority as may be specified in the company's Articles of Association) requiring the company to be wound up voluntarily; or
- (b) where any period fixed or any event specified in the company's Articles of Association for the duration of the company elapses or occurs and the shareholders of the company have passed an ordinary resolution (greater than a fifty percent majority) requiring the company to be wound up voluntarily.

There are separate provisions in the Companies Law relating to the voluntary winding-up of an exempted limited duration company which are slightly but not fundamentally different from the provisions relating to other types of company as explained above.

### **The Date of Commencement of a Voluntary Winding-up**

A voluntary winding-up is deemed to have commenced at the time of the passing of either of the resolutions set out in paragraphs (a) and (b) above.

### **The Effect of a Voluntary Winding-up**

The effect of the commencement of a voluntary winding-up is that a company ceases from that date to carry on its business except as may be required for the beneficial winding-up of its affairs. However, unless otherwise provided for by its regulations, its corporate state and all its corporate powers continue until the affairs of the company are fully wound up. Upon the appointment of the liquidator all the powers of the directors cease except insofar as the company, by ordinary resolution of its shareholders or the liquidator, sanctions their continuance.

There is no statutory requirement under Cayman Islands law for the directors of the company to swear a statutory declaration of solvency or to provide the liquidator with a statement of affairs, although the latter is the usual practice.

Any transfer of shares made after the commencement of a voluntary winding-up or any alteration in the status of any members of the company is void unless the transfer is made to or with the sanction of the liquidator in his capacity as such.

There is no regime under the Companies Law equivalent to a creditors' insolvent voluntary winding-up. However, it is usual practice in the Cayman Islands for an insolvent voluntary winding-up to be conducted subject to the supervision of the Grand Court.

## **The Voluntary Liquidator**

Usually the resolution of the shareholders of the company requiring the voluntary winding-up will designate a liquidator, failing which any person so designated in the Articles of Association will automatically become the liquidator, failing which the directors of the company will automatically become the liquidators. The Court has power on the application of a shareholder to appoint a voluntary liquidator to fill any vacancy. It may also remove a voluntary liquidator on cause shown and appoint a replacement voluntary liquidator.

A voluntary liquidator has similar powers to an official liquidator (i.e. a liquidator appointed compulsorily by the Court) under the Companies Law. However, a voluntary liquidator is not an officer of the Court. He is a fiduciary to the creditors and (if the company is insolvent) to the shareholders of the company and has a duty to collect in and apply the assets of the company in satisfaction of its liabilities *pari passu* but giving effect first to the rights of preferred and secured creditors. After all creditors are paid off the liquidator must distribute the surplus (if any) amongst the shareholders in accordance with their rights and interests in the company.

## **The Conclusion of the voluntary winding-up and the company's dissolution**

Once the voluntary liquidator has completed his duties and the affairs of the company are wound up, he must prepare an account showing the manner in which the company has been wound up including details of any property of the company that has been disposed of during his time in office. After this has been done the liquidator must call a general meeting of the company's creditors and shareholders for the purpose of presenting his account to them. After the general meeting has been held and the liquidators' report has been approved, the liquidator must make his final return, including a copy of his account and his final report on the conduct of the liquidation, to the Registrar of Companies. Three months after the date of registration of this return by the Registrar the company is deemed to be dissolved and ceases to exist and its name will be removed from the Register of Companies maintained by the Registrar.

## **COMPULSORY WINDING-UP (WINDING-UP BY THE COURT AT THE REQUEST OF CREDITORS OR CONTRIBUTORIES)**

### **Compulsory Winding-up (Winding-up by the Court)**

A company may be wound up compulsorily on a petition to the Grand Court if:

- (a) the shareholders of the company pass a special resolution (greater than two-thirds majority or such greater majority as the Articles of the company may specify) requiring the company to be wound up by the Court;
- (b) the company does not commence its business within a year from its incorporation, or suspends its business for a whole year;
- (c) the company is unable to pay its debts; or
- (d) the Court is of the opinion that it is "just and equitable" that the company should be wound up.

The following parties have locus to present a petition for the compulsory winding-up of the company:

- (i) the company itself;
- (ii) a creditor;
- (iii) a shareholder (if the company concerned is solvent on a balance sheet basis).

The directors of a company do not have locus standi to present a petition in their own name. Further, if the company has "Table A" style Articles of Association (ie. standard form articles of association for a Cayman Islands company as set out in the Companies Law) the directors do not have the management power to present a petition in the name of the company for a winding-up simply on the authority of a board resolution.

However, the directors may nonetheless exceed their powers and present a petition in the name of the company and this will be valid if this breach is subsequently ratified by the shareholders of the company in general meeting. Accordingly, as long as an ordinary resolution of the shareholders authorises the company to present the petition the directors can do so. This can be a useful procedure where there is insufficient shareholder support to enable a special resolution to be passed.

### **Winding-up on the basis that the company is unable to pay its debts**

Winding-up by the Grand Court on a compulsory petition on the grounds set out in subparagraphs (a) and (b) above is self-explanatory but extremely unusual, the usual circumstances being on the petition of a creditor who is owed an undisputed debt and that the company is unable to pay its debts. The Grand Court will deem a company unable to pay its debts if:

- (a) the undisputed debt is greater than CI\$100 (US\$120) and the creditor has served on the registered office of the company a statutory demand for payment and the company has then failed to pay the debt within three weeks
- (b) execution on a judgment or order obtained in the Grand Court has been returned unsatisfied in whole or in part
- (c) it is proved to the satisfaction of the court that the company is unable to pay its debts.

The statutory minimum of CI\$100 is only relevant to a creditor who is relying on subparagraph (a) above. A creditor who is relying on subparagraphs (b) or (c) above is not subject to such a minimum level of debt in order to establish his locus to petition. In a case relying on subparagraph (c) above the Court will only consider the actual liabilities of the company as at the date of the hearing of the petition (ignoring any contingent claims) in assessing whether it is unable to pay its debts.

The Grand Court will not entertain a winding-up petition based on a debt which is disputed. If the Grand Court is satisfied that there is at least an arguable defence to a debt, the petition will be struck out with costs awarded to the company. It is also possible for a company to obtain an injunction against a person seeking to petition for its winding-up in reliance upon a debt which is disputed.

### **Just and equitable winding-up**

The Grand Court will entertain a winding-up petition seeking to wind up a company if it is satisfied that it is just and equitable for the company to be wound up. This equitable jurisdiction is exercised most frequently in shareholder disputes where the company's business was conducted as if it were a partnership between the shareholders. It will also exercise its discretion to wind-up a company on a just and equitable basis if it is satisfied that the company has lost its substratum and is unable to conduct the business which it was incorporated to do.

### **Effect of a compulsory winding-up order on the status of the company**

When making a compulsory winding-up order, the liquidation is deemed to have commenced at the date of presentation of the petition. The effect of this is that the liquidation is back-dated and any disposal of the company's property during the intervening period is void unless the court orders otherwise. All other actions and proceedings against the company are automatically stayed as from the date of the order.

Upon the making of a winding-up order all of the directors' powers are revoked and all the powers of management vest in the official liquidator.

### **The Official Liquidator**

Unlike the position in England where the Official Receiver is almost always appointed first as liquidator on the making of a compulsory winding-up petition and will hold that office until the first creditors' meeting, in Cayman, when making a winding-up order, the Grand Court will appoint an official liquidator immediately. This is usually one or more members of one of the international accounting firms, all of whom carry on business in the Cayman Islands. The court will also direct whether the official liquidator may exercise his statutory powers with or without the need for further sanction of the court. An official liquidator is an officer of the Grand Court and is responsible and answerable to the court, as well as owing fiduciary duties to the creditors of the company. He has extensive powers under the provisions of Part V of the Companies Law, including the power to carry on the business of the company should this be beneficial to the winding-up and to sell the real and personal property of the company. The official liquidator is also authorised to do all acts and to execute on behalf of the company any deeds, receipts or other documents. He may also bring and defend legal proceedings in the name of the company, although he will usually seek the specific sanction of the court before doing so. The official liquidator is under a duty to investigate the affairs of the company and to collect in its assets for their distribution *pari passu* to creditors after taking into account and giving effect to the rights of any preferred or secured creditors.

## **WINDING-UP SUBJECT TO THE SUPERVISION OF THE GRAND COURT**

### **Voluntary winding-up subject to the supervision of the Grand Court**

If a company wishes to commence an orderly voluntary winding-up of its business but suspects that it may be or become insolvent or that there are likely to be issues arising in the liquidation that may be contentious or that guidance from the Grand Court is likely, at some stage, to be required, it is usual for the shareholders who are voting for a voluntary liquidation to direct that the voluntary liquidator should thereafter apply to the Grand Court for the voluntary winding-up to continue subject to the court's supervision. On the making of an order by the Grand Court the winding-up is then known as a winding-up subject to the supervision of the court. The Voluntary Liquidator will then, for all practical purposes, have powers equivalent to those of an official liquidator.

The Grand Court has power on hearing such a petition to direct that meetings of the company's creditors should be called in order to ascertain their wishes and views on whether the liquidation should be made subject to court supervision or simply continue on the normal voluntary basis. The Court may also direct that the creditors' views as to the choice of liquidator or any other matter pertinent to the winding-up, should be ascertained. This is a useful power which enables creditors, if they believe that the person appointed as voluntary liquidator by the shareholder(s) is inappropriate, to request that the Grand Court appoint a different person, who they may perceive to be more independent, as liquidator.

If there are legal proceedings against the company, the voluntary liquidator is likely to consider it appropriate to have the liquidation conducted subject to court supervision. As in the case of a compulsory winding-up order, on the making of such an order for court supervision all legal proceedings against the company are automatically stayed. A voluntary liquidation alone has no such effect on legal proceedings against the company.

### **The effect on the status of the company of an order for winding-up subject to court supervision**

Under the Companies Law, and subject to any express restrictions imposed by the Grand Court, a liquidator conducting a voluntary winding-up subject to court supervision has effectively the same powers, obligations and duties as an official liquidator in a compulsory winding-up. For the purposes of striking down any transactions by or with the company, the date of commencement of such a liquidation continues to be the original resolution to place the company into voluntary liquidation is passed, notwithstanding the date of the order that the winding-up should be subject to Court supervision.

## WINDING-UP BY THE REGULATORY AUTHORITIES

### Winding-up by the authorities

The regulatory laws of the Cayman Islands give the relevant regulator the power to wind up a company conducting regulated business. For example, if the Cayman Islands Monetary Authority (CIMA) is of the opinion that a licensed bank or trust company:

- (a) is likely to become unable to meet its obligations as they fall due;
- (b) is carrying on business detrimental to the public interest, the interest of its depositors or of the beneficiaries of any trust or other creditors;
- (c) has contravened the Banks & Trust Companies Law; or
- (d) has failed to comply with the conditions of a licence granted under the Law,

then under the Banks & Trust Companies Law the licence may be revoked and a person (usually an accountant) appointed to assume control of the licensee's affairs. A report is then made to CIMA by the person so appointed and, if it is thought appropriate, a petition may be presented to the Grand Court for the winding-up of the bank or trust company and for the appointment of an official liquidator. Similar provisions are available in respect of companies conducting business as mutual funds under the Mutual Funds Law.

Under the Companies Management Law an application may be made at the instigation of the CIMA for a licensed corporate management company to be wound up in the public interest or on the basis that the licensee is insolvent.

The regulatory framework in the Cayman Islands is in a state of ongoing change and it is likely that the powers of the relevant regulator will be enhanced in relation to other companies and structures carrying on licensed businesses.

**CO-OPERATION OF INSOLVENCY COURTS (DESIGNATION OF RELEVANT COUNTRIES  
AND TERRITORIES) ORDER 1986 (SI NO.2123)**

The Cayman Islands is a "designated territory" under the Co-operation of Insolvency Courts (Designation of Relevant Countries and Territories) Order of the UK made in 1986 pursuant to section 426 of the UK Insolvency Act 1986. As a result, the Grand Court may request the assistance of the insolvency courts in the UK in matters concerning any Cayman Islands insolvency. In providing such assistance the UK courts may apply any aspect of either Cayman Islands or UK insolvency law as appropriate in providing the requested assistance. This mechanism has been used a number of times by Cayman Islands' insolvency practitioners to assist in the recovery of assets and/or to commence ancillary proceedings in support of the Cayman Islands' insolvency regime.

## **SUSPECT TRANSACTIONS**

### **Fraudulent Preferences under the Companies Law**

A liquidator (whether voluntary or official) has the power to apply to the Grand Court for an order that a payment to a creditor of the company should be set aside on the basis that its dominant intention was to prefer that creditor over others.

### **Transactions at an under value**

Under the Fraudulent Dispositions Law, any disposition of a company's property at an undervalue with an intention to defraud other creditors is voidable at the instance of a creditor who is prejudiced as a result. "Undervalue" in relation to a disposition of property is defined as:

- (a) the provision of no consideration for the disposition; or
- (b) the provision of consideration for the disposition which is significantly less than the value of the property disposed of.

The right to bring proceedings with any creditor who is prejudiced by the disposition who must demonstrate that there was an element of bad faith in the transaction concerned. Also the creditor must commence the proceedings to set aside the transaction within six years of its date. If he is successful, the court will set aside the transaction to the extent of the consequent loss to the creditor. It may be possible for a liquidator to make use of this statute to bring a class action on behalf of all creditors to the full extent of the loss to the company as a result of a fraudulent disposition.

### **Asset recovery**

Common Law tracing and recovery of assets unlawfully removed from or dissipated by a company is available outside of the statutory framework with the use of both local and worldwide Mareva orders, as well as Anton Pillar and Norwich Pharmacal relief to assist insolvent companies track down and recover assets removed or dissipated prior to the commencement of insolvency proceedings.