MAPLES GROUP

UPDATE

Good News for Debtors Seeking Access to the Cayman Islands Restructuring Regime

Reforms to Cayman Islands restructuring laws, which are expected to come into force in late 2021 or early 2022, have now been published by the Cayman Islands Government.

Debtors seeking to restructure their debt in the Cayman Islands, with the protection of a stay on unsecured creditor action, will be able to do so without needing to file a winding up petition. While the Cayman Islands has always been receptive to international restructurings, the current position is that, debtors seeking the protection of a restructuring stay in the Cayman Islands have to file a winding up petition and seek the appointment of provisional liquidators. Although the current regime has been effective in practice, filing a winding up petition in order to restructure is counterintuitive and unpalatable for some debtors.

The new regime, will provide for a new stand-alone global restructuring stay on unsecured creditor action, outside the winding up procedure. The debtor will apply to the Cayman Islands court (the "Court") for the appointment of restructuring officers who, while the company's management will ordinarily be left in control of the company, will help facilitate a restructuring. A global stay will arise immediately upon filing the application, similar to a Chapter 11 or administration stay, and the restructuring takes place within the breathing space created by the stay. How the restructuring is implemented is flexible and could involve a consensual deal with creditors, a Cayman Islands scheme of arrangement or a restructuring proceeding in another jurisdiction (for example, Chapter 11 in the United States or an English or Hong Kong scheme of arrangement).

These new proceedings, while retaining all that is positive with the prior law, will significantly enhance the Cayman Islands restructuring regime by:

- Removing the need to file a winding up petition in order to obtain a stay on creditor action.
- Providing for the stay (although not the appointment of restructuring officers) to arise automatically on filing the Court papers without the need for any Court hearing (in the prior law the moratorium only kicked in on the appointment of the provisional liquidators).
- Providing that, as a matter of Cayman Islands law, the stay will have extraterritorial effect.
- Including provisions which provide the potential for Cayman Islands schemes of arrangement to compromise debt governed by English law (an important consideration in light of challenges arising from Brexit) thereby broadening the circumstances in which Cayman Islands restructuring proceedings may provide the best fit.

The restructuring moratorium will not change important creditor protections under Cayman Islands law. There will remain no stay in any Cayman Islands insolvency or restructuring proceeding on the enforcement of security by

secured creditors. Further, specific legislative provisions have been included to ensure that the Cayman Islands remains a preeminent jurisdiction for bankruptcy remote finance vehicles.

Restructuring Moratorium – FAQs

What is the restructuring moratorium?

The restructuring moratorium is a stand-alone regime where a company (including, in certain circumstances, a foreign company) can apply to the Court for the appointment of restructuring officers. On the filing of the application, the company obtains a moratorium (stay) on legal proceedings being continued or commenced by unsecured creditors against the company. This results in breathing space for a company that is in financial distress to pursue a restructuring. The restructuring moratorium is also available to exempted limited partnerships ("ELPs") and limited liability companies ("LLCs").

The restructuring moratorium can be used in support of a scheme of arrangement, a formal foreign restructuring proceeding (such as Chapter 11) or to explore a consensual deal with creditors. The moratorium has been crafted with flexibility in mind; flexibility to meet the needs of the stakeholders and the circumstances of the company in question.

The Court will decide whether or not to appoint restructuring officers. Creditors and, in certain circumstances, shareholders have the ability to be heard on, among other things, as to whether or not restructuring officers should be appointed. If the Court decides to appoint restructuring officers, the moratorium will continue.

The application should be heard within 21 days of being filed, but if the company needs the assistance of restructuring officers urgently, an interim appointment is possible pending the hearing of the application.

In what circumstance is it expected that the restructuring moratorium will be used most frequently?

We expect the moratorium to be used most frequently in restructuring the debt of a Cayman Islands incorporated holding or finance company. This should particularly be the case where the governing law of the debt is New York, but the moratorium may be relevant where the debt is governed by other laws (for example, English law). See the section on international recognition below.

Further, where a company is incorporated in a jurisdiction which does not have a restructuring regime that works for the required debt restructuring, it will be possible to: (i) register the company as a foreign company in the Cayman Islands; and (ii) if required, potentially relatively easily, shift certain aspects of the company's activities to the Cayman Islands, to enable the company to take advantage of the restructuring moratorium and utilise a Cayman Islands scheme of arrangement.

Will the moratorium prevent secured creditors from enforcing their security or exercising contractual rights of set-off or netting?

No. The key policy elements of freedom of contract and the creditor friendly nature of the jurisdiction are not affected.

Will the moratorium prevent counterparties from exercising their contractual rights, for example in relation to capital call rights and related issuance of shares?

No. The moratorium will not affect the ability to exercise contractual rights (unless legal

proceedings are required to exercise the contractual rights).

Will the moratorium have extra-territorial effect?

As a matter of Cayman Islands law, yes. In practice, this means that the moratorium will bite on parties who are subject to the jurisdiction of the Cayman Islands Courts – this includes, among others, Cayman Islands incorporated entities and partnerships (for example, companies, LLCs and ELPs). Therefore, creditors who are incorporated in the Cayman Islands (such as hedge funds) will, as a matter of Cayman Islands law, be caught by the moratorium. However, whether the moratorium is recognised and enforceable in foreign jurisdictions is a question of the relevant foreign law –see further below in relation to international recognition.

Who can apply to the Court to appoint restructuring officers?

Only the company can apply. This is because, as a matter of policy, the company will need to be on board with the restructuring. The company's involvement is not optional and an involuntary filing by a creditor to drag a company to the table is not possible.

What criteria must be satisfied in order to appoint restructuring officers and obtain the moratorium?

The test remains the same as under the prior regime. The company must: (i) be unable or likely to become unable to pay its debts; and (ii) intend to present a compromise or arrangement to its creditors.

The first limb is a cash flow test which includes an element of futurity- how far into the future the Court can look is highly fact specific.

The second limb has a low bar, for example, there is no need for a company to have a formulated (or even partially formulated) restructuring plan. The low bar enables a company to obtain the protection of a moratorium in the embryonic stages of a restructuring and negotiate with creditors within that safety net . There must though be a genuine intention to explore a restructuring and evidence to demonstrate this.

Must the proceedings to implement the restructuring take place in the Cayman Islands?

No. There is no requirement that any restructuring of the company's debts takes place in the Cayman Islands. As well as a Cayman Islands scheme of arrangement, the restructuring moratorium can be used to support any other restructuring proceeding in any other jurisdiction or an informal work-out with creditors. Flexibility to obtain the best result for stakeholders is a fundamental driving force behind the new law and the Cayman Islands is not territorial as to the jurisdiction in which the restructuring is implemented.

Who can be restructuring officers?

Restructuring officers will be independent Court-appointed fiduciaries who will supervise the restructuring process. A restructuring officer must be a qualified insolvency practitioner and will be an officer of the Court. A foreign insolvency practitioner may be appointed as a restructuring officer but there must always be one Cayman Islands practitioner appointed.

What role does the restructuring officer play?

The Court has complete flexibility as to the role the restructuring officer plays. For example, the restructuring officer can play a light role, leaving

the management to continue day-to-day operations (effectively a debtor in possession proceeding), while the restructuring officer provides an independent, focused and specialist oversight role in the company's restructuring. This can involve vetting a restructuring plan which has been formulated, providing an independent and impartial voice in negotiations with creditors or assisting the company in coming up with a restructuring plan from the ground up. At the other end of the spectrum, there may be circumstances where it is appropriate to divest the management of their powers with the restructuring officer taking over management and performing a much more active role (although it is envisaged that such circumstances are likely to be rare in practice).

Who pays for the restructuring officer?

The remuneration and expenses of a restructuring officer will ordinarily be paid out of the assets of the company. If the company goes into liquidation the expenses and remuneration of the restructuring officer will come ahead of the expenses and remuneration of any provisional or official liquidators.

The Court is given the power to make provision for the payment of liabilities incurred and falling due during the period in which the restructuring officer is appointed.

What protections are there for creditors?

There are a number of protections built in for creditors (and other stakeholders):

- As mentioned above, secured creditors rights are not affected by either the filing of an application to appoint restructuring officers or the appointment of restructuring officers. As a matter of Cayman Islands law, secured creditors remain entitled to enforce valid and enforceable security interests.

- An application to appoint restructuring officers will be advertised both domestically and, if relevant, internationally. The application is therefore on notice to all stakeholders. While the moratorium (stay) applies from filing, creditors are free to apply to the Court to lift the moratorium.

- Creditors have the right to be heard on an application to appoint restructuring officers and to nominate their own restructuring officers instead of those nominated by the company (for example, if the creditor has concerns about the independence of the company's nomination).

- A creditor may seek leave of the Court to present a winding up petition (either before or after restructuring officers are appointed). This recognises that a creditor may, for example, not want to keep kicking the can down the road and opt for liquidation instead. Procedural mechanisms exist to ensure that the two applications, which have competing end goals are coordinated (the competing end goals being, on the one hand, to rescue the company and, on the other hand, to end the life of the company). The Court will make the decision on whether the company should be given the opportunity to pursue a restructuring or be liquidated. The Court has regularly demonstrated that it will give a potential restructuring a chance to breathe and that it, ordinarily, regards liquidation as a remedy of last resort. We expect these principles to continue to apply in the context of an application to appoint restructuring officers.

- Creditors have, at any point in time after the appointment of restructuring officers, the right to apply to the Court to remove and

replace the restructuring officers or vary or discharge the order appointing restructuring officers.

- Shareholders have the same rights as above; although the extent that shareholders views will be given weight will heavily depend on whether the shareholders are in the money.

International Recognition

International recognition will depend on the relevant jurisdiction's law in which recognition and assistance is sought. However, in relation to jurisdictions that have implemented the Model Law on cross-border insolvency, from the Cayman Islands law perspective, the expectation is that recognition and assistance will be available. This is because the appointment of restructuring officers does not contain any substantive differences which impact on recognition from the previous restructuring provisional liquidation model. Restructuring provisional liquidation proceedings were routinely recognised in Model Law jurisdictions (including, importantly, in the United States under Chapter 15).

New York Law-Governed Debt

Where the debt to be restructured is New York law governed (as is currently common in Cayman Islands based debt restructurings), Chapter 15 recognition will continue to be a key component of any restructuring. This is because, among other things: (i) it allows for a moratorium within the territorial jurisdiction of the United States on the enforcement of security; and (ii) where the restructuring is effected through a Cayman Islands scheme of arrangement, the recognition and enforcement of the terms of the scheme.

English Law-Governed Debt

The restructuring moratorium includes separate provisions permitting a restructuring officer to propose a scheme of arrangement – these provisions mirror the current scheme legislation that is part of Cayman Islands company law. This means that Cayman Islands law will have two sets of scheme provisions – one specifically for restructuring officers within the insolvency law (a restructuring officer scheme) and general provisions available more widely. The reason for the specific restructuring officer scheme is to open up the possibility of compromising English law debt through a Cayman Islands scheme of arrangement. The fact that the scheme provisions sit within the wrapper of the restructuring moratorium should allow such a scheme to fall within certain English legislative provisions allowing for the recognition and enforcement of insolvency and restructuring proceedings commenced in specified countries (of which the Cayman Islands is one).

Can the company's directors apply for the appointment of restructuring officers without authority in the company's articles of association or a shareholder resolution?

Yes. The rule in the Cayman Islands that a director is unable to file a winding up application on behalf of the company without authority to do so in the articles of association or from shareholders does not apply to an application to appoint restructuring officers.

Is there any change to the fact that the directors cannot engage the winding up jurisdiction on behalf of the company without permission to do so in the articles of association or from shareholders?

Yes. The default position for companies incorporated **after the commencement of the new law** is to allow directors to file a winding up

application on behalf of the company without needing the authority to do so in the articles of association or from shareholders. This prevents the situation where directors need to file for liquidation proceedings but, without cooperation from a friendly creditor, are unable to do so. The default position will be that directors will be able to make the filing on behalf of the company.

However, the articles of association may expressly remove or modify the directors' authority to present a winding up petition on the company's behalf. Providing this opt out is important for the Cayman Islands structured and asset finance industry, where bankruptcy remoteness is key from both the stakeholder and rating agency perspective.

For companies incorporated **prior to the commencement of the new law**, the position remains the same. Directors will require permission in the articles of association or from shareholders to file a winding up petition. In order to avoid the need to conduct a large-scale review of current companies' articles of association, it was decided that there should be no retrospective change to the law.

Are there any other important changes to the restructuring laws?

Yes, in relation to schemes of arrangement which require a shareholder vote the requirement for a majority in number (the often referred to head count test) of each class of shareholders present and voting at the relevant meeting will be removed. The approval threshold will be 75% by value of those shareholders voting at the relevant meeting. This avoids an issue which can occur where an overwhelming majority of shareholders by value approve the restructuring but a large number of small shareholders do not.

Can a company still apply to the Court to appoint provisional liquidators?

Yes, although the legislative provisions allowing a company to apply to appoint provisional liquidators for the purpose of pursuing a restructuring will be repealed; a company may still apply to appoint provisional liquidators. The Court may appoint provisional liquidators if it considers it appropriate to do so.

Caroline Moran and Nick Herrod from the Group's law firm, Maples and Calder, led the legislative reform project and worked closely with the industry, the judiciary and Government in drafting the enhanced regime.

Further Information

If you would like further information, please reach out to your usual Maples Group contact or any of the persons listed below.

Cayman Islands

Aristos Galatopoulos
+1 345 814 5241
aristos.galatopoulos@maples.com

James Eldridge
+1 345 814 5239
james.eldridge@maples.com

Caroline Moran
+1 345 814 5245
caroline.moran@maples.com

Nick Herrod
+1 345 814 5654
nick.herrod@maples.com

Hong Kong

John Trehey
+852 2971 3014
john.trehey@maples.com

Aisling Dwyer
+852 3690 7449
aisling.dwyer@maples.com

Nick Stern
+852 3690 7494
nick.stern@maples.com

London

Christian La-Roda Thomas
+44 20 7466 1648
christian.la-rodathomas@maples.com

October 2021