Holt: The first appointment of restructuring officers to an SPC in Cayman

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*Collas Crill acted as Cayman Islands legal counsel to Holt Fund SPC (**Company**) in respect of its successful application for the appointment of restructuring officers. This was the first time that the Grand Court of the Cayman Islands **(Court)** was called on to consider the application of the restructuring officer regime provided for in Part V of the Cayman Islands Companies Act (as revised) (**Act**) to a segregated portfolio company (**SPC**).*

*The jurisdictional gateway for the appointment of restructuring officers is that the company in respect of which the appointment is made is "liable to be wound up". The principal issue before the Court in respect of the Company was whether an SPC could be wound up, based on the insolvency of one or more of its segregated portfolios. For reasons handed down on 25 January 2024 (**Reasons**), the Honourable Justice Kawaley, held that an SPC could be wound up on that basis.*

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On 19 December 2023, the Honourable Justice Kawaley granted an order appointing Mr David Griffin and Mr Iain Gow of FTI Consulting (Cayman) Ltd as joint restructuring officers to the Company (**JROs**) pursuant to Section 91B of the Cayman Islands Companies Act (as revised) (**Act**).

Background

The Company is an SPC and operates an investment fund through four segregated portfolios (**SPs**). Two of those SPs, referred to as **SP02** and **SP03** (collectively, **Portfolios**), invested in US bonds and US real estate. As between the Portfolios, the investments of SP02 consist of US bonds and an investment in SP03. In turn, SP03 holds an indirect investment in a mixed use real estate project from which a fluctuating income stream is generated.

The terms of SP02 provide that, subject to any temporary suspension, redemptions may be made on a quarterly basis. In contrast, SP03 is a closed-ended investment portfolio and is currently operating within its initial lock-up period. Significantly, the corporate documents of the Portfolios established an operational structure whereby the Company maintained no general assets and incurred liabilities only in respect of its SPs. This was reflected in the manner in which business of the Company was conducted through each of the Portfolios.

The Portfolios faced severe liquidity issues as a result of the aggressive interest rate rises by the US Federal Reserve during 2023. Those rises served to compound the difficulties caused by the COVID-19 pandemic, which caused significant depreciation of asset prices to which the Portfolios were exposed. The persistence of these factors over a sustained period of time inhibited the Portfolios from generating sufficient liquidity from the underlying investments to discharge the debts of the Portfolios.

Stakeholders were understandably concerned by the prolonged financial difficulties and the Company formed the view that it was in the best interests of the Portfolios' stakeholders to seek the appointment of restructuring officers.

On 17 October 2023, the Company presented a petition for the appointment of the JROs pursuant to Section 91B of the Act on the grounds that the Company:

(i) is or is likely to become unable to pay its debts as defined in Section 93(a) of the Act; and

(ii) (ii) intends to present a compromise or arrangement to its creditors (or classes thereof) pursuant to Section 86 and/or 91I of the Act, the law of a foreign country or by way of a consensual restructuring (**Petition**).

At the hearing of the Petition his Lordship, the Honourable Justice Kawaley, expressed concern as to whether the winding-up jurisdiction could be invoked on the insolvency of one or more of several SPs in circumstances where the SPC as a whole was not said to be insolvent. This concern apart, his Lordship was of the view that the requirements for appointing restructuring officers were otherwise met.

Jurisdiction to appoint restructuring officers to a SPC

Justice Kawaley readily accepted the Company's submissions that Restructuring officers can be appointed in relation to any company which is liable to be wound-up, and that an SPC is a company which is liable to be wound up under the Act.

As set out in the Reasons, Section 91A(a) defines a company for the purpose of the restructuring officer regime as *"any company liable to be wound up under section 91"*. In turn, section 91 confers jurisdiction on the Grand Court to wind-up, inter alia, *"(b) a company incorporated and registered under this [Act]".* Section 213 (1) of the Act provides that "…any exempted company may apply to the Registrar to be registered as a segregated portfolio company".

The additional requirement of a company's liability – rather than eligibility - to be wound up, is that the company is unable (or is unlikely to be able) to pay its debts. In this respect, Section 91B(1)(b) refers expressly to Section 93, which provides that "a company shall be deemed to be unable to pay its debts if… (c) it is proved to the satisfaction of the Court that the company is unable to pay its debts."

In the context of a winding up petition, the ability or inability to pay debts is a cashflow test. As established by the Privy Council in ***SEB Conway & Anor (JOLs Weavering)*** [2019] UKPC 36 [at para 16], this includes an assessment of whether the company is unable to pay its debts, and to allow consideration as to whether, on the balance of probabilities, the company does not (or will not) have the resources to discharge those debts that will fall due in the reasonably near future[1].

The issue for Justice Kawaley was whether the Court may be satisfied that an SPC is unable to pay its debts, by reason that one or more of its SPs is cashflow insolvent. Ultimately, his Lordship answered that question in the affirmative.

When is an SPC unable to pay its debts?

SPCs are regulated by Part XIV of the Act. It was uncontroversial that while an SPC may establish one or more SPs through which the SPC may conduct business, those SPs do not have separate legal personality[2], and that in conducting business, the directors of an SPC are required to ensure that the assets of the Company and the assets that are attributed its SPs (and each SP) are kept separate and identifiable.

The terms of Section 223 expressly modify the statutory liquidation waterfall which otherwise applies in a liquidation, and stipulate that the segregation between and distribution of assets attributed to an SP, and those which are properly assets of the SPC, must be maintained during the winding up of the SPC.

It was submitted that the effect of Part XIV is not to carve out SPCs from liquidation within Part V, but to modify the operation of that process in a way which is consistent with the limited recourse regime created by Part XIV more broadly, and arguably when it matters most. His Lordship held that the terms of Section 223 confirm that an SPC may be wound up and that where this occurs, respect must be given by the liquidator to the statutory separation of assets and liabilities linked to segregated portfolios[3].

Notably, the terms of Part XIV do not modify the insolvency test as it applies to SPCs from that applicable to companies that are not also SPCs. This is in contrast to the corresponding Bermudian statutory framework applicable to Segregated Accounts Companies.

The Segregated Accounts Companies Act 2000 (Bermuda) expressly modifies the insolvency test applicable to segregated account companies for the purpose of winding up petitions, and states that:

"Winding up of segregated accounts companies

(1) Subject to this section, a segregated accounts company shall be wound up in accordance with the provisions of this Act, the Companies Act 1981 or the Limited Liability Company Act 2016 (as the case may be) and any other Act or rules which apply to the winding up of a company, save that in the event of any conflict, the provisions of this Act shall prevail.

(1A) For the purposes of determining whether a segregated accounts company may be wound up on the ground of insolvency:

a. *the test of insolvency which applies under section 162 of the Companies Act 1981 or section 109 of the Limited Liability Company Act 2016 (as the case may be) and (in the case of an insurance company) section 33 of the Insurance Act 1978 shall apply; and*

b. ***assets and liabilities linked to segregated accounts shall not be taken into account****…." (emphasis added)."*

As held by his Lordship, this contrasting legislative approach supported the Company's contention that in the absence of express statutory language in the Act modifying the insolvency test applicable to winding up petitions in relation to SPCs, there were no grounds for inferring any such legislative intent.[4]

It is then a question of what debts can properly be characterised as debts of an SPC. The provisions of Part XIV of the Act provide that the debts of an SPC necessarily include the debts of each of its SPs, and that the assets of the SPC comprise the assets that are accounted for as SP assets. This is illustrated by the terms Section 219(2) which defines SP assets as comprising "the assets of the segregated portfolio company held within or on behalf of the segregated portfolios of the company", and with regard to liabilities, Section 221 which states that:

"Where a liability of a segregated portfolio company *to a person arise from a matter, or is otherwise imposed, in respect of or attributable to a particular segregated portfolio:*

a. *Such liability shall extend only to, and that person shall, in respect of that liability, be entitled to have recourse only to:*

i. *Firstly, the segregated portfolio assets attributable to such segregated portfolio; and*

ii. *Secondly, unless specifically prohibited by the articles of association, the segregated portfolio company's general assets, to the extent that the segregated portfolio assets attributable to such segregated portfolio are insufficient to satisfy the liability, and to the extent that the segregated portfolio company's general assets exceed any minimum capital amounts lawfully required by a regulatory body in the Islands". (emphasis added)."*

In successfully submitting that the insolvency of an SPC may be established by reference to the assets and liabilities of a single SP, Justice Kawaley accepted that the recent decision of Doyle J in *Re Coinful*, FSD 86/2023, Judgment dated 5 July 2023 (unreported) provided authority for the Company's position.

This was fortified by the approach taken by the Honourable Justice Parker in Performance Insurance Company SPC (in official Liquidation)**[5]** in which his Lordship appointed Ms Angel Barkhouse as an additional liquidator with sole and exclusive responsibility for the liquidation of two of 12 SPs.

Justice Kawaley found that he was bound to accept the powerful submissions made on behalf of the Company that *Performance* demonstrated that:

(a) The insolvency of one or more of several segregated portfolios could be attributed to an SPC for the purposes of exercising the Court's winding up jurisdiction under the Act; and

(b) That official liquidators could be appointed to deal with assets and liability of specifically segregated portfolios.

Commentary

This decision, is a welcome addition to the jurisprudence which establishes the Cayman Islands as a legally robust and commercially minded insolvency and restructuring jurisdiction.

The reasons of Justice Kawaley indicate that receivership is not the exclusive mechanism available in respect of a financially distressed segregated portfolio, but that the restructuring regime is sufficiently flexible to apply to an SPC as a company in toto, or to specific assets and interests as the circumstances may require.

Furthermore, the decision brings clarity as to how the primary jurisdictional gateway, of demonstrating that a company is liable to be wound up on the basis of an actual or anticipated inability to pay debts, may be satisfied where the application concerns an SPC.

For further information or advice on this please contact a member of the team listed.

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[1] By way of submissions, the Company acknowledged the similarity in the solvency test in Section 91B (b) of the Act with the solvency test which is relevant to applications for receivers of Segregated Portfolio assets in Section 224 of the Act. The Company noted that the insolvency test applicable in the receivership context was at that time the subject of a pending judgment of the Cayman Islands Court of Appeal in the *Matter of Oakwise* (unreported decision of Doyle J dated 26 May 2023). It was submitted that in the

context of the company restructuring regime, the cash flow test as characterized in the ***SEB Conway (Weavering)*** is the relevant test for the purposes of this application.

[2] Section 216, the Act

[3] Reasons, para 11

[4] Reasons, para 14

[5] FSD 70/2021, Judgment dated 6 April 2022 (unreported)

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