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A Comparison of Insolvency Regimes and Fiduciary Duties: United States, Mexico, Offshore and Beyond

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Restructuring in the Cayman Islands: The New Regime

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On August 31, 2022, significant amendments to Part V of the Cayman Islands Companies Act ("Act") took effect to revamp the Cayman Islands restructuring regime. These amendments introduced the new role of a court-appointed "Restructuring Officer" and a dedicated "Restructuring Petition." The Cayman Islands restructuring officer regime ("RO Regime") shares certain features with the Chapter 11 bankruptcy procedure in the US and Canada's Companies' Creditors Arrangement Act.

Now that the RO Regime is approaching its two-year anniversary, we take the opportunity to provide a brief overview of the RO Regime and an update on how it is working in practice based on the first decisions such as *Re Oriente Group Limited*, *Re Aubit International* and *Re Holt Fund SPC*.

The RO Regime has been developed over a number of years with extensive consultation between the Cayman Islands government, the local judiciary, and a number of financial services industry participants (including attorneys and insolvency practitioners). The introduction of the RO Regime has been welcomed by the financial services industry as a useful tool for companies in distress (and their stakeholders) to assist with the protection of a distressed company's value and a way to provide "breathing space" while a restructuring is carried out.

One benefit of the RO Regime is that there is now a clear distinction between winding-up processes and rescue or recovery paths. Before enactment of the RO Regime, a winding-up petition was required to be presented prior to any application to appoint officeholders (including for the purpose of promoting a restructuring). The filing of a winding-up petition was often the precise act that a distressed company (and/or its stakeholders) was trying to avoid, particularly where such a filing might trigger a corresponding public announcement on a stock exchange or an event of default on the company's debts. Given the global reach of many Cayman Islands companies, it is understandable that stakeholders in other jurisdictions would often have an instinctive negative reaction to terms such as "winding-up petition" and "liquidator."

It is now possible to initiate restructuring efforts using a bespoke method with the benefit of a statutor moratorium effective from the time of filing a restructuring petition that is similar to the US Chapter 11 stay (while avoiding the negative connotations associated with the winding-up petition process).

KEY FEATURES

- A company may seek the appointment of restructuring officers on the grounds that (i) the company is or is likely to become unable to pay its debts; and (ii) intends to present a compromise or arrangement to its creditors.
- The petition seeking the appointment of a restructuring officer may be presented by the directors of a company: (i) without a shareholder resolution and/or an express power to present a petition in its articles of association; and (ii) without the need to present a winding-up petition. This addresses longstanding issues related to the rule in *Re Emmadart Ltd* [1979], which prevented directors of Cayman Islands companies from presenting a petition to wind up a company (in order to restructure or otherwise) unless expressly authorised by the articles of association.
- The moratorium will arise on presenting the petition seeking the appointment of restructuring officers, rather than from the date of the appointment of officeholders, and it will have extraterritorial effect as a matter of Cayman Islands law. This was aimed at tackling the uncertainty in the interim period where a winding-up petition had been filed with a view to restructuring, which might have triggered events of default, but a stay on claims only occurred after officeholders were appointed.
- The default position is that this will be an *inter partes* process with adequate notice to be given to all stakeholders.
- The powers of restructuring officers are flexible. The extent to which the directors will continue to manage the affairs of the relevant company will be defined by the order and will depend on the facts of the particular case.
- During the restructuring proceedings, the company will be able to seek sanction of a scheme of arrangement, a parallel process in a foreign jurisdiction, or a consensual compromise.
- Secured creditors with security over the whole or part of the assets of the company will still be entitled to enforce their security without the leave of the court and without reference to the restructuring officers. Unsecured creditors and other stakeholders must seek leave initiate proceedings and circumvent the stay.

RE ORIENTE GROUP LIMITED, DECEMBER 8, 2022

(FSD 231 OF 2022) (IKJ)

Justice Kawaley handed down the first written judgment on the RO Regime. *Re Oriente Group Limited* provided a number of important clarifications on the law, including the following:

- Given that the RO Regime expanded the scope of the stay under the previous regime (discussed above), the Court commented that the statutory stay on proceedings under the RO Regime "might be said to turbo charge the degree of protection filing a restructuring petition affords to the petitioning company." Accordingly, in Re Oriente, the Court found that following the presentation of a winding-up petition against a company, there is no prohibition on a company presenting a restructuring petition and such filing triggering the automatic stay under the RO Regime.
- The Court emphasised that the "jurisdiction to appoint restructuring officers is a broad discretionary jurisdiction" to be exercised where the Grand Court is satisfied that, among other things:
    - the statutory precondition of insolvency or likely insolvency of the company is met by credible evidence from the company or some other independent source;
    - the statutory precondition of an intention to present a restructuring proposal to creditors or any class thereof is met by credible evidence of a "rational proposal with reasonable prospects of success"; and
    - the proposal has or will potentially attract the support of a majority of creditors as a "more favourable commercial alternative to a winding up of the company."
- The Court indicated that the previous body of case law on restructuring under the former rescue regime would continue to be applicable to the new RO Regime.

RE AUBIT INTERNATIONAL, OCTOBER 4, 2023 (FSD 240 OF 2023) (DDJ)

In the second notable decision on the RO Regime, Justice Doyle reviewed the established jurisprudence and set out a nonexhaustive list of twenty-five factors to be considered in future restructuring applications under the RO Regime, such as the importance of demonstrating that the company was insolvent or likely to be insolvent, and whether a proposed restructuring will have a real prospect of being beneficial to creditc whole. Justice Doyle also emphasised that the Court will be wary to avoid abuse of the restructuring o regime by companies with no intention of restructuring and permitting hopelessly insolvent companies to continue trading.

In this case, Justice Doyle found that the petitioning company did not meet the statutory requirements appoint restructuring officers, as although it was unable to pay its debts (i.e., insolvent), it failed to meet the

second requirement because there was "extremely limited information concerning the proposed 'restructuring plan.'"

Justice Doyle indicated that although the Court did not go so far as to require that the petitioning company presently had a restructuring plan or that one would be implemented in short order, it was still incumbent on the Court to scrutinise whether there was, on the evidence before it, a genuine and realistic intention to present a credible restructuring plan.

RE HOLT FUND SPC, JANUARY 26, 2024 (FSD 0309 OF 2023) (IKJ)

In a recent development, Justice Kawaley ordered the first appointment of restructuring officers over one or more portfolios of a segregated portfolio company ("SPC"). SPCs are different from typical Cayman companies in that the assets and liabilities of each segregated portfolio are segregated from each other during the life of the SPC and in liquidation, which is known as the segregation principle. Typically, where a particular portfolio has insufficient assets to meet claims of creditors, a receiver may be appointed for the purpose of an orderly closing down of the business of that portfolio.

Until this judgment, it was not clear that restructuring officers could be appointed in relation to specific portfolios given that each portfolio is not a separate legal entity.

This decision illustrates the flexibility of the SPC regime compared with both traditional companies and corresponding segregated portfolio regimes elsewhere. However, the application to appoint restructuring officers was unopposed in this case, so it will be interesting to see if such appointments are subject to challenge in future.

TAKEAWAY

While not appropriate for all circumstances, the RO Regime will be a sensible and effective method by which large, multinational groups may seek to restructure their debt obligations and other affairs for the benefit of their stakeholders.

The Cayman Courts have provided helpful clarification on a number of aspects of the RO Regime, including the breadth of the automatic stay, the applicability of the RO Regime to SPCs, and the importance of a clear restructuring plan before asking the Court to engage its jurisdiction to appoint restructuring officers. It is clear that the Court is concerned with avoiding abuse of the new restructuring regime while also promoting consistency and certainty, albeit under a turbocharged framework.

This clarification will be especially important for foreign courts in considering whether to recognise and assist Cayman Islands restructuring officers in future. Foreign courts can take comfort in the fact that the Cayman Islands Court remains astute to guard against any abuse of the new regime by carefully analysing whether the statutory preconditions for appointment are met in the circumstances of each case.

The key to a successful restructuring, through the Cayman RO Regime or otherwise, will always be timely action, with the right advisor team to guide the process.

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2024 Amendments to the Delaware General Corporation Law and Alternative Entity Statutes

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On July 17, 2024, Delaware Governor John Carney signed into law the 2024 amendments to the General Corporation Law of the State of Delaware (the "DGCL"), the Delaware Limited Liability Company Act (the "LLC Act"), the Delaware Revised Uniform Limited Partnership Act (the "LP Act"), the Delaware Revised Uniform Partnership Act (the "Partnership Act"), and the Delaware Statutory Trust Act (the "Statutory Trust Act"). The LLC Act, the LP Act, the Partnership Act and the Statutory Trust Act are sometimes referred to as the "Alternative Entity Statutes."

Each of the amendments will become effective on August 1, 2024. Set forth below is a brief summary of the most significant changes contemplated by these amendments.

What You Need to Know:

Amongst other changes, these amendments:

- Codify a board of directors' ability to enter into stockholder agreements for minimum consideration;

- Clarify the approval process and notice requirements for certain corporate agreements;
- Authorizes the use of penalty provisions in merger agreements;
- Authorize inclusion of amendments in merger documents; and
- Confirm and clarify mechanisms for revoking termination or dissolution.

Delaware General Corporation Law

Authorization of Stockholder Agreements (DGCL § 122(18))

Newly-added Section 122(18) of the 2024 DGCL Amendments codifies the ability of a Delaware corporation's board of directors to provide contractual rights to stockholders, including the right to participate in certain decision-making on behalf of the corporation, in the form of a stockholder agreement. This new subsection is in direct response to a recent Delaware Court of Chancery Opinion, *West Palm Beach Firefighters' Pension Fund v. Moelis & Co.*, C.A. No. 2023-0309-JTL (Del. Ch. Feb. 23, 2024). In *Moelis*, the Chancery Court considered the validity of a stockholder agreement which delegated certain approval rights to the corporation's founder. The Court held the stockholder agreement was unenforceable because it constituted impermissible delegation of the board's managerial authority in violation of Section 141(a) of the DGCL. The *Moelis* decision prompted significant concern from Delaware corporate law practitioners regarding the implication of the decision more broadly on the common practice of entering into stockholder agreements, and the Court noted that "greater statutory guidance may be beneficial" in light of the "expansive" use of such agreements between corporations and their stockholders.

Section 122(18) now provides such guidance, expressly codifying a corporate board's authority to enter into stockholder agreements for minimum consideration and provides a non-exhaustive list of provisions which may be lawfully included in a stockholder agreement, including:

- Requiring the approval or consent of one or more persons or bodies (including the board of directors, or any current or future directors, stockholders or beneficial owners of stock) before the corporation may take a specific action;
- Restricting or prohibiting a corporation from taking an action specified in the agreement; and

- Agreeing that the corporation or one or more persons or bodies (including the board of directors or any current or future directors, stockholders or beneficial owners of stock) will take, or refrain from taking, a specific action.

Importantly, however, Section 122(18) does not allow for stockholder agreements that would bind the board or individual directors in their official capacities as parties to the agreement. Section 122(18) also provides that the corporation, and not any individual person (such as a director), may be subject to remedies for breach of the stockholder agreement. Moreover, the synopsis to Section 122(18) confirms that no agreement under that Section will be enforceable if it contravenes the certificate of incorporation of the corporation or Delaware law. That said, Section 122(18) provides an exception whereby a stockholder agreement which places a prohibition on a board will not be deemed unenforceable simply because the board is explicitly authorized to take the prohibited action in the certificate of incorporation.

Additionally, Section 122(18) provides that the board must receive consideration for entering into a stockholder agreement. The new subsection charges the board with determining the minimum consideration necessary for entering into such an agreement and provides examples of what may constitute such minimum consideration, including requiring stockholders to take or refrain from taking certain actions.

The amendments also make clear that nothing in the revised Section 122 disturbs directors' existing fiduciary duty obligations or impacts existing case law. Additionally, the amendments affirm that directors reserve all of the powers granted to them under Section 122 unless otherwise noted in the certificate of incorporation.

Board Approval of "Substantially Final" Agreements (DGCL §§ 147, 262 and 268)

New Sections 147, 262, and 268 of the 2024 amendments address issues surrounding board approval and notice of mergers and acquisitions following a recent Court of Chancery decision in *Sjunde AP-Fonden v. Activision Blizzard, Inc.*, C.A. No. 2022-1001-KSJM (Del. Ch. Feb. 9, 2024). The *Activision* case concerned the acquisition of Activision by Microsoft which, the plaintiff-stockholder argued, failed to comply with certain requirements of the DGCL. In particular, the plaintiff argued the Activision board failed to properly approve the merger because the merger agreement that was approved was not "final" and also failed to provide sufficient notice of the merger to stockholders. The Court held that the board must approve a final or "essentially complete" form of the merger agreement and concluded that the inclusion of a summary of the merger in a

proxy statement did not constitute proper notice. Likewise, the Court held that attaching the merger agreement to the proxy statement did not constitute proper notice because the agreement did not include the surviving corporation's certificate of incorporation—an essential document appended to the merger agreement.

With regard to merger approval, the 2024 amendments enact new DGCL Section 147, which provides that whenever a board is required to approve or take some action with regard to an agreement, instrument, or document, it must be in its final or substantially final form when approved or acted upon. Pursuant to the synopsis to Section 147, "substantially final" means all material terms must be included in the agreement, instrument, or document or readily ascertainable to the board through other materials. If any question remains at to whether an approved agreement, instrument, or document was "substantially final" at the time of approval, Section 147 allows a board to adopt a resolution ratifying the approval of or action taken regarding any agreement, instrument, or document that must be filed with the Secretary of State or referenced in any certificate. The ratification must occur before filing and is effective as of the date of the original approval or action.

Additionally, new Section 268(a) now allows merger agreements to exclude provisions relating to the certificate of incorporation of a corporation whose shares of stock will not be converted or exchanged in the merger, other than for shares of the surviving corporation's stock. Furthermore, new Section 268(b) clarifies that, unless explicitly provided for by the merger agreement, any disclosure letter and schedules regarding representations, warranties, covenants, or other conditions are not considered a part of the merger agreement under the DGCL. Accordingly, such documents may be negotiated without formal approval of the board and are not required to be included in the notice to stockholders, but still have any effects as provided in the merger agreement (such as qualifying representations and warranties).

Finally, new Section 232(g) clarifies the notice requirements to stockholders and provides any document enclosed with, annexed or appended to a notice is deemed a part of the notice. The synopsis to Section 232(g) further provides that the attached materials are considered a part of the notice for compliance purposes only and do not otherwise constitute "per se" materials to stockholders.

Penalty Provisions for Wrongful Termination of Merger Agreements (§ 261)

New Section 261 of the DGCL concerns the penalties and consequences for wrongfully terminating a merger agreement. Section 261 is in direct response to the Court of Chancery's ruling in *Crispo v. Musk*, C.A. No. 2022-0666-KSJM (Del. Ch. Nov. 4, 2023), wherein the Court considered the validity of a merger agreement provision which required the buyer to pay a lost premium to target stockholders for wrongfully terminating the merger. The Court deemed the provision invalid because a "target company has no right or expectation to receive merger consideration, including the premium," and, thus, "has no entitlement to lost-premium damages" if the merger falls through.

New Section 261(a)(1) explicitly provides that a merger agreement may include provisions which penalize a party who fails to comply with the agreement or execute the merger. Such penalties can include payment of lost premium or other economic advantages the stockholders of the non-breaching party would have been entitled to if the merger went forward. The synopsis to Section 261(a)(1) confirms that these provisions are enforceable notwithstanding any contract law to the contrary.

Section 261(a) also allows a corporation, if entitled to payment under the agreement, to enforce the obligations of the breaching party and collect penalties. Corporations are permitted to keep these payments and need not distribute them to stockholders, however, directors must still abide by their fiduciary duties in deciding whether to approve, perform or enforce a penalty provision. Lastly, Section 261(a)(2) allows for a stockholder representative to be appointed who can be authorized to enforce the rights of stockholders under applicable agreements.

Alternative Entity Statutes

Mergers & Consolidations

Several amendments were made to the Alternative Entity Acts with regard to filing requirements and documentation related to mergers and consolidations. These include:

- Domestic partnerships merging under Section 15-902(m) of the Partnership Act, which may not have previously filed a statement of partnership existence with the Delaware Secretary of State, are now required to file a statement of partnership existence prior to merging.

- The Partnership Act, the LP Act and the LLC Act have each been amended to provide that a certificate of merger or certificate of ownership and merger may include any amendments to the surviving entity's certificate of formation, certificate of registered series, certificate of limited partnership or statement of qualification, as applicable (including amending the relevant document in its entirety).
- The LP Act now requires each new general partner that is admitted via amendment to the certificate of limited partnership of a limited partnership surviving a merger to sign the certificate of merger or certificate of ownership and merger before it is filed with the Delaware Secretary of State.

Revocation of Dissolution/Termination

The LP Act and the LLC Act have each been amended to confirm and clarify certain of the mechanisms for revoking termination or dissolution of a limited liability company, limited partnership, protected series or registered series, as applicable. The amendments confirm and clarify that references to the term "other persons" in the LP Act and LLC Act in reference to dissolution or termination are references to other persons whose approval is required for such dissolution or termination of the limited liability company, limited partnership, protected series or registered series pursuant to the partnership agreement or limited liability company agreement, as applicable.

Amendments Specific to the Statutory Trust Act

Mergers & Governing Instrument Amendments

Section 3815(f) of the Statutory Trust Act has been amended to confirm that in the event of a statutory trust undergoing a merger or consolidation, an amendment to a governing instrument or the adoption of a new governing instrument may be effected only with respect to the governing instrument of the surviving or resulting statutory trust and not with respect to the governing instrument of a constituent statutory trust that is not the surviving or resulting statutory trust.

Voting of Securities Held by Statutory Trust

In response to the fact that many registered investment companies have implemented, or are considering implementing, forms of pass-through voting, Section 3608(p) of the Statutory Trust Act has been amended to confirm that the trustees of a statutory trust may authorize the beneficial owners of the statutory trust to direct the voting of

securities held by the statutory trust. A trustee shall have no duties or liabilities with respect to the voting of such securities if the trustees have exercised the standard of care required under the governing instrument or the Statutory Trust Act in connection with such direction given to the beneficial owners.

Conversion or Domestication to a Statutory Trust

The Statutory Trust Act was also amended to provide that in the event of a conversion or domestication of an entity into a Delaware statutory trust, approval of the conversion or domestication to a statutory trust, and the approval of the governing instrument of the statutory trust, are required to occur prior to the time a certificate of conversion or domestication to statutory trust becomes effective, rather than prior to filing of the certificate.

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Knowledge

Directors' duties under Cayman Islands law

17 June 2024

This briefing provides a general overview of Cayman Islands law as it relates to directors' duties. It is not intended to be comprehensive nor a substitute for professional advice in the context of a particular set of circumstances.

This briefing focuses on director duties, which will mainly arise in the context of Cayman Islands exempted companies. Duties of managers in the context of Cayman Islands LLC's and of general partners in the context of Cayman Islands exempted limited partnerships are not considered but will vary, potentially significantly, from the duties set out in this briefing.

Framework

As a general framework, Cayman Islands law is derived from the English common law and, therefore, regard must be given to the English common law principles and statues in conjunction with relevant decisions of the Cayman Islands courts, especially as the duties of a director are not codified under the law. Accordingly, directors' duties are governed by the Companies Act (as Revised) of the Cayman Islands (the "**Companies Act**"), any regulatory laws that apply, the common law and the memorandum and articles of association of the relevant company.

Role of directors

Whilst the role of a director may vary, a director will generally be responsible for the day-to-day management and control of the company. Where there is more than one director, the directors are expected to act collectively as a Board of Directors (the "**Board**") (except to the extent that the Board has delegated specific functions, e.g. to a managing director) and have the authority to manage the company in the company's best interests. Consequently, it is important that all transactions, associated agreements and documents are always considered and approved by the Board at a Board meeting or by written resolution signed by all directors. It is not appropriate for a single director or officer to approve or sign unless authority to do so has been conferred upon him at a Board meeting or by written resolution signed by all directors. Where a company has a sole director, it is still advisable for written resolutions to be executed to record decisions and maintain corporate governance standards, as well as to reflect the requirements of the Companies Act or under the articles of association of the company (the "**Articles**").

The first director(s) of the company are generally appointed by the subscriber to the memorandum of association. Thereafter, directors will generally be appointed by a resolution of the shareholders or a resolution of the directors. Depending on what the company's Articles provide, directors will either serve indefinitely or for a specified term after which they may be eligible for re-election to the Board. Most Articles provide that all powers of the company are vested in the directors, except for those specifically reserved to the shareholders, either under the Companies Act or under the Articles.

Board meetings

There is no specific requirement under general law as to the frequency with which Board meetings must be held (although, where economic substance legislation or a regulatory law or policy applies, there may be additional requirements and the Articles may also prescribe frequency). Instead, the law requires that Board meetings be held sufficiently frequently to enable the directors to fulfil their obligations to the company.

The company's Articles may specify the notice that must be given of a Board meeting. In the absence of any provision in the Articles,

reasonable notice must be given.

Subject to the company's Articles, Board meetings can be held via telephone or video conference or can be replaced by written resolutions signed by all directors. However, it is always important to obtain onshore legal advice to ensure that the method by which meetings are held or resolutions passed, or the physical location of directors during a meeting, does not give rise to tax or regulatory problems.

Voting at a Board meeting will generally be on the basis of one vote for each director present. If the company's Articles provide for it, the chairman may have a casting vote where the voting on any item of business is tied.

Subject to the company's Articles, a director can appoint a proxy or alternate to attend a Board meeting in their place. Typically, a proxy would be appointed to represent a director at one meeting or at meetings held during a limited time period, whereas an alternate would be appointed on a more long-term basis (e.g. if a director was sick). Filing requirements with the Cayman Islands Registrar of Companies may apply depending upon the terms of the appointment of the proxy or alternate.

It is always important to check that any Board meeting is quorate in accordance with the provisions of the company's Articles.

Because a director stands in a fiduciary position, under the general law, they must avoid any conflict of interest when carrying out their duties as a director. However, in practice, conflicts of interest will arise, and the Articles will usually permit a director who has a conflict of interest to nevertheless attend a Board meeting, be counted in the quorum and vote, provided that they have already fully disclosed their conflict of interest to the Board.

Fiduciary and common law duties

Directors are subject to several fiduciary duties, which may be summarised as follows:

- a director is expected to act in good faith and in the best interests of the company;

- a director should not exercise their powers for an improper purpose;

- a director should not fetter their powers;

- a director should not to misapply the assets of the company;

- a director should avoid conflict of interest; and

- a director should not make a secret profit from their position.

Each of these duties is owed to the company and derives from the fact that, under the law, a director is regarded as a fiduciary with obligations similar to those of a trustee. Generally, in this context the company will be represented by the interests of all of its shareholders. However, where the company is insolvent or of doubtful solvency at the relevant time, due regard must be given by the directors when exercising their duties to the interests of creditors of the company. Where financial loss arises as a result of a breach of any of the above duties, a director may be held personally liable to the company for such loss.

In addition to fiduciary duties, directors are subject to a common law duty of care and skill. This duty has, through a succession of judicial authorities in a number of English common law jurisdictions, been tightened over recent years and the approach in those cases has been affirmed by the Cayman courts. Generally, regard will now be given both to the knowledge, skill and experience that could reasonably be expected of the role that a particular director fulfils and to the actual knowledge, skill and experience that the particular director in question possesses, i.e. the test is both objective and subjective. This development in the law is a reflection of the commercial reality that it no longer suffices for a director to be simply a well-meaning amateur but, in most instances, it will be expected that they will be competent and experienced and will adopt a responsible and professional approach to the role.

A director may also be held personally liable where they have been fraudulent or have acted outside their authority.

Statutory duties (all companies)

Under the Companies Act, a director is subject to several statutory duties, which include, but are not limited to:

- Directors are required to keep proper minutes of all Board meetings. The minutes should be signed by the chairperson of the meeting and held on the company's minute book.

- The directors are responsible for ensuring that the company's register of members, register of directors and officers and register of mortgages and charges are kept up to date. The latter two registers must be kept at the registered office of the company in the Cayman Islands whereas, in the case of an exempted company (i.e. a company carrying on business mainly outside the Cayman Islands), the register of members can be kept anywhere.

- The directors must ensure that the company keeps proper books of accounts which reflect a true and fair view of the state of the company's affairs and explain its transactions. Please note that under Cayman Islands law, apart from regulated entities (e.g. investment funds, banks, trust companies, insurance companies, virtual asset service providers and the like) there is no requirement for accounts to be audited.

- A Cayman Islands company is subject to a number of filing requirements with the Cayman Islands Companies Registry, and it is the responsibility of the directors to ensure that these filings are made. Examples include: a change to the company's name, change of registered office, change in directors or officers, any amendments to the company's memorandum of association or Articles and the passing of any special resolution by the shareholders. Appointments of, or changes in, directors or officers must be filed within specific deadlines and failure to do so will lead to default penalties, which can be significant. Because of the importance of ensuring that all filings are made on a timely basis, it is essential that all minutes and resolutions, whether at Board level or shareholder level, are immediately provided by email to the registered office and the company's Cayman Islands legal counsel who will then attend to the necessary filings on behalf of the directors.

- An exempted company has a specific obligation to file an annual return with the Cayman Islands Companies Registry (together with an annual filing fee) confirming that, since the previous return or since registration, there has been no alteration in the memorandum of association (other than any alterations already reported), the company's operations have been carried on mainly outside the Cayman Islands and the company has not traded in the Cayman Islands with anyone except to further the company's business carried on outside the Cayman Islands.

Statutory duties of segregated portfolio companies

A segregated portfolio company (an "**SPC**") is a particular type of Cayman Islands exempted company which is able to create one or more segregated portfolios to segregate pools of assets and liabilities within a single company. Although a segregated pool may be thought of as a silo or sealed compartment within the company, each of them is not a separate legal entity in its own right. Directors of an SPC are subject to several specific statutory duties, which include, but are not limited to:

- The directors must have procedures in place to identify, segregate and keep separate any assets of one portfolio from the assets of another segregated portfolio ("**SP**"). Therefore, it is important that each SP has its own bank account, brokerage account, custody account, etc. Physical segregation rather than accounting segregation is also essential. Any co-mingling of assets across the portfolios are likely to compromise the integrity of the SPC structure.

- The directors must have procedures in place to ensure that any transfers of assets or liabilities between the portfolios are made at full value.

- Where an agreement, contract, deed or other document (collectively the "**documents**") is entered into by an SPC, the directors of the SPC are required to express execution of the documents as "by the [SPC] for and on behalf of the SP" or "by the [SPC] for the account of the [SP]" or "by the [SPC] in the name of the [SP]". The directors must also ensure that the documents

properly identify the relevant SP. Previously, directors of an SPC could incur personal liability as a result of failing to identify which segregated portfolio the SPC was contracting or transacting for. However, the Companies Act no longer deems such personal liability and provides instead a remedial procedure where such a failure does arise.

- Directors are required to make any necessary enquiries to determine the correct SP that the documents or transaction should be attributed to.

- Directors should make the correct attribution and notify all relevant parties in writing of the attributions and their rights. Any party notified, or any party who should have been notified, has the right to object to the court within 30 days of receiving the written notice about the attribution, and the court shall have the power to order the correct attribution to the relevant SP or general asset, or make any other ancillary order it deems just and equitable in the case.

Indemnification of directors and insurance

It is usual for the Articles of a company to indemnify the directors out of the assets of the company in respect of any personal liability that they may incur in acting as a director of the company. Generally, the indemnity clause excludes recovery where losses arise from a director's actual fraud or wilful default. With an increased focus on corporate governance, directors and officers liability insurance has become fairly common for directors.

Additional requirements for directors of regulated companies

In addition to the various responsibilities outlined above, the Directors Registration and Licensing Act (as Revised) of the Cayman Islands requires that individual and corporate directors of regulated mutual funds or other companies who are registered as 'registrable persons' under the Securities Investment Business Act, prior to being appointed as a director be either registered or licensed with the Cayman Islands Monetary Authority ("**CIMA**"). Directors of a private fund are not subject to the Directors Registration and Licensing Act.

A director of a company which is licensed by CIMA (e.g. a bank, trust company or insurer) must also have regard to CIMA's Statement of Guidance: Corporate Governance ("**the SOG**") which is designed to establish best practice guidelines for licensees with regard to corporate governance. The SOG underlines the critical importance of good corporate governance whilst recognising that the way standards are to be achieved may differ according to the licensee's structure, size and complexity. The SOG addresses such issues as Board composition, division of responsibilities, risk management and conflicts, audit function and regulatory compliance. Any director of a company licensed by CIMA should consider the SOG carefully.

For directors of an investment fund registered with CIMA under section 4(3) or 4(4)(a) of the Mutual Funds Act and those investment funds registered with CIMA under the Private Funds Act, specific guidance is given in CIMA's Statement of Guidance for Regulated Mutual Funds: Corporate Governance. The purpose of the guidance is to provide guidance on the minimum expectations for the sound and prudent governance of a regulated mutual fund or private fund, but it is not intended to be prescriptive or exhaustive. The guidance states that the size, nature, and complexity of a regulated mutual fund are fundamental factors in determining the adequacy and suitability of its governance framework. This provides guidance on various matters, including legal and regulatory compliance, oversight of service providers, conflicts of interest, frequency of Board meetings (a minimum of two Board meetings each year), communication with investors, number of directorships held, and various specific duties expected of a director of a regulated mutual fund or private fund. Any director of a regulated mutual fund or private fund should consider the guidance carefully.

If you would like any further information, please get in touch with your usual Bedell Cristin contact or one of the contacts listed.

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GLOBAL BONDS, LOCAL IMPACT: INTERNATIONAL BONDHOLDERS PARTICIPATION IN MEXICAN INSOLVENCY PROCESSES

AUTHORS: JAVIER GARIBAY, LEAH M. EISENBERG

Source: Pratt's Journal of Bankruptcy Law

In this article, the authors examine the critical role international bondholders play in the restructuring efforts of Mexican insolvent companies.

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Judge Wiles Sets Significant Hurdles for Chapter 15 Creditors Seeking Rule 2004 Discovery Via "Good Cause" Requirement

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On Dec. 12, 2023, Hon. Michael E. Wiles of the U.S. Bankruptcy Court for the Southern District of New York (the "Chapter 15 Court") denied a motion filed by creditor Sablon Partners Ltd. in the chapter 15 cases of Americanas S.A. and its debtor affiliates (collectively, the debtors), seeking authorization under Rule 2004 of the Federal Rules of Bankruptcy Procedure to obtain discovery from the debtors and certain third parties. [1] The Chapter 15 Court held that Sablon failed to establish "good cause" because it failed to first seek discovery in the debtors' home country of Brazil. [2] In so holding, the Chapter 15 Court made clear that Rule 2004 cannot be used as a substitute for the discovery process in a chapter 15 debtor's home jurisdiction, [3] and likewise that a chapter 15 creditor cannot circumvent the pending proceeding rule by simply choosing not to initiate a proceeding or ask for discovery in the home jurisdiction. [4]

Americanas' Brazilian Bankruptcy and Chapter 15 Proceeding

On Jan. 11, 2023, Americanas shocked the world when it issued a press release informing the public of "accounting inconsistencies" in the approximate amount of BRL 20 billion ($4.1 billion in USD). Within 10 days of this revelation, Americanas filed for bankruptcy in Brazil. On Jan. 25, 2023, Americanas filed its chapter 15 petition in the Chapter 15 Court.

In the ensuing months, numerous governmental investigations were conducted in Brazil concerning Americanas' alleged accounting fraud. At the same time, many of Americanas' creditors filed their own proceedings seeking discovery, but those proceedings were ultimately voluntarily stayed. [5] One creditor — Sablon — did not bring claims in Brazil and instead went straight to the Chapter 15 Court, asking for broad discovery from the debtors and certain third parties pursuant to Rule 2004.

The Rule 2004 Motion

On Nov. 10, 2023, Sablon filed its Rule 2004 motion, [6] explaining that it was seeking this discovery so that it could evaluate potential claims it believed it may have against the debtors and others. [7] Sablon argued that it had established "good cause" because it was seeking discovery "to investigate the Fraud and potential claims arising therefrom could substantially enhance the Debtors' estates and/or substantially reduce the claims against those estates" and because the Debtors had not initiated any actions related to these potential claims. [8]

In its reply papers, Sablon argued that, although there were proceedings pending in Brazil, the "pending proceeding rule" — which states that "'once an adversary proceeding or contested matter is commenced,' discovery should be sought pursuant to the rules of the contested matter" — did not bar Sablon's Rule 2004 motion because Sablon was not a party to any proceeding in Brazil. [9]

The Ruling

In an oral ruling issued on Dec.12, 2023, the Chapter 15 Court denied Sablon's Rule 2004 motion. The court sidestepped the question of whether Rule 2004 may generally be used by a chapter 15 creditor, [10] noting that "relief under Rule 2004, even if it's available, is discretionary [and] requires a showing … of good cause. And I do not find that good cause is established here." [11]

The court dismissed Sablon's "pending proceeding rule" argument and explained that the fact that Sablon had not sought discovery in Brazil actually weighed against granting Sablon's motion. [12] The court explained that "the pending proceeding rule would … lose a lot of its teeth if you could just say, well, I'm not even going ask in Brazil." [13] The court further held that it would be inappropriate for it to "decid[e] what discovery the parties should be entitled to in connection with" litigation in Brazil, especially where Sablon had no case pending there. [14] The court explained that "it is emphatically not my job to tell a Brazilian court what evidence it ought to be considering in doing what it is doing under Brazilian law, or in deciding for the parties what evidence they're entitled to, and discovery they're entitled to in connection with that proceeding. Those are all matters in the first instance for the parties and the courts in Brazil." [15]

Conclusion

As the Chapter 15 Court made clear, in a chapter 15 case it is the U.S. court's job to "assist in the enforcement of orders that might be entered in the home jurisdiction of the foreign debtor." [16] For a creditor of a foreign debtor that is seeking access to U.S. discovery, the process will likely be quite onerous, if not impossible, as the U.S. court will seemingly be dubious to grant such discovery unless it is doing so to "enforce" an order entered in the foreign proceeding — meaning that the creditor must first seek and obtain relief in the debtor's home jurisdiction, then bring the order before the U.S. court and explain why Rule 2004 is needed to "enforce" that order (and even then the creditor will have to contend with the pending proceeding rule).

While the Chapter 15 Court's ruling in *Americanas* left open the door for chapter 15 creditors to seek Rule 2004 discovery generally, the rubric it set forth for granting such a request significantly limits Rule 2004's usefulness to a creditor that is hoping to quickly obtain broad discovery into a foreign debtor (at least for chapter 15 cases pending before Judge Wiles).

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[1] *In re Americanas S.A.*, No. 23-10092 (MEW) (ECF No. 63). The author served as counsel to third parties LTS Investment Holdings LLC, LTS Investments Inc., LTS Trading Co. LLC and Cedar Trade LLC in matters related to the chapter 15 cases.

[2] *Id.* at 26-28.

[3] *Id.*

[4] *Id.* at 12:1-10.

[5] *Id.* at 6:11-16.

[6] *In re Americanas S.A.*, No. 23-10092 (MEW) (ECF No. 42).

[7] *Id.* ¶ 1.

[8] *Id.* ¶ 56.

[9] *In re Americanas S.A.*, No. 23-10092 (MEW) (ECF No. 59) at 12 (citing *In re Enron*, 281 B.R. at 840).

[10] Courts have often denied creditors the use of Rule 2004 on the basis that certain provisions of chapter 15 limit access to Rule 2004 discovery to the foreign representative. *See* 11 U.S.C. 1521(a)(4); *see also In re Sibaham Ltd.*, No. 19-31537, 2020 WL 2731870, at *4 (Bankr. W.D.N.C. May 4, 2020) ("If … Parties [other than the foreign representative] wish to obtain documents, they cannot do so in the context of an ancillary proceeding such as the Chapter 15 case.").

[11] *In re Americanas S.A.*, No. 23-10092 (MEW) (ECF No. 63) at 27:10-21.

[12] *Id.* at 13:3-11.

[13] *Id.* at 12:1-8.

[14] *Id.* at 13:12-14.

[15] *Id.* at 12:1-8. This reasoning is consistent with the principles of comity underlying chapter 15 and previously recognized by the Second Circuit in the insolvency context. *See, e.g.*, *JP Morgan Chase Bank v. Altos Hornos de Mexico S.A. de C.V.*, 412 F.3d 418, 424 (2d Cir. 2005) (explaining that "deference to the foreign court is appropriate so long as the foreign proceedings are procedurally fair and … do not contravene the laws or public policy of the United States").

[16] *Id.* at 27:22-23.

Faculty

Nicola Cowan is a director at FFP Ltd. in George Town, Grand Cayman, in the Cayman Islands and has more than 15 years of experience in insolvency and restructuring. Originally from the U.K., she has been based in the Cayman Islands since 2011 and specializes in providing independent fiduciary services and insolvency and restructuring advice to offshore registered funds and companies with extensive experience in number of investment strategies, such as structured finance, digital assets and other private-equity strategies. Ms. Cowan acts as a court-appointed official liquidator, court-appointed receiver and voluntary liquidator. She also has acted as a foreign representative in chapter 15 proceedings in the U.S. Ms. Cowan is a board member of a variety of offshore registered funds and companies. She is a Chartered Accountant and a member of the Institute of Chartered Accountants in England and Wales (ICAEW) and a Certified Director, accredited by ICSA Canada. She also is registered with the Cayman Islands Monetary Authority as an Approved Director. Ms. Cowan received her Bsc in management from the University of Manchester.

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Lucian (Luke) Murley is a partner with Saul Ewing LLP in Wilmington, Del. He has experience representing debtors, committees, acquirers, fiduciaries and other significant parties in interest in complex reorganizations and financially distressed situations, both in and out of court. Mr. Murley regularly advises financially healthy businesses that find themselves creditors in chapter 11 cases. He has represented creditors serving on official committees in recent chapter 11 cases such as Alpha Media Holdings LLC and Extraction Oil & Gas, Inc. Mr. Murley has been named in *The Best Lawyers in America* list for Bankruptcy Litigation since 2023, and he is a court-appointed mediator for Delaware. He received his B.Mus. in 1998 from Northwestern Universty and his J.D. in 2004 from the University of Kentucky School of Law, where he served as managing editor of the *Kentucky Law Journal* editorial board and received the Stoll, Keenon & Park *Kentucky Law Journal* Outstanding Service Award.