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The Structure of M&A Deals in the Cayman Islands

David Lamb at Conyers Dill & Pearman looks at Cayman Islands law governing the takeover (or privatisation) of public companies.

INTRODUCTION

This guide deals in general terms with certain aspects of Cayman Islands law governing the takeover (or privatisation) of public companies.

The Cayman Islands also has a stock exchange (the "CSX") and a Code on Takeovers and Mergers and Rules Governing Substantial Acquisitions of Shares which applies to all companies listed on the CSX apart from open-ended mutual funds. When a company listed on the CSX is also subject to primary regulations governing takeovers and mergers by a recognised stock exchange (as defined in the CSX listing rules) or other applicable law, then those primary regulations will generally govern the conduct of the takeover. Early consultation with the Council of the CSX is strongly recommended when transactions are subject to the dual jurisdiction of the CSX and an overseas regulator. The Cayman Islands Takeovers Code does not contain any compulsory acquisition or squeeze-out provisions.

REGULATIONS GOVERNING TAKEOVERS

- The Companies Law (2016 Revision) and other applicable legislation.
- Cayman Islands Code on Takeovers and Mergers and Rules Governing Substantial Acquisitions of Shares.
- Domestic Takeover Codes and Listing Rules when the shares of the target are listed or traded. These often impose additional thresholds which must be met before any compulsory acquisition can be effected.
- The memorandum and articles of association of the target and any shareholder rights plan or other material contracts.
- Domestic rules on disclosure and transparency, insider dealing, market manipulation and financial promotion.

GENERAL OFFERS

PROCEDURE AND ACCEPTANCES

A general offer for all the shares of the target or all the shares of a particular class must be made and accepted by the holders of at least 90% of such shares to enable the offeror to acquire the remaining shares compulsorily. Cayman law allows a maximum four-month offer period within which this level of acceptance must be reached.

COMPULSORY ACQUISITION NOTICE AND TIMETABLE

A compulsory acquisition notice seeking to acquire the remaining shares may not be served before the expiration of four months from the date the offer was made and must be served within a two-month window commencing on the expiration of this four month period. This means it will usually take a minimum of five months from the date of posting the offer document to complete the acquisition of 100% of the target (assuming no action is taken by any dissentient shareholders).

When a compulsory acquisition notice is given, the bidder is entitled and bound to acquire the shares of the remaining shareholders on the same terms as the general offer, unless an application is made by dissentient shareholders to the Grand Court and the Grand Court thinks fit to order otherwise.

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DISSENTIENT SHAREHOLDERS

An application may be made by any dissentient shareholders within one month of the date on which the compulsory acquisition notice was given to prevent the compulsory acquisition, usually on technical grounds. Dissentient shareholders do not have express appraisal rights whereby they could apply to the Grand Court to have the fair value of their shares appraised or assessed by the Grand Court, although the Grand Court has a broad discretion to make whatever orders it considers appropriate.

Within one month of the compulsory acquisition notice the bidder must send a copy of the compulsory acquisition notice to the target and pay the consideration to the target. If an application has been made to the Grand Court then this must be done within one month of that application being determined. The target is then required to register the bidder as the holder of the shares and to hold the consideration on trust for the dissentient shareholders.

SCHEMES OF ARRANGEMENT

PROCEDURE

A takeover by way of scheme of arrangement involves the target proposing a scheme to its shareholders to cancel their shares (a cancellation scheme) or to transfer their shares to the bidder (a transfer scheme) in return for cash or securities of the bidder. A cancellation scheme usually avoids stamp duty or documentary tax which would otherwise be payable on a transfer scheme (and on a general offer).

The board of the target will be in control of the scheme and be responsible for drafting the composite scheme document, making the applications to the Grand Court, mailing the composite scheme document to shareholders, holding the relevant meetings and making the necessary filings. The bidder will undertake to abide by the scheme and pay the scheme consideration.

INDICATIVE TIMETABLE

An indicative timetable setting out the major steps is set out below:
Day 1: File draft petition/summons for directions
Day 21: Directions hearing (depends on court availability)
Day 25: Despatch composite scheme document
Day 55: Court Meeting to approve the scheme and EGM to approve the reduction in capital (cancellation scheme)
Day 56: File chairman's report of the Court Meeting
Day 66: Petition hearing to sanction the scheme and capital reduction
Day 69: Effective Date - file court order with Registrar of Companies

SCHEME DOCUMENT

The composite scheme document will include the expected timetable, a letter from the board of the target, a letter from the independent directors or board committee, a letter from the independent financial advisers, an explanatory statement, financial and general information, the scheme of arrangement document itself and notice of the relevant meeting(s).

APPROVALS

A scheme of arrangement requires approval from the Grand Court as well as the approval of the directors (in practise).

All schemes must also be approved by a majority in number (head count) representing three-fourths in nominal value (share count) of the scheme shareholders voting at the requisite meeting which will have been convened pursuant to an order of the Grand Court.

The voting requirements of any applicable Takeovers Code must also be met.

In addition, the shareholders present and voting at the court meeting must represent a fair cross-section of the shareholders as a whole and every effort should be made to secure a good attendance by shareholders.

The statutory thresholds apply to each class of share. A class will be created if shareholders have rights against the target company which are so dissimilar as to make it impossible for them to consult together with a view to their common interest. The makeup of any classes will normally be settled at the directions hearing but this determination is not necessarily binding at the subsequent petition hearing.

The statutory majority of shareholders must also act bona fide with no coercion of minority shareholders and the scheme must be one that an intelligent and honest man acting in respect of his interests in the class might reasonably approve.

Unlike a general offer these thresholds cannot be reduced or waived; if they are not met, the scheme will fail.

EFFECTIVE DATE

The scheme will be effective when a copy of the court order is delivered to the Registrar of Companies for registration.

AMALGAMATIONS BY WAY OF SCHEME OF ARRANGEMENT

Amalgamations may also be effected through a "special" scheme of arrangement. The scheme of arrangement must have been proposed for the purpose of or in connection with: (i) the "reconstruction" or "amalgamation" of the bidder and the target; and (ii) the transfer of the whole or any part of the undertaking of any company concerned in the scheme of arrangement.

MERGERS AND CONSOLIDATIONS

MERGER

Merger means the merging of two or more constituent companies into a sole remaining constituent company (the "surviving company") and the vesting of the assets and liabilities of the constituent companies in the surviving company.

CONSOLIDATION

Consolidation means the combination of two or more constituent companies into a new consolidated company and the vesting of the assets and liabilities of the constituent companies in the consolidated company.

The cessation of a constituent company which participates in a consolidation or which is not the surviving company in a merger does not require a winding-up.

PROCEDURE

The directors of each constituent company must approve a written plan of merger or consolidation (the "Plan"). The Plan must contain certain prescribed information including the basis of either converting the shares in each constituent company into shares of the consolidated company or surviving company and the rights attached to the shares or cancelling those shares in exchange for the applicable consideration, any proposed amendments to the memorandum and articles of the surviving company in a merger, or the proposed new memorandum and articles of the consolidated company in a consolidation, details of all secured creditors and the effective date of the merger/consolidation.

APPROVALS

The Plan must be approved by a special resolution of the shareholders of each constituent company. Any other authorisation required by a constituent company's articles of association must also be obtained.

Shareholders do not need to approve a merger between a Cayman parent company and a Cayman subsidiary. For this purpose, a subsidiary is a company of which at least 90% of the issued shares entitled to vote are owned by the parent company.

The consent of each holder of a fixed or floating security interest over a constituent company is required unless this requirement is waived by the Grand Court.

Other consents (and filings) may be required, for example, under the Banks and Trust Companies Law, Securities Investment Business Law, Mutual Funds Law or Insurance Law.

FILINGS

The Plan must be filed with the Registrar of Companies, together with supporting documents including:

(a) a declaration:
  (i) of solvency (debts as they fall due);
  (ii) that the merger or consolidation is *bona fide* and not intended to defraud unsecured creditors of the constituent companies;
  (iii) of the assets and liabilities of each constituent company;

(iv) that no proceedings are outstanding and that no order has been made or resolution passed to wind up a constituent company or to appoint a receiver, trustee or administrator in any jurisdiction;

(v) that no scheme, order, compromise or arrangement has been made in any jurisdiction whereby the rights of creditors have been suspended or restricted.

(b) an undertaking that a copy of the certificate of merger or consolidation will be given to members and creditors of a constituent company and published in the Cayman Islands Gazette.

DISSENTIENT SHAREHOLDERS AND APPRAISAL PROCESS

A dissentient shareholder of a Cayman constituent company is entitled to payment of the fair value of his shares as assessed by the Grand Court upon dissenting to a merger or consolidation unless: (i) an open market exists for the shares on a recognised stock exchange or interdealer quotation system at the end of the dissent period (see below); and (ii) the merger or consolidation consideration consists of shares or depository receipts of the surviving or consolidated company, or shares or depository receipts of any other company which are listed on a national securities exchange or designated as a national market system security on a recognised interdealer quotation system or held of record by more than 2,000 holders on the effective date of the merger or consolidation. The exercise of appraisal rights will preclude the exercise of any other rights save for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.

THE FOLLOWING PROCEDURE WILL APPLY:

1. The dissentient shareholder must give written notice of objection (notice of objection) to the constituent company *before* the vote to approve the merger or consolidation.
2. Within 20 days of the vote approving the merger or consolidation, the constituent company must give written notice of the approval (approval notice) to all dissentient shareholders who served a notice of objection.
3. Within 20 days (dissent period) of the approval notice a dissentient shareholder must give a written notice of dissent to the constituent company demanding payment of the fair value of his shares.
4. Within seven days of the expiry of the dissent period or within seven days of the date on which the plan of merger or consolidation is filed with the Registrar of Companies (whichever is later), the constituent company, surviving company or consolidated company must make a written offer (fair value offer) to each dissentient shareholder to purchase their shares at a price determined by the company to be their fair value.
5. If the company and the dissentient shareholders fail to agree the price within 30 days of the fair value offer (negotiation period), then within 20 days of the expiry of the negotiation period the company must apply to the Grand Court to determine the fair value of the shares held by all dissentient shareholders who have served a notice of dissent and who have not agreed the fair value with the company.

The exercise of appraisal rights has been an increasing trend following the *Integra Group* case in 2015 and a number of other cases are in process.

EFFECTIVE DATE

The effective date of a merger or consolidation is the date the Plan is registered by the Registrar of Companies, although the Plan will usually specify the effective date and may provide for an effective date not exceeding 90 days after the date of registration.

EFFECT OF A MERGER OR CONSOLIDATION

All rights, benefits, immunities, privileges and property (including business and goodwill) of each of the constituent companies will vest in the surviving or consolidated company which will be liable for all debts, contracts, obligations, mortgages, charges, security interests and liabilities of each constituent company. Existing claims, proceedings, judgments, orders or rulings applicable to each constituent company will automatically apply to the surviving company or the consolidated company.

CERTIFICATE OF MERGER OR CONSOLIDATION

A certificate of merger or consolidation is issued by the Registrar of Companies which is *prima facie* evidence of compliance with all statutory requirements in respect of the merger or consolidation ■