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New Cayman Islands Restructuring Regime: Modern Land and a Modernised Approach

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Cayman Islands companies have dominated the restructuring news cycle of late for a variety of reasons, including recent judicial commentary as to the effect of obtaining recognition under Chapter 15 of the U.S. Bankruptcy Code.

Although there were recent indications by the Hong Kong Court to the contrary, the U.S. Bankruptcy Court has now clarified that, provided that a foreign court properly exercises jurisdiction over a foreign debtor in an insolvency proceeding, and the foreign court's procedures are appropriate, a decision of the foreign court approving a scheme or other restructuring plan that modifies or discharges New York law governed debt is enforceable and effective.

This recent clarification comes at a time when significant amendments to Part V of the Cayman Islands Companies Act (the "Act") are due to take effect and revamp the domestic restructuring regime. Amendments to the Act are set to introduce the role of a court-appointed "*restructuring officer*" and an originating process by way of a new "*restructuring petition"*. The commencement order for the amendments to the Act has been approved, with an effective date of 31 August 2022.

The restructuring officer regime will provide a clearer demarcation between distinct winding-up and rescue paths. As opposed to being required to present a winding-up petition with a view to then promoting

a restructuring, it will be possible to initiate restructuring efforts using a bespoke method with the benefit of a statutory moratorium effective from the time of filing the restructuring petition.

The recent case of Modern Land, involving cross-border recognition of a Cayman Islands scheme of arrangement, and the modernised Cayman Islands restructuring framework are discussed below.

The Recent Example in Modern Land

Modern Land (China) Co., Ltd. ("Modern Land") is a company incorporated in the Cayman Islands and has shares listed on the Hong Kong Stock Exchange. Modern Land is the holding company for a group that conducts real estate investment and development in China and the U.S.

When faced with liquidity issues, Modern Land sought to adopt a conventional approach to restructuring certain major debt by proposing a scheme of arrangement in its place of incorporation. New York law-governed notes were the subject debt instrument. Once the scheme was approved by the Cayman court, Modern Land applied for recognition of the scheme under Chapter 15 of the U.S. Bankruptcy Code.

The application was made in the U.S. a short time after a decision of the Hong Kong court, which involved the recognition of provisional liquidators and the approval of a scheme of arrangement for Rare Earth Magnesium Technology Group ("Rare Earth"), a Bermudian-incorporated company. In that case, Rare Earth and the provisional liquidators pursued a debt restructuring which led to a scheme of arrangement being put forward and sanctioned in Hong Kong.

In the course of delivering reasons in relation to the Rare Earth sanction order, some *obiter dicta* remarks were made in relation to the effect of recognition via Chapter 15 of the U.S. Bankruptcy Code. It was suggested that, as the Rule in *Gibbs* provides that a debt is treated as discharged only if it is compromised in accordance with the law of the jurisdiction which governs the law of the debt, a substantive proceeding may be required in that jurisdiction to safeguard against potential attacks elsewhere. It was indicated that Chapter 15 may not be treated as substantive in that it does not itself operate as a compromise or discharge of U.S. governed debt.

Accordingly, it was said that an "offshore" scheme of arrangement (e.g., in Bermuda or the Cayman Islands) merely recognised in the U.S. may not bind a creditor (e.g. in Hong Kong) who did not participate in the foreign scheme of arrangement process.

Subsequently, in the context of the Modern Land decision, the U.S. Bankruptcy Court stated that certain of the Hong Kong Court's comments in Rare Earth were not correct as a matter of U.S. law. The U.S. Bankruptcy Court held in Modern Land that a Cayman Islands scheme of arrangement recognised as a main proceeding under Chapter 15 would constitute a substantive discharge of New York law governed debt. This is an important clarification for restructuring lawyers and officeholders.

A Potential Benefit of Appointing Officeholders

It is worth noting that, after receiving supplemental submissions and evidence on the point, the U.S. Bankruptcy Court was satisfied that Modern Land had its centre of main interests (COMI) in the Cayman Islands and that the Cayman scheme could be recognised as a "foreign main proceeding." As a matter of U.S. law, under Chapter 15, the debtor's registered office is presumed to be the centre of the debtor's main interests, although this presumption can be rebutted.

As noted in the Modern Land opinion, neither Modern Land nor any of its creditors had presented a winding up petition in the Cayman Islands. There were also no independent court-appointed officeholders overseeing the process. Instead, Modern Land had negotiated a restructuring support agreement and proceeded with a consensual scheme of arrangement on that basis.

In determining whether COMI was in the Cayman Islands, the U.S. Bankruptcy Court observed in Modern Land that the debtor would have had an "*easier case if [officeholders] had been appointed*" in the Cayman Islands. This is consistent with the analysis in prior cases involving Cayman Islands companies before the U.S. Bankruptcy Court, such as *Fairfield Sentry* and *Suntech Power Holdings*. Therefore, aside from the obvious benefits of fiduciary oversight and court protection, it is clear that, from a U.S. perspective at least, appointing independent officeholders may help with establishing a presence and connection to a particular jurisdiction.

A Modernised approach

In light of the decision in Modern Land and the current focus on restructuring the debt of Cayman Islands companies, the new restructuring officer regime is timely and should form a key part of the options analysis for directors and advisers to Cayman Islands companies.

Some of the important features of the new regime are that:

- 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 restructuring 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

- The moratorium will arise on presenting the petition seeking the appointment of restructuring officers, rather than from the date of the appointment of officeholders

- The default position is that this will be an *inter partes* process with adequate notice to be given to all stakeholders

- The powers of a restructuring officer will be flexible and will be defined by the terms of the appointment order made by the Cayman Court. 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

- 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

Under the new regime, if there is a feasible proposal to put to stakeholders and a restructuring officer is appointed, an application to sanction a compromise or arrangement with creditors and/or members may be made in the restructuring proceedings without the need to commence separate proceedings to promote a scheme of arrangement under section 86 of the Companies Act. If the restructuring fails and the company is ultimately wound up, the winding up will be deemed to have commenced from the date of presentation of the restructuring petition. Accordingly, whether successful or unsuccessful, there will be an efficient route to a sensible outcome.

Although legislators around the world sought to give directors breathing space during the global pandemic, those are not permanent measures. As the world begins to return to some level of normalcy, directors would be wise to reassess any cavalier tendencies that have developed while management has had the benefit of a “safe harbour” or perceived “free pass.” The key to a successful restructuring, through

the restructuring office regime or otherwise, will be timely action with the right advisor team to guide the process.

As highlighted by the decision in Modern Land, a Cayman Islands restructuring process—together with recognition abroad (as necessary)—will continue to be a sensible and effective method by which large, multinational groups may seek to reorganise their debt and other affairs.

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