Cross-Border Restructuring: The Cayman Islands Option

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Introduction

The global economy is increasingly cross-border in nature, and so are restructurings of companies with a presence in multiple jurisdictions. This manifestation of globalisation can raise some particularly challenging issues if the company finds itself in financial difficulty. The issues are even more acute if the company is incorporated in a jurisdiction without a sophisticated restructuring regime.

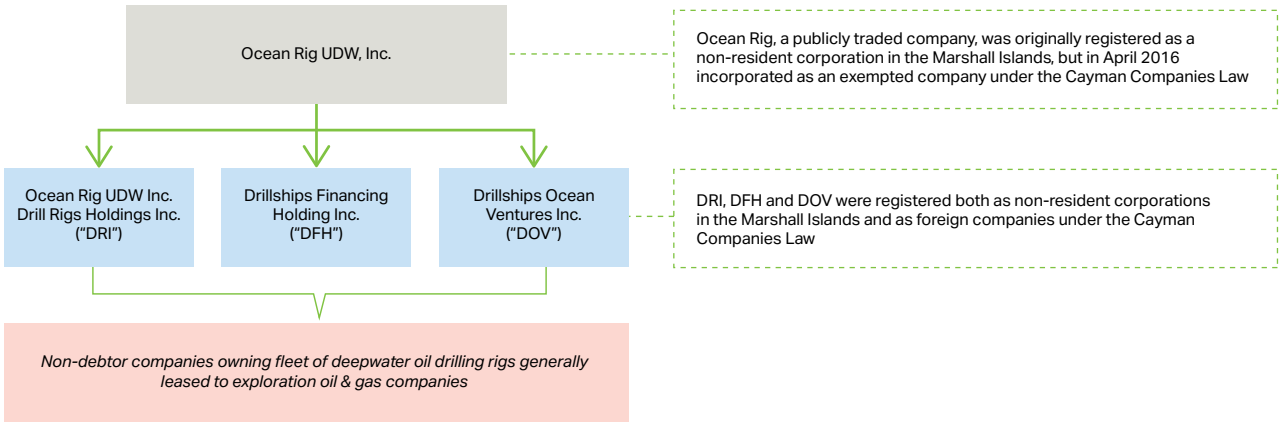
In such circumstances, the company in question will often look for solutions offered by other available jurisdictions. For example, it has become common for the Courts in England to approve a scheme of arrangement in respect of a foreign company. Alternatively, a company may look to Chapter 11 in the United States of America. However, in cases where Chapter 11 or an English scheme may not be appropriate (for example, due to cost, lack of jurisdictional nexus, timing or adverse tax consequences), the recent Ocean Rig restructuring demonstrates that the Cayman Islands provides another option for high profile, complex, cross-border restructurings.

Cayman Scheme

A scheme of arrangement is specifically provided for under the Companies Law in the Cayman Islands (the "**Cayman Companies Law**"). Generally, the provisions are the same as those set out in the Companies Act in England. Accordingly, the process involves the approval of the scheme by each class of the affected creditors/members (by a majority in number representing 75% in value of those voting at the relevant meeting) and the subsequent approval of the scheme by the Court. The Cayman Islands' Court will normally follow English case law where there is no local precedent available, meaning there is a very high degree of certainty as to how the Cayman Court will approach any restructuring.

As with an English scheme, once effective, a Cayman scheme binds all creditors/members, including any dissenters to the proposals, but it is worth noting, like in an English scheme, a Cayman scheme will only be effective where each class of creditor/member approves the scheme. Accordingly, unlike under Chapter 11 (where a plan may be confirmed even with respect to a non-accepting class, subject to certain circumstances), if any class of creditors/members that is affected by the scheme does not approve the scheme, the Cayman scheme will be defeated.

Ocean Rig Corporate Structure



Ocean Rig

Ocean Rig UDW Inc. ("**Ocean Rig**") is an international offshore deep-water drilling contractor which recently completed a complicated and high profile restructuring in the Cayman Islands comprising four schemes of arrangement. It involved an exchange of approximately U.S.$3.7 billion of debt for new equity in the company, U.S.$450 million of newly issued debt and U.S.$288 million in cash.

The four relevant companies in the Ocean Rig structure were all initially incorporated in the Marshall Islands (a parent and three subsidiaries). In order to take advantage of a Cayman scheme of arrangement, which in contrast to the Marshall Islands offered a legitimate opportunity for restructuring as opposed to liquidation, the parent company transferred its incorporation to the Cayman Islands prior to the restructuring proceeding and the three subsidiaries each registered in the Cayman Islands as foreign companies under the applicable provisions of the Cayman Companies Law.

With these registrations, the four foreign companies were provided the jurisdictional gateway to take advantage of the Cayman Companies Law. The resulting Cayman proceedings were subsequently recognised as foreign main proceedings under Chapter 15 of the U.S. Bankruptcy Code in August 2017 (which recognition necessarily included a finding that the "center of main interests" or "COMI" for all four debtors was in the Cayman Islands). One month later, in September 2017, the Chapter 15 court entered a separate order making the approved Cayman schemes binding and enforceable in the U.S.

An important and useful element of the Ocean Rig restructuring was that the companies were able to obtain a moratorium on claims both in the Cayman Islands and in the United States prior to the scheme being presented to the creditors. The reason for this is that the Cayman Companies Law allows a company to seek the appointment of a provisional liquidator where a company is or is likely to become unable to pay its debts *and* intends to present a scheme of arrangement. The

Chapter 15 COMI Considerations

- In making its COMI determination, the Chapter 15 court relied on, inter alia, the lack of any real connection to the Marshall Islands aside from initial incorporation / registration, and the actual activities of the debtors in the Cayman Islands (such as board meetings). Importantly, the court also addressed challenges to allegations that the pre-filing shift of COMI to the Cayman Islands was bad faith COMI manipulation.
- In determining that the COMI shift was done in good faith in order to gain access to a restructuring regime that provided for more options than just a liquidation, the court stated that "[t]he only provisions under [Marshall Islands] law that address financially distressed corporations…contemplate dissolution and, therefore, any insolvency in the [Marshall Islands] would invariably result in a value-destroying liquidation process. Accordingly, the [debtors'] COMI shift to the Cayman Islands was done for legitimate reasons, motivated by the intent to maximize value for their creditors and preserve their assets. The Court finds that the [debtors'] COMI was not manipulated in bad faith." *In re Ocean Rig UDW Inc., et al.*, 570 B.R. 687, 707 (Bankr. S.D.N.Y. 2017).

benefit of this provision, as was seen in Ocean Rig and several other restructurings in the Cayman Islands,[1] is that where a provisional liquidator is appointed, there is an automatic stay preventing any claims from being brought or continued against the company. Not only does this give a company valuable breathing space in the Cayman Islands, the provisional liquidator's appointment can also be recognised under Chapter 15, thereby enabling the provisional liquidator to obtain similar relief from the U.S. Bankruptcy Court (often by way of provisional relief while a motion for recognition of a foreign main proceeding remains pending, after which such relief is automatic). This, in turn, also gives a company invaluable breathing space in the U.S. while it formulates its restructuring proposals. Upon the successful conclusion of the restructuring, the provisional liquidator is discharged. Ultimately, once presented, 100% of Ocean Rig's participating creditors approved the scheme for each of the Marshall Islands entities and 98% approved the scheme for the parent company.

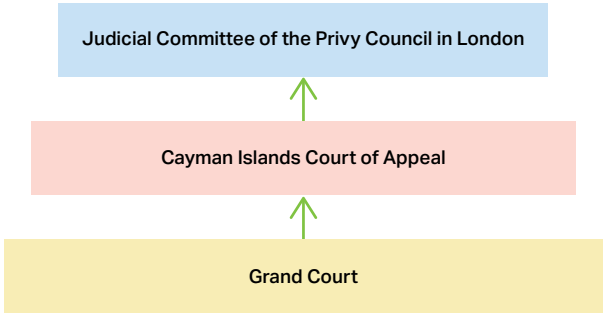
When to use the Cayman Scheme?

We do not expect the Cayman scheme to displace the use of English schemes of arrangement or Chapter 11. However, it may become an attractive option to entities that can demonstrate that their COMI is in the Cayman Islands, which at this point is a growing group, as nearly 100 Latin American companies (public and private) in Standard & Poor's Capital IQ database have direct subsidiaries in the Cayman Islands.[2] Additionally, the Cayman scheme may be attractive in restructurings where its benefits outweigh the use of Chapter 11 and in circumstances where an English scheme may not be appropriate, for example if shifting the COMI of the relevant company to England would cause adverse tax consequences.

By its nature, the Cayman Islands lends itself to transactions involving a cross-border fact pattern. One of its biggest advantages is that it provides neutrality for all parties to the transaction by eliminating any bias brought by home field advantage—neither creditors nor debtors will suffer any disadvantage by having the case decided in an opposing party's home jurisdiction. This is particularly acute in transactions involving multiple counterparties in multiple jurisdictions with often conflicting legal systems.

In addition, the Cayman Islands is a leading international finance centre, which is supported by a sophisticated and comprehensive infrastructure of professionals and advisers. Due to the nature of the jurisdiction and its extensive use in the financial services industry, the Cayman Islands Courts hear a very large number of cases relating to cross-border disputes and restructurings. In addition, the ultimate Court of Appeal is the Judicial Committee of the Privy Council in London. This provides a huge amount of legal certainty to all participants.

Cayman Islands Appeal Structure



The scale, complexity and successful execution of the Ocean Rig restructuring sets a precedent for the use of the Cayman Islands scheme in other cross-border restructurings. It has put the Cayman Islands firmly on the restructuring map. ■

Advantages to a Cayman Islands Scheme of Arrangement

— Similarity to U.K. Scheme of Arrangement and reliance on English law where no local precedent exists → high level of predictability in outcomes

— Allows for relief through Chapter 15 → preclude dissenting creditors from bringing competing insolvency proceedings and seeking to attach assets in the United States

— Low country risk → political and economic stability for companies domiciled in Cayman Islands and proceedings located there

1. Examples include the CHC Group restructuring, involving U.S.$1.6 billion in outstanding debt obligations, the ATU Group restructuring, which is believed to be Cayman's first ever "pre-pack" restructuring, the LDK Solar restructuring, involving U.S.$700 million in debt obligations and the Mongolian Mining restructuring, involving U.S.$760 million in debt obligations.
2. S&P Global Market Intelligence, Capital IQ Database (2012) (last visited February 16, 2018). The potential for using the Cayman Islands to effectuate cross-border restructurings takes on particular significance when considering that foreign companies can meet the jurisdictional requirements of the Cayman courts by, *inter alia*, paying a de minimis fee (approximately U.S.$1,600 as of January 1, 2018) to register as a foreign company (although Cayman courts do retain discretion to reject jurisdiction depending on the determined level of contacts with the Cayman Islands). Moreover, past cases demonstrate that the courts have taken a pragmatic approach to jurisdiction, and will typically not find forum shopping objectionable where the Cayman scheme is being pursued for legitimate purposes, such as the benefit of creditors.

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She specialises in both corporate and finance work, with a focus on private equity, investment funds, structured finance and capital markets. Prior to joining Mourant Ozannes, Jennifer worked in-house at Wells Fargo in London where she advised on a broad range of finance matters including securities, M&A, structured finance, bank lending, energy and financial regulatory work. Before Wells Fargo, Jennifer was at Cleary Gottlieb Steen and Hamilton LLP.