THE ELEVENTH INSOL/UNCITRAL/
WORLD BANK JUDICIAL COLLOQUIUM
SAN FRANCISCO, MARCH 2015.

FORUM SHOPPING IS BAD; CHOICE OF FORUM IS GOOD?
- THE INVESTMENT FUND PERSPECTIVE -

When the captioned question is asked in relation to imminent insolvency proceedings, we see from the research of Irit Mevorach[1], that one could posit the answer: *"…it depends on what are the motives or objectives of those who seek to change the forum of the insolvent or troubled entity*".

If their objective is to benefit from advantages which a different legal regime would offer for the restructuring of the entity to preserve value for shareholders, or as in the case of the United States Chapter 11 debtor-in-possession regime, to get "*breathing space*" for re-financing; then a change of forum or "forum shopping" may be both necessary and permissible. So also, if the objective is to maximize returns for investors or creditors because a different legal regime has more modern provisions for schemes of arrangement and compromise.

[1] "Forum Shopping in times of Crisis: A Directors' Duties Perspective", by Irit Mevorach, Associate Professor, University of Nottingham. At risk of over-simplification, other writers appear to take a similar view. See, for instance: Adrian Walters and Anton Smith: "Bankruptcy Tourism under the EC Regulation on Insolvency Proceedings: A view from England and Wales". International Insolvency Review Vol 19 No.3, 2009. And Cross Border Insolvency, COMI Shifts: An entitlement under E.U. Fundamental Freedoms?, By Deabhaile Banahan, Universidade Catolica Portugesa, Global Law School, Dissertation 30 Nov 2012, concluding…"if a debtor shifts its COMI for pure liquidation purposes, not intending in any way to save its business, or pursue a genuine economic activity, but merely to benefit from a more debtor friendly regime to the detriment of its creditors, then this will be considered an artificial arrangement and restrictions placed on the shift of COMI in such circumstances will be justifiable because the shift of COMI would be fraudulent and abusive"

A Paper presented to the INSOL Judicial Colloquium,
At San Francisco, 21-22 March 2015
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However, as the antithesis, forum shopping will be deemed unacceptable where the objective is fraudulent or abusive, including where the objective is to "steal a march" on other creditors or investors by obtaining an undue preference over assets of the insolvent entity[2].

All such objectives, whether good or bad, will however be informed by the nature of the business of the entity involved. Although this is axiomatic, examples which come readily to mind can be illustrative.

In the European Union context, there are a number of reported examples of relocations to the UK on the brink of insolvency from elsewhere within the European Union, apparently because of the attractiveness of the UK's voluntary arrangement procedures and pre-pack administrations for the restructuring of failing enterprises[3].

I am asked to address a gathering of fellow insolvency judges on this subject, it being understood, of course, that my perspective is that of a Cayman Islands judge, informed by the kind of insolvency or restructuring business coming before the Cayman court.

These days, a company carrying on international business from within the Islands would typically be one of four kinds:

[2] As the UK Privy Council recently found to be the case with the Shell Pension Fund's attempt through the Dutch Court to garnish and attach assets of the Fairfield Sentry Fund in liquidation at its place of incorporation in the BVI, assets which were held by the Dutch Citco Bank as custodian, at its branch in Dublin Ireland. Shell's blatant attempt at forum shopping was restrained by a world-wide anti-suit injunction in aid of the BVI liquidation and Shell was required to prove its claim there, along with those of all other claimants, in keeping with the principle of universalism. See: *Stichting Shell Pension Funds (Appellant) v Krys et al* [2014] UKPC 41.
Also as foreshadowed at paras (29) –(31) of the commentary on the proposed new E.U. Regulations on Cross-Border Insolvency set to come into effect in June/July 2015: E.U. Council Communique 16636/14, Brussels 26 February 2015, setting out the position of the Council at First Reading of the Draft Regulations.

[3] See for example *Re European Directories(DH6)BV [2010] EWHC 3472 (Ch)* ; *Re Hellas Telecommunications (Luxembourg 11 SCA [2009] EWHC 3199 (Ch))*; *Gallery Capital S.A (2010) WL 4777509*.;

1. a holding company having subsidiaries in other places such as the BVI, owning and carrying on enterprises of different kinds in still other places, such as the PRC or Latin America;

2. an SPV set up for the purposes of a joint venture or to hold assets such as aircrafts or ships or to conduct business as a captive insurer;

3. an asset holding company underlying a large family discretionary settlement; or

4. a hedge fund company serving as the corporate vehicle for a feeder or master fund structure and whose assets are invested in markets around the world;

There are of course, other kinds or categories of companies to be identified by reference to their use but for present purposes, these four broad categories will serve as a fair summary of the use of Cayman companies.

Of these four categories of companies I will discuss the fourth in particular – that which has involved the most significant body of insolvency litigation – the hedge fund or investment fund company. There are some 10,000 investment fund companies registered in the Cayman Islands. They hold something in the order of 70% of all assets invested worldwide in hedge funds. They are established in Cayman as the *choice of forum* for a number of good reasons. These include the availability of competent legal, accounting and other professional services; direct access to capital markets through the banks and other financial houses located in Cayman; the well-established, predictable and independent legal and judicial systems based on British Law; and of course, the absence of corporate profit or capital gains taxes.

Despite such well known and acceptable reasons for choice of forum, there have been cases in which hedge fund liquidators appointed by the Cayman courts have been refused recognition in the United States by the strict – some would say too strict – application of the COMI principles[4], such that the rights and expectations of investors are not consistently addressed by the grant of recognition under the United States Bankruptcy Code ("USBC"); and despite Chapter 15's lineage from the UNCITRAL Model Law ("the Model Law").

Article 17 of the Model Law is designed to enable the courts of different countries to render assistance to each other, even while addressing the problems presented by improper forum shopping and by the conflict of laws challenges posed by choice and change of forum. Towards those ends, for the purposes of granting recognition to a foreign proceeding as a "main" or "non-main" proceeding, the determination of the center of main interest ("COMI") or the requirement of an "establishment" in the foreign jurisdiction in which the debtor is the subject of the proceedings, is of the essence of the Model Law.

The objective of this paper is not to argue other than that the Model Law provides a rational basis and practicable basis for the grant of recognition.

However, in the case of an investment or hedge fund company, too strict an application of the "COMI" or the "establishment" test can operate to deny recognition and assistance to foreign representatives on entirely artificial bases and such that the interests of those who are entitled upon insolvency can be unfairly hampered or even denied.

[4] See below, in respect of the *Bear Stearns* and In *Re Basis Alpha Yield* cases.

As originally drafted, it must be doubtful that the Model Law was intended to be applied as a strict code so as to deny recognition in cases where the application of comity would have readily resulted in the grant of recognition. As the Guide to the Enactment of the Model Law explains, the purpose of Article 17 is to indicate that, if recognition is not contrary to the public policy of the enacting State and if the application meets the requirements set out in the article, recognition will be granted as a matter of course (emphasis added). This philosophy of the Model Law is hardly consistent with an overly strict view of the requirements either of the "COMI" or the "establishment" test of Article 17[5].

A central theme of my discussion will be to examine the concerns which arise for the liquidation of investment/hedge fund companies and of course, for their investors; where an overly strict application of the COMI test operates to deny recognition to a foreign liquidation of such a company.

I begin with the well-known *Bear Stearns* case. Certain *Bear Stearns* funds were established using Cayman Islands companies as a master/feeder hedge fund structure. Investors from around the world were invited to invest on the basis, apparent from the Funds' constitutional documents, that the Funds were domiciled in the Cayman Islands and so that Cayman Law would govern them. Having been hugely successful in attracting investors, the funds became over-exposed to collateralized mortgage debt and collapsed with the rest of that market during the 2008 financial crisis. There were allegations of fraud and breach of fiduciary duties against the promoters and

[5]The writer notes however, that the Model Law was revised in July 2013 to provide that COMI is determined as at the date of commencement of the foreign proceedings. Thus, apparently precluding activities developed during and for the purposes of the liquidation proceedings themselves, from being considered as giving rise to COMI; but Cf: Fairfield Sentry Ltd in the USC 2ND Circuit (below).

investment managers of the Funds. They had carried on the management and control of the assets, not from within the Cayman Islands but from New York; where the real base of operations was maintained and the bulk of the records were kept.

But not everything was done from New York. In addition to the registered offices of the Fund companies being in Cayman as their place of incorporation, certain directorship services, certain basic administrative services and the annual audits were conducted form Cayman and by the time of the liquidation, significant amounts of assets had been relocated to Cayman. Requests from investors for redemption of their shares were, as with the typical Cayman fund, submitted to the Cayman based administration but most important of all though, as one might think, the Funds had been placed in liquidation and were under the supervision of the Cayman court as the court of their place of incorporation.

It may be regarded as surprising given those circumstances, and when viewed from the point of view of private international law as now embodied in the principle of "modified universalism"[6], that the New York bankruptcy Court refused to grant not only recognition of main proceedings, but also of its own motion[7], refused to find that the Funds had an "establishment" in the Cayman Islands and so refused also to grant the Cayman liquidation proceedings recognition as foreign non-main proceedings.

[6] As articulated in the Cambridge Gas case, see below.

[7] In Re Bear sterns High-Grade Structured Credit Strategies Master Fund Ltd, 374 B.R. 122 (Bankr. S.D.N.Y 2007) (Upheld on appeal to the District Court). The Petition was unopposed. The Court cited the dictum of Learned Judge Hand from *United States v Marzano149 F.2d 923, 925 (2nd Cir. 1945) that "A judge is more than a moderator; he is charged to see that the law is properly administered, and it is a duty which he cannot discharge by remaining inert".* The court also pointed out that the Guide to the Application of the Model Law explains that while Article 16 establishes presumptions, they do not prevent an enquiry leading to their rebuttal if the conclusion suggested by the presumption is called into question by the court or an interested party.

In coming to its decision, the New York Court reversed the presumption in section 1516 Company of Chapter 15 [reflecting Articles 2 and 17 of the Model Law] that the debtor's registered office is its center of main interests. The Court declared, as a matter of American Law, that the presumption should be applied only in cases where there is no serious controversy (especially in order to permit and encourage fast action in clear cases) and that the burden of proof was upon the foreign representative, in controversial cases, to demonstrate COMI or to show that there was an establishment. As expressed in the judgment of the Court, even if raised from no other source, that "controversy" could be raised by the Court itself.

Having thus raised its own concerns, the Court held that principles of comity as hitherto understood, had been replaced by the concept of "recognition" as required by Chapter 15 and that recognition had to be distinguished from relief, although the latter could not be obtained without the former. Further, that it is at the stage of considering whether and if so, what kind of relief should be given, that comity would guide the exercise of judicial discretion.

In arriving at its decision, the New York District Court also discussed the European case in *Re Eurofood IFSC Ltd* 2006 E.C.R. 1-3813 and the English case in *Re Daisytek-Isa Ltd* [2003] All E.R. (d) 312; and concluded that both those cases were consistent with its analysis and application of the COMI test as one requiring the Court itself to be satisfied that the test is met even in the absence of any partisan objection[8].

[8] It is worth noting though, that in *Eurofood,* the ECJ, while agreeing that the COMI was ascertainable by reference to where the head office functions were carried out, also emphasized that COMI also had to be "objective and ascertainable by third parties". In other words, the presumption regarding the location of the place of the registered office could be rebutted upon it been shown that the debtor regularly administered its interests elsewhere in a manner that is ascertainable by third parties, which, in the case of the head office location of

This analysis presents stark difficulties for investment fund companies which conduct their different functions in different places. The difficulty with the overly-strict application of the COMI test is that it does not reflect the objectives for which investment funds are properly established and operated and the fact that their liquidators applying for recognition from a place not readily regarded as their COMI will not necessarily involve improper forum shopping. In order to maximize returns as one of the benefits obtained from being established in a jurisdiction like the Cayman Islands,investment funds are established in the Cayman Islands as a matter of *choice of forum* for the advantages only briefly mentioned in passing above. The choice of forum is important to the investors' decision to invest and reflects their expectation that Cayman law will apply to the liquidation of their investments if things go wrong.

In order to achieve these objectives, it is often neither necessary nor desirable that the Funds should have to establish a center of main interest in the traditional sense defined in Chapter 15 or the Model Law, within the Cayman Islands. What is necessary is that the transactional documents, like the Fund itself, are compliant with and governed by Cayman Law and that investments and returns to investors are properly booked as rendered in Cayman in keeping with its laws. Hence, for instance, the requirement that the Funds must be audited by the established accounting firms in keeping with generally accepted accounting standards, within the Islands. To

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Eurofood in Italy did not happen and so Ireland was held to be the COMI. The fact that the parent company Parmalat in Italy could control the economic choices of its subsidiary in Ireland was not enough to rebut the presumption that the COMI of the subsidiary was in Ireland where it was registered.
In Re Daisy-tex, the COMI test was satisfied so as to allow that Group to enter into administration under the English statutory regime notwithstanding that some members were registered in France and Germany. The English court, in determining that the COMI of the Group was in England, took into account that the head office in Bradford, England had negotiated 70% of the supply contracts for the French and German companies so that the majority of creditors by value would regard Bradford as the COMI; moreover, two of the UK parent companies had given guarantees to many of the suppliers in respect of French and German debt, providing a further link to the UK.

the extent the books and records are not all kept or available within the Islands, what this requires in practice is that the auditors must be given access to them wherever they may be.

And there is no lack of transparency in any of this. Not only are there well-established tax information exchange agreements ("TIEAs") with all the major jurisdictions in which the Funds operate or invest, but when returns are maximized due to the absence of corporate and capital gains tax and dividends paid to investors, their obligation to declare and pay taxes which are due in their countries of domicile are in no way diminished.

These are obligations moreover, which the TIEAs will help to enforce. But all that aside, what is crucial for the success of the Funds, is that they are regarded internationally by all the markets in which they operate, as domiciled in and so as being able to acquire the benefits of investing through the Cayman Islands.

For these purposes, Cayman hedge funds are also fully and transparently regulated. They are required, at minimum, to maintain registered offices and certain functions must be undertaken here, such as legal, audit (already mentioned) and directorship services. This regulatory presence allows the funds to maximize other economies of scale available by the carrying out of the more substantial operations of management, and investment of assets from offices in the larger onshore financial centers, like London and New York. But there can be no denying the fact that they must maintain a real presence in the Cayman as described above, far more substantial than the mere "letterbox" presence of yore.

Such was the situation with the *Bear Stearns* funds, as indeed was the situation with other Cayman Islands funds which were placed in liquidation by the Cayman court as a consequence of the global collapse of the markets in 2008[9].

Despite the fact that the Bear Stearns Funds carried out the regulatory activities required as well as the economic activities discussed above, the liquidators were denied both main and non-main recognition by the S.DN.Y Bankruptcy Court[10].

An obvious and reasonable, albeit rhetorical, question arises by way of response to this denial of recognition of the Cayman liquidation: why does the physical location overseas of most of an investment Fund's assets and management activities suffice to outweigh the presumption in the Model Law[11], that the Fund's COMI (and thus its establishment as well), are at the place of registration where no less important and necessary economic and regulatory activities, essential to its business as an investment fund, are carried out?

Fortunately, the case law has progressed in the United States as I will come to discuss below, and recent pronouncements of the United Kingdom Privy Council (" UKPC"), are also helpful on the point.

[9] Cf: *In Re Sphinx Ltd*, 351 B.R.(Bankr. S.D.N.Y 2006)("sPHINX1") AND *In Re Sphinx Ltd* 371 B.R. 10 (S.D.N.Y 2007) ("Sphinx 2") – where the S.D.N.Y court denied main recognition but granted non-main recognition to the Cayman liquidation proceedings; and *In re Basis Alpha Yield* 381 B.R. 37 – denying unopposed summary judgment on the issue of COMI, regardless of the presumption, because the Cayman court-appointed representative had "failed to submit sufficient information for the court to make a determination").

[10] In the case of foreign main proceedings recognition, the right of the foreign representative directly to bring enforcement action for recovery of assets. In the case of non-main or secondary recognition, the right, inter alia, to so do by leave of the S.D.N.Y Court.

[11] And legislation based on it, such as Chapter 15 of the USBC.

The presumption in favour of the place of incorporation as the forum for the liquidation of an investment fund was authoritatively affirmed by the UKPC in its judgment in the *Shell Pension Fund* case (above) in its rejection of Shell's blatant attempt at improper forum shopping declaring that [43]:

> *"There appears to the Board to be nothing to suggest that allowing Shell an advantage over other comparable claimants would be consistent with the ends of justice. Nor, in the circumstances, should Shell find this surprising. It invested in a company incorporated it the British Virgin Islands and must, as a reasonable investor, have expected that, if that company became insolvent, it would be wound up under the law of that jurisdiction."*

Contrary to that plainly correct dictum, an overly strict application not only of the COMI but also of the "establishment" tests, will likely result in investors having to petition the courts, not only at the place of incorporation but also at the place or places where the assets are located, for commencement of insolvency proceedings and so for the appointment of multiple trustees or liquidators – the very outcome that the Model Law and the principles of universalism are themselves aimed at preventing.

In the case of an insolvent hedge fund, a more flexible and pragmatic application certainly of the "establishment" test should be taken – the approach eventually taken, for instance, in the *SPhinX* case. There the S.D.N.Y. Bankruptcy Court opined that the granting of non-main proceedings

was a 'better choice"[12], emphasizing the importance of flexibility and concluding that recognition of non-main proceedings was a "pragmatic resolution"[13].

And for these purposes, investors can note with a sense of optimism, the reasonable and pragmatic approach more recently taken by the New York Courts, to the grant of recognition as foreign main proceedings to the liquidation of the Madoff related *Fairfield Sentry* Liquidation in the BVI, on the basis, inter alia, that post-liquidation, the COMI of that fund had been established in the BVI by the liquidators establishment of an office there and by the collection of assets there.[14]

But to return to my basic proposition, demonstration of the existence of a "non-main proceeding" should require proof of a lesser connection, namely that the debtor has an "establishment" within the State where the foreign proceeding is taking place. The term "establishment" is defined as "*any place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services*".[15] There is a legal issue whether the term "non-transitory" refers to the duration of a relevant economic activity or to the specific location at which the activity or to the specific location at which the activity, is carried on.[16] But whichever of those two views is taken, emphasis should be laid on the fact that the non-transitory economic activity does not have to be carried out by "employees" at a place of operation owned or occupied

[12] 351 B.R at 122.
[13] 371 B.R. at 19.
[14] USBC, s.d.n.y. 22 July 2010. Although the Model Law was revised in July 2010 to provide that COMI is determined as at the date of the foreign proceedings, the U.S. Congress has not similarly amended Ch. 15 of the Bankruptcy Code and so *Fairfield Sentry* remains binding precedent.
[15] UNCITRAL Model Law art. 2
[16] The Judicial Perspective on the UNCITRAL MODEL LAW; para. 64

exclusively by the debtor; it should suffice that the activity is carried out by agents or professional service providers at premises owned or occupied by them.

On that view, there should be no doubt that the typical Cayman investment fund incorporated in and having a registered office in the Cayman Islands, with independent directors, legal advisors, administrators and auditors, maintain at least an "establishment" within the Cayman Islands.

Cooperation and coordination

Another way of addressing and recognizing the realities and economic importance of distressed investment fund companies may be found within the provisions of Articles 25-32 of the Model Law. These provisions emphasize the importance of co-operation and co-ordination between court-appointees, measures which do not depend on the prior grant of recognition to the foreign proceedings[17].

As the Judicial Perspective on the Model Law also notes[18] :

> *"Court cooperation and coordination are core elements of the Model Law. Cooperation is often the only realistic way, for example, to prevent dissipation of assets, to maximize the value of assets or to find the best solutions for the reorganization of the enterprise. It is also often the only way in which proceedings concerning different members of the same enterprise group taking place in different states can be coordinated. Cooperation leads to better coordination of the various insolvency proceedings, streamlining them with the*

[17] The UNCITRAL Model Law on Cross-Border Insolvency: the Judicial Perspective (finalized and adopted by the United Nations Commission on International Trade (UNCITRAL) on 1 July 2011); para. 190
[18] At para. 188

object of achieving greater benefits for creditors. .. Moreover, as recognition is not a pre-requisite, cooperation may occur at an early stage and before an application for recognition is made".

There are a number of ways in which cooperation and coordination can take place between court-appointed insolvency officials, including of course, the fostering of court-to-court communication for the making of orders which will operate in tandem between the different jurisdictions. Indeed, this kind of communication is encouraged by the Model law and addressed in the UNCITRAL Legislative Guide.[19]

As the Judicial Perspective notes:

"*The ability of courts, with the involvement of the parties, to communicate "directly" and to request information and assistance "directly" from foreign courts or foreign representatives is intended to avoid the use of traditional but time-consuming procedures such as Letters Rogatory and Exequatur. This ability [although to be undertaken carefully and with appropriate safeguards for the protection of the substantive and procedural rights of the parties] is critical when the courts need to act with urgency.*"[20]

Another important means of cooperation and coordination is the cross-border insolvency agreement and it is to that alternative, as it has been deployed within Cayman Islands proceedings, that I would wish to invite attention in the rest of this paper.

[19] Part 3, specifically in paras. 14-40 chap. 111 and recommendations 240-245.

[20] An important recent development in the common law world in this area are the UKPC's decisions in *Singularis Holdings Limited* [2014] UKPC 36 and *PWC v Saad Investments Co. Limited* [2014] UKPC 35, to be discussed below.

The cross-border insolvency agreement

The use of cross-border insolvency agreements of various kinds is now an established feature of cooperation between Cayman insolvency proceedings and insolvency proceedings before foreign courts.

The land mark Pooling Agreement entered into between the three major ***BCCI*** banking companies in 1992[21] still serves as a paradigm for cross-border cooperation. It was the first such effort to have resulted in a unitary approach to the liquidation of a global banking entity, resulting in the near universal pooling of assets and liabilities so as to maximize the returns to depositors of the bank worldwide[22].

Described as "*an elegantly pragmatic approach to the recognition of a foreign liquidator of a local company*"[23] was that of Quin J in *Re Lancelot Investment Funds Ltd*[24] where that judge stayed the Cayman liquidation proceedings to allow the Cayman liquidator to enter into a cooperation agreement with the Chapter 7 trustee appointed by the US Bankruptcy court for the Northern District of Illinois. The Chapter 7 trustee had been appointed by the Illinois Court and had raised strenuous objections to the appointment of the Cayman liquidator notwithstanding that the entity was a Cayman fund company.

[21] Reported at 1992-93 CILR n7. Many branches of BCCI (Overseas) did not enter into the pooling agreement but instead were "ring-fenced" so as to prefer local depositors. These depositors were nonetheless allowed on the basis of the hotch-pot principle, to top up to the level of the global liquidation where the ring-fenced assets yielded a lower return for those depositors. See Wight (as liquidator of *BCCI (Overseas) Ltd) v Eckhardt Marine G.m.b.H*. 2003 CILR 211 (P.C.) and *In Re BCCI* 2009 CILR 373.
[22] In the end depositors received 91 cents per dollar of deposit.
[23] Offshore Commercial Law in Bermuda, Chp 23: *Common Law Judicial Cooperation in Cross-Border Insolvency Cases*, page 521, para 23.50, Ian RC Kawaley (now Chief Justice of Bermuda).
[24] 2009 CILR 7

He argued that as the assets were within the United States, the appointment of the Cayman liquidator would only add to the complexity and expenses of the liquidation. There were however, significant assets also within the Cayman Islands and the investors who petitioned the Cayman court for winding up had invested with the expectation that any disputes over their rights would be resolved in keeping with Cayman law[25].

Accordingly, in *Lancelot,* the Court did not accede to the Trustee's objections, holding instead that although the Court recognized the United States as the principal place for the liquidation of the company, its incorporation and many of the arrangements for the investments were governed by the laws of the Cayman Islands and would therefore have to be examined and assessed against such laws in keeping with the rights and expectations of the investors. The combination of those factors indicated the need for the appointment of at least a single Cayman liquidator but the Cayman liquidation was stayed with directions to the liquidator to discuss and enter into a protocol with the Trustee, with the expressed understanding that an application by the Trustee to be appointed as a second official liquidator by the Cayman court would be granted. In these ways the Court would ensure that the principles of comity and universalism in corporate insolvency would be observed.

The result was a cross-border protocol between the Chapter 7 Trustee and the Cayman liquidator which allowed them to wind up the affairs of the fund by sharing their responsibilities for the different activities in Illinois and in Cayman; while meeting the expectations of the investors

[25] It is not uncommon also that investors expect that any conduct or allegations of irregularity would be investigated and subsequent appropriate steps taken in keeping with Cayman law. For an earlier example of such factors determining that the liquidation should take place in Cayman see: *In Re Philadelphia Alternative Asset Funds Ltd*. 2006 CILR N7, per Henderson J., followed and applied by Quin J. in *Lancelot* (above).

without adding to the overall costs of the liquidation. Especially in this regard, a key aspect of the cross-border protocol allowed the Chapter 7 Trustee to scrutinize the fees charged by the Cayman appointee before sanction for those fees would be given by the Cayman court.

A more recent example of a successful cross-border agreement arose out of less auspicious circumstances. They involved a blatant attempt at forum shopping by the former promoters of a group of Cayman investment fund companies who filed for Chapter 11 debtor in possession bankruptcy in the USBC of the Southern District of New York (S.D.N.Y.); despite being on notice of petitions filed by investors to wind up the same companies in Cayman.[26]

In *Soundview*, the obvious conflict of laws dilemma that this situation created was of understandable concern to the S.D.N.Y. bankruptcy judge who threatened the Cayman liquidators with sanction by way of contempt, if they took any steps in relation to the companies after the Chapter 11 filing, without the leave of his court.

Eventually however, and after sight of the reasons for judgment from the Cayman court issued upon the appointment of the Cayman liquidators[27], S.D.N.Y. Judge recognized the need for co-operation and co-ordination and directed the United States Trustee as follows:

> *"Ultimately, I am authorizing and directing the U.S. Trustee to appoint a chapter 11 trustee in these cases…. But I am granting relief from the stay to allow the JOLs to stay in place and to allow the existing Cayman proceeding to*

[26] *Soundview Elite Ltd et al*, FSD Causes 111, 112 and 113 of 2013, Grand Court of the Cayman Islands, written judgment 13th December 2013 and *In RE Soundview Elite Ltd*, Chapter 11 Case no:13-13098 (REG) U.S.B.C. S.D.N.Y. Gerber J.. 24th January 2014 and 24th December 2014.
[27] See fn 12.

continue…subject to the entry of a satisfactory protocol governing the proceedings in the two nations.

As noted above, it appears at this juncture to be desirable and in some respects essential to give the Chapter 11 trustee responsibilities for U.S. investigation, issuance of U.S. subpoenas and U.S. document demands; any U.S. litigation that turns out to be warranted, and any acts that otherwise need to be accomplished within the U.S. B*ut it's less obvious that the Chapter 11 trustee would need to do anything else, and I have no particular preference with respect to anything else. Ultimately, it's best for the stakeholders to discuss with the fiduciaries what these estates' needs and concerns are, and what division of responsibilities most effectively meets them and in the most cost-effective manner*."

As the result, a cross-border protocol was indeed entered into and by a second stipulation and agreed order granted both by the Cayman judge and the S.D.N.Y. Bankruptcy judge, the Cayman liquidators and the Trustee are directed to file an addendum to the protocol.

This addendum must now set forth, among other things, their proposed distribution scheme for allowed claims, including the valuation methodology to be used by the Trustee and the liquidators for the allowance, disallowance or rejection of claims or debts filed by or on behalf of investors in the debtor companies.

There have been other examples of cross-border protocols involving Cayman Court appointed officials and their foreign counter-parts but time does not now allow even for a passing discussion of them.[28]

[28] For instance, in *Re EnRon Ltd. (In Liq.)* 9UNREP. Grand Court)(fee protocol agreement between the Cayman liquidators and the Texan Trustee in bankruptcy to cover work that had to be done in the Cayman Islands*); In Re Fruit of the Loom* 2000 CILR N7, (where in the absence of specific statutory powers enabling the court to make administration orders over companies, the court used its wide discretion under the statute to appoint provisional liquidators to allow them to cooperate with the Chapter 11 (debtor-in-possession) trustee and the board of the company to allow the company to restructure and refinance itself for the benefit both of creditors and shareholders).

The Cayman Islands statutory
regime for cross-border co-operation

Insolvency judges are now well aware of the importance of granting courts the flexibility and discretion they require for cooperating with foreign courts or foreign representatives[29]. Indeed, from comments I have seen from the minutes of the Second Judicial Colloquium dating as far back as March 1997, it was well recognized by the judges then present, that there should be at least the minimal legislative under-pinnings available in every country to clarify ensure the judges' jurisdiction to provide cross-border cooperation.

The Cayman Islands response to this requirement, although not yet adopting wholesale the UNCITRAL Model Law, has nonetheless been, I would venture to say, succinct and effective. The primary provisions are in section Part XVII of the Companies Law (2013 Revision), sections 240-242 as follows:

[29]As was emphasized at the Second UNCITRAL-INSOL Multinational Judicial Colloquium on Cross-Border Insolvency, held in New Orleans in March 1997.

"PART XVII – International Co-operation

240. In this Part-

"debtor" means a foreign corporation or other foreign legal entity subject to a foreign bankruptcy proceeding in the country in which it is incorporated or established;

"foreign bankruptcy proceeding" includes proceedings for the purpose of reorganizing or rehabilitating an insolvent debtor; and

"foreign representative" means a trustee, liquidator or other official appointed in respect of a debtor for the purposes of a foreign bankruptcy proceeding.

241. (1) Upon the application of a foreign representative the Court may make orders ancillary to a foreign bankruptcy proceeding for the purposes of-

(a) recognising the right of a foreign representative to act in the Islands on behalf of or in the name of a debtor;

(b) enjoining the commencement or staying the continuation of legal proceedings against a debtor;

(c) staying the enforcement of any judgment against a debtor';

(d) requiring a person in possession of information relating to the business or affairs of a debtor to be examined by and produce documents to its foreign representative; and

(e) ordering the turnover to a foreign representative of any property belonging to a debtor.

(2) An ancillary order may only be made under subsection(1)(d) against

(a) the debtor itself; or

(b) a person who was or is a relevant person as defined in section 103(1).

242. (1) In determining whether to make an ancillary order under section 241, the Court shall be guided by matters which will best assure an economic and expeditious administration of the debtor's estate, consistent with-

(a) the just treatment of all holders of claims against or

interests in a debtor's estate wherever they may be domiciled;

(b) the protection of claim holders in the Islands against prejudice and inconvenience in the processing of claims in the foreign bankruptcy proceeding;

(c) the prevention of preferential or fraudulent dispositions of property comprised in the debtor's estate;

(d) the distribution of the debtor's estate amongst creditors substantially in accordance with the order prescribed by Part V;

(e) the recognition and enforcement of security interests created by the debtor;

(f) the non-enforcement of foreign taxes, fines and penalties; and

(g) comity.

(2) In the case of a debtor which is registered under Part IX, the Court shall not make an ancillary order under section 241 without also considering whether it should make a winding up order under Part V in respect of its local branch."

Cases decided under these provisions[30] have produced helpful results.

One resulted in the recognition of an Icelandic court-appointed official termed a "moratorium assistant" to administer the affairs of a distressed bank within the Cayman Islands and the restraint of commencement or stay of any proceedings I the Cayman Islands against the bank, without the leave of the Court; see: *In re Straumur-Barduras Bank*[31].

In *CIGNA Worldwide Ins. Co. v Ace Ltd.*[32] the Court (per Cresswell J.) used its case management powers to stay local proceedings against a Cayman Insurance company in liquidation, in recognition of bankruptcy proceedings in Delaware involving an affiliate insurance company and to await the outcome of proceedings in Delaware.

In *Picard v Primeo Fund*[33], Mr. Picard as trustee of the infamous Madoff Funds appointed by the bankruptcy court S.D.N.Y. was granted recognition by the Cayman court observing the principle of modified universalism, including leave to bring insolvency proceedings by way of avoidance and restitutionary claims to recover assets from parties within the jurisdiction of the Cayman court. At first instance it was held (per Jones J.) that recourse to common law powers was

[30] Administered in keeping with the Foreign Bankruptcy Proceedings (International Co-operation) Rules 2008.
[31] 2010(2) CILR 146.
[32] 2012 (1) CILR 55.
[33] 2013 (1) CILR 164.

necessary to allow Mr. Picard to bring recovery proceedings in the Cayman Islands because the statutory powers under Part XVII of the Law[34] did not allow the court to enforce foreign *in personam* avoidance claims. This was, however, later disapproved on appeal by the Court of Appeal but the question whether the common law jurisdiction could have been invoked in the circumstances of the case to recognise Mr. Picard's appointment, was reserved by the Court of Appeal being aware that *Singularis* would soon be heard by the Privy Council on a similar issue and pending the outcome of that case before the Privy Council[35].

The Privy Council, while acknowledging the existence of the common law power to assist a foreign liquidator, did not agree that the section 24(1)(e) power did not allow the Cayman court to enforce a foreign *in personam* avoidance claim.

A further consequence of the decision of the Privy Council, is its broad public policy limitation upon the grant of assistance by means of the common law powers, in holding that the Bermuda court could not assist the Cayman court appointed liquidators, by granting them relief which their home court could not have granted.

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[34] See section 241 (1)(e) above.

[35] *Singularis Holdings (in liq.)* (supra): Singularis was one of the SAAD Group of Investment companies established it the Cayman Islands which carried on investments around the world, including in Saudi Arabia to which jurisdiction important records had been taken and secreted away resulting in the need of the Cayman Islands liquidator to recover them from the former auditors, PWC. Hence the application to the Bermuda Court where PWC's branch office formerly responsible for auditing Singularis was based.

An earlier attempt by the liquidators qua liquidators of the related entity SICL Ltd. (in liquidation) also failed. There the liquidators had successfully applied to the Bermuda Court to wind up SICL in Bermuda and so get access to the same powers to compel PWC to hand over working papers. The Privy Council held on appeal that the statutory power vested in the Bermuda Court to wind up a Bermuda entity, did not extend to a foreign entity like SICL [2014] UKPC 35.

In *Singularis*, the question considered by the Privy Council were (a) whether the Bermuda court had a common law power (to be applied by analogy to statutory powers relating to domestic proceedings but in the absence of statutory powers for rendering assistance to foreign insolvency proceedings) to assist the foreign liquidation taking place before the Grand Court of the Cayman Islands, by ordering the production of information, and (b) whether, if such a power existed, it was exercisable in circumstances where an equivalent order could not have been made by the court of the foreign proceedings (i.e.: the Cayman court).

The Privy Council considered that the principle of modified universalism[36] was relevant; that is: that the courts have a common law power to assist foreign liquidators, accepting that the principle is founded in the public interest in the ability of courts conducting insolvency proceedings to do so on the worldwide basis. This principle the Privy Council considered, must however be applied on a basis that is consistent with the local substantive law from which the court (in this instance the Bermuda court) derived its jurisdiction.

In holding that the Bermuda court did not have the power to grant assistance in this case, the Privy Council, in what may be described as a new limitation upon the common law jurisdiction to render assistance, placed great store by the fact that the order which the liquidators sought from the Bermuda court was not one which the Cayman court, as the forum of the liquidation, could have granted. The Privy Council proceeded on the basis (conceded by the liquidators but not found to be so by the Privy Council itself), that the information that the liquidators requested belonged to PWC as it comprised their working papers and so did not belong to the Singularis

[36] As explained by Lord Hoffmann in his famous dictum in the *Cambridge Gas* [2007] 1 AC 508, (517, para. 17) and in *HIH Casualty and General Insurance* [2008] 1 WLR 852; and as is regarded as having survived the critical curtailment of the principle as explained by the UK Supreme Court in *Rubin v Eurofinance SA [2012] UKSC 46*

liquidation estate, the latter being the only basis upon which the Cayman court could have compelled PWC, as the former auditors to hand them over[37].

Accordingly, the Privy Council held that the Court of Appeal of Bermuda was correct in allowing the appeal against the order and so in rejecting the Singularis liquidators' attempt to compel PWC to hand over their working papers, an attempt which the Court of Appeal had described as "forum shopping".

The Privy Council's decision, despite what can fairly be described as its "public policy limitation" upon the common law power to render assistance, is nonetheless to be welcomed by those jurisdictions which have not yet adopted the Model law or enacted similar provisions for international co-operation . This is so because the Privy Council implicitly affirmed some earlier decisions which invoked the common law powers, including that from Bermuda itself in *Re Founding Partners Global Fund Ltd.*[38] (granting assistance to other Cayman liquidators in that case) and as followed and applied recently in Hong Kong by Justice Harris in his affirmative response to a letter of request from the Cayman court in *Re China Medical Technologies Ltd.*[39]

The outcome in *Singularis,* when seen as a public policy prohibition against improper forum shopping, may be contrasted with the outcome in the U.S. Courts of Appeal 2nd Circuit in its

[37] While an exactly comparable power to require the former auditors to surrender their working papers was not available to the Cayman Court, a statutory power to require them to answer interrogatories and to attend with their working papers before the court to answer questions exists but appears not to have been explained to the Bermuda Court (nor therefore to the Privy Council). Had the liquidators sought a letter of request from the Cayman Court to the Bermuda Court (instead of relying upon the general powers given at the time of their appointment to apply to foreign courts) the Cayman statutory power would likely have been explained in the letter of request and the outcome may well have been different.

[38] 2011 Bda LR 22.

[39] HCPM 902/2014; 21 July 2014; discussed by Justice Harris at this Colloquium. See also the decision of Deemster Doyle in the Isle of Man case: *In re Impex Services Worldwide Ltd. [2004] BPIR 564.*

recent decision in *Krys v Harnum Place LRC* (*In Fairfield Sentry Ltd.*[40]). In that case, the U.S. Court of Appeal held that the sale of assets which fell within the regime of the Securities Investors Protection Act ("SIPA") and therefore deemed to be within its jurisdiction, could be reviewed and set aside notwithstanding that the sale had been negotiated at arms-length between the liquidator and sanctioned by the BVI Court as the proper forum of the liquidation of Fairfield Sentry. And this was notwithstanding that the BVI liquidation had been so regarded by the U.S. Courts themselves, recognition as foreign main proceedings having already been granted to them by the bankruptcy court, S.D.N.Y.

Thus this decision, quite remarkably, allowed the Fairfield Sentry liquidator to recover from his "seller's remorse", when it became apparent that the assets, in light of the greater than expected recoveries achieved and declared by the Trustee in the global liquidation of the Madoff Funds, were worth approximately $40 million more than he had believed.

This intervention by the NY Court was based on that court's finding that section 363 of the Bankruptcy Code applied to the SIPA assets, allowing the sale to be reviewed by the New York Court on the basis that the assets were located there.

Conclusion

The foregoing discussion of the cases reveals an encouraging move by Courts internationally towards acceptance of the principle of (modified) universalism in bankruptcy or insolvency proceedings. This is evident notwithstanding the sometimes overly-strict application of the COMI or "establishment" test and notwithstanding the revision of the Model Law in July 2013 to

[40] 2nd Cir., Sept. 26, 2014.

set the date for the identification of COMI or proof of an "establishment", at the date of commencement of the foreign proceeding and not after. This would preclude reliance on a COMI which was changed or the setting up of an establishment, post-liquidation. But this revision to the Model Law is yet to be adopted in many States that follow the Model Law, notably among them, the U.S.A. As we have seen from *Fairfield Sentry* (above); where COMI was deemed to have developed post-liquidation, the revised Model Law approach would be contrary to the pragmatic approach taken by the bankruptcy court S.D.N.Y, in circumstances which will be very similar to those in which the liquidation proceedings of many investment funds will need to seek recognition abroad.

And, despite what may be regarded as the Privy Council's policy driven limitation upon the common law power to render assistance, we see from the *Singularis* decision, that the common law power is alive and well and is available to be called upon in many circumstances. Thus, the cases illustrate that the power exists to recognise the proper choice or change of forum as well as, in the appropriate case, to disapprove or disallow improper forum shopping.