BRIEFING

Recent Changes to the Companies Winding Up Rules

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The Companies Winding Up (Amendment) Rules, 2013 (the "Amendment Rules") came into operation on 1 March 2013. Orders 3, 8, 9, 11, 15, 19 and 25 of the Companies Winding Up Rules 2008 (the "Principal Rules") have been revoked and replaced by new orders. Order 9 had previously been amended by the 2010 Amendment Rules.

Many of the changes are welcome and are likely to increase efficiency, for example through the use of letter applications for validation of share transfers and applications relating to liquidation committees, and the removal of the need for court hearings in some supervision applications. Other changes increase and clarify certain service, notice and advertising requirements.

Some of the changes are substantive, and reflect a move away from liquidator autonomy and towards a more uniform, court governed process. These include sweeping changes to the terms under which liquidators will be able to retain lawyers and a substantially reduced role for liquidators in *inter partes* proceedings affecting the rights of various stakeholder constituencies.

One rule is designed to ensure that petitions are served on the day that they are filed. This is a worthy aim, but will result in at least 24 hours' delay in the presentation of all winding up petitions, possibly more, if the Court does not meet its self-imposed target. Correspondingly, this will delay the deemed commencement of any winding up, with the stakeholder protection that ensues. We will have to wait to see the practical effect of this reform over the coming months.

In this briefing, we set out all of the changes brought into effect by the Amendment Rules. For ease of reference, we have organised these below in declining importance, starting with the 'substantive changes', followed by the 'procedural improvements' and finally by the 'minor revisions'.

Substantive Changes

Winding Up Orders

Liquidators' Powers

Every winding up order *must* now state which, if any, of the powers contained in Part I of Schedule 3 of the Companies Law ("powers exercisable with sanction") are given to the official liquidator (O.3, r.17(3)).

In most cases, liquidators will want the order appointing them to include powers to engage staff and (given the new rules regarding their lawyers) to engage attorneys and other professionally qualified persons to assist them in the performance of their functions.

Sanction Applications

Official Liquidators' right to be heard

Official liquidators no longer have the right to be heard on every sanction application. However, it remains the official liquidators' duty to attend and be prepared to assist the Court in respect of any sanction application made by the liquidation committee or a stakeholder (O.11, r.3(2)).

Inter Partes proceedings

Where a sanction application gives rise to an issue in respect of the substantive rights as between the company and any stakeholder(s), or class(es) of stakeholder(s), the Court may direct that it shall be adjudicated as an *inter partes* proceeding between the relevant stakeholder classes. In such cases, the Court may make:

- a representation order; and/or
- directions limiting or preventing the liquidators' participation in such proceedings (O.11, r.3(3)).

These rules are designed to facilitate *inter partes* proceedings between representative

stakeholders, in order to establish their competing rights (eg to receive distributions) within a liquidation. This is a legitimate aim, but unless managed carefully this process may risk sidelining liquidators who may be best able to determine these issues, whilst encouraging parties to expend estate resources advancing their own interests. It will be interesting to see whether the Court develops some form of threshold test as to when it considers disputes sufficiently arguable to warrant such proceedings between rival stakeholders.

Official Liquidators' Lawyers

Engagement letters

The Principal Rules previously provided that liquidators and liquidation committees could require the fees charged by the liquidators' lawyers to be taxed. However, the effectiveness of such provisions was open to doubt in cases where liquidators had engaged foreign lawyers under contracts not governed by Cayman Islands law. The Amendment Rules go much further and bring a great deal more certainty to the position, at the cost of reduced flexibility.

First, they reverse the former rule dispensing with the liquidators' need for court sanction to engage lawyers for certain purposes. Now liquidators need court sanction before engaging *any* lawyers for *any* purpose (regardless of whether or not those lawyers are admitted in the Cayman Islands) (O.25, r.1(1)).

Second, the Amendment Rules provide that, unless the Court sanctions otherwise, all lawyers *must* be remunerated on a time spent basis, which hourly rates *must* be set out in the engagement letter (O.25, r.2(1)).

Third, the Amendment Rules provide that the terms upon which *all* lawyers are engaged by the official liquidator *must* be stated in writing and signed by both parties (O.25, r.1(2)).

- In every case, that letter *must* provide particulars of the basis on which the lawyers will be remunerated, including, if applicable, a statement of the agreed hourly rates (O.25, r.1(3)).
- Where *foreign* lawyers are engaged, the letter *must* also provide that:
  - The contract is governed by Cayman Islands law;
  - The lawyer/law firm submits to the *exclusive jurisdiction* of the Court for all purposes in connection with the engagement;
  - The lawyer/law firm understands and agrees that the amount of fees payable by the official liquidator is subject to taxation in accordance with this Order; and
  - The lawyer/law firm shall have no right to exercise any lien over his files as against the official liquidator (O.25, r.1(4)).
- The rule states that official liquidators have *no authority* to engage *any* lawyers on terms which are inconsistent with the requirements of this rule. It also states that any term of an engagement letter or retainer agreement which is inconsistent with the requirement of this rule shall be void and of no effect (O.25, r.1(5)).
- This rule does not affect the validity of engagement letters made prior to 1 March 2013 (O.25, r.1(6)).

These new rules offer stakeholders the protection of having a route through which liquidators' lawyers' fees can be taxed. It is not clear to what extent they will affect any engagements that began prior to 1 March 2013, but which had not yet been confirmed in writing. In addition, it will be interesting to see whether the Amendment Rules discourage foreign lawyers from accepting engagements from Cayman Islands liquidators.

One potential concern relates to the fact that liquidators will now require court sanction before entering into agreements for lawyers to be remunerated on anything other than a time spent basis. This may give rise to increased costs in situations where, for example, an estate has limited funds and its liquidators are forced to seek permission to instruct foreign lawyers on a contingency fee basis. It will be interesting to see to what extent the Courts approve liquidators' commercial decisions in these cases.

Procedural Improvements

Winding up Petitions

Listing

Before presenting *any* petition (whether presented by a creditor, contributory or the Authority) the petitioner's attorney *must*

apply in writing (by letter or e-mail) to the Registrar to have the proceeding assigned to a Judge and to fix a hearing date. Only after the proceeding has been assigned and a hearing date has been fixed and endorsed on the petition or stated in a notice of hearing filed simultaneously with the petition, may that petition be filed (O.3, r.5, r.11, r.14).

As stated above, the worry here is that this may lead to delays in presenting petitions, with consequent effects on stakeholder protections.

Service

It was always the case that a creditor's petition had to be served on the company *immediately* after it was presented. Now the Amendment Rules clarify that:

- a creditor's petition must also be served on the Authority *immediately* after the petition has been presented, where the company is carrying on a regulated business (the Principal Rules contained no deadline) (O.3, r.5(4)); and
- a contributory's petition and summons for directions must also be served on the company and every member of the company whom the petitioner has or intends to name as a respondent to the petition *immediately* after being presented and issued. Service on any additional persons will be a matter for directions (O.3, r.11, r.12).

Advertisement

A creditor's petition no longer has to be advertised in countries where it is likely to come to the attention of that company's contributories. However, it does have to be advertised in a newspaper having a circulation in *the country or countries* where it is likely to come to the attention of the company's creditors (O.3, r.6(2)).

The language used in the earlier rule was "... having a circulation in *a* country...". It is not clear whether the replacement of "*a* country" with "*the country or countries*" means that the petition must be advertised in *all* such countries, but it appears that this might be the intention.

The advertisement must now also contain the name and address of the nominated liquidators, as well as the other usual information (O.3, r.6(4)(d)). This is reflected in the revised form (CWR Form No. 3). This revised form also provides that:

- any stakeholder may be heard on the questions of whether or not a winding up order should be made and who should be appointed as official liquidator; and
- any stakeholder opposing the appointment of the nominated liquidator must nominate a suitable alternative, who consents to act and has sworn an affidavit complying with the requirements of CWR O.3, r.4.

Liquidation Committees

Applications

Any application made to the Court regarding liquidation committees may now be made in writing by letter addressed to the assigned Judge. That letter must be supported by an affidavit (O.9, r.9).

This is a welcome refinement, designed to save legal costs. However, it is not entirely clear when such applications will arise. This is because the Amendment Rules do not contain any of the references to Order 9, rule 1(7) of the CWR, which was brought into operation as part of the Companies Winding Up (Amendment) Rules 2010. That rule related to applications in circumstances where it was practically impossible to establish a liquidation committee and accordingly the liquidator needed leave either to dispense with a liquidation committee, or to establish a liquidation committee with an irregular number or combination of stakeholders.

It does not appear that this deletion was deliberate and we would not be surprised to see it added back into a later revision of the CWR. Certainly there are no references to any other form of application in the new Order 9. In addition, the new rule states that a liquidation committee shall be established in respect of every company which is being wound up by the Court, *unless the Court otherwise directs* (O.9, r.1(1)).

Notice of liquidation committee meetings

Liquidation committees may, by unanimous consent, agree to hold meetings on short notice (whereas previously the minimum notice was five business days for a telephone meeting and 10 business days for a physical meeting) (O.9, r.4(6)).

Deadline for written resolutions

Under the Principal Rules, written resolutions would be passed if signed by every member of the committee within 14 days. Now, allowing greater flexibility, the applicable period or deadline shall be set by the official liquidator (O.9, r.5(9)).

Reconstitution

The Amendment Rules provide that if, during the course of a liquidation, the liquidator changes his certification as to the company's solvency, all liquidation committee members who no longer have an interest in the liquidation shall *automatically cease* to be members of that committee. The liquidator *must* then hold a meeting of interested stakeholders for the purpose of electing new members amongst the interested group (ie creditors if the company is insolvent or contributories if it is solvent). This rule does not prevent the liquidator convening a meeting in anticipation of his change in certification (O.9, r.3).

Voluntary liquidations

Supervision orders

Section 124 of the Companies Law requires a voluntary liquidator to apply for a supervision order, where the company's directors have not signed a declaration of solvency within 28 days of the commencement of the voluntary liquidation.

The Amendment Rules provide that, where the voluntary liquidator is a qualified insolvency practitioner, who has sworn an affidavit verifying that he is willing and properly able to accept an appointment as official liquidator, the Court may make a supervision order *without the need for any hearing*, as long as it is satisfied that:

- notice has been given to the company's relevant stakeholders; and
- there is no reason to believe that any of them objects to the appointment of the voluntary liquidator as official liquidator (O.15, r.5(1)).

Form 21 (the Declaration of Solvency) has also been updated. Now all directors are required to sign the same document. The guidance on the revised document also reminds all directors that making a declaration without reasonable grounds constitutes a criminal offence.

Share Transfers

Applications for validation orders

The Amendment Rules allow liquidators, transferors or transferees to make such applications by letter addressed to the assigned judge, provided that:

- the shares in question are fully paid; and
- the liquidator does not object to the transfer.

This letter must be supported by:

- an affidavit confirming that the shares are fully paid and that the liquidator has no objection to the transfer (presumably this would either be an affidavit sworn by the liquidator, or exhibiting a letter in support provided by the liquidator); and
- a draft of the order sought.

If the requirements for a letter application are not met, the application must be made by summons and supported by an affidavit sworn by or on behalf of the applicant, which contains a full explanation of the reasons for the transfer and the applicant's response to the liquidator's objections. That summons (and, we assume affidavit, although this is not specified in the rules) must be served on the liquidator (O.19, r.4, r.5).

Minor Revisions

Winding Up Petitions

Amendment

Once served, winding up petitions may only be amended with the leave of the Court (O.3, r.2(3)).

Contributory's Petitions

The reference to a contributory petitioning for alternative relief under section 94(3) of the Companies Law has been removed. This does not appear to have any practical consequence and is probably designed to ensure that contributories realise that their only route to any alternative relief is to establish that it would be just and equitable for the company to be wound up (O.3, r.11(1)).

Application to fix a trial date for a contributory's petition

Normally the Court will fix a trial date at the directions hearing of a contributory's petition. In the few cases where it does not, these applications are necessary. They no longer have to be made in accordance with GCR

Order 34 (which, at least in theory, involved a long-winded process under which the petitioner sent a "notice to fix a trial date" to the Clerk of the Court; the Clerk of Court arranged an appointment at her office within 14 days of receipt of that notice; and the parties furnished the Clerk with certain written particulars three days before that meeting).

Winding Up Orders

Directions

There is no longer a rule stating that any order made at the petition hearing by which directions are given to the liquidator may be set out in a separate order. However, it is safe to assume that the Court retains the inherent power to make such orders.

Stakeholder Meetings

Meetings held by conference call

All notices and advertisements of such calls must now *either* specify the dial in number and codes (which was the position under the previous rule), *or* provide a contact number and e-mail address to which stakeholders may apply to obtain those details. This will reduce the dangers of attendance on such calls by non-stakeholders (O.8, r.5(2)(a)).

Minutes of stakeholder meetings

The Amendment Rules expressly state that *the* (original) minutes must be kept as part of the records of the liquidation (whereas previously copies could be kept). They also state that copies must be circulated to all stakeholders *within* 28 days of the meeting (whereas previously there had been no time limit) (O.8, r.10).

Voluntary liquidations

Supervision orders

The Principal Rules relating to the requirement to give notice and advertise the hearing of an application for a supervision order have been tidied up, in order to make it clear that:

- notice of the hearing must be provided both to the company's *creditors* and (if applicable) its members (previously there was no mention of creditors); and
- the petition *hearing* must be advertised (the previous requirement was to advertise the petition) (O.15, r.5).

CWR Form No. 22 ("Advertisement (Application for Supervision Order)") has been updated to include the details of the voluntary liquidators, the details of the proposed official liquidators and a statement that any stakeholder opposing the appointment of the nominated liquidators must nominate a suitable alternative, who consents to act and has sworn an affidavit complying with the requirements of CWR O.3, r.4.

Official Liquidators' Lawyers

Taxation of Liquidators' Lawyers costs

The Amendment Rules add a reference that taxation under this order shall be governed by and conducted in accordance with GCR Order 62 ("Costs"). This does not appear to reflect any material change in this procedure, but merely clarifies the fact that the broader principles set out under Order 62 apply to taxation of liquidators' lawyers' costs.

Conclusion

For the most part, the Amendment Rules are to be welcomed and should reinforce Cayman's reputation as a premier, user-focused jurisdiction.

We hope that this briefing has been helpful. Please note that it does not constitute legal advice and we do not accept any liability for reliance on it. If you have any questions, please contact Peter Hayden, head of litigation and insolvency at peter.hayden@mourantozannes.com, Simon Dickson, partner, at simon.dickson@mourantozannes.com or Nicholas Fox, managing associate, at nicholas.fox@mourantozannes.com