

UPDATE

Additional liquidator appointed to mitigate conflicts of interest in the winding of a Cayman SPC

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A Cayman segregated portfolio company, Performance Insurance Company SPC, was placed into official liquidation. The joint liquidators' appointment extended to all of the underlying segregated portfolios (SPs), some of which were solvent and others insolvent. Two of the solvent SPs applied to the Grand Court of the Cayman Islands seeking the appointment of an additional liquidator of the company to separately represent the interests of those solvent SPs on the basis that the original liquidators were conflicted in administering both the solvent and insolvent SPs. The Grand Court's decision on the application helpfully sets out how recoveries and costs are to be managed in the liquidation of a segregated portfolio company and the circumstances in which it might be appropriate to appoint an additional liquidator.¹

Cayman Islands' Segregated Portfolio Companies

Segregated Portfolio Companies (SPCs) are Cayman Islands exempted companies which contain segregated cells (referred to as segregated portfolios). These SPs are separately identifiable, but do not have a legal personality separate from the SPC of which they form part. Part XIV of the Companies Act (2022 Revision) (the **Act**) sets out the legislative framework governing SPCs.

A fundamental feature of SPCs is that the assets and liabilities of each SP are separate and 'ring-fenced' from the other SPs within the same SPC. As a result, a creditor of one SP cannot have recourse to the assets of another SP. Any assets held by the SPC itself are general assets. Maintaining the integrity of the segregated portfolio structure is critical to the SPC structure. Directors of a SPC have a statutory obligation to keep segregated the portfolio assets from general assets, and to keep the assets of each SP separate and separately identifiable from the other SPs.

The Act provides that the assets of a SP can only be used to meet the liabilities of that SP, and are not to be used to meet the liabilities of the SPC or other SPs. The Act also provides for strict segregation in a liquidation.

Background

In February 2021, joint voluntary liquidators were appointed to Performance Insurance Company SPC (the **Company**). The voluntary liquidation was subsequently converted into an official liquidation, and the voluntary liquidators were appointed as joint official liquidators (the **JOLs**).

In November 2021, the Applicants filed a summons seeking the appointment of an additional joint official liquidator (**AJOL**) with sole and exclusive responsibility for the liquidation of Bottini Insurance SP (**Bottini SP**) and SSS Insurance SP (**SSS SP**), both solvent SPs in the Company. The Applicants were the shareholders of Bottini SP and SSS SP.

¹ *In the Matter Performance Insurance Company SPC (In Official Liquidation)* (unreported, 6 April 2022).

The liquidation was the result of an alleged fraud in relation to certain of the SPs in the Company, but notably not Bottini SP and SSS SP. Throughout this process, the Applicants' businesses were and remained solvent, and operational.

It was the JOLs' stated intention to wind-up the Company and the (insolvent) SPs affected by the fraud, but to novate the unaffected SPs, including Bottini SP and SSS SP, resulting in the transfer of the unaffected (solvent) SPs to new structures. However the JOLs refused to permit the novation of the solvent SPs unless they agreed to bear a pro rata share of the general liquidation fees and expenses. As a result, the Applicants faced claims of hundreds of thousands of dollars from the JOLs to exit the structure.

The Applicant's position

The Applicants contended that the JOLs' claim to be entitled to shift the general costs of the liquidation of the Company and the insolvent SPs onto the solvent SPs was contrary to the statutory scheme relating to SPCs in the Act, which confirms the segregation of each SP's assets from the liabilities of other SPs and of the company.

The Applicants submitted that a liquidator's usual statutory right to pay general liquidation expenses, including the liquidator's remuneration, out of a company's assets does not override the statutory segregation of individual SPs set out in the Act. To do so would render the statutory segregation meaningless.

The Applicants held that the structure of the Company as a SPC put the JOLs in a position of conflict between the competing interests of the solvent and insolvent portfolios in the Company. On this basis, the Applicants sought the appointment of an AJOL to have sole remit of the liquidation of the Applicants' portfolios.

Decision

The Court accepted the Applicants' position that the assets of the SPs are not available to back stop or guarantee the general liabilities or expenses of the SPC, including those of the liquidation - as is explicitly provided by the Act.

The Court considered the authorities *In re Asia Private Credit Fund Limited*² and *In re Alpha Re Limited*,³ in support of the position that it is the interests of those having the real economic interest in the outcome of the liquidation that should be considered and prioritised when appointing office holders (and in conducting liquidation proceedings). The Court accepted that the interests of the Applicants, as the parties with the sole economic stake holdings of Bottini SP and SSS SP, were the primary concern in considering whether an AJOL should be appointed.

The Applicants accepted that the costs of the proposed appointment would be borne entirely by them. There was therefore no prejudice to any other stakeholder of the Company or the other SPs. If an AJOL was appointed, the overall cost burden on the estate would be reduced as the official liquidators would have less to do.

The Court held that in circumstances where it was clear that the JOLs were reasonably perceived to be conflicted, it was necessary and appropriate that the AJOL should be appointed. The appointment would ensure that the economic stakeholders of Bottini SP and SSS SP would have confidence that their assets and liabilities were being dealt with appropriately and in the best interests of Bottini SP and SSS SP.

The Court granted the appointment, and limited the JOLs' and AJOL's powers by providing that the JOLs would no longer be empowered to act in respect of Bottini SP and SSS SP; the AJOL would have sole and exclusive responsibility for the liquidation of Bottini SP and SSS SP, and would have no authority to act on behalf of the Company or any other SPs of the Company; and from the date of the order appointing the AJOL, the fees and expenses of the JOLs would not be allocated to Bottini SP and SSS SP, and conversely Bottini SP and SSS SP would be solely responsible for the fees and expenses of the AJOL.

² *In re Asia Private Credit Fund Limited* [2020] (1) CILR 134.

³ *In re Alpha Re Limited* (unreported, 2 March 2018).

Conclusion

The decision considers the nuances involved in the liquidation of a SPC. The importance of keeping the portfolios segregated may justify the appointment of additional liquidators to oversee the liquidation of certain segregated portfolios, separate from the liquidation of the SPC as a whole. The decision is also a reminder that the interests of the economic stakeholders are paramount in liquidation proceedings, and it is important that they have confidence that the liquidation proceedings are being managed in their best interests.

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