

Navigating a return of funds to shareholders of a Cayman Islands exempted company

GUIDE

Last reviewed: July 2023

The process of returning funds to shareholders of a Cayman Islands exempted company (a **Company**) can be relatively straightforward, so long as it is implemented in accordance with the laws of the Cayman Islands. The consequences of getting it wrong are not straightforward, with the possibility of personal liability for directors effecting an unlawful return of capital.

Every scenario is unique, which requires consideration and application of the particular facts in play. Beyond the case specific fact pattern, the general framework enabling a return of funds to shareholders is set out here. This guide is not a substitute for case specific Cayman Islands legal advice.

Dividends

Cayman Islands law prescribes that a Company may only pay dividends out of its profits or share premium. It falls primarily to the directors of the Company to determine if the financial position of the Company enables it to pay a dividend to the shareholders. Depending on the terms of a Company's articles of association, it may also be necessary to pass a shareholder resolution.

Any Company paying a dividend must be solvent. In the Cayman Islands context, this means the Company is able to pay its debts as they fall due in the ordinary course of business. This cash flow solvency test involves having some regard to debts which fall due for payment in the reasonably near future as well as debts which have already fallen due. As to what future debts are deemed as falling due in the 'reasonably near future', is a question to be determined on a case-by-case basis depending on all of the circumstances, and with reference to the underlying business of the company.

Profit

There is no Cayman Islands statutory definition of profit and there is limited authority of the Cayman Islands courts as to what constitutes profit. What constitutes profit will depend upon the circumstances of a Company at a given time.

Share premium

Share premium is the amount paid by shareholders on the shares of a Company in excess of the nominal or par value of such shares. The Companies Act (as amended) of the Cayman Islands provides that where a Company issues shares at a premium, whether for cash or otherwise, an amount equal to the premium on those shares over the nominal or par value of such shares is to be transferred to an account called the share premium account. The share premium account may be applied to pay dividends to shareholders in certain circumstances.

Redemption or repurchase of shares

A Company may redeem or repurchase its shares out of its profits or its share premium. Unlike dividends, a Company may redeem or repurchase its shares out of share capital in certain circumstances.

A Company may only redeem or repurchase its shares if such shares are fully paid up to their nominal or par value. A Company may not redeem or repurchase its shares if, as a result of the redemption or repurchase, there would no longer be any issued shares (note that treasury shares, as discussed below, do not meet the criteria for this purpose).

The ability of a Company to redeem or repurchase its shares is subject to any restrictions in the Company's articles of association. To be redeemable, shares must either have been issued as redeemable shares or, subject to the Company's articles of association, the rights attaching to the issued shares have been varied to make them redeemable.

As with paying a dividend, any Company repurchasing or redeeming its shares must be solvent, in accordance with the cash flow solvency test outlined above.

Cancellation of redeemed or purchased shares

Subject to a Company holding shares that have been redeemed or repurchased as treasury shares, shares redeemed or repurchased by a Company are treated as cancelled on redemption or repurchase and the Company's issued share capital is reduced accordingly. Such shares are then available to be re-issued by the Company. The redemption or repurchase of shares by a Company is not to be taken as reducing the amount of the Company's authorised share capital.

Treasury shares

Treasury shares are permitted under Cayman Islands law and, subject to any restrictions in the Company's articles of association, it is possible for a Company to acquire and hold its own shares, rather than cancel shares which have been redeemed or repurchased.

A Company that holds treasury shares may at any time cancel such shares or transfer them to any person, whether or not for valuable consideration, including at a discount to the par value of such shares.

So long as a Company holds treasury shares, the Company will be listed in the register of members as holding those shares but is not treated as a member for any purpose. A treasury share held by the Company cannot be voted at any meeting of the Company and will not be counted in determining the total number of issued shares at any given time. No dividend may be made to the Company in respect of a treasury share.

Court sanctioned reduction of share capital

In certain circumstances, an application may lie to the Grand Court of the Cayman Islands to confirm a proposed reduction of share capital of a Company.

Contacts

A full list of contacts specialising in Cayman Islands corporate law can be found [here](#).