

THE LENDING
AND SECURED
FINANCE REVIEW

NINTH EDITION

Editor
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THE LAWREVIEWS

Published in the United Kingdom
by Law Business Research Ltd
Holborn Gate, 330 High Holborn, London, WC1V 7QT, UK
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www.thelawreviews.co.uk

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ISBN 978-1-80449-185-0

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

ABREU ABOGADOS

ALLEN & OVERY

BREDIN PRAT

CMS PASQUIER CIULLA MARQUET PASTOR SVARA & GAZO

DE BRAUW BLACKSTONE WESTBROEK

GOWLING WLG

LENZ & STAEHELIN

MORI HAMADA & MATSUMOTO

ODI LLP

PAUL, WEISS, RIFKIND, WHARTON & GARRISON LLP

SLAUGHTER AND MAY

SYCIP SALAZAR HERNANDEZ & GATMAITAN

TRAVERS THORP ALBERGA

URÍA MENÉNDEZ ABOGADOS, SLP

PREFACE

This ninth edition of *The Lending and Secured Finance Review* contains contributions from leading practitioners in 15 different countries, and I would like to thank each of the contributors for taking the time to share their expertise on the developments in the corporate lending and secured finance markets in their respective jurisdictions, and on the challenges and opportunities facing market participants. I would also like to thank our publishers without whom this review would not have been possible.

I hope that the commentary that follows will serve as a useful source for practitioners and other readers.

Azadeh Nassiri

Slaughter and May

London

June 2023

CAYMAN ISLANDS

*Agnes Molnar and Richard Mansi*¹

I OVERVIEW

i Introduction to the Cayman Islands

In terms of assets under management (AUM), the Cayman Islands is the largest offshore jurisdiction for investment funds and financing structures. One reason for this is a particular legal and regulatory framework that pays specific regard to the requirements of sophisticated institutions, fund managers, lenders and investors. Based on well-established English common law principles, the legal regime has been enhanced by specific statutory enactments, invariably driven by user input. The judicial system is reputable, highly efficient and well regarded. As the Cayman Islands is a British Overseas Territory and Crown Dependency, the Judicial Committee of the Privy Council comprised of UK Supreme Court and Commonwealth judges is the final court of appeal. This provides market participants with a full array of legal precedents and a high degree of certainty. The legal framework is described as creditor friendly with no Chapter 11 or equivalent procedures that might frustrate enforcement of security arrangements. The laws of the Cayman Islands provide certainty of execution and outcome to lenders and, as such, secured lending and fund financings to Cayman Islands borrowers are increasing in number and volume on a yearly basis.

ii Cayman borrowers

While Cayman Islands-domiciled funds and their portfolio companies dominate the borrowing market, we increasingly see corporate borrowers, often using dedicated Cayman Islands special purpose vehicles (SPVs). Given the absence of restrictions under Cayman Islands law and regulation as to investment objectives, Cayman Islands alternative investment funds are used for the full range of alternative strategies, including hedge, private equity, venture capital, infrastructure, real estate, private debt and cryptocurrencies, as well as traditional long-only investing. Consequently, the variety of fund structures and underlying investment pools necessitates a broad range of bespoke financing solutions.

iii Flexible financing structures

A newly formed private equity fund with a large amount of uncalled capital will typically borrow against the capital commitments of the investors (known as subscription facilities) and secure such borrowings by assigning the rights over the capital calls by way of security. Midway through the fund's investment period, the borrowing base may also be formed by reference to the net asset value of the fund's assets (known as hybrid or net asset value (NAV)

¹ Agnes Molnar and Richard Mansi are partners at Travers Thorp Alberga.

facilities). Private debt and credit funds more often seek NAV-type facilities, borrowing against a portfolio of loans and securing such borrowings by way of share security over the portfolio companies or raising capital via securitisation structures. Secondaries funds that acquire and hold limited partnership and other equity interests in existing funds may secure their borrowings over those interests. There has also been recent growth in NAV facilities for real estate and infrastructure funds.

As for the more liquid hedge fund alternative strategies, their financing may involve traditional lending (e.g., to bridge subscriptions and redemptions with security over collateral assets, much like a traditional mutual fund bridge funding), although their principal financing of trading activity typically entails gearing through margin, repurchase agreements, derivatives and other synthetic structures. This often leads to quasi-security arrangements, including title transfer security and sophisticated netting arrangements.

iv Documentation

Facility documentation is usually governed by New York or English law (largely based on the Loan Syndications and Trading Association (LSTA) and Loan Market Association (LMA) terms, respectively) and the terms vary depending on the framework of the fund and its investment structure. The documentation will need to be particularly tailored where the fund borrower has a single investor (known as a separately managed account) or there are multiple separately managed accounts in the structure (known as the umbrella structure). A Cayman Islands law-governed security package is determined by the structure and investments of the fund. Cayman Islands law provides full flexibility as to the types of assets over which security can be validly created. In a multi-tiered master-feeder structure, lenders might require cascading security in the security package, and with parallel fund structures, cross-collateralisation may be necessary. Corporate borrowers might also secure their financing over other assets such as ships, aircraft, receivables or intellectual property.

II LEGAL AND REGULATORY DEVELOPMENTS

The Cayman Islands continues to meet international regulatory and transparency standards in respect of its financial industry. We have outlined below some of the most significant regulatory developments.

i Mutual Funds Act and Private Funds Act

The Cayman Islands Monetary Authority (CIMA) is the authority responsible for financial services regulation, covering Cayman Islands open-ended funds, which fall under the Mutual Funds Act (2021 Revision) (MFA) and closed-ended funds, which fall under the Private Funds Act (2021 Revision) (PFA). Open-ended funds are defined as funds that offer redeemable interests to investors. Interest here means a share in a company, a unit in a unit trust or a partnership interest. Open-ended funds and their associated master funds must be regulated by CIMA to conduct their business.

A private fund, for the purposes of the PFA, is a fund in which investor funds are pooled for reward and professionally managed and where the investors do not have day-to-day control over the acquisition, holding, management or disposal of the fund's investments. The definition excludes funds regulated under the MFA, joint ventures, proprietary

vehicles, incentive schemes, pension funds, debt-issuing vehicles, holding vehicles, preferred equity financing vehicles, single managed accounts, syndication companies and certain other arrangements.

From a lender's perspective, investigating the regulatory status of a Cayman Islands borrower and its compliance with any relevant statutory requirements imposed under the MFA or PFA regimes should form part of their due diligence and facility agreement documentation process. A failure to register with CIMA and the subsequent loss of such registration represent a credit risk for the lender and it should therefore require a Cayman Islands borrower in the due diligence phase to provide evidence of compliance with all relevant requirements and undertakings in the finance documents to maintain its CIMA regulatory status and to comply with all other relevant regulatory obligations during the term of the financing.

In relation to Cayman Islands fund borrowers that are within the scope of the PFA, lenders need to be aware that a private fund cannot accept capital contributions without the fund first complying with the registration requirements imposed under the PFA. Given the importance of this registration, it is usually a condition precedent to closing fund finance facilities that closed-ended fund borrowers register with CIMA before finance is extended and undertake continuing compliance with applicable PFA obligations. In addition, contractual protections are customarily incorporated in the finance documents to serve as early warnings of non-compliance. However, robust and fully perfected security over capital call rights might further enhance a lender's right to demand an investor's capital contribution upon default by the fund borrower.

ii Securities Investment Business Act

Under the Securities Investment Business Act (2020 Revision) (SIBL), a Cayman Islands person who conducts securities investment business must be licensed by or registered with CIMA. Securities investment business includes the business of managing securities, advising on securities, arranging deals in securities or dealing in securities. Securities are widely defined to encompass shares, bonds, futures, options, contracts for differences and other typical investments. Accordingly, most fund managers, advisers and placement agents that are organised or have a place of business in the Cayman Islands fall within SIBL. Review of the status of a Cayman Islands fund manager under SIBL therefore forms part of the lender's due diligence, particularly when a closed-ended fund borrower has delegated to its manager the authority to exercise the power of the general partner to call capital contributions from the limited partners of the fund borrower.

iii Economic Substance Act

Depending on the precise role and structure of the borrower and its service providers, other regulatory laws may also be relevant, such as the International Tax Cooperation (Economic Substance) Act, (2021 Revision) (ES Act), which implements the economic substance standards of Action Point 5 of the Organisation for Economic Co-operation and Development Base Erosion and Profit Shifting initiative. The ES Act requires a relevant entity that carries on a relevant activity to satisfy the economic substance test and to make certain compliance-related filings with the Cayman Islands Tax Information Authority (TIA). Investment funds and the vehicles through which they invest are generally out of scope for the purposes of the ES Act; however, the service providers to a fund may be subject to the ES Act.

The relevant activities for the purposes of the ES Act are the businesses of banking, fund management, distribution and service centre, financing and leasing, headquarters, holding company, insurance, intellectual property and shipping. When a fund manager or a portfolio company (which might be a borrower, co-borrower or guarantor in the financing) is structured as a Cayman Islands company or limited liability partnership, it constitutes a relevant entity and, as such, its activity might fall within the scope of the ES Act.

Lenders should therefore be aware of the requirements of the ES Act that might be imposed upon their borrowers and those borrowers' service providers and, where relevant, should obtain comfort from due diligence and contractual protections (such as representations with regard to compliance and undertakings to provide evidence of such compliance) in the finance documents.

iv Anti-money laundering

The Anti-Money Laundering and Combatting of Terrorist Financing (AML) regime of the Cayman Islands requires Cayman Islands entities conducting relevant financial business (e.g., funds regulated under the MFA and PFA) to designate an individual to act as their anti-money laundering compliance officer and to adopt written policies and procedures to meet the requirements of the AML regime. From a lender's perspective, a non-AML compliant Cayman Islands borrower could pose a reputational risk or even result in non-compliance with its own AML obligations. In serious cases of non-compliance with the Cayman Islands' AML regime by a borrower, CIMA has the power to apply to court to seek an order for its winding-up, something that would no doubt trigger a financing default under the finance documents. Therefore, as part of their due diligence, lenders should request evidence from prospective borrowers of compliance with their AML obligations and may also insert covenants in the finance documents requiring fund borrowers to maintain compliance with the requirements of applicable AML regimes.

III TAX CONSIDERATIONS

The Cayman Islands does not have a direct taxation regime as a matter of centuries-old fiscal policy. Accordingly, no taxes are imposed under Cayman Islands law on the profits, income, gains or appreciations of Cayman Islands borrowers and there is no withholding in respect of any dividend, distribution or interest payment by a Cayman Islands borrower. Nominal stamp duties apply to documents executed or brought into the Cayman Islands. There are no exchange or currency controls in the Cayman Islands.

Notwithstanding the absence of direct taxation, a Cayman Islands borrower formed as an exempted company desiring additional comfort on this matter may obtain an undertaking from the government of the Cayman Islands that for a period of 20 years from the date of the undertaking certificate, no laws of the Cayman Islands imposing any tax on profits, income, gains or appreciation shall apply to such borrower and that no tax in the nature of estate duty or inheritance tax shall be payable on the equity interests of that borrower. A borrower formed as an exempted limited partnership may obtain a similar undertaking for a period of 50 years. A unit trust fund may also obtain a similar undertaking for a period of 50 years, provided it excludes investors resident or domiciled in the Cayman Islands (other than Cayman Islands exempted companies and non-resident companies).

The ongoing global initiatives to enhance anti-money laundering and counter-terrorist financing practices and to establish Foreign Account Tax Compliance Act (FATCA) and

Common Reporting Standard (CRS) regimes have overall proved positive for Cayman Islands funds and corporate borrowers, in that the Cayman Islands applies the highest international standards of anti-money laundering and tax transparency. The required administrative functions and procedures are now routinely delegated to administrators as part of their agreed compliance processes. Cayman Islands fund structures are generally subject to the FATCA and CRS reporting regimes of the Cayman Islands. FATCA requires foreign financial institutions (FFI) (Cayman Islands funds are largely in scope) to report information on accounts of US taxpayers to the US Internal Revenue Service. The conclusion of a Model 1B intergovernmental agreement between the US and the Cayman Islands facilitates compliance with FATCA reporting requirements. A Cayman FFI will report directly to the TIA and once it complies with the relevant reporting and procedural requirements, it will be treated as deemed a compliant FFI and shall not be subject to automatic withholding on US source income. The Cayman Islands has also entered into and implemented similar multilateral arrangements with more than 100 jurisdictions as part of the CRS regime, which provides for the collection and automatic disclosure of information to the tax authorities in the jurisdiction of tax residence of the investor of the investment amount of that investor in a Cayman Islands fund and in respect of any distributions paid to that investor. There is a generally a very high level of compliance with the FATCA and CRS regimes and their reporting requirements in the Cayman Islands and lenders can obtain comfort from ongoing compliance from tailored contractual protections in the finance documents.

IV CREDIT SUPPORT AND SUBORDINATION

i Security

As in any common law jurisdiction, the purpose of any security created in favour of a lender is to recognise that the lender will be able to look to the particular asset or the sale proceeds obtained from that asset if the borrower fails to discharge its liabilities in accordance with the finance documents. Moreover, a secured lender will be protected on the borrower's insolvency and should be repaid in full and ahead of the borrower's other creditors subject to any rules of priority, provided its security is validly perfected and not capable of being set aside. Cayman Islands law-governed security documents usually grant a power to the secured creditor to appoint a receiver under the terms of the security document to sell the secured asset on its behalf. Although this contractual power is typically exercisable upon a borrower default, the parties can freely agree how to govern their contractual relationship and, as such, a receiver could be appointed even before a default in circumstances where, for example, the secured creditor reasonably believes that its security is in jeopardy. A Cayman Islands chargor may grant security over any of its assets and the four main types of security recognised under Cayman Islands law are mortgages (legal and equitable), charges (fixed and floating), liens and pledges. This chapter does not cover the creation of security over Cayman Islands real estate, aircraft, intellectual property and ships.

Mortgages

Legal mortgages

Legal mortgages are the most comprehensive and secure form of security. A legal mortgage is the transfer, by conveyance or assignment, of the legal ownership of an asset by way of security. This transfer is subject to an obligation to retransfer ownership of the asset to the mortgagor if the mortgagor discharges its liabilities. Advice should always be obtained as to

whether any such transfer triggers an onshore tax liability. A legal mortgage over debts or choses in action created by an absolute assignment in writing (which is not purported to be by way of charge only)² can secure borrowings over capital commitments or provide security for borrowings of limited partners over their partnership interests.³ Additionally, in order for such an assignment to take effect as a legal assignment, express notice in writing must be given to the debtor, trustee or other person from whom the assignor would otherwise have been entitled to claim the debt or chose in action.⁴ In the case of security over investors' capital commitments, the relevant limited partners (for partnerships) or shareholders (for exempted companies) and, in the case of security over a partnership interest, the general partner (on behalf of the partnership), should receive the notice of assignment. Lenders should review the relevant constitutional documentation (partnership agreement or articles of association, as applicable) to ensure that granting of security and its enforcement, or both, is permissible (or at least not prohibited or hindered thereunder) and, if it is not, should insist upon the removal of any prohibition of transfer or assignment in favour of the secured creditors prior to the financing being put in place.

Equitable mortgages

An equitable mortgage is the transfer by the mortgagor of its beneficial interest in the relevant asset to the mortgagee while the legal interest remains with the mortgagor. An equitable mortgage is weaker than a legal mortgage because a bona fide purchaser for value of the legal estate without notice of an equitable mortgage will take free from the equitable mortgage. An assignment will be equitable if it relates to an equitable interest over a chose in action, relates to future rights⁵ or does not satisfy the notification requirement of a legal assignment.

Charges

Charges are always equitable in nature. Chargors do not transfer legal or equitable interests in the asset to the chargee; nor do they confer a right of possession. Instead, the chargee has a right to resort to the asset in order to realise it and apply the sale proceeds towards payment of its debts. A fixed charge over a particular asset should give the chargee control of any dealing or disposal of the asset of the chargor as dealing or disposal of the secured asset will be prohibited under the security document. This prohibition is crucial, as without sufficient control over the secured asset being granted in favour of the chargee, the fixed charge risks being re-characterised as a floating charge. In contrast to a fixed charge, a floating charge is floating over the charged asset prior to default, meaning that the chargor is free to deal with the asset without reference to the chargee until the occurrence of a default, which causes the floating charge to crystallise over the asset and become a fixed charge. The Exempted Limited Partnership Act (2021 Revision) (ELP Act) expressly recognises that any asset of an exempted limited partnership may be subject to a floating charge.

Assignment by way of charge generally refers to the circumstances where the chargee and the chargor contractually agree that the chargee has a fixed or floating charge over the

2 See Section IV.i 'Charges'. Charges do not transfer an interest in the secured asset but rather create an encumbrance over the secured asset that would entitle the chargor to exercise the power of sale and satisfy outstanding payment obligations out of the sale proceeds.

3 See Sections 31 and 32 of the Exempted Limited Partnership Act (2021 Revision).

4 See Section 5(2) of the Property (Miscellaneous Provisions) Act (2022 Revision).

5 See *Holroyd v. Marshall* (1862) 11 ER 999.

choses in action. The effect of the charge (being an encumbrance on the choses in action) is that the benefit of the choses in action is assigned to the chargee for the duration of that charge so it obtains the right to use the choses in action (and receive any proceeds obtained in respect of it) to discharge the debt.

Liens and pledges

Liens and pledges are dependent upon delivery of possession of the secured asset; thus, they are rarely used in Cayman law-governed security structures.

ii Registration

There is no public system of registration of security in the Cayman Islands and therefore no basis for constructive knowledge of a registered charge. A Cayman Islands company security provider is required under the Companies Act (2023 Revision) (Companies Act) to note a short description of the secured asset, the amount of the security and the name of the secured creditor on its internal register of mortgages and charges, which must be maintained at its registered office in the Cayman Islands. Failure to register leaves the mortgagor or chargor and its directors open to financial penalty but does not invalidate the security itself and, unlike some jurisdictions (e.g., England and Wales), there is no statutory time limit within which registration must take place. It is nevertheless important for lenders to review a company's internal register of mortgages and charges as part of their initial due diligence and to ensure that their security is registered as soon as possible following its creation (although this will not by itself guarantee priority in ranking of such mortgage or charge over any mortgage or charge existing prior to its creation).

In addition to updating the register of mortgages and charges with details of security created by the company itself, when a mortgagor or chargor grants security over its shares in a Cayman Islands incorporated company, it is common practice to enter a notation in the register of members of that company to give notice of the security to third parties. However, the memorandum and articles of association of a Cayman Islands company and the register of members of a Cayman Islands exempted company are not publicly available documents. As such, not only is there no principle of constructive knowledge in relation to the contents of those documents, but it also follows that appropriate specific consents to inspect them must be obtained. In the case of a security interest granted over a partnership interest in a Cayman Islands exempted limited partnership, the general partner is required under the ELP Act to note the security interests in respect of which it has received valid notice in the register of security interests of the partnership and under the ELP Act, such register may be inspected by any person during usual business hours.

iii Guarantees and other forms of credit support

Guarantees

Under a guarantee, the guarantor guarantees the payment obligations of one party to a contract to another party thereto. Subject to the terms of the guarantee document, lenders do not necessarily obtain any security solely by virtue of the guarantee. The provision of a guarantee by a company is subject to any limitations contained in the guarantor's constitutional documents and will also be subject to corporate benefit limitations. In a master-feeder financing, when lenders request that the feeder entity guarantees the borrowings of the master fund (instead of entering into cascading security over the uncalled capital or other assets of the feeder entity),

it is advisable to apportion the guarantee of the feeder entity to its capital commitment in the master fund. Otherwise the feeder guarantor might ‘over-collateralise’ the borrowings of the master fund and perhaps be left, at best, with a deferred subrogated claim on the master fund.

Quasi security

Certain financing structures involving, for example, sale and leaseback or repurchase of securities, factoring, retention of title, netting (including multilateral set-offs) and other structures involving the transfer of ownership of securities are all common in the Cayman Islands. The inclusion of netting, set-off, limited recourse and non-petition provisions in contracts is a well-established practice and recognised under Cayman Islands law, and such provisions are crucial building blocks in certain SPV and synthetic financing structures. Segregated portfolio companies offer structural segregation by ring-fencing assets and liabilities on a segregated portfolio basis. Negative pledges included in security documents have proved useful in preventing the creation of subsequent charges ranking in priority or *pari passu* with the security interest that they purport to protect.

iv Priorities and subordination

Cayman Islands law recognises both contractual and structural subordination and the Companies Act specifically provides that an otherwise enforceable agreement to contractually subordinate claims shall be recognised in a liquidation of a Cayman Islands company. The corporate veil may only be pierced in very narrow circumstances,⁶ and there is no general principle of substantive consolidation upon insolvency.

The priority of competing security interests (when a number of creditors have taken security over the same asset) is determined by reference to established English common law rules, which Cayman Islands law generally follows. In practice, however, secured creditors often avoid the issue by putting in place a deed of priority or subordination. Absent such an arrangement and subject to perfection requirements, the following rules apply:

- a* a fixed security interest will have priority over a floating charge even if that fixed security interest is created after the floating charge (unless the subsequent fixed chargee has actual or constructive notice of a negative pledge included in the security document preventing such fixed charge from being created);
- b* a fixed charge and mortgage rank in priority according to the date of their creation (although this principle can be circumvented by tacking⁷ and a bona fide purchaser for value of a legal estate without notice will override equitable interests, including the interest of a charge);
- c* floating charges over the whole undertaking of a company rank in priority according to the date of their creation;⁸ and
- d* security over choses in action rank in priority according to the date of notification of debtors (*Dearle v. Hall*).

An asset in respect of which a valid security interest exists at the time of liquidation of a Cayman Islands company or exempted limited partnership falls outside the scope of its

6 See *Prest v. Petrodel Resources Ltd* (2013) UKSC 34.

7 See *Hopkinson v. Rolt* (1861) 9 HL Cas 514.

8 See *Benjamin Cope & Sons Ltd* (1914) 1 Ch 800.

liquidation and the secured creditor is generally free to enforce its security at any time in accordance with its terms. Upon insolvency, the assets of a company or exempted limited partnership are to be distributed in the following order of priorities (and always subject to the priority of competing security interests):

- a* in satisfaction of the rights of fixed charge creditors;
- b* in satisfaction of the expenses and costs of the liquidation (including the liquidator's remuneration);
- c* in satisfaction of the rights of preferred creditors (e.g., taxes, wages and certain sums due to employees);⁹
- d* in satisfaction of the rights of floating charge creditors;
- e* in satisfaction of the provable debts of the unsecured creditors of the company or exempted limited partnership (but having regard to priority where a creditor is subordinated to other creditors);
- f* in paying statutory interest on any proved debt; and
- g* distribution of any surplus assets to the shareholders of the company or limited partners of an exempted limited partnership, in accordance with their shareholdings or partnership interests, respectively.

v Foreign law considerations

Where a combination of jurisdictions are involved in the structure, there is an added level of complexity as different governing laws may govern different aspects of the contractual arrangements. In complex, cross-jurisdictional fund structures, while the governing law of the financing documents is usually English or New York law, the governing law of an exempted limited partnership agreement in respect of a Cayman Islands exempted limited partnership, for example, would be the laws of the Cayman Islands. In some cases, the general partner could be formed outside the Cayman Islands, and in those circumstances, generally, we would expect that security over the capital call rights of the general partner will follow the governing law of the partnership agreement, although due diligence of the documentation is certainly required.

Similar issues should be considered in light of the *situs* of other security assets. The Cayman Islands do not generally have any mandatory provisions of law that would require Cayman Islands security to be taken over assets with their *situs* within the jurisdiction and courts will generally respect and give effect to valid foreign law security interests. Consideration should, however, be given to the applicable governing law and *situs* in the event of enforcement.

Regardless of the governing law of the security, in respect of any security taken over an asset with a Cayman Islands *situs*, any Cayman Islands law perfection requirements should be followed. Moreover, where the mortgagor or chargor is a Cayman Islands company or a limited partner of a Cayman Islands exempted limited partnership, the foreign law security should be noted in the register of mortgages and charges, in the case of a company, and in the register of security interests, in the case of a security interest created over a partnership interest in a Cayman Islands exempted limited partnership.

⁹ See Section 141 of the Companies Act (2022 Revision). Preferential debt includes wages, certain other sums due to employees, taxes and sums due to depositors of an insolvent bank holding an 'A' licence issued under the Banks and Trust Companies Act (2021 Revision).

The priority of foreign law security granted by a Cayman Islands security provider over Cayman Islands or foreign assets (assuming such security is validly created and fully perfected under foreign law) will, as a matter of Cayman Islands law, depend upon the subject matter of the security. In the case of tangible movables (e.g., a bearer bond), the question will be decided according to the *situs* of such tangible movable. In the case of intangible movables (e.g., debts and other choses in action), the governing law of the intangible movable or, in some cases (for example, financial instruments), the *lex situs* will determine priority. In some cases (provided the relevant laws allow), the lender may require two carefully formulated security documents to take security over the same asset, one governed by the law of the location of the asset and one governed by the law of the finance documents. This may afford the lender flexibility to choose the most convenient jurisdiction for enforcement or insolvency proceedings.

V LEGAL RESERVATIONS AND OPINIONS PRACTICE

i Corporate benefit

The directors of a Cayman Islands company proposing to grant a guarantee or security over its assets or to guarantee or secure the obligations of another entity must ensure that this is in the best interests of the guarantor or security provider as a whole. If the guarantor or security provider does not derive commercial benefit from the transaction, the corporate benefit to the company could be called into question. In those circumstances a shareholder, creditor or liquidator of the guarantor or security provider could bring an action against the company before a Cayman Islands court, which could order that the guarantee or security be set aside.¹⁰ In addition, the directors could incur personal liability where they have breached their fiduciary duty to act in the best interests of the company, although collateral contractual provisions usually provide for broad director exculpation and indemnification.

ii Financial assistance

There are no statutory financial assistance rules under Cayman Islands law equivalent to those existing under English law.

iii Insolvency

Companies

Upon commencement of a formal insolvency process, certain transactions of an insolvent company are susceptible to challenge, pursuant to the provisions of the Companies Act, as outlined below. These legislative measures derive from the common law principle that a court will not allow an entity to arrange its affairs to frustrate the legitimate interest of its creditors in the event of its insolvency.

Fraudulent dispositions

A disposition of property made at an undervalue by or on behalf of a company with an intent to defraud its creditors shall be voidable by the liquidator. Such action must be brought within six years from the date of the relevant disposition. The burden of proof in establishing

10 See *Prospect Properties Ltd v. McNeill* (1990–1991) CILR 171.

the intent to defraud lies with the liquidator. Note that creditors may in some circumstances bring fraudulent disposition claims themselves, outside of the liquidation process, in accordance with the provisions of the Fraudulent Dispositions Act.¹¹

Fraudulent trading

If in the course of the winding up of a company, it appears that any business of the company has been carried out with an intent to defraud its creditors or the creditors of any other person or for any fraudulent purposes, the liquidator may apply to court for a declaration that any persons who were knowingly parties to such fraudulent trading shall be liable to make such contributions (if any) to the company's assets as the court thinks proper. There is no prescribed time under the Companies Act prior to the winding up of the company during which the contested trading must have taken place.

Voidable preferences

Every conveyance or transfer of property or charge thereon and every payment obligation and judicial proceeding made, incurred, taken or suffered by a company at a time when it was unable to pay its debts (as defined in the Companies Act) and made or granted in favour of a creditor with a view to giving that creditor a preference over the other creditors of the company shall be invalid if it occurred within six months immediately preceding the commencement of liquidation of the company.

Clawback claims are quite rare in the Cayman Islands. Bringing a successful claim would be challenging, given the difficulty to satisfy the requirements of fraudulent intent or an intent to prefer. Many of the above provisions are based on historic legislation from England and Wales, which have since been updated to lower the threshold to bring a claim. A lender with valid first ranking security is unlikely to be affected by a clawback claim in any event because the assets that are the subject of their security interest will fall outside the scope of the liquidation of the company, provided the original grant of security is not the subject of the clawback challenge.

Exempted limited partnerships

Pursuant to the ELP Act, many of the rules regulating the winding up and insolvency of Cayman Islands companies apply to the winding up of exempted limited partnerships. For instance, in principle, a liquidator of an insolvent limited partnership could bring a clawback claim. Partnership assets in respect of which valid security has been created also fall outside the scope of the dissolution of an insolvent limited partnership in the same manner as a company.

iv Recognition of foreign law and foreign judgments

The courts of the Cayman Islands will recognise and give effect to the choice of the parties to a contract of a particular governing law if the selection was made in good faith and would be upheld as a matter of that governing law by the courts of that jurisdiction.

Where the parties have agreed to submit disputes arising out of or in connection with their contract to the courts of a particular jurisdiction, a judgment obtained in such jurisdiction (other than certain judgments of a superior court of any state of the Commonwealth of

¹¹ See Fraudulent Disposition Act (1996 Revision).

Australia) will be recognised and enforced in the Cayman Islands at common law without any re-examination of the merits of the underlying dispute, by an action commenced on the basis of the foreign judgment debt. This is provided that such judgment is given by a foreign court of competent jurisdiction and is final, for a liquidated sum, not in respect of taxes or a fine or a penalty, and was not obtained in a manner and is not of a kind the enforcement of which would be contrary to the public policy of the Cayman Islands.

VI LOAN TRADING

As mentioned above, New York or English law tends to be selected as the governing law in financing transactions in which Cayman Islands borrowers or obligors are involved. When those facility agreements are based on LSTA/LMA forms, they are designed to be freely transferable by the lenders. Fund borrowers in particular heavily negotiate loan transfers and attempt to regulate potential eligible transferees by way of white lists, black lists or explicit transfer restrictions in the facility agreements. In addition to the provisions of the applicable facility agreement, one must also have regard to any applicable provisions of the relevant governing law to ascertain any rules regulating loan-trading transactions.

In terms of any Cayman Islands law-governed security interest that has been created to secure the obligations arising under a tradable loan, the transfer or assignment provisions in the relevant security document or documents typically follow those of the facility documentation. If the loan is validly transferred to a new lender, the Cayman Islands law-governed security should also transfer upon execution of the relevant transfer documentation.

LSTA/LMA form facilities tend to be designed as syndicated structures whereby the security interest is granted in favour of a security trustee who holds it in trust for the benefit of the secured creditors. Cayman Islands law applies common law trust principles and therefore recognises trust mechanics. Assuming that the security trustee remains in place following a loan transfer, no further registration requirements need to be completed. In other circumstances (e.g., in respect of bilateral loans, where no security agent has been appointed or if there is a change of security agent), the details of the new creditor (and security agent, if applicable), following a loan and security transfer, should be noted on the register of mortgages and charges of the borrower.

VII OTHER ISSUES

There are currently no other issues of note.

VIII OUTLOOK AND CONCLUSIONS

While the outlook remains strong in 2023, several important factors will weigh on investors' and managers' minds as they think about doing deals. The macroeconomic environment, market volatility and heightened regulatory oversight present challenges for the fund industry. Increased inflation and the war in Ukraine have dialled up global disruption, causing geopolitical and economic uncertainties around supply chains, energy prices, and other economic factors, as well as untold human suffering. The question of outflows of capital from China remains another known unknown, and the latest liquidity crises of the banking sector have triggered a sharp decline in global bank stock prices and intervention by regulators to prevent a global meltdown.

Inflation, tightening Central Bank monetary policies, the appreciation of the US dollar and rising commodity, oil and food prices are contributing to currency depreciation in emerging markets. Private equity managers will continue to prepare their portfolios for difficult market conditions. For a continued bear market, private equity managers are pumping up the liquidity.¹² Uncertainty around the sustainability of the current growth rate is likely to persist, and inflation and tax rises will remain a major concern. For the financing market, the combination of lower asset prices and increased financing costs may increase competition in fundraising, and we expect the increasing use of bespoke structures that are tailored to sponsors' needs. Collateralised fund obligation structures aggregating multiple funds assets, rated note structures or an increasing use of continuation funds are all part of those bespoke solutions. We expect the further growth of secondaries markets using deferred consideration, flexible debt financing and cross-fund equity financing as useful tools. Private equity and venture capital investments in Central and Eastern Europe are ready to ride the rising tide of growth as private credit managers expect growth to take place across emerging markets.

Private credit, as the second-largest alternative asset class after private equity, has performed strongly, mainly as it offers benefits for investors looking for strong growth opportunities at a time of constrained mainstream lending. Recent challenges within the banking sector such as liquidity mismanagement and extensive bailouts are also shifting our focus towards alternative credit providers. Private credit provides alternative sources of credit and liquidity to the economy. They are essential for growth. They provide liquidity when other credit providers are retrenched. Distressed assets and direct lending are currently the most sought-after private credit strategies, making up 60 per cent of AUM in the asset class.¹³ According to the Alternative Credit Council, the estimated AUM of private credit is at US\$805 billion,¹⁴ out of which direct lending's AUM of US\$452 billion is now double that of the second-largest private credit strategy, distressed debt's AUM at US\$277 billion. Environment, social and governance (ESG) is also of growing importance for both investors and fund managers, and some of the largest private credit funds have launched record-breaking funds with ESG considerations.

With the continuous rise of preferred equity and hybrid facilities, the fund finance market is poised for more growth with the increase of alternative credit providers, and we expect that sponsors will be turning to fund-level credit to fill liquidity needs both as a defensive measure and for opportunistic investments. Flexibility will remain paramount when those private equity sponsors are looking for robust liquidity solutions for their complex and bespoke fund structures. We have no doubt that the growth of the private equity and private credit markets will continue with considerable pace, and with that, we anticipate increasingly complex fund structures paired with flexible liquidity solutions. We also anticipate that these increasing complexities will solidify the position of the Cayman Islands as an offshore jurisdiction for investment funds due to its sophisticated legal and regulatory framework, and we expect that some of the robust liquidity solutions will become core financing options throughout the life cycle of investment funds.

12 Institutional Investors: Private Equity's Outlook Is Mixed as They Prepare for Headwinds, published on 14 October 2022.

13 Prequin Global Private Debt Report 2022.

14 Debevoise & Plimpton – 2022 Private Equity Mid-Year Review and Outlook.