

## Mergers and consolidations of Cayman Islands companies

May 2009

The Companies (Amendment) Law 2009 adopted this month in the Cayman Islands introduces a new and much-needed statutory merger regime which does not require court application or approval. Previously Cayman Islands companies could merge or amalgamate only pursuant to a scheme of arrangement procedure which required the approval of the Cayman Islands Court. In practice rather than submit to this cumbersome and costly process Cayman Islands companies needing to merge would often migrate into BVI or Delaware using statutory deregistration and continuation provisions, merge in such jurisdiction and then the successor company would migrate back to the Cayman Islands.

The new law brings the Cayman corporate regime into line with the regimes of other offshore jurisdictions such as BVI and Delaware which both have merger regimes in place and in the majority of cases it should prove a simple and effective method of merging corporate enterprises. The first part of this part of this note will summarise the procedure. The second part of the note will deal with the interpretation and practical ramifications of the shareholder consent requirement.

### Overview

The law provides a process for *merger* (meaning the assets, rights, obligations and liabilities of two or more companies are assumed by one of those companies) or *consolidation* (meaning the assets, rights, obligations and liabilities of two or more companies are assumed by a new Cayman Islands company). In this note *Merger* will be deemed to include merger and consolidation, a *Constituent Company* is a company participating in a *Merger* and a *Successor Company* is the new or existing company acquiring the businesses of the Constituent Companies.

### Who can be party to a Merger?

- 1) Any Cayman Islands company limited by shares other than a segregated portfolio company.
- 2) Any foreign company provided that such company is not the Successor Company.

### Material Conditions to Merger

**Good Standing and Solvency** – each Constituent Company must be in good standing and solvent – the Cayman Islands applies a cashflow test of ability to pay debts as they fall due for solvency.

**Written Plan** – the directors of each Constituent Company must prepare and approve by board resolution a written Plan of Merger.

**Shareholder Consent** - a shareholder consent is required from the shareholders of each Constituent Company (as to which see below).

**Regulatory conditions** – any proposed merger which involves a regulated entity such as a bank or insurance company must comply with applicable regulatory requirements.

**Foreign law conditions** – in the case of any Merger including a foreign entity the entity must be permitted to merge by applicable foreign laws and its constitutional documents.

**Secured Creditors** - the consent of secured creditors of the Constituent Companies is required unless a Cayman Islands court waives such requirements.

### Contents of the Merger Plan

Each Merger Plan must contain details of:

- 1) the Constituent Companies and respective shareholdings;
- 2) the rights and restrictions applicable to shares in the Successor Company and the shares, cash or other property each shareholder of a Constituent Company will receive – the merger regime is flexible and permits shares in Constituent Companies to be exchanged for shares in a Successor Company and/or any other assets, debt obligations, cash or other property of any kind;
- 3) the directors and officers of the Successor Company;
- 4) any benefits to be received by the directors of Constituent Companies;
- 5) the name, registered office and memorandum and articles of association of the Successor Company; and
- 6) the date on which the Merger Plan is to become effective.

### Material Documents to accompany Merger Plan

The following documents are required to accompany any Merger Plan:

- a director's declarations in respect of:
  - (i) solvency;
  - (ii) that the Merger is not intended to defraud unsecured creditors;
  - (iii) that all applicable regulatory requirements have been complied with; and
  - (iv) that any Constituent Company not being the Successor Company has retired from any fiduciary offices held by it.
- a statement of the assets and liabilities of each Constituent Company;
- an undertaking to notify shareholders and creditors of the Merger and to publish a notice of the Merger in the Cayman Islands Gazette; and
- a good standing certificate.

### Shareholder Consent

The law provides requirements for:

- (a) a shareholder resolution by majority in number representing seventy-five per cent in value of the shareholders *voting together as one class*; and
- (b) if the shares to be issued to each shareholder in the consolidated or surviving company are to have the same rights and economic value as the shares held in the constituent company, a special resolution of the shareholders [generally 2/3rds of the shareholders voting at a shareholder meeting unless a higher percentage is specified in the articles] *voting together as one class*.

Shareholders entitled to vote include all shareholders irrespective of whether or not their shares have voting rights under the articles.

It is our view that the *and* linking the two sub-sections may be an error and should be read as *or* but even if it is to be read as *or* it is unlikely to be material as paragraph (b) will rarely apply in the usual course as in any Merger of material corporate entities the shareholders are unlikely to receive shares having the same rights and economic value in the Successor Company as the assets, rights and obligations attributable to shares of the Successor Entity will usually be an aggregate of those of each Constituent Company.

### Parent/Subsidiary Merger

The law provides that the shareholder consent is not required in the case of any Merger of a parent with its subsidiary company with subsidiary being defined as a company 90% or more of whose voting shares are held by the parent company. The definition which refers to voting shares only is not ideal as the voting and economic ownership of Cayman Islands companies is often split for tax, regulatory or ease of administration reasons. Cayman hedge funds, for example, often have one class of voting management shares with no material economic rights and one or more classes of non-voting participating shares held by investors.

### Dissenting Shareholders

The law provides a right to dissenting shareholders to obtain fair value for their shares (determined by agreement or failing that on court application). This right will rarely apply as it is disapplied where (i) shares in the relevant Constituent Company are traded on an open market on a recognised stock exchange or recognised interdealer quotation system; or (ii) where the shareholders of a Constituent Company will receive (A) shares in the Successor Company; or (B) shares in any other company whose shares are traded on an open market on a recognised stock exchange or recognised interdealer quotation system.

### Practical ramifications

The shareholder consent requirement provides for shareholders to vote together as one class and viewed in isolation might be seen to give rise to inequitable results when applied to companies with minority shareholders having a separate class of shares with entrenched rights. Examples of this might be a class of preference shares providing a preferred fixed return or a class of shares with a performance-linked return held by company management, particularly if a preference is lost under the constitution of the Successor Company.

Even though shareholder class consents are not expressly required by the legislation clients should note that in preparing any Plan of Merger the directors of each Constituent Company have overriding common law obligations to take into account the respective interests of all classes of shareholders. We would therefore recommend that shareholder class consents are always obtained approving the terms of any Plan of Merger before adoption. Going forward, particularly when acting for minority shareholders, we would also recommend specifically including in shareholder class rights an express right to approve or veto any proposed Plan of Merger before such plan is executed or filed on behalf by the Directors.

*Should you require any further information or guidance on this subject please contact Jonathan Culshaw ([jonathan.culshaw@harneys.com](mailto:jonathan.culshaw@harneys.com)) in our London office.*

*The foregoing discussion and analysis is for general information purposes only and not intended to be relied upon for legal advice in any specific or individual situation*