Snapshot: Cayman Islands Court of Appeal clarifies test for security for costs

Insights - 21/04/2022

The Cayman Islands Court of Appeal [1] has recently delivered helpful clarification on the principles which apply with respect to security for costs when the official liquidators of an insolvent fund seek to bring claims against its former management. Where it is clear to the Court that a defendant was responsible for management decisions immediately before a company entered insolvency, the Court may exercise its discretion, notwithstanding the impecuniosity of the plaintiff company, not to order payment of security for costs.

It is well settled that in the Cayman Islands, if a plaintiff fails to make out its claim against a defendant, it will ordinarily be liable for the defendant's costs for defending those proceedings. The Companies Act (2022 Revision) contains a statutory jurisdiction by which the Court, if satisfied that a Cayman Islands plaintiff company might have insufficient assets to satisfy a costs award in favour of a defendant, will order the plaintiff company to give sufficient security or have proceedings stayed pending satisfaction of security requirements. The provision for costs is known as "security for costs". [2]

The statutory jurisdiction is exercised by the Court in two stages:

1. is the Court satisfied that there is reason to believe that if the defendant is successful in the defence, the assets of the company will be insufficient to pay the defendant's costs?
2. and, if so, the Court will exercise its discretion to decide whether to order security for costs having regard to all the circumstances of the case

Where official liquidators bring recovery claims on behalf of insolvent estates, it is not ordinarily disputed that the insolvent plaintiff company meets the first stage activating the security for costs jurisdiction (ie if unsuccessful, its assets will be insufficient to pay the defendant's costs). The focus for the Court is, therefore, whether the other circumstances of the case make it appropriate to order security for costs.

In *Traded Life Policies Fund*, the fund acting by its Joint Official Liquidators brought claims against the former directors, and the former service providers to the fund arising from, among other things, breach of fiduciary duties, allegations of fraudulent trading, overpayment of management, director, adviser and administrative fees, management expenses and policy movement fees which were purportedly unmerited. Focussing its attention on the second stage of the test, the Court of Appeal considered authority from the English High Court [3] which sets out the relevant criteria for the Court to consider when exercising its discretion. In particular, the Court of Appeal considered whether "the company's want of means has been brought about by any conduct by the defendants", also known as the "impecuniosity factor".

Generally, a court considering an application within proceedings will not make a determination as to liability for any particular aspect of a case, because issues of liability are usually reserved for the trial court which will have considered the relevant evidence and will have the benefit of written and oral submissions on the matters in dispute. In the context of security for costs, the court is restrained from making a determination about whether the plaintiff company's financial dire straits are a consequence of any action or inaction by the defendants. Accordingly, where responsibility and liability are intertwined the Court will err on the side of caution against making findings as to liability and will often award security for a defendant's costs.

For this reason, at first instance the Grand Court granted security for costs. It considered that responsibility for the plaintiff company's impecuniosity and liability were "so inextricably bound together in this particular case so as to make it difficult to identify a clear factual position in advance of any trial".

However, the Court of Appeal carefully considered different lines of authority on this facet of security for costs and emphasised the distinction between responsibility and liability for a company's insolvency. The Court of Appeal ultimately found that in specific circumstances, the Court is able to divorce responsibility (for a company's impecuniosity) from liability where it is clear that a defendant was responsible for management decisions immediately before a company entered insolvency. The Court was satisfied that its conclusion "involves no element of prejudgment on the substantive issues raised in the proceedings" and overturned the decision on appeal.

The decision is particularly relevant to Cayman Islands' insolvency, fraud and asset recovery practitioners who regularly consider the availability and merits of bringing claims against current and former directors who profited from their positions and left the company or fund in financial ruin. It should also serve as a reminder to the management of Cayman Islands companies facing solvency issues and may reduce the potency of using security for costs as a means to reduce a claimant's appetite to pursue former management for losses.

[1] *Traded Life Policies Fund in Official Liquidation et al v Jeremy Leach et al* (Unreported, CICA, 21 December 2021)

[2] For principles governing security for costs more generally, please see our briefing: The Grand Court of the Cayman Islands grants security for costs in Abraaj related proceedings

[3] *Sir Lindsay Parkinson & Co Ltd v Triplan Ltd* [1973] 1 QB 609

About Ogier

Ogier is a professional services firm with the knowledge and expertise to handle the most demanding and complex transactions and provide expert, efficient and cost-effective services to all our clients. We regularly win awards for the quality of our client service, our work and our people.

Disclaimer

Meet the Author

Gemma Bellfield (nee Lardner)

Partner

Cayman Islands

E: gemma.bellfield@ogier.com

T: +1 345 815 1880

Key Contacts

Jordan Constable

Associate

Cayman Islands

E: jordan.constable@ogier.com

T: +1 345 815 1808

Related Services

Dispute Resolution

Enforcement of Judgments and Awards

Fraud and Asset Tracing

Funds Disputes

Corporate and Financial Services Disputes

Legal

Related Sectors

Restructuring and Insolvency