HARNEYS
Cayman Islands

guide

Segregated Portfolio Companies

Any Cayman Islands exempted company (the most common Cayman corporate vehicle limited by shares), including those to be established as funds, may be registered as a segregated portfolio company (an ***SPC***). Registration as an SPC can be made either at the point of incorporating the company or subsequently. The concept of an SPC is that the relevant company, which remains a single legal entity, may create separate segregated portfolios (each, a ***Portfolio***) such that the assets and liabilities of each such Portfolio are statutorily ring-fenced from the assets and liabilities of each other Portfolio and the general assets and liabilities of the company. Income and other property of an SPC not attributable to any Portfolio constitute the general assets of the company.

INTRODUCTION TO SPCs

Benefits

The principal benefit of using an SPC for establishing segregation of assets and liabilities (as opposed to alternative methods such as contractual limited recourse wording) arises out of the fact that the ring-fencing is embedded in statute rather than contract and so has the benefit of statutory recognition in the place of incorporation of the SPC. The other important benefit of the SPC regime is that as a statutory regime, it also binds non-consensual third parties and so extends the ring-fencing concept to parties who would otherwise not be covered by contractual ring-fencing.

Satisfaction of Liabilities

The liabilities of any specific Portfolio may not be met out of the assets of any other Portfolio. The general liabilities of an SPC may not be satisfied out of the assets attributable to any Portfolio but the general assets of an SPC can be applied to the liabilities of any Portfolio to the extent that the assets attributable to such Portfolio are insufficient to meet Portfolio liabilities, unless the Articles of Association of the SPC expressly prohibit such application of general assets. It is usual for the Articles to create such prohibition to prevent the failure of a Portfolio from having any adverse effect on the general assets of the SPC.

Portfolio Shares, Dividends and Distributions

One or more classes of shares may be designated to each Portfolio and the proceeds of issue of such shares are allocable to that same Portfolio alone.

Principles relating to the payment of dividends or other distributions, and the payment of the redemption price of shares, are applied to each Portfolio in isolation as if each Portfolio were a separate legal entity. As such, payments in respect of dividends, distributions and redemptions of shares may only be funded out of the assets of the Portfolio in respect of which the relevant shares were issued and account only needs to be taken of the balance sheet of the Portfolio that is paying the dividend, distribution or redemption.

Segregation of Assets/Entering into of Contracts

Directors are required to establish and maintain the segregation both of the general assets of an SPC and the assets of each Portfolio although the directors are entitled under statute to move assets between segregated portfolios and between a segregated portfolio and the general assets of the SPC at full value. In addition each contract or agreement to be entered into on behalf of each Portfolio, must specify on its face that it is entered into by or on behalf of the directors and on behalf of, such Portfolio.

Recognition and Contractual Protection

There has not yet been a case in which a foreign court has specifically ruled on the validity of the segregation of assets and liabilities of a Cayman Islands SPC although a similar statutory segregation of assets and liabilities is found in an increasing number of jurisdictions. Where assets are located outside of the Cayman Islands it is common to add a level of contractual protection in the relevant transaction documents which provides that recourse is limited to the specific Portfolio assets and also removes grounds for any potential claim of a counterparty raised on the basis that he was unaware of the nature of the statutory restrictions in respect of incurred liabilities.

If required, to reduce exposure to the courts of other jurisdictions, documents evidencing payment obligations can be governed by Cayman Islands law and parties can agree to submit to the exclusive jurisdiction of the Cayman Islands courts in such documents. Care should also be taken with generic set-off and netting provisions found in standard form banking and brokerage documents which will need to be specifically tailored to respect the segregation of assets and liabilities in an SPC structure.

Directors' Duties and Liabilities

The directors of an SPC have a continuing obligation to ensure that all contracts are entered into in the name of the correct Portfolio and that all assets and liabilities are properly attributed between the general assets, and each Portfolio.

The principal duties of directors of all Cayman companies including SPCs are derived from English common law, which in summary requires a director of a company to act honestly and in good faith and in what that director believes to be in the best interests of the company; when acting he must act for a proper purpose and must not fetter his future discretion. In addition to the common law duties, Cayman legislation provides that any contract or other arrangement which is to be binding on a Portfolio must be executed by or on behalf of the directors on behalf of, and clearly referencing, the relevant Portfolio. The legislation does provide for a remedial mechanism in the event that an attribution has been incorrectly made without the directors incurring any personal liability.

USES OF SPCs

Standard offshore fund structures such as multi-class hedge funds, umbrella funds, master-feeder structures and managed account platforms can benefit from the ability to set up statutory ring-fencing to protect against cross-liability issues between assets and liabilities of different classes with separate equity and debt profiles.

Insurance vehicles and in particular captives may be set up to provide that individual insurance or product lines are segregated in different Portfolios thus protecting them from losses arising from the other categories of business written by the insurer.

Examples of other uses include the creation of multiple tranche debt issuing vehicles in cases in which an additional level of statutory ring-fencing is preferred to add another level of protection to the usual provision of separate security and/or limited recourse wording.

Conversion to an SPC
Any exempted limited company in good standing can apply to be registered as an SPC.

The company will, along with other formalities, require the consent of its shareholders given by way of a special resolution and the consent of the Cayman Islands Monetary Authority (CIMA) if the Company is regulated. In addition the company will require either (i) the consent of all the creditors; or (ii) to have given adequate notice of the proposal to all creditors and have received the consent of at least 95% by value of all creditors of the company.

RECEIVERSHIP AND LIQUIDATION

Making a receivership order in respect of a particular Portfolio
The Grand Court of the Cayman Islands may make a receivership order, and appoint a receiver over a particular Portfolio's assets upon the application of the SPC, any director, any creditor or shareholder of a Portfolio or CIMA (in the case of a fund or other regulated entity only).

The Grand Court will make an order if it is satisfied that either:

1. the assets attributable to any particular Portfolio are or are likely to be insufficient to discharge the claims of the creditors of that Portfolio; or

2. there is a desire for there to be an orderly winding down of the business attributable to any particular Portfolio and it is proposed to distribute the Portfolio assets to those entitled to have recourse to the Portfolio.

Effect of receiving order
The making of a receivership order by the Grand Court creates a stay of proceedings against the SPC in relation to the Portfolio in respect of which the receivership order is made. No suit, action or other proceedings may be taken or instituted against that Portfolio's assets without the leave of the Grand Court. Further, once a receivership order has been made, the powers of the SPC's directors cease in respect of the business of or attributable to the specific Portfolio's assets.

Effect of general SPC liquidation on a receivership

The Grand Court cannot make a receivership order if the SPC is in liquidation and any receivership order made ceases to be of effect upon the commencement of any liquidation of the SPC. An SPC may not commence a voluntary winding up without the prior leave of the Grand Court if any of its Portfolios are the subject of a receivership order. The remuneration and expenses of a receiver are met from the assets of the specific Portfolio in respect of which the receiver was appointed in priority to all other claims.

Winding up or Liquidation

Save for the fact that if a Portfolio is in receivership leave of the Grand Court is required for a voluntary winding up, an SPC may be wound up or liquidated in the same manner as any other Cayman Islands company. However, any liquidator appointed must continue to maintain procedures to segregate and keep segregated Portfolio assets from other Portfolio assets and the general assets of the SPC. Further, he must only discharge Portfolio creditors' claims from the assets of the relevant Portfolio. If the creditor has only a claim against the general assets of the Company he has no right to claim against the assets attributable to any Portfolio.

Cost of setting up a SPC

Fee (where share capital does not exceed US$51,000)	CI$	US$
SPC registration fee	$1,100	$1,342
SPC annual fee	$2,600	$3,171
Fee for each additional segregated portfolio	$300 (Maximum of $1,500)	$366 (Maximum of $1,829)

FURTHER INFORMATION

Please contact any of the following Harneys lawyers if you require additional information on segregated portfolio companies:

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