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CERTAINTY WITH LLC LEGISLATION

Modern Cook Islands LLC Act

LLC legislation has recently been promulgated in the Cook Islands. The Cook Islands Limited Liability Companies Act 2008 (the Act) follows the model adopted in a number of U.S. States. It goes further, however, to give statutory certainty on several key issues of concern to US attorneys using domestic US LLC statutes. The Act also introduces several unique asset protection features, consistent with the approach taken by the Cook Islands in this area.

The Cook Islands LLC is a separate legal entity with rights and liabilities separate from its members. It can of course sue and be sued, it can hold title to property, and it can enter into enforceable obligations. It is responsible for its own debts and third parties can be secure in the knowledge that they are dealing with a properly constituted legal entity in an excellent common law jurisdiction.

Planners can structure a Cook Islands LLC to suit any particular needs. The Act provides a broad foundation to structure an LLC according to its own rules, rather than have them dictated by statute. The operating agreement may contain any provisions for the conduct of its business as long as they are lawful. Certain provisions (designed to protect the interests of its members) are mandatory.

Advisors and their clients appreciate that confidentiality is an important part of LLC formation and operations. The Act includes strong confidentiality provisions in line with the other legislation in the Cook Islands. The names of the members and managers of a Cook Islands LLC are only held by the resident agent. It is an offence to divulge details about an LLC or its business without proper authority. Furthermore any proceedings relating to an LLC or the Act are to be heard *in camera*, with reports to be edited prior to publishing.

In addition to advantages associated with tax structuring, management control, and confidentiality the Act provides distinct and unique provisions to protect a members interests.

The Charging Order - A Creditor's Sole Remedy

Like most LLC jurisdictions, a creditor of a member is permitted to apply for a charging order against a membership interest. The Act provides additional clarification and certainty in this area however, setting out the availability of other remedies, the nature and extent of a charging order, and the rights of the creditor against that membership interest.

S 45 of the Act is the starting point. A creditor is defined as any person whose judgment is recognised by the High Court of the Cook Islands, and includes any person who claims to have a general assignment of a member's property whether arising from an intestacy, bankruptcy or otherwise.

S 45 (6) is specific that the sole remedy for a creditor against a membership interest in a LLC is the right to apply for a charging order.

- (6) *The charging order remedy given by this section shall be the sole and exclusive remedy available to a Creditor in respect of a members membership rights.*

Similar provisions in other jurisdictions have been interpreted by courts (in the absence of sufficient definition of the exact nature of a charging order), to include rights similar to those of a mortgagee in possession, of an assignee, or of a lien holder. Any uncertainty in the Cook Islands has been removed by clear provisions including sub clauses (7) & (8) of section 45 providing as follows:

- (7) *For the avoidance of doubt and without limiting the generality of subsection (6):*
- (a) *a charging order shall not be construed to constitute a lien on a member's interest in a limited liability company;*
 - (b) *the Creditor in whose favour a charging order is issued pursuant to this section shall not thereby become an assignee of any membership interest or any part thereof, nor shall that Creditor hold or be entitled to exercise any membership rights in relation to that interest;*
 - (c) *any member holding any membership interest subject to a charging order shall continue to exercise all his membership rights, and obligations in relation to those rights, in all respects as if the charging order had not been issued;*
 - (d) *subsection (6) shall apply whether the limited liability company has a single member or multiple members.*
- (8) *For the avoidance of doubt and without limiting the generality of subsection (6) and subsection (7), a person in whose favour a charging order has been issued shall have no right to:*
- (a) *interfere in the manager's management of the limited liability company including any sale of its assets;*
 - (b) *liquidate or seize the assets of the limited liability company;*
 - (c) *restrict the business of the limited liability company; or*
 - (d) *dissolve, or cause the dissolution of, the limited liability company.*

Practical Aspects of the Charging Order

An interim charging order may be applied for ex parte, but will only have a life of a maximum of 30 days. The applicant will need to ensure the defendant is served with the proceedings and must deal with the application expeditiously if a full charging order is to issue. Otherwise, a charging order, once granted, is good for five years, after which the creditor must apply for a new order.

In assessing the amount which may be recoverable pursuant to a Charging Order, the Cook Islands Court must exclude any exemplary, pecuniary, retributory or similar types of damages that are part of the creditor's claim.

A charging order provides for the creditor to receive distributions of capital or income which would, but for the charging order, have been received in the hands of the member. The distinction between having rights to those distributions and having rights as a member is important. For example, if the limited liability makes a call on members for capital in accordance with its rules, the company may use a distribution due to the member to meet that capital contribution notwithstanding the charging order. This is consistent with the charging order being seated at the member side of the equation rather than the company. The distribution never reaches the member so the creditor has no claim upon it.

Importance is given to the member and the LLC being separate legal persons. An action by a creditor against a member, or the fact of a charging order being issued, is not sufficient to support discovery orders or injunctions being issued against the LLC itself.

Non Recognition of Foreign Judgments

The provisions regarding foreign judgments entrench the Cook Islands Court as the proper forum for determining claims by creditors against members. Foreign interlocutory orders (including injunctions, discovery etc) against an LLC, relating to a claim by a creditor against a member, cannot be recognized or given effect by the Cook Islands Court. Furthermore, foreign judgments against LLC membership rights or interests which purport to charge, levy, attach or assign such interests, cannot be recognised or enforced in a Cook Islands court.

Transfer between Jurisdictions

The Act provides a smooth process for existing LLCs to transfer their domicile to the Cook Islands. Similarly a Cook Islands LLC is able to move to another jurisdiction.

A simple application process is completed by the proposed registered agent in the Cook Islands and copies of the LLC's organisational documents and certificate of formation are provided to the Registrar. Upon registration the LLC is deemed to have commenced its existence in the Cook Islands on the date that it was originally organised.

However, LLCs wanting to escape existing corporate debts would do well to avoid the Cook Islands. The Act specifically provides that with redomiciliation the LLC takes its prior debts with it and any action against the company, whether already filed or not, prior to redomiciliation, may be continued and any judgment entered shall be enforceable against that LLC in the Cook Islands.

Summary

The new legislation provides a comprehensive framework for the formation and operation of LLCs. While providing enhanced protective features it is not intended to provide a substitute to the already highly recognised Cook Islands asset protection trust. Rather, it is expected to provide a useful addition to attorneys and financial advisers both on its own, and in conjunction with the establishment of Cook Islands trusts, to achieve the maximum protection along with operational flexibility.

About the Authors

This article was prepared by Reuben Tylor and Antony Will. Reuben and Antony are directors of Cook Islands Trust Corporation Ltd. They assisted in drafting the Cook Islands LLC Act, and promoting it with the government agencies in the Cook Islands.

CIT was incorporated in the Cook Islands in 1988, and is licensed as a trustee company. The directors of CIT are Laveta Short, Reuben Tylor, and Antony Will. Reuben Tylor was appointed as a principal of a trustee company in 1982 and has specialized in offshore work since that time. In 1989, he pioneered and developed the first asset protection legislation for which the Cook Islands is the dominant international jurisdiction. Laveta Short has had a distinguished international career as a lawyer, a Cabinet Minister, and foreign diplomat. Antony Will joined CIT in 2000 as in-house counsel, and has been Managing Director since 2003.