

Flexibility and balance

Leonard A Birmingham of Harneys discusses one of the reasons why the BVI is one of the world's most stable financial centres

Shares in British Virgin Islands (BVI) companies are not subject to stamp duty or any other tax on transfer in the BVI. Financial assistance is not prohibited and there is no requirement for a public filing of a company's register of members. But a number of other interesting aspects of BVI company law create advantages and opportunities in terms of structuring and implementation of M&A involving a BVI company.

The main methods of achieving a business combination as a matter of BVI law are:

- Share purchase
- Asset purchase
- Public offer for shares in target
- Plan of arrangement
- Scheme of arrangement
- Statutory merger or consolidation
- Minority squeeze out

Share purchase

As one would expect, such transactions are documented by a share purchase agreement (SPA) negotiated by the parties. There will sometimes be heads of agreement but there is no mandatory approach to a share purchase as a matter of BVI law. Owing to the nature of the vast majority of transactions involving BVI companies, the SPA will in most cases be governed by a law other than BVI law. As a result, the main issues that arise as a matter of BVI law are the mechanics of transfer, changing the registered office and registered agent of the BVI company and addressing ancillary matters such as changing directors, revoking powers of attorney and bank mandates. One point that purchasers tend to miss but needs to be carefully borne in mind for certain BVI companies is that the shares may be subject to compulsory acquisition by the company if either the Memorandum or Articles, the rights of the shares or a subscription agreement for the issue of the shares, permits the same. It is therefore necessary to rule out the possibility of compulsory acquisition by ensuring that none of the above permits the company to acquire its own shares without the consent of the shareholders. If that step is not taken it is possible for a purchaser to be suddenly relieved of its shares by the company if those shares were for example, issued pursuant to a subscription agreement (which is a private document) that empowered the company to

compulsorily acquire the same.

An asset purchase will similarly be documented by an asset purchase agreement negotiated by the parties.

Public takeovers

There is no Stock Exchange, no Takeover Code and no Securities legislation in the BVI. Accordingly, there are no set procedures to be followed as a matter of BVI law except that the directors of the target company are subject to duties under common law and the BVI Business Companies Act 2004 (as amended). The main common law duty is to be honest and not mislead the shareholders. Because of the relative lack of legal infrastructure in this regard, consideration should be given before the relevant company's listing – for example on the London Stock Exchange – regarding whether relevant provisions of the City Code will be included in the Listco's Memorandum and Articles. It is of course advisable to do this (and it has been done in respect of several listings) because in many cases it provides a recognisable and familiar framework for the directors of the BVI Listco, many of whom are familiar with the City Code. The other main issues that arise are break fees and poison pills. In relation to break fees, the directors must be mindful of their duties and secondly must consider whether the break fee might amount to a penalty. Regarding poison pills, in order to have a chance of being upheld, it would have to be adopted before the takeover offer is contemplated.

Merger or consolidation

This is one of the more popular methods of acquiring a BVI company. Part of the reason

for this is its simplicity and the fact that it is based on statute so that as long as the statutory procedures are followed correctly it is difficult to go wrong. By operation of law, two or more existing BVI companies, or one BVI-incorporated and one not (provided that foreign law permits the merger), may merge into one of the constituent companies. In the case of consolidation, the constituent companies combine to form a new company, which is the consolidated company. The Act permits shares to be cancelled, reclassified, converted into money or other assets, or into shares, debt obligations or other securities, in the surviving or consolidated company. Shares of the same class may be treated differently; some members may be given shares in the surviving or consolidated company while others of the same class can receive cash instead.

With the merger of the constituent companies into the surviving company, the surviving company acquires the rights, powers, immunities and all the business and assets of the constituent companies, but also becomes liable for all their debts, claims and obligations. Such debts and obligations, and any judgment or cause of action against the constituent companies, are not released by the merger. Proceedings pending against the constituent companies at the time of the merger are also not abated or discontinued but may be enforced, prosecuted, settled or compromised by or against the surviving company, and the surviving company may be substituted in the proceedings.

Consolidation has the same consequences except that the new consolidated company acquires the assets and becomes subject to the liabilities. Merger or consolidation with a foreign company, where the surviving company or new consolidated company is a foreign company, has the same consequences unless the laws of the foreign jurisdiction provide otherwise.

The procedure involves four stages which, in outline, are as follows: approval of a plan of merger or consolidation by the directors of each constituent company; approval of the plan by a resolution of members of each constituent company; execution of Articles of Merger or Consolidation by each constituent company; and filing of the Articles of Merger

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Author biography



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Leonard Birmingham is global head of the corporate and commercial department and head of Harney Westwood & Riegels (London). He specialises in all aspects of BVI and Anguilla corporate, commercial and banking law. Birmingham's client base spans several jurisdictions and consists mainly of established public and private companies, founders and investors in start-up companies, company directors and shareholders, law firms, and banks. This international practice has enabled him to be involved in initial public offerings and listings on

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or Consolidation with the Registrar of Corporate Affairs in the BVI (the Registrar). The Registrar, if satisfied that the requirements of the Act (including the provision relating to the name of the company) have been complied with, must register the Articles of Merger or Consolidation and issue a certificate. In the case of a consolidation, it must issue a certificate of incorporation of the new consolidated company. The merger or consolidation is effective on the date the Articles of Merger or Consolidation are registered, or a subsequent date not exceeding 30 days as is stated in the Articles of Merger or Consolidation.

The written plan of merger or consolidation must contain certain matters specified by the Act including the terms and conditions of the proposed merger or consolidation and the way in which shares in the constituent companies are to be treated. For a merger, the plan must contain a statement of any amendments to be made to the Memorandum of Association or Articles of Association of the surviving company as a result of the merger; for a consolidation the plan must annex the Memorandum and Articles to be adopted by the new

consolidated company.

Regarding members' approval, the plan must be given to all members whether or not they are entitled to vote or consent on the merger or consolidation. Approval is by members' resolution, which can be by a vote at a meeting or by written consent. It requires a majority of the votes of those members entitled to vote unless the Memorandum or Articles specifies a higher majority. Shareholders of a class of shares are only entitled to vote as a class in one of two situations: either if the Memorandum or Articles so provide or if the plan contains provisions that, if contained in a proposed amendment to the Memorandum or Articles, would entitle the class to vote on the proposed amendment as a class.

The Articles of Merger or Consolidation must contain the plan of merger or consolidation, the dates when the Memorandum and Articles of each constituent company were registered and the manner in which the merger or consolidation was authorised by each constituent company. When filing the Articles of Merger or Consolidation with the Registrar, another document must also be filed and registered by the Registrar: in the case of a merger, it will be

any resolution to amend the Memorandum and Articles of the surviving company and in the case of a consolidation it will be the Memorandum and Articles for the new consolidated company.

As regards mergers or consolidations involving foreign companies, including foreign private equity funds, these are only allowed if the law of the foreign jurisdiction permits it. The BVI constituent company must comply with the provisions of the Act, and the foreign company must comply with the law of the jurisdiction of its incorporation. If the result of the merger or consolidation is a foreign company, there are provisions for ensuring that proceedings for any claim under the Act can be served on it in the BVI by requiring an irrevocable appointment of its registered agent to accept service of such proceedings and requiring its agreement that it will promptly pay dissenting members. Such appointment and agreement must be filed. It must also file its foreign certificate of merger or consolidation, or, if the foreign authority does not issue such a certificate, whatever evidence of merger or consolidation the Registrar considers acceptable.

Minority shares

A squeeze-out procedure may be implemented if members entitled to vote and holding 90% of the votes of the outstanding shares and 90% of the votes of the outstanding shares of each class of shares entitled to vote as a class, instruct the company in writing to redeem the shares held by the remaining members; this action is subject to the provisions of the company's Memorandum and Articles. Upon receipt of the instruction the company must redeem those shares; no discretion is afforded to the company's directors to refuse to carry out the instruction. This is a compulsory redemption of the shares of minority shareholders at the instance of the majority.

The law does not prescribe any procedure in which such redemption should be carried out or how the redemption price shall be determined. Thus, the company must decide on the manner of the redemption and set the redemption price, although it must give written notice of these to the member whose shares are to be redeemed. Thereafter, some of the notice and appraisal provisions in the section on dissenters' rights apply to ensure that a member who dissents receives fair value. Such a redemption is not a distribution and no solvency determination is required.

Arrangements

A BVI court approved merger or demerger may provide benefits of a fiscal or regulatory nature in other jurisdictions and BVI law provides for (i) plans of arrangement and (ii) schemes of arrangement. The former is a process to effect a very wide range of restructurings by way of court approval and must be instigated by the board. The latter involves an application by the

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company, a creditor, a member or a voluntary liquidator and provides a statutory framework for the company, and allows some or all of its creditors or members to compromise or change their rights against the company subject to the court's supervision.

Plans of arrangement and schemes of arrangement have a degree of overlap. It is conceivable that we will see some rationalisation in the future.

There may be a number of reasons for using arrangements over other forms of corporate restructuring in any given case: it may be necessary to obtain the consent of creditors (for which there is no requirement under the other mechanisms discussed above); it may be necessary to obtain court approval to bind all members and creditors; or it may be necessary to obtain court approval for exemption from foreign legislation, for example, from the registration requirements of the US Securities Act 1933 for securities.

Ordering and organising

Taking plans of arrangement first, the definition of "arrangement" in the section on plans of arrangement is wide. It refers to reorganisations, mergers, consolidations, separations of businesses, dispositions of assets or businesses, dispositions or exchanges of shares or securities, amendments to the Memorandum and Articles, dissolutions and, importantly, any combination of these. These can of course take place outside the context of a plan of arrangement.

Where the arrangement involves a merger or consolidation with companies not registered under the Act, the procedure can only be used if the surviving company or consolidated company will be incorporated under the Act.

A plan of arrangement has several stages. First, the directors must approve a plan of arrangement if they consider that it is in the best interests of the company or its creditors or members. The plan must contain details of the proposed arrangement. The directors must then apply to the court for approval of the arrangement. The court can make orders as to the persons who should be notified of the arrangement, as well as whose approval should be obtained, and the manner of giving such notification or obtaining such approval. The directors must confirm the plan as approved by the court if they wish to proceed with it, give notice to those directed by the court and, if required by the court order, submit the plan for approval by those persons as the court order requires.

If those persons as required by the court order approve the plan, the company must execute Articles of Arrangement containing the plan of arrangement, the court order approving the plan and a statement of the manner in which it was approved.

The Articles of Arrangement must be filed with the Registrar who must register them and issue a certificate. The arrangement is

effective from the date the Articles of Arrangement are registered or a later date, not more than 30 days later, as stated in the Articles of Arrangement.

Although a literal reading of the Act suggests that court approval must precede the approval by those whose approval is made necessary under the court order, the procedure can be (and in practice sometimes is) reversed, that is, the court approval may take place after approval by others. This is because the court hearing is generally likely to involve an initial hearing and a final hearing. At the initial hearing the court can give directions as to who should be notified of the arrangement and the plan and in what manner; directions about advertisements; and directions regarding whose approval must be obtained and in what manner – for example, whether any class should vote as a class. Pursuant to these directions approval can be obtained. Thereafter a final hearing can take place at which any interested persons may appear and be heard. The court may then approve or reject the arrangement with or without any amendments as it may direct. The advantage of this sequence of events is that a dissenting minority shareholder may still have an opportunity to be heard on why the plan should not be approved. The court can also allow any shareholders or holders of securities or debt obligations to dissent from the proposed arrangement and receive fair value for their shares or, as the case may be, securities or debt obligations.

Schemes of arrangement, on the other hand, are similar to schemes provided for by section 425 of the English Companies Act 1985 (UK). They are not intended to be confiscatory in nature but to provide a statutory and court-sanctioned exchange of collective rights of creditors or shareholders. The scheme must be approved by 75% of the creditors or shareholders; there must be complete transparency and the court will only sanction a scheme if it is fair.

An application for a scheme of arrangement may be made to the court by the company or a creditor, member, administrator or liquidator of the company. The arrangement or compromise must be proposed between a company and its creditors, members or class of either. Upon the application the court may order a meeting of the members or creditors or class of either. Statutory Regulations may provide for information and explanations to be contained in or accompany the notice calling a meeting of members, creditors or class thereof. However, at present no such Regulations exist.

A court order has effect when a copy of the order has been filed with the Registrar. A copy of the court order must also be attached to every copy of the company's Memorandum of Association issued after the date of the order. When the court makes an order the reconstruction remedies of the Act for example, merger, consolidation, and plans of

arrangement and dissenters' rights do not apply to the company. A member of a company is entitled to payment of the fair value of his shares upon dissenting from any of the foregoing (save for the scheme of arrangement) and the Act stipulates the applicable procedures.

Business combinations in most common law jurisdictions take a somewhat similar approach to the BVI. A few interesting differences, and which should therefore inform structuring at the outset of transactions, are as follows:

- The duties that apply to directors are those applying at common law and under the Act, which are well known or easily identifiable. The law in the BVI also provides a degree of flexibility which, in general terms, permits directors of a subsidiary to act in the best interests of the parent even though not in the best interests of the subsidiary, and this also applies to joint ventures. In some other jurisdictions the applicable rules are less well known or tend to be less flexible.
- In the BVI only the Act and the common law apply, providing shareholders with the freedom to apply more stringent standards to their arrangements if deemed fit, such as adopting parts of the City Code. In the UK, there are several statutes or quasi-statutes that impact business combinations: the Financial Services and Markets Act 2000, the City Code, the Criminal Justice Act 1993, the Enterprise Act and the UK Listing Authority Sourcebook of Rules and Guidance.
- No stamp duty applies to share transfers in the BVI.
- No prohibition against financial assistance.
- No statutory disclosure requirements for shareholders.

Flexibility and a sensible balance in terms of BVI corporate law have been its hallmarks for decades providing a level of predictability that is indispensable. Shareholder protection is not sacrificed and is in several instances available under the Act or can be built into the company's framework. This is probably one reason why the Global Financial Centres Index 2008 has ranked the BVI among the most stable of financial centres worldwide.

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