

BRITISH VIRGIN ISLANDS CORPORATE ARRANGEMENT SCHEMES

With a global economic downturn in full swing, companies around the world are looking for ways to safeguard their future existence. The strategies employed to do so are numerous and varied but a number of companies have employed the use of corporate arrangement schemes entered into with their creditors, investors and other stakeholders as a way to refocus and preserve their business.

The BVI Business Companies Act, 2004 (the “Act”) which regulates companies incorporated in the British Virgin Islands (“BVI”) provides for the use of such schemes and in terms of process, timing and cost is very effective in comparison to some of the schemes available in other popular offshore jurisdictions. Below, we will examine the forms of arrangement schemes available under BVI law and briefly discuss their procedure and some of the benefits which they can bring to companies in distress. Firstly, we will examine “arrangements” which are primarily company driven and then “schemes of arrangement” which are primarily creditor driven or driven by the company whether acting through its board or a liquidator in an insolvency or potential insolvency scenario.

Arrangements

The term "arrangement" is defined in section 177 of the Act and includes: (a) an amendment to the memorandum or articles (the constitution) of a company; (b) a reorganisation or reconstruction of a company; (c) a merger or consolidation of one or more companies that are companies registered under the Act with one or more other companies, if the surviving company or the consolidated company is a company incorporated under the Act; (d) a separation of two or more businesses carried on by a company; (e) any sale, transfer, exchange or other disposition of any part of the assets or business of a company to any person in exchange for shares, debt obligations or other securities of that other person, or money or other assets, or a combination thereof; (f) any sale, transfer, exchange or other disposition of shares, debt obligations or other securities in a company held by the holders thereof for shares, debt obligations or other securities in the company or money or other property, or a combination thereof; (g) a dissolution of a company; and (h) any combination of any of the things specified in (a) to (g) above.

Initiating the arrangement

To initiate an arrangement, the directors of a company, if they determine that it is in the best interests of the company, its creditors or its members, must first

approve a plan of arrangement which contains details of the proposed arrangement. Upon approval of the plan of arrangement by the directors, the company must make application to the court for approval of the proposed arrangement.

Court approval

The court may, upon receiving the application make an interim or a final order that is not subject to an appeal unless a question of law is involved. In making an order, the court may determine the notices to be obtained, determine persons who may dissent, conduct a hearing and permit any interested person to appear, and approve or reject the plan of arrangement as proposed or with such amendments as the court may direct.

Where the court makes an order approving a plan of arrangement, the directors of the company, if they are still desirous of executing the plan, must confirm the plan of arrangement as approved by the court whether or not the court has directed any amendments to be made thereto. The directors of the company, upon confirming the plan of arrangement, must (a) give notice to the persons to whom the order of the court requires notice to be given; and (b) submit the plan of arrangement to those persons for such approval, if any, as the order of the court requires. It is likely that approval by the shareholders and/or creditors will be needed. With respect to shareholder approval, this would generally be at least the threshold level required to pass a shareholders resolution under the memorandum and articles of association of the relevant company but depending on the nature and substance of the arrangement, the court may require a higher threshold.

Registering articles of arrangement

After the plan of arrangement has been approved by those persons that the order of the court required approval from, articles of arrangement must be executed by the company containing (a) the plan of arrangement; (b) the order of the court approving the plan of arrangement; and (c) the manner in which the plan of arrangement was subsequently approved (following court approval).

The articles of arrangement are then filed with the Registrar of Corporate Affairs in the BVI (“Registrar”) who will register them. Upon the registration of the articles of arrangement, the Registrar will issue a certificate in the approved form certifying that the articles of arrangement have been registered. An arrangement is effective on the date the articles of arrangement are registered by the Registrar or on such date subsequent thereto, not exceeding thirty days, as is stated in the articles of arrangement.

Examples of uses of a court approved scheme

The arrangement process is often used in cases where the transaction could have been carried out as strictly private matter without court approval, but where the benefits and the certainty which comes with court approval outweighs using the typical corporate route. For example, in one case, a reverse takeover transaction was carried out using a BVI court approved arrangement which allowed the

company to seek exemption from registration under the US Securities Act, 1933, (which provides an exemption in respect of court approved transactions). In another case, a BVI court approved arrangement was used to de-merge eight BVI subsidiaries of a BVI holding company into the hands of newly created BVI companies held personally by individuals in Russia which enabled the parties to mitigate certain income tax charges in Russia in the hands of the recipient individuals. The charges were mitigated by using a BVI court approved arrangement which facilitated the use of an exemption pursuant to Russian tax law.

Schemes of Arrangement

Pursuant to section 179A of the Act, where a compromise or arrangement is proposed between a company and its creditors, or any class of them, or between the company and its members, or any class of them, the court may, on the application of a person specified below order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be summoned in such manner as the court directs.

Making the application

The application may be made by: (a) the company; (b) a creditor of the company; (c) a member of the company; (d) if the company is in voluntary liquidation within the meaning of section 202 of the Act, by the voluntary liquidator; or (f) if an Insolvency Act liquidator has been appointed, by that liquidator.

It should be noted that if a majority in number representing seventy five per cent in value of the creditors or class of creditors or members or class of members, as the case may be, present and voting either in person or by proxy at the meeting, agree to any compromise or arrangement, the compromise or arrangement, if sanctioned by the court, is binding on all the creditors or class of creditors, or the members or class of members, as the case may be, and also on the company or, in the case of a company in voluntary liquidation or in liquidation under the BVI Insolvency Act, 2003 on the liquidator and on every person liable to contribute to the assets of the company in the event of its liquidation.

Filing the court order

An order of the court made will have no effect until a copy of that order has been filed with the Registrar. A copy of an order of the court made must be annexed to every copy of the company's memorandum of association issued after the order has been made.

In the context of a scheme of arrangement, "arrangement" includes a reorganisation of the company's share capital by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both of those methods.

Benefits of corporate arrangement schemes

There are a number of benefits to using corporate arrangement schemes including:

- (i) flexibility - an arrangement scheme may be tailored to deal with the specific circumstances of the company and the various parties involved;
- (ii) securing early payment for creditors - where an arrangement scheme facilitates early payment of some debt owed by the company;
- (iii) shareholder equity - some residual shareholder equity may be realised if the arrangement scheme is implemented prior to insolvency;
- (iv) fiscal benefits - in some cases a court approved arrangement scheme could provide fiscal benefits, for example, in one case as described above a BVI court approved arrangement allowed a company to seek certain registration exemptions under the US Securities Act;
- (v) certainty - providing some degree of certainty as to the roles of the various parties and the expected outcome on the basis that it is court approved; and
- (vi) community benefits – an arrangement scheme may help to protect a company which would otherwise have to lay off staff; and/or close business.

Conclusion

The above procedures available under the Act may help to safeguard a company's future and their use and applicability is certainly something which creditors, investors and stakeholders dealing with distressed BVI companies, should explore.

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If you would like further information about corporate arrangements, please contact Michael Gagie (michael.gagie@harneys.com) or Christopher Simpson (christopher.simpson@harneys.com) at our Hong Kong office or your usual Harney Westwood & Riegels lawyer. Alternatively, you may visit our website at www.harneys.com.

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