

# ENFORCING SECURITY OVER MORTGAGED ASSETS IN THE BRITISH VIRGIN ISLANDS: THE EMERGING BATTLE GROUNDS



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There has been a significant increase in the number of lenders enforcing against secured assets in the BVI, which has entailed an uptick in the appointment of out of court receivers. As heavily leveraged businesses approach a global recession, this trend is likely to continue. In this article, Christopher Pease and Megan Elms highlight the types of disputes that are arising out of such appointments.



## Appointment

As many offshore companies operate as holding vehicles, security is often granted by way of share mortgage. The BVI Business Companies Act, 2004 (the BCA), provides a mortgagee with security over shares in a BVI company a statutory right to appoint receivers

over those shares. That right is typically mirrored in the underlying security instrument.

The process for appointing receivers in the BVI is set out in the BVI Insolvency Act, 2003 (the Insolvency Act).



## Powers and duties

Once appointed, out-of-court receivers act as agent for the mortgagor unless the instrument pursuant to which they are appointed provides otherwise. While receivers are generally personally liable for their actions, this agency affords them a degree of protection as they act in the name of and on behalf of the mortgagor.

BVI legislation is relatively light-touch on the powers granted to a receiver,

generally deferring to what has been agreed and set out within the instrument pursuant to which the receiver is appointed. In the case of security over shares, the receiver will generally have the power to (i) sell the shares, (ii) vote the shares and (iii) take such other steps as they consider necessary or desirable to protect, improve or realise the shares.

According to the Insolvency Act, receivers are subject to a primary duty to exercise their powers (i) in good faith and for a proper purpose and (ii) in a manner in which they believe (on reasonable grounds) to be in the best interests of the person on whose behalf they are appointed. To the extent consistent with these primary duties, a receiver has a secondary duty to have reasonable regard to the interests of certain interested parties, such as creditors and those with an interest in any equity of redemption.



## Disputes relating to the appointment of receivers

As the number of receiverships rise, so does the range of issues being disputed by mortgagors, often in seeking to prevent the appointed receivers from exercising their powers. The following trends are beginning to emerge:

- 1 Challenges to appointment:** a mortgagor seeking to resist having their security enforced will often start by challenging the validity of the receiver's appointment by reference to the security documents. The relevant documents must have been properly executed and valid, the right to appoint receivers must have accrued (usually contingent upon a default) and the necessary processes carried out to notify the mortgagor of the default and give effect to the receiver's appointment.
- 2 Extent to which the Insolvency Act applies to receiverships over shares in BVI companies owned by an individual or entity located elsewhere:** the Insolvency Act has an entire part that governs the appointment of receivers. However, there is ambiguity as to whether several key provisions, such as those setting out the duties of a receiver, apply to all receivers appointed in relation to assets in the BVI.

Various provisions apply specifically to a receiver of a 'company', a company being defined as a company in respect of whose assets a

receiver is appointed, unless the context requires otherwise. The overarching definition of a 'company' in the Insolvency Act is restricted to BVI registered companies. Arguably, therefore, where a receiver is appointed over shares in a BVI company, but not the assets of a BVI company, these provisions do not apply.

This ambiguity can lead to disagreements over what steps should or should not be taken by receivers and provides fertile grounds for legal disputes.

- 3 Balancing duties:** the tripartite nature of receiverships (between mortgagee, mortgagor and receiver) has given rise to extensive authority on how receivers ought to balance the various duties that arise. But there is no one-size-fits all solution: a receiver must evaluate the competing interests according to the circumstances of their appointment. They cannot solely protect the interests of their appointer, particularly if there is likely to be substantial excess value in the secured assets after the debt has been repaid.
- 4 Internal conflicts:** a receiver appointed over shares may not have a readily saleable asset, as a share sale is often found not to be a commercially viable option. As a result, receivers commonly look to obtain control of asset holding companies as soon as possible by exercising a shareholder's voting power to reconstitute the board (and those of any subsidiaries). Receivers therefore often simultaneously hold office as receiver and director.

As director, a receiver will owe further duties; to whom will depend on the company's solvency. While insolvency may be assumed in a receivership scenario, where appointments are taken at different levels within a group, or where there is likely to be significant equity after repayment of the secured debt, this may not be the case.

A receiver who is also a director must be mindful as to how the arising duties interact. Where there is likely to be residual value in a company, a director may need to act in the interests of the company and/or its other creditors despite the purpose of their appointment as receiver being to repay the secured debt. If it occurs to the receiver/director that the company is insolvent, then a decision would need to be taken as to whether the company should be placed into liquidation. While this may appear absurd in the context of fixed charge receiverships, the bespoke issues created by offshore security structures means these are issues that receivers are increasingly having to grapple with.

As the number of receiverships, and by extension the numbers of such disputes, increase, it is only a matter of time before the BVI courts render a judgment that will provide guidance and shape how future BVI receiverships are to be approached.

