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British Virgin Islands

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IN SUMMARY

While there has not been the deluge of restructuring deals that insolvency practitioners had predicted as a result of the global pandemic, it is certainly true that the British Virgin Islands saw an increase in the number of schemes and 'light touch' provisional liquidations in 2020 and 2021 as a result of the economic effects of covid-19, and this is a trend that is likely to increase, particularly with the British Virgin Islands entities' exposure to China-related debt.

DISCUSSION POINTS

- The recent schemes of arrangement that have been approved
- The increased willingness of the judiciary to assist struggling companies that have a realistic prospect of trading their way out of difficulty
- Possible reforms to the restructuring regime

REFERENCED IN THIS ARTICLE

- Insolvency Act 2003
- Business Companies Act 2004
- Section 179A of the Business Companies Act 2004
- *Constellation Overseas Limited and 5 others* – BVIHC (Com) 2018/0206 – 2012, 13, 19 December 2018, 5 February 2019
- *Century Sunshine*
- *Tungshu Venus Holdings Limited v Zhang Rui Kang* – BVIHCM 2020/ 0115 Wallbank J dated 5 November 2020
- *Rock International* and *Constellation* – BVIHC 2020/ 184
- English Court of Appeal in *Re: BTR Plc* [2000] 1 BCLC 740 at 744
- *In re Rock Int'l Inv.*, No. 20-35623 (MI) (Bankr. S.D. Tex. Dec. 11, 2020)

While there has not been the deluge of restructuring deals that insolvency practitioners had predicted as a result of the global pandemic, it is certainly true that the British Virgin Islands saw an increase in the number of schemes and 'light touch' provisional liquidations in 2020 and 2021 as a result of the economic effects of covid-19, and this is a trend that is likely to increase, particularly with the British Virgin Islands entities' exposure to China-related debt. This review discusses those recent schemes of arrangement that have been approved and the increased willingness of the judiciary to assist struggling companies that have a realistic prospect of trading their way out of difficulty. It will also discuss possible reforms to the restructuring regime.

The British Virgin Islands is a self-governing overseas territory of the United Kingdom. It is a leading international finance centre which is tax neutral, politically stable and economically secure. The legal system is based on English common law with the final appellate court being the Privy Council (comprising members of the UK Supreme Court) in London. The legal infrastructure, tight control policies and modern legislation have resulted in it being widely recognised as an ideal and stable jurisdiction for investment vehicles. Such investment vehicles have been particularly popular with Chinese, Russian and South American interests and it is not uncommon to find British Virgin Islands companies being used to raise finance on the international markets with British Virgin Islands companies issuing bonds in relation to operating companies in mainland China, Russia and South America.

The source of restructuring law in the British Virgin Islands is found in two statutes: the Insolvency Act 2003 and the Business Companies Act 2004, which together provide a comprehensive restructuring regime. While the Insolvency Act was largely modelled on the UK Insolvency Act 1986, there are significant differences that can trip up the unwary. For example, while the Insolvency Act 2003 makes provision for administration orders, the section has not been enacted. Similarly, Part 18 sets out the UNCITRAL Model Law on Cross-Border Insolvency, which has also not been enacted. Equally the British Virgin Islands restructuring regime includes tools that have not traditionally been part of English law such as Canadian-style plans of arrangement.

For companies seeking to reorganise their capital or debts there are three main routes available: a plan of arrangement, a scheme of arrangement or a creditors' arrangement. Plans and schemes are governed by the Business Companies Act 2004 and creditors' arrangements are governed by the Insolvency Act 2003.

Plans of arrangement are at the discretion of the directors, do not require the 75 per cent in value threshold to be satisfied, but do require court sanction. There is no statutory moratorium available in relation to plans of arrangement so a company remains vulnerable to creditors' claims.

Schemes of arrangement are governed by section 179A of the Business Companies Act between a company and its creditors and/or members or any class or classes of them. The section does not use the term 'scheme of the arrangement' specifically in the body of the text but rather refers to 'compromise or arrangement'. There is no indication in the legislation as to the procedure for obtaining court sanction but the British Virgin Islands follows the English court practice, first by obtaining permission to convene a meeting and second by obtaining the court sanction. The court will not merely rubber stamp the scheme but will analyse it critically to make sure it is fair, reasonable and efficacious. At the meeting 75 per cent in value must vote in favour of the scheme in order for it to be binding. As with plans of arrangement there is no statutory moratorium available and therefore the scheme remains liable to upset by creditor claims until sanctioned by the court.

Creditors' arrangements are arrangements that can be entered into between the company and its unsecured creditors without court sanction provided there is a sufficient number (75 per cent by value) of creditors in favour.

A recent major development relates to the use of provisional liquidators by way of light touch appointments. Unlike other offshore jurisdictions such as the Cayman Islands and Bermuda, the British Virgin Islands did not have a practice of using provisional liquidators for restructuring purposes but rather to preserve assets at risk of dissipation pending the appointment of full liquidators.

Since 2019 the Commercial Court has developed a practice whereby provisional liquidators can be appointed in support of a subsequent restructuring plan, usually a scheme of arrangement. In those cases, the aim is to provide the company with some breathing space in order to come to an agreement with the requisite percentage of creditors.

In *Constellation Overseas Limited and 5 others*[1] Justice Adderley, after an extensive review of the English and Commonwealth authorities, determined that the Court had 'a very wide common law jurisdiction' to appoint provisional liquidators in support of a restructuring plan. Crucially, in *Constellation* there was no evidence of over 75 per cent support from creditors at the time of making the application (the threshold

1 BVIHC (Com) 2018/0206 – 2012, 13, 19 December 2018, 5 February 2019.

for actual approval of a scheme of arrangement). In fact, the support was initially very limited but in circumstances where there was no complaint of mismanagement of the company's affairs and there was some prospect of a forthcoming agreement with creditors, the BVI Commercial Court agreed that an appointment was appropriate. This was followed by a successful application to sanction a scheme of arrangement under section 179A as discussed further below.

Constellation was followed by Justice Jack in the 2020 case of the Chinese fertiliser group Century Sunshine. The four British Virgin Islands entities were part of a wider group of companies held by a Cayman listed company, Century Sunshine Group Holdings Ltd. Century Sunshine Group represented the largest vertically integrated developer and producer of magnesium alloy products and ecological fertiliser business in the People's Republic of China. While it had enjoyed several years of strong growth and profitability, Century Sunshine Group's sales and production had been negatively affected by the PRC holiday extension and logistical delays due to covid-19 since early 2020. There had been a drop in revenue in the first four months and reduced liquidity in operating cash flow as a result. At the time of the application to appoint provisional liquidators, Century Sunshine Group was in default of an approximately US$563,563,000 Singapore bond issue which had been guaranteed by the companies. It was for this reason that the Group sought to restructure its debts in the Cayman Islands, Bermuda and the British Virgin Islands.

Justice Jack granted the appointment of provisional liquidators EY on the basis that there was some support from creditors and the liquidation analysis demonstrated that the return to creditors would be 0–40 per cent for unsecured creditors and 33.6–100 per cent for secured creditors, whereas the board considered that 100 per cent return would be achievable on a restructuring.

The case was noteworthy for two reasons. First, it was one of the first cases where the Court sanctioned the implementation of the JIN Guidelines across three jurisdictions – British Virgin Islands, Bermuda and the Cayman Islands – with the aim of a holistic restructuring across the Group. Second, the Court addressed the issue of the moratorium under section 174(1) of the Insolvency Act 2003, which provided that where an application for appointment of a liquidator had been issued but not determined, where any action is pending against the company an application can be made to stay such proceedings. In *Constellation* proceedings had been issued and therefore the stay was granted. In *Century Sunshine* no other proceedings had been issued. The Court, however, accepted the submission that even though no other proceedings against the companies had been commenced at the time of the application, the Court ought to grant a conditional moratorium so that in the event any actions were

commenced against the companies they could obtain the benefit of the moratorium under section 174(1) of the Insolvency Act 2003 and an automatic stay would be imposed. The case is still ongoing.

The British Virgin Islands courts have also been alert to the misuse of restructuring proposals by debtor companies. In *Tungshu Venus Holdings Limited v Zhang Rui Kang*[2] the Court rejected the contention that a statutory demand ought to be set aside on the basis that the company was seeking to restructure its debts in circumstances where the evidence indicated that the company would not achieve the requisite 75 per cent of support from creditors and there was no evidence that the statutory demands per se would jeopardise the restructuring or make it more difficult for the company or group to raise finance.

Schemes of arrangement pursuant to section 179A of the Business Companies Act 2004 have proved a useful tool for companies in difficulty over the course of 2020 and 2021.

Section 179A(3) of the Act provides:

> *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 Insolvency Act, on the liquidator and on every person liable to contribute to the assets of the company in the event of its liquidation.*

Under section 179A(2), Business Companies Act 2004 an application may be made by the company and there is nothing in the Business Companies Act 2004 that prescribes the subject matter of a compromise or arrangement.

Prior to *Rock International* and *Constellation* (discussed below) there was very little by way of authority in the British Virgin Islands by way of approach the court ought to take in relation to the sanctioning of a scheme of arrangement. The court therefore considered the English authorities in relation to its exercise of discretion as to whether to sanction a scheme of arrangement. In particular the English Court of Appeal in *Re: BTR Plc* [2000] 1 BCLC 740 at 744 set out the relevant test as follows:

2 BVIHCM 2020/ 0115 Wallbank J dated 5 November 2020.

in exercising its power of sanction the court will see, first, that the provisions of the statute have been complied with, second that the class was fairly represented by those who attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent, and thirdly, that the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.

The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision of the meeting; but, at the same time, the court will be slow to differ from the meeting, unless either the class has not been properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found on the scheme.

The court must also be satisfied that the resolutions have been passed by the requisite majority in accordance with the Business Companies Act in a meeting duly convened and held in accordance with the order convening the meeting. The majority is that of those who vote, not those entitled to vote, nor of those who are present. This means that creditors who are not present in person or by proxy, or who, although present, do not vote, may be ignored. English case law suggests that the court will ordinarily recognise that the best assessment of whether a scheme is in the interests of those to be bound by it is the vote of those present and voting at the meetings:

Under what circumstances is the Court to sanction a resolution which has been passed approving of a compromise or arrangement? . . . If the creditors are acting on sufficient information and with time to consider what they are about, and are acting honestly, they are, I apprehend, much better judges of what is to their commercial advantage than the Court can be. (Re English, Scottish, and Australian Chartered Bank [1893] 3 Ch 385)

The court must be satisfied that the scheme meeting was truly representative:

if the court is satisfied that the meeting is unrepresentative, or that those voting in favour at the meeting have done so with a special interest to promote which differs from the interest of the ordinary independent and objective shareholder, then the vote in favour of the resolution is not to be given effect by the sanction of the court (Re BTR plc, per Chadwick LJ)

The central issue is whether the scheme is fair in relation to the various interests involved and so could reasonably have been approved at the scheme meetings. In this regard the court will have regard to the relevant comparator to the scheme, namely, the terms of the scheme as against an insolvent liquidation. This is because:

> *an intelligent and honest scheme creditor would . . . give a special consideration to a comparison between the likely, or even probable, future of his debtor company should there be, on the one hand, no scheme and should there be, on the other hand, the scheme proposed. (Re Marconi plc [2003] EWHC 1083 (Ch))*

This highlights the need to have a properly prepared liquidation analysis as the basis for the comparison.

These principles were successfully applied in two cases over the course of 2020. *Rock International Investment Inc*[3] concerned a British Virgin Islands special purpose vehicle incorporated for the purpose of raising finance for the parent and its subsidiaries through the issue of US$300 million in notes pursuant to a New York law governed indenture. The parent and its subsidiaries were in the business of research and development, production, sales and logistics of chemical products, new energy batteries and real estate development. As a result of cross-group defaults and liabilities as guarantor for debts of other companies unrelated to the group, the parent experienced a tightened cash position and liquidity problems. The parent's creditworthiness deteriorated, affecting its ability to refinance, which contributed to the further decline in business for the parent and its subsidiaries. Business was also adversely affected by the covid-19 pandemic because of restrictions on transportation routes.

As a result the company sought sanction from the British Virgin Islands courts to enter into a scheme of arrangement whereby there would be a cash payment of US$185 million to the scheme funded by way of an asset sale together with a consent fee and a work fee. The scheme was overwhelmingly supported by the creditors and approved by the Court on 10 December 2020.

It was subsequently recognised in the United States in *In re Rock Int'l Inv.*, No. 20-35623 (MI) (Bankr. S.D. Tex. Dec. 11, 2020) where the judge held that the British Virgin Islands was the main centre of interest and therefore the main foreign

3 BVIHC 2020/ 184.

proceeding, that the scheme was not contrary to public policy and that the scheme and all orders of the British Virgin Islands courts were granted comity and had full force and effect in the United States.

Constellation was another major success for the British Virgin Islands during 2020, allowing a Brazilian restructuring plan and Chapter 15 recognition in the United States to proceed in parallel with a British Virgin Islands scheme of arrangement in relation to one entity which fell outside of the Brazilian plan. The Court took a pragmatic approach to what was one part of larger global restructuring of the group.

While the British Virgin Islands has, like other offshore jurisdictions, successfully adopted the utilisation of 'light touch' provisional liquidators, there are proposed legislative changes afoot to provide a more bespoke restructuring regime. Cross-class cramdowns within schemes would be a fillip to companies looking to restructure in the British Virgin Islands, as would the formalisation of DIP financing and a streamlined cross-border recognition process. These welcome updates would be fitting for one of the world's leading incorporation centres.

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