HARNEYS
British Virgin Islands

article

Managing the various arrangements

British Virgin Islands ("**BVI**") company law usually takes pride in simplifying itself to try and keep the jurisdiction as "user-friendly" as possible for the users of offshore companies. Although in most instances the legislature has been successful in this regard, one area which perennially causes clients and their legal advisors confusion is the bewildering array of options which come under the broad umbrella of "arrangements" in the BVI.

Strictly speaking, there are three types of "arrangement" that a BVI incorporated company can enter into:

(1) a plan of arrangement, under section 177 of the BVI Business Companies Act, 2004 (the "**BCA**");

(2) a creditors' arrangement, under Part II of the Insolvency Act, 2003 (the "**IA**"); and

(3) a scheme of arrangement, under section 179A of the BCA.

In broad terms, plans of arrangement are intended to deal with restructuring equity interests, and creditor's arrangements are intended to deal with restructuring debt, with schemes of arrangement sitting slightly in the middle. However, each of the three types of arrangement have varying degrees of flexibility but each has subtly different requirements for approval, and so legal advisors will often wish to consider whether it may be appropriate to use the "wrong" tool in certain instances to achieve the best outcomes for their clients.

Plans of arrangement

Of the three types of arrangement, plans of arrangement have the oldest pedigree in BVI law, and for various reasons it is easiest to consider them first. Technically speaking, these are simply known as "arrangements", but in order to differentiate them from schemes of arrangement and from creditors' arrangements, they are normally referred to as plans of arrangement, reflecting the central document which the proposed arrangement will implement.

The provisions of the BCA closely resemble the original section 82 of the International Business Companies Act, 1984 (now repealed). Under both the old legislation and the new, the board of directors of a BVI company was permitted to approve a plan of arrangement to restructure the company's affairs, which might involve:

(a) an amendment to the memorandum or articles;

(b) a reorganisation or reconstruction of a company;

(c) a merger or consolidation of one or more companies that are registered under this Act with one or more other companies, if the surviving company or the consolidated company is a company incorporated under the BCA;

(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).

As will be readily apparent, the possible combination of corporate steps which may be included in a plan of arrangement constitutes a fairly broad church. In practical terms, the directors could approve a plan which would recast the company (or companies) into almost any shape, fashion or form, and restructure the interests of the holders of shares and debt. Some of the individual sub-paragraphs listed in section 177(1) of the BCA (and replicated above) are themselves fairly broad and non-specific; a "reorganisation or reconstruction" could encompass a great many different things, as could "a separation of two or more businesses carried on by the company."

Once the directors have resolved to approve a plan of arrangement, they must then make an application to the BVI court for approval of the proposed arrangement. At the hearing (which is normally referred to as the "first hearing"), the court has the power to:

(a) determine what notice, if any, of the proposed arrangement is to be given to any person;

(b) determine whether approval of the proposed arrangement by any person should be obtained and the manner of obtaining the approval;

(c) determine whether any holder of shares, debt obligations or other securities in the company may dissent from the proposed arrangement and receive payment of the fair value of his shares, debt obligations or other securities;

(d) conduct a hearing and permit any interested person to appear; and

(e) approve or reject the plan of arrangement as proposed or with such amendments as it may direct.

Once the court has approved the plan of arrangement, then the directors may, if they still wish to proceed, confirm the plan of arrangement as approved by the court and then give notice of the plan to each person who the court requires notice to be given, and obtain the consent of each person whose consent the court has indicated is required. Once all relevant consents and approvals are in place, the directors prepare articles of arrangement (which include the plan of arrangement and the relevant court order) which are then filed with the Registrar of Companies. Once the articles of arrangement are filed with the Registrar of Companies, she will issue a certificate in approved form, and the arrangement has effect from the date of registration (or on such later date, up to 30 days later, as may be specified in the articles).

In practice, the court will usually prescribe which persons must be given notice and which persons must give their consent at the first hearing, and will then fix a subsequent hearing date (the "second hearing") at which all of the relevant persons would normally be expected to attend and comment on the plan of arrangement. In the normal course of things, the court will usually require the widest possible notice of the proposed arrangement to be given, and they will expect any person who might dissent or be adversely affected to be given the fullest opportunity to make their objections known. The plan is then fully approved at the second hearing after the court is satisfied that all of the relevant parties have either received the necessary notice or given consent.

Many of the plans of arrangement in the BVI are entirely consensual and the relevant parties have all agreed the relevant plan in advance. Plans of arrangements are often used to take advantage of extreme flexibility of BVI company law to reorganise groups in a single stroke in a way which might be time consuming, expensive or otherwise undesirable if done in a series of individual steps. They simply provide an expedited system for taking a series of steps, and can be used to sidestep "chicken-and-egg" problems which can bedevil complicated reorganisations.

Where plans of arrangement are contested, the court will be particularly mindful of the risk of imposing an arrangement which may unfairly prejudice

the rights of a particular stakeholder. Inevitably where there is disagreement, one party is going to be disappointed with the outcome, but the presupposition is that maintaining an uncomfortable *status quo* is preferable to stripping a party unwillingly of its rights. However, unlike a scheme of arrangement or a creditor's arrangement (as to which, see below), there are no specific approval thresholds which must be met. But, also unlike a scheme of arrangement or a creditor's arrangement, there is a clear system whereby dissenters can be bought out.

The legislation expressly contemplates that holders of shares, debt or "other securities" may be permitted by the court to dissent from the proposed arrangement, and provides a mechanism (in section 179 of the BCA) whereby dissenters may, if so permitted, require that their rights be purchased for fair value by the company. The relevant section relating to dissenter's rights is much less flexible than the statutory provisions which surround it - it is drafted solely with references to shareholders, and contemplates that the relevant dissent would be made at a shareholders meeting. In practice, plans of arrangement do not legally require a shareholder meeting at all (although the court will almost always provide for shareholder consent), and there are no provisions whatsoever to deal with dissenting creditors or other securities holders. However, given the requirement of a court order, the court has wide powers to structure the methods by which dissenters can make their objections known, and be bought out for fair value, and this should be sufficient to paper over the relevant statutory cracks. The expectation would be that the valuation mechanisms in section 179(9) of the BCA would apply to both shareholders as well as the holders of debt and other securities.

Creditors' arrangements

Where the board of directors of a BVI company believes on reasonable grounds that it is insolvent or is likely to become insolvent, it may resolve to appoint a licensed insolvency practitioner to be the interim supervisor of the proposed creditors' arrangement, and the relevant insolvency practitioner must accept or endorse the appointment. The proposed arrangement may:

(a) cancel all or any part of, or vary, a liability of the company;

(b) vary the rights of the company's creditors or the terms of a debt;

(c) provide for circumstances in which persons who become creditors of the debtor after the approval of an arrangement are entitled to be paid under the arrangement in priority to creditors bound by the arrangement;

(d) specify a date or a time at which liabilities of the debtor will be calculated and provide how liabilities arising after that date are to be dealt with;

(e) be entered into in conjunction with any other arrangement, reorganisation or scheme taking effect under the law of another jurisdiction, whether subject to court approval or otherwise; and

(f) provide for the whole or partial cancellation of a liability of the company in return for shares of any kind or for the issue by the company, or by any other person, of a debenture or a security interest; and

(g) relate to an amendment of the company's memorandum or articles that affects the likelihood of the company being able to pay a debt or satisfy a liability.

The legislation expressly contemplates that where the relevant company is in liquidation, the liquidator may appoint himself as the interim supervisor.

The interim supervisor must file notice of his appointment with the Registrar of Companies within two business days. Once appointed, the principal duty of the interim supervisor is to prepare a report on the proposal for the company's creditors, and to assist in this, the company is required to furnish him with a statement of affairs of the company, and the IA confers upon the interim supervisor wide powers to call for further documents or information from the company's directors and officers.

The interim supervisor must call a meeting of the company's creditors within 28 days of his appointment, which must also be advertised. Each creditor must be sent a copy of the interim supervisor's written report. Notice of the meeting (and all relevant documents) must also be given to each of the company's members and directors.

At the meeting the creditors may resolve to approve or reject the proposal, or to adjourn the meeting to a future date no later than three months after the appointment of the interim supervisor. The approval or modification of a creditor's arrangement requires the votes of the holders of 75% or more in value of the company's debt.

Within four business days of the determination of the proposal, the chairman of the meeting is required to prepare a report stating the outcome of the meeting and setting out a list of the creditors and the values of their respective debts. A copy of this report is then sent to each creditor, and a copy is filed with the Registrar of Companies.

If the proposal is approved, then the supervisor (who in practice, will normally be the same person who acted as interim supervisor) must file notice of his appointment with the Registrar of Companies within two business days, and the proposal is made binding on the company and each of its members and creditors.

The IA expressly provides that the rights of (a) a secured creditor, and (b) a preferential creditor, may not have their rights adversely affected by a creditor's arrangement without their consent.

Creditors' arrangements differ from the other two forms of arrangement most noticeable in that:

(1) they do not, in the ordinary course, require any application to be made to the BVI court (although creditors who believe that they have been "unfairly prejudiced" have the right to ask the court to intervene); and

(2) they require a licensed insolvency practitioner to act as supervisor of the arrangement.

There is scope for debate on whether that makes a creditor's arrangement cheaper than the other two types of arrangement or not; people's views on the subject are usually determined by whom they regard as more expensive to retain - litigation lawyers or licensed insolvency practitioners.

Schemes of arrangement

If plans of arrangement are the oldest form of arrangement in BVI law, then schemes of arrangement are the newest, being introduced in an amendment act in 2005. The change was a deliberate attempt to copy similar provisions which had been a popular feature of Cayman Islands law.

When compared to plans of arrangement, the legislative provisions relating to schemes of arrangement seem admirably brief and focused. Section 179A of the BCA simply states that where there is a proposed compromise or arrangement between a company and its creditors (or any class of them) or the company and its members (or any class of them), then an order may be sought from the court calling a meeting of the creditors or members (or, in either case, the relevant class). An application can be made by the company, any creditor, any member or the company's liquidator.

Once the relevant meeting has been called, the proposed compromise or arrangement needs to be approved by 75% in value of the creditors or members (or, in either case, the relevant class), and if so approved and if sanctioned by the court, will then be binding on the remaining members of the class and the company, and (if the company is in liquidation) any person who is bound to contribute to the assets of the company once the relevant order has been filed with the Registrar of Companies (although the Registrar does not issue a certificate to confirm registration). The company is also bound by law to attach a copy of the court order approving the scheme to every copy of its memorandum of association after the date of the order.

The provisions relating to schemes of arrangement are almost brutally short, and most notable for what they do not contain rather than what they do.

(1) There is no statutory protection for the rights of secured creditors or preferred creditors (although in practice it is highly unlikely that the court would sanction a scheme of arrangement which interfered with secured creditors' rights or preferred creditors' rights without their consent).

(2) There is no provision for dissenter's rights.

(3) There is no requirement for any form of official supervision of the scheme of arrangement (beyond the requirement of court sanction).

(4) There does not appear to be any consideration of how restructuring the rights attached to one class of shares or debt may have an impact on other classes of shares or debt issued by the company.

(5) Although it is reasonably clear what will amount to 75% in value in relation to debt, it is less clear how this would apply to different classes of shares, particularly if one or more class of shares are shares of no par value.

Despite its apparently deceptive simplicity, schemes of arrangement have not yet proved particularly popular in the BVI. At the date of writing, only one scheme of arrangement has been fully implemented in the approximately six years that the statutory provisions have been available. It is not entirely clear why this is the case, although it may be possible to speculate that if the parties need to incur the time and cost of two full court hearings to implement the relevant arrangement, they may be more likely to opt for a plan of arrangement under section 177 of the BCA which appears to offer more flexibility with respect to outcomes, and enables the court to consider the position of a wider range of stakeholders in relation to the arrangement.

However, the use of schemes of arrangement may become increasingly popular as parties who believe they would have trouble securing the additional consents needed for either a plan of arrangement or a creditor's arrangement may feel that they have better prospects getting the smaller number of approvals (ie. only the same class or shares or debts) necessary for the court to approve a scheme of arrangement.

Summary

Whilst the users of BVI companies are fortunate to have at their disposal so many different options to reorganise their company's affairs, should restructuring be necessary, such reorganisations are expensive, and care needs to be taken that all of the options are properly considered to maximise prospects of a successful outcome.

Which arrangement is most suitable? A thumbnail guide.			
	Plan of arrangement	**Creditor's arrangement**	**Scheme of arrangement**
Restructuring debt or equity?	Either or both, but emphasis on equity	Debt	Equity or debt (but not both)
Court approval?	Yes	No	Yes
Supervisor?	No	Yes	No
Consents and approvals?	As directed by the court	75% in value	75% in value
Dissenter's rights?	Yes	No	No
Statutory protection of secured creditors?	No	Yes	No
Insolvency requirement?	No	Yes	No
Permitted during liquidation?	Yes	Yes	Yes

Further Information

The foregoing is for general information purposes only and not intended to be relied upon for legal advice in any specific or individual situation.

For more information on the subject please contact Colin Riegels (colin.riegels@harneys.com) or your usual Harneys contact.

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