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## *Buyer Beware: How to Ensure the Valid Issuance of BVI Company Shares*

*Subscribers for shares in a British Virgin Islands (BVI) company usually assume that such shares have been validly issued and they are quick to point to their share certificate or even the share register of the BVI company as absolute evidence of that fact.*

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*A purported shareholder's assumption is most often tested when he attempts to sell his shares.*

They are often surprised to learn that the issuance of a share certificate for registered shares can be an optional step for a BVI company and further that possession of a registered share certificate does not truly indicate ownership of shares for the purposes of BVI law.

On the other hand, subscribers who point to the share register of a BVI company as evidence that they own shares are correct to do so, but such ownership may be challenged based on the facts surrounding the terms on which the shares were issued.

A purported shareholder's assumption is most often tested when he attempts to sell his shares.

Recently concluded due diligence exercises have revealed the following missteps:

(a) payment for a share is not made in cash but the resolutions approving the share issue either do not mention this or mention it in passing; and

(b) resolutions have been passed approving the share issuance, the share register has been updated and the share certificate issued but the subscriber has not agreed in writing to pay for the shares and no consideration, in any form, has been paid to the BVI company because of logistics (the company may not have opened a bank account) or the subscriber may simply not have appreciated that payment should have been made at the time.

Such omissions have serious consequences under BVI law.

Not only can they affect the validity of a shareholder's ownership, they can also impose liability on a company's directors as the BVI Business Companies Act (the **BCA**) demands that every company shall at all times have one or more members and provides that if a company has no members, a director, or any other person doing business in the name of or on behalf of the BVI company, can be sued and held personally liable for the company's debts.

Below, we examine requirements which must be adhered to, so as to ensure that shares have in fact been validly issued.

## Share issuance

The BCA in many instances copied the language of its predecessor legislation – the International Business Companies Act (the **IBCA**). An exception to this arises with respect to the provisions relating to share issuances.

A distinction must be drawn between the requirements for a share issue by:

- (i) companies originally registered under the IBCA to which the provisions of Schedule 2 Part IV of the BCA (the **Schedule**) apply (the **Part IV Cos**); and
- (ii) companies originally registered under the BCA and companies originally registered under the IBCA but which elected to disapply the provisions of the Schedule (the **BCA Cos**).

## Part IV Cos vs BCA Cos

### *Part IV Cos*

Section 17 of the Schedule dictates that “no share...may be issued until the consideration in respect of the share is fully paid, and when issued the share is for all purposes fully paid and non-assessable ...”.

Section 19(2) of the Schedule goes on to indicate that shares issued upon the conversion of, or in exchange for another share or debt obligation or other security in the company “shall be treated for all purposes as having been issued for money equal to the consideration received or deemed to have been received by the company”.

For Part IV Cos therefore, consideration for a share is due at the time of issuance and once such consideration is paid as a factual matter, then any share issued is fully paid.

### *BCA Cos*

Section 36 of the main provisions of the BCA obviates the need for payment of consideration at the time of the issue of the share and instead states a BCA Co may, subject to its memorandum and articles, issue “bonus shares, partly paid shares and nil paid shares”.

Further, the main provisions of the BCA do not contain an equivalent of section 19(2) of the Schedule.

With BCA Cos, there is no guarantee that an issued share is fully paid.

### *New Requirements – Sections 48 and 49*

In addition to allowing for the valid issuance of partly or nil paid shares, the main body of the BCA added two very significant sections which apply to share issuances by both Part IV Cos and BCA Cos.

## Section 48

Section 48 dictates that “before issuing shares for a consideration other than money, the directors shall pass a resolution” stating:

- “(a) the amount to be credited for the issue of the shares;
- (b) their determination of the reasonable present cash value of the non-monetary consideration for the issue; and
- (c) that, in their opinion, the present cash value of the non-money consideration for the issue is not less than the amount to be credited for the issue of the shares.”

The section seems straight forward - if cash is paid for a share, then there is no concern but if payment is to be made in any manner other than by cash, this will trigger the need for the statutory language to be included in the share issuance resolutions.

Some forms of memorandum and articles for BVI companies indicate the statutory requirement but many, including those for Part IV Cos, may not. In addition, some BVI registered agents (**RAs**) flag the requirements of the section or some clients are advised of the provision when they consult with their attorney but the section 48 language is frequently omitted simply because clients are not informed of the demands of the legislation.

Further, a question arises in connection with the capitalisation of loans and in situations where shares are issued in exchange for other shares or other securities issued by the company.

Part IV Cos appear to be excluded from the requirements of section 48 of the BCA by virtue of the language in Section 19(2) of Schedule 2 Part IV of the BCA, which provides that consideration in the form of shares or debt obligation or other security in the company shall be treated as money.

BCA Cos are not exempt from section 48 however and some argue that in relation to the capitalisation of loans, the loan amount is the consideration being paid for the shares and it is money and therefore that section 48 language is not necessary. Others are of the opinion that “past consideration” concerns arise on a loan capitalisation and they therefore embrace the more conservative view that the consideration paid is the benefit that the company derives from the forgiveness of the debt - which is not money - and therefore section 48 language is needed.

As the inclusion of the statutory language is not detrimental, it is best to err on the side of caution and we recommend that section 48 wording be inserted in the authorising resolutions of BCA Cos prior to the issuance of a share in connection with a loan capitalisation or a share exchange or conversion.

## Section 49

Pursuant to section 49, a share that:

- “(a) increases the liability of a person to the company; or
- (b) imposes a new liability on a person to the company,

is void if that person, or an authorised agent of that person, does not agree in writing to become the holder of the shares.”

Whilst the language of section 49 is not as straightforward as section 48, the result of a failure to adhere to the section is strikingly clear.

Section 49, does not specify the circumstances in which the issuance of a share could create or increase the liability of a person to a BVI company. In our view however such circumstances must include when a share is issued but full consideration is not paid at the time of issuance.

The proposed issuance of any nil or partly paid share will therefore require a subscriber or his agent to agree in writing to take such share and a failure to do so will render the share issuance void.

A concern here is whether this section will also be relevant if the par value of a share increases after the date of its issuance.

The BCA requires both Part IV Cos and BCA Cos to issue par value shares for no less than their par value. Section 47(3) of the main body of the act stipulates that if less than par value is paid for the share then “the person to whom the share is issued is liable to pay to the company an amount equal to the difference between the issue price and the par value.”

Some argue that if a share is issued and the full par value is paid at the relevant time, then sections 47 and 49 ought not to apply if the share’s par value is subsequently increased, as the increase in par value is distinct from a new share issue.

There is however room for a contrary argument so that a shareholder may be asked to agree in writing to continue to hold a previously fully paid up share, where its par value is to be increased but the difference between the initial par value amount paid and the new par value amount will not be received by the company until a future date.

## Solutions

Both sections 48 and 49 are easily complied with.

The directors in making the statements necessary under section 48 are not statutorily required to seek official valuations to assist them in their determinations, so provided that they act in accordance with their fiduciary duties, the directors may independently calculate the figures to be inserted in the resolutions.

BVI legal practitioners are often asked whether a subscription letter must be executed in relation to a share issuance. In the past, the general response to this question has been “no” but section 49’s requirements would be easily addressed with the introduction of such letters as standard practice.

We would suggest that in the same way that consent letters for a person to act as a director are now typically included in incorporations packs circulated by RAs, a basic subscription letter could also be included, which would alert subscribers to their BVI law obligations.

For subscribers who find that they have overlooked the requirements of sections 48 and 49, we would strongly recommend that they consult with BVI counsel to evaluate their position.

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