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Insolvency & Restructuring in the BVI: An Emerging Trend of Using Insolvency Practitioners in the Context of Commercial Litigation?

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Introduction

Nobody knew what effect the enactment of the BVI Insolvency Act in 2004 would have on the insolvency and restructuring market in the BVI, but it has not necessarily developed in the manner expected by some insolvency and legal practitioners. The flow of insolvent liquidations and receiverships has been fairly modest, but despite progressive increases, there has not been the explosion of appointments some had expected from a jurisdiction with almost 803,000 company registrations at 30 June 2007.¹ This can easily be explained by the generally benign global economy which has applied equally to BVI registered companies as others.

Statistics produced by the BVI Financial Services Commission for the years ended 31 December 2004, 2005 and 2006, show the total number of appointments under the Insolvency Act has increased significantly from 23 appointments in 2004 to 46 in 2005 and 87 in 2006.

The current global economic slowdown and the typical roles of BVI companies, for example, as holding companies in complex group structures, vehicles for joint ventures, hedge/mutual funds and captive insurance companies, amongst others, are almost certain to result in an increase in the number of insolvencies of BVI companies during 2008. It is clear, however, that any anticipated increase in the number of insolvencies can be accommodated following the significant growth

in the teams of experienced insolvency practitioners (IPs) and lawyers now well established in the BVI.

A major development in the judicial system in the BVI is the future establishment of the Commercial Court, which will be part of the Eastern Caribbean Supreme Court. Premises have been identified and advertisements placed for an experienced judge. This development will be welcomed as it continues to demonstrate the BVI's commitment to meeting the needs of companies registered in the jurisdiction.

An emerging trend?

Commercial cases reaching the Courts in the BVI often involve large, complex and frequently, highly acrimonious disputes which are global in reach. The creation of the dedicated Commercial Court will further enhance the reputation of the BVI as a reliable jurisdiction, with its appeal routes to the Eastern Caribbean Supreme Court of Appeal and the Privy Council in London. The level of litigation involving BVI companies means that IPs are frequently being appointed by the BVI Court as Court-appointed Receiver or Provisional Liquidator of companies involved in commercial disputes. Types of cases seen recently include:

- Shareholder disputes;
- Disputed ownership of assets;

	2004	2005	2006
Receiverships	3	16	3
Provisional Liquidations	4	8	28
Insolvent Liquidations	16	21	56
Company Voluntary Arrangements	0	1	0
Total appointments	23	46	87

Data for the year ended 31 December 2007 was not available at the time of publication.

Notes

¹ BVI Financial Services Commission Statistical Bulletin, volume 7 June 2007.

- Asset protection arrangements;
- Allegations of fraud or other improper conduct;
- Breaches of duty and/or conspiracy; and
- General contractual disputes.

Court-appointed receivership and provisional liquidation are regarded as draconian remedies of last resort. However, recent cases in the BVI have demonstrated that the Court is prepared to make appointments of Receivers or Provisional Liquidators, when there are strong grounds, in the context of commercial litigation proceedings, thereby activating powerful tools for identifying, tracing and securing assets. This is particularly the case in circumstances where Freezing and Disclosure Orders have proven to be ineffective and where there continues to be a real risk that assets will be dissipated and/or books and records are at risk of destruction.

The role of a Receiver or Provisional Liquidator, when appointed in such an interlocutory capacity, is to 'hold the ring'. In other words, to take such steps as he or she considers appropriate to identify, locate and obtain possession and/or control of property for the benefit of those who are entitled to it, pending the outcome of the wider proceedings. Such appointments are probably encountered much more frequently in the BVI than in other jurisdictions such as the UK, because of both the activities of BVI companies and the nature of the commercial disputes and situations referred to above. During 2007, the BVI Court has demonstrated a robust attitude to the appointment of Receivers and Provisional Liquidators, often on an *ex parte* basis (it should be noted that Respondents have a right to apply to the Court, on notice to the Claimant, to vary or discharge the Order and there will be an *inter-partes* hearing sometime after the *ex parte* Order is made).

The purpose of this article is not to review, in any detail, the powers given to Receivers and/or Provisional Liquidators, but to use recent cases to: (i) illustrate the circumstances in which such appointments are being made by the BVI Court; and (ii) consider some of the practical issues which may arise from the perspective of the IP, the Claimant and Respondent.

Court-appointed receiverships

The BVI Court has jurisdiction to appoint a Receiver in circumstances where it appears 'just and convenient

that an order be made ... either unconditionally or upon such terms and conditions that the Court or judge thinks fit'.² As a result, a Court-appointed Receiver's powers are set out in the Order under which he or she is appointed. It should be noted that the terms of the Order are drafted by the Claimant and are, therefore, tailored towards the facts of the case and the needs of the Claimant. Orders will typically authorise the Receiver to:

- Identify and secure the assets over which he or she has been appointed, wherever they may be located;
- Exercise all of the powers which would be vested in the Respondents directors (to the exclusion of the directors), save for the power to defend the receivership proceedings; and crucially
- To bring proceedings against any person.

A Receiver appointed by the BVI Court will also have the statutory powers given to Receivers appointed under a debenture or contract and contained in the Insolvency Act. This is in contrast to the United Kingdom where such provisions do not exist. However, these rather basic and fundamental powers will usually be incorporated in the terms of the Order under which the Receiver was appointed. The Insolvency Act contains some rather helpful provisions regarding the level of co-operation which should be given to a Receiver of a BVI company. In short, a company and its officers must give the Receiver such assistance as he or she may reasonably require. This includes making available any relevant books, information and documents under their control and, if required by the Receiver, verify by statutory declaration that such books, information and documents are complete and correct.³

Recent Court-appointed receiverships

The following cases, all of which are either current or recent, serve to illustrate the wide range of differing circumstances where appointments have been made and some of the unusual and interesting matters arising.

Case study I

The first case we will look at is current and involves a trust company that sought the appointment of a Receiver to two BVI companies. The Receiver's appointment

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- 2 The BVI Court's jurisdiction to appoint Receivers arises out of section 24 of the West Indies Associated States Supreme Court (Virgin Islands) Ordinance, Cap 80. Part 51 of the Civil Procedure Rules, 2000, also provides for the appointment of Receivers and outlines the procedure by which such applications should be made.
- 3 These requirements are enforceable by order of the Court. The sanction for failure to comply with such an order is a fine of US\$5,000 and/or up to 12 months imprisonment.

arose out of the concerns of the Trustee and principal beneficiaries of three discretionary trusts, regarding the conduct and future intentions of the representative of the Trusts' protector. The Trustee commenced proceedings in various jurisdictions to identify and secure control of the Trusts' assets. As part of this process, William Tacon was appointed by the BVI Court as Receiver of the assets of the 2 BVI Respondents.

The Receiver identified and secured substantial cash deposits and other quoted investments, held in the Respondent's accounts at institutions located in several jurisdictions. The subsequent disclosure of bank records for those accounts and others, revealed that substantial sums had been paid to third parties for no apparent commercial benefit or consideration and that there was a connection to parties resident in the United States of America. The Receiver filed an application in the New York District Court, Southern District of New York, for judicial assistance pursuant to section 1782 of 28 United States Code, which directly led to an Order that the Receiver be entitled to take evidence from the representative of the protector by way of deposition.

The evidence adduced during the two day deposition of the party concerned materially assisted the Receiver and the Trustee in filing joint proceedings in the New York Court against the representative of the protector and certain entities allegedly owned and/or controlled by him. These proceedings enabled the Receiver and the Trustee to obtain a Temporary Restraining Order (subsequently replaced by a Preliminary Injunction), preventing those parties from taking any action to dispose of the assets which may have been received from, or held on behalf of, the Respondent BVI companies.

The New York proceedings remain ongoing, but it is clear that the appointment of a Receiver was imperative, as Freezing and Disclosure Orders alone would not have enabled the claimant to identify and trace the assets identified by the Receiver, nor would they have provided a platform for the deposition proceedings to be initiated and assets held by third parties to be secured. The entire process of seeking recognition and proceeding to the deposition was quick, taking only a few weeks.

Case study 2

In this case, the Claimant filed proceedings in the BVI against a number of BVI registered companies, thought to hold shares which had been issued to them in knowing breach of fiduciary duties and pursuant to a common law conspiracy. In brief, the Claimant alleged that a number of former employees had, during their employment with it performed services for clients and failed to account to the Claimant for fees properly payable. It was alleged that the fees received by the former employees of the Claimant included shares in a company the Claimant had advised in relation to its initial

public offering, which in fact had been issued to the Respondents. The Claimant alleged that these breaches of fiduciary, contractual and other duties represented a fraud on the Claimant. Various orders were subsequently made by the BVI Court, appointing William Tacon as Receiver over certain of the Respondents.

The purpose of the receiverships was to require disclosure to be made to the Receiver as to whether or not funds and/or assets in which the former employees might have had an interest (or over which the Claimant should have had an interest) had been directed to the Respondents.

An unusual feature of the original Orders obtained was that the Receiver was obliged to disclose his findings to the Claimant. These Orders were subsequently modified, following applications being made by certain of the Respondents, on the basis that the Court's previous Orders were too far-reaching and did not sit comfortably with the neutral position of the Receiver as between the parties to the proceedings.

The Receiver frequently reported to the Court the outcome of his investigations by way of detailed written reports, which were also made available to both the Claimant and the Respondents. Information was made available to the Receiver by Respondents on the basis that it would not be disclosed to the Claimant, but could be included in his reports to the Court. Commercially sensitive, prejudicial or confidential information potentially relevant to the Court, was brought to its attention through the use of redacted reports and sealing orders, as necessary. The Court has or will determine the point of time at which the various receiverships should be discharged on the grounds that they can no longer serve any purpose.

Case study 3

The BVI Court has appointed Joint Receivers in *Danone Asia PTE Limited and others v. Golden Dynasty Enterprise Ltd and others*. The Claimants were subsidiaries of the French listed food and beverage company, Groupe Danone, which had been used to enter into joint venture agreements in Peoples Republic of China (PRC) with the Wahaha Group.

The Respondents were 8 BVI registered companies, thought to hold shares in various other companies registered in PRC. In May 2007, the Claimants had commenced arbitration proceedings before the Stockholm Chamber of Commerce, in relation to certain breaches of the joint venture agreements. The Respondents to those proceedings were various PRC companies which were alleged to be connected to the Wahaha Group. The Claimants claimed to have evidence which demonstrated that the Stockholm Respondents had, through the BVI Respondents, been unlawfully engaged in production or business activities in direct competition with the Claimants' Joint Venture companies in PRC. The

Claimants further argued that the profits and/or assets produced from these unlawful acts were being diverted or concealed using the BVI Respondents.

Essentially, the Arbitration Proceedings in Stockholm, together with other ancillary proceedings commenced in the Los Angeles Supreme Court, were focused on the substantive claims as to the alleged breaches of the joint venture agreements. The BVI proceedings, in conjunction with similar proceedings filed in Samoa, were initiated to secure the proceeds of the alleged breaches. In November 2007, IPs from KPMG in BVI and Hong Kong were appointed as Joint Receivers of the BVI Respondents. However, it appears from articles in the press that shortly thereafter, both parties agreed temporarily to suspend all litigation proceedings in order to pursue settlement discussions. It is unclear whether those settlement discussions remain ongoing, but it is quite possible that the appointment of the Joint Receivers over the BVI Respondents was a factor in the parties' decision-making process.

Overview

These cases demonstrate that the Court will appoint receivers when it is satisfied that assets need to be identified and secured. In our experience, the Court does not entertain applications lightly, but is, nonetheless, prepared to be robust and decisive. The circumstances of the above mentioned cases are widely different but serve to illustrate the attitude of the Court.

Provisional liquidations

The appointment of a Provisional Liquidator is sometimes seen by Claimants as a more attractive alternative to filing a writ action, together with seeking injunctive relief or the appointment of a Receiver. The need for speed, for example, if there is a risk of dissipation of assets, can make an application to appoint a Provisional Liquidator appropriate, rather than pursuing the usual remedies available to a creditor. The decision whether a Claimant or Applicant seeks to appoint a Receiver or a Provisional Liquidator will very much turn on the facts of each case. The appointment of Provisional Liquidators can be an especially damaging, and possibly terminal, development for a trading company, and as such, is not a decision taken lightly by the Court.

The Insolvency Act provides that the BVI Court may appoint a liquidator if the company is insolvent

or it is just and equitable to do so. Appointments on the just an equitable ground in the BVI are relatively more commonplace than in the UK, as a result of the amount of litigation involving allegations of fraud or other inappropriate behaviour. If interim relief is granted to an Applicant through the appointment of a Provisional Liquidator, the Court will ordinarily determine whether the Provisional Liquidation should be discharged, or liquidation ensue, within six months of the date on which the original application was filed.⁴ The Court is cognisant of the need for matters to be determined as quickly as possible, in view of the uncertainty that is caused by an appointment.

The role of a Provisional Liquidator is similar to that of a Court-appointed Receiver, in that he or she is appointed on a temporary basis to identify and maintain the value of any assets which may be owned or controlled by the Company and they are in a neutral position as between the parties. A Provisional Liquidator has all of the statutory rights and powers given to a Liquidator, save for the power to make distributions. Thus, a Provisional Liquidator will have much wider powers of investigation as regards the company's affairs than a Receiver. One important consideration, which may dictate the nature of the relief sought, is that a Provisional Liquidator (in contrast to a Court-appointed Receiver) can initiate and defend proceedings in the name of the Company in his or her own right.

Some examples of circumstances in which it may be just and equitable to wind up a company have been established in case law, but these examples are by no means exhaustive. Importantly, it appears to have been accepted by the Eastern Caribbean Court of Appeal in *RBG Global SA*, that, where there is *prima facie* evidence that that a company has been used as an instrument of fraud, there was a good arguable case that the company be placed into liquidation on the just and equitable ground.

When making an application for the appointment of a Provisional Liquidator, an Applicant will need to demonstrate that they have the requisite *locus standi* to bring the application. Pursuant to the BVI Insolvency Act, an application on the just an equitable ground can only be made by a creditor, a member or the company itself.⁵

Recent examples

A recent example of a company placed into provisional liquidation on the company's own application is Boston Life & Annuity Company Limited, where IPs from

Notes

⁴ The Court may extend this period in 'special circumstances'.

⁵ An application to appoint a liquidator can also be made in respect of a regulated entity by the BVI Financial Services Commission and the Attorney General can make an application on public interest grounds.

KPMG were appointed and subsequently confirmed as Liquidators.

In terms of appointments on the application of a creditor, the BVI Court has addressed the question of standing by citing the English case, *Re Claybridge Shipping Co*, which confirmed that the issue of standing is satisfied if the Applicant can establish a good arguable case that it is a creditor of the company.

In *Kensington International Limited v Montrow International Limited*, the Applicant had previously obtained four judgments against a sovereign State in the amount of some US\$93 million, in the English Commercial Court. The defendant was a BVI registered company and the sole shareholder of another company (which was not registered in the BVI) that held the rights to exploit certain valuable assets located in the State concerned. The Applicant obtained an Order for the appointment of a Provisional Liquidator to both companies having argued that the Defendant and its subsidiary were part of a complex scheme to render judgment-proof assets held by them against enforcement by the Applicant and the State's other judgment creditors. Furthermore, the Applicant argued that the BVI Defendant was likely to be an alter ego of the State in question. The Court-appointed William Tacon as Provisional Liquidator of Montrow International Limited and its overseas subsidiary.

The decision was appealed but the Court of Appeal upheld the judgment in the first instance and agreed that matters needed to be explored further at the substantive hearing. The BVI Order was subsequently recognised by the Royal Court of Jersey and notwithstanding challenge by the Jersey based directors of the BVI Company, the Royal Court ordered the directors to comply with the terms of the BVI Order.

This example demonstrates that the decisions of the BVI Court can withstand challenge and scrutiny in other important jurisdictions.

Practical considerations and other issues

Fees and relationship of Office Holder to Claimant

It is often the case that there are insufficient assets available in an estate, or they cannot easily be realised, to meet the fees and expenses of the Receiver or Provisional Liquidator. In such circumstances, it will be necessary for the Claimant or Applicant to provide adequate funding to the Office Holder, on such terms as may be agreed between them, pending any Order being made for costs and expenses to be met from the estate.

Applications for the payment of fees and expense from estates may be attractive to Claimants and Applicants from a cash flow perspective, but they are not granted by the Court as a matter of course. In a recent contested case, the Court adjourned a Receiver's application, pending the hearing of the Respondent's application to

discharge the Receivership Order. The Court expressed sympathy with the Respondent's submissions that the Receiver's remuneration should not be paid from the assets under his control, in circumstances where it was possible that the receivership would be discharged and that the Court may order his remuneration be paid by the Claimant.

Neutrality

The need for Court-appointed Receivers and Provisional Liquidators to be, and to be seen to be, neutral as between the parties, is of the utmost importance. The Office Holder, who is usually being funded by the Claimant or Applicant, must at all times be cognisant of his or her impartial position. This can create a tension if a Claimant or Applicant sees the Office Holder as being little more than an extension of their own legal team, who is obliged to act upon their instructions.

Damages

The appointment by the Court of a Receiver or Provisional Liquidator can cause considerable damage. The BVI Court will not, therefore, make an order appointing a Receiver or a Provisional Liquidator, without an undertaking in damages being given by the Claimant. In most cases, the Court will require fortification of the undertaking with security. This is particularly the case where the Respondent is an active trading company. The sums involved may not be particularly high, in one case the sum deposited amounted to US\$100,000, when the claim itself amounted to almost US\$100 million. In another case, no fortification was required as the Claimant was itself a BVI registered company.

Directions

As Officers of the Court, Receivers and Provisional Liquidators are entitled to seek directions from the Court on matters pertaining to their appointment. For example, the Office Holder may wish to initiate legal proceedings in another jurisdiction and in such circumstances, it is prudent for Court sanction to be obtained. It may also be wise for sanction to be given by an independent judge, who is not involved in the substantive proceedings.

Reporting

It is fair to say that Office Holders are no strangers to updating the Court on the actions taken following their appointment and the progress of their investigations. However, Receivers and Provisional Liquidators appointed in connection with commercial litigation proceedings must be mindful of the fact that their reports

will be subject to a high level of scrutiny, as both parties may well be seeking to use the Office Holder's findings in support their positions in the wider proceedings.

Approach adopted by Office Holder

The effectiveness of the appointment of a Receiver or Provisional Liquidator will ultimately depend upon the approach taken by the individual Office Holder. He or she could adopt an active role in terms of seeking information, initiating proceedings for the recovery of assets and obtaining the assistance of Courts in other jurisdictions. Alternatively, a passive approach may not achieve much more than the relief obtained from Freezing and Disclosure Orders.

Conclusion

The Court in the BVI has demonstrated its willingness to appoint Receivers or Provisional Liquidators in cases where these processes are appropriate. Quite rightly, nothing should be taken for granted, but well structured applications made on strong grounds are likely to succeed. The processes themselves, as part of wider proceedings, are powerful with asset identification and protection, combined with investigatory powers, at their core.

Recent experience shows the Courts and legal practitioners have demonstrated both responsibility and pragmatism in their use of these processes. Parties contemplating proceedings of this kind can be confident that the BVI possesses a Court, lawyers and IPs who are all able to deal effectively with challenging circumstances, often involving large amounts of money.

International Corporate Rescue

International Corporate Rescue addresses the most relevant issues in the topical area of insolvency and corporate rescue law and practice. The journal encompasses within its scope banking and financial services, company and insolvency law from an international perspective. It is broad enough to cover industry perspectives, yet specialized enough to provide in-depth analysis to practitioners facing these issues on a day-to-day basis. The coverage and analysis published in the journal is truly international and reaches the key jurisdictions where there is corporate rescue activity within core regions of North and South America, UK, Europe Austral Asia and Asia.

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