British Virgin Islands Joint Venture Companies

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Preface

This publication has been prepared for the assistance of those who are considering establishing a joint venture company in the British Virgin Islands. It deals in broad terms with the requirements of British Virgin Islands law. It is not intended to be exhaustive but merely to provide brief details and information which we hope will be of use to our clients. We recommend that our clients seek legal advice in the British Virgin Islands on any specific proposals before taking steps to implement them.

Conyers Dill & Pearman

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1. INTRODUCTION

A business company incorporated under the laws of the British Virgin Islands is a common and useful joint venture vehicle. Setting up such companies, particularly for investment into China, is a busy practice area for our firm. Generally, such a company will have two or more shareholders, and a shareholders agreement structuring the relationship between them. A joint venture company may be used for a variety of purposes, including to hold shares in an operating company or to finance the acquisition of a specific asset. This publication discusses the law of the British Virgin Islands pertaining to joint ventures.

2. SHAREHOLDERS AGREEMENTS

When structuring a joint venture company, consideration must be given as to whether specialised memorandum and articles of association are required to ensure the deal set out in the shareholders agreement is enforceable in accordance with its terms. The BVI Business Companies Act (the "BC Act") provides that two or more members of a company may by agreement in writing provide that in exercising any voting rights the shares held by them shall be voted (a) as provided by the agreement, (b) as the parties may agree, or (c) as determined in accordance with such procedure as they may agree upon.

However, the shareholders agreement will also deal with the management and administration of the company as well as contain rights and restrictions on the transfer of shares of the company. It is likely that certain provisions of the shareholders agreement must be included in the memorandum and articles of association of the joint venture company, and it is possible that certain provisions of the shareholders agreement should be included in the memorandum and articles of association.

Provisions in the shareholders agreement dealing with matters which are determined exclusively by the memorandum and articles of association (such as quorum and notice requirements) must be incorporated into the memorandum and articles of association in order to be enforceable. It may be prudent to include other provisions of a shareholders agreement in the memorandum and articles of association of a company. Such provisions generally include rights and restrictions on the transfer of shares, such as pre-emptive rights, rights of first refusal, tag-along rights, drag-along rights, coat-tail rights and other similar rights. While the provisions in the shareholders agreement may be enforceable in their own right as a matter of contract law, it is possible for a court to merely award damages in the event of a breach of the shareholders agreement rather than specific performance. Specific performance (such as invalidating a transfer of shares in breach of pre-emption requirements) is an equitable remedy available at the court's discretion. Specific performance will only be ordered when the court determines that damages are not adequate to compensate the injured party for the breach of the shareholders agreement. It may also be difficult to quantify damages in certain cases. As such, we recommend that consideration be given to whether certain provisions should be included in the memorandum and articles of association of the company to ensure that any violation of the above rights or restrictions is necessarily void or voidable.

3. APPOINTMENT OF DIRECTORS

Another area where consideration should be given to including provisions of a shareholders agreement in the memorandum and articles of association of a company is the appointment of directors. Shareholders agreements often require that a shareholder be entitled to elect a director to the board of

directors of the company. However, unless otherwise provided, directors are elected by resolution of shareholders approved by a majority of the votes cast at a duly constituted shareholders meeting. The effect of the shareholders agreement is to only require a shareholder to vote for another shareholder's nominee. It has been our experience that where there is a dispute between shareholders, one of whose nominee directors has resigned or passed away, it is often difficult to obtain the necessary vote of the other shareholder to elect a replacement director, notwithstanding he had agreed to vote for the other shareholder's nominee. While recourse may be made to the courts, this is sometimes not desirable in the early stages of a dispute. Further, in the event an application is made to the court, the aggrieved shareholder must rely on the equitable discretion of the court to grant specific performance, which as indicated above, the courts will only allow when damages are not an adequate remedy. As such, we recommend that the power for a shareholder to appoint a director be included in the memorandum and articles of association. The method to accomplish this objective is to create a separate class of shares for each shareholder who will have the right to elect a director. In this instance, each class of shares will have the right to elect a certain number of directors and the relevant shareholder will hold all the shares of that class.

4. FIDUCIARY DUTIES

The BVI Business Companies Act provides that a director of a company that is carrying out a joint venture between the shareholders may, when exercising powers or performing duties as a director in connection with the carrying out of the joint venture, if expressly permitted to do so by the memorandum or articles of association of the company, act in a manner which he believes is in the best interests of a shareholder or shareholders, even though it may not be in the best interests of the company. This statutory language allows a joint venture company to vary the fiduciary duty obligations of a director under common law.

Typically, a director owes its fiduciary duty to the company as a whole. This can create difficulties for a director where a proposal is clearly in the best interests of the company, but is not supported by the shareholder who nominated such director. In that instance, the director must either approve the proposal or risk breaching his fiduciary duty to the company. Joint venture companies that wish to avoid this issue for their directors may vary this fiduciary duty in their memorandum and articles of association.

It should be noted that the ability to vary such a duty is to the best of our knowledge unique to the British Virgin Islands. There is no case law on point such that if it is intended to include such a provision in the memorandum or articles of association care should be taken to consider its impact in connection with the proposed joint venture company.

5. PUBLIC INSPECTION

The memorandum and articles of association of a British Virgin Islands business company are filed with the Registrar of Corporate Affairs (British Virgin Islands) and as such are available for public inspection. While the memorandum and articles of association are drafted in general terms (referring to members generally rather than to the names of specific members), clients should advise Conyers Dill & Pearman of any sensitivities in this regard.