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Insolvency 2022

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British Virgin Islands: Trends & Developments

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Trends and Developments

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Market Analysis

Throughout 2022, the British Virgin Islands (BVI) has remained one of the most significant international jurisdictions. According to the latest BVI Financial Services Commission (FSC) statistical bulletin dated June 2022, in the BVI there were 370,150 active business companies with a further 2,257 active limited partnerships, a significant increase on the previous year.

The BVI has retained its status as one of the most significant jurisdictions in the international corporate service sector and, in particular, the insolvency and restructuring sector. Throughout this period, the BVI has proved to be a resilient and agile jurisdiction that has been at the forefront of emerging insolvency and restructuring sectors such as crypto-assets.

Crypto-Assets

In late 2021, the BVI Commercial Court appointed joint liquidators over Torque Group Holdings Limited, which operated a Singaporean-run cryptocurrency trading platform. In assisting the liquidators, the BVI court confirmed the status of crypto-assets as assets or property and that they should be treated as such for the purpose of the BVI Insolvency Act. The Court recognised that ownership of crypto-assets comes down to who holds the private key that facilitates dealing with those assets. In the Torque case, Justice Wallbank (Ag) found that crypto-assets held in personal wallets of Torque users belong to the users whereas assets held in user trading wallets were held by Torque (and were therefore available to the liquidators and the credi-

tors of the company) as Torque held the private keys to those wallets. This was a useful and early determination by the BVI courts as to how crypto-assets would be dealt with following the appointment of liquidators over BVI entities that deal with crypto-assets.

Hot on the heels of this decision was the appointment by the BVI Commercial Court of joint liquidators over the collapsed crypto hedge fund, Three Arrows Capital. Three Arrows Capital was one of the most prominent crypto-asset hedge funds and its collapse highlights the extent of the global financial crisis of the digital asset market. The BVI Commercial Court acted quickly in appointing liquidators over the fund and steps are currently being taken to identify assets and achieve the best possible return for creditors.

The BVI continues to show that it is a market leader when dealing with distressed crypto-asset funds and trading platforms.

Chinese Restructuring

The BVI has taken a prominent position in assisting companies that have fallen on hard times following the Chinese property market collapse. This is due, in part, to a large amount of the foreign investment being structured through BVI companies.

Such companies have been assisted greatly by the BVI court's implementation and continuing acceptance of "light touch" provisional liquidators with a mandate to restructure a company's debts with a view to ensuring that a company

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can continue as a viable going concern while providing creditors with a better outcome than they could otherwise expect to receive in a liquidation (being the other realistic alternative). Additionally, in 2020 the BVI court granted a blanket statutory moratorium on prospective claims following the appointment of provisional liquidators in order to provide the company with essential breathing room to implement the restructuring without creditors taking action against the company. These decisions have brought the BVI in line with other common law jurisdictions, such as the Cayman Islands, and promote the concept of restructuring debt as an alternative to a liquidation.

The BVI court's continued support of light touch provisional liquidators has been vital when dealing with the BVI finance vehicles that provide funding to property developments in the People's Republic of China (PRC). The regime allows the company and its investors space to consider potential workouts without the fear of opportunistic creditors seeking to advance their own position by taking steps to enforce their debts before a restructuring plan can be agreed. This accentuates the innovative methods deployed by the BVI's legal and financial services professionals as well as the BVI court during times of financial crisis.

Sequana

While the BVI is a largely self-governing British Overseas Territory, its legal system is engrained in English common law and equitable principles. The courts follow precedent and, while not binding, English court judgments are routinely cited in argument and, in the absence of a good reason to depart from English jurisprudence, will usually be followed.

We cannot therefore comment on recent developments in the BVI insolvency space without referencing the key guidance given by the UK Supreme Court when it handed down its judgment in the case of *BTI 2014 LLC v Sequana SA & Ors* [2022] UKSC 25.

For the first time, the decision provides guidance from England's highest court on the point at which the directors' "creditor duty" is engaged (ie, when the obligation of the directors to take into account the interests of creditors arises).

The Supreme Court held that the interests of creditors will be paramount where the company is irretrievably insolvent. However, from the time that the company is insolvent, bordering on insolvency or an insolvent liquidation is probable, the interests of both shareholders and creditors need to be appropriately balanced by directors.

Interestingly, the Supreme Court confirmed that while the creditor duty exists, the duty is not a standalone duty that is owed to creditors directly. The creditor duty forms part of the directors' duty to act in the best interests of the company as a whole. As part of this duty, whose interests are at stake (who has "skin in the game": shareholders or creditors) alters depending on the company's financial position.

Importantly, the Supreme Court found that the creditor duty does not arise where there is merely a "real and not remote risk of insolvency at some point in the future" or, as held by the Court of Appeal, "when the directors know or should know that the company is or is likely to become insolvent". The Supreme Court was, even more so than the Court of Appeal, attune to the fact that companies may experience fluctuating economic fortunes but that directors need to be able

to take, within appropriate confines, commercial risk.

The key takeaways from the Supreme Court's decision are as follows.

- The precise point in time at which the duty to consider the interests of creditors arises remains highly fact specific.
- The creditor duty is not a standalone duty, but rather part of the duty of a director to act in the best interests of the company having regard to who has skin in the game at that point in time.
- Insolvency in the context of this analysis is not limited to cash-flow insolvency, but extends also to balance sheet insolvency.
- From the point in time that the duty to take into account the interests of creditors is engaged:
 - (a) the directors must strike a balance between the consideration of the interests of shareholders and creditors, until such time at which the company is irretrievably insolvent (when the creditors' interests are paramount); and
 - (b) shareholders cannot ratify the directors' breach of the duty (as it is recognised that creditors also have an economic interest at that point in time).
- Claims for breach of the creditor duty will subsist and exist independent of statutory claims that can be brought on behalf of companies (for example, liquidators' claims).
- While directors should always document the rationale and analysis behind entering into any transaction, where the creditor duty is engaged this becomes even more important so as to demonstrate later down the line that the relevant decisions were taken in good faith, with appropriate advice and consideration given to the interests of creditors.

- This decision left open the question of scope of liability and remedies in relation to a director's breach of the creditor duty – this will be another area where the law will need to develop.

Sanction Applications

Also in 2022, in the matter of Haode Investment Inc (in liquidation) and Summer Fame Limited (in liquidation), Justice Jack (Ag) of the BVI Commercial Court held that a liquidator's sanction application should be determined by reference to the circumstances existing at the time of the liquidator's decision, and that subsequent events should not be taken into account.

This is particularly relevant where the asset in question has appreciated in value after the liquidator's decision to sell. By the time the sanction application is heard, the liquidator may be able to sell the asset for a higher price in the market. In that case, the original decision to sell may no longer be in the best interests of the liquidation estate; and the liquidator (and the creditors and shareholders) may no longer support the sanction of the original decision.

Justice Jack held that the court will ignore subsequent events, even if it means rejecting a better outcome for the liquidation estate.

Justice Jack concluded that events after the sanction application should not be taken into account. This was because of the following (among other grounds).

- The court's decision would be arbitrary if subsequent events were taken into account. The hearing of a sanction application takes place after the liquidator's decision. Any appeal hearings take place later still. If the court's decision in each case is based on market

conditions as at the date of the hearing in question, the outcome merely depends on the hearing date and in that sense is arbitrary.

- The court's function on such an application is to review the liquidator's decision, which is in the past. The court would be stepping outside that remit if it took into account events after the decision was made. The court places itself in the shoes of the liquidators at the time the decision was made.

This decision, particularly in allowing interests extraneous to the liquidation estate to be factored into a sanction application, is important guidance in an area in which Justice Jack acknowledged there is a "surprising dearth of authority".

The decision may be welcomed by officeholders and counterparties seeking deal certainty in the liquidation context.

On the other hand, liquidators seeking more flexibility may look, where practicable and commercially viable, to negotiate terms allowing the sale price to fluctuate based on market conditions until the matter is finally determined by the court.

Further, a relevant consideration in this matter was the fact that the liquidators had already signed the Share Purchase Agreement and were contractually bound to issue the sanction application. The outcome may have been different if the liquidators were not yet subject to a binding contractual obligation.

It is also noteworthy that a "fiduciary out" clause (stating that the liquidator's obligation to obtain sanction is subject to their duties as a liquidator) would not appear to assist in such circumstances.

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