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Private Equity 2022

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British Virgin Islands: Law & Practice

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Maples Group

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BRITISH VIRGIN ISLANDS

Law and Practice

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1. Transaction Activity

1.1 M&A Transactions and Deals

The British Virgin Islands (BVI) has long been a favoured jurisdiction for asset holding and transaction structuring among private equity sponsors given the jurisdiction's tax neutrality, robust legal system and ease of use and entity set-up. For so long as these attractions remain, we expect the jurisdiction's popularity to continue and for BVI entities to retain a significant presence in M&A activity around the world.

1.2 Market Activity

While other jurisdictions including the Cayman Islands have been dominant in the world of offshore investment funds, the BVI continues to gain increasing popularity in the closed-ended sector of the industry. More and more single investor or single investment funds and "club deals" are being structured through the BVI, in addition to co-investment vehicles set up to hold a single investment for one or more investors within the framework of an existing closed-ended fund structure.

2. Private Equity Developments

2.1 Impact on Funds and Transactions

The rise in BVI investment fund activity has been driven in part by certain differences in regulation of closed-ended funds between the Cayman Islands and BVI, which are discussed elsewhere below.

Limited Partnership Act (As Revised) (the "LP Act")

In addition to such regulatory arbitrage, the introduction in the BVI in 2017 of refreshed partnership legislation in the form of the LP Act has also attracted new users to the jurisdiction. The LP Act replaced the somewhat under-utilised international limited partnership regime, and offers managers an extremely flexible and modern structuring tool for closed-ended investment funds.

The LP Act draws significant influence from the limited partnership regimes of other jurisdictions. BVI limited partnerships now share many of the features of those other offerings, including broad freedom of contract and the ability to limit the liability of passive investors.

BVI limited partnership general partners are also subject to substantially the same unlimited liability for limited partnership debts and liabilities, and statutory duties at all times to act in good faith and (subject to any express provisions to the contrary in the limited partnership agreement) in the interests of the limited partnership.

The BVI limited partnership regime demonstrates a handful of technical refinements over and above those of certain other popular jurisdictions in the investment fund industry. For example, while it is not uncommon for limited partnership legislation to permit the use of non-domestic entities as general partners, under the LP Act a non-BVI entity does not need to first register as a foreign company in the BVI to be eligible to act as general partner of a BVI limited partnership.

BVI limited partnerships may also be formed with a separate legal personality – an option that is not available in all other competitor jurisdictions. While this does not constitute them as separate bodies corporate, it does permit any charge created over an asset of a BVI limited partnership that is then registered with the Registrar of Limited Partnerships in the BVI (the "Registrar") to then have priority over any other charge over the

same asset that is either unregistered or registered subsequently.

The registration process for BVI limited partnerships is straightforward and requires only submission to the Registrar of a registration statement (signed by each general partner) containing certain prescribed limited partnership information, a letter of consent from the limited partnership's proposed registered agent in the BVI, and confirmation of whether the limited partnership is to be formed with separate legal personality, together with the payment of the requisite USD750 government registration fee. Registration will usually take up to four working days.

3. Regulatory Framework

3.1 Primary Regulators and Regulatory Issues

Securities and Investment Business Act (As Revised) (SIBA)

BVI funds are subject to regulation under SIBA if they constitute "private investment funds". A private investment fund is defined under SIBA as a company, partnership, unit trust or any other body that:

- collects and pools investor funds for the purpose of collective investment and diversification of portfolio risk; and
- issues fund interests that entitle the holder to receive an amount computed by reference to the value of a proportionate interest in the whole or in a part of the net assets of the company, partnership, unit trust or other body.

Accordingly, where there is no collective investment or diversification of portfolio risk, a fund will not technically constitute a private investment fund and accordingly will not be subject to regulation under SIBA. This is a notable driver behind the increased use of the BVI for single investor or single investment funds, club deals and co-investment vehicles as mentioned above – particularly where time is of the essence in deal structuring and execution.

SIBA imposes a general prohibition (with limited carve-outs) on the promotion of private investment funds and their carrying on of business unless and until recognised formally as such by the BVI Financial Services Commission (FSC).

In order to be eligible for recognition, the constitutional documents of a private investment fund must:

- specify that the offer of fund interests to investors must be made on a "private basis" only;
- restrict the number of shareholders or investors to 50; and
- restrict the offer to "professional investors" and a minimum initial investment of USD100,000 for each such investor.

The application process for recognition requires the payment of application fees and the submission to the FSC of a completed application form together with a number of supporting documents including the fund's constitutional documents, offering documentation, if any – if none, then an explanation for the lack of it must be provided – and valuation policy. The recognition process will typically take between five and seven working days following the submission of all required documents.

Private investment funds are subject to various ongoing obligations following recognition, including the retention of:

- a suitably qualified person – known as an "appointed person" – to take responsibility for undertaking the management, valuation and safekeeping of fund property;
- an auditor (although this need not be a local auditor based in the BVI), together with the submission to the FSC of annual audited accounts unless exempted under certain limited circumstances; and
- an authorised representative based in the BVI empowered to liaise with the FSC on a fund's behalf.

Any change to any of the foregoing personnel must be notified to the FSC within certain prescribed timeframes specified under SIBA.

Anti-money Laundering

The business of being a private investment fund constitutes "relevant business" for the purposes of the BVI Anti-Money Laundering (AML) Regulations (As Revised), and as a result private investment funds are subject to the BVI AML regime. In addition to the regime's know-your-client (KYC) investor onboarding requirements, a private investment fund must also appoint a suitably qualified money laundering reporting officer.

The officer, who may be internal or appointed externally, will act as the liaison with the BVI Financial Investigation Agency in relation to AML compliance matters, and will have responsibility for ensuring compliance by the fund's staff with AML law and regulation, and any internal reporting protocols and compliance procedures the fund may have adopted.

A BVI investment fund that does not constitute a private investment fund under SIBA and is not otherwise regulated in the BVI will not technically be subject to the jurisdiction's AML regime. However, it is both recommended and accepted market practice for unregulated funds of this nature to conduct investor onboarding KYC and due diligence as if subject to the regime.

US Foreign Account Tax Compliance Act (FATCA) and the OECD's Common Reporting Standard (CRS)

BVI funds, whether recognised as private investment funds or not, will also constitute "(foreign) financial institutions" under FATCA and CRS (as each is extended to the BVI). Accordingly, such investment funds are subject to the regimes' registrations, account due diligence and account reporting requirements.

4. Due Diligence

4.1 General Information

It is uncommon for substantive activity to be undertaken by BVI entities within the territory itself, so BVI due diligence will typically be limited to an entity's constitution and books and records and its compliance with applicable local law and regulation.

4.2 Vendor Due Diligence

It is not uncommon for a buyer to rely on vendor due diligence provided the transaction does not have any specific BVI regulatory or complex financial aspects where the buyer may prefer their own due diligence report to address these issues.

5. Structure of Transactions

5.1 Structure of the Acquisition

The structure for the acquisition of shares in a BVI Company will be driven, predominantly, by the structure of the shareholding. Where shares are closely held, the execution of a private treaty

sale and purchase agreement or the use of applicable drag-along provisions would be typical. In the event that shares are more widely held it would be common to see the use of the BVI statutory merger provisions. BVI statutory mergers have been a popular mechanic in the jurisdiction for many years being used in both private and public transactions. Court-sanctioned schemes of arrangement are possible in BVI but are not generally used. The terms of an acquisition will be driven by commercial rather than BVI-specific factors.

5.2 Structure of the Buyer

The single investor, single investment, club deal and co-investment fund structures that have become increasingly common in BVI will quite often invest into underlying portfolio investments directly and will themselves be party to transaction documentation. BVI closed-ended investment funds structured more as fully functioning blind pool funds – which still remain rarer – will, however, more typically establish separate acquisition structures for the downstream transactions to be undertaken by them as opposed to investing directly. Such special purpose vehicles will usually be corporate entities and may be formed in a wide range of jurisdictions, including BVI – the choice often being driven by broader tax considerations.

5.3 Funding Structure of Private Equity Transactions

There is no overarching norm for the financing of transactions undertaken by BVI funds – nor need there be as a matter of BVI law, given the inherent flexibility that BVI investment structures can offer. The choice of financing methodology will therefore usually be driven more by commercial (and cultural) considerations at the sponsor, fund and portfolio company level.

5.4 Multiple Investors

As noted above, club deal arrangements and co-investment vehicles are more and more frequently structured via BVI where they can avoid the need for private investment fund registration because they are established either for a single investment or a single investor.

Club deals will typically comprise a consortium of investors who will come together through a BVI aggregator vehicle to invest collectively and who will have management and economic rights apportioned between them as agreed contractually.

Classic co-investment structures (where they involve multiple investors), however, will usually have investors take passive stakes as limited partners, with the vehicles then investing alongside the main private equity funds in which the co-investment vehicle limited partners are also separately invested.

6. Terms of Acquisition Documentation

6.1 Types of Consideration Mechanisms

There is generally no restriction on the type of consideration that can be offered on a private treaty sale or negotiated offer. Consideration can therefore include, among other things, cash, loan notes and shares. The structuring of the consideration will be driven and agreed by the parties.

6.2 Locked-Box Consideration Structures

There is no common practice in BVI; this will be driven and agreed by the parties in each transaction.

6.3 Dispute Resolution for Consideration Structures
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.4 Conditionality in Acquisition Documentation
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.5 "Hell or High Water" Undertakings
There is no common practice in BVI; this will be driven and agreed by the parties in each transaction.

6.6 Break Fees
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.7 Termination Rights in Acquisition Documentation
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.8 Allocation of Risk
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.9 Warranty Protection
Warranty coverage in transactions in the BVI is generally limited to title of target shares or assets, capacity and authorisation to enter into the transaction, solvency and accuracy and completeness of information provided to the buyer.

6.10 Other Protections in Acquisition Documentation
There is no typical practice in BVI; this will be driven and agreed by the parties in each transaction.

6.11 Commonly Litigated Provisions
Litigation of private equity transactions are rare in BVI. The most likely potential for litigation would be the exercise of dissenter's rights on a statutory merger.

7. Takeovers

7.1 Public-to-Private
The market for take private transactions involving BVI companies continues to be active, these often involve private equity parties. There have been a number of take privates in Asia involving Chinese ListCos and in the UK involving companies listed on the London Stock Exchange.

7.2 Material Shareholding Thresholds
There are no material shareholding or disclosure thresholds relevant under BVI law. Where the founders (and others) are leading a listed take private transaction, disclosure around shareholdings in a target would usually be included in the offer documents for the transaction.

7.3 Mandatory Offer Thresholds
There are no material offer thresholds relevant under BVI law.

7.4 Consideration
Both cash and shares are commonly used in BVI.

7.5 Conditions in Takeovers
Any conditions to an offer will be determined by the jurisdiction in which the business operates and relevant market considerations rather than

by any BVI-specific factors. There are no restrictions, as a matter of BVI law, as to what deal security measures a bidder can seek; break fees, match rights, force-the-vote provisions and non-solicitation provisions would all be permitted. However, it should be noted that, in agreeing any such provisions, the directors of a BVI company must act in accordance with their fiduciary duties, ie, their duties to act honestly, in good faith and in the best interests of the company.

7.6 Acquiring Less Than 100%

There are no restrictions under BVI law in respect of governance rights for a shareholder holding less than 100% of the issues shares of a company. As a matter of BVI law, absent any alternate provisions or class rights in the constitutional documents, a shareholder acquiring a majority of shares in a BVI company can amend the memorandum and articles of association, approve a statutory merger (subject also to board approval) and put the company into voluntary solvent liquidation.

There are two statutory mechanisms to squeeze out minority shareholders under BVI law. Members of a company holding 90% of the votes of the outstanding shares entitled to vote may give written instructions to the company directing it to redeem the shares held by the remaining shareholders. A squeeze out will give rise to the right of the minority shareholder to dissent and receive payment for "fair value" of their shares.

In addition, an alternate option is to squeeze out the minority by way of statutory merger as BVI law provides that a parent company (meaning a company that owns at least 90% of the outstanding shares of each class of shares in another company) may merge with its subsidiary without the need for shareholder approval. While it is unclear if, in the context of a parent subsidiary merger, dissent rights are available to a minority shareholder, it would be prudent to make such right available to avoid any implication that the statutory merger route was used (as opposed to the statutory squeeze out) in order to deny the minority shareholders the opportunity to dissent.

7.7 Irrevocable Commitments

Where an offer is recommended by the board of directors of the target, obtaining irrevocable undertakings or commitments from the main shareholder(s) is common. There is no common practice in BVI as to the timing or nature of the undertakings which will be determined and agreed by the parties in each transaction.

7.8 Hostile Takeover Offers

Hostile takeovers of BVI companies are permitted but rare. While some offers may start out being hostile, they generally evolve into a recommended offer.

The flexibility of BVI companies means that they are able to amend their constitutional documents to incorporate protective provisions in line with investor expectations. It is common for public BVI companies to adopt provisions and protections from the takeover codes of the relevant jurisdiction of the exchange upon which their shares are listed. Such provisions provide comfort to investors and can also deter unwelcome bids.

8. Management Incentives

8.1 Equity Incentivisation and Ownership

There is no common practice in BVI; any terms will be determined and agreed by the parties in each transaction.

8.2 Management Participation
See **8.1 Equity Incentivisation and Ownership**.

8.3 Vesting/Leaver Provisions
See **8.1 Equity Incentivisation and Ownership**.

8.4 Restrictions on Manager Shareholders
See **8.1 Equity Incentivisation and Ownership**.

8.5 Minority Protection for Manager Shareholders
See **8.1 Equity Incentivisation and Ownership**.

9. Portfolio Company Oversight

9.1 Shareholder Control
The extent and scope of control and governance rights enjoyed by BVI closed-ended funds at the portfolio company level will often be driven by the relative size of the stake acquired, as well as by the market norms of where the portfolio company is situated. This will therefore not usually be a question driven by BVI-specific matters.

9.2 Shareholder Liability
The "corporate veil" effectively separates the legal person who owns a company from the company itself. A duly incorporated BVI company is a legal entity separate from those who incorporate it, with rights, liabilities and property of its own. This is also the position within a group of companies where the fundamental principle is that each company in a group is a separate legal entity possessed of separate legal rights and liabilities.

Under BVI common law, the circumstances where a BVI court will allow the corporate veil to be "pierced" or "lifted", so as to hold a member of a company liable for the company's acts, are rare and limited. Such circumstances include, for instance, where a company is misused as a device or façade to conceal wrongdoing, or is used for an illegal or immoral purpose.

9.3 Shareholder Compliance Policy
The AML compliance obligations to which a closed-ended BVI fund regulated as a private investment fund is subject will extend to capture its investment activity and not just activities at the fund level itself. For this reason, the operators of such funds will commonly seek to ensure that portfolio companies have in place satisfactory compliance measures in this regard.

Practice for unregulated closed-ended funds in the BVI is more divided, given the jurisdiction's AML regime does not technically apply.

10. Exits

10.1 Types of Exit
There is no typical practice in BVI with private equity funds being established with a wide variety of exit terms. "Dual track" exits are uncommon.

10.2 Drag Rights
It is common to see the inclusion of drag rights in the constitutional documents of BVI companies. There are no typical terms in BVI; these will be determined and agreed by the commercial parties in each transaction rather than by any BVI-specific factors.

10.3 Tag Rights
As with drag rights, the use of tag rights is common in BVI. Again, there are no typical terms in BVI; these will be determined and agreed by the parties in each transaction rather than by any BVI-specific factors – legal or otherwise.

10.4 IPO

The use of BVI entities to effect IPOs on a variety of international exchanges is a well-trodden path. However, the terms of any lock-up arrangements or ongoing relationships will be determined by reference to the relevant exchange and jurisdiction rather than by any BVI-specific factors.

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