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# The BVI Company in a Russian Context



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**ACCORDING TO THE LATEST STATISTICS** released by the BVI Financial Services Commission, incorporation levels for BVI companies are now back to the levels seen before the global financial crisis. Perhaps unsurprisingly, volumes continue to be driven in large part by the BRIC economies, with Russia and CIS-based clients being a key reason for this success.

Historically, the popularity of the BVI with Russian clients was due to the double-taxation treaties in place between Cyprus and many of the ex-Soviet states (Russia and Ukraine being the most prominent), where BVI companies formed part of so-called 'sandwich structures' (with the Russian asset at the bottom, which asset is wholly owned by a Cypriot holding company, which, in turn, is wholly owned by a BVI business company). Regular exposure to BVI companies as a result of these structures has also seen clients in Russia using BVI companies independently of Cypriot vehicles, often where taxation benefits are not the primary objective and where, for example, they wish to take advantage of the more straightforward company law regime in place in the BVI, as well as the additional layers of confidentiality in place for BVI companies (where the registers of directors and shareholders are not in the public domain, whereas they are in Cyprus).

## Why the BVI?

Until recently, it was not possible under Russian law for Russian companies to enter into shareholders' agreements. To a

large part, this reflected a cultural reality in Russia that there was a suggestion of bad faith if joint venture parties felt the need to document their agreement, rather than rely upon the more informal 'gentleman's agreement' that had been prevalent prior to the adoption of the market economy in Russia. With the rapid growth of the Russian economy, the need for a more formal approach to joint ventures had become apparent. Top US and UK law firms that had opened offices in Moscow were regularly advising their clients to enter into shareholders' agreements, often without a suitable Russian corporate vehicle which could validly execute them.

At the same time, the sandwich structures noted above were becoming more and more popular. In the context of a joint venture, while many joint ventures were documented under Cypriot law, there were some perceived benefits to using the BVI company at the top of the structure: BVI law has deliberately pitched its companies' legislation (the BVI Business Companies Act, 2004) to be as flexible as possible, with (for example) no prohibition on financial assistance as existed historically under Cypriot law. Perhaps of more importance to Russian clients was the confidentiality point made above, as this is often a key driver for clients in the Russian market. The fact that the BVI is a British dependency, with a robust legal system and with the Privy Council in London as the ultimate appellate court are also very appealing to clients in Russia.

## Documenting the Agreement

As shareholders of BVI companies can document their agreement under the governing law of their choice, those US and UK law firms mentioned above could prepare detailed joint venture or shareholders' agreements using their own English or US law-governed precedent documents, subject to the caveat that those documents must not contravene BVI law (which, given the flexibility of BVI law, is rare). Russian clients would also take comfort from the fact that BVI companies can submit to international arbitration, often a key commercial point for the parties to a joint venture involving Russian parties.

Once the shareholders' agreement has been agreed, the next step is to tailor the memorandum and articles of association (M&As) (being the constitutional documents of the BVI company, which are in the public domain and on file with the Registrar of Corporate Affairs in the BVI) to track the commercial provisions of the shareholders' agreement.

## Getting the Balance Right

This is always a fine balance to strike for the BVI lawyer drafting the M&As; on the one hand, the more the shareholders' agreement and M&As are aligned, the more options the joint venture parties have on a dispute, with a party being able to proceed with an action based on either a breach of the shareholders' agreement (with the contractual remedies available to them) or in the BVI courts based on the M&As (with additional constitutional remedies available

under BVI law for breaches of the M&As).

On the other hand, with the M&As being in the public domain, parties are often sensitive to disclosing too much of the commercial deal, which is a particular concern for clients in the Russian market, where resistance is especially keenly felt. As a result, we see a variety of approaches being taken to documenting BVI joint ventures to provide for the bespoke requirements of the particular deal in the Russian market.

### Dispute Resolution

As ventures have matured inevitably some relationships have soured and there have been particularly high profile fallout in the energy and telecomms sectors over the past number of years. This has put to test the remedies available to BVI joint venturers and the specialised Commercial Court, set up as a forum in which the disputes can be determined.

### When Disputes Occur?

Disputes between shareholders at the level of the BVI company are often driven by one party's attempt to gain control of an underlying asset either directly or through its downstream subsidiaries. This has been attempted through a majority shareholder seeking to dilute others interests, the creation of classes of preferred shares or seeking to exercise influence at board level through the manipulation of board appointments. In the worst cases, the underlying asset may have been dissipated from the structure into the hands of a third party.

### Tackling Oppression: Unfair Prejudice Actions

A joint venturer who considers the affairs of the company are being or are likely to be, conducted in a manner that is, or is likely to be oppressive, unfairly discriminatory or unfairly prejudicial can seek a raft of remedies (section 184I of the BC Act). The Court can make any order it thinks fit, including a forced buy-out, setting aside previous decisions, compensation payments or in extreme cases, the appointment of a receiver or liquidator.

### Derivative actions

The proper claimant for a wrong done to

the company (for example, an asset being stripped out) is usually the company. However, where the company itself will not take action against the wrongdoer, BVI law allows a minority shareholder to bring a derivative action against the wrongdoer, ie one brought in the name of the company itself. If permission for this kind of claim is granted by the Court, the shareholder can enforce a claim by, or rectify a wrong done to, the company, thereby indirectly protecting his own shareholding. This can be especially useful in tracing and following proceedings where a JV asset has been removed from the structure.

### Appointing a Liquidator

The Insolvency Act 2003 provides that the Court may appoint a liquidator, on the application of a member of the Company, if the Court is of the opinion that it is just and equitable to do so. Although the grounds for a just and equitable appointment are wide, in the context of a JVV the main grounds relied on are usually fraud, deadlock in the management of the company, or breakdown of trust and confidence in a quasi-partnership situation. Where urgent relief is needed to protect assets, the Insolvency Act also allows the appointment of a provisional liquidator in order to speedily take control of the company. A liquidator enjoys a suite of powers that include the ability to revisit certain transactions that may have been motivated to prefer creditors or seek redress against directors for fraudulent or insolvent trading.

### Freezing Orders

BVI Courts also have the ability to freeze assets held by BVI companies, something which is frequently used to preserve shares and other assets which may have been transferred away from a JVV and into a third party's hands. In addition to "standard" freezing injunctions, the development of free-standing 'Black Swan' freezing injunctions means that BVI courts can now also grant freezing injunctions in support of proceedings commenced abroad. This is particularly useful for Russian-owned JVVs as the BVI Court can move quickly to provide complementary relief to proceedings that have flared up in other jurisdictions.

### The Silent Treatment

Where a quorate shareholders' meeting is incapable of being held (for example, because one shareholder deliberately fails to attend a shareholders' meeting in order to paralyse the company's decision-making), section 86 of the Act can provide a useful remedy to order a meeting of members to be held and conducted in such manner as the Court orders where it impracticable to call or conduct a meeting in the manner prescribed by the Memorandum or Articles, and it is in the interests of the members that a meeting be held.

The Court could in theory order that a shareholders' meeting be held with a reduced quorum requirement, although it should be noted that this would likely follow a protracted period of frustration.

### Other Pro-Shareholder Provisions

The BC Act also contains a number of miscellaneous pro-shareholder protective provisions, including the following:

**S.175:** Shareholder approval for disposal of assets: This section provides that (subject to the M&As) any sale of more than 50 per cent in value of the assets of the company have to be approved not only by a resolution of directors but also by a resolution of shareholders;

**S.184B: Power to restrain conduct.** If a company or a director of a company engages in conduct that contravenes the Act or the M&As, the Court has the power, on the application of a member or a director, to make an order directing the company or director to comply with, or restraining the company or director from engaging in, the conduct that would contravene the Act or the M&As.

**S.179: Payment of fair value for shares:** Any member of a company is entitled to payment of the fair value of his shares upon dissenting from a range of decisions, including merger, consolidation, asset sales in certain conditions and plans of arrangement.

In the same manner that BVI law provides a flexible and straightforward platform for Russian joint ventures to prosper, it brings a safe and effective means of resolving disputes between the parties. ■