



Guide to Taking Security in the British Virgin Islands

TABLE OF CONTENTS

PREFACE	2
1. TAKING SECURITY IN THE BVI	3
2. SECURITY OVER SHARES.....	4
3. OTHER SECURITY INTERESTS	6
4. RIGHTS OF FOREIGN CREDITORS	7
5. ENFORCEMENT CLAIMS BY SECURED CREDITORS/REMEDIES.....	8

PREFACE

This Guide summarises the process of taking security and the enforcement of security in the British Virgin Islands (“BVI”). The BVI is an overseas territory of the United Kingdom offering the benefits of a well established legal system, favourable tax treatment and a creditor friendly insolvency regime.

This Guide focuses on the legislative and regulatory framework for the taking of security over both real (or “immovable”) and personal (or “moveable”) property; the methods by which a creditor may register a charge; the rights of foreign creditors; and the enforcement of claims by secured creditors in the BVI. This Guide also discusses the methods by which a creditor may enforce security in the BVI granted pursuant to an instrument governed by a law other than that of the BVI.

It is recognised that this Guide will not completely answer the detailed questions that clients and their advisers may have; it is intended to provide a summary of the BVI’s legal and regulatory environment in relation to taking security. This Guide is, therefore, designed as a starting-point for a more detailed and comprehensive discussion of the issues.

Whilst we have made every effort to ensure the accuracy of the statements made herein, we accept no liability for any errors. In all cases specialised advice from counsel qualified in the BVI should be obtained.

Appleby
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1. TAKING SECURITY IN THE BVI

Under the BVI Business Companies Act, 2004 (as amended) (the “Act”), and subject to its constitutional documents (memorandum and articles of association), a BVI company may, by an instrument in writing, create a mortgage, charge or other encumbrance over any of its assets situated in any part of the world in accordance with the law of any jurisdiction of the company’s choice, and the mortgage, charge or other encumbrance will be binding on the company to the extent, and in accordance with the requirements, of the chosen law.

Security granted by a BVI company pursuant to a mortgage, charge or other encumbrance must be recorded in the company’s register of charges, and may be registered publicly. The registration regimes provided for under the Act (private and public) do not apply, however, to real property situate in the BVI or to ships and/or aircraft, which are discussed below.

(a) Private Registration of Charges

Under §162 of the Act, a BVI company must keep, at the company’s registered office or at the office of its registered agent, a register of all relevant charges created by the company showing:

- where the charge is a charge created by the company, the date of its creation or, if the charge is a charge existing on property acquired by the company, the date on which the property was acquired;
- a short description of the liability secured by the charge;
- a short description of the property charged;
- the name and address of the trustee for the security or, if there is no trustee, the name and address of the chargee;
- unless the charge is a security to a bearer (see below), the name and address of the holder of the charge; and
- details of any prohibition or restriction (negative pledge), if any, contained in the instrument creating the charge on the power of the company to create any future charge ranking in priority to or equally with the charge.

A company that contravenes these requirements commits an offence and is liable on summary conviction to a fine of \$5,000.

(b) Public Registration of Charges

Although not mandatory, an application may be made by the chargor company itself or by the lender (as chargee) to the BVI Registry of Corporate Affairs (the “Registrar”) under §163 of the Act to register the charge in the Register of Registered Charges of the BVI Company as maintained by the Registrar. This statutory right for the chargee to register a charge can prove useful to a secured creditor.

Provided the registration requirements of the Act have been complied with (by filing the relevant forms and paying a registration fee of US\$100), the Registrar will register the charge in the Register of Registered Charges of the BVI Company and issue a certificate of registration of the charge, a copy of which will be sent to the company and to the chargee stating the date and time on which a charge was registered. A certificate of

registration is conclusive proof that the requirements of the Act have been complied with and that the charge referred to in the certificate was registered on the date and time stated in the certificate.

There is no time limit within which details of the charge must be entered on the company's register of charges or in the company's Register of Registered Charges at the Registry. Failure to enter details on either register does not affect either the validity or the enforceability of the charge. As discussed above, however, a registration in the company's Register of Registered Charges at the Registry determines the priority of charges created on or after 1 January 2005.

(c) Variation and Release of Charge

A variation in the terms of a charge may also be registered following initial registration by means of an application made by (or on behalf of) either the company or the chargee and the Registrar will issue a certificate of variation of the charge in this regard.

Where a registered charge ceases to affect the charged property of the company, the company must file a notice with the Registrar specifying the property that has ceased to be affected by the charge in the approved form and must be signed by or on behalf of the chargee. Once filed, the Registrar will issue a certificate of cessation.

(d) Priority Rules

A charge on the property of a company registered pursuant to §163 of the Act has priority over subsequently registered charges and any unregistered charges.

Charges created prior to the coming into force of the Act (1 January 2005) continue to rank in the order which they would have ranked had §166 of the Act not come into force, and where they would have taken priority over a charge created on or after 1 January 2005, they will continue to take priority after 1 January 2005 by reference to the register of charges created by the company and maintained at the company's registered office.

Notwithstanding the foregoing, the order of priorities of charges is subject to any express consent of the holder of a charge that varies the priority of that charge in relation to other charges that it would, but for the consent, have had priority over or any agreement between chargees that effects priorities in relation to the charges held by the respective chargees. Further, a registered floating charge is postponed to a subsequently registered fixed charge unless the floating charge contains a prohibition or restriction (negative pledge) on the power of the company to create any future charge ranking in priority to or equally with the charge.

2. SECURITY OVER SHARES

It is common for borrowing companies to provide security over the shares in companies of the borrowing group, including BVI entities, either by taking legal or equitable security over the shares.

Pursuant to §66 of the Act, a mortgage or charge over the shares of a BVI company need not be in any specific form but must clearly indicate:

- the intention to create a mortgage or charge; and
- the amount secured by the mortgage or charge or how the amount is to be calculated.

Where the governing law of a mortgage or charge is not BVI law:

- the mortgage or charge must be in compliance with the requirements of its governing law in order for the mortgage or charge to be valid and binding on the company; and
- the remedies available to the mortgagee or chargee will be governed by the governing law and the instrument creating the mortgage or charge.

Alternatively, where the governing law of a mortgage or charge of shares is BVI law, in the case of a default, the mortgagee or chargee is entitled to the following remedies:

- subject to any limitations or provisions to the contrary in the instrument creating the mortgage or charge, the right to sell the shares, and
- the right to appoint a receiver who, subject to any limitations or provisions to the contrary in the instrument creating the mortgage or charge, may (i) vote the shares, (ii) receive distributions in respect of the shares, and (iii) exercise other rights and powers of the mortgagor or chargor in respect of the shares, until such time as the mortgage or charge is discharged.

The powers of the receiver will be established by the terms of the share charge and will normally include the power to sell the secured shares. Pursuant to §118 of the BVI Insolvency Act, 2003 as amended (the “Insolvency Act”), a receiver is required to give notice to the Registrar upon appointment and, if the BVI company is regulated by the BVI Financial Services Commission (the “FSC”), to the FSC also.

The remedies provided by §66 of the Act, however, are not exercisable until (i) a default has occurred and has continued for a period of not less than thirty days, or such shorter period as may be specified in the instrument creating the mortgage or charge, and (ii) the default has not been rectified within fourteen days or such shorter period as may be specified in the instrument creating the mortgage or charge from service of the notice specifying the default and requiring rectification.

(a) Legal Security over Shares

Legal security over shares requires the transfer of the charged shares to the chargee and entry of the chargee in the chargor’s register of members as the holder of title to the charged shares. As a result, the use of equitable security is more common.

(b) Equitable Security over Shares

Equitable share security will require the chargor, at a minimum, to deliver signed and undated instruments of transfer for the charged shares, existing share certificates in relation to the charged shares and undated resignation letters signed by the directors to the chargee. Often BVI companies will provide in their memorandum and articles of association that the directors of the company retain the right to refuse the transfer of shares and if this is the case, these provisions should be altered as a condition of the share security (or at least, formal confirmation that the directors will not refuse the transfer of shares on enforcement should be obtained). Upon enforcement, the chargee ought then to be able to date the instruments of transfer and the director’s resignation letters, enabling the chargee to become the shareholder of the charged shares (once the register of members is amended to reflect the new shareholder) and to appoint new directors. In the absence of cooperation from the chargor company, an application to court may be required.

Under §66(8) of the Act, a notation of the share security and the chargee's interest in the shares may be made in the register of members of the BVI company whose shares have been charged and a copy of the annotated members' register may be filed with the Registrar. The Act is silent as to the legal effect of the entry of the notation on the members' register but it may be deemed to be constructive notice to third parties who inspect the register. A notation may only be carried out by the chargor and, therefore, if the chargee desires such notation to be made, it is important that the instrument creating the mortgage or charge contain a covenant requiring the chargor to attend to the notations and registrations and provide the chargee with documentary evidence that they have been carried out.

3. OTHER SECURITY INTERESTS

(i) Real Property

Mortgages may be made by way of sale, demise or assignment subject to a proviso for reassignment and an equity of redemption. No interest in land in the BVI, however, including a charge, can be acquired by any person not deemed to belong to the BVI unless such person has a land holding license under the Non-Belonger Land Holding Regulation Act (Cap. 122) (a "Land Holding Licence").

Security over land and buildings must be effected by way of legal charge, in statutory form, executed and attested in the manner required by the BVI Registered Land Ordinance and registered at the BVI Land Registry.

(ii) Personal Property

The nature of a security interest granted over personal property will be determined by:

- the property interest of the party granting the security at the time the security interest is granted;
- the terms of the security document; and
- the nature of the property being encumbered.

Further, an absolute assignment in writing of any debt or other legal chose in action, where notice is given to the debtor or other contracting party is deemed effective.

(iii) Negotiable Instruments

A pledge of a negotiable instrument will be effective. Where the chargor is a BVI company it is advisable to register the security interest pursuant to the Act as discussed above.

(iv) Cash

A bank deposit may be assigned by way of security, provided the terms of the deposit agreement permit this. A secured party who is taking security in a bank deposit maintained with a third party bank should consider whether the bank in which the deposit is held could set-off any other obligations due from the party granting the security to that bank.

(v) Goods

A charge over goods and chattels in the BVI can be effected by way of a registered bill of sale. Where the goods are capable of actual delivery, a common law pledge or lien will also be effective.

(vi) Contracts/Insurance Policies

The benefit of a contract may be assigned by way of security. The assignment would have to be equitable and notice of the assignment would need to be given to the other contracting party. The assignment can extend to all rights, benefits and interests in the charging company at present and in the future, including debts and claims present and future in connection with the contract and claims against insurers. The proceeds of an insurance policy may be charged by way of assignment in the same manner as the benefit of any other contract.

(vii) Intellectual Property

If a charge is granted by a BVI company then it is advisable to register the security interest pursuant to §163 of the Act as discussed above. In addition, the security interest in a trademark may be recorded under the Trade Marks Act. Registration of a security interest under the Trade Marks Act, however, may only be recorded against the mark itself and not the proprietor of the mark.

(viii) Ships

BVI shipping law is governed in part by the United Kingdom Merchant Shipping Act 1988, as extended to the BVI.

A secured party who takes a security interest in a ship registered in the BVI should register that security interest with the Registry of Shipping. Priority among registered charges is determined by order of registration. The usual form of security is a mortgage. The form is the same as that used for ships registered in the UK.

(ix) Aircraft

Registration of BVI aircraft is effected through the Civil Aviation Authority for the BVI. Charges over BVI registered aircraft are usually effected by way of a registered bill of sale.

4. RIGHTS OF FOREIGN CREDITORS

As a general principle, foreign creditors are not subject to any legal disability under BVI law, due to their foreign status. However, a creditor who takes security over land situate in the BVI must hold a Land Holding License.

Often the rights of foreign creditors are expressed to be governed by a law other than BVI law. As a general principle, BVI courts would uphold the choice of governing law. Where the parties expressly select the law of the contract, the courts will give effect to that choice, except for procedural, revenue or penal laws or those laws the application of which would be inconsistent with public policy considerations, as they apply to a BVI company.

5. ENFORCEMENT OF CLAIMS BY SECURED CREDITORS / REMEDIES

(a) Real Property

- (i) Power of Sale: Under BVI law, after a specified period of default, a lender exercising a power of sale has the power, by deed, to convey the property sold, free from all interests and rights to which the mortgage has priority, but subject to all estates, interests and rights which have priority to the mortgage. Therefore, a first mortgagee selling a property may do so free of subsequent mortgages. A subsequent mortgagee may, however, only sell the subsequent mortgagee's interest in the property. If the subsequent mortgagee wishes to sell the property unencumbered, he will either have to redeem any prior mortgages, or come to some arrangement with the prior mortgagee to release the interest being sold.

The sale proceeds received by the selling lender, after he has discharged any prior encumbrances (such as mortgages) to which the sale is not made subject, or after he has paid into court a sum to meet any prior encumbrance, must be held by him on trust and must be applied in strict order: first, to pay all costs, charges and expenses properly incurred by him; second, to discharge the principal, interest, costs, and other money, if any, due under the mortgage; and the residue of the mortgaged money must be paid to the person entitled to the mortgaged property, or authorised to give receipts from the proceeds of the sale of it.

A purchaser need not enquire whether the power of sale has arisen, or indeed whether the mortgagee is otherwise justified in selling. Statute provides that where a conveyance is made in exercise of a power of sale, the title of the purchaser shall not be impeachable on the ground that no case had arisen to authorise the sale, or the due notice was not given, or that the power was otherwise improperly or irregularly exercised.

- (ii) Foreclosure: A power of sale does not affect the lender's right of foreclosure. Foreclosure can only be exercised by court order. Technically, foreclosure means that the borrower's equity of redemption is extinguished by the court, leaving the lender as both legal and equitable owner of the property. Subsequent mortgagees' rights would be extinguished if they did not oppose the order and, if they did oppose, the most likely result would be an order for sale instead.
- (iii) Taking possession: Because a lender has a legal estate, he is entitled to take possession and may take it, for example, by directing tenants to pay rents to the lender.

A mortgagee in possession, however, has a duty to account strictly, meaning that lenders usually wish to avoid taking possession accidentally. The usual object in taking possession is either to sell, or to intercept the rents and profits. The lender must not receive any personal advantage beyond what is due to him i.e. the lender must account not only for what he receives, but also for all that he ought to have received, had he managed the property with due diligence.

- (iv) Appointment of Receiver: Receivers are appointed in order to receive rents and to manage property. This is therefore a remedy similar to taking possession, without the liability of being a mortgagee in possession. The receiver is deemed to be the agent of the borrower, and the borrower is solely responsible for the receiver's acts or defaults, unless the mortgage deed provides otherwise. The receiver has the power to demand and recover all the income of the property of which he is receiver, by action or otherwise, in the name either of the mortgagor or the mortgagee, to the full extent of

the estate or interest which the borrower can dispose of, and to give effectual receipts. A person paying money to the receiver shall not be concerned to enquire whether any case has happened to authorise the receiver to act.

The receiver is entitled to retain money out of that received by him for both his remuneration and to satisfy all costs, charges, and expenses incurred by him as receiver. This commission is to be at a rate of interest specified in his appointment, and may not exceed the statutory rate on the gross amount of all monies received. If no commission is specified, then the commission is at the statutory rate on the gross amount, or such higher rate as the court thinks fit to allow, on an application made to it for that purpose.

The receiver must apply all money received by him in the following order:

- in discharge of all rents, taxes and outgoings, which affect the mortgaged premises;
- in keeping down all annual sums or other payments, and the interest on all principal sums, having priority to the mortgage under which he is appointed;
- in payment of his commission, and in paying the premiums on fire, life, and other insurance which are properly payable under the mortgage deed or under statute, and the cost of exercising necessary or proper repairs directed in writing by the mortgagee;
- in payment of the interest due under the mortgage; and
- in or towards discharge of the principal if so directed in writing by the mortgagee.

The residue of the money, if any, is to be paid by the receiver to the person who, but for the possession of the receiver, would have been entitled to receive the income of the property, or who is otherwise entitled to the property.

(b) Personal Property

- (i) **Judicial:** Secured creditors do not normally require the assistance of the court in order to enforce security. Hence a creditor under a debenture or other security instrument including a floating charge may proceed to appoint a receiver pursuant to the terms of the instrument.
- (ii) **Receivership:** Receivers and administrative receivers may be appointed by the court or pursuant to contractual rights.

The procedure for the private appointment of a receiver depends on the terms of the security document. Typically there will be provision for various events of default upon which the security holder becomes entitled (among other things) to appoint a receiver.

Provision is also made under BVI law for the appointment of an “administrative receiver” i.e. a receiver of the whole or substantially the whole of the business undertaking and assets of a company appointed by a floating charge holder.

(iii) Set-Off

At the commencement of liquidation proceedings, mandatory set-off rules as contained in the Insolvency Act apply to all cross-claims provided they are mutual and measurable in monetary terms. Where, prior to the appointment of a liquidator, there have been mutual credits, mutual debts or

other mutual dealings between a debtor and a creditor, claiming or intending to claim in insolvency proceedings:

- an account will be taken of what is due from each party to the other in respect of those mutual credits, mutual debts or other mutual dealings;
- the sum due from one party shall be set-off against the sums due from the other party; and
- only the balance of the account, if any, is payable to the debtor.

These provisions are mandatory and the parties do not have the discretion to dispense with the set-off rules. However, the set-off rules do not apply to claims where a creditor has actual notice that the insolvent party was insolvent at the time the creditor advanced credit to or acquired a claim against the insolvent party.

For more specific advice on Taking Security in the British Virgin Islands, we invite you to contact one of the following:

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