

BRIEFING NOTE

2020

COVID-19: A practical guide to frequently asked offshore law questions

Coronavirus (“**Covid-19**”) is continuing its spread across the world, with more than 68 million confirmed cases in 220 countries and more than 1.5 million deaths. In response, governments worldwide have implemented far ranging containment measures, such as travel restrictions, mandatory quarantine and social distancing. Many of our clients have additionally activated their business continuity and contingency plans and put in place alternate workplace arrangements and/or heightened measures to ensure the health and safety of their employees. These policies have disrupted “business as usual” and our clients with British Virgin Islands (“**BVI**”) and Cayman Islands companies have faced a number of challenges accordingly.

In this brief guide, we address certain of the most frequently asked BVI and Cayman Islands law questions that our clients have posed in connection with the difficulties that Covid-19 presents in the context of corporate and finance transactions. We also offer some practical guidance and considerations with respect these issues.

1. Meetings

Subject to a company’s memorandum and articles of association (“**M&A**”), BVI and Cayman Islands law does not impose any restrictions on where a meeting of the board of directors and/or shareholders can be held. That being said, the board of directors should always take into account any tax and economic substance implications (discussed below) when determining the location of a meeting.

In the event it is not possible to hold a face-to-face meeting of the board of directors and/or the shareholders, BVI and Cayman Islands law does offer the following alternative options subject to the M&A of the relevant company permitting such options:

- i. A meeting of the board of directors and/or the shareholders may be held by telephone or by other electronic means so long as those persons participating can hear each other. “Electronic means” typically includes video conferencing facilities, Skype, Zoom, Teams and any similar electronic service. As a practical matter, it is important to ensure that the notice of the relevant meeting includes all information that is necessary for the participants to attend via the chosen electronic platform.

- ii. The board of directors and/or shareholders (as appropriate) may pass resolutions unanimously in writing. BVI law also permits written resolutions to be passed by a simple majority provided that is expressly permitted by the M&A. Any written resolutions may be executed in counterpart. If the relevant directors or shareholders (as applicable) are located in different time zones and timing is not critical, passing resolutions in writing may be appropriate.

The following additional options should also be kept in mind for the purposes of facilitating a meeting with the required quorum:

- i. A shareholder of a BVI or Cayman Islands company may appoint a proxy who may speak and vote on behalf of that shareholder at a meeting. The instrument appointing the proxy should be in writing and comply with any requirements of the relevant company's M&A.
- ii. If permitted by the relevant company's M&A, a director of a BVI or Cayman Islands company may appoint an alternate to exercise all of the powers and perform all of the responsibilities of that director. The instrument appointing the alternate should be in writing and comply with any requirements of the relevant company's M&A.

2. Economic substance

The BVI International Tax Authority (“**BVI ITA**”) has confirmed that only those board meetings relating to a BVI company's “core income generating activities” are required to be held in the BVI. If, owing to Covid-19, this is not achievable, BVI entities should retain documentary evidence with reasons. Please note that appointing alternate directors in the BVI and/or hosting virtual board meetings as detailed above may assist in achieving compliance. The BVI ITA has also confirmed that all directors do not have to attend board meetings in the BVI – only as many as are required to make the relevant meeting quorate.

The Cayman Islands' Department for International Tax Cooperation has confirmed that it will adopt a case-by-case approach in determining whether an entity has passed the Economic Substance test in its reporting that is due in 2021 where board meetings are held virtually due to Covid-19. In the event board meetings are held virtually, documentary evidence should be kept with reasons.

3. Execution of documents

BVI law and Cayman Islands law do not generally require documents to be signed with traditional wet-ink signatures by the parties at a signing meeting. Instead, parties entering into commercial contracts will most likely sign a hard copy document in wet ink, which is then converted into electronic form and sent by e-mail. In this regard, it is important to keep in mind the common law “Mercury” guidelines.

As an alternative, and subject to the conditions and exceptions discussed below, a document may also be signed electronically. This may take a number of forms. For example, a signatory may type his/her name into a soft copy of the relevant contract,

or apply an electronic image of his/her handwritten signature into the relevant signature block. A web-based e-signing platform, such as DocuSign, may also be used to a similar end. It is important to ensure that the M&A of the relevant company and the terms of the applicable commercial contract do not prohibit the use of electronic signatures.

It is worth noting that multiple forms of execution may be used by the parties to an agreement as a matter of BVI law and Cayman Islands law. For example, one or more parties may use an electronic signature, while one or more of the other parties may sign by wet ink.

The Electronic Transactions Law (2003 Revision) of the Cayman Islands (the “**ETL**”) and the Electronic Transactions Act 2001 of the BVI (the “**ETA**”) recognize electronic signatures as legally valid, binding and enforceable so long as the relevant signatory intends to sign the applicable document and the signature is reliable in light of its purpose and the circumstances. Broadly speaking, an electronic signature is deemed to be “reliable” if:

- i. the means of creating the electronic signature is linked to, and under the control of, the relevant signatory and of no other person; and
- ii. any alteration to the electronic signature made after the time of signing is detectable.

It is worth noting that BVI law also requires the consent of the counterparty if the other party signs a document electronically.

Traditional wet-ink signatures are still required for certain documents with special execution formalities or for other reasons. For example, documents that need to be notarized or filed with certain registries or authorities may need to be executed by hand. Wills and certain property related documents also need to be signed using wet-ink signatures. Importantly, whilst the ETL expressly approves the use of e-signatures with respect to the execution of deeds by Cayman Islands companies, the ETA provides that anything required to be done by deed may not be executed by e-signature. Whilst this has not been tested in the courts to our knowledge, our view is that this exclusion does not apply to documents that are executed as a deed but are not required to be executed as such as a matter of law.

As a practical matter:

- i. BVI and Cayman Islands companies transacting with banks or other financial institutions should establish whether wet-ink signatures will be required with respect to security documents or any other finance documents. This is fairly typical in cross-border financing transactions.
- ii. To the extent that a legal opinion is required with respect to a document that is executed using an e-signature, it is important to check whether counsel will be able to issue a clean opinion, or whether certain assumptions and qualifications will be required.

- iii. Directors of BVI and Cayman Islands companies should consider whether their internal signing policies (if any) need to be updated to cater for the use of e-signatures.

To the extent that any transaction documents need to be sealed as a matter of the governing law of that document, the board of directors of the applicable company should locate the common seal at the outset of the transaction, or authorize the creation of one in a timely fashion. It should be noted that whilst BVI companies must maintain a common seal, Cayman Islands companies do not and directors should be made aware of this to avoid any potential delays in signing.

To the extent that the directors of a BVI or Cayman Islands company may not be available to sign documents using wet-ink signatures or electronically, the relevant company should consider whether a power of attorney ought to be put in place, or whether it is otherwise appropriate to authorize certain persons to sign documents on behalf of that company by way of a resolution of the board of directors. It may also be possible to appoint an alternate director as referenced above. These types of measures should be considered as part of a company's overall business continuity and contingency planning.

4. Company registries

The BVI Registry of Corporate Affairs and the Cayman Islands Registrar of Companies remain open with some relatively minor changes to cater for Covid-19. Registered agents in the BVI and registered office providers in the Cayman Islands are, on the whole, also operating relatively normally in our experience.

5. Liquidity and financial distress

Covid-19 has had a significant impact on the earnings and revenue streams some companies. Some companies have lost their investment grade credit ratings and investors have sold down positions in newly created sub-investment grade debt. Lenders have also generally focused on preserving capital and supporting existing clients with bridge financing and liquidity, leaving less appetite for new corporate loan transactions. In addition, certain borrower-friendly terms that regularly featured in loan documentation prior to Covid-19, such as unrestricted subsidiary structures which facilitate additional borrowing, have become more heavily negotiated.

Loan defaults have also increased due to an inability to service debt. For example, US institutional loan defaults climbed to 3.9% on a trailing 12-month basis in June. To put this into perspective though, default rates remain considerably lower than the 10%+ levels observed in 2009 following the global financial crisis. This is due to the fact that many companies have managed to draw down on revolving credit facilities and obtain payment holidays/covenant suspensions and waivers from financial institutions. The increasing prevalence of loan transactions done on cov-lite terms prior to Covid-19 has also mitigated the risk of breaching covenants and triggering a default.

The following practical points may assist the board of directors of a BVI or Cayman Islands company which is experiencing a liquidity crisis and/or seeking to mitigate any potential insolvency risks:

- i. **Treat creditors fairly (and where they are of the same class, equally).** BVI and Cayman Islands law include a vast range of statutory provisions which seek to protect creditors from the unfair distribution of a company's assets prior to a formal insolvency process. For example, directors may be personally liable for disposing of assets at an undervalue or preferring particular creditors over others. Such transactions may also be unwound by the courts. Directors of a BVI or Cayman Islands company that are continuing to trade in a situation where the relevant company is of dubious solvency should take appropriate legal advice to ensure that they continue to meet all of their statutory and common law obligations.
- ii. **Ensure compliance with fiduciary and common law directors' duties owing to the company.** Broadly speaking, these include the duties:
 - a) to act with reasonable care, diligence and skill;
 - b) to act in good faith in the best interests of the relevant company;
 - c) to exercise a director's powers for proper purposes;
 - d) to avoid conflicts of interest;
 - e) not to fetter a director's discretion; and
 - f) not to misuse or misappropriate the relevant company's property.

Any breach of these duties may result in personal liability on the part of a director and the relevant transaction may be set aside by the courts.

It is important to note that the board of directors of a BVI or Cayman Islands company has a duty to consider the interests of its creditors as paramount if that company is insolvent or of dubious solvency. This is because the creditors are the ultimate beneficiaries of an insolvent company's assets. As noted above, appropriate legal advice should be sought if the relevant company's solvency is in question.

- iii. **Review contracts to consider whether a default or insolvency event has been (or could be) triggered.** Most commercial contracts governed by BVI or Cayman Islands law contain a force majeure clause which may allow a party to terminate the contract and/or be excused from complying with certain of its terms. Whether Covid-19 constitutes a force majeure event will depend on the specific drafting in each case. If it does not, it may nevertheless be possible to rely on the common law doctrine of frustration to excuse performance.
- iv. **Hold regular board meetings with detailed minutes.** The directors of a BVI or Cayman Islands company should keep each other updated in



times of financial distress as a company's financial outlook can rapidly change. This should include forming a plan as to how to return the company to health or achieve the best result possible for creditors. Keeping detailed meeting minutes additionally ensures that there is a written record of such proceedings in the event that any of the directors' decisions are challenged at a later date.

- v. **Frequently review financial information.** The board of directors should ensure that a BVI or Cayman Islands company's balance sheet and cash flow position is frequently reviewed with appropriate advisors to detect any solvency concerns. This is particularly important because a director's compliance with his/her fiduciary and common law duties may include an assessment of his/her actual knowledge and what a reasonable person with the director's skills and competence ought to have known in that director's position.
- vi. **Seek ratification.** In certain instances, it may be appropriate to obtain shareholder approval in order to ratify transactions that a company is proposing to enter into. For example, it is relatively commonplace to obtain such approval in circumstances where a BVI or Cayman Islands company enters into a transaction where there is no or little corporate benefit to it. This includes companies that are providing third party collateral support to group entities that are in financial distress.

This publication is not intended to be a substitute for specific legal advice or a legal opinion. For specific advice, please contact:

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