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Legal Briefings

Winding up a company on just and equitable grounds in the British Virgin Islands

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In the absence of any shareholders agreement in place, the rights of the shareholders of a British Virgin Islands (“BVI”) company are governed by the terms of the company’s Memorandum and Articles of Association. However, there can be situations where the majority who control the company act in a way that is prejudicial to the rights of the company’s minority shareholders. In this situation, the BVI courts have jurisdiction to address issues relating to minority shareholder rights and unfair prejudice. One of the most common remedies sought by an aggrieved shareholder is the winding up of the company on just and equitable grounds.

This Legal Briefing will provide an overview of the unfair prejudice regime in the BVI and the remedy of winding up a company on just and equitable grounds. Further, situations where the remedy may or may not apply are also explored in this Legal Briefing.

Unfair prejudice

The BVI Business Companies Act (Revised 2020) (as amended) (“BCA”) provides statutory basis for shareholders to bring an unfair prejudice claim. A shareholder who considers that the company’s affairs “*have been, are being or are likely to be, conducted in a manner that is, or any act or acts of the company have been, or are, likely to be oppressive, unfairly discriminatory, or unfairly prejudicial to him or her in that capacity, may apply to the Court for an order*”.

In assessing whether the company’s affairs that the aggrieved shareholder has claimed has caused them unfair prejudice, the BVI courts will apply an objective test. Each situation is different. In order to assess whether there is unfair prejudice, the BVI court will consider, amongst other factors:

- 1) the company’s constitutional documents (i.e. its Memorandum and Articles of Association);
- 2) the specific facts and circumstances concerning the unfair prejudicial conduct; and
- 3) shareholders’ agreement (if any).

Available remedies

If, on an application by the prejudiced shareholder, the BVI court “*considers that it is just and equitable to do so*”, it may make any such order as it thinks fit, including, one (or more) of the following:

- a) require the company or any other person to acquire the shares of the aggrieved shareholder or pay them compensation;

- b) regulate the future conduct of the company's affairs;
- c) amend the company's Memorandum and Articles of Association;
- d) appoint a receiver of the company;
- e) appoint a liquidator under the Insolvency Act (Revised 2020) (as amended) (the "Act");
- f) direct the rectification of the company's records; and
- g) set aside any decision made or action which was taken by the company or its directors which were in breach of the BCA or the company's constitutional documents.

In light of the above, the BVI court (once satisfied that unfair prejudicial conduct has occurred) have broad discretion as to the relief it can grant in order to address and remedy the prejudice that the shareholder has suffered. Notwithstanding the remedies set out above, in practice, most claimants seek either:

- 1) a buy-out of their shares (so as to redeem or withdraw their equity from the company at fair value); or
- 2) the winding up of the company.

BVI court's winding up jurisdiction – the just and equitable ground

As stated above, one of the most common remedies sought by an oppressed minority shareholder of a BVI company is the court's just and equitable winding up jurisdiction.

The Act

The court's jurisdiction to wind up a BVI company on just and equitable grounds is based on statute, namely, the Act. The court's powers are expressly set out in the Act, which provides that the court may, on the application of a shareholder, appoint a liquidator if it "*is of the opinion that it is just and equitable that a liquidator should be appointed*". It should be noted that the court's power in this respect is circumscribed later in the Act (see below), which provides that where "*an application to appoint a liquidator is made by a shareholder...if the Court is of the opinion that—*

- a) *the applicant is entitled to relief either by the appointment of a liquidator or by some other means; and*
- b) *in the absence of any other remedy it would be just and equitable to appoint a liquidator, it shall appoint a liquidator unless it is also of the opinion that some other remedy is available...and that he or she is acting unreasonably in seeking to have a liquidator appointed instead of pursuing that other remedy.*"

Case law

The Act does not contain any guidance as to what exactly constitutes "just and equitable" in relation to applying for an order to appoint a liquidator of the company to wind it up. To that effect, case law authority from the BVI as well as other common law jurisdictions provide useful guidance as to the scope of the court's power to appoint a liquidator where the court is of the opinion that it is just and equitable to do so. As a starting point, the House of Lords in the English case *Ebrahimi v Westbourne Galleries Ltd*¹ ("*Ebrahimi*") held that the tendency to try to create categories under which the remedy must be brought was wrong – "*general words should remain general and not be reduce to the sum of particular instances.*"²

A similar approach was also taken in the BVI. In *Fortune Bright Global Limited v Central Shipping Co., Limited*³, the BVI court stated that the just and equitable basis for the appointment of a liquidator was broad and the foundational principles continue to evolve and be refined⁴. Further, the Court of Appeal of the Eastern Caribbean Supreme Court held in *Chu Kong v Lau Wing Yan and Ocean Sino Limited*⁵ (a case

¹ [1973] AC 360

² [1973] AC 360 at [374]

³ BVIHC (COM) 2015/0036

⁴ BVIHC (COM) 2015/0036 at [27]

⁵ BVIHCMAP2017/0020

which was later reversed on other grounds on appeal in the Judicial Committee of the Privy Council – see below) that the just and equitable ground was a wide one and “*must be generously construed to include a wide range of circumstances capable of invoking the court’s jurisdiction.*”⁶

Situations where companies have been wound up on just and equitable grounds

It is not possible to provide an exhaustive list of the circumstances where the above equitable principles will apply. The broad equitable principles are to be applied to different cases before the court. The court, when determining whether to make an order, “*must itself evaluate the factual matrix in order to form a view as to whether a sufficient reason for making the order is demonstrated.*”⁷ Notwithstanding this, below is a list of situations which may justify the appointment of a liquidator and the winding up of the company on just and equitable grounds:

Loss of substratum or purpose

A company may be wound up on the just and equitable ground where there has been a loss (or failure) of substratum or objects (e.g., where the company was formed for a certain purpose which has now come to an end, been abandoned or has otherwise become impossible to achieve).

In *Re Klimvest PLC*⁸, the English High Court ordered the winding up of a public listed company on the just and equitable ground for loss of substratum. Judge Cawson KC (sitting as a High Court Judge) held, *inter alia*:

- 1) that whether or not a company can be wound up for failure of substratum is a question of equity between the company and its shareholders; and
- 2) if a company cannot practically pursue its purpose or if the company will not pursue the purpose (or has abandoned it), then a company ought to be wound up as having lost its substratum or purpose.

Judge Cawson KC in *Re Klimvest PLC* applied Jenkins J’s dictum in the English case of *Re Eastern Telegraph Co., Ltd*⁹ that “*if a shareholder has invested his money in the shares of the company on the footing that it is going to carry out some particular object, he cannot be forced against his will by the votes of his fellow shareholders to continue to adventure his money on some quite different project or speculation.*”¹⁰

Where the company is sham

The courts are likely to wind up a company on the just and equitable ground where the company was not formed for a legitimate purpose, but merely with the purpose of extracting money from shareholders and was, from the very beginning a “*sham, a bubble, a trap*”¹¹.

Functional deadlock

The Judicial Committee of the Privy Council (which is the highest court of appeal for BVI cases) in *Chu v Lau*¹² (on appeal from the BVI courts) recognised that winding-up was a shareholder’s remedy of last resort. Notwithstanding this, the Privy Council stated that a just and equitable winding-up may be ordered if:

⁶ BVIHCMAP2017/0020 at [45]

⁷ *Australian Securities and Investments Commission v Letten (No 10)* [2011] FCA 498 at [14]

⁸ [2022] EWHC 596 (Ch)

⁹ [1947] 2 All ER 104

¹⁰ [1947] 2 All ER 104 at [109]

¹¹ *Re Neath Harbour Smelting & Rolling Works* (1886) 2 TLR 366 at [339]

¹² [2020] UKPC 24

- 1) there is a functional deadlock, i.e. where an inability of shareholders to co-operate in the management of the company's affairs has led to an inability of the company to function at board or shareholder level)¹³; and
- 2) the company is a corporate quasi-partnership, a just and equitable winding-up may be justified if there is an irretrievable breakdown in trust and confidence between the shareholders (essentially on the same grounds as would justify the dissolution of a true partnership)¹⁴.

Unauthorised change in the type of business or activity of the company

It should be noted that a breakdown in the relationship between a company's shareholders is not, in of itself, justification for winding up the company. The Court of Appeal of the Eastern Caribbean Supreme Court in Wang Zhongyong and Others v Union Zone Management Limited and Others¹⁵ stated that for such a situation to escalate to the level of a just and equitable winding up of the company, it must represent or lead to a breach of some underlying agreement (either express or implied) or "*some unauthorized change in the type of business or activity for which the company was incorporated in the first place.*"¹⁶ In light of this, it would be just and equitable that a company be wound up if it was incorporated for a specific and limited purpose and where the majority shareholders had ignored that purpose.

Lack of probity in the conduct of the company's affairs

A shareholder does not need to only rely on circumstances which affect them in their capacity as a shareholder in order to bring a claim on the just and equitable ground. The scope is wide for an aggrieved shareholder - they can also rely on any circumstances which affect them in their relations with the company or other shareholders. A company can be wound up on the just and equitable ground if, for example, a lack of probity (in the form of allegations of breaches of fiduciary duty) may constitute the basis of a just and equitable winding up.

The Judicial Committee of the Privy Council in the case of Janet Livingstone Loch and Another v John Blackwood Limited¹⁷ ("**Loch**") stated that at the foundation for winding up a company on the just and equitable ground, there must be a justifiable lack of confidence in the conduct and management of the company's affairs (e.g. because of fraud or serious misconduct by the company). This lack of confidence must be based on the conduct of the company's directors (and not in respect of the directors' private life or affairs). Further, such lack of confidence must not be based on the aggrieved shareholder's dissatisfaction with being outvoted on the company's business affairs. However, the Loch case further stated that "*wherever the lack of confidence is rested on a lack of probity in the conduct of the Company's affairs, then the former is justified by the latter, and it is under the statute just and equitable that the Company be wound up.*"¹⁸

Failure to pay reasonable dividends

The amount of remuneration for directors, as well as the level of dividend to be declared are, in short, commercial decisions for a company to make (although such decisions must be made in good faith in the company's best interests as a whole). In the English case of Re a Company (No 00370 of 1987) Ex p. Glosop¹⁹, Harman J. stated that "*directors have a duty to consider how much they can properly distribute to shareholders.*"²⁰ If the directors failed to recommend the payment of a dividend to shareholders without due regard to the right of shareholders to have profits distributed to them as far as is commercially possible, the directors' decision would be open to challenge. It should be noted that the non-payment of dividends in

¹³ [2020] UKPC 24 at [14]

¹⁴ [2020] UKPC 24 at [15]

¹⁵ BVIHCMAP2013/0024

¹⁶ BVIHCMAP2013/0024 at [53]

¹⁷ [1924] AC 783

¹⁸ [1924] AC 783 at [3]

¹⁹ [1988] 1 WLR 1068

²⁰ [1988] 1 WLR 1068 at [1076]

itself does not automatically constitute unfair prejudice. However, where the company can afford to pay reasonable dividends and the directors paid themselves excessive remuneration, the failure to pay dividends can form the basis on a winding up on the just and equitable ground.

Situations where companies have not been wound up on just and equitable grounds

Following on from the above, below is a non-exhaustive list of situations which were not enough to justify winding up a company on the just and equitable basis.

If shareholder is acting unreasonably in failing to pursue alternative remedy

On hearing an application by a shareholder to appoint a liquidator over a company on the just and equitable ground, the court will not appoint a liquidator if there is an alternative remedy and the shareholder is acting unreasonably in failing to pursue that remedy. This is perhaps the most important reason a company would not be wound up even if the shareholder is entitled to the relief. The threshold for bringing a successful unfair prejudice claim is high because winding up a company is a drastic and draconian remedy. Given the high bar, a practical point for the aggrieved shareholder to bear in mind is that they should try and seek a realistic alternative, such as a buyout of their shares by another party. It should be noted that where an offer has been made to buy the shareholder's shares at fair value and where such offer has been rejected, the shareholder's unfair prejudice claim may fail if the court concludes that the offer was at fair value because such offer (at fair value) would reflect the remedy that the court is likely to award and so to commence (or continue) such a claim would constitute an abuse of process.

Claim should not be to vindicate personal or business reputation

A claim to wind up a company on just and equitable grounds is not "*an appropriate vehicle for the vindication of personal or business reputation, except insofar as that is incidental to the adjudication as to whether the relief sought is justified.*"²¹

Breakdown in confidence between shareholders due to "aggrieved" shareholder

In *Ebrahimi*, it was stated that there would be no winding up if the breakdown in confidence between shareholders was due to the conduct of the "aggrieved" shareholder²².

Where shareholder's interest is adverse to those of the company

The court will not grant a winding up order where:

- 1) the shareholder seeks to protect interests other than their interests as a shareholder of the company; or
- 2) the application to wind up was not presented as "bona fide" but was made to achieve some collateral purpose (and not to bring about the company's winding up).

An example of this would be the English case of *Re JE Cade & Son Ltd*²³. The petitioning shareholder was the freeholder of land leased to the company which had security of tenure of the land. The court refused to order possession of the land.

²¹ *Re FI Call Ltd* [2015] EWHC 3269 (Ch) at [64]

²² [1973] AC 360 at [387]

²³ [1991] BCC 360

Conclusion

The just and equitable ground for winding up a BVI company is a wide, yet powerful remedy for an aggrieved shareholder. The court has broad discretion as to whether to grant such remedy. The winding up of a company that has no chance of continuing would bring finality to the company's mismanagement and/or misconduct and would appoint independent liquidator(s) in charge to investigate the company's affairs as well as collect the assets and distribute them.

Further Assistance

This publication is not intended to be a substitute for specific legal advice or a legal opinion. If you require further advice relating to the matters discussed in this Legal Briefing, please contact us. We would be delighted to assist.

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