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Directors' duties on the insolvency of a BVI company

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At all times, directors of a company incorporated in the British Virgin Islands (the "BVI") needs to be aware of their role and responsibilities as director, in particular where the company is insolvent or of doubtful solvency.

This client guide provides an overview of the duties of a director of a company and the types of claims that a director of a company can face under the BVI Business Companies Act, 2004 ("BCA") and the BVI Insolvency Act, 2003 (the "IA") in particular:

- the roles and responsibilities of directors of a company, both generally and when a company is in the zone of insolvency;
- the personal liabilities that a director may face where a company enters into an insolvency process; and
- the steps a reasonably prudent director can be expected to consider and, if appropriate, take when a company is in the zone of insolvency.

Directors' duties under the BCA

The director of a company owes duties to the company as a whole and the shareholders whilst the company is solvent. The general duties of a director of a company are contained in its constitutional documents, statute, in equity and the common law. These duties apply to both de jure directors (i.e. those directors listed on the register of directors) and to de facto directors (i.e. persons who act as director, even though they do not have the title of director).

We have set out, in the table on page 3, a summary of directors' duties as a matter of BVI law under the BCA.

Change in directors' duty from shareholders to creditors

Where a company is in the zone of insolvency, the directors of the company should, so far as possible, consider when it became apparent to them (or should have become apparent to them) that the company was likely to become insolvent, as from that stage onwards, the interests of the Company's creditors should have been given paramount consideration.

Insolvency Act claims

If a company does end up in liquidation, either via the appointment of liquidators to the company by a members' qualifying resolution or via a court application, then upon the appointment of the liquidators, the control of the company is handed over to the liquidator and the directors cease to have the power to manage the business and affairs of the company. For further information on the appointment of liquidators to an insolvent company, please refer to our client guide.

The liquidators have statutory powers of investigation and will require the directors to complete a statement of affairs and call for documentation to be provided by the directors and others (including any and all legal advice provided to the Company). The liquidators can also, if necessary, conduct examinations of directors and officers.

The IA provides for a number claims that a liquidator can bring, either in his own name or on behalf of a company, in order to recover assets to make up a shortfall in a company's assets to pay creditor claims. These claims can be split into two categories: (i) malpractice claims, where the company has carried on business improperly and claims can be brought against the persons who caused a company to act improperly (usually, its directors), and (ii) voidable transaction claims, where a company has entered into transactions that are voidable under the IA. The latter claims are usually brought against third parties who have benefited from the transaction and not against the directors personally. For the purpose of this guide, we have set out details of possible malpractice claims below.

Malpractice claims

Sections 254 to 258 of the IA deal with so-called malpractice claims. These are the principal ways in which a director may be ordered to contribute assets to an insolvent company and they include liability for misfeasance (i.e. a breach of director duties), fraudulent trading and insolvent trading. These applications can only be brought by a liquidator.

- **Misfeasance**: The IA misfeasance remedy provides a summary procedure to make persons, including directors, liable to compensate the company for misfeasance, breach of fiduciary duties or other duties to the company. To hold a director accountable under this section it must be shown that he/she/it was guilty of misfeasance or in breach of a fiduciary duty or other duty in relation to the company, and/or that he/she/it has misapplied or retained or become accountable for any money or other assets of the company. This is essentially a "catch-all" provision which enables a liquidator to pursue directors in respect of their breaches of duty, including their breach of duties under the BCA (see table above) or to creditors when the company was on the verge of insolvency.
- **Fraudulent trading**: The court can also make an order against a company's directors if it is satisfied that, at any time before the commencement of the liquidation of the company, any of its business has been carried on by those directors 'with the intent to defraud creditors of the company or creditors of any other person; or for any fraudulent purpose'. In such cases, the court can declare that a director is liable to make a contribution that the court considers proper towards the company's assets. This is not limited to directors and officers, but applies to anyone who has been involved in carrying on the company's business. There are no statutory defences to fraudulent trading, but it is necessary that actual dishonesty (i.e. bad faith) be proved. As a result, such claims are rarely brought in practice.
- **Insolvent trading**: The directors of a company can be liable for insolvent trading where the directors of a company knew or ought to have known that there was no chance that the company would avoid going into insolvent liquidation but failed to take steps to minimise losses to the company's creditors. The directors can become liable for any further losses sustained by the company after the point where they knew or ought to have concluded that there was no reasonable prospect of the company avoiding going into insolvent liquidation, unless they took every step with a view to minimising the potential loss to a company's creditors.

If a Court does finds that a director is liable for misfeasance, fraudulent trading or insolvent trading, it has a wide discretion as to the amount in which the director should contribute to the assets of the company. Usually the order is compensatory, rather than punitive, and is limited to the amount of loss the court finds the director has actually caused, by his particular actions or inaction, to the company. The exception to that would be in the context of a finding of dishonesty or fraud on the part of the director, which may lead to a more punitive order.

Seek advice

Any director who is concerned that their company is in the zone of insolvency should seek specialist advice from a BVI insolvency and restructuring lawyer and/or a BVI insolvency practitioner. Please feel free to contact a member of our Carey Olsen restructuring and insolvency team should you require advice on this matter.

Continued

Duty	Summary
To act honestly and in good faith	To act in a manner that the director believes to be the best interest of the company (or, if the memorandum and articles allow, the best interests of that company's parent).
To act in the best interest of the company	To act in the best interest of the company (or, if the memorandum and articles allow, the best interests of that company's parent).
To exercise powers for a proper purpose	To not act, or agree to the company acting, in a manner that contravenes the BCA or the memorandum or articles the company.
To disclose personal interests	To disclose the fact that he/she/it is personally interested in a transaction on entered into or to be entered into by the company, to the board of the company.
To exercise duties with care, diligence and skill	To exercise powers or perform duties with the care, diligence and skill that a reasonable director would exercise in the same circumstances taking into account, but without limitation the nature of the company, the nature of the decision and the position of the director and the nature of the responsibilities undertaken by the director.
To confirm the solvency test when making distributions	Directors of a company may, by resolutions, authorise a distribution by the company to members at such time and of such an amount, as they think fit if they are satisfied on reasonable grounds, that the company will, immediately after the distribution the solvency test[1]. If a distribution is paid in breach of this provision, it is an unlawful distribution.
Shift of duty to creditors in the zone of insolvency	The directors owe a duty to consider or act in the best interests of creditors at a time when the company is insolvent or on the verge of insolvency (often known as the 'zone of insolvency'), and at such a time, the interests of creditors should be considered paramount.

1 For companies incorporated under the BCA, a company satisfies the solvency test if (i) the value of the company's assets exceeds it liabilities; and (ii) the company is able to pay its debts as they fall due.

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