

# Distributions, share purchases and redemptions under the BVI Business Companies Act

GUIDE

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One of the factors that makes the British Virgin Islands (**BVI**) an attractive place in which to incorporate a company is that the BVI Business Companies Act 2004 (as amended) (the **Act**) is modern, flexible and not overly prescriptive.

This guide examines the key aspects of distributions, share purchases and redemptions by a BVI company\* under the Act.

## Directors' duties

The directors of a company should only make a distribution or purchase or redeem shares at the option of the company if they believe that it is in the best interests, and for a proper purpose, of the company to do so. Otherwise they will be in breach of their statutory and common law duties to the company.

## Distributions

A company's articles of association will normally contain provisions dealing with the payment of distributions. The Act imposes additional obligations relating to the payment of distributions.

### What is a distribution?

Under the Act, a distribution is any direct or indirect transfer by a company of any of its assets (other than any of its shares), or the incurring by it of a debt, to or for the benefit of, a shareholder, whether made by:

- the purchase of any asset;
- the purchase, redemption or other acquisition of any of its shares;
- the transfer of any debt; or
- any other means.

A distribution includes a dividend but excludes an issue of bonus shares.

### Solvency tests

The Act only allows the directors of a company to authorise a distribution if they are satisfied on reasonable grounds that the company will, immediately after the distribution is made, satisfy the following tests (the **solvency tests**):

- the value of its assets will exceed its liabilities; and
- it will be able to pay its debts as they fall due.

The solvency tests are frequently included in a company's articles of association.

The resolution of directors authorising the distribution must contain a statement that, in their opinion, the company will satisfy the solvency tests immediately after the distribution is made.

If, after a distribution has been authorised but before it is made, a director ceases to be satisfied on reasonable grounds that the company will satisfy the solvency tests immediately after the distribution is made, the distribution is taken not to have been authorised.

### **No maintenance of capital rules**

There are no maintenance of capital rules under the Act so it is relatively simple for a company to make payments to its shareholders. Any asset of a company (including the consideration paid for its shares) may be distributed to its shareholders if its directors comply with the requirements regarding the solvency tests mentioned above.

### **Clawback**

#### **From shareholders**

If a distribution is made to a shareholder in circumstances where the company did not satisfy the solvency tests immediately after the distribution was made, the company may recover the distribution from the shareholder unless:

- the shareholder received the distribution in good faith without knowing that the company did not satisfy the solvency tests;
- the shareholder has taken actions relying on the validity of the distribution; and
- it would be unfair to require the distribution to be repaid in whole or part.

#### **From directors**

If, after a distribution has been authorised but before it is made, a director:

- ceases to be satisfied on reasonable grounds that the company would satisfy the solvency tests immediately after the distribution is made; and
- fails to take reasonable steps to prevent the distribution being made,

the director is personally liable to repay to the company any part of the distribution that is not recovered from the shareholders.

In addition, if a company became insolvent as a result of a distribution being made, the directors would be in breach of their statutory and common law duty to the company to act with care, diligence and skill and potentially personally liable to pay the company an amount equal to the distribution.

### **Share purchases and redemptions**

#### **Distribution**

Under the Act, the purchase or redemption by a company of its shares constitutes a distribution except where it:

- redeems the shares at the option of the shareholder, or on a specified date, in accordance with the rights attaching to the shares;
- redeems the shares pursuant to a right of the shareholder to have the shares redeemed or to have them exchanged for cash or other property;
- redeems the shares under a squeeze out;
- acquires the shares at fair value as a result of a dissenting shareholder requiring it to do so under the Act; or
- acquires fully paid shares for no consideration from a shareholder by way of surrender of the shares.

Consequently, a company may generally only purchase or redeem its shares if the directors comply with requirements regarding the solvency tests mentioned above.

However, even where the directors are not required by the Act to be satisfied that the solvency tests will be met, clearly they cannot purchase or redeem shares if, as a result, the company would become insolvent. This would amount to a breach of their statutory and common law duties to the company.

## Surrender

A company may acquire its own fully paid shares for no consideration from a shareholder by way of surrender of the shares. The shareholder must surrender the shares by giving the company a written surrender notice signed by it.

## Source of payment

A company may fund the purchase or redemption of its shares from any source.

## Nature of payment

There is no concept of share capital (whether in respect of par value or any amount paid in excess of it) under the Act. Instead, the Act refers to the consideration paid for the issue of a share. Consequently, the Act does not categorise the amount paid for the purchase or redemption of a share (no matter the source of the payment) as being either capital or income in nature.

Where the nature of the payment is important to the shareholder for tax or other reasons, it would be necessary to look to the accounting principles under which the company's financial statements are prepared (if it prepares financial statements) or the tax laws of the place where the shareholder is resident for tax purposes.

## Procedure

The Act sets out procedures for the purchase or redemption of shares. These procedures will apply unless a company's memorandum or articles of association disappplies them and includes its own provisions for the purchase or redemption of shares.

## Options under the Act

### *General*

Where a company wishes to purchase or redeem its shares, it has two options under the Act. It may make:

- an offer to all shareholders (a **pre emptive offer**) to purchase or redeem shares that:
  - would not (if accepted) affect the relative voting and distribution rights of shareholders; and
  - gives each shareholder a reasonable opportunity to accept the offer; or
- an offer to one or more shareholders (a **non pre emptive offer**) to purchase or redeem shares:
  - to which all shareholders have consented in writing; and
  - is permitted by the company's memorandum or articles of association and complies with the requirements set out below.

In the case of a pre emptive offer, the terms of the offer may allow the company to acquire additional shares from a shareholder if another shareholder does not accept the offer in whole or part.

In the case of a non pre emptive offer, the directors may only make the offer if they have passed a resolution stating that in their opinion:

- the purchase or redemption is to the benefit of the remaining shareholders; and
- the terms of the offer (including the consideration offered for the shares) are fair and reasonable to the company and the remaining shareholders.

The resolution of directors must set out the reasons for holding the opinion.

A shareholder (usually one to whom the offer has not been made) has the right to apply to the High Court to prevent the proposed purchase or redemption on the grounds that it is not in the best interests of the remaining shareholders or that the terms of the offer and the consideration are not fair and reasonable to the company or the remaining shareholders.

## Redeemable shares

Where a share is issued as a redeemable share, the Act states that, if the share is redeemable:

- at the option of the shareholder and the shareholder gives the company a redemption notice, the company must redeem the share on the date specified in the notice or (if no date is specified) on the date on which the notice is received; or
- on a specified date, the company must redeem the share on the specified date.

From the date of redemption, the former shareholder will rank as an unsecured creditor of the company for the redemption amount. If, however, the company goes into insolvent liquidation before the redemption amount is paid, the former shareholder is unable to claim for the redemption amount in the company's liquidation in competition with its creditors.

## Provisions in the Articles

The vast majority of companies disapply the share purchase and redemption provisions in the Act in their articles of association. Typically, a company's articles of association will authorise the directors to purchase or redeem shares at any time, from any shareholder, for any price and on any terms, they think fit.

Where a company has disapplied the share purchase and redemption provisions in the Act:

- unless its memorandum or articles of association specify otherwise, the company cannot purchase or redeem a shareholder's shares without the consent of the shareholder; and
- the company will normally purchase or redeem shares by sending the shareholder a short letter setting out the terms on which it proposes to buy or redeem the shareholder's shares and the shareholder will counter sign the letter and return it to the company to signify the shareholder's consent.

## Shares cancelled

Any shares that have been purchased or redeemed by a company are taken to be automatically cancelled unless they are to be held as treasury shares.

## Treasury shares

If a company is not prohibited from doing so by its memorandum or articles of association and its directors decide to do so, a company may hold as treasury shares any shares that it purchases or redeems. The company may not hold as treasury shares more than 50 per cent of its shares in issue.

All rights and obligations attaching to a treasury share are suspended and may not be exercised by or against the company while it holds the share as a treasury share.

## \* Scope of this guide

This guide considers Business Companies incorporated under the Act. It does not cover International Business Companies incorporated under the International Business Companies Act 1984.

## Contacts

A full list of contacts specialising in BVI law can be found [here](#).