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Barristers & Attorneys

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MAJORITY OF SHAREHOLDERS APPROVE SALE OF BANK OF BERMUDA TO HSBC plc

On 16th February, 2004, a majority of the shareholders of the Bank of Bermuda approved the sale of the Bank to HSBC plc at a Special General Meeting called for that purpose.

Following the meeting, the Chairman of the Bank of Bermuda, Mr. Joseph Johnson, pointed out that "it was a sad day and the end of a tradition, with the Bank of Bermuda having offered banking services as an independent entity for 114 years".

Of the 28.99 million shares outstanding held by close to 6,912 shareholders, a significant majority of 24.3 million of the shares (representing 83.8 percent of the bank's shares) voted at the Special General Meeting and 91 percent of those shares voted in favour of the sale.

Nine percent of the shares that voted (2.4 million shares) were lodged against the sale. It is interesting to note that HSBC plc cannot avail itself of the 'notice of acquisition of remaining shares' provision laid down by Section 103 of the Companies Act, 1981 since it had not acquired 95% of the shares at the Special General Meeting referred to above.

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This article has not taken into consideration any special provisions found in the Bank of Bermuda Private Act, the Memorandum of Association or the Bye-laws of the Bank that may be in conflict with the provisions with respect to minority shareholders found in the Companies Act, 1981.

Under the Companies Act, 1981 in the event that HSBC had acquired 95 percent of the shares of the Bank of Bermuda, Section 103 would have given it the right to acquire the remaining 5% of the shares. Section 103 states as follows:-

(1) The holders of not less than ninety-five per cent of the shares or any class of shares in a company (hereinafter in this section referred to as the "purchasers") may give notice to the remaining shareholders or class of shareholders of the intention to acquire their shares on the terms set out in the notice. When such a notice is given the purchasers shall be entitled and bound to acquire the shares of the remaining shareholders on the terms set out in the notice unless a remaining shareholder applied to the Court for an appraisal under subsection (2):-

Provided that the foregoing provisions of this subsection shall not apply unless the purchasers offer the same terms to all holders of the shares whose acquisition is involved.'

(2) Any shareholder to whom a notice has been given under subscription (1) may within one month of receiving the notice apply to the Court to appraise the value of the shares to be purchased from him and the purchasers shall be entitled to acquire the shares at the price so fixed by the Court.

(3) Within one month of the Court appraising the value of any shares under subsection (2) the purchasers shall be entitled either -

(a) to acquire all the shares involved at the price fixed by the Court; or

(b) cancel the notice given under subsection (1).

Reasons For Incorporating In Bermuda

- Respected International Business jurisdiction (built on the principle of "know your customer");
- Tax Neutral Business Environment (no income, capital gains, transfer or withholding taxes);
- Business sensitive and well established Legal System (based upon English common law);
- Minimal Government Annual Reporting except for Restricted Businesses;
- Access to Capital Markets (through Bermuda Stock Exchange listings);
- Access to one of the most successful Insurance/Reinsurance Markets in the world;
- Reliable Banking System;
- Efficient Support Services (legal, accounting, management, corporate and trust services);
- State-of-the-Art Global Internet Services and Telecommunications (connecting Bermuda to the world); and
- Friendly yet efficient business environment for holding Company Meetings.

(4) Where the Court has appraised any shares under subsection (2) and the purchasers have prior to the appraisal acquired any shares by virtue of a notice under subsection (1), then within one month of the Court appraising the value of the shares if the price of the shares they have paid to any shareholder is less than that appraised by the Court they shall either -

(a) pay to such shareholder the difference in the price they have paid to him and the price appraised by the Court; or

(b) cancel the notice given under subsection (1) and return to the shareholder any shares they have acquired and the shareholder shall repay the purchasers the purchase price.

Another option available to the Bank of Bermuda is to exercise its rights pursuant to Section 42A of the Companies Act, 1981 to purchase its own shares if authorized to do so by its Memorandum of Association or Bye-laws.

What are the rights of the minority shareholders (representing nine percent of the shares of the Bank)? They can sell their shares at the price offered by HSBC plc or continue to hold their shares in the Bank and possibly be subject to a Bank 'Buy Back' provision or apply to the Court for an appraisal (once they receive a Section 103 Notice) or apply to the Courts under the common law just and equitable rules.

This is not intended to provide legal advice to any person who may read this article. For further information or legal advice on this topic, please contact Lynda Milligan-Whyte at lmw@milligan.bm.

CORORATE GOVERNANCE UPDATE

Company Meetings

It is important that clients who have established Bermuda exempted companies familiarize themselves with the proper procedures for convening, holding and dealing with meetings of Bermuda exempted companies and the necessity to keep certain records of that company at its registered office in Bermuda.

A Bermuda exempted company is subject to Bermuda law with respect to the manner in which company and board of director meetings are convened, recorded and held. In particular, the Companies Act, 1981 ("the Companies Act") sets out the legal requirements for company meetings and the Bye-laws of the Company may expand upon these legal requirements.

In convening meetings of the Company, proper notice must be sent to each shareholder or director (as the case may be). With respect to shareholder meetings, the Companies Act requires at least five days' notice when convening such meetings and the Bye-laws of a particular company may expand the minimum notice requirement.

For Board of Director meetings, there is no minimum requirement laid down in the Companies Act, but when such meetings are convened, proper notice must be given to all directors. Case law in Bermuda has given judicial interpretation as to what constitutes 'proper notice' of Board meetings and the test is "what is reasonable in the circumstances". If all of the directors reside outside of Bermuda then the notice period may be significantly more than if all of the directors were resident in Bermuda.

Such notices of meetings are kept in the records of the Company to provide evidence that each director or shareholder did receive proper notice. If the Secretary of the Company is outside of Bermuda, he or she must ensure that the minute book which is kept in Bermuda has a copy of any notices. The consequence of not showing that proper notice was given to directors or shareholders could render the meeting voidable if challenged.

A Bermuda exempted company must hold an Annual General Meeting each year and there is no statutory requirement that such a meeting be held in Bermuda. Also, the Directors of a Bermuda exempted company must convene a meeting each year to appoint the officers of the Company and otherwise deal with the business of the company. Meetings of the Board of Directors can be held in or outside of Bermuda or as determined in accordance with the Bye-laws of the Company.

Pursuant to the Companies Act a Bermuda exempted company must have a registered office in Bermuda at which the books and records of the Company are kept. The 'books and records' of the Company include the minute book, share register, register of directors and officers, all contracts entered into by the company, all financial statements (and auditors' reports) and all minutes of meetings of the Company.

In particular, Section 81 of the Companies Act specifically requires that every company shall cause minutes of all proceedings of general meetings and of all proceedings of meetings of its directors to be entered in books kept for that purpose; and minutes prepared in accordance with Section 81 shall be kept by the secretary at the registered office of the company and shall be evidence of the proceedings.

If any contract is to be signed under the common seal of the Company, the seal, which is kept at the registered office of the Company in Bermuda, is affixed to such contracts by any two directors or one director and the secretary of the company. If the Company has more than one seal, such duplicate seal can be kept outside of Bermuda and used to authenticate documents entered into on behalf of the Company, but copies of any such documents authenticated using the duplicate seal must be sent to the registered office in Bermuda. This requirement for keeping copies at the registered office applies to all documents (whether under seal or not);

For further information on the legal requirements relating to Company Meetings, please contact Lynda Milligan-Whyte at **lmw@milligan.bm.**

RICHMOND GROUP LIMITED AND ITS AFFILIATES

Richmond Corporate Services Ltd. - provides corporate administration and compliance services to Bermuda companies, partnerships and trusts.

Richmond Financial Managers Ltd. - provides a wide range of management services to its clients. It can also assist in advising insurance professionals on the Bermuda regulatory environment, particularly the capital requirements, solvency margins and liquidity ratios.

Richmond Investments (Bda) Limited - provides investment advisory services to clients of the Richmond Group of Companies who are institutional and high net worth individuals.

Richmond Nominees Limited - provides nominee services to clients of the Richmond Group of Companies who are institutional and high net worth individuals.

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VOLUNTARY WINDING UP: SHAREHOLDER APPROVAL NOT NECESSARILY REQUIRED UNDER BERMUDA LAW

In what appears to be the first considered ruling of its kind in Bermuda, the Supreme Court of Bermuda has recently ruled that shareholder approval is not necessarily required in order for a company (through its directors) to petition the court for the company to be wound-up on the basis of insolvency. The primary question in the matter of *Re. First Virginia Reinsurance Ltd* (the "Company") was whether its directors were competent to authorise the presentation of a petition for winding-up by the Company without shareholder approval in circumstances where the Bye-Laws of the Company do not explicitly confer such as power.

The Facts

The facts of the *First Virginia Re* case, so far as are relevant, were that the Company was insolvent in that it was unable to meet its obligations as and when they fell due. This flowed from the fact that the principal creditors of the Company (who may well be shareholders as well) included affiliates recently placed into receivership in the United States, the allegedly improper drawing down of a trust fund established to secure the Company's reinsurance obligations and the filing against the Company in the United States of two class action lawsuits.

In addition to the commercial insolvency referred to above, the court found that independent actuarial reviews (which the Company did not necessarily accept) indicated that on a balance sheet basis the Company had a deficit of between roughly $79 million and $111 million.

The Board resolved at a meeting of directors to authorise the Company to apply immediately for the appointment of a provisional liquidator.

Notwithstanding that no reason was explicitly spelled out, the court found that seeking prior shareholder approval for the presentation of a petition to wind-up the Company was not practicable.

The Bye-Laws

The court found that the Bye-Laws of the Company were in standard form, by Bermuda standards. Bye-Law 3 of the Company provided, in part, as follows:-

"In managing the business of the Company, the Board may exercise all such powers of the Company as are not, by statue or by these Bye-Laws, required to be exercised by the Company in general meeting, subject, nevertheless, to these Bye-Laws, the provisions of any statue and to such regulations as may be prescribed by the Company in general meeting."

The question naturally arose as to whether the power to petition for the company's winding-up was required to be exercised by the company in general meeting (i.e. by the shareholders) by either statue or by the Bye-Laws themselves.

The court found that neither the Bye-Laws nor the Companies Act 1981 (the "1981 Act") expressly required shareholder approval of an application to the court for the Company's winding up. This led to the next question: Can such a requirement be read into either the Bye-Laws or the 1981 Act by way of necessary implication?

The Law

Prior to the *First Virginia Re* decision, it had been widely believed in Bermuda that shareholder approval would be required in order for a Company to present a petition to the court for its own winding-up on the authority of the English decision in *Re. Emmadart*. That case, which was decided in 1978, was considered by the court in detail, as were a number of Australian authorities. Following a careful analysis of all of the authorities presented, the court came to the conclusion that *Re. Emmadart* ought not to be followed in Bermuda and that the reasoning behind the Australian series of cases was to be preferred.

Moreover, the court found that there was no need for the directors to seek shareholders' approval to ratify the board decision to present a petition in the Company's name. This aspect of the ruling is consistent with the shifting nature of directors' fiduciary duties in the face of actual or apprehended

insolvency (see January, 2004 newsletter). In the face of actual or apprehended insolvency, the directors' primary duty is to the creditors of the Company.

The court also recognized that under sections 243 and 245 of the 1981 Act, directors are exposed to criminal liability for various fraudulent acts committed in a period (up to 12 months) preceding the commencement of a winding-up and that those same directors face civil liability for fraudulent trading, which includes carrying on the business of the Company when it is known to be insolvent, under section 246 of the 1981 Act.

The court, quite rightly, asked itself, in the context of actual insolvency, where the directors of a Company are to have primarily regard to the welfare of the Company's creditors: Why should the directors' powers be construed as excluding the right to take what may be the most important step toward achieving that goal, the ability to present a petition without shareholder approval (which may not be forthcoming)?

In short, the court clearly ruled that it is competent for the directors of an insolvent Company to present a petition to the court for the appointment of a provisional liquidator without reference to the shareholders (whether prior or subsequent); and that the interest of the Company would either include or exclusively be constituted by the interest of the creditors for the time being; the directors being obliged to act in the best interest of the Company as so defined, the shareholders cannot validity withhold their consent for the directors to present a petition where this was objectively required. Shareholder approval in such circumstances would have no substantive meaning or significance and would merely be a procedural requirement which would frequently impede the Company in taking steps designed to protect its own interests.

For those reasons, the court found that where shareholder approval has no substantive significance in the determination by the directors of an insolvent Company that a winding-up petition should be presented, there was no need for shareholder approval at all. The position would be otherwise in the case of a solvent Company, the vital interests of which cannot be determined

without reference to the shareholders. The general rule that the interests of the Company are synonymous with those of the shareholders on whose behalf all major decisions are taken would come into play in the case of a solvent Company.

The information contained in this note represents the author's view of certain aspects of the decision discussed. This note is not intended to be exhaustive. Legal advice should be obtained in respect of any particular question relating to insolvency law in Bermuda.

For further information on corporate insolvency and related questions, please contact Paul A. Harshaw, Senior Associate at **paharshaw@milligan.bm**.