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Corporate Relocations: Bermuda Group Holding Companies

Preface

This publication has been prepared for the assistance of those who are considering the establishment of a Bermuda company to act as a group holding company where its shares will be listed on a recognised stock exchange. It deals in broad terms with the legal requirements for the establishment and operation of such companies. It is not intended to be exhaustive but merely to provide brief details and information which we hope will be of use to our clients. We recommend that our clients seek legal advice in Bermuda on their specific proposals before taking steps to implement them.

This publication relates only to certain aspects of a corporate relocation. Further publications entitled “Bermuda Exempted Companies” and “Prospectuses and Public Offers by Bermuda Companies” provide additional details on Bermuda law relating to companies and their administration and are available on request.

Before proceeding with the incorporation of a company in Bermuda, persons are advised to consult their legal, tax and other professional advisers in their respective jurisdictions.

Copies of the Bermuda Companies Act 1981, as amended, have been prepared and are available on request.

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1. INTRODUCTION

Bermuda is one of the leading jurisdictions for group holding companies. In many instances the shares of such companies are quoted on stock exchanges around the world including New York, London, Toronto, Hong Kong and Luxembourg.

In general, a corporate relocation will result in a Bermuda company (“Holdings”) replacing the existing group holding company of a jurisdiction other than Bermuda (the “Parent”) with Holdings’ shares becoming held directly by the existing shareholders of the Parent (the “Shareholders”).

The means of implementing the relocation will very much depend upon the existing group structure and commercial requirements applicable to the group. Such relocations are typically carried out (i) by way of a scheme of arrangement under the laws of the jurisdiction of the Parent (in the case of an existing public company) or (ii) as a part of an initial public offering or new issue of shares.

This publication assumes that the Parent’s shares (or at least a significant portion thereof) are widely held.

2. IMPLEMENTATION OF A RELOCATION

The principal statute applicable to companies is the Companies Act 1981, as amended (the “Companies Act”). Holdings will be incorporated by registration under the Companies Act in the usual manner, full particulars of which are set out in our publication, “Bermuda Exempted Companies”, which is available on request. Various documents, including copies of the most recent annual audited financial statements of the Parent, must be submitted to the Bermuda Monetary Authority (the “BMA”) as a part of the application process.

In general, a relocation will involve interposing Holdings by means of a share exchange either (i) above the Parent, that is, between the Parent and the Shareholders or (ii) initially below the Parent and subsequently distributing Holdings' shares to the Shareholders (in this publication referred to as a "reorganisation"). In addition, a relocation may often form part of a public issue of shares.

2.1 Share Exchange

An exchange requires, in effect, that Holdings make an offer to each of the Shareholders with a view to acquiring their shares of the Parent in exchange for shares of Holdings. In order to be successful, such a scheme would generally necessitate acceptance of such offer by 100% of the Shareholders. In some circumstances, therefore, the offer will be structured so as to comply with takeover laws applicable in the jurisdiction of the Parent with a view to being able to force out a dissenting (or apathetic) minority. Alternatively, the offer will be structured as a scheme of arrangement in the relevant jurisdiction under which all Shareholders are bound.

There is no minimum share capital requirement for companies under Bermuda law (other than for insurance companies). Once any amount of the share capital is subscribed for and all requisite organisational meetings have been held, a Bermuda company is generally in a position to commence business. Initial shares of Holdings can be issued to one or a small group of the Shareholders who support the relocation with a view to those shares being included in such persons' allocation of shares on the completion of the exchange. Alternatively, the initial shares of Holdings can be issued to nominees who will transfer the shares to Shareholders as a part of the exchange. Depending upon the commercial requirements, new shares can be issued to new investors and, further, such shares may comprise a separate class of shares.

For simplicity's sake, the proposals will often be structured so that the offer is made on the basis of one share of Holdings for each share of the Parent. Of course, the offer can be made on some other basis depending upon the commercial requirements of each case.

It is common, however, to structure the offer in such a way that a relatively large share premium arises on the issue of the shares of Holdings. This can be achieved by providing for a lower par value of the shares of Holdings than that of the Parent. Alternatively, the number of Holdings shares offered may be less than the number of shares of the Parent to be acquired. For instance, the offer may be made on the basis of one Holdings' share for every ten shares of the Parent.

Once the share exchange is effected, the Shareholders will no longer be holders of the Parent's shares but rather holders of the shares of Holdings. The Parent will be a wholly-owned subsidiary of Holdings.

2.2 Reorganisation

A reorganisation transaction will often be commenced by incorporating Holdings as a subsidiary of the Parent and transferring the Parent's assets to it. Depending upon the nature of the existing corporate structure, it may be possible to effect this aspect of the reorganisation with relative ease.

Often one will structure Holdings such that the aggregate par value of the shares issued to the Parent is less than that of the issued capital of the Parent. The assets of the Parent can be transferred to Holdings either voluntarily or in exchange for the issue of shares of Holdings to the Parent.

The final stages of the reorganisation will be effected in whatever manner is appropriate under the laws of the relevant jurisdiction. In some instances, the shares of Holdings will be distributed to the Shareholders as a dividend. In other cases, the Parent will be liquidated and its only real asset, the shares of Holdings, distributed to the Shareholders *in specie*.

3. PROVISIONS APPLICABLE TO PUBLIC COMPANIES

While Bermuda law contains no express distinction between public companies and private companies, there are certain provisions of the Companies Act, and certain policies of the relevant authorities, which apply specifically to companies whose shares are listed on a stock exchange.

3.1 Branch Share Registers

Where shares of a Bermuda company are listed on an appointed stock exchange or have been offered to the public pursuant to a prospectus filed in Bermuda, the company may keep one or more branch registers outside Bermuda. Notice of the establishment of such a branch register must be given to the Registrar of Companies in Bermuda. Where a branch register is established, the principal register of members of the company located at the registered office in Bermuda must be updated as soon as reasonably practicable.

3.2 Prospectus Requirements

Where a Bermuda company seeks to offer its shares to the public, the company will generally be required to comply with the prospectus provisions of the Companies Act. Unless the company's shares are already listed on an appointed stock exchange (which includes most of the world's major exchanges), or accepted by a competent regulatory authority (which includes the U.S. Securities and Exchange Commission), any company proposing to offer shares to the public must produce a prospectus and file it with the Registrar of Companies. The Companies Act specifies certain information which must be contained in a prospectus. Bermuda's prospectus content requirements rarely pose any practical problems for a Bermuda public company, since the company will invariably produce a prospectus that will be approved or accepted by an appropriate authority or exchange in the jurisdiction in which its shares are listed.

3.3 Securities Clearances

In general, a Bermuda company must obtain the prior approval of the BMA for any issue or transfer of its shares to non-residents of Bermuda. However, this restriction, which would otherwise be unworkable for a publicly traded company, has been eliminated by the BMA's "blanket" permission for the issuance and free transferability of all shares of a publicly listed Bermuda company as long as the company maintains its listing on an appointed stock exchange.

3.4 Staggered Board

The Companies Act allows for a company's bye-laws to establish any manner in which the shareholders are to elect the company's directors and to set any term for such directors to serve. This allows the bye-laws to stipulate that only a percentage of the company's directors are to be elected each year. Further, the bye-laws may provide that the board (rather than the shareholders) may fix the size of the board from time to time, and appoint directors to fill any vacancies resulting from an increase in the size of the board. Since the Companies Act also allows the bye-laws to restrict the shareholders' ability to remove directors, these provisions can be highly effective tools to discourage a hostile takeover.

3.5 Poison Pill

Similarly, the US practice of adopting "poison pill" rights plans is designed to encourage potential acquirers to work with a company's board. While not common among Bermuda companies, poison pills are nevertheless quite often adopted by the boards of Bermuda public companies.

4. GENERAL PROVISIONS APPLICABLE TO COMPANIES

The following provisions of the Companies Act are of general application to exempted companies incorporated in Bermuda.

4.1 Memorandum of Association & Bye-laws

The constitutional documents of a Bermuda exempted company consist of its certificate of incorporation, memorandum of association and bye-laws. The certificate of incorporation and memorandum of association are on file with the Registrar of Companies. They are a matter of public record and available for inspection by the public at the offices of the Registrar.

The memorandum of association must state that the liability of its members is limited to the amount (if any) for the time being unpaid on the shares respectively held by

them. The memorandum of association will also provide that the company's objects are unrestricted or will set out the specific objects of the company.

The memorandum of association and bye-laws of a Bermuda company may be amended. If amendments to the memorandum of association will allow the company to carry on restricted business activities, consent of the Minister is required. Any amendment to the memorandum of association must be approved by the company in general meeting. The bye-laws may be amended by the directors, subject to the approval of the shareholders of the company in general meeting in accordance with the terms of the bye-laws. The bye-laws can provide that a special resolution (i.e. a resolution greater than a simple majority) is required to amend the memorandum of association or the bye-laws.

Once approved, the amended memorandum of association must be registered with the Registrar of Companies.

4.2 Purchase of Shares by Companies

A company, if authorised by its memorandum of association or bye-laws and subject to certain requirements, may purchase its own shares. Such purchases may be effected out of the capital paid up on the purchased shares, profits otherwise available for dividends or out of the proceeds of a new issue of shares made for that purpose. Any premium paid on purchase over the par value of the shares must be provided for out of profits otherwise available for dividends or out of the company's share premium account. Such purchase may not be made if, on the date on which the purchase is to be effected, there are reasonable grounds for believing that the company is, or after the purchase would be, unable to pay its liabilities as they become due. The shares so purchased may be held as treasury shares (if treasury shares are explicitly permitted under the bye-laws) or otherwise will be cancelled, in which case the company's issued (but not authorised) capital shall be diminished accordingly. Shares purchased are available for re-issue.

4.3 Dividends and Distributions

A Bermuda company will have funds available to declare and pay a dividend or distribution only if it satisfies the requirements of the Companies Act, which are designed to ensure that creditor claims are not prejudiced by payments of dividends or distributions.

Under the Companies Act, a company shall not pay dividends, or make a distribution out of contributed surplus, if there are reasonable grounds for believing that (a) the company is, or would after the payment be, unable to pay its liabilities as they become due or (b) the realisable value of the company's assets would thereby be less than its liabilities. For this purpose, contributed surplus includes proceeds arising from donated shares, credits resulting from the redemption or conversion of shares at less than the amount set up as nominal capital and donations of cash and other assets to the company. Accepted approaches to determine realisable value include valuing assets using a mark to market approach, obtaining a professional valuation or using generally accepted accounting principles.

4.4 Protection of Minorities

Class actions and derivative actions are generally not available to shareholders under Bermuda law. The Bermuda courts, however, would ordinarily be expected to permit a shareholder to commence an action in the name of a company to remedy a wrong to the company where the act complained of is alleged to be beyond the corporate power of the company or illegal, or would result in the violation of the company's memorandum of association or bye-laws. Furthermore, consideration would be given by a Bermuda court to acts that are alleged to constitute a fraud against the minority shareholders or, for instance, where an act requires the approval of a greater percentage of the company's shareholders than that which actually approved it.

When the affairs of a company are being conducted in a manner which is oppressive or prejudicial to the interests of some part of the shareholders, one or more shareholders may apply to the Supreme Court of Bermuda, which may make such order as it sees fit, including an order regulating the conduct of the company's affairs

in the future or ordering the purchase of the shares of any shareholders by other shareholders or by the company. Bermuda law also provides that a company may be wound up by the Bermuda court if the court is of the opinion that it is just and equitable to do so. Both these provisions are available to minority shareholders seeking relief from the oppressive conduct of the majority and the court has wide discretion to make such order as it may think fit.

Except as mentioned above, claims against a company by its shareholders must be based on the general laws of contract or tort applicable in Bermuda.

A statutory right of action is conferred on subscribers of shares in a company against persons (including directors and officers) responsible for the issue of a prospectus in respect of damages suffered by reason of an untrue statement therein but this confers no right of action against a company itself. In addition, a company itself (as opposed to its shareholders) may take action against its directors and officers for breach of their statutory and fiduciary duty to act honestly and in good faith with a view to the best interests of a company.

4.5 Management

The Companies Act has no specific restrictions on the power of directors to dispose of the assets of a company. It does, however, require that every director and officer shall, in exercising his or her powers and discharging his or her duties, act honestly and in good faith with a view to the best interests of the company and that he or she shall exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. In addition, every director and officer must comply with the Companies Act, the regulations made thereunder and the bye-laws of the company.

4.6 Requirements for Officers or Representatives in Bermuda

Each Bermuda exempted company is required to have at least one director and a secretary. A director of an exempted company may be an individual or any legal person (including any company or association or body of persons, whether corporate

or unincorporate). For practical reasons, it is most common for the office of director to be filled by an individual or a company.

To satisfy the residency requirement contained in the Companies Act, the secretary or at least one director must be ordinarily resident in Bermuda. A company may satisfy the residency requirement by appointing either an individual or a company to act as its resident representative in Bermuda.

4.7 Accounting and Auditing Requirements

The Companies Act requires a company to cause proper records of account to be kept with respect to (a) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place; (b) all sales and purchases of goods by the company; and (c) the assets and liabilities of the company. The records of account must be kept at the registered office of the company or at such other place as the directors think fit and at all times must be open to inspection by the directors or the resident representative. The records of account must be kept for a period of five years from the date on which they were prepared.

All members of a company are entitled to receive a copy of every financial statement prepared in accordance with these requirements at least five days before the general meeting of the company at which the financial statements are to be tabled. If the company has, by resolution of the members, elected to waive the requirement for an annual general meeting, the financial statements must still be made available to the shareholders within the prescribed time limit.

5. TAXATION AND EXCHANGE CONTROL

5.1 Taxation

At the date of this publication, there is no Bermuda income or profits tax, withholding tax, capital gains tax, capital transfer tax, estate duty or inheritance tax payable by a Bermuda company or its shareholders, other than shareholders ordinarily resident in Bermuda.

An exempted company may apply for and is likely to receive from the Minister of Finance of Bermuda under the Exempted Undertakings Tax Protection Act, 1966 an assurance that, in the event of there being enacted in Bermuda any legislation imposing tax computed on profits or income, or computed on any capital assets, gain or appreciation, or any tax in the nature of estate duty or inheritance tax, such tax shall not until March 2035 be applicable to the company or to any of its operations or to the shares, debentures or other obligations of the company except insofar as such tax applies to persons ordinarily resident in Bermuda and holding such shares, debentures or other obligations of the company or any land leased or let to the company.

No stamp duty is payable with respect to any instrument executed by an exempted company or in respect of an instrument relating to an interest in an exempted company. Stamp duty may, however, be payable in respect of transactions involving Bermuda property.

An exempted company is required to pay a fee in Bermuda at the time of its incorporation and in January of each year thereafter (if incorporation occurs after 31st August in a year, the fee is reduced by half for that year). The fee is provided for on a sliding scale and based upon the company's authorised share capital. For a current listing of government fees, please contact Conyers Dill & Pearman.

5.2 Exchange Control

Bermuda is independent for the purposes of exchange control which is operated under the Exchange Control Act 1972 and related regulations.

Exempted companies are designated non-resident for exchange control purposes. The non-resident designation allows such companies to operate free of exchange control regulations and enables them to make payments of dividends, to distribute capital, to acquire, hold and sell any currency and foreign securities without reference to the BMA.

This publication should not be construed as legal advice and is not intended to be relied upon in relation to any specific matter. It deals in broad terms only and is intended merely to provide a brief overview and give general information.

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