

ALDERNEY COMPANY LAW REFORM COMMITTEE

Presentation

Consultation Project Paper

Introduction

Alderney is a small island economy which has its own legislative and legal systems governing business associations, loans, investments, securities and insolvency.

Much of the legal structure on which the economy is based does not optimise the conditions necessary to support the effort, energy, ingenuity and productivity of those involved and resident on the island, nor does it comply with accepted standards for the wider corporate and investment community. It is broadly recognized that the momentum of established businesses and the attraction of new innovative activity are not, of themselves, giving best possible benefit to the island and its population. The paradigm case is that insolvency of an established business leads to redundancy and dereliction of property¹ rather than to renewal and recapitalisation. Much of this is not only because of inefficiency and cost of the physical infrastructure such as transport, but also because the legal environment² in which the island works does not provide secure, cost-effective and efficient mechanisms for raising the funds necessary to build on the capital wealth of the island and its population. This inadequacy of the island's antiquated legal environment is one that should not be a necessary consequence of island life on Alderney with the availability of efficient and cheap worldwide electronic, audio visual, and virtual communication and its geographical position adjacent or close by the metropolitan areas of the UK and European Union, particularly at a time of sharply falling fuel prices.

Given that the physical infrastructure is capable of being upgraded and transport and electronic communication systems can be put right, this Consultation Project Paper has been commissioned by the Alderney Company Reform Committee (the "Committee"), a sub-

¹ e.g. the Chez, The Albert, Rea's Bar, The Georgian a year or two ago, the clothing shop on Braye Street and various other businesses.

² The existing legal framework and the accessibility to necessary legal advice.

committee of the Policy and Finance Committee of the States³ to set out the objectives to update and reform the relevant parts of the law to produce a legal infrastructure which will be fit for purpose to give the islanders an economical and encouraging business environment in which they can exercise their ingenuity and talent to bring economic success to the island.

It can be widely understood that the physical infrastructure⁴ requires the backing of an efficient set of laws which accord with the island's needs including those which our external partners across the waters and as part of the international community require as minimum standards regulating our environment and our interchange with them. The essential components of a legal infrastructure that will support the operation of the economy includes efficient and low cost business organisations, security and finance facilities and an insolvency system backed by good available "on island" low cost legal advice and business assistance.

These requirements derive their thrust from the fact that our small island needs an efficient, modern, low cost legal structure ideally better and more economical than those enjoyed by the island's partners so that our island attracts new businesses. A legal system that enables and encourages investment and improvements will ensure our island does not fail and become reliant on benefits granted by others.

The legal structure that we are analysing for cost effectiveness and compliance with modern business and community project requirements covers the following areas:

- 1) Alderney Company Law (including public/private entities carrying out projects on or for the island).
- 2) Alderney Finance and Security Law relating to raising money for business and island projects both in the private sector and through public and private project initiatives with clarification of the Alderney government's powers to participate in such projects in such ways as the community may need.
- 3) Alderney Insolvency Law providing enterprises and the island with an accessible, low cost, efficient method of quickly turning round failing ventures or recycling capital

³ Robert McDowall (States of Alderney), Victor Brownlees (Alderney Chief Executive), Peter Castle (Chancery Barrister and Bencher of Lincoln's Inn London).

⁴ Property dedicated to residential, business, historical/modern, farm, recreational, sport etc, aircraft runway(s), quay(s), roads, water, electricity, power, telephonic/wireless and similar communication purposes.

into new ventures thereby keeping “down time” to a minimum and stopping creeping dereliction of property and loss of jobs.

- 4) Accessibility on island of competitive low cost, legal and business advice as required by a modernised legal system.

The Law of Business Associations: the Alderney Company

The Faculty of Laws, University College London (Dr Iris H-Y Chiu, Dr. Martin Petrin and Ms Anna Donovan) provided a study of Alderney Company Law and produced an important report (with assistance from members of the Committee and the Greffier of the Court of Alderney), entitled “Gap Analysis of UK and Alderney Company Law” (the “Analysis”). Following is a summary of some of the central parts of the Analysis, a copy of which is obtainable upon request from the States of Alderney.

The Analysis states on page 4 that if Alderney wishes to engage in the arena of competition for global incorporations, a balanced approach must be taken to meet both the needs of business and the demands of the global investment and financial management sector. Subjects for review would include among other things shareholder powers in the general meeting, shareholder remedies, directors' duties and corporate transparency. Furthermore, efficient structures of capital management and company dissolution could be adopted. If full advantage is to be taken of central filing and electronic corporate registers, incorporation and registration of shares, securities and other corporate registrations can be fully streamlined and available to all companies.

The Analysis emphasises key areas for review with respect to the Alderney Company Law where important matters contained in the UK companies' legislation are ignored or only partially dealt with in Alderney Company Law or where modern modes of communication and recording could be adopted for Alderney to its great advantage.

The Analysis (which should be referred to for greater detail) deals with the following areas:

- *The Definition of 'Public Company'*

- *Simplification of Company Constitution and Reform of Incorporation and Register Services*
- *Enhancing the Legal Framework for Corporate Governance*
- *Directors' Duties and Liability*
- *Enhancements in Corporate Transparency*
- *Enhancing the Legal Framework for Corporate Governance*
- *Facilitating Shareholder Participation and Voting at General Meetings*
- *Share Capital and Distributions*
- *Debentures*
- *Takeovers, Mergers, Divisions and Schemes of Arrangement*
- *Corporate Resolution, and*
- *Creditor Enforcement*

The Analysis identifies that the UK corporate economy is very much based on public or traded companies while Alderney's economy at present is mainly comprised of small private businesses. Despite the differences between the island economy and that of the UK, the Analysis suggests that international trends are increasingly bringing island jurisdictions such as Alderney into contact with international corporate investments and therefore the UK company law provides a good comparison. Nevertheless, the Committee believes that other island jurisdictions should be looked at as well for appropriate solutions. It is essential, however, in the modern world that Alderney obtains and retains a good reputation as a genuine and fair jurisdiction both for the business community, for the companies already incorporated on the island such as in gaming, and for the future development of its economy and expansion of its links from over the water.

The Analysis identifies a clear need for reform (a) for the needs of the business community on Alderney and (b) for the needs of the investing community to catch up with mainstream company and corporate law as practised worldwide. It is considered that UK Company Law as a result of the familiarity of the nearby London corporate investing community lends itself to being an important guide to what Alderney Company Law should provide. That is not to suggest that there are not significant areas where Alderney Company Law cannot take its own direction to facilitate company management. For example, by improving the electronic methods for interface with general meetings, for company incorporations, accounts filings, registration of

shares and share rights, shareholder disputes, unfair prejudice, derivative proceedings, maintenance of securities and similar registers, securities disputes both with the company and between security holders inter se.

The Committee believes that, like in the UK, such company matters can be managed without requiring the involvement and added expense of a legal fiduciary professional⁵ or other analogous legal professional, particularly as there are no existing on-island Alderney legal practices. At present Alderney Law fails to provide by law for instruments, contracts, transactional and other documents to be recognised in electronic form and as legally binding with electronic signatures or for filings to be made electronically. Moreover, legal advice is not readily available otherwise than at a distance, from the Guernsey Bar. The failure to make use of modern electronic facilities in the most advantageous way and the necessity of obtaining legal advice from one off-island bar ratchets up the cost of doing business on Alderney unnecessarily and falls behind international practice. Besides, with respect to Companies, Securities and Insolvencies, different laws are in force in Alderney from those in Guernsey. The Committee proposes to adopt a much more extensive but more economic administrative structure for what is largely registry work operated by a system of electronic filing for company reports, shareholder rights, security registration and other documents and also making provision for voluntary reduction of capital, and similar changes accompanied by appropriate valuations and other evidence generally without the need for court hearings, but with the facility to conduct any hearings required over video link where necessary.

The Committee further proposes that where professional legal assistance is required, such assistance for an Alderney Company should (on payment to the Alderney Companies Registry of a prescribed annual fee) be able to be provided by any advocate or barrister or solicitor qualified to practise as advocates in the various parts “Designated Jurisdictions” of the British Islands⁶ and who have so practised for a period of 5 years and that the Companies Registry shall admit such persons to conduct such business, and the Alderney Companies Registry shall also have authority to admit barristers, solicitors and such other persons who appear to the Registry as having equivalent experience from any other common law jurisdiction together with insolvency practitioners and chartered or similarly qualified accountants having equivalent

⁵ Corporate Services Provider with full fiduciary licence from the Guernsey Financial Services Commission.

⁶ Bailiwick of Guernsey, Jersey and Isle of Man, England and Wales, Northern Ireland and Scotland i.e. the jurisdictions, countries and territories to which section 426 of the UK Insolvency Act 1986 applies by being extended by Order in Council (“the Designated Jurisdictions”).

experience. It would be incumbent on the Companies Registry to maintain a list of those having paid the fee for the current year and who are therefore entitled to practice before them.

Alderney Finance

The Law of Security Interests

The Committee has considered the following impediments to the operation and development of Alderney businesses, as summarised below and set out in the paper commissioned for the Policy & Finance Committee of the States of Alderney, entitled “Key Objectives of Alderney Business Insolvency Law: Building Capital for Economic Growth” *prepared for the Committee 16 December 2015*.

- It is of the essence that a business must be able to obtain, at low cost, cash as working capital for its operations by using all its assets including stock and intangible benefits arising from the business on an operating or continuing basis to provide security for loans and investments. Otherwise, a commercial enterprise cannot survive and will ultimately “die” to the detriment not only of the owners and investors of the business, but also of the community to which the failed business provided jobs, tax revenues and collateral business opportunities (e.g., suppliers and tradesmen).
- Enterprise finance will not and cannot be made available at a reasonable cost without a transparent security and insolvency system that will fairly protect the diverse interests of lenders, investors, and borrowers should the business fail. For solvent companies, the ability to use the going concern value of the business to raise capital by way of a floating charge encourages growth and development of the enterprise. In the case of a distressed company, it is to the advantage of the entire community that the company’s business and assets be available for the creditors, investors and borrowers to use to restructure the company’s historical debt so that the value of the business and its assets are preserved, including jobs, tax revenues, repayments of loans over time and returns on investments.

- Given that a commercial business consists generally of fixed and circulating capital with stock, it is a requirement that adequate economic resources should be available for business operations and that the law should protect the respective rights of the company, its investors, and its lenders and trade creditors.
- The applicable Alderney Laws are defective because there is no easily referenced law enabling a business to raise money for its operations, growth or development using as security the business's stock, working capital or fixed assets. Without laws establishing a clear and certain security framework for lenders, the risk to a lender is great in the event a business should fail. Thus, in such circumstances banking and lending institutions are reluctant to lend or otherwise fund a business venture as the business cannot cheaply and with certainty make its going concern value, including assets, goodwill and stock, available to stand as a form of secure collateral for a loan to the business. To reduce the risk to lenders and thereby reduce the costs of business loans and credit, there should be a procedure for the simple registration of security over a business's property on a floating basis, to include all forms of business property such as goodwill, stock and everything that makes up a going concern value, which would provide a lender with certainty as to the enforceability of their security interest and of their priority vis a vis other lenders/creditors. There is no such provision within the Alderney Law.
- Under existing Alderney Law, security over a moveable asset requires either possession or reservation of title by the lender so that intangibles and stock associated with the on-going business are unavailable for the business enterprise to use to raise capital to operate or improve the business. Only a facility agreement enforceable personally (which does not give security over the collateral itself) is available which is legally no more secure than a personal contract. Thus, there is no equivalent to the floating charge or lien effective as a security over stock and good will and other intangibles of a continuing business. The absence of such a tool which has been a part of the bedrock of the commercial success of many countries particularly the UK and the USA during their respective industrial revolutions makes the raising of cash for the ongoing business more costly and problematic than it should be for both borrower and lender.

- Under the separate laws of each part of the Bailiwick of Guernsey security has traditionally been in essence by pledge, which effectively requires possession to be taken by the security holder. Although Guernsey Law does make further provision for security agreements that they should be in writing and provides for security to be created over bank accounts and that the security can be enforced or sold under court order, it too falls short of providing adequate certainty to lenders.⁷ Alderney, however, does not even appear ever to have passed a statute equivalent to the Security Interests (Guernsey) Law and accordingly in Alderney the matter appears to rest on the additional uncertainty of local common or customary law.
- In a business context, as a result of the foregoing, it is difficult and more costly than it should be to raise capital for business enterprises and projects on Alderney because the legal system's defects prevent businesses from using their assets and work product as security to support their acquisition of the capital they require to continue and expand their operations.
- Alderney Companies operating in the commercial environment frequently are engaged on projects developed or initiated by the government of Alderney, under policy decisions made by the island's democratic organ, the Alderney States. The States should develop a clear legislative legal statement of its powers to raise and advance finance by way of facility, guarantee or any other appropriate method in order for it to fund and engage in or participate with others in public and private initiatives or projects.

The Law of Insolvency

- The Law of Alderney regarding insolvency is both antiquated and undeveloped. There is no equivalent of reorganisation or administration under the Enterprise Act of the UK, indeed there are no laws that encourage or facilitate reconstruction or rescue at all. There is no legal structure which encourages the business lenders or investors to advance further money for working capital needs while a distressed business is

⁷ Security Interests (Guernsey) Law 1993.

reconstituted or reconstructed rather than liquidated, leading to inevitable closure and liquidation of the business and to the loss of its value to the island. The currently existing sources of law and related rights and remedies which underpin the Law of Alderney regarding insolvency may be summarised as follows:

- *Customary law (Norman): En desastre (“in disaster”) and saisie (“seizure” i.e. “arrest”).*
- *Voluntary liquidation with NO creditor involvement even where the business is insolvent.*
- *Compulsory liquidation.*

Case studies are not available, but a common problem in Guernsey which has similar law, is that businesses operate without adequate working capital. This inadequacy cannot easily and cheaply be remedied through borrowing and other forms of capitalisation on a floating charge or lien because as noted above, such legal financial securities are not recognised. This discourages or makes more costly or difficult the raising of finance through borrowing money and obtaining other funds secured by the going concern value of the business because creditor priorities and security laws do not adequately protect lenders whose loans are not secured by liens on other types of property, pledges secured by possession, or personal guarantees. Thus, both start ups and established enterprises have no low cost way of raising cash and require the proprietors to maintain unused resources as a standby instead of a business loan.

Upon insolvency, the paradigm case on Alderney where working capital is inadequate is a breakup of the distressed business and a sale of its assets in an uncontrolled liquidation, accompanied by removal of the premises/site from participation in Alderney’s business zone for a longer or shorter period of time to the detriment of the community as a whole, e.g., loss of tax revenue and loss of jobs. Because there is no restructuring or rescue legislation or, at a stage before insolvency, any government finance scheme or initiative, there is no alternative to closing down a distressed going concern with the loss of all of the benefits the business has built up over time. The inability of distressed businesses to restructure their debts is to the detriment of Alderney because liquidations result in the loss of jobs (frequently resulting in

emigration from the island), loss of tax revenues, banks are discouraged from lending or even considering lending to Alderney businesses, and economic activity is reduced generally.

Alderney Law governing creditor and investor priorities also appears to the Committee to be defective and uncertain due to drafting contradictions and errors in the legislation. Under the Preferred Debts Laws, priorities in an insolvent winding up are governed by an extremely simplistic list of debts having priority to be paid out of the assets of the insolvent company, largely comprised of certain rents and wages.⁸ However, under section 135 of the Companies (Alderney) Law 1994, save for rules of law regarding “*preferential payments*”, the assets are divisible pari passu. Section 135 therefore wholly conflicts with the Preferred Debts legislation in that preferential payments are very different from preferred debts, as preferential payments have nothing to do with creditor priorities at all and are simply unlawful payments made within 6 months of the commencement of liquidation, which must be repaid to the estate. This conflict in the laws creates uncertainty and must be resolved for the legal position with regard to priorities and preferential payments to be made clear to both borrowers, lenders, and trade creditors.

In practice, a business in Alderney has to terminate all of its employees, close up the premises, and then conduct an *ad hoc* auction and/or “*ring round the island*” for interest in the remaining goods and stock (assuming the stock was not encumbered at the time of purchase with a “*retention of title*” clause that requires the business to return stock back to the seller).

There is no requirement for liquidators or other officials to be insolvency practitioners or to have any experience in the field. In Guernsey, while the legal position is the same, the liquidators and administrators will generally be experienced insolvency practitioners: a difference arising from the absence of established legal practises with relevant experience wishing to practice Alderney Law on the island of Alderney. Given that those insolvency practitioners on Guernsey will have been trained in relation to the law of England and Wales, Guernsey frequently has resort to the precedents and rules of the Insolvency Service in the UK, which include a series of Statements of Insolvency Practice (“SIP’s”) providing guidance in many fields some of which have been adapted for Guernsey, including Voluntary

⁸ Preferred Debts (Guernsey) Law 1983 and Preferred Debts, Desastre Proceedings and Miscellaneous Provisions (Guernsey and Alderney) Law 2006

Liquidation (SIP3) and Voluntary Administration (SIP16), which includes pre-packs for sales of businesses on a going concern basis when pre-agreed with the purchaser and creditors before the proceedings are issued. There does not seem, however, to be any established practice for a “pre-pack plan” for use in Guernsey in the nature of a work out with a stay while the debts are discharged over time. The Committee wishes to encourage on Alderney a rescue/work out culture for the economic good of the island. The various national depressions were seminal events that were instrumental in making countries realise that business closures under the liquidation insolvency model failed to preserve business, jobs and economic activity to the detriment of the regional communities. It was this that spurred the introduction of the rescue culture led by the new bankruptcy codes which favoured the rescue model whereby wherever possible the debts would be paid off over time by a continuation of the business. The Committee proposes that Alderney introduces insolvency laws which with the leadership of the Insolvency Master, will favour the continuation of established distressed businesses and the payment of debts over time wherever possible.

a. Insolvency in the United Kingdom, Guernsey, Jersey and the Isle of Man

Alderney as part of the Channel Islands has jurisdiction under section 426 of the Insolvency Act 1986 of the UK to enforce insolvency orders issued by courts in the UK, the Bailiwick of Jersey, and the Isle of Man (the “Designated Jurisdictions”) in Alderney as if they were made in Alderney, by virtue of the Insolvency Act 1986 (Guernsey) Order 1989 (“Order 1989”), extending subsection 4, 5, 10 and 11 of section 426 to the entire Guernsey Bailiwick. In the case of *The Liquidator of Seagull Manufacturing Co Ltd v Colin and Susan Slinn*, Guernsey Court of Appeal, August 1991, it was held that subsection 5 is applicable in Guernsey, but by implication this will in practice bind all of the Channel Islands which are subject to the Channel Islands Court of Appeal. As noted above, it is proposed by the Committee that in respect of company work on Alderney, the practitioners from each of these jurisdictions should be permitted to practice as it is expedient and economic to use the full resources and experience of all the bars of these jurisdictions who will be involved with what are broadly common issues and with the added advantage of broadening the solutions that will be brought to the legal table.

b. Cross Border Insolvency

The UNCITRAL Model Law has been adopted by many modern commercial jurisdictions, including for example the UK, the USA, Australia, New Zealand, Canada, and the British Virgin Islands. The Model Law promotes certainty and in turn economic growth because it provides a common terminology and procedure that international lenders and investors can rely upon and consider when assessing their lending and investment risks in the event of business insolvency. Considering that “*no man is an island unto himself*”⁹, it would enhance Alderney’s commercial reputation and economic growth to have a statutory insolvency regime for cross-border reciprocity when dealing with jurisdictions outside the scope of Order 1989.

The Committee proposes that Alderney should move to adopt the UNCITRAL Model Law (in a form appropriately tailored to Alderney’s proposed reformed Company Law), notwithstanding that Guernsey has not done so and appears to have no plans to do so.

c. Insolvency in Alderney

Alderney has an insolvency jurisdiction, but does not appear to have specialised Insolvency or Court Rules to deal with the insolvency jurisdiction of the Alderney Court. The Committee proposes that as the absence of such rules creates uncertainty in the rights and remedies upon which borrowers and lenders must rely in the event of a borrower’s insolvency, this omission should be remedied with respect to Alderney’s proposed Companies Registry and Company Insolvency Office by the respective officials.

The Committee proposes further that the Alderney Court jurisdiction over Companies, Company Securities and with respect to Insolvency matters be exercised by the proposed Companies Registry and Insolvency Master.

d. Creditor Rights

Creditor interests and rights vis-a-vis the borrower and amongst creditors have until now been (largely) ignored, save in respect of the class of creditors whose claims are for certain rents and wages (mentioned in note 7 to the text above). The Committee considers that in all

⁹ Which might be rephrased as “No island is an island sufficient unto itself”.

Company based cases of insolvency or doubtful solvency, the creditors should be recognised as having a right to be involved in the process as do the company and its owners.

The accessibility of legal advice on Alderney

The accessibility of professional legal advice on Alderney is particularly problematic as there appears to have never been a particular interest in established commercial legal practices to set up offices on the island. This accessibility problem of the relevant professional advice coupled with the requirement that company incorporation documents must be “signed off” by quasi-lawyers (corporate services providers with a full fiduciary licence granted by the Guernsey Financial Services Commission.) is not cost effective for Alderney. Effectively, obtaining legal advice requires either the visit of a commercial lawyer to the island or the shipping of documents and clients off island. Moreover, the corporate management businesses on Alderney themselves have to resort to legal advice off island at a cost both in time and expense. All these requirements raise the transactional cost for no sufficient reason and in some cases may cause the company transaction to “go without” when it is needed.

If Alderney takes full advantage of expanding its company and insolvency capabilities with full reliance on modern secure electronic forms of communication and the introduction of notarised documents from other partner jurisdictions, the problem of the extra cost of professional advice can be remedied by introducing a comprehensive system whereby all company and insolvency business can be carried through electronically and providing a procedure for recognition of practicing rights by the Companies Registry and Company Insolvency Office.

Objectives

Introduction of a new cost effective and user friendly commercial legal structure with the following objectives:

- a. Enhancement of efficiency and reduction of the costs of company formation and administration for company promoters, directors and administrators.*
- b. Introduction of legal processes and administration for securitisation of company assets, through adoption of UK Law and practice on the subject as modified for Alderney's needs.*

- c. Replacement of the very antiquated legislation on insolvency with a legal regime which reflects contemporary law in the UK and Designated Jurisdictions on corporate insolvency and corporate reconstruction.*
- d. Improvement of shareholder rights consistent with current practice in Common Law.¹⁰*
- e. Adoption of all modern means available to introduce a fully automated company and insolvency registry practice economically and at low cost to the advantage of both the users and the island community in general.*

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¹⁰ Excerpts from Committee Minutes of meeting held on 10 December 2015.