

Corporate governance in the Turks & Caicos Islands

Misick & Stanbrook

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Overview of recent corporate governance reforms

The Turks & Caicos Islands (TCI) is a British overseas territory and a zero-tax jurisdiction. Its law is a mix of English common law, some UK statutes which have been extended to TCI, and local ordinances. The usual TCI corporate vehicle for international business is the exempted company limited by shares, commonly known as an IBC, and the law discussed in this chapter relates to IBCs.

TCI has an extensive regulatory regime covering almost all aspects of the local financial industry designed to impose financial, professional and corporate governance standards. Banks, company formation agents, insurance companies (including insurance managers, brokers and agents), trust companies, investment dealers and mutual fund administrators are subject to stringent licensing and regulatory requirements.

The basic regulations governing banks, insurance companies and professionals, and trust companies have been in place since the early 1990s. Additional regulation of company formation agents, investment dealers and mutual fund administrators has been introduced in recent years, along with more stringent anti-money laundering provisions, limitations on banking and corporate secrecy laws, and structures for the exchange of information with overseas regulatory agencies.

These changes have come about in response to both local needs (regulation of investment dealers) and the influence of international organisations such as the Organisation for Economic Cooperation and Development (OECD), the Financial Action Task Force (FATF) and the International Monetary Fund (IMF), and their worldwide campaigns to expand financial and corporate transparency and promote better corporate governance. Those reforms have included the following:

- the establishment of TCI's main financial regulator, the Financial Services Commission, as an independent statutory body with its own funding;
- the enactment of statutory provisions to immobilise bearer shares in TCI companies;
- the enactment of stringent anti-money laundering provisions in the Proceeds of Crime Ordinance and subsidiary legislation, and the establishment of the Money Laundering Reporting Authority. The legislation is broadly similar to all-crimes money laundering legislation

in the United Kingdom and in other British overseas territories;

- the enactment of the Overseas Regulatory Authority (Assistance) Ordinance 2001. This authorises the licensing committee of the TCI Financial Services Commission to assist an overseas regulatory authority in the exercise of its regulatory functions. Regulatory functions do not include “functions directly or indirectly relating to assessing, imposing or collecting taxes of any kind”. In qualifying circumstances, that assistance may extend to requiring a TCI company manager to disclose the beneficial owners of IBCs. The ownership of a TCI IBC is not a matter of public record, and so these provisions are calculated to enhance financial and corporate transparency;
- the imposition of greater due diligence/know-your-client requirements on company managers and formation agents. While there is no obligation in the ordinary course to disclose beneficial ownership of TCI IBCs to unauthorised third parties, TCI company managers are now statutorily obliged to retain on file details of beneficial ownership of companies for which they provide a registered office, including notarised photo identification, references and address confirmation;
- the response to OECD, FATF and other international initiatives. In a March 2002 letter to the OECD, TCI’s then chief minister committed TCI to the principles of effective exchange of information in tax matters and transparency. The chief minister emphasised that the establishment of a level playing field among all the OECD member countries, and also those non-member jurisdictions with which it is materially in competition in the provision of cross-border financial services, was essential; TCI was, he said, determined to protect its economic interests and fiscal autonomy, and the issue of developing and maintaining a level playing field was critical to those interests. In common with most zero-tax

financial centres, TCI was recently reviewed by the IMF. The findings have been disclosed to the TCI Financial Services Commission and are currently under discussion. The findings, and the TCI response to them, have not yet been made public.

TCI has been satisfactorily reviewed by the FATF and has never appeared on any FATF black list; and

- the EU Savings Tax Directive. In line with other British overseas territories, TCI will be subject to this directive and is likely to impose a withholding tax on the accounts affected. TCI is not a major centre for the holding of international funds (although TCI corporate entities are widely used internationally), and the directive is therefore not expected to have a major impact on the territory.

Shareholders’ rights

Right to call meetings

Shareholders holding not less than 15 per cent of the issued shares are entitled to requisition a general meeting to propose a special resolution. Sometimes, the articles of association (bylaws) of the company will allow the requisitioning of a meeting by a smaller number.

Quorum and voting requirements

This is dictated by the articles rather than by statute. Typically, the quorum requires the presence (in person or by proxy) of the holders of not less than 50 per cent of the outstanding voting shares.

Decisions requiring more than majority approval

The following decisions require a special resolution (75 per cent approval of the shares represented at the meeting):

- alteration of the articles;
- change of the company’s name;
- appointment of an inspector to examine the company’s affairs;

- decision by the members to have the company wound up by the court;
- decision by the members to have the company wound up voluntarily;
- delegation to creditors of the power to appoint a liquidator;
- entry into any arrangements with respect to the powers to be exercised by the liquidator;
- any arrangement between a company about to be wound up voluntarily and its creditors;
- a decision as to the disposal of the books, accounts and documents of the company where the company has been wound up voluntarily;
- certain payments to and compromises with creditors in a voluntary winding-up;
- sale of business or property of a company in, or proposed to be in, voluntary liquidation in return for shares or interests in the acquiring company;
- a decision by the company to be bound by provisions of the Companies Ordinance from which it is otherwise exempt;
- alteration of the memorandum of association (charter);
- a decision to be treated as an ordinary TCI company;
- purchase by the company of its own shares, if the articles do not otherwise authorise the manner of purchase; and
- a decision by a limited life company to extend its duration.

Right to propose resolutions for adoption

Fifteen per cent of the shareholders, exercising their statutory power to requisition the meeting, can do

so for the purposes of proposing a special resolution. Otherwise, shareholders' meetings are governed by the articles. These will typically allow the proposal of resolutions by shareholders.

Right to question directors, officers and auditors

Shareholders have the right to question directors and officers at shareholders' meetings. While all companies are obliged to keep proper accounts, there is no statutory audit requirement.

Nomination and election of directors

The shareholders, in accordance with the voting rights attached to their shares, elect the board.

Right to inspect corporate records

Shareholders have a right to inspect the register of members and the register of directors and secretary. Shareholders holding not less than 15 per cent of the shares of the company may apply to the court for the appointment of an inspector of the company's affairs. The directors and officers are obliged to provide all books, accounts and documents relating to the company to the inspector, who is entitled to examine the officers and agents of the company under oath. The members may, by special resolution (without application to the court), appoint an inspector who will have the same powers as one appointed by the court.

Initiation of litigation

Shareholders following an appropriate resolution passed at a general meeting can sue in the name of the company (a true derivative action). An individual shareholder can bring proceedings against directors by way of a representative action (ostensibly on behalf of all shareholders), with the company joined as a nominal defendant (sometimes referred to as a derivative action).

Protection of minority shareholders

Minority shareholders in TCI companies have very limited rights. The holders of not less than 15 per cent of the issued shares can require the holding of a general meeting to propose and discuss a special resolution. A similar proportion can require the

appointment by the court of an inspector of the affairs of the company. With these exceptions, minority shareholders of TCI companies have minimal rights, other than to voice their discontent at a general meeting. There is no statutory obligation to hold a general meeting annually and so holders of less than a 15 per cent interest are denied even that privilege.

Shares with limited rights of participation are rare, except in quasi-trust structures. The use of non-voting shares or of shares of limited voting rights is not uncommon to ensure control by a dominant party where the dominant party's share entitlement on a *pro rata* basis might be insufficient to do so.

Disclosure of shareholdings

The register of members is available for inspection. Of course, the real beneficial ownership of the shares concerned may be hidden through the use of shell or holding companies. In the absence of provisions limiting transfer or requiring disclosure in the articles (and such provisions are unusual), no disclosure is required.

Exercise of corporate powers and recourse to the courts or administrative agencies

The rights of the shareholders in this regard – limited though they may be by the standards of mainland jurisdictions – are straightforward and relatively easy to exercise.

Management structure and the role of directors

Main management and board structures

The most common management structure used by TCI companies is the single board.

The only statutory requirement is that each company must have at least one director and one secretary. The director and the secretary can be the same person. A director or secretary of a TCI company can itself be a company.

There is no requirement that a certain number or proportion of the directors be non-executive directors or independent directors.

Election of directors

Typically, the board members are nominated and elected by the shareholders, and their term of office will be until their successors are elected or appointed. While the articles or terms of the appointment may set a time limit on the period of appointment (eg, until the next general meeting), there are otherwise no such limitations. The articles will usually reserve to the directors a right to fill a vacancy in their number.

Directors must be aged at least 18 and must not be mentally incapacitated in any way. There are no education or nationality requirements.

The directors need not be shareholders of the company.

Directors' duties

The duties of directors of TCI companies fall into two main categories: duties of good faith and honesty (or fiduciary duties), and duties of skill and care. Duties of good faith and honesty are owed to the company itself, and not to the shareholders. The fiduciary duties owed to the company include:

- a duty to act in good faith in the interests of the company;
- a duty to act for proper purposes;
- trusteeship of the company's assets, rendering a director answerable for any misapplication of those assets in which he participated and which he knew or ought to have known to be a misapplication; and
- a duty to avoid a conflict of interest.

In relation to his duties of skill and care, a director:

- is not expected to be an expert unless appointed as such;
- must exercise reasonable care and diligence;
- may reasonably rely on co-directors and officers of the company; and

- must use fair and reasonable diligence in the management of the company's affairs.

Most of the duties referred to are owed to the company and the company will therefore usually be the party entitled to redress in the event of their breach.

As to liability to third parties, any director who is party to a fraud or to the commission of any other tort (civil wrong) is personally liable to the injured party. Thus if, by order of the directors, a copyright is infringed, the directors who are parties to the infringement are personally liable, as is the company. If the injured party is a shareholder, that shareholder has same rights to sue for the wrong as an injured party who is not a shareholder.

The articles will frequently have a clause indemnifying directors and officers against liabilities incurred in the course of their office, except liability incurred as a result of their wilful neglect or default. Directors' and officers' insurance coverage is available on the usual terms.

The TCI Companies Ordinance imposes criminal penalties on directors for a variety of offences, including:

- breaches of the prospectus rules;
- failure to produce documents to duly appointed inspectors;
- perjury relating to a company;
- false statement in relation to certain statutorily required declarations regarding the business of an IBC;
- disclosure of confidential information;
- concealment of the names of creditors (in connection with an application for a reduction of capital); and
- sundry minor offences punishable by fine, relating to filing documentation and matters of that ilk.

In the absence of a criminal offence, the directors' duties referred to above are largely enforced by civil remedy.

There are no restrictions or requirements on the roles that individual board members may hold within the company. Neither is there a requirement that the roles of chairman of the board and managing director/chief executive officer/president be separated.

Directors are appointed and removed by shareholders. On the appointment of a liquidator in a voluntary liquidation, all powers of the directors cease, except as otherwise approved by the shareholders at a general meeting or by the liquidator.

Operation of the board

Certain decisions of the board require the approval of a special resolution of shareholders (75 per cent approval of those voting). Certain alterations of the capital structure of a company require an ordinary resolution of shareholders (simple majority). Otherwise, responsibility and decision making is largely a matter for the board, in compliance with the directors' duties.

The agenda for board meetings is determined by the board itself, which will review such materials as it deems appropriate. The power of a minority group of shareholders to call a general meeting in certain circumstances can act as an incentive to the board to include items of concern to minority shareholders on the agenda.

The frequency of board meetings will vary from company to company; there is no statutory requirement in this respect. While the company is obliged to maintain minutes of all resolutions and proceedings of directors' meetings at its registered office, there is no requirement to make those records available to shareholders. The recourse for an aggrieved shareholder would be to apply for the appointment of an inspector, who would be entitled to require production of those records.

A chairman is usually appointed to preside over the directors' meetings. Unless specified in the articles, the chairman will not have a casting vote.

TCI companies are frequently closely held and so committees of the board of directors,

although usually permitted by the articles, are not commonplace.

Executive officers

The legally required minimum is one director and secretary; a sole director may also be secretary. The articles would usually allow for the appointment of a managing director, treasurer and such other positions as are deemed appropriate by the board.

The appointment of a general counsel/chief legal officer is very rare in TCI companies.

The position of company secretary is statutorily required. The secretary's responsibilities are not fixed by law, although they may be specified in the articles. Usually they are administrative in nature and include:

- minuting the proceedings at meetings of the shareholders and directors issuing corporate notices to shareholders;
- corresponding with shareholders in regard to share transfers and the like; and
- maintaining the corporate record books and registers.

Remuneration

The remuneration and benefits of directors are determined by the directors. Given that TCI companies are usually closely held, shareholders are likely to be fully familiar with levels of remuneration.

Conflicts of interest

Conflicts of interest between the company and a significant shareholder, a director or a senior executive officer are not statutorily addressed. One of the primary duties of a director is to avoid such conflicts, and he may be civilly liable to the company if he does not do so. A senior executive officer may similarly be obliged under the terms of his employment contract to avoid such conflicts, and may be civilly liable if he fails to do so.

With respect to transactions between a company and its directors and officers, the directors

and officers are bound by their duties to the company, fiduciary and otherwise. They will be liable to the company for breach of those duties. In relation to transactions with significant shareholders, majority shareholders have very limited rights, but may seek appointment of an inspector with a view to drawing light on suspect transactions. In smaller, closely held companies, cosy transactions between a company and its shareholders, directors and officers will be liable to scrutiny by a liquidator, and may render the parties concerned liable to action by the liquidator on behalf of the company. There are no statutory provisions of the type usual in larger jurisdictions, such as restrictions on loans to directors and the like.

Unless imposed by contract or by the articles, and subject to common law duties to the company in the case of directors and employees, there are no restrictions preventing significant shareholders, directors and senior officers from dealing freely in the company's shares or securities.

As TCI companies are usually closely held, there is typically no code of corporate governance to which they adhere or code of conduct applicable to their personnel.

Related-party transactions are not governed by any government regulations outside the field of corporate and securities laws, such as fair trade regulations.

Accounts and audits

All TCI companies are statutorily required to keep proper books of account. There is no legal requirement for those accounts to be filed at the Companies Registry or otherwise with any government body. There is no statutory requirement for audit of the company's accounts.

Enforcement

Because TCI is largely a corporate domicile for closely held companies, there has been no domestic pressure for the enhancement or increased enforcement of corporate governance laws and

regulations. International bodies have been pressuring the TCI government to introduce enhanced corporate transparency, and those concerns are being addressed in the context of the international level playing field in financial services. In recent years the emphasis has been more on regulation of financial services providers than on corporate governance itself.

The emphasis is overwhelmingly on enforcement of corporate governance rules by shareholders or other interested parties utilising their civil remedies in the courts.

Sarbanes-Oxley

Hitherto, the Sarbanes-Oxley Act has had no effect on corporate governance law, regulations and practices in TCI.

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