In The Supreme Court of Bermuda

CIVIL (APPELLATE) JURISDICTION

2016: No. 255

IN THE MATTER OF SECTION 16 OF THE BERMUDA BAR ACT 1974

AND IN THE MATTER OF ORDER 55 OF THE RULES OF THE SUPREME COURT, 1985

AND IN THE MATTER OF WALKERS (BERMUDA) LIMITED

BETWEEN:

WALKERS (BERMUDA) LIMITED

Appellant

-v-

BERMUDA BAR COUNCIL

Respondent

JUDGMENT

(in Court)[1]

Application for registration as professional company-Bermuda Bar Act 1974, section 16C-proposed operation as licensee of global legal services firm- public policy requirement that local companies be controlled by Bermudians-Companies Act 1981, section 114

Date of hearing: January 9, 2017
Date of Judgment: January 12, 2017

[1] The present Judgment was circulated without a hearing to save costs.

Mr Michael Todd QC of counsel and Mr Kevin Taylor, Taylors, for the Appellant
Lord David Pannick QC of counsel and Mr Delroy Duncan, Trott & Duncan Limited, for the Respondent

Introductory

1. The Appellant appeals by Notice of Originating Motion against the refusal of the Respondent on June 10, 2016 to grant the Appellant a Certificate of Recognition (as a "professional company") under section 16C of the Bermuda Bar Act 1974 ("the 1974 Act"). The Appellant's application was refused on the grounds that the terms upon which the Appellant proposed to operate in Bermuda (in relationship with an international law firm ("Walkers Global")) would entail a contravention of section 114 of the Companies Act 1981 ("the 1981 Act"), which requires local companies to be owned and controlled by Bermudians. At the time of the relevant application, 100% of the Appellant's shares were owned by Bermudians. At the time of the present appeal, the Appellant's shares were 99% owned by a Bermudian lawyer and 1% owned by lawyer with a local Permanent Residence Certificate.

2. The central ground of the appeal is essentially that the Respondent erred in law in finding that the basis on which the Appellant proposes to operate as a professional company is unlawful by virtue of contravening the Bermudian control provisions of section 114 of the 1981 Act. The Respondent's Skeleton Argument made it clear that the only objection to the Appellant being granted a section 16C Certificate was the contention that its issuance was prohibited on public policy grounds. Apart from this pivotal consideration, the Bermuda Bar Council accepted that the Appellant met the express requirements under section 16B for the grant of a Certificate under section 16C of the Act.

3. Accordingly, the appeal turns on an analysis of what constitutes foreign 'control' as a matter of construction of section 114 of the Companies Act 1981 in its statutory context and construed with specific reference to the legal and commercial basis on which the Appellant has indicated it proposes to operate if it is granted the Certificate it seeks. This wider legal context necessarily requires attention to be given to the statutory scheme under the Act which has given rise to the present appeal.

4. What constitutes 'control' for the purposes of compliance with the public policy requirements of section 114 of the Companies Act 1981 has been authoritatively determined by the Judicial Committee of the Privy Council in *Bermuda Cablevision Ltd. et al-v-Colica Trust Co. Ltd.* [1998] A.C. 198. Lord Steyn articulated a necessarily open-ended test, a test which on one view had clear limits and which on another view was broad and unbounded. What the nature and extent of that test is and how it applies to the particular factual circumstances of the present case are the central points for determination on the present appeal.

Bermuda Bar Act 1974 provisions

5. For most of Bermuda's legal history and for the first 35 years of the 1974 Act, Bermudian lawyers could only operate as sole proprietors or in partnership with one another. In response to a combination of local needs and developments driven by globalisation internationally, Part IVA ("***PROFESSIONAL COMPANIES***") was enacted by way of amendment to the 1974 Act with effect from October 19, 2009. It is a notorious fact that the primary purpose of this enactment was to enable Bermudian lawyers, particularly those engaged in potentially high risk international commercial work, to be able to practise their profession with the significant protections of limited liability. It is a matter of record that all of the existing firms in 2009 specialising in international legal work (and the new ones formed since) now practise through professional companies registered under Part IVA of the 1974 Act.

6. Only four sections in Part IVA merit reproduction here even though their contents are not controversial. The provisions are for present purposes more relevant for what they do not contain than for their actual contents. Firstly, section 16A provides:

> "***Establishment of professional company***
> *16A(1)Subject to this Act and the rules, one or more barristers, each of whom holds a valid practising certificate issued under section 10, may establish a professional company for the purpose of providing professional services of the sort provided by individuals who practise as barristers or act as registered associates.*
>
> *(2)Subject to this Act and the rules, a professional company may carry on the practice of law in Bermuda.*"

7. Secondly, section 16B prescribes more detailed requirements:

> "***Conditions for professional companies***
> *16B (1) A professional company shall meet all of the following conditions—*
>
> *(a) the company must be incorporated as a company limited by shares within the meaning of the Companies Act 1981 and be in good standing with the Registrar of Companies;*
>
> *(b) the memorandum of association of the company must provide that the company has as its principal object the provision of professional services of the sort provided by individuals who practise as barristers or act as registered associates;*
>
> *(c) all of the issued and outstanding shares of the company must be legally and beneficially owned, directly or indirectly, by one or*

more individuals, each of whom is a barrister who holds a valid practising certificate issued under section 10;

(d) subject to subsection (3), all of the directors of the company must be barristers, each of whom holds a valid practising certificate issued under section 10;

(e) every barrister who is employed by the company as a barrister must hold a valid practising certificate issued under section 10 or 10A;

(f) every person who is employed by the company as an agent of the company to perform functions specified in section 15 must be a registered associate;

(g) the letterhead and promotional material for the company must clearly indicate that it is a limited liability company;

(h) the company shall obtain and maintain in effect insurance against professional liability under a policy of professional liability insurance issued by an insurance company that is registered as an insurer under the Insurance Act 1978 or is authorized to provide insurance under equivalent legislation in another jurisdiction; and

(i) the memorandum or bye-laws of the company must provide for the manner in which shares of a member of the company who dies or ceases to hold a valid practising certificate are to be disposed of.

(2)The Council may prescribe minimum requirements for a policy of professional liability insurance under subsection (1)(h), including the minimum amount of cover to be provided.

(3)In the case of a professional company that has only one shareholder, that shareholder—

(a) shall be one of the directors of the company; and

(b) shall elect or appoint as a director one other person, who need not be a barrister who holds a practising certificate, subject to the Council being satisfied that the person is a fit and proper person to be elected or appointed as a director of a professional company.

(4)A shareholder of a professional company shall not create any charge or other third party interest over his or her shares in the company."

8. The latter section did not, as it might, create any prohibition on franchise-type or brand-licensing arrangements. Nor did it confer any power on Bar Council to regulate the terms on which relationships with foreign legal companies or other entities might be formed. It does not, while mandating that all shares in the company be owned by persons with practising certificates, impose any nationality requirements at all, presumably because Part 1X of the Companies Act covers this terrain. However, subsection (4) of section 16B does address the issue of control in one narrow commercial sense by prohibiting shareholders from using their shares by way of security.

9. The present appeal most directly relates to an application for a section 16C Certificate. This section provides:

> "***Issuance of certificate of recognition***
> *16C(1)A company may apply to the Council for a certificate of recognition.*
>
> *(2)If the Council is satisfied that a company meets the conditions for a professional company set out in section 16B, the Council shall issue to the company a certificate of recognition as a professional company for the period from the date of issue to December 31 in the year in which the certificate is issued.*
>
> *(3)A professional company may apply in November in any year for a certificate of recognition for the following year.*
>
> *(4)If the Council is satisfied that a professional company continues to meet the conditions for a professional company set out in section 16B, the Council shall issue to the professional company a further certificate of recognition as a professional company for the period of one calendar year from January 1 next following the date of the application.*
>
> *(5)An application by a company for a certificate of recognition shall be made by a director of the company.*
>
> *(6)An application shall be made in such form as may be prescribed and shall be accompanied by the following—*
>
> *(a) the prescribed fee;*
>
> *(b) a declaration signed by a director of the company declaring that the*
> *conditions set out in section 16B have been met in respect of the company; and*
>
> *(c) any other documentation and information that may be prescribed.*

(7)A certificate of recognition shall be in such form as may be prescribed.

(8)The Council shall cause a list of the names of professional companies that have obtained certificates of recognition to be published in the Gazette, in the same manner as practising certificates under section 10(5).

(9)A copy of the Gazette that contains the name of a professional company published pursuant to this section shall be prima facie evidence in any court of the holding of a valid certificate of recognition by that professional company at the time of publication of the name."

10. The present appeal is made under the following section of Part IVA of the 1974 Act:

"***Appeal***
16E(1)Any barrister or company aggrieved by a decision of the Council to refuse an application for a certificate of recognition, or to suspend or revoke a certificate of recognition, may appeal to the Supreme Court against that decision within one month of being notified of it.

(2)Section 13[2]*, and any rules referred to in that section that apply to an appeal by a barrister in relation to a practising certificate, apply, with any necessary modifications, to an appeal under this section by a barrister or a company in relation to a certificate of recognition.*"

The Companies Act 1981

11. Section 114 of the 1981 Act provides as follows:

"***Circumstances in which local company may carry on business***
114<u>(1)No local company shall carry on business of any sort in Bermuda unless—</u>

[2] Section 13 provides as follows:

" ***Appeals***
13(1)Any barrister aggrieved by a decision of the Council refusing an application made under this Part may appeal to the Supreme Court against that decision within one month of being notified of it.

(2)Upon hearing any appeal under subsection (1), the Supreme Court may make such order, including an order for costs, as it thinks just.

(3)The practice and procedure to be followed in relation to applications and appeals under this section shall be as prescribed by rules of court."

> *(a) it is a company which, at the relevant time, complies with Part I of the Third Schedule or is a wholly-owned subsidiary of such a company; or*
>
> *(b) it is a company mentioned in Part II of the Third Schedule; or*
>
> *(c) it is licensed under section 114B and, at the relevant time is carrying on such business in accordance with the terms and conditions imposed in such licence, and not otherwise; or*
>
> *(d) it is a wholly-owned subsidiary of a company referred to in paragraph (c);*
>
> *(e) it is a company the shares of which are, at the relevant time, listed on a designated stock exchange and which is engaged as a business in a material way in a prescribed industry, or is a wholly-owned subsidiary of such a company.*
>
> *(1A)Section 118 shall not apply to a company referred to in subsection (1)(e).*
>
> *(2)Any local company that carries on business in contravention of subsection (1) shall be liable to a fine of one hundred dollars in respect of each day that it carries on business in contravention of the subsection.*
>
> *(3)The Minister may by regulations amend Part I of the Third Schedule, and any such regulations shall be subject to affirmative resolution procedure.*
>
> *(4)Section 132 shall apply mutatis mutandis to any company mentioned in Part II of the Third Schedule as if it were an exempted company.*" [Emphasis added]

12. Section 114 contains the main statutory requirement for local companies to comply with, inter alia, Part I of the Third Schedule. It is the Schedule itself which formulates the statutory concept of Bermudian control. So far as is relevant to the present appeal, the Third Schedule provides as follows:

> "***PART I***
> *PROVISIONS TO BE COMPLIED WITH BY A LOCAL COMPANY CARRYING ON BUSINESS IN BERMUDA*
>
> *1. (1) The company shall be controlled by Bermudians.*
>
> *(2) Without prejudice to the generality of sub-paragraph (1), at least sixty per centum of the total voting rights in the company shall be exercisable by Bermudians.*

2. (1) The percentage of Bermudian directors, and the percentage of shares beneficially owned by Bermudians, in the company shall not be less than sixty per centum in each case:

Provided that the company shall not be deemed to be in breach of this paragraph in so far as, and so long as, it is acting in accordance with sub-paragraph (2).

(2) The company shall act in accordance with this subparagraph if the percentage of shares beneficially owned by Bermudians in it falls below sixty per centum by virtue of factors which are beyond its control and it gives notice in writing to the person who is not Bermudian and whose ownership of shares results in the percentage so falling, as soon as the directors become aware of that fact, that—

> *(a) he must divest himself of his interest in those shares as soon as may be and, in any event, not later than three years from the date upon which he receives the notice; and*
>
> *(b) he must not exercise any voting rights attaching to such shares from the date upon which he receives the notice, and the three years calculated in accordance with paragraph (a) have not elapsed:*

Provided that the Minister, may in any particular case, for good cause, extend the period of three years for a further period not exceeding one year.

(3) For the purposes of sub-paragraph (2), the directors of a company shall be deemed to become aware that the percentage of shares beneficially owned by Bermudians in their company is less than the percentage specified in sub-paragraph (1) three days after the day upon which any director of a company would, if acting with due diligence, have become aware of that fact."[Emphasis added]

13. "*Bermudian*" for these purposes is defined, so far as is material for present purposes, as follows by section 113(1):

"*(b) any person who has Bermudian status by virtue of the law relating to immigration from time to time in force.*"

14. However, section 113 explicitly addresses the issue of the substance of ownership in a way which incorporates notions of control by providing as follows:

"*(3) No share shall be deemed to be beneficially owned by a Bermudian if-*

> *(a) that Bermudian is in any way under any obligation to exercise any right attaching to that share at the instance of, or for the benefit of, any person who is not Bermudian; or*
>
> *(b) that share is held jointly or severally with any person who is not*

Bermudian; or

(c) that share is owned by a subsidiary company of the company concerned."

15. It was clear from the outset that these statutory provisions did not in terms prohibit franchise-type of brand-licensing arrangements which compromised the commercial autonomy of a local company. The only explicit prohibition was on arrangements which on their face or in effect defeated the statutory requirements that local companies (to operate locally without a permit) should be at least 60% Bermudian beneficially owned or controlled.

The proposed contractual arrangements between the Appellant and Walkers Global

16. At the beginning of the hearing I made an Order sealing the proposed Licensing and Service Agreement and Loan Agreement until further Order of the Court on confidentiality grounds. The main elements of the proposed contractual arrangements are as follows:

    (a) Walkers Global will retain ownership in the global brand name "Walkers" and license its exclusive use by the Appellant in Bermuda for a fixed quarterly fee with either party having the right to terminate the contract on 12 months' notice;

    (b) Walkers Global will supply the Appellant with a comprehensive suite of administrative/managerial support services at rates comparable to those charged to other licensees elsewhere;

    (c) Walkers Global will provide substantial financial support on terms which reflect a symbiotic relationship between licensor and licensee with Walkers Global in a dominant position.

17. None of these contractual arrangements has any direct interface with the Appellant's management or ownership structure which is 99% Bermudian owned with a sole director who is Bermudian. Under standard Bye-laws, the Board is charged with managing the company subject to control by the shareholders in general meeting. The proposed arrangements nonetheless clearly propose to confer on Walkers Global a considerable amount of commercial influence over the Appellant.

18. However, the Respondent contended that the commercial reality was reflected in press statements made by Walkers Global in May 2015, somewhat provocatively from a Bermudian perspective, before the Appellant had even been incorporated (on 20 October 2015), let alone applied for a Certificate of Recognition under section 16C of the 1974 Act two days later. A 21 May 2015 press release stated:

    "*…The firm has also announced that it intends to open an office in Bermuda, making Walkers the first major international offshore firm to enter the Bermuda market.*"

19. The Appellant in effect submitted that this and related press pronouncements were premature marketing hype which had no bearing on an analysis of the proposed contractual arrangements as submitted months later in support of the relevant application.

The 10 June 2016 Bar Council Decision

20. The substance of the decision made after an exchange of correspondence in which Bar Council raised concerns about the application which the Appellant sought to allay was as follows:

> "*1. Whether or not the requirements of sections 16 B and 16 C of the Bermuda Bar Act 1974 are satisfied, Bar Council considers that upon entering into the proposed commercial arrangements with Walkers Global, the Company will not comply with the provisions of section 114 of the Companies Act 1981.*
>
> *2. The Company will be dependent on Walkers Global in financial and organisational terms…It will be dependent on Walkers Global for services for which it will pay a substantial licensing fee and Walkers Global has imposed strict limitations on the use of its goodwill and reputation and brand, the breach of which will result in the termination of the agreement. The reality of the proposed arrangement will be that the Company will be so beholden to Walkers Global that the latter is effectively in control. This accords with the manner in which Walkers promoted the launch of its Bermuda venture. Therefore, for the purposes of the Companies Act, Bar Council considers that the Company is, in reality, not 'controlled by Bermudians', giving that concept the broad and purposive interpretation adopted by the Judicial Committee of the Privy Council in Bermuda Cablevision Ltd. and Others-v-Colica Trust Co. Ltd. [1998] AC 198.*"

21. The Appellant's principal Mr Kevin Taylor in pressing for Bar Council to make a decision on his company's application in an email dated April 26, 2016 acknowledged that the role of overseas law firms in Bermuda was a matter of legitimate concern for Bar Council in policy terms even if the 1974 Act conferred no legislative authority for dealing with the topic. He wrote:

> "*I am aware that there is a sub-committee of Bar Council dealing with 'overseas law firms'-it was referenced in the Annual Report that was circulated at the AGM. An excerpt from page 10 of the Report reads 'It is going to take a collaborative effort between the Bar Council , the Minister of Immigration and the overseas law firms to get this right, as the goal here is to promote our jurisdiction while continuing to create opportunities for Bermudians.*"

22. The background to the rejection of the Appellant's application which implicitly appears from the evidence before this Court may fairly be summarised as follows. The Appellant is seeking to exploit what it sees as an open door to Bermudian professional companies to use an international legal service provider's brand in Bermuda. The Respondent is seeking to develop a policy (and possibly a legislative framework) for regulating such activities and in the interim would like to close that door in the interests of its stakeholders. The only legal ground it has to stand on is section 114 of the Companies Act 1981 and the argument that the Minister's permission is required under section 114B to permit Walkers Global to 'operate' in Bermuda through a local company which the foreign company controls.

The test for control established in Bermuda Cablevision Ltd. et al-v-Colica Trust Co. Ltd. [1998] A.C. 198

23. Mr Todd QC argued that the Judicial Committee in the *Bermuda Cablevision* case found that section 114 had been contravened by reference to the following key factual findings which were focussed rather than open-ended in scope:

    (1) the foreign minority shareholder was given the right to veto key Board decisions under the bye-laws which conferred substantial managerial control at et Board level; and

    (2) under a consultancy agreement the minority shareholder had the indefinite right to receive 60% of the company's profits.

24. Lord Pannick QC countered that Lord Steyn in his judgment in that case had clearly articulated a broad and flexible test for control designed to cut through legal technicalities and engage the commercial realities of the position.

25. Each of these submissions was to some extent well founded. The Privy Council undoubtedly found that the relevant arrangements contravened section 114 of the 1981 Act and the Third Schedule on two main grounds, and rejected a narrow approach to the meaning of control (including the submission that the provisions were penal and should be construed narrowly). The impugned basis upon which Bermuda Cablevision had been operating included the following main features:

    - In 1986, Bermuda Cablevision, which lacked the capacity to viably operate, agreed in principle with the McDonald interests that if the McDonalds constructed a cable television system in Bermuda they would receive 60% of the profits;

    - In 1987, the McDonald's US corporation agreed to use its best endeavours to finance the construction of the cable system in Bermuda and the McDonald's Caymanian company entered into a consulting agreement with Bermuda Cablevision pursuant to which they were entitled to receive 60% of the company's profits;

- That same year the Bye-laws were amended so that the McDonald interests, despite being minority shareholders, had a casting vote at Board level;

- After the requisite telecommunications license was obtained by the company, the McDonald interests lent over $8 million to the company on commercial terms but assuming the risk that the company would fail.

26. Colica Trust Co. Ltd. became a shareholder of Bermuda Cablevision after it had been operating on this basis for some years and challenged the legality of the arrangements. On the question of whether the relevant arrangements were unlawful because the company was not controlled by Bermudians, Lord Steyn held as follows:

> "*8….The control issue.*
>
> *The question is whether the arrangements put in place to protect the investment made by the McDonald interests have had the result that the company has been carrying on business in breach of paragraph 1(1) of Part I of the Third Schedule which requires that the company 'shall be controlled by Bermudians'. Counsel for the appellants submitted that the authorities establish that the natural meaning to be given to the word 'controlled' in paragraph 1(1) is control by virtue of a simple majority of the votes entitled to be cast at general meetings of the company. For this proposition counsel cited several tax cases which included three decisions of the House of Lords, namely British American Tobacco Company Limited v. Inland Revenue Commissioners [1943] A.C. 335; Inland Revenue Commissioners v. J. Bibby & Sons Limited [1945] 1 All ER 667; and Barclays Bank Limited v. Inland Revenue Commissioners [1961] A.C. 509. The decisions cited do not assist. Indeed a study of the reasoning in those decisions shows that expressions such as 'control' and 'controlling interest' take their colour from the context in which they appear. There is no general rule as to what the word 'controlled' means. Contrary to the submissions of counsel for the appellants, the expression 'controlled by Bermudians' in paragraph 1(1) is not a term of art. The expression must be given the meaning which the context requires. Paragraph 1(1) is the general provision and paragraph 1(2) is a specific provision introduced by the words 'Without prejudice to the generality of sub-paragraph (1)'. Nothing in Part I of the Third Schedule warrants a restrictive interpretation of paragraph 1(1) to limit its scope to control by means of a vote at general meetings. Indeed paragraph 2(1), so far as it requires the percentage of Bermudian directors not to be less than 60%, shows that the legislature did not proceed on the myopic footing that control can be exercised only through a vote at general meetings. That the legislature was alive to the fact that businessmen might by 'arrangement, artifice or device' create the appearance of compliance with the legislation is made clear elsewhere: see section 113(2). This was the context in which the legislature adopted the broad general statutory requirement of control by Bermudians. The generality of the meaning of control in such a context is*

illustrated by the famous decision of the House of Lords in Daimler Co. Ltd. v. Continental Tyre and Rubber Company (Great Britain) Limited [1916] 2 A.C. 307. Lord Parker of Waddington observed (at page 340):-

> *'... I think that the analogy is to be found in control, an idea which, if not very familiar in law, is of capital importance and is very well understood in commerce and finance. The acts of a company's organs, its directors, managers, secretary, and so forth, functioning within the scope of their authority, are the company's acts and may invest it definitively with enemy character. It seems to me that similarly the character of those who can make and unmake those officers, dictate their conduct mediately or immediately, prescribe their duties and call them to account, may also be material in a question of the enemy character of the company. If not definite and conclusive, it must at least be prima facie relevant, as raising a presumption that those who are purporting to act in the name of the company are, in fact, under the control of those whom it is their interest to satisfy.'*

9. While those observations dealing with an issue of trading with the enemy cannot be treated as definitive in the present case they are illustrative of a possible wide general meaning of the concept of control in the context of companies. And their Lordships are satisfied that there is nothing in the present contextual scene which justifies any restriction on the natural width of the expression 'controlled by Bermudians'. Indeed, if one has regard to the purpose of the legislation this conclusion is reinforced. The purpose of the requirement is plainly to ensure that Bermudian resources remain Bermudian. And it must have been intended to make an effective provision to this end. Giving the words in paragraph 1(1) their ordinary meaning achieves this legislative purpose.

10. Once the appellants' restrictive interpretation is rejected, as their Lordships do, it is perfectly plain that the McDonald interests controlled Cablevision by the scheme constituted by the amended Bye-laws and the Consulting Agreement. They controlled the board of directors through a casting vote and they controlled general meetings through the special resolution procedure. And they entrenched their entitlement to receive 60% of the profits of Cablevision by the provision that the Consulting Agreement cannot be terminated without their consent. In every relevant sense the McDonald interests had and have control of Cablevision. The consequence of this holding must necessarily be that Cablevision has carried on business contrary to the provisions of section 114 of the Companies Act 1981, and unlawfully, since 1987.

11. In the light of this conclusion it is unnecessary to consider the alternative argument of Colica that the non-Bermudian control of Cablevision violates the legislative policy of the Telecommunications Act 1986 and the Cable Television Service Regulations 1987 under which the relevant licence was granted." [Emphasis added]

27. So it is entirely correct that the Judicial Committee (a) relied on minority shareholder control of the Board and an agreement for the minority shareholder to receive a majority of the company's profits as key indicia of control (ignoring key logistical and financial support), and (b) adopted a broad functional approach to the concept of "control". However, the contending theses advanced by counsel were essentially as follows:

- **The Appellant**: section 114 only prohibits arrangements which confer corporate control to non-Bermudian interests and/or a disproportionate share of the profits;

- **The Respondent**: the proposed arrangements infringe section 114 because (a) the goodwill of the company will consist wholly or substantially of the foreign-owned "Walkers" brand, (b) the company will be heavily dependent on Walkers Global for logistical support, (c) the company will be heavily dependent on Walkers Global for finbancial support, and (d) Walkers Global's own pronouncements suggest that the real intent of the arrangements is to permit the foreign entity to run a Bermuda operation.

28. Accordingly the crucial controversy upon which the outcome of the present appeal turns is what are the statutory parameters of "control" for the purposes of Part IX of the 1981 Act? Are they limited to corporate control and/or beneficial ownership, or does it embrace potentially ill-defined and limitless manifestations of commercial control as well? Does Part IX of the Companies Act 1981 by necessary implication prohibit Bermudian-owned companies from operating under a foreign-owned brand, either in principle or on a case by case basis depending on the character of the relevant contractual terms? The answers to these questions are ultimately a matter of statutory interpretation it being common ground that this Court is bound by the general principles enunciated in *Bermuda Cablevision Ltd. et al-v-Colica Trust Co. Ltd.* [1998] A.C. 198.

The statutory meaning of "controlled by Bermudians"

<u>Pre-1981 legislative approaches to local business being carried out by foreign companies</u>

29. The External Companies (Jurisdiction in Actions) Act 1885, still in force today, was enacted to facilitate service of process on "[c]*ompanies and corporate bodies incorporated out of Bermuda, for banking, insurance or other trading purposes, and doing business in Bermuda by agents or branches*". Foreign companies have clearly operated in Bermuda for many years.

30. Probably the first statutory distinction made in Bermudian law between a locally incorporated and owned company authorised to conduct business in Bermuda and locally incorporated but foreign owned company only authorised to carry on business outside of Bermuda came in the incorporation by private act era when Elbon Limited was incorporated in 1935 with non-Bermudian shareholders. Probably the first Bermudian statute of general application to regulate the nationality of share ownership in relation to local companies came even earlier: the Companies Act 1923.

Section 20(1) of the 1923 Act[3] provided that persons other than British subjects could not be allotted more than "*two-fifths of the total number of the existing shares issued by the company*". These are the origins of what would come after the enactment of the 1981 Act to be known as the 60/40 rule and demonstrates that regulation of the extent to which foreign interests can participate in locally trading companies has deep roots indeed[4].

<u>The Companies Act 1981 and company categories</u>

31. The 1981 Act is primarily designed to apply to companies incorporated in Bermuda although it is clear from section 4 that parts of the Act apply to "*non-resident insurance undertakings*"[5] and "*permit companies*" ("*overseas companies*" given permission to trade in Bermuda). Separate parts of the Act deal with the following different categories which are relevant for present purposes:

    (1) Part IX (directly relevant) deals with local companies;

    (2) Part X (indirectly relevant) deals with exempted companies; and

    (3) Part XI (indirectly relevant) deals with overseas companies.

32. Part IX primarily regulates the extent to which local companies can carry on business within Bermuda, in short by either satisfying the Bermudian ownership requirements or obtaining a permit from the Minister. For Bermudian law purposes at least, a local company is a company entitled to conduct business locally. Part X regulates companies which are incorporated as such without imposing any nationality restrictions on ownership while strictly limiting the circumstances in which business can be carried on in Bermuda. In short, exempted companies can conduct business with each other, conduct business outside of Bermuda from a base within Bermuda and require a permit to conduct substantive local business activities.

33. Part XI contains an important (or potentially significant) prohibition on overseas companies conducting business in Bermuda:

> "***Overseas company not to carry on business without a permit***
> *132 (1)An overseas company shall not engage in or carry on any trade or business in Bermuda without a permit from the Minister issued under section 134.*
>
> *(2)Any permit issued to an overseas company enabling it lawfully to engage in or carry on any trade or business in Bermuda under the authority of any Act other than this Act or the Non-Resident Insurance Undertakings Act 1967*

[3]This provision was referred to in argument in the *Bermuda Cablevision* case at page 202 B-C.
[4] Kawaley (ed), '*Offshore Commercial Law in Bermuda*' (Wildy, Simmonds & Hill: London, 2013) at paragraphs 1.20-1.22, 1.42-1.48
[5] As defined by the Non-Resident Insurance Undertakings Act 1967.

shall be deemed to be a permit issued under section 134 if valid on 1 July 1983 and for so long as it remains valid.

(3)For the purposes of this Part "engage in or carry on any trade or business in Bermuda" includes the engaging in or carrying on any trade or business outside Bermuda from a place of business in Bermuda.

(4)A company shall be deemed to engage in or carry on any trade or business in Bermuda if it occupies premises in Bermuda or if it makes known by way of advertisement, or by an insertion in a directory or by means of letter heads that it may be contacted at a particular address in Bermuda or is otherwise seen to be engaging in or carrying on any trade or business in or from within Bermuda on a continuing basis:

Provided that a company shall not be deemed to engage in or carry on any trade or business in Bermuda by reason only that—

(a) a travelling salesman representing the company who has been permitted to land in Bermuda as such establishes a temporary place of business in Bermuda; or

(b) meetings of its officers or members are held in Bermuda; or

(c) the company is buying or selling or otherwise dealing in shares, bonds, debenture stock obligations, mortgages or other securities issued or created by an exempted undertaking, or a local company, or any partnership which is not an exempted undertaking.

(5)A company shall be deemed to engage in or carry on any trade or business in Bermuda if it makes known by way of advertisement or by any statement on a web site or by an electronic record as defined in the Electronic Transactions Act 1999 that it may be contacted at a particular address in Bermuda or if it uses a Bermudian domain name." [Emphasis added]

34. This is important because it complements the provisions of Part IX which require local companies to be Bermudian owned and controlled by prohibiting overseas companies themselves from carrying on business in Bermuda. On the one hand it adds force to the public policy value Parliament has placed through the provisions of Part IX on ensuring that local business is not conducted by overseas companies without express permission. Understandably no reliance was placed on section 132 by the Respondent in the present case because the Certificate has been refused on the grounds the grounds that a locally incorporated company intends to act in breach of section 114.

35. On the other hand the fact that section 132 appears to merely prohibit an overseas company from conducting local business in its own name indirectly highlights the perhaps unsurprising fact that there is no general prohibition on overseas companies indirectly operating in Bermuda through the instrument of commercial transactions with local companies, including selling goods and services and/or property of every kind. Nor is there any express prohibition on an overseas company selling intellectual

property rights or rights in its proprietary brand for use in Bermuda by a local company.

36. When construing the relevant provisions of Part IX of the 1981 Act, it is important to remember that their primary focus is not on the activities but rather the ownership and control of the local company. The Bermudian activities of overseas companies (regardless of the national identity of their owners or controllers) are most directly regulated by Part XI.

Part IX of the 1981 Act

37. Section 114 ("*Circumstances in which local company may carry on business*") provides that "[n]*o local company shall carry on any sort of business in Bermuda*" unless it either complies with Part I of the Third Schedule, has a permit under section 114B, or is a wholly owned subsidiary of a company which meets either of these two requirements. The ban on business being carried on in Bermuda is an absolute one if the relevant requirements are not met.

38. The relevant requirements in the present case are found in Part I of the Third Schedule as the Appellant contends that it does not require a permit while the Respondent contends that it does. It is common ground that the need for a permit only arises if the Appellant falls without Part I of the Third Schedule. The crucial provisions are the following:

> "*1. (1) The company shall be controlled by Bermudians.*
>
> *(2) Without prejudice to the generality of sub-paragraph (1), at least sixty per centum of the total voting rights in the company shall be exercisable by Bermudians.*
>
> *2. (1) The percentage of Bermudian directors, and the percentage of shares beneficially owned by Bermudians, in the company shall not be less than sixty per centum in each case…*"

39. The only explicit requirements are that at least 60% of the voting rights and beneficial share ownership should be in Bermudian hands. It is noteworthy that the generality of the "control" requirements of paragraph 1(1) are linked with the express voting rights provisions found in paragraph 1(2). That makes it clear that corporate control lies at the heart of the construct of the "*controlled by Bermudians*" requirement. In paragraph 2 (1) the beneficial ownership requirements are explicitly spelt out and may be seen as complementary to the control requirements. The standard corporate governance rule given statutory force under the 1981 Act (see e.g. sections 71-72, 91 and 93) is that companies limited by shares are controlled by the majority of their shareholders who elect directors at annual general meetings to manage the company's business activities.

40. There is a close connection between control and beneficial ownership not simply because of voting rights but because of economic rights as well. Although rights attaching to shares are potentially capable of being expressed in an infinite variety of

ways, the most elementary economic notion underpinning most corporate ventures is that corporate profits are distributed on a *pro rata* basis so that a 60% shareholder would receive 60% of the total dividend declared. This connection is made manifest in the way in which section 113 defines the term "*Bermudian*"[6] for the purposes of Part IX as a whole, linking the concepts of beneficial ownership and control. Lord Steyn in *Bermuda Cablevision* was clearly influenced by this section in a general sense, referring as he did[7] to a subsection which did not directly apply in that case and does not directly apply to the present case:

> "*(2)For the purposes of subsection (1), a company shall be deemed to be a wholly owned subsidiary of another company if the latter company enjoys the beneficial interest in all the shares of the former company through beneficial ownership or as beneficiary under a trust, express or implied, or through a nominee shareholder, to the exclusion of any other person, and control in the former company cannot, by means of any arrangement, artifice or device, be exercised either directly or indirectly by persons who are not Bermudians.*"[Emphasis added]

41. In other words, a wholly owned subsidiary of a local company can trade locally without a permit even if the subsidiary is owned by way of a trust or nominee registered shareholder, provided that the subsidiary is in substance controlled by Bermudians. Beneficial ownership and control are inextricably intertwined in section 113(2). The same is true when one comes to analyse the statutory definition of beneficial share ownership. Section 113(3) provides:

> "(3) No share shall be deemed to be beneficially owned by a Bermudian if-
>
> (a) *that Bermudian is in any way under any obligation to exercise any right attaching to that share at the instance of, or for the benefit of, any person who is not Bermudian; or*
>
> (b) *that share is held jointly or severally with any person who is not Bermudian; or*
>
> (c) *that share is owned by a subsidiary company of the company concerned.*" [Emphasis added]

42. Exercising rights attaching to shares "*at the instance of*" a person clearly embraces exercising voting rights at the direction of a person who is not the registered shareholder. Exercising rights attaching to shares "*for the benefit of*" a person other than the registered shareholder clearly, although perhaps somewhat less obviously,

[6] The relevant basic definition of "*Bermudian*" is found in section 113(1)(b): "*any person who has Bermudian status by virtue of the law relating to immigration from time to time in force*".

[7] At page 208A-B.

includes the situation where a 60% shareholder agrees (inconsistently with their strict bye-law rights) that a 40% shareholder can receive 60% of the company's profits. So in *Bermuda Cablevision*, the finding that the company was not "*controlled by Bermudians*" by reference to both voting control and economic benefit was made in a statutory context in which both voting control and real beneficial (or economic) ownership were explicitly the overlapping key statutory criteria.

<u>Summary: the meaning of "controlled by Bermudians</u>

43. In my judgment the breadth of the concept of 'control' articulated by the Privy Council does not extend beyond the parameters of the statutory context in which the term is found, parameters which are crucially elucidated by the factual context in which the *Bermuda Cablevision* case itself was decided. That context is concerned with ensuring that that the 60% voting and beneficial ownership rights attached to a local company's shares are in substance, and not just in form, exercised by and for the benefit of Bermudians. It is noteworthy that the only judicial authority cited by the Privy Council on the meaning of 'control' was House of Lords decision concerned with piercing the corporate veil in order to enforce wartime prohibitions on trading with the enemy. The following extract from Lord Paddington's speech in *Daimler Company Limited-v-Continental Tyre and Rubber Company (Great Britain) Limited* [1916] 2 A.C. 307 at 340 was adopted by Lord Steyn in *Bermuda Cablevision*:

> "…*I think that the analogy is to be found in control, an idea which, if not very familiar in law, is of capital importance and is very well understood in commerce and finance. The acts of a company's organs, its directors, managers, secretary, and so forth, functioning within the scope of their authority, are the company's acts and may invest it definitively with enemy character. It seems to me that similarly the character of those who can make and unmake those officers, dictate their conduct mediately or immediately, prescribe their duties and call them to account, may also be material in a question of the enemy character of the company. If not definite and conclusive, it must at least be prima facie relevant, as raising a presumption that those who are purporting to act in the name of the company are, in fact, under the control of those whom it is their interest to satisfy.*"

44. I accept the central submission of Mr Todd QC that when the entirety of this passage is read in the context of the report of the case as a whole (as opposed to merely the last sentence relied upon by Lord Pannick QC), it is clear that what was under consideration was broad practically viewed ownership or quasi-ownership control, both in the House of Lords in *Daimler* and the Judicial Committee in *Bermuda Cablevision*. A further passage from *Daimler* (at page 345) puts this conclusion beyond doubt:

> "*The enemy character of individual shareholders and their conduct may, however, be very material on the question whether the company's agents, or the persons in de facto control of its affairs, are in fact adhering to, taking*

> *instructions from, or acting under the control of enemies. This materiality will vary with the number of shareholders who are enemies and the value of their holdings. The fact, if it be the fact, that after eliminating the enemy shareholders the number of shareholders remaining is insufficient for the purpose of holding meetings of the company or appointing directors or other officers may well raise a presumption in this respect.*"

45. It is this practical corporate control-focussed reasoning that the Judicial Committee applied in the *Bermuda Cablevision* case in pivotally deciding that the ability of the minority shareholder to control key Board decisions through its nominated directors combined with its contractual entitlement to a majority share of the company's profits evidenced that the company was not controlled by Bermudians in compliance with section 114 of the 1981 Act.

Do the proposed arrangements in relation to the Appellant contravene section 114 of the Companies Act?

46. Once one arrives at the finding that the term "*controlled by Bermudians*" speaks to the ability to exercise the sort of power and/or receive the sort of economic benefits equivalent to holding more than 40% of a local company's shares, the Respondent's case becomes very doubtful indeed. Lord Pannick's primary argument was that section 114 prohibited all forms of control, including what amounted to commercial dependence on foreign support as long as using the Walkers brand was the Appellant's main commercial *raison d'être*. I have rejected that argument primarily based on a comparatively straightforward purposive approach to what I consider to be ultimately the natural and ordinary meaning of the relevant statutory words.

47. I have not been wholly unaffected by the unattractive spectre that adopting so broad an interpretation of section 114 of the 1981 Act in the present Judgment could potentially undermine all manner of other commercial arrangements or at least cause them to be subject to doubt. Accepting Lord Pannick's submission on a narrower aspect of this point, section 114 is <u>not</u> a penal provision which should automatically be construed strictly against the Crown. The true rule of construction is that courts should be slow to apply a penal provision in cases of real doubt as to its application. Where the legislative purpose is clear, the courts must give penal provisions their intended effect: *R-v- Z (Attorney General for Northern Ireland's Reference* [2005] 2 AC 645 (per Lord Bingham at paragraph 23). Construing section 114 in its statutory context and against the longstanding history of the 60/40 rule in Bermudian legal history, there is no convincing support for concluding that Parliament intended by necessary implication to prohibit commercial influence and potential corporate control <u>in addition to</u> the far clearer prohibition on concrete arrangements designed to circumvent the express provisions of the statute governing beneficial ownership and corporate control.

48. In my judgment, section 114 is not infringed merely because a local company is commercially dependent on a foreign loan. It is not for this Court to effectively find that local companies are prohibited from borrowing abroad to fund their Bermudian

operations in circumstances where Parliament has not expressly signified any such legislative intent. Nor is section 114 infringed merely because, or in addition to the loan, the local company is dependent on foreign services where there is no convincing basis for inferring any such legislative intent. Where the local company under consideration is 99% owned by a Bermudian and is seeking to operate as a professional company in a regulated profession, the genuineness of the company's constitutional documents cannot be effectively impeached by reference to admittedly injudicious 'marketing hype' from the foreign brand owner, especially since those pronouncements were made before the Appellant was even incorporated. After all, the value of the global professional brand is quite obviously materially dependent on a reputation for ethical and lawful conduct, which makes it impossible to believe that a global law firm would announce an intention to flout Bermudian law to the world.

49. Even the combination of all of these factors, properly analysed, does not engage section 114 seriously or at all-unless one views the statutory scheme as prohibiting by necessary implication all such licensing or franchise arrangements. This conclusion in no way minimizes the legitimacy of the policy view that the Bermuda Bar Council may well have genuinely formed: that the proposed arrangements excited suspicion in the absence of any governing regulatory regime under the 1974 Act and resulted in a conviction that such activities ought not to be exempt from regulation under Bermudian law.

50. The most beguiling argument which Lord Pannick QC advanced was presented in an attractive manner. He contended that the essence of a company's business is its goodwill and under the proposed arrangement that goodwill (the title to the "Walkers" brand) would always be owned by Walkers Global, a foreign entity. On this basis, the relationship should be viewed through the lens of the foreign interested party. It was coming into Bermuda, generating income from its key asset, and when the license arrangement came to an end, it would take the local company's key asset away with it. On this basis, in effect, the true beneficial owner of the Appellant would always be Walkers Global, the foreign controlling entity. This was inconsistent with the legislative scheme's principal object, as identified by Lord Steyn, which was "*to ensure that Bermudian resources remain Bermudian*". However, Mr Todd QC replied that this analysis was flawed, in part because the local lawyers would generate goodwill independently of the licensed brand name and in part because the local company effectively 'owned' a distinctive right: the right to use the brand name in Bermuda. He also countered his opponent's protectionist rhetoric by contending that it would enhance Bermudian resources for a new company to bring new business and employment to Bermuda.

51. These rhetorical arguments do not ultimately affect the pertinent legal analysis. It may well be to some extent a valid way of framing the nature of the proposed arrangements, focussing on the benefits the global brand owner hopes to receive, to view that owner as, in effect, a modern day pirate, using local allies to navigate safely through Bermuda's protective reefs, to 'plunder' valuable resources ashore. But if this is valid spin to place on the proposed business plan, it must also be viewed through the local business owner's lens. He is seeking to create a new business to exploit Bermudian legal resources and has chosen to exclusively exploit a valuable foreign brand which necessarily requires the ancillary deployment of the brand owner's management systems as well. As noted above, I am bound to find that the focus of

Part IX of the 1981 Act is not on business forms but ensuring that companies which purport to be Bermudian owned and controlled in compliance with the ‘60/40’ rule are in substance and reality constituted on a lawful basis. In my judgment, the “*Bermudian resources*” which section 114 seeks to protect are the ability to conduct business and generate profits in Bermuda. The form of statutory protection which Parliament has provided is to provide that only local companies can do business within Bermuda (without a permit) and to qualify for this entitlement they must be in substance as well as in form be at least 60% owned and controlled by Bermudians. I find that the Appellant’s proposed operating arrangements as a professional company under the Bermuda Bar Act leave no room for doubt that the company will be in the requisite statutory ‘real-world’ sense owned and controlled by Bermudians. Its main object is to act as a professional corporation under the 1974 Act. The brand licensing arrangements can be terminated by either party on 12 months’ notice; the company can change its name and operate under an entirely new brand at the election of its Bermudian shareholder.

52. Section 114 prohibits Bermudian beneficial shareholders with a stake of 60% or more in a local company proposing to operate in Bermuda without a permit from entering into arrangements which dilute the voting power and economic interest which would and should ordinarily attach to their stake in the company. Based on the specific facts of the present case, I find that the statute does not go further to prohibit a Bermudian shareholder who undoubtedly has the legal right to control the company and obtain a commensurate share of its profits from pursuing a business model contemplated by the Appellant. This is a model which merely makes the company commercially “beholden” to a key foreign supplier of product, brand or intellectual property rights, logistical support and/or financial support. Is it possible that these formal arrangements could in practice turn out to be a sham at worst or sailing close to the wind at best? That is entirely a matter of speculation and the starting assumption, particularly when the human actors concerned are regulated professionals whose long term commercial interests are aligned with maintaining reputations for probity, can only be that parties concerned intend to comply with rather than evade the law. In these circumstances, where the Appellant will be subject to a continuing duty to comply with section 114, it matters not that the future financial profile of the proposed business is presently less than clear.

53. Although in my judgment it would be a bridge too far in terms of statutory interpretation for this Court to find that section 114 by implication prohibits licensing arrangements of the sort that the Appellant proposes to enter into, it is easy to see that the Bermuda Bar Council would be assisted by legislative support to regulate (either itself or through an appropriate Minister) the terms on which foreign legal brands can be used by local professional companies. I should add that it is not apparent to me that the most pressing concerns underpinning any such regulatory regime would be the minutiae of the financial or service arrangements that Bermudian professional service firms enter into. What those concerns might be was not canvassed in the present appeal, which focussed on a different statutory regime altogether. My gentle suggestion that some regulation might be helpful involves no tacit criticism of the proposed arrangements in this case. Rather, it is to express sympathy with the conundrum which confronted the Bermuda Bar Council and prompted the decision to

refuse to issue the Certificate sought by the Appellant on grounds which I have found to have been unsound in legal terms.

Conclusion

54. For the above reasons the appeal is allowed on the grounds that the proposed arrangements regulating the proposed operation of the Appellant as a professional corporation under the Bermuda Bar Act are not contrary to section 114 of the Companies Act and/or public policy.

55. I will hear counsel, if required, on the terms of the final Order and as to costs although there is no obvious reason why costs ought not to follow the event.

Dated this 12th day of January 2017 __________________________

IAN RC KAWALEY CJ