A CONSTRUCTION OF "RECONSTRUCTION": ARTICLE 127 OF THE COMPANIES (JERSEY) LAW 1991

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Under art 127 of the Companies (Jersey) Law 1991 the Royal Court has a broad range of powers which can be utilised by a company seeking approval for a scheme of arrangement. For those powers to be engaged, the court must be satisfied that what is proposed amounts to a reconstruction of the company. In English case law considering equivalent provisions, the meaning of "reconstruction" has been strictly interpreted to mean that the shareholders in the old and new companies are substantially the same. In In re LXB Retail Properties plc*, the Royal Court decided not follow the narrow construction of the word "reconstruction" in English case law, opting instead for a wider and more pragmatic meaning in the commercial context. This decision opens the way to a broader range of corporate reconstructions in the context of a scheme of arrangement.*

1 *In re LXB Retail Properties plc*[1] has provided the first definition of the word "reconstruction" in art 127 of the Companies (Jersey) Law 1991 ("the Companies Law") and provides an useful reminder that a Jersey court will always look to interpret a statutory provision from a Jersey perspective even where the provision in question is closely modelled on an English equivalent and in an area of law where the Jersey courts often follow English case law.

2 *LXB* is a decision arising at the first stage in an application to the Royal Court for approval of a scheme of arrangement under art 125 of the Companies Law. LXB Retail Properties ("the company") is a Jersey incorporated, closed ended investment fund specialising in property development in the UK. It was proposed by the directors to realise the investments and wind up the company. The very nature of property development however means that the developer (in each case a subsidiary of the company) assumes legal liabilities arising from the planning process and the developments themselves. Some of these liabilities are contingent and may never arise; others endure for long periods of time. The option for the company was therefore to await the

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[1] [2018] JRC 049 (Clyde-Smith, Commr and Jurats Nicolle and Blampied).

effluxion of these periods of time or adopt a solution which would enable the company to come to an orderly termination of its existence in a shorter time frame. The latter was the favoured option and, accordingly, it was proposed to hive off those subsidiaries with liabilities to a third party entity, which would be cash collateralised to meet those liabilities as and when they fell due, and proceed to realise the company's assets, discharge its liabilities and wind it up. The company's preference was to do this via a scheme

3 A scheme of arrangement falls within the broader category of "compromise or arrangement" between a company and its creditors (or any class of them) or its members (or any class of them) which is available under art 125 of the Companies Law. Its underlying purpose is to effect a binding change in the relationship between these parties where it would be difficult, uncertain or impossible to achieve this in any other way. The construct was originally introduced in England via the Joint Stock Companies Agreement Act 1870 and applied only to creditors but gradually evolved to include members. There is nothing in the Companies Law that prescribes the subject matter of an arrangement or a scheme so in principle it can concern anything which the company and its members or creditors may properly agree between themselves. As between members and a company, the words are broad enough to cover any restructuring of rights and obligations. In practice, as case law has evolved, the requirement for court approval of a scheme restricts the subject matter to one which is a genuine and fair agreement or compromise between a company and its members or creditors. This is ensured by the requirement for agreement to the scheme by a certain majority of those whose rights are affected and by the court being satisfied that no-one is unfairly prejudiced by the scheme.

4 The process has developed to encompass a wide range of uses such as solvent reorganisations of a company or group structure (including takeovers, mergers and demergers) and insolvent restructuring (including debt for equity swops). In Jersey, the process has been utilised in a limited range of ways but typically to effect the sale and purchase of shares in the company in question, albeit often in very sophisticated processes (see *In re TSB Bank Channel Islands Ltd*[2] for an example of a scheme for the sale and purchase of shares in the company; and *In re Royal Bree's Hotel Ltd*[3] for an example of a compromise with creditors. A key attraction for those involved in promoting a scheme is that once it is sanctioned by the court it is

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[2] 1992 JLR 160.
[3] UJ No 1994/168, Royal Ct, 1 July 1994; 1994 JLR *N*–6a.

binding in law. Thus whilst it might be impractical (or perhaps impossible) to get all of the creditors or members to agree to what is proposed, the use of the specified majority threshold enables a scheme to be approved.

5 The Companies Law is the primary statute concerned with Jersey company law. It replaced an amalgam of prior statutes being the *Loi (1861) sur les sociétés à responsabilité limitée* and the Companies (Supplementary Provisions) (Jersey) Law 1968 (collectively referred as the Companies (Jersey) Laws 1861 to 1968). The Companies Law followed a major review commissioned by the States of Jersey which included an analysis of local company law and an intention to introduce a company law which met the requirements of modern Jersey, not least those arising from its evolution into an international finance centre.[4]

6 The Companies Law drew its primary inspiration from the Companies Act 1985 and, to a lesser extent, the Companies Act 1948. Influence came from the Ontario Business Corporations Act 1982 and the Australian Companies Act 1961 model.[5] Nevertheless, whilst the Companies Law has "many similarities" with the 1985 Act, it has been "adapted to meet the particular needs and demands of companies registered in Jersey".[6] Since its promulgation in 1991, the Companies Law has been refined and changed and there have been numerous amendments to the statute. There have also been a number of subordinate statutes made under it. In many respects, Jersey company law is materially similar to English company law under either the Companies Act 1985 or the Companies Act 2006 but there are some key difference such as the principle and rules regarding capital maintenance.

7 On the usual basis, English and Commonwealth case law, where the relevant statutory provisions and/or principles are the same or similar, will be of persuasive effect on a Jersey court in the company law context. As the Royal Court put it in *In re TSB Bank Channel Islands Ltd* referring to s 206(1) of the Companies Act 1948, as re-enacted with a minor change in s 425 of the Companies Act 1985—

> "the wording of our article is in identical terms with the English Acts . . . it would , we think, be a cause for some surprise if, with

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[4] P Omar and D Hoccom, *Company Law. Jersey Law Course 2017–18*. (Institute of Law) para 1.1. Tab 54.
[5] *Ibid*, para 1.2.
[6] M Dunlop, *Dunlop on Jersey Company Law* (1st edn, Oxford 2010), para 1.2. Tab 55.

identical provisions in our Law, we did not have the fullest regard to the very strong persuasive effects of interpretation given by English courts to the relevant sections of the Companies Acts. Indeed, not only by the English courts but also by the Scottish courts, since the two Acts (of 1948 and of 1985) applied and apply both in England and Scotland."[7]

8 That case concerned a scheme of arrangement and would now, in the light of *State of Qatar v Al Thani*,[8] be viewed as overstating the persuasive effect of English case law to a degree. Nonetheless, in this context, English and Commonwealth case law remains of persuasive value. A more recent example of the influence of the former may be seen in the discussion in the recent case of *In re Galasys plc*[9] where the court had to consider the validity of certain resolutions of directors and shareholders. From para 32, the court considered various English judgments dealing with the principle of corporate governance by directors and the limited exceptions to that principle. In the field of ratification and of the ratification of the decisions by or on behalf of Jersey companies, the Jersey court has also followed English case law as is evident from the decision in *Izodia Plc v Royal Bank of Scotland International Ltd*.[10]

Compromises or arrangements under the Companies (Jersey) Law 1991

9 Article 125 of the Companies Law provides as follows—

"**Power of company to compromise with creditors and members**

(1) Where a compromise or arrangement is proposed between a company and its creditors, or a class of them, or between the company and its members, or a class of them, the court may on the application of the company or a creditor or member of it or, in the case of a company being wound up, of the liquidator, order a meeting of the creditors or class of creditors, or of the members of the company or class of members (as the case may be), to be called in a manner as the court directs.

(2) If a majority in number representing—

(a) 3/4ths in value of the creditors or class of creditors; or

[7] 1992 JLR at 162.
[8] 1999 JLR 118.
[9] 2016 (2) JLR 347.
[10] 2006 JLR 346, at para 103.

(b) 3/4ths of the voting rights of the members or class of members,

as the case may be, present and voting either in person or by proxy at the meeting, agree to a compromise or arrangement, the compromise or arrangement, if sanctioned by the court, is binding on—

(i) all creditors or the class of creditors; or

(ii) all the members or class of members,

as the case may be and also on the company or, in the case of a company in the course of being wound up, on the liquidator and contributories of the company.

(3) The court's order under paragraph (2) has no effect until the relevant Act of the court has been delivered to the registrar for registration; and the relevant Act of the court shall be annexed to every copy of the company's memorandum issued after the order has been made.

(4) If a company fails to comply with paragraph (3), it is guilty of an offence."

10 There are two points worth commenting on at this stage. First, English authorities which have considered the scope of the equivalent provisions of the Companies Act 1985 (s 425) and Companies Act 2006 (s 895) have held that the terms "compromise" and "arrangement" are to be construed widely. Secondly, the term "a compromise or arrangement", used in both the English legislation and the Companies Law, denotes two different things. A compromise is a settlement of a disagreement and therefore requires a dispute: *Sneath v Valley Gold Ltd*[11] and *Re Bluebrook Ltd*.[12] An arrangement, in contrast, need not involve any compromise of a member/creditor's rights in relation to the company and indeed most schemes of arrangement involving members do not involve such a compromise. For instance, a scheme of arrangement for the acquisition of the shares in a company by a third party does not involve any compromise but does amount to an arrangement because it involves a change in the membership of the company: *Re Savoy Hotel*.[13]

[11] [1893] 1 Ch 477, CA.
[12] [2010] BCC 209.
[13] [1981] Ch 351.

11 A relatively recent case which shows the breadth of the concept of an "arrangement" is the English case of *In re T&N Ltd (No 4)*.[14] In that case David Richards, J (as he then was) found that a scheme which compromised the rights of asbestos claimants not against the company but against the company's insurers was within the scope of the section. It was held (paras 53–54)—

> "In my judgment it is not a necessary element of an arrangement for the purposes of section 425 of the 1985 Act that it should alter the rights existing between the company and the creditors or members with whom it is made. No doubt in most cases it will alter those rights. But, provided that the context and content of the scheme are such as properly to constitute an arrangement between the company and the members or creditors concerned, it will fall within section 425. It is, as Nourse J observed,[15] neither necessary nor desirable to attempt a definition of arrangement. The legislature has not done so. To insist on an alteration of rights, or a termination of rights as in the case of schemes to effect takeovers or mergers, is to impose a restriction which is neither warranted by the statutory language nor justified by the courts' approach over many years to give the term its widest meaning. Nor is an arrangement necessarily outside the section, because its effect is to alter the rights of creditors against another party or because such alteration could be achieved by a scheme of arrangement with that other party.
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> 54 These considerations all go to the meaning of arrangement in section 425 and hence the jurisdiction of the court under the section to sanction a scheme of arrangement. They do not fetter the discretion as to whether to sanction a scheme of arrangement. The looser the connection between the subject matter of the scheme and the relationship between the company and creditors concerned, the more substantial might be the objections on discretionary grounds to sanctioning the scheme."

12 There are three stages in the process by which a scheme of arrangement under art 125 of the Law becomes binding on shareholders which were summarised in the judgment of the Royal Court *In re Computer Patent Annuities Holdings Ltd* ("*CPAHL*")[16]—

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[14] [2007] Bus LR 1411.
[15] In *In re Savoy Hotel Ltd* [1981] Ch 351, at 359.
[16] [2010] JRC 011.

"There are three stages in the process by which a scheme of arrangement under Article 125 of the Companies Law becomes binding:—

(i) First there is an application under Article 125(1) for an order that a meeting of shareholders or creditors if necessary be called. It is at this stage that the Court should consider whether or not to summon separate class meetings and if so, who should be summoned to each meeting. The Court will not look at the merits at this stage (See Re Telewest Communications Plc [2004] EWHC 92).

(ii) Secondly, the scheme proposals are put to the court-convened meeting and are approved by a majority by number representing 3/4ths of the voting rights of members present and voting in person or by proxy . . .

(iii) Thirdly, and assuming the requisite approval at such meeting is given, the Court exercises its discretion as to whether to sanction the arrangement: see Re National Bank Ltd [1966] 1 All ER 1006 at 1012 approved by the Royal Court in Re Telewest Finance (Jersey) Limited [2004] JRC 109."

13 Although the *CPAHL* case concerned a scheme of arrangement involving members of the company, there is no reason in principle why the same process would not apply to an arrangement involving creditors or a compromise.

A scheme for the reconstruction of a company

14 Article 127 of the Companies Law provides the court with additional powers in certain circumstances where it is being invited to sanction a compromise or arrangement:

"**Provisions for facilitating company reconstruction or amalgamation**

(1) This Article applies where application is made to the court under Article 125 for the sanctioning of a compromise or arrangement proposed between a company and any persons mentioned in that Article.

(2) If it is shown—

(a) that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of a company or companies, or the amalgamation of 2 or more companies; and

(b) that under the scheme the whole or part of the undertaking or the property of a company concerned in the scheme ('a transferor company') is to be transferred to another company ('the transferee company'),

the court may, either by the order sanctioning the compromise or arrangement or by a subsequent order, make provision for all or any of the following matters—

(i) the transfer to the transferee company of the whole or part of the undertaking and of the property or liabilities of a transferor company;

(ii) the allotting or appropriation by the transferee company of shares, debentures, policies or other similar interests in that company which under the compromise or arrangement are to be allotted or appropriated by the company to or for any person;

(iii) the continuation by or against the transferee company of legal proceedings pending by or against a transferor company;

(iv) the dissolution, without winding up, of a transferor company;

(v) the provision to be made for persons who, within a time and in a manner which the court directs, dissent from the compromise or arrangement;

(vi) such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation is fully and effectively carried out.

(3) If an order under this Article provides for the transfer of property or liabilities, then—

(a) that property is by virtue of the order transferred to, and vests in, the transferee company; and

(b) those liabilities are, by virtue of the order, transferred to and become liabilities of that company,

and property (if the order so directs) vests freed from any hypothec, security interest or other charge which is by virtue of the compromise or arrangement to cease to have effect.

(4) Where an order is made under this Article, every company in relation to which the order is made shall cause the relevant Act of the court to be delivered to the registrar for registration within 14 days after the making of the order; and in the event of failure

to comply with this paragraph, the company is guilty of an offence.

(5) In this Article, 'property' includes property, rights and powers of every description and 'liabilities' includes duties."

15 Article 157 is concerned with the situation where the compromise or arrangement relates to a scheme of reconstruction or amalgamation, a process which for it to be engaged requires at least two companies. If pursuant to that process, at least part of the undertaking or of the property of one company is being transferred to another company, the court, when considering the sanctioning of an "arrangement" under art 125 is granted a discretionary power to make certain ancillary orders. Those orders are predominantly aimed at enabling the transfer of rights and obligations to the transferee company, including the assets and liabilities of the transferor company. They also include the power to dissolve the transferor company without the need for it to undertake a winding up process.

The facts of the application by LXB Retail Properties plc

16 In simple terms, the scheme proposed on behalf of the company was to realise as much value as possible from its remaining assets, return cash to its shareholders and transfer to an independent company the remaining subsidiaries with liabilities and assets, together with sufficient cash to collateralise those liabilities. The company would then be dissolved without the need to engage in a winding up process. In a complex structure, the process required a number of detailed stages for it to be accomplished (see para 15 of the judgment).

17 The company therefore sought to avail itself of the court's powers under arts 125 and 127 of the Companies Law. From the company's perspective, there were thus two pre-conditions required to be proved to the court's satisfaction before it sought an order convening the court meeting of shareholders. First, the proper engagement of art 125, namely that what was intended by the company was a scheme proposing (in this case) an arrangement. Secondly, whether art 127 would be engaged, namely (in this case) that the scheme was a scheme for the reconstruction of the company. They were pre-conditions since without their satisfaction there could be no court approval of what was proposed, either at the convening hearing or the subsequent application for a dissolution, and there would have been no point progressing to the convening hearing.

Was the scheme capable of constituting an arrangement?

18 The court found that the first precondition was satisfied. The scheme was capable of constituting an "arrangement".

19 There was a requirement for some "give and take" or accommodation on each side (citing *In re NFU Development Trust Ltd*[17]) and it was satisfied in this case since what was proposed was the transfer without consideration of some of the assets of the company to a third party company in return for which the company would be able to realise its remaining assets in a shorter timeframe and with lower costs than a process of realisation or commencement of a summary winding up (paras 21 and 23 of the judgment).

20 Although not a prerequisite (*per In re T&N Ltd (No 4)*[18]), in fact members' rights in relation to the company were to be altered by the proposed scheme in that it entailed discharge of a requirement of the articles of association for proposals to be put to shareholders concerning the voluntary liquidation, reconstruction or other re-organisation of the company and, once approved, those shareholders who had voted and opposed the scheme or not voted at all could not challenge the decision to implement the scheme (para 23 of the judgment.

Did the scheme constitute a scheme for the reconstruction of the company?

21 The court found that the second precondition was also satisfied and we shall focus on this aspect, the construction of art 127, as it decided something for the first time in the Jersey jurisdiction and reaffirmed an important principle of our jurisprudence in relation to English case law on equivalent statutes.

22 As we have seen, art 127(2) comprises two prerequisite limbs, both of which must be satisfied before the court's powers under art 127 become exercisable. The first limb requires that at least part of the undertaking or property of the company involved in the scheme is being transferred to another company. The court found this was satisfied: under the scheme, part of the property of the company was being transferred to another company in order for it to manage those assets with certain contingent liabilities. The second limb requires that the "arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of a company".

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[17] [1972] 1 WLR 1548.
[18] [2007] Bus LR 1411.

The meaning of "reconstruction" in English statutes

23 A potential obstacle to satisfaction of this limb was the meaning given to "reconstruction" in the equivalent English statutory provision (s 427 of the Companies Act 1985) by English case law, as most recently interpreted in *Re Mytravel Group plc*[19] (Mann, J as he then was). In that case, the applicant company applied to the court seeking the convening of meetings of shareholders and certain creditors to consider a scheme of arrangement under s 425 of the Companies Act 1985 (which is virtually identical to art 125 of the Companies Law). The scheme also sought to engage s 427 which is similarly close to identical to art 127.

24 The applicant (as its name would imply) operated in the travel industry, selling holidays and travel services. It had very heavy borrowings and had suffered significant losses. It was attempting to turn the business around and wished to restructure. To that end, the company sought to make a consensual arrangement with its creditors and had negotiated a debt for equity swap with certain of the creditor groups. However one group (referred to as the bondholders) did not accept the offer. If they had, restructuring could have been consensual and there would have been no need for a scheme.

25 In outline, the scheme envisaged that the assets and undertaking of the applicant company would be transferred to a new company (Newco); a limited quantity of the company's debts would be assumed by Newco but the bulk of them (but not the bonds, which were to be left behind) would be turned into equity in Newco. The existing shares in the company were to be transferred to Newco in which the existing shareholders would be allotted only a small percentage (4%) of Newco's shares. Four major creditors were to be allotted 94% of the shares in Newco and in return the company would be released from its obligations to them ("the converting creditors"). The provisions of s 427 were invoked because the scheme required a court order to effect the transfer of assets and liabilities from the company to Newco.

26 The bondholders objected to the proposed arrangement and submitted that the proposed arrangement could not be brought within the wording of s 427 whose operation was essential to the scheme. Although the hearing was strictly speaking an application for leave to convene meetings to consider the scheme, the court accepted that the applicability of s 427 was a jurisdictional point which ought to be dealt at this earlier stage; if the scheme failed to pass that hurdle there was no point in proceeding further.

[19] [2005] BCC 457.

27 The key point to the bondholders' objection was that it was not "a scheme for the reconstruction of [the company]". It was clear that the scheme meant that current shareholders in the company would have only a small, minority shareholding in Newco. The bondholders argued that it was essential to the concept of reconstruction that the shareholders in the new company were the same (or substantially the same) as the shareholders in the old company.

28 The history of ss 425 and 427 was essential to this point. The former, in its current form, was introduced in 1907. The latter only became law in England in the Companies Act 1929 which statute had its roots in a report of the Company Law Amendment Committee 1925–26 which considered stamp duty and amalgamation. It recommended no stamp duty should be charged on the transfer of property of one company to another "on a reconstruction under which at least 90% of the original capital of the new company was held by shareholders in the old company". It also recommended giving the court power to sanction schemes for amalgamations without the necessity of either company going into liquidation. The result was two strands of legislation: s 55 of the Finance Act 1927 which provided for relief from capital and transfer stamp duty in cases of reconstruction or amalgamation; and what is now s 427. From this history, Mann J concluded[20]—

> "This common source of each strand of legislation is to be borne in mind in construing the expression 'reconstruction' because that word appears in s55 of the 1927 Act and in other legislation. For that reason it is necessary to consider how that word has been construed in a fiscal context."

29 The analysis started with *Re South African Supply & Cold Storage*[21] where it was necessary to construe the words "reconstruction or amalgamation" in a company's memorandum of association. Buckley J observed that neither word had a definite legal meaning and both were commercial rather than legal terms—

> "In each case one has to decide whether the transaction is such as that, in the meaning of commercial men, it is one which is comprehended in the term 'reconstruction' or 'amalgamation'."[22]

30 He continued[23]—

[20] At 464.
[21] [1904] 2 Ch 268.
[22] At 281.
[23] At 286.

> "What does 'reconstruction' mean? To my mind it means this. An undertaking of some definite kind is being carried on, and the conclusion is arrived at that it is not desirable to kill that undertaking, but that it is desirable to preserve it in some form, and to do so, not by selling it to an outsider who shall carry it on—that would be a mere sale—but in some altered form to continue the undertaking in such a manner as that the persons now carrying it on will substantially continue to carry it on. It involves, I think, that substantially the same business shall be carried on and substantially the same persons shall carry it on. But it does not involve that all the assets shall pass to the new company or resuscitated company, or that all the shareholders of the old company shall be shareholders in the new company or resuscitated company. Substantially the business and the persons interested must be the same. Does it make any difference that the new company or resuscitated company does or does not take over the liabilities? I think not. I think it is none the less a reconstruction because from the assets taken over some part is excepted provided that substantially the business is taken, and it is immaterial whether the liabilities are taken over by the new or resuscitated company or are provided for by excepting from the scheme of reconstruction a sufficient amount to answer them. It is not, therefore, vital that either the whole assets should be taken over or that the liabilities should be taken over. You have to see whether substantially the same persons carry on the same business; and if they do, that, I conceive, is a reconstruction."

31 In *Brooklands Selangor Holdings Ltd v Inland Revenue Commissioners*,[24] the court had to consider the word "reconstruction" in a stamp duty context. Pennycuick J said[25]—

> "I will deal first with the question whether those transactions amounted to a reconstruction. In ordinary speech the word reconstruction is, I think, used to describe the refashioning of any object in such a way as to leave the basic character of the object unchanged. In relation to companies, the word 'reconstruction' has a fairly precise meaning which corresponds, so far as the subject matter allows, to its meaning in ordinary speech. It denotes the transfer of the undertaking or part of the undertaking of an existing company to a new company with substantially the same persons as were members of the old company."

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[24] [1970] 1 WLR 429.
[25] At 444.

32 He then turned to consider the application of those principles to the case before him[26]—

> "Turning to the facts of the present case, the substance of the scheme is that the undertaking of B.S.R. is partitioned between Plantation Holdings and the minority shareholders in proportions corresponding to their holdings of the ordinary stock of B.S.R., the preference stockholders being paid off. That partition, in order to comply with the requirements of company law, was carried out by the transfer of part of the undertaking of B.S.R. to the new company in consideration of stock in the transferee company, *i.e.* the taxpayer, and the issue of that stock directly to the minority shareholders by way of reduction of capital. The effect of that transaction is that the holders of the stock in the tax payer company are most substantially different from the holders of the stock in B.S.R. That is to say, they consist of approximately half only in value, though the vast majority in number, of the holders of the stock in B.S.R. So the transaction represents the transfer of a part of B.S.R.'s undertaking from the holders of the whole of the stock in B.S.R. to the holders only of approximately half the stock in B.S.R. That, I think, involves a substantial alteration in the membership of the two companies within the meaning of the passages which I have quoted from the judgments of Chitty J and Buckley J.[27] It seems to me that that transaction is not a reconstruction and that a transfer made pursuant to that transaction falls neither within the letter nor within the intent of section 55."

33 As the court in *Mytravel* noted, these passages in *Brooklands* were approved in other cases in a stamp duty context (*Baytrust Holdings Ltd v IRC*[28] and *Swithland Investments Ltd v IRC*[29]) and by Millett J (as he then was) in *Re Courage Group's Pension Schemes*[30] in the context of a proposed alteration in a pension scheme[31]—

> "The essential character of a corporate reconstruction is that substantially the same business is carried on and substantially the same persons continue to carry it on."

[26] At 446.
[27] In *Hooper v Western Counties and South Wales Telephone Co Ltd* (1892) 68 LT 78 and *In re South African Supply and Cold Storage Co Ltd* [1904] 2 Ch 268, respectively.
[28] [1971] 3 All ER 76.
[29] [1990] STC 448.
[30] [1987] 1 WLR 495.
[31] At 541.

34 More recently in *Fallon v Fellows (Insp of Taxes)*,[32] Park J had to consider whether a scheme was for the purposes of reconstruction or amalgamation in a capital gains tax context. Referring to the *South African Supply and Cold Storage Co* case, he stated[33]—

> "In the context I think it is clear that when the learned judge referred to the persons carrying on an undertaking, he had in mind the shareholders who were carrying it on through a corporate body. He was referring to persons carrying on an undertaking in the sense of owning it, not in the sense of being involved in the management and conduct of the business operations. The basic concept is that one starts with a group of shareholders who own a business through one corporate vehicle and one ends with the same group of shareholders or substantially the same group of shareholders, who own the same business or substantially the same business still through a corporate vehicle, but now through a different corporate vehicle."

35 Mann J noted how the restricted meaning of "reconstruction" drawn from stamp duty cases was particularly apparent in *Oswald Tillotson Ltd v ORC*:[34]

> "When I come to consider the purpose of this section, and to see why there is to be immunity and exemption from transfer stamp duty, I find that it is because the old company is really represented or replaced by the new company, and the shareholders in the new company are to be in substance the shareholders of the old company. It is because there has been not an out-an-out transfer for cash but merely a reconstitution of the same corporators in a new company. Bearing that principle in mind and realising that the test is to see whether or not there is a real identity as to not less than 90% of the shareholders, I come to the conclusion that the meaning of the word 'issue' is something more than the mere giving of an allotment letter to an old shareholder enabling him to vote with the shares offered to him at his volition."

36 The bondholders argued in *MyTravel* that the common source of the English fiscal and corporate legislation which allowed for reconstruction in a particular tax context indicated that the same approach ought to apply to the word "reconstruction" in s 427. The applicant company countered by submitting that *South African Supply*

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[32] [2001] STC 1409.
[33] At para 13.
[34] [1933] 1 KB 134, at 155.

set the relevant test in a corporate and non-tax context. Most of the other authorities were tax cases (mainly stamp duty) and if "reconstruction" had acquired a narrower meaning in that context (requiring a substantial identity of shareholders in the old and new entity) that was peculiar to the relevant stamp duty provisions. There was, it argued, no basis for the narrower fiscal meaning to colour reconstruction in a company law context.

37 Mann J accepted the submissions of the bondholders[35]—

> "I consider that I am constrained by authority not to do so. I do not consider that the authorities can be dismissed in the manner which Mr Sheldon suggests. Although the stamp duty cases were obviously decided in their own legislative context, and whilst I accept that the statutory provisions in issue in those cases contain express qualifications in relation to shareholdings, the remarks made by the judges are general in their nature and they make sense in conceptual terms. The thrust of them involves treating the company for these purposes as the same as its corporators. The company is reconstructed when those corporators, who for these purposes are treated as carrying on the business of the company, are the same in both the old and the new companies. In the present case, where that substantial identity is not present, what might be said to be reconstructed is not so much the company as its debts. The undertaking of the company is, for these purposes, different from the company itself . . .
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> Furthermore, and more importantly, the tax cases take as their parting point, either directly or indirectly, the dicta of Buckley J in *South African Supply*. Those remarks were uttered not in a fiscal context, but in a company law context, albeit not in the context of a statutory provision because the judge was there considering the meaning of the word in the memorandum of association of the company. In my view, despite the earlier words which suggest that the word has no definite meaning, and which suggest that it should be given its commercial meaning, when Buckley J considers what it means on p.286 he was elaborating some of the key features, or perhaps indicating what he thought that the term would mean to commercial men. Reading that passage fairly, it seems to me to be clear that he thought it was of the essence of a reconstruction that substantially the same shareholders should be involved in both old and new companies. He refers to the fact that 'the persons now carrying it [*i.e.* the undertaking] on will substantially continue to carry it on'. It is

[35] At paras 30–31.

> clearly implicit that the persons who are carrying it on are the shareholders. It is true that he uses the expression 'the persons interested'—an expression seized on by Mr Sheldon. However, in its context that seems to me to be a synonym for the shareholders. The sentence in which it is used follows immediately after a sentence in which he refutes the suggestion that 'all the shareholders of the old company shall be shareholders in the new company'. He explains this by saying that 'substantially' the same people must be involved. The emphasis in that section is on the word 'substantially'. That is the point that he is addressing. I see no warrant for treating him as extending the class of people who should be treated as carrying on the undertaking. That means the shareholders. So when he says at the end of the passage in question, 'you have to see whether substantially the same persons carry on the same business; and if they do, that, I conceive, is a reconstruction', he is referring to the shareholders who he clearly treats as being the persons carrying on the business for these purposes. Of course, he was not considering an insolvent company, but I do not think that the persons who, for these purposes, are carrying on the business changes when a company becomes insolvent. The shareholders are still carrying on the business as much they were before (for these purposes), but the interests of the people who have to be taken into account change because the interests of the creditors intrude—see the passage from *Kinsela* cited above. This does not change the analysis of who is carrying on the business for the purpose of Buckley J's exposition. I think that his emphasis on the identity of shareholders is reinforced by what he says at p.287 when, in the context of an amalgamation, he requires that substantially all the corporators should be parties."

38 Accordingly, approval for the scheme could not be given under s 427. There was therefore no point in holding any meetings to consider the scheme and the court declined to order them. It is to be noted that the applicant appealed the decision in this case, but not on this point.

The meaning of "reconstruction" in art 127 of the Companies Law

39 What then was the Jersey court to make of the word "reconstruction" in art 127 of the Companies Law, in a context where that provision (indeed the whole process relating to arrangements) was virtually identical to that of the equivalent English statutes and where English case law on equivalent provisions typically carries significant persuasive influence on a Jersey court.

40 The Royal Court decided to interpret the word "reconstruction" in its own context, taking account of English case law guidance on its meaning in a general commercial milieu, but declined to be constrained in the manner indicated in *MyTravel* since the Jersey provision does not share the same fiscal source and therefore the English case law construing that word in a fiscal context had no relevance.[36] Instead, working from first principles, it found the word "reconstruction" not to be a legal term and thus has no definitive legal meaning—following *Re South African Supply* (para 46 of the judgment), and it is a commercial term, without an exact meaning or definition. Accordingly, the court must decide whether a given transaction would be considered to be a "reconstruction", "in the meaning of commercial men".[37]

41 The court accepted that the facts of the application were fundamentally different from those in *MyTravel*. The arrangement did not involve the transfer of the company's undertaking to a new company in which the existing shareholders did not participate. The shareholders were to remain as shareholders of the company and would receive the proceeds from the company's realised assets. There was to be a transfer of some assets to a new company but these were assets were with associated liabilities which would take some time to deal with and resolve. The court therefore did not need to decide whether "reconstruction" requires that substantially the same business shall be accrued on by substantially the same persons (as indicated in *Re South African Supply*) (paras 46–48 of the judgment).

42 The court agreed with the submissions made on behalf of the applicant that: by definition "reconstruction" must be narrower than that of "arrangement"; a reconstruction must entail some form of reconstruction of the company's affairs from a commercial perspective; and "reconstruction" implies some form of continuance.[38] It also accepted that what was proposed was in fact a reconstruction.

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[36] At para 45.
[37] At para 46.
[38] At para 49.

First, the scheme proposed the collapse of the company's balance sheet. This would entail the realisation of its assets, discharge of its liabilities and distribution of excess cash reserves to shareholders with the ultimate aim being an orderly dissolution. Secondly, the scheme involved a change in the current duties of the board of directors and their freedom to manage the company's affairs. These duties were currently defined in the articles of the company and in law (primarily art 74(1) of the Companies Law). If the scheme were sanctioned by the court, the directors would be obliged to put it into effect and thereby bring the company's commercial affairs to an end. Thirdly, the scheme would effect an alteration of the shareholders' relationship with the company. That relationship was likewise governed by the articles and the law. If the scheme were sanctioned by the court, the shareholders would have rights relating to the management of the company's affairs in that they could insist on implementation of the scheme and its implantation towards dissolution by a certain date.[39] The changes, in the court's view, were comprehensive changes in the company's affairs.[40]

43 As the company argued, the scheme could be contrasted with the more usual form of arrangement that has historically come before the court for sanction whereby company A acquires company B. There the scheme objects and terms are wholly or primarily discharged once the scheme is completed; the share transfer does not change company B's balance sheet; once A owns B, there is no legal change in the relationship between company B and its board of directors or between company B and its shareholders; even if the composition of the board of directors of company B changes (as it often does in a takeover), that does not change the relationship between the board and the company. Even if the articles change as a result of the takeover, that does not change the fundamental nature of the board's or shareholders' relationship with the company, which are still governed by the articles.[41] Such a scheme does not therefore amount to a reconstruction.

Conclusion

44 The judgment in *LXB* is important for two reasons. First, it declined to adopt a narrow construction of "reconstruction" in art 127 of the Companies Law. Beyond the requirements that it must entail some form of change to a company's affairs from a commercial

[39] At paras 50 and 54.
[40] At para 51.
[41] At para 52.

perspective and a degree of continuance, it was not prescriptive as to what constitutes a "reconstruction". It left open the issue of whether reconstruction should be wholly or partly determined by reference to shareholder composition, that is whether it requires similar or equivalent participation by the existing shareholders in the reconstructed company. However one can anticipate a flexible, fact-based approach to this issue with a close analysis of what is actually proposed as to change to and continuance of the undertaking. In its rejection of the narrower conclusion of *MyTravel* it opens the way for a broader range of corporate reconstructions in the context of an arrangement or compromise Secondly, and more importantly, it emphasises an important point of local jurisprudence. Even though the wording of the statutory provision may be closely drawn on an English equivalent, and the typically English case law interpreting that equivalent will be persuasive on a Jersey court, the context of that case law is important. As here, where a particular construction has arisen for reasons which have no relevance to Jersey, the Royal Court will return to first principles and interpret the Jersey provision in the local context.

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