

## Establishing a Hedge Fund in the BVI

Are you thinking of setting up an investment fund in the BVI? This document provides an overview of the hedge funds industry in the BVI and why it is such an attractive jurisdiction for hedge funds. We explain the regulatory regime in the BVI, the fund structures and fund products available and how we can support you from the initial structuring and planning conversations, all the way through to the launch and ongoing support.

The investment funds industry in the BVI is regulated by the Financial Services Commission (the **Commission**) and the primary legislation which governs the industry is the Securities and Investment Business Act 2010, as amended (**SIBA**).

This guide focuses on the open-ended hedge fund industry, but it should be highlighted that the BVI has a separate regulatory regime for private equity and other closed-ended funds (known as Private Investment Funds or **PIFs**) – these are discussed in a separate legal guide. Do let us know if you would like further details.

### What factors determine whether a hedge fund must be regulated in the BVI?

Generally, an entity will be considered to be a ‘mutual fund’ and will be subject to regulation under SIBA if:

- It collects and pools investor funds for the purpose of collective investment
- It is open ended (ie its equity interests are redeemable at the option of its investors)
- The equity interests that it issues and that are redeemable entitle the holder to receive an amount calculated by reference to the value of a proportionate interest in the whole or a part of the net assets of the fund

### Which hedge fund product is right for me?

The BVI benefits from a diverse offering of hedge fund products suited to everyone from the start-up manager setting up an incubator fund to established institutional fund managers with billions under management. Its pragmatic flexibility over the twenty-five years of prudent regulation has actually been a large driver for the popularity it has generated amongst the global investment funds community.

The characteristics of the products available are set out below. If you need help choosing the most suitable product for your fund, please contact us.

#### Incubator fund

The incubator fund is aimed at emerging managers and allows them a two year incubation or “validity” period (with an extension of up to 12 months available with permission from the Commission) to establish a track record and test its viability. During that period, the fund can operate with light regulation, very limited mandatory service providers and without having to carry out an audit.

An incubator fund must remain within the following thresholds:

- Having no more than 20 investors
- Each investor, having been invited to invest, must make a minimum initial investment of US\$20,000
- The net assets of an incubator fund must not at any time exceed US\$20 million

Before the end of the validity period (or, if earlier, when it exceeds the relevant thresholds for two consecutive months) an incubator fund is required to convert to a private, professional or approved fund. If the fund determines that it is not viable to continue, it is required to wind up its operations. The incubator fund is required to conduct an audit as part of its conversion to a private or professional fund.

An incubator fund benefits from a fast track approval process, enabling it to commence business as an incubator fund two business days after submitting a complete application to the Commission.

## Approved fund

The approved fund is aimed at managers looking to establish a fund with a private offering to a small group of investors on a longer term basis. An approved fund is restricted to:

- Having no more than 20 investors
- Having net assets which do not at any time exceed US\$100 million

The approved fund has similar characteristics to the private fund recognised under SIBA, including no minimum initial investment for investors. Unlike the private fund, the approved fund is not required to appoint an auditor. It is also not required to appoint a manager or a custodian, unless it is set up as an SPC (please see below for more details). It is required to appoint an administrator to ensure there is some suitable oversight of its operations.

Like the incubator fund, the approved fund benefits from the fast track approval process, enabling it to commence business as an approved fund two business days after submitting a complete application to the Commission.

## Private fund

Private funds do not have a minimum initial investment amount for each investor or any “professional” or “sophistication” test for investors. This has made them popular with start-up managers, allowing a friends and family offering.

A private fund is restricted to either:

- Having no more than 50 investors, or
- Only making an invitation to subscribe for or purchase fund interests on a private basis

Private funds must be recognised by the Commission before they carry on business. Historical policy guidelines issued by the Commission under the previous mutual funds regime suggested that a fund will be regarded as having commenced its business when a prospectus, or other document the purpose of which is to make an invitation to purchase or subscribe for shares of the fund, is published.

## Professional fund

Professional funds are the most popular category of regulated fund and make up approximately 65 per cent of all regulated funds in the BVI. The interests in a professional fund may only be made available to “professional investors” and the minimum initial investment by each professional investor must not be less than US\$100,000 (or other currency equivalent), unless the investor is an “exempted investor” in which case there is no minimum initial investment.

A “professional investor” is a person:

- Whose ordinary business involves, whether for that person’s own account or the account of others, the acquisition or disposal of property of the same kind as the property, or a substantial part of the property, of the fund; or
- Who, whether individually or jointly with their spouse, has a net worth in excess of US\$1,000,000 (or other currency equivalent) which does include the primary residence

An “exempted investor” means:

- The manager, administrator, promoter or underwriter of the fund; or
- Any employee of the manager of the fund

A professional fund may carry on its business or manage or administer its affairs for a period of up to 21 days without being recognised under SIBA.

## Public fund

A public fund is generally viewed as a retail product. Accordingly, the regulatory burden placed on a public fund is considerably higher than that of a private or professional fund.

Public funds must be registered by the Commission before they carry on business. A public fund is not subject to any BVI restrictions on the categories or number of investors it may invite to invest in the fund.

Registered public funds may not make an invitation to the public or any section of the public to purchase shares unless prior to such invitation they publish a prospectus which complies with SIBA and the Public Funds Code, which is approved by and signed on behalf of the fund's directors and which is registered by the Commission. Investment funds in the BVI are subject to various ongoing statutory requirements under SIBA and other secondary legislation. Incubator and approved funds are subject to lighter regulatory requirements, whereas the burden is higher for public funds.

Please contact us for our separate guides on continuing obligations for all of these types of funds.

## What hedge fund structure should I use?

The vast majority of BVI hedge funds are established as companies limited by shares under the BVI Business Companies Act 2004 (**BCA**) and we would generally recommend using this structure. Limited Partnerships are also quite common. Although permitted, we rarely see unit trusts but we would of course be happy to discuss them with you.

### BVI Business Companies

A BVI Business Company is a separate legal entity from its investing shareholders (whose liability is limited by statute). The shareholders of a BVI Business Company have no direct legal or beneficial interest in any of the assets of the company which are instead legally and beneficially owned by the company itself.

The BCA is very flexible for structuring funds. For example, there is no concept of "authorised capital" or "share capital" under BVI law, and shares do not need to have any par value or capital attributed to them. The directors may also designate different series of shares within each class of shares without the need to amend the constitutional documents of the fund, giving flexibility to funds wishing to use series accounting techniques to achieve equalisation of performance fee allocations among shareholders.

The BCA also allows private, professional, public, incubator and approved funds to be structured as SPCs. An SPC is a single company with the benefit of statutory segregation of assets and liabilities between segregated portfolios established within the company. The assets and liabilities of each segregated portfolio are legally segregated from both the assets and liabilities of each other segregated portfolio and the general assets of the company (ie those assets not held within one or on behalf of any segregated portfolio). SPCs are popular for multi class or umbrella funds in which two or more segregated portfolios use different investment strategies.

### Limited partnerships

A BVI limited partnership is formed by a general partner and at least one limited partner executing a limited partnership agreement (or adopting a statutory model form agreement) and the registered agent submitting a registration statement and registered agent consent to act to the BVI Registrar of Limited Partnerships. The partnership agreement forms the internal governing document of the limited partnership, dealing with issues such as partnership contributions and withdrawals and the day-to-day running of the limited partnership and does not have to be filed with the BVI Registrar.

A BVI limited partnership can elect whether to have a separate legal personality distinct from its partners. The general partner of a BVI limited partnership is ultimately liable for the debts and obligations relating to the limited partnership. As a matter of BVI law, a limited partner BVI limited partnership is not liable for the debts and obligations of the limited partnership (save for the amount contributed and any unpaid commitment).

The general partner of a BVI limited partnership is typically a company or LLC and does not need to be a BVI entity. There is no requirement for the general partner to appoint a BVI resident director or for the directors to register with the Commission.

## What service providers will I need to get started?

SIBA requires BVI hedge funds to appoint the following service providers:

	Investment Manager	Administrator	Custodian	Auditor	Authorised Representative
Incubator	*	*	*		✓
Approved	*	✓	*		✓
Private	✓	✓	✓	✓	✓
Professional	✓	✓	✓	✓	✓
Public	✓	✓	✓	✓	✓

\*Incubator and approved funds do not have to appoint these service providers unless they are set up as SPCs. If they are set up as SPCs, the incubator or approved SPC fund can apply to the Commission for an exemption from the requirement to appoint an investment manager and/or custodian, but must appoint an administrator.

Every BVI hedge fund is required to appoint an authorised representative in the BVI to liaise between the fund and the Commission. This is a service offered by Harneys Corporate Services Limited's associated services business, Craigmuir Authorised Representative Limited.

## I have existing relationships with some service providers but they are not based in the BVI. Can I appoint them to my BVI fund?

A BVI hedge fund is not required to appoint BVI service providers and so you are likely to be able to use the providers you are already familiar with. The Commission requires (in accordance with SIBA and policy guidelines) that a functionary of a BVI hedge fund (ie the manager, investment advisor, administrator or custodian) must satisfy the Commission's fit and proper criteria. But to fast-track this process, the Commission will generally automatically accept a functionary that is located and appropriately regulated in a "**Recognised Jurisdiction**".

The following countries have been designated by the Commission as Recognised Jurisdictions:

Argentina, Australia, Bahamas, Bermuda, Belgium, Brazil, Canada, Cayman Islands, Chile, China, Curacao, Denmark, Finland, France, Germany, Gibraltar, Greece, Guernsey, Hong Kong, Ireland, Isle of Man, Italy, Japan, Jersey, Luxembourg, Malta, Mexico, Netherlands, New Zealand, Norway, Panama, Portugal, Singapore, Spain, South Africa, Sweden, Switzerland, United Kingdom, and the United States of America.

Accordingly, an application for approval, recognition or registration of a fund whose functionaries are domiciled in a Recognised Jurisdiction and hold the appropriate regulatory status in that jurisdiction will generally be processed without further assessment of the fit and proper status of such functionaries.

The Commission may also accept a functionary domiciled in another jurisdiction if the applicant can satisfy the Commission that the jurisdiction has a system for the effective regulation of investment business, including funds business.

Whilst not deemed to be functionaries in accordance with SIBA, clearly directors and auditors are two other key service providers to a fund. Again, and unlike other fund jurisdictions, there is no requirement for a director or the auditors of a BVI hedge fund to be based in the BVI. The auditor of a public fund (but not any other category of BVI hedge fund) must be approved by the Commission.

## I am also going to need to set up a new investment management vehicle to manage my BVI fund. Can you assist with that?

Absolutely, although it should be pointed out again that the investment management vehicle can be based in any of the Recognised Jurisdictions listed above if required.

But if you would like to establish an investment manager in the BVI (and our clients commonly do), the two basic regulatory options are (i) the full investment management license under Part I of SIBA; or (ii) the approved manager regime.

The application for a SIBA licence is substantial and involves the submission of a wide variety of documents to the Commission. Whilst a number of our clients do hold the full SIBA license, the approved manager product has proved hugely attractive as it provides eligible fund managers and advisers with a less onerous regulatory regime. Those eligible for approved manager status may submit a simple application to the Commission and commence business seven days later without waiting for formal approval.

The key restriction for an approved manager is that aggregate assets under management of all open ended funds under the management of the approved manager cannot exceed US\$400 million and capital commitments of all closed end funds under management cannot exceed US\$1 billion.

Please contact us if you would like further information on either of these options.

## Any other regulatory obligations I should be thinking about?

A BVI hedge fund also has the following regulatory obligations under BVI law:

- Appoint a money laundering reporting officer (in accordance with the fund's obligations under the BVI Anti-Money Laundering Regulations 2008 and the BVI Anti-Money Laundering and Terrorist Financing Code of Practice 2008 (as amended)). This person is often one of the directors or a representative of the administrator who is conducting the onboarding of investors on behalf of the fund
- Put in place procedures for investor on-boarding which address typical investor identification requirements and the reporting of suspicious activities to the BVI Financial Investigations Agency, and documenting how the fund complies with BVI anti-money laundering procedures (if an administrator is not appointed given they would naturally perform this function)
- Register and report with the BVI International Tax Authority (*ITA*) to meet the fund's automatic exchange of information obligations under the United States Foreign Account Tax Compliance Act (*FATCA*) and the OECD Common Reporting Standard (*CRS*) as implemented in the BVI.

Harneys would be pleased to advise on compliance with the above obligations.

## What fees are payable to the Commission?

Fees payable by BVI funds to the Commission are competitive and lower than in most other offshore and onshore jurisdictions. Fees are payable on application and annually and are set out in the table below.

	Application Fee (US\$)	Annual Fee (US\$)**
Incubator and Approved Funds	US\$2,000*	US\$1,200
Private and Professional Funds	US\$850	US\$1,200
Public Funds	US\$1,200	US\$1,800

\*This fee is inclusive of the \$200 fee for obtaining an original certificate of recognition from the Commission

\*\*This fee is halved for the first year where an application is made after 30 June

## How long will it take to set up my hedge fund?

The time taken to set up your fund will depend largely on how long it takes to agree terms with service providers and finalise your strategy and offering documents. However, a rough guide to the time frame for establishing each type of fund is set out below:

Fund	Incorporation/Formation of Company/Partnership	Time to Prepare Documentation & Submit Application to Commission	Time for Approval/Recognition/Registration by Commission
Incubator	Same day* (allow 3 days for documents to be returned from the registry)	Up to 3 weeks	2 business days for a complete application
Approved	As above	Up to 3 weeks	As above
Private	As above	Up to 5 weeks	Within a week
Professional	As above	Up to 5 weeks	Within a week
Public	As above	Up to 8 weeks	3 weeks

\* We must obtain “know your client” information and a retainer before we can submit the formation/incorporation request to the registry

In assisting you with the formation of a new fund, our services are likely to include the following, although we will always tailor our provision to meet your specific needs:

- Advising on the structure of the fund
- Preparing constitutional and organisational documents, including bespoke articles of association for a BVI business company limited by shares or limited partnership agreement for a limited partnership
- Drafting or reviewing from a BVI perspective the private placement memorandum and subscription agreement
- Drafting or reviewing from a BVI perspective the investment management agreement between the fund and the manager
- Reviewing and commenting, from a BVI perspective, on the administration agreement
- Reviewing the fund’s valuation policy
- Preparing resolutions for the launch of the fund
- Advising on the regulatory requirements in the BVI and preparing and making an application for approval/recognition or registration of the fund with the Commission
- Making all necessary filings in respect of the fund
- Liaising with Harneys Corporate Services Limited and Craigmuir Authorised Representative Limited in relation to the provision of registered office/registered agent/authorised representative and related corporate services for the fund
- Providing you with a summary of the continuing obligations of your fund

In addition, we have excellent relationships and work closely with a variety of other service providers including administrators, custodians, brokers, auditors and independent directors and would be very happy to make introductions to you if you have not already identified the service providers you intend to use.



For more information and key contacts please visit [harneys.com](https://www.harneys.com)

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