

## The Many Benefits of British Virgin Islands Investment Funds



*By Ayana Hull* - SENIOR ASSOCIATE

One of the main reasons the British Virgin Islands (**BVI**) is often chosen as a jurisdiction for investment managers to set up their fund vehicles is the flexibility the legislative regime provides for structuring these funds. There are over 2,200 regulated funds and almost certainly a similar amount of unregulated fund vehicles established in the BVI. Our understanding through years of working alongside some of the biggest names in the industry is that investment managers are seeking a jurisdiction with three basic characteristics: political stability, an efficient and reliable legal system and experienced industry practitioners on the ground. The BVI happily possesses all three. This has led to a very wide range of clientele showing a keen interest in the jurisdiction, from well-established institutional fund managers in major jurisdictions around the world with billions in assets under management all the way through to individuals wishing to set up incubator funds with a small amount of start-up capital and wishing to establish a successful track record. The legislation allows for this diversity by offering a product suitable to every shape and size of investment business and ensures that the BVI stays on the cutting edge of global financial services.

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### Structuring Vehicles

Although the limited partnership and the unit trust are available vehicles through which fund managers who are more familiar with those investment structures can structure funds, the limited liability company (a BVI business company limited by shares) is still the most popular for investors whether the fund to be structured is a stand-alone fund or a master-feeder fund. Since the BVI Business Companies Act, 2004 introduced the ability for funds to be structured as segregated portfolio companies (**SPCs**), fund managers have also taken advantage of this type of company in structuring their BVI funds.

### Choosing “a BVI”

The standard BVI business company is very useful where a fund may be utilising a single investment strategy, investing in securities of a similar nature and risk profile or focusing on one type of investment product. It can also be used to structure an umbrella fund, whereby each sub-fund is demarcated by a separate class of shares in the fund, each sub-fund is traded as a separate investment fund and the accounts of each sub-fund are separated from each other by the creation of separate class accounts. There is a fundamental limitation to using the standard BVI business company as a structuring vehicle however - that of third party liability. Although for internal accounting purposes, the accounts of each class of shares in the fund will be regarded as separate and investors will only receive proceeds from the class of shares in which that particular investor invested, this distinction amongst sub-funds within a fund, does not hold true as it pertains to third party creditors. A creditor of a particular sub-fund in a fund structured through a standard BVI business company will have recourse to the assets of any other sub-fund within the fund, where the assets of the particular sub-fund are not sufficient to satisfy the amount owed to the creditor.

### The SPC alternative

It is for this reason that the SPC is gaining traction as a structuring vehicle for BVI funds that employ a multi-investment strategy for multiple investment products and which carry different risks and realization horizons. The SPC structure contains one or more segregated portfolios each of which is regarded as a separate legal entity for asset protection purposes. Deploying a BVI SPC is a particularly useful tool in the hands of a fund manager in order to segregate investment products and risks in a more efficient way so that the assets attributable to a particular segregated portfolio are held by the company as if a separate fund and to ensure that these assets are not available to meet the company's general liabilities or the assets attributable to other portfolios. Hence, where segregation of assets is desired, the SPC provides a higher level of protection for these assets under BVI law.

Further, as start-up fund managers seek to find more economical ways to launch funds in a much more careful investment climate, trends are also developing in the BVI whereby the SPC is not only used within the same fund structure but also by unrelated funds and investment managers who are seeking to gain economies of scale by sharing a single BVI SPC platform. On such a platform, all the unrelated entities similarly share a single offering document with each fund and fund manager being allocated its own segregated portfolio on the platform and with a specifically tailored supplement which

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would provide greater details of the specifics of the investment program of each fund and the specific risks applicable to the particular fund and investment program.

### **Costs**

The BVI is not only flexible in terms of structuring vehicles; it is flexible in terms of costs as well. The costs involved in setting up a BVI fund are very modest when compared to other jurisdictions and this low cost-base compared to most other offshore jurisdictions also places the BVI in an advantageous position. Initial and annual government and regulatory fees associated with establishing a stand-alone fund are in the range of \$2050 - \$2800 (initial fees) and \$1,350 - \$2100 (annual on-going annual fees) depending on the maximum number of shares the fund is authorised to issue. Legal fees in relation to fund documentation will vary based on a variety of factors but are very competitive with other jurisdictions as well.

Similarly, initial and annual government and regulatory fees will be in the range of \$4,750 - \$5,500 (initial fees) and \$4,050 - \$4800 (annual on-going fees) for an SPC with two segregated portfolios depending on the maximum number of shares the fund is authorized to issue. Again, legal fees will depend on the number of portfolios and the approach to drafting the documents (the offering memorandum and each supplement).

Also, with SPCs, as there is no limit on the maximum number of portfolios an SPC can create and the maximum total initial fees in any given year payable by a mutual fund SPC is capped at a maximum of US\$10,000, the SPC platform mechanism provides an additional structuring option available for multiple unrelated start-up managers to establish investment vehicles by sharing the annual fees associated with a single SPC.

### **Recent Augmenting Initiatives**

Coupled with the mutual funds product is a new and less onerous regulatory regime pursuant to which BVI domiciled investment managers (approved managers) can obtain approval status within a 30-day period but are able to commence business in this capacity seven days after the application for approval is made to the BVI regulator. Where time to market is critical, the approved manager product can be quite convenient for managers and advisors. It is also a good asset in the regulatory basket of a fund manager as the manager can boast a regulated product (which most investors prefer) whilst avoiding exposure to the full gamut of the licensing regime.

Further, the flexibility of being an approved manager is such that the approved manager can act as manager or advisor to any number of BVI private or professional funds as well as funds domiciled outside the BVI in a jurisdiction which is deemed a "recognised jurisdiction" if they have the characteristics of a private or professional fund. The approved manager is subject to caps of aggregate assets under management of US\$400 million for open-ended funds and aggregate capital commitments of US\$1 billion for closed-ended funds. Only where an approved manager exceeds these respective caps and continues to do so for three consecutive months, will such a manager need to become licenced under the Securities and Investment Business Act, 2010 (*SIBA*).

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Whilst an approved manager must appoint an authorised representative, it is not required to satisfy any capital adequacy or professional indemnity insurance requirements. There is also no requirement to appoint a compliance officer and the Regulatory Code, 2009 does not apply to this type of manager. Such a manager is also not required to appoint an auditor or submit audited financial statements. Financial statements together with a director's certificate and a report on the approved manager provided to the Commission within six months of the end of each financial year will be sufficient.

The flexibility of the BVI as a jurisdiction was also recently demonstrated with a very pragmatic decision to allow private equity funds the choice of using the word "fund" in their names. Closed-ended funds are not required to be regulated under SIBA and prior to this forward-thinking decision could not use the word "fund" in their names as only entities required to be regulated (open-ended funds) could do so. The decision is a welcomed augmentation to the BVI fund product offering.

### **Judicially Sound**

Yet another feature shouldering the BVI fund product which is noteworthy of highlighting, and which gives comfort to managers and investors, is the dedicated commercial court which has its seat of operation in the BVI. The commercial court has always taken a judicial approach in hearing fund related disputes which tends to provide certainty to managers that the mechanisms set out in the offering documents of BVI funds to control liquidity and related operational issues can be relied upon. A consistently reliable legal system is critical to managers in choosing a jurisdiction to domicile their funds and provides another significant weapon in the BVI's arsenal of its financial services product offering.

### **AIMFD Ready**

Managers and investors who are also concerned as to whether BVI funds are suitable for their European investors in light of the Alternative Investment Fund Manager Directive (**AIMFD**) would be pleased to know that BVI funds continue to be suitable investment products for European investors as the BVI has taken the requisite steps to ensure that BVI funds qualify for passporting in the EU. The BVI has entered into a cooperation agreement with the European Securities and Markets Authority (**ESMA**) and has Tax Information Exchange Agreements (**TIEAS**) in place with many European countries (with more in the pipeline) in accordance with their domestic private placement rules and in an effort to ensure that BVI funds are in position to comply with the requisite EU directive as necessary.

### **FATCA Prepared**

Likewise, investors may have concerns with the effect that the US Foreign Account Tax Compliance Act (**FATCA**) and its UK counterpart have on BVI domiciled funds. In November of 2013, the BVI signed an Intergovernmental agreement (**IGA**) with the UK and a similar agreement, the Model 1B IGA with the USA in July of 2014. The Agreements mean that BVI funds will report certain information about US and UK investors to the BVI International Tax Authority who will then pass it on to the IRS and HMRC respectively. The approach has been welcomed by industry as it simplifies FATCA compliance and reporting obligations for BVI domiciled hedge funds and private equity funds.

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### **Jurisdiction of Choice**

The BVI therefore offers a sophisticated, soundly regulated, highly regarded and well respected array of fund structuring products at a very competitive cost. Investors are familiar with these products, they are comfortable with how they work and as a result, these products are extremely popular in the global financial market. These products are underpinned by a mature regulatory infrastructure, a well-developed financial services industry, a proven judicial system, creditor-friendly insolvency legislation, and a jurisdiction that is eager to take the necessary internationally required measures to ensure that its funds continue to be marketable to investors in onshore jurisdictions. All of these benefits combine for a very diverse BVI fund product, which in turn makes the BVI a practical, flexible and suitable jurisdiction of choice for managers and investors ■

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