



Overview of Investment Funds in the British Virgin Islands

Introduction

The British Virgin Islands (BVI) is now the second largest jurisdiction for regulated investment funds in the world. But what exactly makes it so appealing to fund sponsors and investors? And what are some of the benefits of choosing the BVI over other offshore jurisdictions?

BVI FUNDS:

Why Choose the BVI for Establishment of an Investment Fund?

The BVI possesses many advantages to fund sponsors and investors including: a sophisticated legal system based on English law and appealable to the Privy Counsel in the UK; a tax neutral environment; a stable political and economic jurisdiction committed to remaining fully compliant with international financial regulatory norms and regulations; no regulatory restrictions on investment policies or strategies; no requirement to appoint local directors, functionaries or auditors; a fast track procedure for professional fund approval; a range of professional service providers; and comparably low start-up and ongoing fees and costs.

Choice of Entity (Investment Funds)

In the BVI, the fund vehicle for investment funds can be a business company, segregated portfolio company, unit trust, partnership or other body, thereby offering more choices than those available in Bermuda or the Cayman Islands.

A fund may be open-ended or closed-ended. Closed-ended funds possess a fixed capital; so while the asset prices may fluctuate, the amount of shares that the fund possesses does not shift over time. Investors do not have the right to redeem their interest in a closed-ended fund without the consent of the fund's manager. These types of funds are unregulated. Open-ended funds, on the other hand, are comprised of shares, units or limited partnership interests that may then be redeemed periodically by fund investors. Unlike closed-ended funds, open-ended funds are regulated.

Types of Funds

The types of open-ended funds in the BVI are: (1) professional funds, (2) private funds, (3) public funds, (4) incubator funds and (5) approved funds. Professional, private, and public funds must be registered or recognized and are regulated by the SIBA.¹ Incubator and approved funds were recently created as of June 2015 and are governed by The Securities and Investment Business (Incubator and Approved Funds) Regulations 2015.

1. Professional Funds

Professional funds are open-ended. They make up more than 70% of the registered and recognized funds in the BVI. To qualify as a professional fund the entity's constitutional documents must specify that its shares are only made available to "professional investors". A "professional investor" is a person:

- A. whose ordinary business involves, whether for that person's own account or the

¹ The Securities and Investment Business Act, 2010 of the British Virgin Islands ("SIBA").

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

B. who has signed a declaration that he, whether individually or jointly with his spouse, has net worth in excess of such sum \$1,000,000, and whose initial investment is not less than \$100,000.

2. *Private Funds*

Private funds are open-end funds with constitutional documents that specify:

- a. the fund is not authorized to have more than fifty investors; or
- b. an invitation to subscribe for, or purchase, fund interests issued by the fund shall be made on a private basis only.

A “private basis” invitation includes invitations made to specified persons without the intention of their shares becoming available to others, or to those with whom there is a pre-existing relationship (business or otherwise).

3. *Public Funds*

Public funds are those not falling into the criteria of either professional or private funds. They possess no specific investor criteria; instead, they are afforded a level of flexibility that comes with a higher level of oversight.

4. *Incubator Funds*

Incubator funds are designed to allow managers to quickly and cheaply set up a fund so that they can establish an investment strategy track record. If the manager’s strategy is successful within two years of formation, the incubator can easily be converted into a private, professional or approved fund. If the incubator fund is not successful after two years, the manager may dissolve it or convert to an ordinary company. The manager may also seek a twelve-month extension from the Financial Services Commission (“FSC”), but it must seek to convert into either a private, professional, or approved fund at the end of the extension term.

The restrictions on incubator funds include that:

- a. Only “sophisticated private investors” may invest in the fund, who are defined as “a person who has been invited to invest in an incubator fund and the amount of his or her initial investment is not less than \$20,000”;
- b. The total number of investors in the fund is limited to 20; and
- c. The net assets of the fund must not exceed \$20 million.

5. *Approved Funds*

Like incubator funds, approved funds can be easily organized and are limited to a two year life span. Approved funds must also limit the total number of investors to 20, but may have net assets of up to \$100 million.

Structure of Funds

BVI Business Company

The majority of open-ended funds are formed as BVI business companies authorized to issue shares that, subject to restriction, may be redeemed. The maximum number of shares that a

company is authorized to issue and the classes of shares that may be offered, together with the rights, privileges, restrictions and conditions attached to each class must be set in the company's memorandum of association. Normally an open-ended fund would designate a limited number of management shares, held by the sponsors of the fund, and the remainder being issued in one or more classes of non-voting redeemable shares.

International Limited Partnership

An International Limited Partnership ("ILP") is often used in a closed-ended fund structure or as a master fund in an open-ended master feeder structure. An ILP requires a general partner and at least one limited partner. The general partner of the ILP need not be domiciled in the BVI. As in the United States, a general partner of an ILP is liable for the debts and obligations of the ILP whereas a limited partner is only liable for the amount of capital committed.

Unit Trust

All assets of a trust are vested in trustees under a trust deed which divides the beneficial ownership of the fund into a number of units which generally are transferrable and redeemable. The trust deed sets forth the rights and obligations of the trustee and unit holders. In the BVI, if a trust company serves as the trustee, it would be required to be licensed under the Banks and Trust Companies Act.

Formation of Funds/Procedure for Companies

Incorporation

To incorporate a BVI business company, the memorandum and articles of association must be filed with the Registrar of Corporate Affairs. The memorandum and articles of association prescribe the operational functions of the fund including valuation dates, procedures for share issue and redemption, methods for pricing shares and valuing assets voting rights, restrictions on transferring or issuing stock and director responsibilities.

Recognition and Approval

Once incorporated, a professional or private fund must apply for "recognition" which entails a finding by the FSC that the fund satisfies the requirements of the SIBA. An application form is submitted to the FSC along with a certified copy of the incorporation documents, and the firm's prospectus. For a professional fund, the submission of the subscription agreement is also required. The FSC will review the application form to ensure that the functionaries to the fund are acceptable and review the organizational and offering documents to ensure the language mandated by the SIBA has been incorporated.

Once the FSC is satisfied that the fund meets the criteria, it enters the details of the fund in either the Register of Professional Funds or the Register of Private Funds (depending on the type of fund that was formed), and a certificate of recognition is awarded.

Incubator and approved funds must submit an application and fee to the FSC for approval. The application must include the fund's constitutional documents, a description of the fund's investment strategy and a written warning to investors. Incubator and approved funds may begin operations within two business days of receipt of the application by the FSC. Both funds must submit annual unaudited financial statements and semi-annual returns to the FSC.

Fund Directors and Service Providers

Professional, private, incubator and authorized funds must possess at least two directors; one of these directors is required to be an individual, who is charged with the management and supervision of the fund.

In addition, professional and private funds have to possess, at all times, a fund manager, fund administrator and a custodian, unless an exemption applies. The details on these persons must be provided for in the application for recognition. These posts also require that the custodian remain independent from the manager and the administrator, absent controls in place to command independence.

For registered, professional funds, the FSC may, at its discretion, exempt the requirement that there be a manager, custodian, or auditor. For public funds, the FSC can exempt from the requirement that there be a custodian; however, there is no auditor exception, and the auditor must be approved by the FSC.

Approved funds require only an administrator, while incubator funds do not need to have a manager, administrator or custodian.

Conversion

If an incubator or approved fund exceeds the limit on the number of investors or the amount of investments held by the fund during two consecutive months, the fund must notify the FSC within seven days. Incubator funds must then convert into a private, professional or approved fund. Approved funds have the option of converting into either a private or professional fund. Both types of funds must start the process of liquidating the fund or make the necessary amendments to the fund's constitutional documents so that it is no longer a mutual fund (as defined under SIBA).

Approved Manager Regulations

In 2012, a new "regulation light" fund manager regime was adopted by the FSC. The new regime offers an alternative to full licensing under the SIBA for fund managers or advisers domiciled or doing business in the BVI. Under the regulations, an Approved Manager can act as an investment manager to any number of private or professional funds recognized under the SIBA as well as any number of BVI closed end funds. To qualify a manager must be:

- (a) organized as a BVI company or limited partnership;
- (b) be proposing to act as the investment manager or investment advisor to a private fund, professional fund or a closed-ended fund domiciled in the BVI or a foreign fund investing substantially all of its assets in a BVI domiciled fund;
- (c) satisfy the Financial Services Commission's (FSC) fit and proper test, and;
- (d) have, in the case of open-ended funds, aggregate assets under management of no more than \$400 million and, in the case of closed-ended funds, aggregate capital commitments of up to \$1 billion.

Once this is satisfied, the investment manager or investment advisor must then go through an application process and provide the following documentation to the FSC:

- (a) a copy of the applicant's constitutional documents;

(b) the details of each director or general partner and senior officer of, and each person who owns or holds a significant interest in, the applicant (for these purposes, "significant interest" shall have the meaning ascribed to it in SIBA);

(c) a written declaration by the applicant that each director or general partner and senior officer of, and each person who owns or holds a significant interest in, the applicant is fit and proper in accordance with Schedule 1A of the Code;

(d) the number and details of the funds that the applicant intends to act for upon commencement of relevant business;

(e) the date upon which the applicant intends to commence relevant business;

(f) a copy of the investment advisory or investment management agreement between the applicant and each person with whom the applicant intends to act;

(g) a written confirmation as to which individual will be carrying out the day-to-day investment business functions of the applicant;

(h) a written confirmation as to whether or not the applicant has delegated or intends to delegate any of its relevant business functions (and where any of the functions will be so delegated, an outline of the functions which will be delegated; details of the person to whom the functions will be delegated; and a copy of the delegation agreement);

(i) a written confirmation from the applicant's legal practitioner that the legal practitioner has agreed to act for the applicant; and

(j) a written declaration by the applicant's authorized representative or legal practitioner that the application for approval as an investment manager is complete and meets the application requirements of the Approved Managers Regulations.