



## British Virgin Islands Regulatory Update

### Recent Regulatory Advances

The regulatory regime in the British Virgin Islands (“BVI”) has expanded recently, as the BVI authorities have responded to various international initiatives by introducing regulation intended to accord with international best practice for financial services business and implement standards laid down by the International Monetary Fund (“IMF”) and the International Organisation of Securities Commissions (“IOSCO”). The effects of these developments extend beyond the BVI, including to the MENASA region and other markets where BVI business companies are popular vehicles for matters ranging from asset holding to complex financial structures.

Until recently, banks and trust companies have been regulated under the Banks and Trust Companies Act, 1990 and hedge funds and their managers have been regulated under the Mutual Funds Act, 1996 (the “Mutual Funds Act”), but investment business generally has not been regulated. This has changed with the introduction of the Securities and Investment Business Act, 2010 (“SIBA”), which replaces the Mutual Funds Act and governs investment business and hedge funds. SIBA came into force on 17 May 2010, with the exception of Part II, which relates to public issues of securities in the BVI and will come into force at a date to be determined. The Mutual Funds Regulations, 2010 (the “Mutual Funds Regulations”) and the Financial Services Commission (Securities and Investment Business Fees) Regulations 2010 took effect the same day. In due course, it is expected that the Mutual Funds Regulations will be supplemented by the “Public Funds Code” (applicable to public funds, as described below).

In addition, the Financing and Money Services Act, 2009 (“FMSA”) came into force on 31 March 2010 and the Regulatory Code, 2009 (“Regulatory Code”) came into effect on 1 February 2010. This note highlights certain changes arising from these developments and summarises a recent amendment to the Financial Services Commission Act, 2001 (the “FSC Act”).

## Securities and Investment Business Act

### Investment Business

SIBA requires any person carrying on “investment business” in or from within the BVI to obtain a license from the Financial Services Commission (the “FSC”). For this purpose, a BVI business company that carries on investment business from anywhere in the world is deemed to carry on such business from within the BVI, so is subject to the licensing requirement unless it has the benefit of an exemption. In addition, a person is deemed to carry on investment business in the BVI if it: (a) occupies premises in the BVI for the purposes of carrying on investment business; or (b) solicits a person in the BVI for the purpose of offering to provide a service that constitutes investment business. Transitional provisions in SIBA include a grace period of 6 months (starting from the commencement date of 17 May 2010) for licensing of persons already carrying on investment business prior to the commencement date.

“Investments” are broadly defined, and include shares, interests in a partnership or fund, debentures, bonds, other debt instruments, warrants and other rights, options, futures and certain other derivatives, certain long-term insurance contracts and other interests relating to such investments. “Investment business” also is broadly defined, and includes carrying on by way of business the following “investment activities”: dealing in and arranging deals in investments, managing investments, providing investment advice and providing custodial or administration services with respect to investments or operating an investment exchange. As a result, in very broad terms (and this list is not exhaustive), BVI companies carrying on business as investment managers, investment advisers, administrators, custodians, market makers, broker/dealers and market intermediaries should expect to be required to apply for a license from the FSC. It is worth specifically noting that while SIBA generally will not regulate closed ended funds, BVI managers (and other functionaries) to closed ended funds likely will be required to obtain a license, in contrast to the pre-SIBA position.

SIBA contains some exemptions from the licensing requirement, all of which are relatively limited. First, there is a list of “excluded activities” which are carved out from the definition of investment business. These excluded activities are unlikely to have a great deal of significance for the majority of BVI companies carrying on investment business. For example, they include matters related to employee share schemes, dealing as bare trustee where no remuneration is received and investment business which is incidental to the sale of goods or the supply of services.

Second, there is a list of “excluded persons”. In this regard, there are two key exemptions from the licensing requirement for persons who (only) carry on the following activities: soliciting or making an offer to provide an investment business

service to or through certain qualified persons; and providing investment business services to a company of which a person is a director, a company in the same group, a joint venture or another partner in a partnership, provided that in each case no remuneration or commission is paid in respect of the relevant investment business (excluding normal remuneration received while acting in such a capacity).

SIBA imposes a number of obligations on licensees. For example, the prior approval of the FSC will be required for certain corporate actions and changes of control, such as the appointment of a director or senior officer, the disposition or acquisition by any person of a significant interest in the licensee (whether by transfer, charge, share issuance or other capital reorganization), the establishment of a branch or representative office outside of the BVI or the formation or acquisition of a subsidiary and, in the case of licensees other than fund managers and administrators (which are subject to a notification requirement), a change to the corporate name or the name under which the licensee carries on business. Amongst other things, licensees are obliged to maintain their business in a solvent condition, to maintain such professional indemnity and other insurance as may be prescribed, to comply with any capital requirements prescribed by the Regulatory Code and to meet certain other corporate governance and record keeping requirements. Licensees under SIBA are also required to have an “authorised representative” (described below) unless the licensee has a significant management presence in the BVI.

It is expected that the Regulatory Code (described below) will be amended so as to apply to SIBA licensees and that a new section containing obligations which are specific to SIBA licensees will be introduced. SIBA provides that the Regulatory Code may make provision for various matters relating to licensees.

### Hedge Funds

With respect to hedge funds, SIBA effectively replicates the provisions of the Mutual Funds Act, which has been repealed and replaced with Part III of SIBA. While SIBA does introduce certain additional requirements, there are no dramatic changes to the regulation of hedge funds. While a full description of the hedge fund regime is beyond the scope of this note, certain key changes are highlighted below. Regulation of public funds is likely to increase further upon the enactment of the Public Funds Code.

By way of background, BVI is the second most popular jurisdiction for hedge funds in the world after the Cayman Islands. Funds are divided into professional funds, with a minimum investment of US\$100,000 and a net worth test of at least US\$1,000,000, private funds, where the fund may have no more than fifty shareholders, and public funds, which are all hedge funds other than private or professional funds. These funds categories remain the same under SIBA, although for professional funds, all investors

(rather than a majority) will need to meet the minimum investment threshold (with limited exceptions, for example with respect to employees and fund functionaries). The registration of existing public funds and the recognition of existing private and professional funds will automatically be continued under SIBA. Funds incorporated in a jurisdiction other than the BVI can no longer be registered as a public fund. Instead, there is a new, fourth category of "recognised foreign funds", which allows foreign funds which are subject to an equivalent supervisory regime to public funds to offer their shares in the BVI.

Prior to the introduction of SIBA, public funds were required to have a manager, administrator, custodian and auditor, and the Mutual Funds Regulations extend this requirement to all private and professional funds, reflecting the FSC's already existing policy in this regard. Exemptions from the requirements to appoint a manager and custodian (but not an administrator) will be available on application, but a cogent reason for the exemption must be provided. To the extent an exemption is applied for, the FSC is likely to expect the structure to be otherwise more robust (for example, where other service providers are of international repute) and to otherwise be satisfied that there are adequate systems and controls in place for the protection of investors.

Public funds are obliged to appoint an auditor and make their financial statements available to the shareholders. Under SIBA, auditors appointed by a public fund (and any relevant licensee, meaning a licensee that is designated as such under the Regulatory Code) must be qualified under the Regulatory Code and approved by the FSC. Audited financial statements that comply with SIBA must be filed with the FSC. Under the Mutual Funds Regulations, similar audit requirements apply to professional and private funds unless an exemption is obtained from the FSC.

The auditor of a public fund or a licensee is obliged by SIBA to report certain matters to the FSC, including information that suggests that the licensee or fund is, or is likely to become, insolvent and certain breaches of SIBA, the Regulatory Code or regulations relating to money laundering or the financing of terrorism. Similar requirements may apply to auditors of professional and private funds pursuant to the Mutual Funds Regulations.

In accordance with previously existing FSC policy, SIBA requires that all funds must notify the FSC of any change in their functionaries, as well as changes to the directors, auditors, constitutional documents of the fund and other material matters relating to the fund.

SIBA introduces the concept of an “authorised representative”. All funds (and certain licensees, as mentioned above) will be required to appoint a local authorised representative, which will be a BVI entity or individual certified by the FSC for this purpose. Any applicant for certification will need to meet the FSC’s fit and proper criteria. The authorised representative will act as the liaison between the FSC and the fund or licensee, and will be required to maintain such records as are prescribed by the Regulatory Code (in respect of a licensee) or the Mutual Funds Regulations (in respect of a fund).

All BVI companies are obliged to have a registered agent in the BVI. While it is anticipated that registered agents also may serve as authorised representatives, it is unlikely that all registered agents will be able to do so, as it is expected that the authorities will certify only registered agents that have experience with hedge funds for this purpose. We fully expect that Codan, the affiliated registered agent to Conyers Dill & Pearman, will be granted a license to act as an authorised representative and will therefore be able to provide this service (in addition to the existing registered agent service) to Conyers’ clients.

An additional material change resulting from SIBA is the requirement that a specified form of “investment warning” be included in the offering document of a private or professional fund. A fund is prohibited from accepting a subscription from an investor unless it has received a written acknowledgement that the investor has received, understood and accepted the prescribed warning. As such, all private and professional funds will need to update their offering memorandum and their template subscription agreements accordingly.

It is also worth noting that new professional funds may now carry on business for a period of 21 days (instead of the previous 14) prior to being recognised under SIBA, provided an application for recognition is submitted within 14 days of commencing business.

Any BVI business company that acts as manager, administrator or custodian to a hedge fund must obtain an investment business license under SIBA. A fund manager or administrator that is already licensed under the Mutual Funds Act will automatically be licensed under SIBA.

#### Other

SIBA also regulates certain other activities including the public issue of securities in the BVI and market abuse, including insider dealing, market manipulation and making misleading statements to the market. However, these regulations generally only apply

to such activities if they take place in the BVI. As mentioned above, to date, the provisions relating to the public issue of securities have not come into effect.

## Financing and Money Services Act

The FMSA came into force on March 31, 2010. It imposes a licensing requirement on persons carrying on (non-bank) financing, which captures activities relating to the provision of credit and leasing property (other than real estate), and money services, which includes services such as money transmission, cheque cashing, currency exchange and the issuance, sale and redemption of money orders or travellers cheques. As drafted, the requirements applicable to financing should apply only to businesses that are operating in the BVI. For money services, however, BVI companies are deemed to operate in the BVI, so these regulations could apply to BVI companies carrying on this type of business elsewhere in the world. Companies to which the regulations apply will need to apply to the FSC for a license, and will be obliged to comply with various requirements relating to their business as set out in the FMSA and the Regulatory Code.

For those entities that require a licence and were already carrying on the regulated activity as at March 31, 2010, FMSA provides for a 6 month transitional period during which the regulated activities can be lawfully continued and a licence applied for.

It should be noted that those persons having an investment business license under SIBA are generally exempt from the requirement to obtain a license under FMSA in order to offer currency exchange services, provided that the FSC is notified 14 days in advance of the licensee's intention to offer such services.

### Regulatory Code

The new Regulatory Code came into effect in the BVI in February. It regulates licensed entities in the BVI, and is expected to regulate licensees under SIBA. It does not regulate hedge funds, but in due course it will regulate BVI licensed managers and other functionaries of hedge funds as well as banks, trust companies, insurers, registered agents and providers of money services business in the BVI. The Regulatory Code includes fundamental principles applicable to all licensees (related to, e.g., ownership structure, financial resources and management and operational structure) as well as specific requirements applicable to certain categories of licensees. It sets out practice standards as well as prior notification and approval requirements, including for any changes to the structure of the company, such as a change in directors or shareholders, or a change in beneficial owners. A detailed review of the Regulatory Code is beyond the scope of this note, but advisors of any licensed BVI entities should seek advice with respect to its application.

As a note, the Regulatory Code does not directly cover the obligations of a licensee with respect to the prevention of money laundering or terrorist financing. These are covered in the Anti-Money Laundering Regulations, 2008 and the Anti-Money Laundering and Terrorist Financing Code of Practice, 2008 issued by the FSC under the Proceeds of Criminal Conduct Act, 1997.

### Whistle blowing

A recent amendment to the FSC Act introduced a “whistle blowing” provision. As mentioned above, all BVI business companies are obliged to appoint a registered agent. The provision requires any registered agent to notify the FSC when it knows, or has reasonable grounds to suspect, that a licensee under any BVI financial services legislation for which it acts as registered agent has committed a breach or an offence under the FSC Act or any financial services legislation. The whistle blowing requirement does not yet apply to licensees under SIBA or FSMA, although it is expected that Schedule 2 of the FSC Act will be amended in due course so as to cover such licensees.

The requirement also applies to an authorised representative, insurance manager or any other person who acts in the capacity of an agent with respect to a licensee, appointed under the FSC Act or any BVI financial services legislation.

It should be noted that the section only applies to a BVI company that holds a license. It does not apply where the BVI company is unlicensed (even if it is required to be licensed).

### Conclusion

The regulatory developments in the BVI are a positive response to global trends, and reflect the BVI authorities’ continued commitment to effective regulation and maintenance of the reputation of the BVI as a leader in the financial services sector. In very general terms, BVI business companies carrying on business outside of the BVI should not be affected, unless they are carrying on financial services business (including investment business and money services business), in which case the intention of the authorities is to require licensing and impose and maintain international standards.



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This article is not intended to be a substitute for legal advice or a legal opinion. It deals in broad terms only and is intended to merely provide a brief overview and give general information.

### **About Conyers Dill & Pearman**

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