



Hedge Funds and the Securities and Investment Business Act

The Securities and Investment Business Act, 2010 (SIBA) was brought into force in the British Virgin Islands (BVI) on May 17, 2010. While the legislation makes some sweeping changes to the regulatory landscape in the BVI, only limited changes have been introduced which are relevant to hedge funds and their functionaries. SIBA has also been supplemented by the “Mutual Fund Regulations”. In due course, a “Public Funds Code” (applicable to public funds) is also expected to be issued.

This note highlights some of the key changes brought about by SIBA and the Mutual Fund Regulations and the positive steps that need to be taken by hedge funds to ensure compliance. A more general overview of the new legislation is available in a separate publication on our website entitled *A New Regulatory Regime in BVI: SIBA 2010*.

A change of legislation; not regulation

As stated above, SIBA and the Mutual Fund Regulations do not bring about any dramatic changes to the regulation of hedge funds. The new regime largely retains the structure of the current regime - in particular, the definition of “mutual fund” and the categories of public, private and professional funds remain the same. Furthermore, many of the “new” requirements introduced by SIBA and the Mutual Fund Regulations were in fact already required by the practice of the Financial Services Commission (the FSC).

The Mutual Funds Act, 1996, which previously regulated all hedge funds, was repealed and replaced with Part III of SIBA. The registration of public funds and the recognition of private and professional funds was automatically continued under SIBA. As such, there is no need for hedge funds which were recognised or registered under the Mutual Funds Act, 1996 to take any action to continue their existing licences.

Key changes for private and professional funds

SIBA and the Mutual Fund Regulations introduce the following key changes for private and professional funds:

- **Audit requirement:** All private and professional funds are required to have an auditor and to submit audited financial statements to the FSC annually. Such financial statements must be prepared in accordance with IFRS, US GAAP, Canadian GAAP or UK GAAP or other internationally and generally accepted accounting standards equivalent to these accounting standards.
- **Authorised representative:** Unless the fund has a significant management presence in the BVI, it is required to appoint a local “authorised representative”, which will be a BVI entity or individual certified by the FSC for this purpose. The authorised representative acts as the liaison between the FSC and the licensee, and is required to maintain certain records. We fully expect that Codan, the affiliated registered agent to Conyers Dill & Pearman, will be granted a licence to act as an authorised representative and will therefore be able to provide this service (in addition to the existing registered agent and secretarial services) to our hedge fund clients.
- **Investment warning and constitutional documents:** SIBA and the Mutual Fund Regulations require that a fund’s offering document contain a prescribed “investment warning”. Specifically the following statements are required to be included in the offering memorandum: (i) that the investor is solely responsible for determining whether the fund is suitable for his investment needs; (ii) that the fund is not subject to supervision by the FSC or by a regulator outside the BVI and that requirements considered necessary for the protection of investors that apply to public funds do not apply to private or professional funds; and (iii) that investment in a private or professional fund may present a greater risk to an investor than investment in a public fund. SIBA prohibits a hedge fund from accepting a subscription from an investor unless it has received a written acknowledgement that the investor has received, understood and accepted the prescribed investment warning. As such, all private and professional funds will need to update both their offering memorandum to include the prescribed investment warning and their template subscription agreement to include the necessary acknowledgement from investors. Furthermore, SIBA requires all private and professional funds to include certain specified provisions in their constitutional documents regarding their status as a recognised private or professional fund.
- **Functionaries:** As was reflected in existing FSC practice, the Mutual Fund Regulations also formally require every private and professional fund to have a

manager, administrator and independent custodian. It is possible to apply to the FSC for an exemption from the requirement to appoint a manager and a custodian, but not an administrator. However, the FSC will need to be satisfied that there are adequate systems and controls in place for the protection of investors prior to granting such an exemption.

- **Minimum investment for professional funds:** For professional funds, all investors (not just a majority as was previously required) will be required to make a minimum initial investment of \$100,000 (with limited exceptions, for example with respect to employees and fund functionaries).
- **Extension of time to carry on business prior to recognition:** 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.

The FSC is also given additional powers under SIBA and the Mutual Fund Regulations to investigate and ensure compliance with the new rules.

Action to be taken by private and professional funds

All private and professional funds will need to take the following positive steps by **December 31, 2010** to ensure compliance with SIBA and the Mutual Fund Regulations:

1. The fund must ensure it has at least two directors, at least one of whom is an individual.
2. The fund must ensure it has a manager, an independent custodian and an administrator. It is possible to apply to the FSC for an exemption from the requirement to appoint a manager and custodian, although not from the requirement to appoint an administrator.
3. Every fund is now required to include a prescribed "investment warning" (described above) in its offering memorandum and ensure that all new investors in the fund acknowledge the investment warning in writing (this is normally achieved by including the necessary acknowledgement in the fund's subscription agreement).
4. The constitutional documents of a professional and private fund must be amended to include specified language relating to their status as a professional or private fund respectively.

5. The fund must appoint a licensed "authorised representative" in the BVI who is responsible for liaising with the FSC on behalf of the licensee.

Finally, every private and professional fund is required to appoint an auditor and file its audited accounts, prepared in accordance with specified accounting standards, with the FSC. If a fund's current financial year commenced prior to May 17, 2010, it is not required to appoint an auditor or file accounts with the FSC until its next financial year. If a fund's current financial year commenced after May 17, 2010, it is required to appoint an auditor and file accounts with the FSC in respect of its current financial year.

The Act and the Mutual Fund Regulations also impose a number of formal notification requirements on private and professional funds, which are already in force. In particular, any amendment to the fund's constitutional documents or offering memorandum, or appointment or resignation of a director or auditor, must be notified to the FSC within 14 days after the fact. If a functionary ceases to be appointed for any reason, the FSC must be notified within 7 days (which notice must include the reasons for the functionary ceasing to act) and 7 days' prior notice is required for the appointment of any new functionary.

Public funds and foreign funds

SIBA and the Mutual Fund Regulations introduce additional regulation for public funds, which is expected to increase further with the enactment of the Public Funds Code. A full review of the regulation of public funds is outside the scope of this publication. However, please do not hesitate to contact us if you require any further information on the regulation of public funds. In particular, it should be noted that, with effect from **December 31, 2010**, a public fund must not offer its shares to the public unless the fund has registered an updated prospectus containing prescribed information with the FSC.

SIBA also introduces a new, fourth category of "recognised foreign funds", which allows certain types of funds incorporated in a jurisdiction other than the BVI and regulated in their home jurisdiction to become recognised in the BVI.

Licensing of functionaries

SIBA requires any BVI business company that acts as manager, administrator or custodian to a hedge fund to obtain an investment business licence under SIBA. A fund manager or administrator that was licensed under the Mutual Funds Act, 1996 was automatically granted the requisite licence upon SIBA coming into force.

SIBA imposes a number of additional obligations on licensed functionaries, a full description of which is outside the scope of this note. However, please let us know if any further information is required in this regard.

In the case of a functionary incorporated and operating outside the BVI, care needs to be taken that there is no “solicitation” of a hedge fund in the British Virgin Islands. Such solicitation could trigger a requirement for the foreign functionary to obtain an investment business licence under SIBA.



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

Conyers Dill & Pearman advises on the laws of Bermuda, British Virgin Islands, Cayman Islands, Cyprus and Mauritius. Conyers' lawyers specialise in company and commercial law, commercial litigation and private client matters. Conyers' structure, culture and expertise enable responsive, timely and thorough service. Conyers provides clients with the highest quality legal advice from strategic global locations including offices in the world's leading financial centres in Europe, Asia, the Middle East and South America. Founded in 1928, Conyers comprises 600 staff including more than 150 lawyers. Affiliated companies (Codan) provide a range of trust, corporate secretarial, accounting and management services.

For more information please contact:

Naomi Little

+1 (441) 298 7828

naomi.little@conyersdill.com

www.conyersdill.com