

GUIDE TO INVESTMENT FUNDS IN BERMUDA

CONTENTS

PREFACE	1
1. Introduction	2
2. Principal Regulatory Framework	2
3. Investment Fund Structures and Forms	4
4. Segregated Accounts Companies and the Segregation of Unit Trust Fund Assets	7
5. Taxation Considerations	8
6. Offering of Shares, Units or Partnership Interests	8
7. Transfer of Ownership	8
8. Documents	9
9. General Information	9
10. Conclusion	10

PREFACE

This Guide is a summary of the law and procedures relating to the establishment and operation of investment funds in Bermuda. It should be read in conjunction with the Appleby Guide to Companies in Bermuda, Guide to Partnerships in Bermuda and Guide to Trusts in Bermuda.

It is recognised that this Guide will not completely answer detailed questions which clients and their advisers may have, it is not intended to be comprehensive. If any such questions arise in relation to the contents, they should be addressed to any member of the Corporate Department, using the [contact information](#) provided at the end of this Guide.

Appleby
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1. INTRODUCTION

For the purposes of this Guide, the term **investment fund** is used to refer to open-ended mutual fund companies, unit trust funds and partnership funds. Closed-ended investment funds (e.g. private equity funds) are not governed by the Investment Funds Act 2006, as amended (**Investment Funds Act**).

2. PRINCIPAL REGULATORY FRAMEWORK

2.1 Investment Funds Act

The Investment Funds Act governs the exclusion, exemption and authorisation of investment funds and contains certain requirements for the formation of investment funds, their operation and the offering of shares, units or interests of investment funds. Investment funds are prohibited from being operated in or from Bermuda unless they are authorised or exempted under the Investment Funds Act. The requirement to be authorised or exempted does not apply to investment funds which are deemed to be private (such as master funds). An investment fund is a private fund if the number of participants is 20 or less and if the promotion, communication and offer to participate in the investment fund is restricted and is not made to the general public.

Unregulated Funds

Bermuda offers a fast track process for Class A Exempt Funds that requires no approval from the Bermuda Monetary Authority (**BMA**). To be eligible for a Class A Exempt Fund, a fund must:

- only be open to qualified participants (as defined below);
- have an investment manager who:
 - is licensed under the Investment Business Act 2003; or
 - is authorised or licensed by a foreign regulator recognised by the BMA (e.g. the SEC); or
 - is carrying on business in or from Bermuda or a jurisdiction recognised by the BMA and who has gross assets under management in excess of \$100 million or is a member of an investment management group that has consolidated gross assets under management of not less than \$100 million;
- appoint an officer, trustee, or representative that is resident in Bermuda and has access to the books and records of the fund;
- appoint an auditor, fund administrator, registrar and a custodian or prime broker; and
- prepare financial statements in accordance with IFRS or GAAP.

A **qualified participant** is:

- (a) an individual who has had a personal income in excess of \$200,000 in each of the two years preceding the current year or has a joint income with that person's spouse in excess of \$300,000 in each of those years, and has a reasonable expectation of reaching the same level of income in the current year (meaning the year in which he purchases an investment);
- (b) an individual whose net worth or joint net worth with that person's spouse in the year in which he purchases an investment exceeds \$1,000,000;
- (c) an individual who has such knowledge of, and experience in, financial and business matters as would enable him to properly evaluate the merits and risks of a prospective purchase of investments;

- (d) a body corporate which has total assets of not less than \$5 million held either solely by the body corporate or partly by the body corporate and partly by one or more members of the same group of which it is a member;
- (e) an unincorporated association, partnership or trust, each of which has total assets of not less than \$5 million held either solely by such association, partnership or trust or partly by it and partly by one or more members of the same group of which it is a member;
- (f) a body corporate whose shareholders fall within one or more of paragraphs (a) to (h);
- (g) a partnership whose members fall within one or more of paragraphs (a) to (h); and
- (h) a trust whose beneficiaries fall within one or more of paragraphs (a) to (h).

If a fund does not qualify for Class A Exempt Fund status, it can make an application to be a Class B Exempt Fund. To qualify as a Class B Exempt Fund, a fund must:

- only be open to qualified participants;
- have an officer, trustee, or representative that is resident in Bermuda and has access to the books and records of the fund;
- appoint an auditor, investment manager, fund administrator, registrar and a custodian or prime broker who are fit and proper to perform the respective functions of their office; and
- prepare financial statements in accordance with IFRS or GAAP.

Regulated Funds

In addition to the exempted status, the Investment Funds Act provides for four categories of authorised fund as follows:

- **Institutional Funds** which are only open to qualified participants or require each participant to invest a minimum of \$100,000 in the investment fund and it has an officer, trustee, or representative resident in Bermuda with access to its books and records;
- **Administered Funds** which must have an administrator which is licensed under the Investment Funds Act and require their participants to invest a minimum of \$50,000 in the investment fund or be listed on a stock exchange which is recognised by the BMA;
- **Specified Jurisdiction Funds** which are funds that incorporate the laws of a specified jurisdiction that is recognised by the Ministry of Business Development and Tourism; and
- **Standard Funds** which are any investment funds which do not qualify to be classified under any of the foregoing categories.

2.2 Regulatory Bodies and their Powers

The formation of companies and partnerships is subject to the approval of the Registrar of Companies (**Registrar**) and the BMA who have unlimited discretion to refuse to permit the incorporation of a mutual fund company or the formation of a partnership fund. The Registrar and the BMA do not regulate the formation of unit trust funds however they are required to apply to the BMA for authorisation or exemption under the Investment Funds Act.

The BMA's consent for the authorisation of an investment fund can be applied for concurrently with the application for permission to incorporate the mutual fund company or form the partnership fund. In the case of a unit trust fund, the application is made once the deed of trust has been constituted.

On or before the date of commencement of business, the operator of a Class A Exempt Fund must certify to the BMA via its electronic filing system **ERICA** that it meets the requirements for Class A exemption. At the time of filing of the certificate, the operator must also file a copy of the fund's prospectus. Upon filing the exemption notification the Class A Exempt Fund can immediately launch.

A fund that qualifies for Class B exemption must apply to the BMA via ERICA. The application is accompanied by the fund's prospectus. Once the application and prospectus have been submitted, the fund will be notified of the outcome of its application within ten days of the application date.

To be authorised, an investment fund must prepare annual audited financial statements, have appointed, or on authorisation will appoint, an investment manager, an auditor and an administrator, ensure that the property of the investment fund is entrusted to a custodian which is licensed or regulated in accordance with the Investment Funds Act and which is independent of the operator of the investment fund. The BMA will also consider whether the service providers and the operator of the investment fund are fit and proper persons and in so considering will take into account their combined experience and expertise in relation to the investment fund. When seeking authorisation of an investment fund, a copy of the prospectus must be submitted to the BMA for review and approval.

If the application for authorisation or Class B exemption is approved, the investment fund may commence to carry on its business and operation. An investment fund which is an exempted undertaking will be designated as non-resident for exchange control purposes by the BMA.

The BMA works closely with institutions and advisers in the private sector to provide as timely a response as possible to requests for consents. The process of incorporation of a mutual fund company or a partnership fund usually takes 24 to 48 hours; the obtaining of other consents from the BMA takes in the range of three to six working days, although this can be expedited depending on the circumstances.

2.3 **Bermuda Stock Exchange Listings and Transfer**

The Bermuda Stock Exchange (**BSX**) has established the "Launch & List" initiative which allows investment funds, while applying for incorporation and classification as an investment fund under the Investment Funds Act, to apply at the same time for a listing on the BSX. The BSX provides a listing platform for all funds, including Class A Exempt Funds which can offer additional transparency to investors.

3. **INVESTMENT FUND STRUCTURES AND FORMS**

3.1 **Mutual Fund Companies**

(a) **Legal Structure**

Under the Companies Act 1981 (**Companies Act**), a number of different types of companies may be formed. The first distinction is that between "exempted" and "local" companies. The former are companies formed in Bermuda primarily to carry on business outside of Bermuda or in Bermuda with other exempted companies; the latter are essentially domestic in nature, formed for the purpose of carrying on business locally. In the case of a mutual fund company the shares of which are to be sold in overseas markets, the exempted company is the appropriate vehicle. However, shares of a Bermuda mutual fund company, which is an exempted company, may also be offered inside Bermuda to local and international investors.

Mutual fund companies are companies incorporated with limited liability by registration. They may be set up with limited or unlimited duration. The constitution of a mutual fund company may provide for various classes of shares, which may be created and offered separately.

(b) Incorporation of a Mutual Fund Company

Mutual fund companies are incorporated by submitting an application to the BMA, consisting of certain statutory forms. In addition, detailed information must be submitted on the promoter or management company of the fund. If the promoter or management company is a recognised institution or a subsidiary of such an institution, this information will usually consist of a summary on that institution, together with its latest annual report (if it is a listed company). If the promoter is a private individual or group of individuals, then details of their investment expertise and curricula vitae for each of them will also need to be submitted.

The timeline of the incorporation of a mutual fund company, after submission of the application to the BMA, is usually 24 to 48 hours. A mutual fund company may only commence business and issue shares after it has been organised and the consents under Bermuda's exchange control regulations (**Exchange Regulations**) and the Investment Funds Act (if any) have been obtained.

(c) Management

The management of a mutual fund company is carried out by its Board of Directors however if the mutual fund company appoints a management company, it will usually be the responsibility of the management company to buy and deal in investments for the mutual fund company and to carry out its general day-to-day operations. The management company may itself sub-contract the investment advisory function to an investment adviser in Bermuda or another jurisdiction. The administration functions are usually delegated by the Board of Directors to the administrator of the mutual fund company.

(d) Duties of Directors and Management Companies

The management company appointed as manager of a mutual fund company and directors of a mutual fund company do not owe a direct contractual duty under Bermuda law to the shareholders. The directors of a mutual fund company owe a statutory duty, as they do in relation to any company, to act in the best interests of the mutual fund company. Usually, most of the directors' management duties are delegated to the management company. The latter may be liable under the contract made with the mutual fund company for any breach of its contractual duties, but only at the instance of the mutual fund company itself. It may be possible in the management agreement to exempt the management company from liability in circumstances which do not involve, for example, dishonesty or fraud, but it is a matter for negotiation and is not specifically regulated by the law.

The management company is, and the directors are, potentially liable in relation to misstatements made in any prospectus published in connection with an offering made to the public.

3.2 Unit Trust Funds**(a) Legal Structure**

Unit trust funds are constituted by a trust deed, usually made between the management company which (or whose affiliate) is promoting the vehicle and the trustee. A unit trust fund has no separate legal personality.

The trust deed will provide for the manner in which the unit trust fund is to be administered, unit holders' rights, the duties, and appointment and removal of the manager and the trustee, investment and borrowing powers and restrictions, and the termination and winding up of the affairs of the unit trust fund. Custody of the assets, accounting and calculation of net asset value are usually performed by the trustee (provided that, if providing the services in Bermuda, the

trustee is also a licensed administrator). The management company is usually responsible for making investments on behalf of the unit trust fund.

(b) **Formation of a Unit Trust Fund**

No governmental consent or approval is required to form a unit trust fund. All that is required is settlement of the terms of the unit trust fund deed and execution of the deed by the trustee and the management company.

Once constituted, however, the unit trust fund may not issue units until relevant contracts and offering materials are approved and the consents required under the Exchange Regulations have been obtained. At the time of the application for such consents, information on the trustee and its investment expertise is usually submitted.

(c) **Management**

In the case of a unit trust fund, the responsibility for the management of the trust's affairs is shared by the trustee and the management company.

(d) **Fiduciary Duties of Trustees**

Trustees act as custodians of the assets of the trust and owe fiduciary duties, under the general law, to unit holders in the trust. There are usually specific provisions in the trust deed giving the benefit of certain exemptions or indemnities to the trustees, but the extent of these is a matter for negotiation and agreement on commercial terms.

3.3 Partnership Funds

(a) **Legal Structure**

Under Bermuda law, two types of partnerships may be created: ordinary or general partnerships and limited partnerships. Bermuda partnerships are also categorised to distinguish between those formed by Bermudians to trade locally and those formed primarily by non-Bermudians to carry on business outside Bermuda from a place of business in Bermuda. The latter category, known as exempted partnerships, usually consist exclusively of partners who do not possess "Bermudian status" within the meaning of the Bermuda Immigration and Protection Act 1956. Exempted partnerships may be either general or limited partnerships and as most partnership funds will be established to offer interests in overseas markets, the exempted, limited partnership is usually the most appropriate vehicle.

Partnership funds are constituted by a partnership agreement which is most often entered into between the management company which (or whose affiliate) is promoting the vehicle as general partner and one or more limited partners. Limited liability status is conferred on a limited partnership by registration, and partnership funds may be established for a fixed term or with unlimited duration.

The partnership agreement will provide for the manner in which the partnership is to be administered, partners' rights, the duties of and appointment and removal of the manager and the general partner, investment and borrowing powers and restrictions, and the termination and winding up of the affairs of the partnership fund. The custody of the assets of a partnership fund is usually delegated to a custodian while accounting and calculation of net asset value are usually performed by the general partner or a management company which may also be responsible for investments.

(b) Formation of a Partnership Fund

Partnership funds are incorporated by submitting an application to the BMA, consisting of certain statutory forms. In addition, detailed information must be submitted on the general partner of the partnership fund. If the general partner is a recognised institution or a subsidiary of such an institution, this information will usually consist of summary information on that institution, together with a copy of the most recent annual report (if it is a listed company). If the general partner is a private individual or group of individuals, then details of their investment expertise and curricula vitae for each of them will also need to be submitted.

The usual time to form a partnership fund, after submission of the application, is one to three working days.

(c) Management

In the case of a partnership fund, the responsibility for the management of the partnership's affairs belongs to the general partner but may be delegated to the management company.

(d) Fiduciary Duties of General Partners

A general partner owes fiduciary duties as a matter of common law and pursuant to the Bermuda Partnership Act 1902 to the other partners of a partnership. These fiduciary duties include the duty to render true accounts and full information of all things relating to the partnership business, the duty to account for private profits and the duty not to compete with the partnership however all of these duties may be varied with the consent of all the partners either in express terms within the partnership agreement or from a course of dealing.

There are usually specific provisions in the partnership agreement giving the benefit of certain exemptions or indemnities to the general partner, but the extent of these is a matter for negotiation and agreement on commercial terms.

4. SEGREGATED ACCOUNTS COMPANIES AND THE SEGREGATION OF UNIT TRUST FUND ASSETS

Under the provisions of the Segregated Accounts Companies Act 2000, as amended, a mutual fund company may be registered as a segregated accounts company enabling it to create different share classes, each representing a segregated portfolio of assets. Accordingly, where a multi-class structure is desired with a separation of liability between classes, it is no longer necessary to incorporate multiple companies in an umbrella form. Instead, a single segregated accounts company may be incorporated with segregated accounts representing each share class. Such accounts enjoy a statutory division of liability, effectively ring-fencing each segregated account from the general liabilities of the company, and from other segregated accounts. Bermuda segregated accounts can invest in other segregated accounts in the same company creating a master/feeder structure.

Consent of the Minister of Finance (**Minister**) is necessary to register as a segregated accounts company. Such consent may be sought at the same time as the incorporation of the mutual fund company and its authorisation or exemption under the Investment Funds Act. Alternatively, it is possible for a mutual fund company to incorporate and commence business, and subsequently apply for permission to operate segregated accounts.

A segregated accounts company must have a Segregated Account Representative who is under a duty to make reports to the Registrar in certain circumstances, including the insolvency of any segregated account or of the general account of the fund. In addition, a segregated accounts company is obligated to maintain

separate accounting records in respect of each segregated account, and to prepare financial statements in respect of each segregated account in accordance with generally accepted accounting principles.

The Investment Funds Act recognises the possibility of the segregation or creation of distinct accounts or sub trusts for unit trust funds if such activity is permitted by the trust deed constituting the unit trust fund. These accounts may be linked to data, assets, rights, contributions, liabilities and obligations of the Particular Account Or An Identified Or Identifiable Pool Of Assets.

5. **TAXATION CONSIDERATIONS**

Bermuda is fiscally neutral in the sense of having no tax applicable to the establishment and operation of investment funds.

Bermuda investment funds are not subject to any tax, as there are no Bermuda corporation, profit, withholding, capital gains or income taxes applicable to an investment fund or to its share or unit holders or partners which are not resident in Bermuda. Upon application, usually made just after incorporation of a mutual fund company or formation of a unit trust fund or partnership fund, the Minister will issue a certificate confirming the exemption of the investment fund from such taxes, which is presently expressed to operate until 31 March, 2035. This assurance is given as a matter of course to any investment fund with exempted status.

Instruments executed by or in relation to an investment fund are exempt from stamp duties. Thus, stamp duties are not payable upon, for example, an instrument that affects the transfer or assignment of a share, unit or interest in an investment fund.

A mutual fund company must pay an annual government fee which is charged on the basis of a sliding scale and calculated by reference to its authorised share capital. It is almost always possible to structure a mutual fund company so that the minimum fee is paid. A partnership fund must also pay an annual government fee.

For any company incorporated in Bermuda managing a unit trust fund, there is also payable an annual fee in respect of each unit trust fund managed by that company. No annual government fee is payable by a unit trust fund itself.

6. **OFFERING OF SHARES, UNITS OR PARTNERSHIP INTERESTS**

A copy of the prospectus of an authorised investment fund must be submitted to the BMA and published or made available to the public on request. The prospectus may not be used in the offer of units to participants until it has been approved by the BMA. The prospectus must be made available to participants without charge at the registered office or the principal office of the investment fund in Bermuda or at the office in Bermuda of at least one service provider.

There are minimum contents and certain disclaimers that must be included in a prospectus.

7. **TRANSFER OF OWNERSHIP**

Every authorised investment fund must appoint a registrar who shall establish and maintain in Bermuda a register of participants. A number of banks and fund service companies in Bermuda provide registrar and transfer agent facilities using computerised systems which are able to deal with widely-held companies, unit trusts and partnerships. It is possible to appoint branch registrars or transfer agents in other jurisdictions, and this is often done. This requires suitable advice as it may have tax and other consequences in those jurisdictions.

Shares in mutual fund companies or units in unit trust funds are transferable by registration only. Bearer shares or units are not permissible. Share or unit certificates need not be issued and may take the form of entries in registers. Partnership interests in a partnership fund may be transferred in accordance with the terms of the agreement which constitutes the partnership.

Transfers will involve the submission of an executed form of transfer accompanied by, if issued, evidence of ownership, e.g. a share or unit certificate. In most cases, these will be sent to the registrar and transfer agent in Bermuda. The Companies Act provides a waiver of this requirement if securities of the mutual fund company are listed on an appointed stock exchange.

Subject to any special provisions in the bye-laws, trust deed or partnership agreement (as, for instance, in the next paragraph), there will be no restrictions on ownership or transfer. This assumes that the consents from the BMA under the Exchange Regulations have been obtained.

Many investment funds created in Bermuda, to be marketed outside the United States, place restrictions on the ability of so-called "US Persons" to hold shares, units or interests in the investment fund and provide (in the constitutional documents) for such shares, units or interests to be compulsorily acquired if these restrictions are breached. These restrictions are a function of US regulatory or tax considerations, and not Bermuda law.

8. DOCUMENTS

In relation to an investment fund, the principal documents usually required for its establishment and the offering of its shares will be a prospectus or offering document, the bye-laws, trust deed or partnership agreement, as applicable, and the material contracts. The latter will include an administration agreement, a custodian agreement and any sub-custodian or co-custodian agreement, a management agreement, where necessary, an investment advisory agreement and a registrar and transfer agent agreement and probably a corporate administrative services agreement.

At present there are no statutory prescribed forms for the majority of these documents, although Bermuda statutes and the Investment Funds Act may require provisions to deal with certain specific matters.

9. GENERAL INFORMATION

9.1 Reporting Requirements – to the Authorities and to Participants

A Class A Exempt Fund must make an annual certification to the BMA on or before 30 June stating that the fund satisfies the requirements for exemption and will continue to satisfy them. Along with the certification, the fund must file its audited financial statements for the preceding year and a statement of any material changes to the fund's prospectus.

A Class B Exempt Fund must make an annual certification to the BMA on or before 30 June stating that the fund satisfies the requirements for exemption and will continue to satisfy them. Along with the certification, the fund must file a statement of any material changes to its prospectus, audited financial statements for the preceding year and a schedule of any changes made to its directors and/or service providers. An operator of a Class B Exempt Fund cannot appoint a service provider or a director without first making a written application to the BMA seeking their approval.

The operator of an authorised investment fund is required to submit a report of activities and performance to the BMA at such times or at such intervals as the BMA may require. Within six months of its financial year end, an authorised investment fund must submit a statement to the BMA confirming that the fund has been in compliance with the provisions of the Investment Funds Act during the preceding financial year or,

if the investment fund has not been in compliance, the particulars of the breach. Service providers are also required to notify the BMA of any breaches by an authorised investment fund of which they are aware. Under the Companies Act, a declaration must be filed in respect of the payment of the annual government fee for a mutual fund company or for the management company of a unit trust fund.

9.2 Marketing

The regulation of advertising and canvassing to persons outside and within Bermuda is the subject to the provisions of the Investment Business Act 2003 and general law (e.g. as to misrepresentation and agency). As most of the investment funds of interest to readers of this Guide will be marketed outside Bermuda, local regulations in each jurisdiction where marketing takes place will determine the form and content of such marketing.

9.3 Management and Advisory Fees

There are no provisions of Bermuda law limiting the nature or extent of advisory or administrative fees which may be charged. Accordingly, these are usually determined by negotiation between the relevant parties.

10. CONCLUSION

The Government of Bermuda, the BMA and the private sector continue to work together closely in the further development of Bermuda's investment funds industry. Their aim is to create an environment which is favourable for the quick, cost-effective and efficient establishment of investment enterprises and to clarify and codify the regulation of funds with the overall goal of strengthening Bermuda's position in the international funds market. This goal is intended to give an operator the opportunity to seize market opportunities and the investor the security that is required in the context of increased international concern for investor protection.

For more specific advice on investment funds in Bermuda, we invite you to contact:

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For the convenience of clients in other time zones, a list of contacts available in each of our jurisdictions may be found [here](#).