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SPECIAL REPORT

BERMUDA 2016

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An innovative and flexible approach



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or many decades, Bermuda has been a thriving international financial centre, including a highly respected hub for global asset management and fund companies. Indeed, our jurisdiction's capital market is the sought-after destination for an estimated \$20bn of financial investment by onshore pensions and governments.

Yet the pressures and challenges facing offshore domiciles have never been tougher. Amid increasing global scrutiny, increased costs, and mounting regulatory requirements, there has been an unprecedented upsurge in negative public and media pressure—too often fuelled by gross

misinformation, hypocrisy or purely political motives.

Bermuda, like many other IFCs, has been the target of such speculation. Rather than cower, however, we have turned this disruption into a valuable opportunity to tell the world why our jurisdiction is different. It's not by chance that our reputation has always been associated with top quality—a blue-chip brand that imbues everything from our high-end tourism product, world-class intellectual talent and superior insurance claims-paying capacity to the America's Cup that we're proud to host in 2017.

Bermuda's name has long been aligned with robust regulation, compliance and transparency and the jurisdiction has proven itself a leader in all spheres. The Bermuda Monetary Authority (BMA) is well regarded for the pragmatic, sophisticated approach it applies to oversight of all financial services on the island; in 2016, its performance was validated by the European Union's award of equivalence with its own Solvency II insurance regulatory regime. That decision is an important vote of confidence that enhances not only our insurance sector, but all financial services in what essentially is our one-stop shop jurisdiction.

Indeed, cross-selling and innovation are increasingly paying dividends in Bermuda, where the traditional lines between insurance, capital markets, trusts, private-client and family-office vehicles are becoming blurred. Agility and adaptability to market needs are the currency of Bermuda's success, more so in the years since the global financial crisis. Its impact, while challenging to the island's economy, also powered the development of highly innovative products such as insurance-linked securities, cat bonds, sidecars, hedge fund re and fund of fund re. The resulting juggernaut of ILS and other "convergence" risk-transfer products has made Bermuda the world leader in this cutting-edge arena, with close to \$20bn in listings, or more than three-quarters of the global capacity.

For a 21-square-mile island, that's quite impressive. So is the fact Bermuda supports some 500,000 jobs worldwide, including 300,000 in the US and 70,000 in Britain, through trade, foreign direct investment and portfolio investment capacity. In this way, our jurisdiction delivers critical stability to global financial systems, smoothing the operation of worldwide business by lowering barriers to trade and investment.

Bermuda has a track record of punching above its weight economically, and these are just a few examples. The island is a petri dish of possibilities, attracting some of the brightest minds and best ideas the world of financial services has to offer. This is what attracts investors and international businesses that seek a home base they can feel assured is not only a unique centre of excellence but also a globally trusted one.

Ross Webber



is CEO of the Bermuda Business Development Agency (BDA), an independent unit that helps international companies start up, relocate, maintain jobs and expand their business on the island. He holds an MBA in Insurance and Financial Risk Management from St. John's University, New York, and is a member of the Institute of Directors (IoD).



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BERMUDA ROUNDTABLE DISCUSSION

SEAN MORAN, OF THE BDA, SPEAKS TO TONESAN AMISSAH OF APPLEBY, KEN MAHADEO OF APEX FUND SERVICES, HENRY KOMANSKY OF OYSTER CONSULTING AND CRAIG BRIDGEWATER OF KPMG ABOUT BERMUDA'S DEVELOPMENT AS A DOMICILE



Sean Moran is a business development manager with the Bermuda Business Development Agency (BDA). His role is focused on promoting Bermuda as a jurisdiction for international business, and assisting asset managers and fund service providers set up and grow in Bermuda.

Sean Moran (SM): What are the key attractions for new firms looking to set up/build their presence in Bermuda? Have there been any recent successes in attracting more firms to do business with or in Bermuda? If so, what are they?

Henry Komansky (HK): Bermuda is just about two hours from most cities in the north-east corridor, including New York and Miami, which makes it an ideal location. Historically, Bermuda has high levels of internet penetration and is often ranked as second in the world due to this factor. Additionally, Bermuda is a sophisticated jurisdiction with a tried and tested civil and commercial law system that supports a vast array of business structures.

The island is proud of its reputation, and through collaboration among the financial services sector, our government and our regulator, the Bermuda Monetary Authority, it continues to lead as a first-class jurisdiction. The depth and knowledge of service providers on the island is also part of our success and remains a key attraction.

In terms of success stories, a large reinsurer made a

very public redomicile back to Bermuda in 2016 from Ireland. This was likely in response to Bermuda's Solvency II equivalency.

We have also seen asset managers set up in Bermuda in addition to more and more start-up companies in the insurance-linked securities (ILS) space. The ILS market has seen significant growth in Bermuda and the Bermuda Stock Exchange (BSX) has responded to the needs of these products by creating a streamlined and efficient process to list ILS.

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THE ISLAND IS TAKING
SERIOUSLY THE
WORLDWIDE PUSH
FOR TRANSPARENCY
AND ACCOUNTABILITY
”

Tonesan Amissah (TA): The 'elevator pitch' is undoubtedly that Bermuda is one of the world's leading financial centres with a long history of not just providing first-class financial and professional services, but doing so within a 'gold standard' regulatory framework.

The island's independent regulatory body, the Bermuda Monetary Authority (BMA), has emphasised its commitment to the broader asset management industry and Bermuda's fund products, which include the ability to file and launch a fund in Bermuda on a same day basis. As other jurisdictions are starting to see a cost creep and

additional licensing requirements, Bermuda is now attracting firms who want a quicker, more cost-effective and easier option without compromising the reputation of the fund. Bermuda's first-class reputation makes this possible. This reputation is built upon a tradition of transparency and regulatory effectiveness, complying with the highest of worldwide standards on anti-money laundering, financial crimes and anti-terrorist financing.

Craig Bridgewater (CB): I would agree that key attractions for Bermuda include: a word-class reputation; the presence of intellectual capital that is highly skilled and innovative; a very responsive approach to adopting international regulations; and flexible but effective and robust regulation.

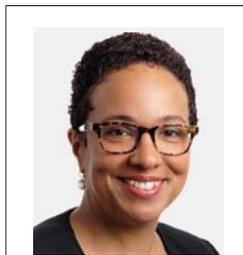
To comment on the last point, the regulation available in Bermuda is appropriate for the corporate vehicles and related activity. Our regulatory environment has been recognised by regulators in other larger jurisdictions such as the US, UK and throughout Europe.

Recently, Bermuda has seen many successes in attracting new business and activities to the jurisdiction. One area of particular note is the convergence space, where we've seen the creation of several structures related to insurance-linked securities (ILS) and hedge-fund backed reinsurers. There has been a commitment to embrace and encourage the ILS asset class in Bermuda, by creating and maintaining the correct legal and regulatory environment in which those structures could thrive.

Ken Mahadeo (KM): Bermuda has an excellent asset management reputation, benefiting from a 400-year-old judicial system and active support of global standards and fund structures. There is a great parity between the progressive nature of the Bermudian funds industry and the innovative, all-inclusive approach Apex takes to delivering services across the full value chain of a fund. We have recognised Bermuda as a key fund jurisdiction for over 13 years; the Apex group was founded in Bermuda in 2003 and to this day remains one of the largest administrators on the island.

Bermuda is now seen as the premier jurisdiction delivering a one-stop shop for funds. It is home to experienced and internationally trained industry professionals delivering a wealth of experience across all services and has provided a solid base to develop Apex's administration business; now a total of 33 offices worldwide and \$45bn AuA. Collaboration is the key to Bermuda's success. The creation of a unified stakeholder focus group combining onshore associations and authorities has brought new opportunities to the island. There have been dozens of new captives as well as large insurers redomiciling to the island; a by-product of this success has been increased interest by private equity firms who are looking at options for placing insurance interests in Bermuda.

SM: What recent legislative changes has Bermuda seen in the last 18 months? Which have been the most pivotal and why?



Tonesan Amissh

is a partner and member of the Funds and Investment Services team within the corporate department. Tonesan specialises in the structuring, formation and day-to-day operations of a wide range of investment vehicles, including mutual funds, hedge funds, unit trusts, private equity, segregated account companies, partnerships and master/feeder structures.



Craig Bridgewater

is head of Investments and Banking at KPMG in Bermuda. He has significant experience providing audit and advisory services to the financial services industry, including Bermuda-based funds and investment managers.

KM: As a global provider with over 600 staff across 26 jurisdictions, Apex has a unique insight into the comparative complexities in the legal and regulatory environments across all fund markets.

During the last 18 months, Bermuda's attractiveness as a fund domicile has further improved, as the BMA and other stakeholders are continuously looking at ways to enhance the legislative framework to adapt to the changing funds landscape.

As we mentioned earlier, ILS has seen a surge in popularity, helping attract larger managers looking for non-correlated investments. Through our ILS services, we have seen a notable growth in funds setting up with insurance-related strategies and bigger funds setting up reinsurance vehicles. The recent investment law changes are making it easier for those managers to establish themselves here.

The passing of the Perpetuities and Accumulations Amendment Act in late 2015 means a more cost-effective application process for trusts looking to establish or relocate there.

It's also worth noting that a committee of local professionals has been formed, producing a Bermudian AIMA branch which will help drive more legal and regulatory enhancements in line with global best practices.

HK: Bermuda continues to enhance its anti-money laundering/anti-terrorist financing regime with amendments to various laws and guidance notes, to bring it in line with the latest Financial Action Task Force (FATF) recommendations and interpretive notes. Furthermore, the island is taking seriously the worldwide push for transparency and accountability and is also updating many other laws including those to creating stronger data protection for the public and implementing international standards for bribery, corruption and fraud.

TA: In March 2016, the Contracts (Rights of Third Parties) Act, 2016 (CRTP Act) became fully operative. The Act is significant in that, subject to its terms, it permits parties to vary the common law doctrine of 'privity of contract', which provides that only parties to a contract may enjoy the benefits and enforce the provisions of that contract. Under the CRTP Act, persons not specifically party to a contract may now be entitled to benefit from and enforce the terms of the contract, subject to certain restrictions. This is particularly relevant in the context of indemnities commonly found in fund documentation, for example, those given pursuant to the terms of investment management agreements.

Looking forward, legislation is slated to be tabled in the House of Assembly later this year for the establishment of limited liability companies in Bermuda. This legislation will be modelled after the Delaware legislation so will be welcomingly familiar to persons who currently operate in the asset management space and we are already seeing interest from potential clients in this regard.

CB: In December 2015, amendments to Bermuda partnership laws came into force.

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 ”

These amendments have allowed for greater flexibility in how partnerships do business. As a result of the amendments, the safe harbour provisions of the Limited Partnership Act 1883 have been enhanced to clarify that if a limited partner undertakes certain actions, they will not be surrendering their limited liability status as a limited partner. The amendments also allow partnerships that have elected to have separate legal personality to hold assets and grant security in their own name. As a result of the amendments, a partnership can convert to a company and vice versa, and overseas partnerships can easily convert or “continue” into Bermuda.

SM: How have various regulatory initiatives such as Solvency II, AIFMD, UK Fatca, CRS, CbC reporting impacted Bermuda’s regulatory environment?

TA: Bermuda was pleased to be selected among the first wave as one of three countries to be assessed in respect to the EU Solvency II Directive and became fully equivalent this year. As a result, Bermuda’s commercial (re) insurers and insurance groups will not be disadvantaged when competing for, and writing, business in the EU, which of course has corresponding advantages for those seeking to access and benefit from the ILS asset class.

AIFMD is obviously very important to a number of jurisdictions outside of the European Union. At this stage it would be presumptuous to comment upon the impact of the initiative as Bermuda is yet to be recognised as a “third country” within that regime. But, if Bermuda does obtain such recognition, that would represent a great benefit to those funds that are already registered within Bermuda and provide a further incentive for those considering which jurisdiction to house their offshore fund. Bermuda is therefore committed to working together with Esmā to show that, like with Solvency II, it is deserving of such recognition.

CB: Yes, all of these initiatives have impacted Bermuda’s regulatory and operational environment. This is not inconsistent with other jurisdictions as changes in international regulation is reshaping how business is conducted globally. Fortunately for Bermuda, the jurisdiction has been at the forefront of the adoption of such regulations.

A “hot topic” with clients when it comes to the disclosure regimes identified is certainly the Common Reporting Standard (CRS). The advantage that Bermuda has over certain other jurisdictions with addressing CRS is that Bermuda adopted a model two approach to Fatca, whereby there was no direct reporting between Bermuda and the US tax authorities. The CRS is more closely aligned to the reporting approach of model one Fatca, where such reporting exists. Having been able to observe the approach of, and issues faced by, other jurisdictions, Bermuda has been able to focus on formulating a response to satisfy CRS reporting requirements which should be more robust and accessible than might otherwise be the case without the benefit of hindsight.

KM: The Bermudian tiering system for ‘opting in’ to various levels of regulation is an attractive pull for managers looking to keep overheads and compliance requirements



Henry Komansky

is an attorney in the Financial Services industry, specialising in compliance, anti-money laundering and counter terrorist financing. He has held executive positions in an international banking group, a long-term life insurance company, and Bermuda’s Financial Intelligence Agency. Prior to moving to Bermuda, Henry was a special agent for the Federal Bureau of Investigation.



Ken Mahadeo

is the managing director for Apex Fund Services in Bermuda. Prior to joining Apex in May 2016, Ken was the managing director for CNS Accounting Solutions, a subsidiary of BDO Cayman, which he established in 2014. Ken has progressive Canadian and international experience and has been in the hedge fund industry for the past 15 years. His expertise and skill sets are broad; covering operations management for investment managers, business development and fund administration. Ken is a certified professional accountant and registered with Nova Scotia CPA office.

manageable. Recent amendments made to the Investment Business Act position Bermuda as a favourable jurisdiction for non-EU passporting under AIFMD, as Tonesan mentioned. Supporting the implementation of directives and ensuring appropriate legislation is drawn up early, means Bermuda offers investors a jurisdiction where they can place capital in well-supervised funds. In regards to administration, larger bank-owned administrators often struggle to provide suitable responses in a constantly changing regulatory environment. It is here that independence is paramount; Apex’s clients receive value through the ability to deliver a flexible service supported by local experts in every jurisdiction. Apex is the only administrator that enables Bermudian fund structures to be used and supported either locally on the island, or in other jurisdictions.

HK: In the last few years, there has been a host of changes in Bermuda following these regulatory initiatives, all five of which have been or are being addressed.

Bermuda has attained Solvency II equivalence, signed up with US Fatca, agreed to report on UK Fatca and signed on to CRS as an early adopter.

In April 2016, Bermuda became the 33rd jurisdiction to agree to the implementation of Country-by-Country reporting (CbC), for which it will collect aggregate information annually relating to the global allocation of income and taxes paid, together with other indicators of the location of economic activity within a multinational business group, starting with 2016 accounts. This information will also clarify which entities do business in a particular jurisdiction and the business activities each entity engages in, and will then be exchanged in accordance with the relevant agreements.

The last jewel for Bermuda’s crown would be obtaining AIFMD third country passport rights.

SM: How is Bermuda capable of meeting a single client’s multiple needs?

CB: Bermuda is capable of meeting a client’s multiple needs in that several of the services and skills required by clients are resident in Bermuda. This ranges from legal to accounting, audit, tax, administration and to trust advisory services. Many of the service providers have access to international networks (such as KPMG and other global professional services firms) and can bring these resources to bear in servicing their clients.

In addition to the excellent environment for service provision, Bermuda offers advantages in relation to capital raising and access to potential investors. Bermuda is a tax neutral jurisdiction, meaning that the fund itself is not the subject of direct taxation. Of course, there may be taxes in the jurisdictions where assets of the fund are located, and investors may be required to pay tax under their own tax rules on any income and capital gains; the point is that Bermuda allows investors access to the fund without including a further layer of complexity.

Investors also want to be sure, and may often be required, to invest in vehicles which are recognised as being regulated in and by a reputable jurisdiction. Again, Bermuda ticks this box.



HK: Bermuda has a long history with a large number of full service law firms, has representation from the “Big Four” accountancy firms, and many other well-established service providers.

International regulatory consultancy firms such as Oyster are able to provide assistance to companies setting up as well as on-the-ground expertise to design a compliance framework which will satisfy their regulatory requirements. Outsourcing of specific compliance functions allows a firm to focus on building their business.

KM: Non-regulated funds in Bermuda benefit from same day registration while regulated authorisations take up to five days, compared with a typical average of four to six weeks across most other fund domiciles – this speed to market is a key requirement for clients. As has been mentioned, the fact that no fund-level tax is imposed and that there are a plethora of high-quantity onshore service providers available, means that Bermuda can offer a full suite of expertise and a safe and secure infrastructure to cover all aspects of a fund’s requirements.

TA: In the legal context, Bermuda offers an extremely well-developed framework for the initial incorporation of stand-alone vehicles and the formation and subsequent or contemporaneous creation of group structures. The flexibility of Bermuda’s law, including with respect to its company and segregated account company statutes and partnership legislation, means that legal advisers are really able to work with clients to reach their commercial objectives within their desired structure, whether that be through including a traditional private equity distribution waterfall in a corporate vehicle rather than a partnership, fund-of-one structures, or putting in place a series of companies with a view to switching them to partnerships if desired in the future.

SM: How does Bermuda differentiate from its rivals? How does it retain its leading status?

TA: Appleby is an offshore law firm with a presence in

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multiple jurisdictions. We do not see those jurisdictions as “rivals” to one another, rather they complement each other and can together offer clients a range of bespoke solutions to their individual needs.

That being said, Bermuda has learned that in order to be successful in the asset management arena, as is true in most instances, you cannot rest on your laurels and must continue to innovate in order to lead.

HK: Agreed. Bermuda certainly has not rested on its laurels as a leading insurance and reinsurance domicile – this is evident from our pursuit of Solvency II equivalency. The island prides itself on regulatory transparency and developing a risk-appropriate regulatory regime.

The long history of strong communication between the public and private sector that was evident during the Solvency II journey is again being reflected in Bermuda’s AIFMD initiative.

The Bermuda Business Development Agency works tirelessly to promote Bermuda and our reputation as a first-class jurisdiction. This effort has shown results in many areas, but none more so than in the hosting of several key conferences over the past couple of years, many of which plan to return on an annual basis.

CB: Ultimately, superior service, appropriate and globally recognised regulation, global connectivity and highly respected intellectual capital all play key roles in maintaining Bermuda as an industry-leader.

KM: Oversight and supervision alongside a continual push toward enhancing regulation in accordance with global standards has kept Bermuda at the forefront of the funds industry. The BDA, with its bold cross-border outreach programme aimed at attracting investment in the jurisdiction, is playing an important role in making Bermuda stand among asset management domiciles. The synergistic relationship between the BDA, BMA, government and industry stakeholders is helping Bermuda bolster its reputation as a world-class financial centre and a progressive leader in asset management. ■

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BERMUDA: OOZING QUALITY

NEIL GLASS OF WW MANAGEMENT EXPLORES THE ROLE OF THE INDEPENDENT DIRECTOR AND WHY THE BERMUDIAN SERVICES OUTSHINE THAT OF ITS RIVALS



Neil Glass serves as an independent director of numerous funds. From 2013 until recently, he led the Bermuda Business Development Agency Asset Management Group, interfacing with senior members of the regulator, government and fund industry as they worked together to renew Bermuda's asset management industry. For more information, contact Neil Glass on +1 441 295 1144 or wwmgmt@logic.bm.

HFMWeek (HFM): Are there any misconceptions regarding independent directors? If so, what are they and are they justified?

Neil Glass (NG): An ever-shrinking group of detractors debate whether independent directors add any value. Back in the days when the majority of fund investors were high-net-worth individuals, in many cases the expectations and demands put on directors were low. There were instances of individuals acting as directors of hundreds of funds. This all changed once institutional investors, with their due diligence requirements, owned the majority of assets under management.

Post-2008 financial crisis, when many independent directors proved their worth, the perceived value of independent directors increased significantly. Today, there are few people who question the importance of a good independent director.

HFM: How do independent directors bring value to Bermuda?

NG: There are a number of very experienced individuals on the island whose wealth of experience will ensure a fund's compliance with its corporate governance requirements. I, for example, have worked in the Bermuda fund space since 1990, and have served as an independent director of funds since 1994. Additionally, I am an independent director of Bermuda, BVI and Cayman funds. This wealth of experience enables me to add significant value to the funds that I serve.

HFM: What makes Bermuda's fiduciary services so high-quality?

NG: With a highly regarded regulatory framework, sophisticated legal system, commercial courts, well developed infrastructure and global companies with a physical presence, Bermuda maintains a reputation as a blue-chip jurisdiction able to quickly respond to market changes while meeting clients' commercial needs. The two other main pillars of Bermuda's international business sector—risk (insurance, reinsurance, captive insurance and insurance-linked securities) and trust and private client industries—demand a world-class workforce of experienced, internationally trained and qualified lawyers, accountants, administrators and independent directors, the same professionals the fund industry also requires.

HFM: Bermuda is known for its tremendous service providers—why is this?

NG: The fact there are so many international companies with a large physical presence on the island means there is a real need for globally distinguished service providers. Bermuda funds do not require local auditor sign-off, administrators, custodians or directors. However, all of these services are available on the island and competitively priced, making Bermuda the ideal one-stop shop for ongoing operations; the resulting competitive spirit provides ideal conditions for market-based economies to thrive in. In fact, because of this on-island expertise and efficiency, many of these services are provided on-island to funds incorporated in other jurisdictions.

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HFM: How is Bermuda's corporate governance innovative and how does it set Bermuda apart from rivals?

NG: Bermuda embraces a culture of collaboration between industry, the regulator and government, with all parties working together to achieve commercial success, and is recognised as a blue-chip jurisdiction and cooperative partner by the international community, including the US and UK. The island currently has 91 treaty partners, including 41 bilateral Tax Information Exchange Agreements (TIEAs) and 87 co-signatories of the Council of Europe's Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

Bermuda is considered a leader on tax-transparency issues by the

US Departments of Justice and State, the US Treasury, the OECD, FATF and G20 nations. In 2009, the island was the first offshore jurisdiction elevated to the OECD's "white list" for jurisdictions that have substantially implemented internationally agreed tax standards. Bermuda is compliant with US and UK anti-money-laundering and anti-terrorist-financing requirements, and does not have banking secrecy laws.

At the same time, Bermuda does not have requirements that add costs and time to processes, but add no value to funds. For example, Bermuda funds do not require a local auditor sign-off, and there is no annual registration fee for Bermudian directors. ■

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INSIDE BERMUDA

CRAIG BRIDGEWATER OF KPMG EXPLORES HOW BERMUDA REMAINS AT THE FOREFRONT OF INTERNATIONAL BUSINESS



Craig Bridgewater

is head of Investments and Banking at KPMG in Bermuda. He has significant experience providing audit and advisory services to the financial services industry, including Bermuda-based funds and investment managers.

The financial services industry in Bermuda has enjoyed a world-class reputation for many years and is one of the world's premier funds jurisdictions. Bermuda has earned its reputation as a sophisticated, well-established and secure jurisdiction through its appropriate and globally recognised regulatory environment, modern infrastructure, highly respected intellectual capital, relative ease of raising capital and innovative fund vehicles.

With its investment services and fund administration capabilities, Bermuda remains at the forefront of international business, offering fund and investment managers access to a full suite of services and skills from the stable of expert professional service providers that are resident in Bermuda. Bermuda is home to experienced and internationally trained and qualified professionals including lawyers, accountants, administrators, bankers and independent directors. Many of the service providers in Bermuda have access to international networks and can bring these resources to bear in their service offerings.

EASE OF SETTING UP AN INVESTMENT FUND VEHICLE IN BERMUDA

The time to establish/register a fund ranges from immediate (for Class A Exempt funds) to five working days. The set up time will be quickest for those new funds that are one of a series of already established funds or is being established by promoters well known to the Bermuda Monetary Authority (BMA). Where promoters are not previously known to the BMA or the investment fund has novel or unusual features, approval could take longer. Applications by institutional funds are fast-tracked and usually take less than five working days.

Formation of an investment fund, preparation or review of its prospectus, and obtaining BMA approval for the fund to sell its shares is normally performed in conjunction with lawyers that are based in Bermuda.

INVESTMENT FUNDS LEGISLATION IN BERMUDA

The existing infrastructure and legislative framework in Bermuda is sound yet versatile enough to make it meet the needs of new entrants.

Open-ended investment companies are incorporated as mutual funds under the Companies Act 1981 (as amended) (the "Companies Act") as exempted companies. Limited partnerships are formed in compliance with the provisions of the Limited Partnership Act 1883 (as amended) and the Exempted Partnerships Act 1992 if established as an exempted partnership. Unit trusts are governed by their trust deed or other instrument establishing the trust.

The Investment Funds Act 2006 (IFA) is the principal legislation that, together with the Companies Act and the trust deed in relation to unit trusts, governs the activities of investment funds operating in or from Bermuda. For the purposes of the IFA an investment fund includes unit trust funds, mutual fund companies, and partnerships. It does not include closed-ended investment companies.

An investment fund may apply for authorisation under the IFA. Requirements for authorisation include the appointment of an investment manager, an independent auditor, an administrator, a registrar and a custodian. Authorised funds are required to submit a report of activities and performance to the BMA on prescribed intervals. Within six months of its financial year end, an authorised fund must submit a statement to the BMA confirming that it has been in compliance with the IFA during the preceding year or, in the case that it has not been in compliance, the particulars of the breach.

Private funds (having less than 20 investors) and closed-ended investment companies are excluded from the IFA. Certain investment funds are eligible for an exemption under the IFA, those being Class A and Class B Exempt Funds.

RECENT LEGISLATIVE UPDATES

Amendments to Bermuda's Partnership laws came into force in December 2015, and provide greater flexibility in how Partnerships can do business. As a result of the Amendments:

- The safe harbour provisions of the Limited Partnership Act 1883 have been enhanced to clarify that if a Limited Partner undertakes certain actions, they will not be surrendering their limited liability status as a Limited Partner
- Partnerships that have elected to have separate legal

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THE TIME TO
ESTABLISH/REGISTER
A FUND RANGES
FROM IMMEDIATE
(FOR CLASS A EXEMPT
FUNDS) TO FIVE
WORKING DAYS
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personality may hold assets and grant security in their own name

- A Partnership can convert to a Company and vice versa, and overseas Partnerships can easily convert or “continue” into Bermuda.

REGULATORY ENVIRONMENT IN BERMUDA

Bermuda’s regulatory and operational environment has been impacted in recent years by the introduction of various international regulatory initiatives, including, Solvency II, AIFMD, Fatca and CRS. These impacts are not inconsistent with other jurisdictions as changes in international regulation is reshaping how business is conducted globally. Bermuda has often been at the forefront of the adoption of such international regulations and at times has achieved first mover status, which has given this jurisdiction a competitive advantage.

The BMA is the main authority responsible for the regulation of investment fund vehicles that are domiciled in Bermuda. The BMA insists that persons proposing to establish funds in Bermuda are of sound business integrity, have relevant industry credentials and are of good financial standing. Bermuda is the jurisdiction of choice for discerning fund managers.

The BMA are committed to the process of qualifying for third country passport rights under the AIFMD that would allow Bermuda-based fund managers to market their AIFs in EU member states on a cross-border basis. Bermuda has made significant progress towards putting in place the necessary legislative framework to meet AIFMD criteria including amendments to Bermuda’s Investment Business Act (IBA) to provide for an AIFMD-compliant, opt-in regime. The legislative updates establish a regime in which the BMA will oversee Bermuda-based managers who wish to market their alternative investment funds via the passport in Europe.

Bermuda have been included in the second wave of non-

EU jurisdictions to be assessed by the European Securities and Markets Authority (Esma) to determine whether the third country passport should be extended to them. Esma is expected to complete its assessment of Bermuda by 30 June 2016.

Bermuda has been recognised as a leader on global tax-transparency issues. Bermuda has more than 90 tax-transparency treaties with countries from around the globe and it was the first offshore financial centre to qualify for the Organisation for Economic Cooperation Development (OECD) ‘white list’ for jurisdictions that have substantially implemented internationally recognised tax standard. In addition, Bermuda has entered into Model Intergovernmental Agreements (IGA) with the US and UK under the respective Fatca regimes.

Bermuda has an effective, robust and proficient regulatory environment that is appropriate for investment fund vehicles and related activities. Bermuda’s regulatory environment was recently recognised by regulators in other larger jurisdictions such as the US, UK and throughout Europe.

INNOVATION

The most recent example of Bermuda’s continued innovation is in the convergence space between insurance and investment funds, where several new insurance-linked securities (ILS) and hedge fund backed reinsurer structures have been set up in Bermuda in recent years. These investment vehicles have increased in popularity in recent years and Bermuda is one of the leading players in this space.

DOMICILE OF CHOICE

Bermuda has always been, and continues to be, a relevant and appealing place to establish an investment fund vehicle. All funds and investment management industry players in Bermuda continue to work diligently to ensure that it remains a premier domicile for many more years to come. ■

ILS²: TRANSFORMATION OF AN INDUSTRY

CORINNE HEWSON OF BENNETT JONES PROVIDES AN ESSENTIAL INSIGHT INTO ILS²



Corinne Hewson's corporate practice is focused on the financial services industry, with specific focus on insurance and reinsurance regulation in Bermuda.

Over the last three decades, alternative sources of capital have become increasingly common in the reinsurance industry. Sourced from a broad array of non-traditional investors such as hedge funds, state funds, pension funds and private equity funds, alternative capital is being deployed in a variety of non-traditional financing structures, often providing material start-up funding for new (re)insurers and special purpose (re)insurance vehicles (SPIs). And, now, an increased demand for ability to trade insurance-linked securities (ILS) in the secondary market.

A BACKGROUND

ILS are non-equity securities issued by SPIs, initially developed to provide additional excess coverage for catastrophe risk in a hard (re)insurance market in the early 1990's by transforming insurance risk into non-correlated investment opportunity, thereby enabling the capital markets to absorb (re)insurance risk. Generally, (re)insurers use cat bonds to transfer major property and casualty risk to the capital markets; enabling them to eliminate such risks from their balance sheet, reducing their overall reinsurance costs and freeing up capital to underwrite new insurance business.

Alternative capital has provided an increasingly significant percentage of funding in the (re)insurance market over the last 30 years that it's not such an 'alternative' source any longer. Indeed, alternative capital's participation in the (re)insurance market is now so commonplace, it is more aptly described as 'non-traditional' funding.

SIDECARS AND CAT BONDS

Alongside SPIs, which offer ILS in a multitude of formats, other common structures formed in Bermuda are referred to as sidecars and cat bonds. While cat bonds and sidecars differ in the form of securities they offer, each can be described on a very basic level as a 'special purpose', closed-end fund with a restricted insurance licence to provide (re)insurance coverage to a defined (re)insurer, or class of (re)insurers (each an insured), for specific insurance risk, or group of risks on a fully collateralised basis, payable on the happening of a defined event (each a triggering event, or trigger) in exchange for the payment of insurance premium.

The cat bond raises the majority of its funding by way of proceeds received on the offering of the ILS to investors via the capital markets. Investors of the ILS receive an interest, by way of a coupon, in the profits earned on the investment of the ILS proceeds and the premium

received by the cat bond on the provision of the (re)insurance coverage. The (re)insurance premium received, along with the proceeds of the ILS, are aggregated and deposited into a collateral trust account held for the benefit of the (re)insurance policyholder. Funds in the collateral trust account are invested in stable, low risk investments, often money market funds. The investment yield on such investments is then passed to the ILS investors via the coupon attached to the ILS.

Sidecars issue participating, non-voting ILS to investors in much the same way as cat bonds. Investors purchase ILS in exchange for an interest, by way of dividend, in the investment yield earned on the commitment of the SPI's collateralised permanent capital received as a result of the aggregation of ILS proceeds and (re)insurance premium (collectively referred to as insurance capital are generally known as sidecars).

An investors' interest in either a sidecar or a cat bond is subordinated to the interests of insurance policyholders (each an insured). In essence, meaning investors may lose up to 100% of the total value of their capital investment and up to 100% of their interest in the investment yield on the occurrence of the relevant triggering event. They may alternatively walk away with up to 100% of their invested capital, up to 100% of their portion in the investment yield and anywhere in between, depending on the way that the SPI's underlying insurance policy is structured and the terms of the form of ILS issued. Thus highlighting the regulatory requirement that ILS investors must have a full appreciation and understanding of the changing levels of risk attached to the securities they invest in. Interestingly, the majority of litigation surrounding ILS has been brought by investors who allege they were ignorant to the complexities of risks involved and the consequent extent to which their investment was at risk.

ALTERNATIVE AND NON-TRADITIONAL INSURANCE

Despite the potential loss of an entire investment, (re) insurance and ILS represent a relatively low risk investment opportunity when the appropriate hedges and diversification strategies are employed by investors. Ultimately, due, in part, to the non-correlation of these products with the financial markets and local and global economics generally. Alternative/non-traditional insurance investors are attracted to ILS by the high investment yields on the invested insurance capital. Meanwhile, the increased participation by non-traditional investors in the (re)insurance market is a logical progression of an investors efforts to diversify their investment portfolios.

The underlying valuation of the ILS is complex, not simply based on the actuarial modelling of the relevant triggering event, but also, is dependent on the kind of triggering event itself, the form and duration of the underlying insurance policy and the return on investment yield. The complexities mean that the level of risk attributable to each issues ILS may change significantly during its existence consequently creating a demand for secondary trading in ILS.

It is anticipated that non-traditional investment in the (re)insurance market will continue to increase as evidenced by the increasing demand for a liquid secondary ILS market. TigerRisk Partners, a highly-respected, prominent reinsurance brokerage and risk/capital advisor group, recently received Finra approval in the US to act as broker for ILS related derivatives (including securities issued by sidecars, cat bonds, industry loss warranties, related swaps and other derivate related to (re) insurance risk on a collective basis (ILS²)). TigerRisk's development of the first collective and cohesive market platform for trading ILS² is considered to be the launching pad for the creation of a liquid market in this form of investment opportunity. Both the insurance industry and the technology industry have long been discussing the inevitable development of a liquid ILS² trading platform with tech start-ups searching to develop technology, or specifically created to facilitate the electronic trading of ILS² and to assist in the pricing of the market and the settlement of ILS² trades. TigerRisk's platform encapsulates a collective ILS² marketspace and is the first out of the block. While TigerRisk's platform is not yet operational (the opening of initial trading accounts and meeting the compliance requirements involved will take some time), it is expected to launch in the near future. Even without the availability of the platform, secondary trading in ILS has increased by more than 25% over the previous quarter, according to reinsurance brokerage AON Benfield and Artemis magazine.

WHAT THE LEGAL LANDSCAPE ALLOWS

Bermuda's current legislative provisions are sufficiently flexible to allow for the commercial trade of ILS², subject to certain conditions which the industry hopes will be augmented to facilitate the electronic settlement of Bermuda-based of ILS². The current legal landscape allows for:

- The issuance and free transferability of non-voting securities in Bermuda (re)insurers, including ILS, subject to certain regulatory notification requirements relating to ownership percentage thresholds, the lowest being 10% or more of the relevant securities in any one Bermuda (re)insurer
- Issuance and transfer of bearer certificates or coupons subject to receiving prior regulatory consent from the Bermuda Regulatory Authority while retaining the prohibition on the issuance of equity securities in bearer form.

Unfortunately, however, Bermuda law does limit the method of transferability of such securities, in that it currently requires that transfers may only be affected with



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the delivery of an executed security transfer form to the issuer's company secretary for registration in the issuer's security register. With the development of electronic trading and settlement of ILS², it is vital that Bermuda provide adequate allowances in order for Bermuda-based ILS to participate in the ILS² market.

HOW DOES THE FUTURE LOOK?

Historically, the benefits of Bermuda's regulatory and legislative flexibility have enabled the jurisdiction to ensure that its regulatory infrastructure keeps the eloquent balance between adequate, sufficient and effective regulation, while maintaining its flexibility and progressive allowance for financial innovation within the markets. Bermuda's reputation as the jurisdiction of choice among other international financial centres continues to increase due, in large part, to this flexibility and willingness to evolve to meet the commercial needs of industry. We envisage that provision for the electronic transfer and settlement of Bermuda-based ILS² will be forthcoming in the future, based on the jurisdiction's historical inclination to adapt and progress with the development of commercial reality. All in all, we look forward to participating in its continued evolution. ■

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WHY CHOOSE BERMUDA?

JONATHAN BETTS, PARTNER AT TAYLORS, SPEAKS TO *HFMWEEK* ABOUT BERMUDA'S UNIQUE POSITION IN THE FINANCIAL LANDSCAPE AND WHY THE JURISDICTION CONTINUES TO EVOLVE

HFMWeek (HFM): What unique regulation and legislation does Bermuda possess that sets it apart from rivals?

Jonathan Betts (JB): The Bermuda government, together with the constituents of the business community and the BMA, have been working hard to develop amendments to legislation in order to make Bermuda increasingly competitive in the offshore funds space. There has been a significant collaborative effort between all parties.

For example, within the last few years, we created new classes of exempt funds - Class A exempt funds that require no regulatory approvals to launch and commence

operations and Class B exempt funds that require only minimal regulatory involvement. The Bermuda message is that we, as a jurisdiction, are constantly trying to develop our investment fund products. More recently, we have adopted changes to our partnership legislation to enhance the Bermuda partnership as a premier offshore product in the investment fund and private equity space and enacted third party rights legislation that will benefit investment managers, investment funds and third-party service providers. The ultimate aim is to make Bermuda as attractive as possible to the asset management industry.

New LLC legislation is currently being prepared and will certainly give clients and sponsors further variety of choice when it comes to selecting different investment vehicles. Furthermore, the legislation in place in Bermuda is easy to use, convenient and adaptable as funds are confident with using similar platforms elsewhere.

HFM: In terms of innovative products and services on offer, what does Bermuda have?

JB: Bermuda comes into its own in the insurance-linked securities (ILS) space; basically, vehicles through which there has been a convergence of the insurance industry and the funds industry. Cayman was the original off-shore ‘destination of choice’ for the catastrophe bond market and ILS vehicles, however, Bermuda has always had a strong reputation as a hub for the insurance and reinsurance industry. And, since 2009, when Bermuda introduced the class of ‘special purpose insurer’, the jurisdiction has led the way for this new type of funds product. The new regulatory framework for this class of special purpose insurer was introduced to make it easy and cost efficient to set up a fully collateralised insurance vehicle. Bermuda boasts around 70% of the ILS market. This exemplifies Bermuda’s willingness and innovation in the financial landscape.

HFM: Experience and history are also vital in the allure of a jurisdiction, how has the experience/knowledge on offer and vivid hedge fund history helped build such a market-leading reputation?

JB: Bermuda has a long and rich history of being a fund friendly jurisdiction which dates as far back as the 1980s. People in the industry know Bermuda’s history in fund set ups and ongoing regulation, and as a result, a broad range of service providers have firmly cemented themselves on the island. The island is home to a wealth of knowledge and experience, this is well spread across all those involved in the industry, including lawyers, accountants, fund administrators and asset managers.

Bermuda is very much a blue-chip jurisdiction and the island has always steered away from simply looking to attract volume business. For example, any person wanting to set up a corporate vehicle in Bermuda or to take a significant interest in a Bermuda company or partnership, has had to go through the process of disclosing beneficial ownership information to, and obtaining the prior approval of, our financial services regulator, the Bermuda Monetary Authority. As we all know, very recently the disclosure of beneficial ownership information has become a very hot topic globally, with various governments and bodies pressing for greater transparency and yet, in practice, Bermuda has maintained a beneficial register through the BMA for over 70 years now.

Our reputation for transparency is very strong, with Bermuda signing up to over 90 tax information exchange agreements as well as implementing Fatca and committing to the early adoption of the ‘Common Reporting Standard’ developed by the OECD. When you look at the various offshore financial centres, it is fair to say that Bermuda is one



Jonathan Betts is a partner and head of the corporate and finance practice at Taylors. Jonathan advises Bermuda-based and international clients on a broad range of corporate matters, focusing primarily on mergers and acquisitions, private equity and banking and finance transactions. He also advises in relation to the formation of investment funds and insurance matters.

of the premium jurisdictions in which to establish a fund.

HFM: Where does Bermuda see most of the competition coming from? How does the environment and ideal location create an appeal?

JB: In North America, Cayman is generally the go-to jurisdiction for hedge funds. And, European managers tend to cast their gaze to the likes of Jersey, Guernsey, Luxembourg and Ireland. The preference is ultimately dependent on the location of the hedge fund manager. What we offer is an ideal environment, a huge array of intellectual capital and experience and also a link between North American and European located managers and investors. Time zone also plays a big part, and physically sitting between the two major geographical hedge fund continents, Bermuda can offer something which most jurisdictions can’t, a convenient connection.

More recently, we have had some success in attracting investment fund managers to set up on the island. The convenient location of Bermuda has played a key role in attracting these managers, being just over two hours’ flight from New York and just over six hours’ flight from London is almost second to none.

HFM: Why should managers choose Bermuda over the competition?

JB: The tax neutrality of the jurisdiction is obviously appealing. Additionally, sitting between North America and Europe certainly acts as a differentiating factor. The infrastructure in Bermuda is well-established and over the years the island has proven time and time again how robust, yet versatile, it can be.

In terms of establishing new business, Bermuda is a welcoming jurisdiction, with increasingly flexible immigration rules, atmosphere and a helpful approach for those looking to set up. Furthermore, the Bermuda Business Development Association has been working very hard to support new business set ups and to provide guidance to those looking to physically establish here.

HFM: What key industry changes are set to be of the most significance to Bermuda in the next five years?

JB: We believe that Bermuda will continue to see growth in the ILS space and interest from hedge funds who are looking to invest in assets where the risk is uncorrelated to the capital markets. As the ILS market continues to mature and fund industry participants become more acquainted with the asset class, we very much hope that the increased exposure to Bermuda as a fund jurisdiction may also have a trickledown effect, encouraging more fund managers and sponsors to consider the jurisdiction as the ideal place to establish their new funds. The appeal in the island also goes hand in hand with the success of those already located here. It is evident that as individuals, funds and businesses build further momentum and successes stories grow, others will follow suit. All in all, Bermuda holds an enviable location in the hedge fund industry, and one that is home to all sorts of opportunities. ■

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IN FUND SET UPS AND
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PROVIDERS HAVE FIRMLY
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ON THE ISLAND
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BERMUDA LEADING THE WAY

MARCIA WOOLRIDGE-ALLWOOD OF THE BERMUDA MONETARY AUTHORITY TALKS TO *HFMWEEK* ABOUT BERMUDA'S ROLE AS A MARKET LEADER



Marcia Woolridge-Allwood and her department are responsible for the supervision of Bermuda's banks, deposit companies, trust and investment businesses, investment funds, fund administrators, corporate service providers, money service businesses, and credit union, as well as the Bermuda Stock Exchange. After six years in the banking industry in Canada and Bermuda, and at Bermuda's Registrar of Companies, Marcia joined the BMA in 1986 and was appointed to her current position in 2010.

HFMWeek (HFM): Bermuda is known for its role as “the world’s risk capital” and as the birthplace of captive insurers. The Bermuda Monetary Authority (BMA) has also recently been successful in achieving Solvency II equivalence from Europe. How has this impacted the island’s alternative investment and hedge funds sector?

Marcia Woolridge-Allwood (MWA): The BMA’s reputation as a top-tier (re)insurance regulator has a positive influence on Bermuda’s financial services sector as a whole, including asset management. Achieving important milestones like Solvency II equivalence gives potential investors/new entrants to the market a level of comfort and trust about the credibility of Bermuda’s regulatory regimes.

The BMA is currently focused on applying for recognition as a jurisdiction from which Bermuda-licensed fund managers can manage and market funds in the EU under the AIFMD.

HFM: Can you describe Bermuda’s regulatory regime for funds and any developments?

MWA: The BMA’s risk-based regulatory framework allows for the appropriate level of regulatory oversight depending upon the nature of the fund (i.e. private, funds of one vehicle or retail funds), as well as the type of investor (i.e. sophisticated institutional investors versus more retail individual investors). For example:

- Standard funds may be offered to retail investors and therefore attract the most comprehensive supervision by the BMA. Administered and institutional funds are only open to qualified investors and undergo moderate/medium supervision
- Private funds contain no more than 20 participants so are considered ‘excluded’ and fall outside of the BMA’s licensing regime
- Specified jurisdiction funds cater to the needs of investors from jurisdictions with special requirements
- Two classes of funds available to institutional funds: Class A Exempt Funds, which can be set up and

launched within one business day provided they meet certain high level criteria, and Class B Funds that must meet the same high level criteria but require pre-approval by the BMA prior to launch.

HFM: In terms of enforcement, what are some of the key issues in Bermuda?

MWA: In our 2016 business plan, the BMA announced a more public approach to enforcement. Moving forward, the BMA will publish details of any use of its enforcement powers. Such publicity will be in the form of a press release issued by the BMA following conclusion of any appeal or after expiry of an appeal period.

Enforcement activities conducted by the BMA over the last two years have resulted in nearly \$2m collected in monetary penalties and fines for material non-compliance.

The BMA’s legislative agenda for 2016 includes the strengthening of enforcement powers via amendments to the Investment Funds Act 2006.

HFM: How does Bermuda work with other countries to harmonise efforts?

MWA: The BMA is a full member of the International Organisation of Securities Commissions (Iosco) and remains actively involved in working with other countries to develop, implement and promote adherence to internationally recognised standards for securities regulation.

Since 6 June 2007, the BMA has been signatory to a Memorandum of Understanding (MoU) with Iosco, which paved the way for protected information sharing when appropriate and the collaboration on the development and implementation of Iosco’s core principles, considered to be the global standard of securities regulation.

In May, I attended Iosco’s 2016 annual conference in Lima where members discussed responses to

the challenges facing markets regulators today. During the four-day meeting, the Iosco Board, the Growth and Emerging Markets (GEM) Committee, the four Regional Committees and the Affiliate Members

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Consultative Committee (AMCC) discussed policy initiatives to strengthen securities market resilience and ensure that securities markets continue to be sustainable sources of finance.

On enforcement cooperation, Iosco's Presidents' Committee approved the text of an Enhanced Multilateral Memorandum of Understanding (Enhanced MMoU) on cooperation and the exchange of information. This followed detailed discussion at the GEM Committee, Regional Committees and the Board.

The Enhanced MMoU, which is aspirational in nature, provides for the additional powers that Iosco believes are necessary for its member regulators to ensure their continued effectiveness in deterring cross-border misconduct and fraud in securities markets. It builds on the success of the current MMoU on cooperation and exchange of information, while taking into account technological and regulatory developments since the launch of the original MMoU in 2002.

The Enhanced MMoU sets out five new powers in addition to those in the current MMoU:

1. To obtain and share audit papers
2. To compel attendance for testimony by being able to apply a sanction in the event of non-compliance
3. To advise and provide existing information to another regulator on how to freeze assets
4. To obtain existing Internet service provider records, not including the content of communications
5. To obtain existing telephone records, not including the content of communications.

It was resolved that arrangements for implementation of the EMMoU will be developed by the Board in consultation with the Regional and Growth and Emerging Markets

Committees with a view to approval by the Presidents' Committee by the end of 2016.

HFM: Bermuda has signed co-operation agreements with the majority of EU member states in relation to the AIFMD. Why is this important and what is the current status of the process?

MWA: Our work continues on the development of an opt-in regime for alternative investment fund managers (AIFM) based in Bermuda. The BMA's AIFM regime provisions were incorporated last August within the existing Investment Business Act 2003 and gave the BMA power to issue AIFM rules.

Parallel to the development of the AIFM opt-in framework, Bermuda has submitted its assessment questionnaire and supporting papers to the European Securities Markets Authority (Esma), in order to determine whether the Bermuda regime qualifies for a third country (non-EU) to enable licensed fund managers to manage and market funds into the EU. Bermuda, along with five other jurisdictions, was selected for consideration in Esma's second wave of assessments, the results of which are expected at the end of June 2016.

HFM: What future amendments to legislation can we expect to see within the next two years? How will these amends impact Bermuda's financial environment?

MWA: In addition to the BMA's plans to finalise development of the legislative regime to enable passporting into the EU, the BMA will continue the consultation process regarding enhancements to Investment Business Act and Investment Funds Act with a view to fully revamping the legislation in 2017. ■



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AN INNOVATIVE TOOL IN PRIVATE WEALTH MANAGEMENT

PETER CH'NG OF CONYERS DILL & PEARMAN DISCUSSES THE FAMILY OFFICE BERMUDA MUTUAL FUND SEGREGATED ACCOUNTS COMPANY



Peter Ch'ng is a director in the Corporate Department in the Bermuda office of Conyers Dill & Pearman having joined the firm in 2001.

The benefits and uses of Bermuda segregated accounts companies (SACs) to ring-fence assets and liabilities in insurance and investment fund structures are long-established. The Bermuda Supreme Court has consistently upheld confidence in, and the strength of the SAC.

In the private client sector, use of an SAC mutual fund company can be a unique addition to the usual combination of trust and corporate entities for wealth management. A private SAC mutual fund dedicated to a high-net-worth family may achieve flexible and diverse investment and inter-generational asset protection objectives, while offering a greater degree of engagement by family investors.

ROLE OF THE FAMILY OFFICE

Affluent families often use a family office to preserve wealth and manage their affairs separately from their business activities. With family members and their wealth and interests spread out globally, contending with diverse legal and cultural considerations in their wealth and estate planning, family offices provide an integrated professional and administrative service, navigating today's highly regulated environment. The family office can be the central coordinator of specialist advisors to determine the best options for the family in terms of philosophy, governance and objectives, including strategic philanthropy.

The family office may also undertake the education of future generations. A chief concern is the need to share the family blueprint with the next generation and to involve them in the management of their own wealth in a controlled family mutual fund structure.

SAC FUND STRUCTURE

The family office incorporates a "personal" mutual fund company registered as an SAC. Segregated Accounts (accounts) may be created by the SAC to individually hold diverse assets or strategies. Each account may issue redeemable participating shares to members of the family and affiliates (in their personal capacity or through a buffer entity such as a company, limited partnership or trust).

They may become beneficial owners of the assets of the accounts through the participating equity. Separate trusts for different branches of the family may hold account-linked shares. A typical family office SAC structure may be depicted as follows:

Redeemable investment shares and associated investments are made available only to family members or their relevant trusts or trustees and would likely be regarded as a qualified private exempted offering.

By creating individual accounts with different investment strategies, the family may mix and match investment portfolios through equity subscriptions.

For example, an SAC may create separate accounts to hold commodities, publicly traded securities to be managed by a licensed US broker-dealer, and more speculative investments such as coal mines in Brazil. The liabilities of each account are segregated and ring-fenced. An investor may choose to invest in the accounts in any desired combination. Further, the shares may be gifted or held for succeeding generations as a nest egg in one or more trusts.

A Bermuda mutual fund SAC with fewer than 20 participants will generally qualify as an excluded private fund under the Investment Funds Act 2006 and will therefore be excluded from regulation by the Bermuda Monetary Authority. Certain investment funds eligible for exemption incur minimal reporting obligations. Audited financial statements for each account may be prepared or collectively waived by the investors.

Unlike unlimited partnerships, investors may also participate actively in investment supervision

by appointing themselves or their advisors to investment committees for specific accounts without losing their status as limited liability investors.

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AFFLUENT FAMILIES OFTEN
USE A FAMILY OFFICE TO
PRESERVE WEALTH AND
MANAGE THEIR AFFAIRS
SEPARATELY FROM THEIR
BUSINESS ACTIVITIES
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BENEFICIAL FEATURES OF THE SAC FUND

Separation and Protection

An SAC affords greater protection against risks and losses, and insulates investments without the need to establish corporate entities. The failure of one account will not affect the solvency or viability of another, unless the latter has undertaken to underwrite the former.

The SAC structure permits portfolio diversity and

solates the risk from each strategy. Each investment is ring-fenced and compartmentalised in respect of access to account reports and information.

In a trust structure, an obligation exists to act in the overall interest of every beneficiary. Investors/beneficiaries in an SAC may choose which account to invest in, according to their individual risk profile and diversification strategy, as each investment is separately owned and maintained. An investor (i.e. a family member or a related trust for their benefit) wishing to exit an investment strategy is able to redeem shares, providing greater flexibility than does a trust.

By law, account transactions may not be inspected by third parties with no interest in the account, potentially offering a wall of confidentiality from exited investors or other family members.

Individualised Dividends and Distributions

The account must be commercially solvent when paying dividends and distributions. There is no requirement for the SAC or all its accounts to be solvent when a dividend/distribution is declared or paid from a solvent account.

Inter-account Support

With investors' consent, the SAC structure allows for one account to transfer assets to or financially support another account. For example, an account may enter into derivative contracts such as currency calls or put options, with another account providing collateral support to the first account. The supporting account is insulated against any direct claim by the trading counterparties of the first account.

The Offshore Benefit

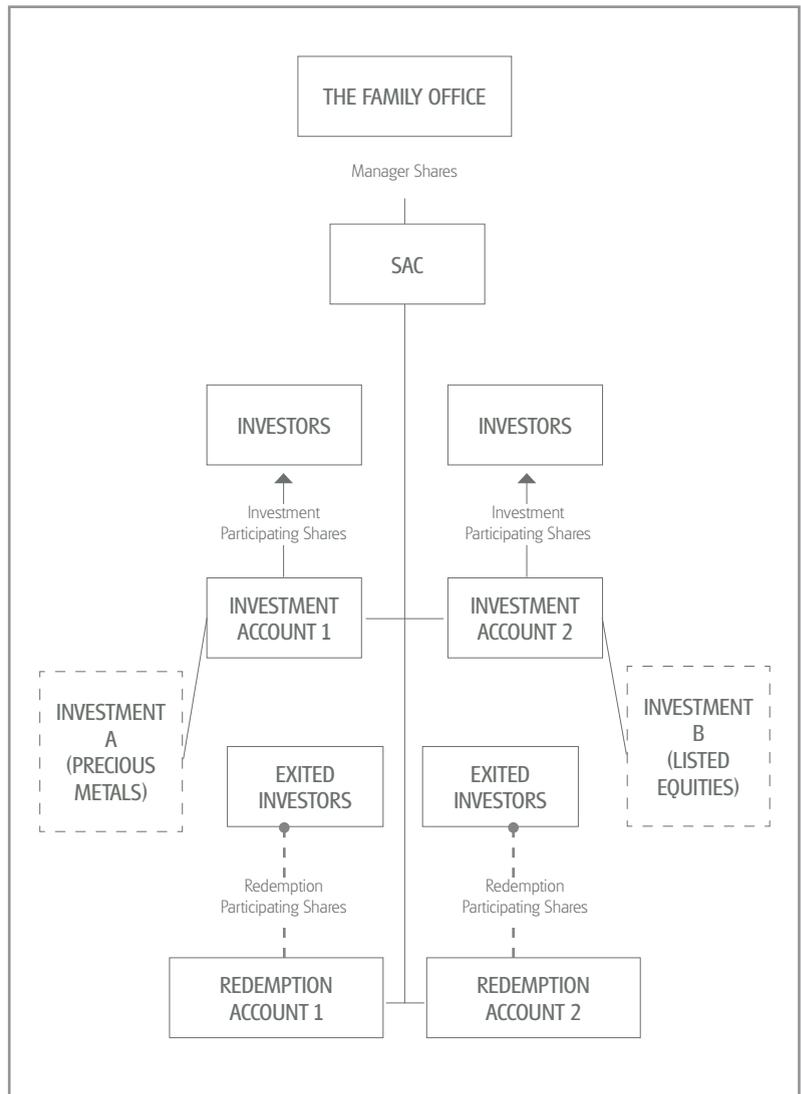
In some instances there could be tax and other legal advantages of legitimately deferring income tax on dividends or capital gains tax from realisation of overseas investment assets, including arising from the redemption of the shares by a SAC that is managed offshore.

A unique feature of the family offshore SAC is for each account to be accompanied by a dedicated and separate "redemption account", for the sole purpose of receiving the proceeds of redemption of shares in the account, without repatriating the proceeds back to the home jurisdiction, possibly incurring a taxable event (see the illustration above). The investors would exchange their participating shares in the account for similar shares in the redemption account, effectively exiting an investment strategy and parking their proceeds in a ring-fenced fund held by the same SAC. Proceeds in the redemption account may subsequently be deployed for reinvestment in any other investment account of the SAC or to external investments.

Costs and Economies of Scale

The administration of separate trust and corporate entities can be costly. An SAC may have any number of accounts, at a lower cost per fund, while centralising administrative control in the same entity.

The family office can take on part of the role and functions of the investment manager or advisor to the SAC and charge a fee/commission to defray its administration costs. It may also fund family-oriented goals and projects.



A family office/investment manager not operating within Bermuda need not be licensed or regulated in Bermuda.

Incorporated Segregated Accounts Companies

Bermuda has been exploring the potential for Incorporated Segregated Accounts Companies (ISACs). ISACs create incorporated accounts with separate legal identity, being advantageously severable from the ISAC core entity. This may prove attractive to members looking to create legally distinct governance for their accounts, but still share back-office functions and costs with the core ISAC, until they are ready to spin off an account into another entity.

Following the banking crisis, many wealthy families and their family offices have retreated from reliance on bank-affiliated advisors and taken greater charge and control. A bespoke SAC provides an efficient tool to hold diverse investment assets with minimal regulation and maximum flexibility for family or close-knit investors to chart their own financial course. ■



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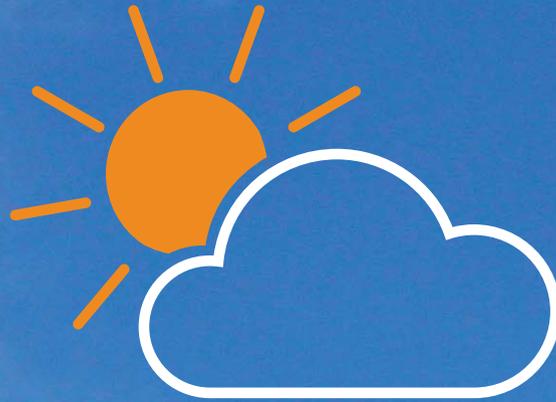
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THE CLEAR CHOICE FOR PRIVATE EQUITY AND HYBRID FUND VEHICLES

BRIAN DESMOND AND SCOTT BURNS OF IKONIC FUND SERVICES EXAMINE WHY BERMUDA SHOULD BE THE DOMICILE OF CHOICE FOR LAUNCHING A PRIVATE EQUITY OR HYBRID FUND STRUCTURE



Scott Burns is the head of Private Equity at IKONIC Fund Services with 19 years of private equity industry experience. Scott has previously held the roles of head of JP Morgan Private Equity & Real Estate Services (JPM Bermuda) and head of Private Equity Fund Services for Schroders Bermuda.



Brian Desmond, FCA, is a founding member of and the CFO/COO for IKONIC Fund Services. Brian has over 17 years of fund industry experience having previously worked at Citigroup Fund Services as Bermuda Country Head and an audit senior in the investment group of Ernst & Young.

Bermuda has focused its efforts on creating a user-friendly regulatory environment for the investment funds industry and, once again, is emerging as a jurisdiction of choice for alternative funds. Bermuda's renowned and long-standing reputation for experienced and cutting edge service providers, a sophisticated and sensible regulatory environment and the ease of establishing a fund entity in Bermuda has helped propel the island to the top of the list of where to domicile a fund. This applies to not only corporate entities but also to limited partnership structures which have benefited from recent amendments made to the partnership legislation, making Bermuda an attractive destination for private equity and hybrid fund structures.

What is a hybrid fund? A hybrid fund combines a traditional hedge fund investment mandate with characteristics historically associated with the closed-ended structure of a private equity fund. The hybrid fund structure has grown in popularity over the past five years, stemming from the changes in the global credit market, ever-increasing regulatory pressures and the search for alpha from illiquid investments. Given the unique structure of both private equity and hybrid fund vehicles, general partners focus on identifying a jurisdiction that has a strong, yet flexible, regulatory and legal framework with well-established service providers who have experience with these fund structures.

LEGAL FRAMEWORK AND REGULATORY ENVIRONMENT

The majority of private equity and hybrid fund structures are set up as partnerships due to nuances attributable to these types of funds and investments. In 2015, Bermuda made significant updates to its Partnership Law, greatly enhancing the use of limited partnerships for both general partners and investors. First and foremost, Bermuda is one of the few jurisdictions that allow partnerships to have separate legal personalities, which means they can hold assets and grant security in their own name. As a result of the recent updates, another key change means exempted limited partnerships can convert to exempted companies, and vice versa, providing the ultimate in flexibility as the needs of the fund change over time be they tax, legal or otherwise. The other key change is likely to pique the interest of private equity managers given their strong desire to protect the anonymity of their investor

base. The general partner of Bermuda limited partnerships is required to maintain a register of limited partners under Bermuda law. The amendment still requires this but now says that the general partner does not need to disclose the partnership register for inspection purposes. These two changes to the Partnership Law alone make Bermuda a compelling jurisdiction option for limited partnership fund vehicles as most other offshore fund jurisdictions cannot offer the same flexibility as Bermuda limited partnerships.

One attractive differentiator that is not commonly known, but definitely makes Bermuda an attractive and cost effective option for partnership fund jurisdiction, is the fact that there is not a need for local audit sign-off as is the case in other well-known offshore jurisdictions. For example, if a general partnership has established a Bermuda exempted limited partnership and conducts most of its business in the US and hence has engaged a US-based audit firm, there is no additional requirement to have the audited financial statements signed off locally in Bermuda. This exception is a material time and cost saver for general partners.

Regulation has drastically increased in the industry over the past decade and varies from jurisdiction to jurisdiction. Bermuda's regulatory environment, which is monitored by the Bermuda Monetary Authority (BMA), is widely known for being robust yet flexible, making it painless to conduct business in the jurisdiction. The BMA takes a risk-based approach to financial services regulation providing a flexible framework for general partners and service providers to operate.

Bermuda has a reputation for having a robust fund governance regime and the legislation which governs Bermuda partnerships does not try to regulate the affairs of a partnership, although, if the partnership agreement does not address a particular situation, the Partnership Act 1902, as amended from time to time, would apply. At the very least, every exempted partnership must have a physical registered office in Bermuda, not a P.O. box as well as a resident representative. If the general partner isn't based in Bermuda they will normally engage their administrator's or law firm's corporate services teams to provide this service. Corporate services professionals, particularly ones affiliated with a fund administrator, are key to ensuring that the exempted limited partnership stays compliant with local regulations. For example, if



there is a change to the general partner of the partnership, the corporate services group can assist with making those changes in compliance with the BMA's requirements.

FUND ADMINISTRATION

Service providers, in particular fund administrators, further contribute to Bermuda being a natural domicile for private equity and hybrid style funds. Many of these fund structures are set up as Bermuda partnerships and Bermuda-based fund administrators are extremely knowledgeable in all facets of the operations of a limited partnership vehicle, from accounting and investor servicing to AML regulatory requirements and fund governance. Fund administrators are well-versed in the nuances of private equity and hybrid structures and have lengthy experience with managing the capital call process, navigating aspects of varying waterfall distribution calculations, facilitating the complexity of subsequent closes and have extensive experience with some of the unique reporting requirements for such fund structures. They have developed their technology and reporting to service this segment of the alternative funds market and have ensured that their service offering follows the International Limited Partner Association (ILPA) standards, yet is flexible enough to adhere to specific limited partner requests.

“
 BERMUDA'S REGULATORY ENVIRONMENT, WHICH IS MONITORED BY THE BMA, IS WIDELY KNOWN FOR BEING ROBUST YET FLEXIBLE
 ”

One big advantage Bermuda has over other jurisdictions, is the depth of both hedge fund and private equity experience in all areas of the service provider landscape. One key reason managers choose Bermuda for private equity and hybrid funds is the incredible depth of experience in the law firms, accounting firms, administrators, directors and consultants. It is very common to find relationships with the senior staff that goes back decades. This close proximity of such depth of private equity and hedge fund experience gives Bermuda a strong advantage in the selection of private equity and hybrid fund formation domicile and service provider selection.

BERMUDA, A COMPLETE JURISDICTION FOR PRIVATE EQUITY AND HYBRID FUND VEHICLES

As the alternative investment industry continues to evolve due to changes driven by regulators, investors, and general partners themselves, Bermuda is well-positioned to be the leading choice as both a location to domicile hybrid funds, traditional private equity entities as well as general partners and also as a leading choice for private equity professional service firms. Bermuda has spent three decades creating a landscape tailor-made for alternative investment vehicles and continues to be a responsive and innovative jurisdiction. The island strives to implement new fund structures and products to provide solutions to the never-ending challenges which arise in this arena. ■

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IKONIC is an independent fund administrator providing administrative support to global investment managers adopting diverse investment styles. Our comprehensive product offering specialises in hedge funds, fund of funds, private equity funds, and ILS funds. IKONIC was founded by a leadership team with significant in-depth knowledge in fund administration and has created a company that is client focused. IKONIC currently services over 140 client entities from its three offices and clients range from emerging managers to large institutional funds. In November 2011, IKONIC and the Horseshoe Group formed a joint partnership called ILS Fund Services Ltd. to provide fund administration and valuation verification services to funds that invest in insurance linked securities. IKONIC Fund Services and ILS Fund Services are licensed fund administrators by the Bermuda Monetary Authority.



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The logo for the Bermuda Business Development Agency (BDA) features the letters 'BDA' in a bold, white, sans-serif font, set against a dark blue rectangular background.

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