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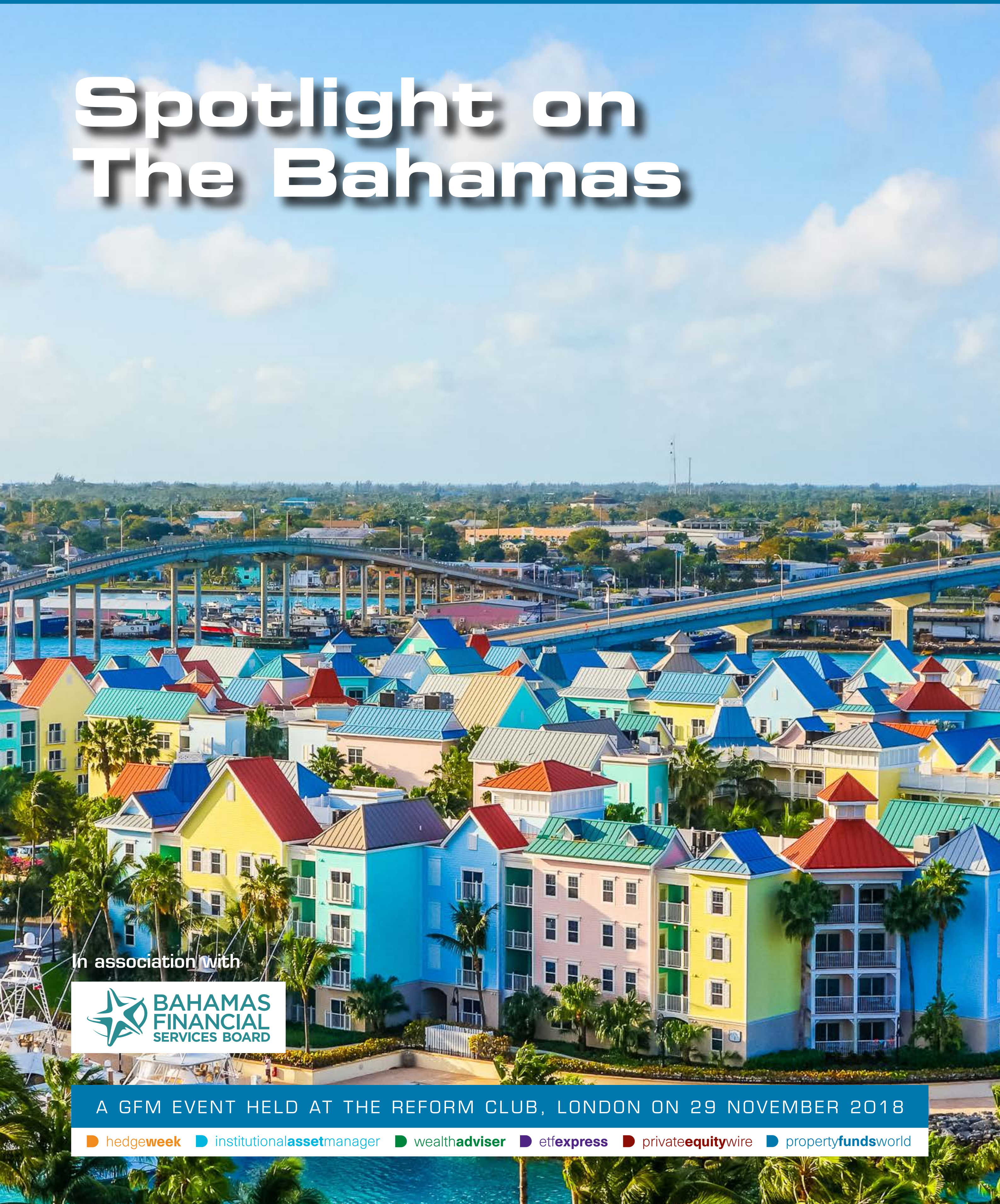

Spotlight on The Bahamas

In association with

BAHAMAS FINANCIAL SERVICES BOARD

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Spotlight on The Bahamas

Opening its doors to the institutional marketplace

By James Williams, Managing Editor, Global Fund Media

On Thursday 29th November 2018, Global Fund Media hosted an exclusive event in conjunction with the Bahamas Financial Services Board (BFSB), to showcase how the jurisdiction is updating its regulatory regime, not only to bring it into closer alignment with global best practices, but also to open itself up to more institutional fund interest.

The event started with a brief introduction by Tanya McCartney, CEO and Executive Director of the BFSB, who acknowledged that this was a time of great change, not least in the UK as the country assesses the "impact as well as the opportunities of Brexit". "We trust that in this process, The Bahamas will be top of mind for you," McCartney remarked to an audience that featured a range of service provider and fund management professionals.

Tanya McCartney, BFSB

To set the scene, McCartney welcomed the Hon Theodore Brent Symonette, Minister of Financial Services, Immigration Trade and Industry. Symonette began by acknowledging that today it is no longer business as usual. International regulatory requirements and compliance standards are becoming more complex yet The Bahamas continues to have an important role to play in delivering wealth management tools to meet the needs of clients.

"We live in a world that has never seen so much wealth and the need to protect that wealth is becoming increasingly relevant," said Symonette. "That is why we feel The Bahamas is the clear choice for financial partners to deliver services to HNW clients around the world. We remain one of the world's foremost wealth management centres, which has historically demonstrated its commitment to providing high quality services spanning a wide variety of fields; private banking, estate planning, asset management, fund administration and other corporate and financial services.

"We recognise the need to be innovative in our approach and to display our strength and commitment as a sustainable international finance centre."

To demonstrate this, over the past two years The Bahamas has expanded its participation on multilateral agreements, such as mutual administrative assistance and tax matters and multilateral competent authority initiatives such as Common Reporting Standards. It is also part of the OECD's multilateral BEPS Convention.

In addition, EU initiatives are being addressed currently by The Bahamian government's Code of Conduct Group.

"The Deputy Prime Minister has tabled the Register of Beneficial Ownership Bill, the Commercial Entities (Substance Requirements) Bill and we have in the pipeline a new Investment Funds Act draft bill. All of those are designed to bring us in line with our commitments to the EU and OECD valuations," explained Symonette.

"In addition, the FATF evaluation report has been published with a scheduled timeframe and we look forward to implementing a number of measures. We've committed to providing financial and human resources to ensure the FATF recommendations are adhered to, moving forward.

"We've also started a process of WTO accession. All told, we believe this sends a loud and clear message to the IFC community that The Bahamas is serious about adhering to global financial standards and making sure we have a clean, competent jurisdiction."

To further underscore its commitment to remaining a progressive, forward-thinking jurisdiction, earlier in 2018 The Bahamas passed a Commercial Enterprise Bill. The purpose of this was to attract people to The Bahamas to develop arbitration technology, international maritime trade, captive insurance, and make it easier for them to transfer their office headquarters to the jurisdiction.

There are numerous benefits to The Bahamas, which will be discussed later in this report. Suffice to say it is an independent, English common law sovereign territory. It offers a range of financial services and products to meet clients' requirements,

"We recognise the need to be innovative in our approach and to display our strength and commitment as a sustainable international finance centre."

Hon Theodore Brent Symonette

and over the years has developed innovative solutions in areas including trust and private banking, capital markets and most recently in support of family offices. It is home to a large cadre of skilled, motivated professionals and as Symonette concluded:

"It is the prime focus of The Bahamas Government to ensure that we maintain high visibility and show our commitment to global regulatory standards."

Investment Funds Bill 2018: key updates & developments

New legislation related to the Investment Funds Bill 2018, recently approved by the Government of The Bahamas features a number of new developments.

The SCB's initiative to overhaul the legislation governing the investment funds industry was launched with the appointment of a technical drafting consultant and the establishment of an IFA project team.

On 27th November 2017, the draft Investment Funds Bill was issued for public consultancy. This concluded on 28th February, 2018. The draft regulations were then issued on 13th April 2018, and that consultation period ended on 15th June 2018.

Subsequent to both releases, the SCB held industry-wide meetings as part of the consultation process. Comments received were all taken into consideration, collated and are presently being reviewed and discussed ahead of the Bill being formally approved by the Ministry of Finance.

Key changes

Some of the key changes relate to:

- Definition of Bahamas versus non-Bahamas based funds;
- "Carry on business in or from within The Bahamas" as a trigger for licensing of funds;

- The ability to appoint international administrators without requiring that they be licensed in The Bahamas;
- The introduction of licensing requirements for investment managers and regulatory oversight of custodians;
- Introduction of an AIFMD regime with a view to The Bahamas qualifying for an EU passport.

The licensing of Bahamas-based funds under the new regime will be defined as those funds that carry on doing business from The Bahamas, are incorporated, registered or established in The Bahamas, have their governing laws in The Bahamas (applicable to unit trusts), or if they invite persons in The Bahamas that are not accredited investors to subscribe to the funds.

A foreign fund to which a Bahamian accredited investor subscribes does not have to seek licensing or registration in The Bahamas.

In her presentation, Christina Rolle, Executive Director of the Securities Commission of The Bahamas said that the new legislation proposed to re-orient the definition of Bahamas-based funds "as well as to rationalise the regulatory regime applicable to non-Bahamas based funds".

"In relation to the definition of an investment fund, the current definition was amended to no longer tie the investment fund to it being a Bahamas-based fund. The proposed definition deletes references to any specific nexus between the fund and the jurisdiction and replaces it with being sold to non-accredited investors in The Bahamas..

"This change in the trigger of licensing rationalises the basis for licensing so that funds are licensed based on the activities of the fund and not the fact that service providers are located and/or licensed in the jurisdiction," explained Rolle.

For non-Bahamas based funds, the SCB has determined not to re-establish the requirement for professional funds sold in The Bahamas to appoint a representative in the jurisdiction and to remove this criterion from the definition of non-Bahamian based funds altogether.

Rolle said that the SCB accepted that such an appointed representative "would be burdensome".

Any regulatory risk arising from the sale of non-Bahamian based funds to accredited investors in The Bahamas is the regulatory burden of the fund's home jurisdiction, she said. "As it now stands, the definition of non-Bahamian based funds no longer includes reference to a fund that is being offered to accredited investors in The Bahamas and is solely linked to a licensee of the Commission: that is, an administrator or fund manager acting on behalf of the fund that is registered in another jurisdiction. In these circumstances only a notification of the fund, to the Commission, is required."

"In relation to the definition of an investment fund, the current definition was amended to no longer tie the investment fund to it being a Bahamas-based fund."

Christina Rolle, Securities Commission of The Bahamas

Under the new Investment Funds Bill, there will no longer be a requirement for Bahamas-based funds to use a local licensed fund administrator.

Rolle said that the SCB accepted this change was necessary "to ensure the jurisdiction opens itself to gain ground globally".

The proposed legislation removes the category of exempt administrator. In addition, the Bill provides that an administrator cannot act on behalf of an investment fund unless it holds a license under the Investment Funds Act or is licensed and operates in a prescribed jurisdiction.

Oversight of fund managers and custodians

The Bill mandates the appointment of an investment fund manager for all Bahamas-based funds except for those funds whose investors are 1) the fund manager or a parent or subsidiary of the fund manager or 2) a feeder fund that invests 100 per cent of its assets in a Master Fund.

Further, the draft Bill proposes a dual system of regulation that will implement a risk-based requirement for either the registration or licensing of the fund manager.

James Williams, Global Fund Media

Michael Paton, Lennox Paton

Ryan Pinder, Graham Thompson

Linda Beidler D'Aguilar, Glinton Sweeting O'Brien

Heather Thompson, Higgs Johnson

Fund managers of Bahamas-based funds which are being sold to accredited investors will only require registration, explained Rolle, while managers of Bahamas-based funds being sold to non-accredited retail investors will need to be licensed.

Licensed fund managers in the jurisdiction will require working capital of USD125K but there is no capital requirement for registered fund managers.

For fund managers who do not appoint a custodian, they will be obliged to ensure that the usual custodial obligations for holding assets are carried out appropriately. Custodian oversight is another example of how the Commission will be applying a risk-based regulatory approach to the jurisdiction, moving forward.

"There is no need to register or license a custodian separately from the investment fund. The proposed provisions require that a custodian be appointed unless exempted by the SCB. The custodian is also required to be independent of the fund administrator, fund manager and operator of the fund," added Rolle.

The draft Investment Funds Bill is currently subject to cabinet approval by the government, which the SCB expects to be passed in early 2019.

The Bahamas value proposition: products and services deep dive

Following Rolle's presentation, a panel discussion featuring a number of leading Bahamian service providers was moderated by James Williams, Managing Editor, Global Fund Media. The panel discussion focused in on three main areas, which included:

- The regulatory landscape – what's new?
- Growth Markets & Service Provider Developments;
- Product Innovations.

The panel included:

- Michael Paton, Head of Corporate & Commercial, Investment Funds and Banking & Securities Group, Lennox Paton;
- Ryan Pinder, Partner, Graham Thompson;
- Linda Beidler D'Aguilar, Partner, Glinton Sweeting O'Brien;
- Heather Thompson, Of Counsel, Higgs Johnson.

1. Regulatory landscape – what's new?

Like all other international finance centres, The Bahamas has found itself to be the focus of the EU Code of Conduct Group, the OECD and the Financial Action Task Force (FATF).

Paton said that the primary issue for The Bahamas in 2018 has centred on the threat of blacklisting by the EU for potentially being an uncooperative jurisdiction for tax purposes. Following a list of criteria in order not to be considered uncooperative, which the EU published in December 2017, it then came out with a list of jurisdictions that were, in effect, on a grey list.

"The EU clearly set out a list of criteria to comply with: for example, we had to bring into force a beneficial ownership register. This will be a decentralised register. The Government and various competent authorities will have the ability search the register. Importantly, however, the register will not be open to public search or access," explained Paton.

Another requirement by the EU is

that anyone doing business activities in The Bahamas must have a "substantive economic presence" on the island. The EU is particularly focused on what it calls highly mobile capital and business. In short, they don't want offshore jurisdictions hosting businesses without substance.

"If you are a fund management business registered or incorporated in The Bahamas, you will be required under the new legislation to have offices, staff, and have the ability to make important strategic decisions from the jurisdiction. Although investment funds per se are not in the scope of this legislation, we are satisfied the amended Investment Funds Bill 2018 will satisfy the EU's requirements," said Paton.

Substance requirements

Given that The Bahamas is home to a number of international banks which has trained and developed local talent over many years, Pinder, who was a minister of financial services for the previous administration, believes the island has the capacity and is "well positioned to service the market when it comes to more emphasis on substance and having decision-makers located here.

"When looking at jurisdictions on a go-forward basis in a new world order of economic substance, The Bahamas is well positioned," said Pinder. Beidler D'Aguilar added that with recent developments upgrading the University of The Bahamas campus, the island is equipped to produce qualified personnel to perform qualified roles in financial and corporate institutions to meet the substance requirements.

"There will also be a need to bring in talent as well and there is a commitment to ensure overseas persons are able to get work permits as essential staff. There will be both a domestic and international component to growth, which is going to improve our financial services sector," said Beidler D'Aguilar.

Commercial Enterprises Bill & Investment Funds Bill 2018

The introduction of the Commercial Enterprises Bill is a reinforcing factor in support of the substantial development of businesses in The Bahamas. "It provides a fast-track process for work permits, as Linda referred to," said Pinder, who went on to emphasise that the updated Investment Funds Bill is especially exciting as it should lead to more institutional funds business being created.

After all, The Bahamas has historically been known as a private wealth centre.

Pinder remarked that one of the most exciting components of the new Investment Funds Act will be the ability to properly allocate the fiduciary obligations in the right places; that is, back to the fund manager and not left solely to the fund administrator.

"That should make it more attractive to setting up institutional funds in The Bahamas. The prospect of future growth in our funds space is very exciting. Major international fund administrators are not in the business of taking on fiduciary risk in the context of fund administration. I think the segregation of duties and the new licensing of fund managers is going to go a long way to demonstrating that we have the commitment to develop an institutional fund market," suggested Pinder.

Beidler D'Aguilar said she had spoken with a number of onshore fund administrators, both in the EU and North America, and that there was now a level of interest "that we just hadn't seen previously".

"Also, we do not require local audit sign-off," stressed Paton. "Our approach when redrafting the legislation was to try to be as facilitative as possible while also meeting our IOSCO principal obligations. We now have a framework in place that makes it much more interesting for institutional funds."

2. Growth markets & service provider developments

One key development that The Bahamas is particularly keen to take a leadership position on is blockchain and the overall growth in 'fintech' services.

As a top-tier regulator, the SCB understands the flexibility needed for new business and as such has been developing the framework that will be required.

Pinder said he was hopeful that the jurisdiction will soon release "some groundbreaking regulation for public consultation that both addresses the framework for cryptocurrency and digital asset offerings, and also for digital asset exchanges based in The Bahamas".

"We've moved at a measured pace but quick enough to attract business to the jurisdiction," he said. "The SCB is certainly seeing a lot of interest in the digital assets space among fund managers."

Whatever legislation does get introduced will need to strike a balance between what has to be regulated and what has to be registered. It is hoped that this pragmatic approach, overseen by a business-friendly regulator, will attract technology entrepreneurs and specialists in the fintech space over the coming years.

To support this, however, The Bahamas will need to continue to build out its business infrastructure.

"It's a case of building on our existing strength," said Thompson. "We've always had a good service provider infrastructure and successive governments have recognised that there is a need to have outside expertise. I think in certain areas we will continue to expand under the new Commercial Enterprises Bill."

Broker/dealer growth

Another interesting growth area, which has been underway over the last couple of years, is an influx of broker/dealer activity, especially with respect to FX. There are now a number of new licensees leveraging local expertise to help them operate in The Bahamas, some of who are experts in the fintech space.

"We are, therefore, seeing a merger of fintech with the broker/dealer community that goes beyond the scope of our traditional private banking environment," remarked Pinder.

A third growth area that the panel brought to the audience's attention was the growth in family office activity.

Beidler D'Aguilar suggested that the need to centralise the collection and maintenance of information because of Common Reporting Standards and other tax reporting requirements was essential when families have large interests across different regions. "As a result," she said, "we are seeing more interest in The Bahamas among family offices because it is home to all the necessary service providers and, moreover, we are well located for the Americas. It is a good place for families to consider, utilising the various investment products we have including trusts, funds, SPVs."

Paton agreed and felt that the relocation of HNW and UHNW individuals continues to be a good opportunity for The Bahamas:

"We have the infrastructure, the lifestyle, the climate, the location. The Latin America market in particular finds the jurisdiction a very interesting place. We are seeing some of the trust companies morphing into multi-family offices as well."

3. Product innovations

The third key area of discussion on the panel related to product innovation; something that The Bahamas has fully embraced over the last five to 10 years and which is, arguably, one of the key requirements of any progressive international finance centre.

While The Bahamas has made significant strides to update its investment funds legislation, Beidler D'Aguilar was quick to stress that this broad overhaul has not changed the nature of the fund products themselves.

One of the more innovative products is the Investment Condominium (ICON). An ICON structure is relatively simple to establish. It can be used for either a SMART Fund or a Bahamian Professional Fund, and one of the advantages is that it can be brought to market through an unrestricted fund administrator.

To briefly explain, the ICON is based on the investment condominium, a form of joint ownership of property under Brazilian civil law, and was integrated into the Brazilian investment funds regime as the means by which managers would establish and register their funds. It is a contractual agreement between an administrator and those investors who have agreed to invest jointly and is similar, in principle, to collective investment schemes in Europe.

"We took that notion and enabled it through a piece of legislation," said Beidler D'Aguilar. "It makes it much easier for Brazilian investors to understand how their Bahamian fund will work because it uses a familiar structure. We see wider interest in the ICON across the Americas. The administrator must be independent, which investors like."

Tax deferral is important for family offices, as well as asset protection and succession planning.

"Going in to an ICON Fund or a SMART Fund gives them that tax deferral and when they redeem, they get taxed at capital gain rates rather than ordinary income tax rates," explained Paton.

With respect to SMART Funds, they fit in to seven different templates that focus on either a limited number of investors, the nature of the investors (accredited versus non-accredited), and a minimum investment criteria.

"We see them being used as incubator funds, for example, and large subscription family funds. They are easily licensed, they only need a term sheet as opposed to a full private placement memorandum and offering document," said Pinter.

Indeed, a fund manager might want to use one as an incubator fund to test their strategy with a limited number of investors, build a track record, and then, at a later point in time, transform it into a Professional Fund.

At which point, the manager can market it to accredited investors.

It is attractive for family offices to have a licensed structure for the purposes of transparency with respect to different family members. This can be important in avoiding conflict and can help manage the family's various investment interests.

Also, there are no restrictions as to the types of assets that can be held by investment funds in The Bahamas. One can use a SMART fund to invest in cryptocurrencies, real estate, wine, art, etc.

"We also have segregated account companies that are utilised for investment funds, which have segregated cells underneath the Master Fund. There is no risk of cross-contamination of liabilities or asset classes. They can all be separately managed within one umbrella fund in different cells," added Pinter.

Conclusion

In summary, The Bahamas is gearing itself up to enter a new stage of growth as it sets out to build more of an institutional funds marketplace to support global fund management activities. By placing more fiduciary duties on the fund operator and the custodian, it is hoped that more global fund administrators will be attracted to the jurisdiction.

And with a clear commitment to digital asset innovation, The Bahamas is putting the pieces in place to remain one of the world's leading, progressive international finance centres. ■