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Bermuda Fund Services 2018



Rigorous regulatory oversight attracts fund managers

Secondary market emerges for ILS products

Strong focus on developing blockchain sector



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Bermuda: One step ahead of the game

By Sean Moran

This year promises to be a big one for Bermuda as we push forward on several strategies to make our market even more attractive and competitive for asset managers and allocators. In doing so, we aim to balance our goals as a jurisdiction with the many geopolitical and regulatory issues taking shape in 2018, including US tax reform, Brexit, and numerous global compliance initiatives.

Yet, these are the types of challenges Bermuda has always thrived on dealing with—and by doing so, has set itself apart from other financial centres. The spirit of innovation that has long been a hallmark of our international business community, as well as the optimism and creativity of our industry leaders, stand us in good stead to weather this current confluence of events.

Bermuda continues to be the example of what a well-regulated, modern financial centre committed to reliability and longevity looks like. In 2017, we became the first UK Overseas Territory to sign Country-by-Country Competent Authority Agreements with both the United Kingdom and United States. The agreements comply with Base Erosion and Profit Shifting (BEPS) tax-transparency standards set by the Organisation for Economic Cooperation and Development (OECD). France awarded Bermuda white-list status fulfilment of Country-by-Country reporting obligations. Bermuda was also declared “largely compliant” by the OECD Global Forum rating. Our AML/ATF assessment by the Caribbean Financial Action Task Force (CFATF) in 2018 will give us another chance to prove the robustness of our regime and build credibility with global regulatory bodies.



Sean Moran, Head of Business Development, Bermuda Business Development Agency (BDA)

Open for business

The continued focus on compliance cannot come at the expense of being business-friendly, however; we must keep delivering quality service to satisfy the commercial needs of our customers and stakeholders.

The CFATF assessment has given our financial regulator, the Bermuda Monetary Authority (BMA), the opportunity to improve efficiencies in its authorisation and ongoing supervisory processes. The BMA will also streamline some of the rules for insurance-linked securities (ILS) funds to allow them Class A Exempt status—featuring same-day registration— if certain requirements are met.

Besides the Class A Exempt, there is an array of fund categories to meet various needs, as well as a suite of structuring options, from the standard limited company (LTD) to the limited liability company (LLC) to the segregated account company (SAC), that has proven very popular due to its flexibility and cost-effectiveness. Our legal professionals will work with you to agree the optimal fund type and structure to fit your needs.

Speaking of professionals, the pool of talent in Bermuda continues to expand. The arrival of new international law firms and fund administrators into the Bermuda market over the past year has created a more competitive environment where customers are spoiled for choice, and where those firms need to be on top of their game to win business. Providers of outsourced compliance and reporting services are also increasing their headcount to meet client demand for greater support in these areas.

At the BDA, our Business Concierge Service is available to assist asset managers



and fund operators to set up smoothly and quickly in our jurisdiction. Providing access to the regulator and government officials, expedited company registration, and introductions to any local service providers you may require, our goal is to make it easy for you to launch your business from Bermuda.

Growth areas

Given Bermuda's status as one of the leading reinsurance markets in the world, it's no surprise we continue to be a dominant player in the ILS space. The majority of funds being registered and launched in Bermuda are situated on the broadening spectrum of alternative risk transfer, where the insurance and capital markets intersect. With creative deal origination, expert underwriting, innovative legal structuring and specialised back-office servicing all happening in one jurisdiction, it's no wonder most asset managers choose Bermuda as the domicile for their ILS products.

But don't forget that Bermuda first made its name in the funds industry many years ago, with the incorporation of the early Steinhardt hedge funds in the 1970s. In the decades that followed, our asset management professionals have adapted to the many flavours of alternative investment styles and asset classes, including private equity, fund-of-funds and hybrid vehicles that require outside-the-box comprehension and a deft servicing approach. Bermuda is certainly a location where these more complex or customised funds can be properly understood, established and administered.

High-net-worth individuals and family offices represent another interesting segment that is driving growth in new fund business. Originating from our very significant and successful trust and private client industry, wealthy individuals and families are increasingly focused on investing in

assets and ventures that have a social, environmental or charitable objective. This impact investing can take many forms, but when facilitated through a tax-neutral Bermuda fund or company structure, it can optimise the investors' returns while still achieving their philanthropic goals. Profit with a purpose.

The fintech revolution

The Bermuda government has committed to making Bermuda a leader in financial technology innovation and adoption. In late 2017, Premier David Burt and a working group comprised of local and international experts embarked on a mission to provide a legal and regulatory framework, and a fit-for-purpose ecosystem, for businesses offering innovative, financial products and services enabled by distributed ledger, or blockchain, technology.

In early 2018, legislation was passed governing initial coin/token offerings (ICOs) from Bermuda, and a raft of new regulation related to virtual currencies and digital asset exchanges is being rolled out before year-end. The move to embrace this rapidly evolving industry is viewed as critical if Bermuda is to remain progressive and relevant in the economy of the future – a future where blockchain technologies and the digitisation of assets are part of everyday business.

The fintech-related laws and regulations, in tandem with Bermuda's new Personal Information Protection Act (PIPA), ensure our jurisdiction offers the safest possible environment for today's and tomorrow's data-driven businesses.

From an asset management perspective, cryptocurrency investment funds will certainly be an asset class in which we expect to see growth. And with Bermuda setting the standard by being the first jurisdiction to regulate such activities, it is not inconceivable we could soon be as synonymous with fintech as we are with insurance. ■

Helping you succeed from strategy through execution



The critical issues that asset and wealth managers face today are forcing a rethink of business strategies.

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Transparency is clear to see

Interview with Scott Watson-Brown & Scott Slater

Tax transparency has been an evolving focal point for the world's economies as governments look to satisfy rigorous global compliance standards and shore up their tax revenues. Western media have focused on international financial centres following recent years' cyber breaches that led to sensationalistic reporting about offshore investments, stoking a public appetite for revelations on high-net-worth financial matters, including taxes.

The standard argument one often hears is 'why should companies avoid paying taxes in their home domicile?' The question certainly has merit, but those posing the question need to take the time to hear the answer – the reality is far more complex and nuanced.

What often tends to get overlooked is how a jurisdiction fits within an organisation's global structure – how does that company operate on a global scale, across numerous markets, catering for a variety of customer and investor needs?

These global structures are not for nefarious purposes, but are designed to allow the efficient deployment of capital to operate, strategise and grow a business and its offerings in the jurisdictions where there is demand.

As PwC's Global CEO Survey 2018 found, **regulation and tax changes are asset management CEOs' greatest worries**. For some asset managers, new tax rules are challenging historic tax structures. More generally, the US Foreign Account Tax Compliance Act (FATCA) and Common Reporting Standard (CRS), the rules for sharing of tax information about individuals between countries places the burden of reporting on financial institutions.

In addition, the US recently enacted comprehensive tax reform, which has caused a review of how US-based businesses and



Scott Watson-Brown, Partner and asset management leader at PwC Bermuda



Scott Slater, Tax Partner at PwC

US-owned foreign businesses are structured and operate.

Scott Watson-Brown is a Partner and asset management leader at PwC Bermuda. He says that it is easier to make sense of things when looking at the complete picture, a view that reflects PwC's depth of experience with multi-national structures.

"A particular country might complain a large corporation has moved capital from one place to another but it is unhelpful to look at isolated transactions. We get to see the full picture and understand our clients' operations and strategic initiatives as they develop their global corporate structure to achieve efficient operations and maximise benefits to customers and investors," says Watson-Brown.

Whilst Bermuda remains a jurisdiction with no income tax (Bermuda maintains a consumption based tax regime), questions over how corporations and fund management groups use the jurisdiction will likely remain. What Bermuda does and will continue to do is provide transparency to other jurisdictions' government departments and maintain its regulatory standards, which are aligned, as a minimum, with global best practices.

In the investment management sector, Bermuda has been at the forefront of transparency. It was one of the early adopters of the OECD's Common Reporting Standard, says Scott Slater, Tax Partner, PwC. "Bermuda has also signed up to a large number of Tax Information Exchange Agreements (TIEAs) and it was an early adopter of country-by-country reporting ("CbCR") under the Base Erosion and Profit Shifting (BEPS) initiative."

The announcement last year that Bermuda was enhancing its beneficial ownership regime is a further example of its efforts to ramp up transparency.

The Bermuda Monetary Authority has done a good job of explaining what processes are in place to capture certain key information in the jurisdiction with respect to beneficial ownership. “Bermuda has been collecting information on the beneficial ownership of companies for over 70 years,” says Watson-Brown.

“The recent amendments to UBO definitions ensures alignment with AML and ATF regulations; this will ensure that there’s no gap between what information is necessary to effect the prevention or detection of money laundering or financing of terrorism and that which is collected. We also entered into an agreement about 18 months ago with the UK to exchange UBO data so that it gets into the hands of the people who actually need it for legitimate reasons,” explains Watson-Brown.

Amendments to the regime will ensure that information about the ownership of entities is updated with relevant information, which is accessible on a timely basis by those with a legitimate interest. With the strengthening of the collection of data, Bermuda continues to show its commitment to the detection and deterrence of serious crimes, including money laundering.

Last year, the UK implemented changes to its beneficial ownership register regime, including the requirement for UK-incorporated companies to make their beneficial ownership registers open to the public.

The Bermuda Government and the BMA understand they have a responsibility to lead the way in how the jurisdiction operates and to date, they’ve done a good job.

“We’ve seen the Ministry of Finance and the BMA increase their efforts and headcount to keep pace with local regulatory developments and with global standards. Reputationally, it is paramount that Bermuda maintains its current position for embracing the constant change in global regulations,” adds Slater.

Both the Bermuda Government and the BMA are very clear in their expectations they set on how people do the business.

In line with global best practices, entities and their service providers are expected to adhere to Anti-Money Laundering (AML) and Anti-Terrorist Financing (ATF) rules in accordance with Proceeds of Crime

Regulations 2008. Moreover, entities will now be required to conduct beneficial ownership record keeping on an ongoing basis. As Watson-Brown states: “The BMA is always very consistent in its approach.

“For companies considering something new, whether it be the next alternative asset class or the creation of a bespoke structure to deliver on investor needs, the BMA is open to listening to what you want to achieve and at PwC, we can help in the achievement of your goals.

“The BMA enjoys having that dialogue because they want to understand what risks you pose to your investors and to the jurisdiction. Through open dialogue, the BMA can determine an effective framework to regulate your business and the associated risks. As a pragmatic regulator, we have seen the BMA develop exempt status for funds and their managers who are subject to scrutiny in home jurisdictions (e.g. the SEC) through to pending legislation to gain equivalence recognition under the AIFMD requirements in Europe.”

In Slater’s view, Bermuda is a progressive jurisdiction that embraces industry developments from a global compliance standpoint. The BMA’s mindset is to embrace “sensible regulation and reporting requirements, ensuring that they are fit for purpose”. He believes that there always needs to be a healthy push/pull in terms of what needs to be implemented.

“The jurisdiction is, I believe, at the right point on the curve in terms of staying current and engaging in dialogue with global regulators in the US and Europe around regulatory developments. That engagement is key,” states Slater.

Watson-Brown agrees: “The collective approach taken by the Bermudan authorities can be summarised as follows: ‘Let’s understand who is coming here, what business they are doing, where the risks lie and how to regulate them; and let’s be consistent in our application of that regulation’.”

For any incoming investor into a Bermuda fund structure, or individual or group looking to establish a platform for their business, that willingness of all parties in Bermuda to engage in dialogue should see Bermuda fare well over the coming years, as offshore jurisdictions continue to be put under the microscope. ■



Bermuda offers managers stability and a blue-chip reputation

By James Williams

Although the Cayman Islands tends to be the default option for most alternative fund managers, there is a good argument for saying that Bermuda is equally, if not more attractive; certainly from a cost perspective and a 'substance' perspective, with a well-established business district in Hamilton, the island's capital.

Indeed, an estimated 400 international companies are physically based in Bermuda, with an increasing number of fund management entities either setting up, or thinking of doing so. After all, Bermuda is only a two-hour flight to the US east coast, making it an ideal location for hedge fund managers and PE managers looking for an alternative to Cayman and the BVI.

"What a lot of people tend to overlook is that the offshore fund market, as a concept, originally started in Bermuda back in the 1980s. Cayman replicated it in the 1990s when Bermuda re-positioned itself to cater for the insurance and reinsurance market, which is now three to four times bigger than the funds industry," says Anthony D'Silva, Director of Incu Global, a fund platform operator which uses a Segregated Account Company umbrella fund structure to host investment advisors, to enable them to launch a fund quickly and cost effectively.

D'Silva points out that after factoring in the Registrar of Companies fees and the BMA government annual fee, the cost of operating a Bermuda fund comes to just under USD3K.

"In the Cayman Islands it is a little over USD10K a year," he says. "The other advantage that Bermuda has over other jurisdictions is audit sign-off. In Cayman, you have to use a Cayman-based auditor to sign off the fund's audit, which adds extra operating costs to the fund. In Bermuda you can appoint an auditor anywhere. We use Deloitte (Malta) for example.

"If you compare the cost of operations, and the regulatory regime, Bermuda is a solid option. In my view, Cayman is the offshore equivalent of Luxembourg, whereas Bermuda is the offshore equivalent of Ireland."

For the many industry professionals who have lived and worked in Bermuda for years, if not all their lives, they have seen a lot of changes to the regulatory landscape and even though its funds industry may have tailed off in years past, there appears to be a renewed focus to foster growth. This, in part, has been helped by the success of Bermuda's ILS fund space.

"Bermuda has upped its game by improving its funds regulation and its fund products, such that what you have now is a fairly even playing field. Cayman attracts a large volume of business but Bermuda still attracts a lot of high quality managers who like its reputation," says Dawn Griffiths, Director and Head of Bermuda Funds Practice at Conyers Dill & Pearman.

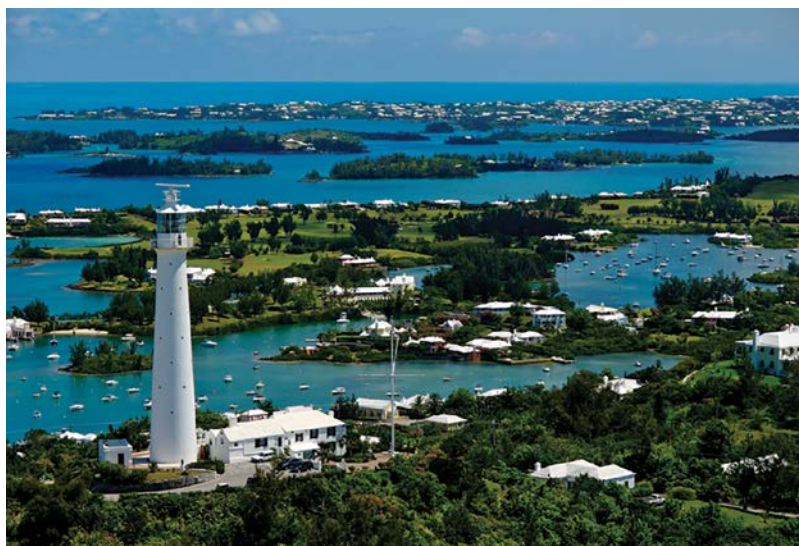
Successive governments in Bermuda have realised how important the fund industry is to this jurisdiction and accordingly have been very receptive in bringing new legislation forward to not only enhance the industry but also allow market innovation.

"The Bermuda Business Development Agency has been very active in this space and provides a concierge service to those that want to launch funds in Bermuda," notes Nitin Aggarwal, Chairman of Beacon.

At year-end 2016, the BMA reported total assets under administration and management of nearly USD200 billion.

"I personally think this is a good time for the fund industry in Bermuda and one which will show much positive growth in the future," adds Aggarwal.

Scott Watson-Brown is Partner and asset management leader at PwC Bermuda. Discussing the funds landscape, he remarks that regulation on closed-end vehicles



has always been very good. "We've seen other jurisdictions take on board some of the provisions that we've had in place for many years, in particular around the Partnership Acts. We have, in response to demand within the funds world, enacted the LLC legislation. Whether it is corporate structures, partnerships, LLCs, it is a matter of staying current and keeping on top of the expectations of those wishing to use these structures.

"In that respect, we see continuous improvement and enhancement of legislation as relates to those structures," explains Watson-Brown. Rather than attempt to break Cayman's stronghold on the hedge fund industry, Bermuda's modus operandi is to provide an alternative option to fund managers.

"If someone wants something a bit different, we can provide it. Family offices are a good example. When people visit Bermuda, they see the infrastructure, they see just how many people are on the ground across different service providers. This leads some to establish an office and staff it with a handful of people so that they have a real, physical operation as opposed to just a letterbox entity.

"Bermuda offers that level of attractiveness, where you can easily put a fully functioning family office here and attract and retain talent to operate that entity. It's also a very attractive place to live," says Watson-Brown.

Bermuda has a different feel to other offshore financial centres. There is, says Griffiths, more of a sense of 'permanence' to it. ► 14



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Regulatory oversight puts Bermuda in prime position

Interview with Ariane West

With some offshore jurisdictions having only moved recently to introduce registers of beneficial ownership, one could argue that having had its own register in place for over 70 years, Bermuda has been ahead of the curve. Now, as global regulatory oversight and transparency expectations rise, Bermuda is well placed to demonstrate that its house is very much in order.

The Bermuda Government and the Bermuda Monetary Authority have always paid close attention and cared to know who is doing business in Bermuda.

"That has been the standard operating procedure for Bermuda throughout its history as an international financial centre," says Ariane West, Partner in the corporate and finance practice at Taylors, a full service law firm which works in exclusive association with Walkers.

She says that whilst other offshore jurisdictions have had to ramp up their regulatory regimes, for the BMA it has been more a case of maintaining a commitment to the highest standards and best practices. What that has meant, in recent years, is keeping abreast of all the updated requirements driven by international initiatives such as CRS, signing up to a FATCA agreement with the US Government, as well as signing up to the BEPS initiative. In April 2016, the island became the 33rd signatory of the *Multilateral Competent Authority Agreement* for the automatic exchange of Country-by-Country reports on income and taxes paid by corporates.

Commenting on the BEPS regulation, West says that becoming signatory is



Ariane West, Partner at Taylors

simply reflective "of our ongoing method of operating".

"We will always look to comply with the highest standards in the marketplace so signing that agreement was really par for the course. We try to be a jurisdiction that has the appropriate level of regulation that adheres to global best practices. Some of the world's largest insurance companies are based here and that wouldn't be the case if we weren't a highly reputable jurisdiction that has appropriate levels of governance, transparency and regulatory stability.

"For us (adapting to global regulatory expectations) is not a sea-change but simply an ongoing commitment to being the best jurisdiction we can possibly be."

As part and parcel of that, the BMA and the Bermuda Government maintain their commitment to ensuring Bermuda's AML framework is keeping up with its obligations by constantly reviewing and adopting best practices within the regulatory regime.

"There are far more demands on financial regulators today, in terms of applying an ongoing oversight function. The frequency and size of data they are collecting is substantial. The demands have been ever increasing, transactions are becoming faster and more sophisticated and it's a matter of keeping pace with the markets," says West.

With respect to industry-specific initiatives, in the investment funds sector and the insurance sector the BMA strives to take an approach of 'smart regulation'.

At all times, it looks to ensure the regulations in place are addressing key

concerns, with respect to regulatory compliance and who exactly is operating in the jurisdiction.

At the same time, says West, the BMA has to ensure that the industry has a product that is fit for purpose and meets the needs of investment managers.

"In the investment funds sector, we have introduced new classes of exempted funds that are looking at trying to focus on the appropriate approach to regulation. For example, if someone is an SEC regulated manager there are Class A Exempted Funds that leverage off of that onshore regulatory oversight by allowing the US manager to benefit from more efficient regulatory processes in Bermuda.

"Also, in the insurance and ILS industry, Solvency II equivalence was a big focus for Bermuda's authorities. As that industry continues to grow and evolve so too has the product offering. The BMA pays close attention to this, ensuring they have a handle on how the different vehicles are being used, different classes of licenses, etc, and that they are being effectively regulated," explains West.

Something that people often overlook is that Bermuda was actually the pioneering jurisdiction for the creation of hedge funds almost 50 years ago, with its prominence in the space continuing into the 1990s.

In the last 20 years, the Cayman Islands has risen to prominence but Bermuda has a long history of serving the investment funds industry.

"At the time, perhaps Cayman was viewed as offering a more user-friendly product and it's true that Cayman has become the pre-eminent jurisdiction for hedge funds but I would say Bermuda has a very comparable service offering. For anybody who has an interest in Bermuda, the fund product is just as good.

"Indeed, some of our fund manager clients choose Bermuda because of its geographical location, being less than a two-hour flight to New York. They want that accessibility to the jurisdiction. There are numerous reasons for why Bermuda might be a natural fit for alternative fund managers but in terms of offering a straight up investment funds product, we can meet the needs of managers just as well as the Cayman

Islands or any other offshore jurisdiction," states West.

There is a bit of a herd mentality at play here. Start-up managers in particular, simply assume that they should launch a Cayman fund because everyone else does but on a like-for-like basis, there is very little difference between the two jurisdictions; in fact from a cost perspective, Bermuda fares better.

"Several service providers here offer an emerging manager platform solution using the Segregated Account Company (SAC) structure. For a manager who is looking to get up and running and build a few years of track record, the SAC platform is a very attractive option.

"We also have the ability for smaller funds with fewer than 20 investors to operate as private funds and not be subject to regulation under the Investment Funds Act. It is only once they pass certain thresholds that the manager would need to register and either apply for exempted fund status or authorisation by the BMA," says West.

She says that for the past seven or eight years, there has been a renewed focus on the investment funds space. This led to a re-appraisal of the Investment Funds Act in 2012.

"We made great strides and efforts to communicate with the market, asking managers what they needed from their offshore jurisdiction and out of that consultation came legislative initiatives to create streamlined classes of exempted funds, as well as the introduction of LLC legislation. That was modelled very closely on the Delaware statute so that we are able to offer managers a product that sits alongside their Delaware onshore LLC vehicle," adds West.

She confirms that Bermuda is very keen to maintain interest among alternative fund managers in the jurisdiction.

"We have been engaged in pursuing an AIFMD-equivalent status, which is still ongoing. It's in the hands of the European Commission at present but we have put in place the requisite legislation to create an equivalency regime. If and when things move forward, we will be ready to further enhance the attractiveness of Bermuda as a jurisdiction to domicile funds," concludes West. ■



10 ► “The Bermuda Government is talking about raising height restrictions in the Hamilton Economic Empowerment Zone to encourage further residential and mixed-use development. We therefore anticipate the financial district changing and evolving over the next few years. The Government wants new business, it wants more managers to physically locate here,” she says.

The quality of service providers is a key factor to the success of any fund jurisdiction.

Service providers like Beacon have invested in technology and implemented complete end-to-end IT solutions on a single platform to help better support fund managers as the complexity of fund products continues to develop.

Beacon’s system is a multicurrency general ledger that is fully integrated within the partnership and portfolio accounting software.

“The enhancements in our technology provide a single dependable hub for accounting data, which facilitates reconciliation and streamlines operations,” explains Graham MacDonald, Director of Operations at Beacon. “The portfolio accounting software tracks, analyses and accurately reports the value of complex investments across numerous portfolios. Built-in flexibilities organise data to efficiently account for all assets and the system is designed to meet the needs of diverse investment managers.

“Not only do our enhanced automated workflow tools streamline back-office operations to a higher level of efficiency, we also provide the best level of service due to

our investment in qualified and professional talent. Our client servicing team are orientated according to each client’s needs where they can expect a personalised touch.”

Another factor is offering managers fund products that meet their needs and are appropriately regulated.

Managers that are either FCA or SEC regulated or have more than USD100 million in AUM and marketing to sophisticated investors can, for example, qualify for Class A exemption. Managers who don’t meet that threshold have the option to use a Class B Exempt Fund, in which case they must make a filing to the BMA. The regulator then has two weeks to come back to the manager with questions or to request further information. If they don’t, the manager is deemed to have approval.

“In the hedge fund space, a lot of our clients really appreciated the ability to use registered but not regulated fund products,” comments Griffiths. “With respect to closed-ended funds, they are not currently subject to regulation under the Investment Funds Act. They operate entirely outside of regulation, which is a very flexible option for private equity managers, although they are subject to AML requirements.”

There may be some consultation by the BMA with industry in the coming months on potentially bringing these funds under the IFA regime but in that case, says Griffiths, “it is anticipated that they would be able to take advantage of the same flexible approach available for open-ended funds, that is, the ability to seek classification as regulated funds or exempted funds.

WHEN SMART COUNTS



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Bermuda's ILS marketplace

Q&A with Brian Desmond

For readers unfamiliar with ILS Funds, can you give a brief summary of the asset class?

Insurance Linked Securities (ILS) are financial instruments sold to investors and whose value is affected by an insured loss event. Two examples of the financial instruments used are catastrophe bonds and collateralised reinsurance contracts.

The buyer of protection, or the entity that is transferring the insurance risk is called the cedent and the seller or writer of the protection could be an individual investor or a hedge fund. For investors in hedge funds, the ILS asset class is not correlated with financial markets, creating diversification benefits and an ability to enhance investment returns.

A hedge fund can buy or sell catastrophe bonds directly in the primary or secondary market. Cat Bonds involve the reinsurance of high severity, low probability events. The bonds are commonly structured as floating rate bonds with maturities of usually less than three years, so the investor would receive coupons periodically and, of course, has the risk of losing the invested principle if a significant loss event occurred.

A hedge fund can also invest in collateralised reinsurance contracts, which are private illiquid deals that usually have a 12-month term. To write reinsurance, the entity writing the business is required to have an insurance licence. Therefore, a hedge fund, for example, cannot enter into private reinsurance deals directly but instead will invest through a Special Purpose Insurer (SPI) or what is commonly called a Transformer.

The hedge fund will purchase preference shares of the Transformer and the Transformer will use the subscription monies received to write the reinsurance transactions.



**Brian Desmond, CSO and EVP
Head of Fund Services at
Horseshoe Group**

Reinsurance transactions can take the form of a traditional reinsurance contract or derivative. The reinsurance limit or notional amount of the reinsurance contract is typically fully collateralised, thus removing any credit risk. The collateral assets are typically held in a trust account in highly rated liquid securities for the duration of the contract period until loss activity can be quantified. If the underlying contract is loss free, the collateral is returned to the investor along with the premium paid in by the reinsurance buyer.

In cases where investors or hedge funds do not have their own 'transforming vehicle', dedicated ILS service providers such as the Horseshoe Group can facilitate through the use of their own Transformer. Horseshoe can help investors interested in establishing an ILS Fund or accessing the ILS market in general, from the set-up phase through to the ongoing administration and valuation work, while also providing them with an infrastructure to invest into specific reinsurance structures.

Please provide a brief history of the ILS market

Back when Hurricanes Katrina, Rita and Wilma hit in 2005, the trail of devastation led to an estimated USD108 billion of property losses. At that time, reinsurance market rates skyrocketed and we saw a lot of reinsurance companies looking for additional capital. Hedge funds started to invest as expected returns for ILS structures were in the mid-teens. Since then, the composition of investors has evolved with the addition of large pension plans and family offices who have bought in to the low-correlation appeal of this asset class.

Since 2005, the market for insurance-



linked securities has increased substantially, creating an industry with approximately USD80 to USD90 billion trading between capital market investors and the insurance industry. The performance returns, over time, have been impressive and help to explain continued investor interest.

In 2006, alternative capital was estimated to make up approximately 4 per cent of the total reinsurance sector. This is now estimated to be in excess of 15 per cent in 2017, so ILS capacity has become an increasingly more meaningful part of the reinsurance sector.

Please provide a brief commentary on Horseshoe's positioning in the ILS market

As a pioneer in the Insurance Linked Securities administration space, Horseshoe has vast experience in all aspects of this unique and complex asset class.

Horseshoe can offer a true one-stop solution for those that want to set up a new ILS Platform, including the provision of fund administration, registered offices, corporate secretarial, insurance management, accounting, transforming, underwriting, claims and actuarial services within one company.

We are the foremost and largest dedicated independent ILS service provider team in the market with no affiliations with other service providers.

Horseshoe has a strong accounting backbone and a comprehensive set of skills

including, corporate services, actuarial, underwriting and claims. On the ILS fund administration side, this wide range of insurance expertise allows us to provide an independent review of complex ILS valuations.

Launching an ILS Platform can be a daunting exercise but it does not need to be if one goes about the process in a methodical and organised fashion. At Horseshoe, our management team provides a consultative approach to all relationships no matter if we are introduced at the early platform formation stage or later on when an established investment management firm is contemplating the launch of a new product.

How did the ILS market react to the large losses in 2017 and what is your outlook for the ILS industry?

The Harvey, Irma and Maria (HIM) events in August and September of 2017 plus the wild fire events in December last year resulted in 2017 being the largest loss-causing year ever and was the biggest test for the ILS industry to date.

The good news is that the ILS industry passed this test, with investors showing their commitment to the space by increasing their overall capital investment in ILS to a greater level than before the large loss events of 2017.

New risk capital is coming to market as investors continue to find ILS an attractive and diversifying asset class. We are seeing investors look for new entries into the insurance and reinsurance business outside of primarily the property cat bond markets. This means new and innovative products and offerings in the life and annuity as well as the casualty space. In fact, in many respects those lines of business are at a stage now where the property focused ILS market was in 2005.

We predict some interesting growth in these areas and overall we believe ILS will continue to become a larger percentage of the overall reinsurance market and will reach the USD100 billion milestone before 2020. ■

The Horseshoe Group is an independent and privately-owned group of companies forming a leading financial services company dedicated to both the insurance linked securities and the alternative fund markets.

Bermuda: The world's blockchain laboratory?

Interview with Dawn Griffiths & Chris Garrod

There is a sense of optimism in Bermuda that the success it has enjoyed over the years in respect of the ILS industry can, over the coming years, be replicated in the cryptocurrency and blockchain arena.

ILS fund managers like the fact that Bermuda has a lot of professionals working on the ground, from legal to administration and auditing. This is particularly important under Solvency II, which places a big focus on substance and physical presence.

"This has been fantastic for the funds industry," says Dawn Griffiths, Director and Head of Bermuda Funds Practice at Conyers Dill & Pearman, one of Bermuda's leading law firms. "The world's biggest ILS managers are based here running funds and we hope some of that success will be replicated in the blockchain and crypto space.

"At a broader level, I think as hedge funds face more corporate governance and substance requirements, they too will look to develop more of a nexus. It is something that Bermuda can offer given its close proximity to New York and we expect to see more managers and family offices beefing up their operations."

The Bermuda Government recognises that the growing prominence of digital assets represents a perfect opportunity to make Bermuda a leading blockchain jurisdiction.

"Bermuda's Class A and Class B Exempt Funds and the surrounding framework will be helpful in the emerging crypto fund space, particularly for those managers wishing to launch private funds with fewer than 20 investors who wish to build a track record without being subject to regulation by the BMA. Some of our major clients have started to introduce crypto futures into their investment strategies and are starting to ask questions about setting up dedicated funds in this space," confirms Griffiths.



Dawn Griffiths, Director and Head of Bermuda Funds Practice at Conyers Dill & Pearman

Chris Garrod is Director at Conyers Dill & Pearman and heads their Blockchain and ICO practice. He explains that the Hon. E. David Burt, Bermuda's youngest ever Premier, is extremely tech savvy with a desire to make Bermuda the world's pre-eminent blockchain jurisdiction.

"I am in discussions presently with government officials on proposed ICO legislation and Bermuda is also thinking about setting up a dedicated government-regulated virtual asset exchange. We are already getting cryptocurrency fund queries from managers wishing to list products on such an exchange. That said, the Bermuda Government is very mindful of AML and ATF safeguards in this space. They are collaborating with the private industry and the BMA to determine how best to introduce new legislation," outlines Garrod.

In its current form, ICO legislation will require a token issuer or a coin issuer to provide sufficient documentation to potential investors and meet certain minimum criteria similar to one would expect with a traditional fund prospectus.

This offering document would need to be filed with the Bermuda Government's Ministry of Finance, with Garrod adding: "Before the ICO commences, it will have to be reviewed and vetted by the Ministry to make sure certain requirements are met. Examples include: who are the people establishing the issuer? Do they have the appropriate expertise to launch an ICO? What is the exact nature of the cryptocurrency business?"

Bermuda is the second largest global reinsurance hub and was once described as the "insurance laboratory of the world".

With the savviness and determination Bermuda has displayed in the past in both the reinsurance and funds space, it could possibly soon be branded as the "blockchain laboratory of the world". ■

- 14 ► “With alternative fund managers thinking about substance and establishing a nexus more to where their funds are located, which is something we’ve already seen in the ILS funds space, I think it is a trend that will continue and benefit Bermuda as a result.”

A third factor is the ability to support start-up managers who need a cost-effective, quick route to market without having to worry about heavy handed regulation or delays in getting their funds approved.

Bermuda is beginning to see more platforms emerging, to cater to this demographic. SAC structures such as Incu Global are an important feature of the landscape. D’Silva confirms that the platform has onboarded two new funds so far in 2018, with another two funds expected to launch in the next six months.

“We are very selective about the managers we choose to work with,” says D’Silva. “I try to meet the managers on the platform at least twice a year but typically it ends up being once a quarter.

“I’m not there to raise capital for any of the managers on the platform but I am willing to introduce them to potential investors, if they are performing well. If they raise additional capital, we don’t charge additional fees. It’s a partnership. We charge a basis point fee for operating on the platform – so if the fund grows in AUM, overall, then we too grow as a platform.

“There are platforms that engage in what I call ‘double dipping’ – that is, they charge a fee for being on the platform and then charge a fee for helping the manager raise capital. That’s one of my bugbears. It can lead to a break down in relationship with the manager, which we do not want.”

Corporate governance & best practices

With offshore jurisdictions coming under greater media scrutiny, helped in part by high-profile cyber attacks, regulatory authorities cannot afford to be blasé about their oversight roles. Turning a blind eye to things is anathema in the eyes of global regulators such as the SEC and political bodies in the form of the European Commission.

Bermuda has actually long been committed to transparency in relation to corporate activity, having maintained a beneficial



ownership register for some 70 years. It was an early adopter of Common Reporting Standards and FATCA and has more than 40 tax information exchange agreements (TIEAs) in place as well as memoranda of understanding in place with 27 countries. It is also a Solvency II equivalent jurisdiction, having been granted equivalence back in November 2015 by the EU.

“There is a wide array of examples to demonstrate Bermuda’s commitment to global best practices,” says Ariane West, partner in the corporate and finance practice at Taylors, a full service law firm which works in exclusive association with Walkers.

“It is a long-standing and constant commitment to uphold best practices as they apply to regulation and transparency. The Bermuda Government and the BMA have always paid close attention and cared to know who is doing business in Bermuda and made it a priority to ensure that Bermuda is not a jurisdiction that would be attractive to parties who perhaps are looking to evade regulation or tax compliance in their home jurisdictions.

“That has been the standard operating procedure for Bermuda throughout its history as an international financial centre.

“Bermuda’s regulatory regime is seen as being user-friendly; for example there’s no local audit requirement, you don’t have to use a Bermuda administrator or have Bermuda-based directors sitting on the board. There is a lot of flexibility and optionality that managers can avail themselves of.”

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ILS as a trusted, institutional asset class

Interview with Sherman Taylor & Sarah Demerling

Within the capital markets, there remain a large number of institutional investors seeking out unique opportunities in alternative investments. One such area is insurance-linked securities (ILS), which have built significant traction since the 2008 financial crash.

Estera has been providing corporate, trust, fund and accounting services for over 25 years and has carved out a leading position in the support of ILS products. Analysis of its book of business over the last 10 years shows that the market capitalisation of ILS products it supports has grown from approximately USD2 billion in 2011 to USD10.8 billion at the end of 2016. Last year, the total market capitalisation of Estera's ILS clients grew 20 per cent to USD12.9 billion and there are signs that this growth trend is set to continue.

"One of the reasons for this is that ILS is not correlated to the broader stock markets; whether the stock markets go up and down has no direct impact on the pricing of ILS," says Sherman Taylor, Associate Director at Estera. "The only thing that could impact an ILS investment is if a covered loss event legitimately attaches to the collateral.

"One of the things we've seen from a historical standpoint is that the loss experience has been good. In 2017, there was a covered loss event after the earthquake in Mexico that attached to one tranche of the IBRD/Foden 2017 Cat Bond. The positive thing that came out of that event for the ILS industry was the orderly way that it responded, with the Cat Bond paying out USD150 million to the Mexican government."

The earthquake that Taylor refers to was a 7.1 magnitude event that hit Mexico on 19th September, 2017. It is estimated to have caused as much as USD4.8 billion of losses to insurance and reinsurance interests.



Sherman Taylor, Associate Director at Estera



Sarah Demerling, Client Director at Estera

"When it came to the January 2018 insurance/reinsurance renewal period, there was some concern that the catastrophe events of 2017, including the Mexican earthquake and several major hurricanes, might have an impact on the ILS market by dampening interest from the capital markets. However, that proved not to be the case. The response of the ILS industry to the 2017 catastrophe events instead gave the capital markets additional confidence in ILS investments because, with each of those events, the system worked precisely as expected to determine whether there were any insured losses attached to ILS capital," explains Taylor.

Recent market data from the Bermuda Stock Exchange (BSX) shows that 2017 was another growth year for Bermuda's ILS market, with 103 new ILS products coming to market during the year with total nominal value of USD11.54 billion.

Estera acted in various roles for 60 per cent of those new products, representing total nominal market value of USD5.8 billion, underscoring its position at the forefront of this asset class.

Far from being scared off by the loss event, the capital markets stepped up to the plate, with hedge funds and other investors continuing to allocate into the asset class, satisfied that, if ever there was a loss event potentially impacting their investment, there will be an orderly resolution, consistent with the transaction documentation, and without any need for arbitration in the courts.

"It is testament to the ILS asset class," says Sarah Demerling, Client Director, Estera. "We have watched it evolve since its infancy. Investors' level of understanding of the ILS space today is much deeper and it shows how resilient the asset class is. Investors reacted very well to the recent loss events, it was a very orderly approach and in short,



it did exactly what it is supposed to do on the 'tin'. Because of the hurricanes last year, there is always a chance you are going to incur losses. One might have thought that investors would run for the hills but the opposite was true.

"The outlook for 2018 is strong, in that sense. Pensions, SWFs are becoming more comfortable and giving a larger allocation of their portfolio to the ILS space."

This is further helped by the fact that ILS structures continue to evolve. Demerling notes that whereas before the space was dominated by heavily regulated Cat Bonds, "we now see a move towards more Cat Bond-lite structures".

'Cat Bond-lite' is a concept developed out of a desire to bring smaller sized ILS, typically less than USD50 million, to market more quickly. These securities are generally brought to the market via private placements. "It is a further commoditisation of the ILS product and a good fit for Bermuda, often making use of Bermuda's segregated accounts company capability, together with its special purpose insurer capability," adds Demerling

Bermuda is uniquely placed to support this asset class given its long-standing reputation in both the insurance world and the investment world. It has the right talent in place to support these two areas of the market in terms of legal, accounting, insurance professionals, audit, trust administration and so on. "A lot of the main players who are active in the ILS industry already have a strong presence in Bermuda and have done so for a while," confirms Taylor.

He adds that because of the experience and reputation the BSX has in the industry, it attracts a lot of ILS deals, which typically require a listing on a recognised stock exchange. At the end of 2017, USD26 billion of ILS capital was listed on the BSX.

This is helped by the fact that Bermuda's regulation has developed in a way that reflects the sophistication of the ILS market. Back in 2009, the Bermuda Monetary Authority made amendments to the Insurance Act 1978 by introducing a new class of "Special Purpose Insurer" (SPI), which enjoys a lighter touch regulatory regime.

"It was well thought out. The minimum capital requirement for an SPI is just USD1," says Demerling. Moreover, there are no investment restrictions and the operator of an SPI can waive the need to have an audit. This makes the SPI the perfect vehicle for issuing ILS.

"In addition, we have Segregated Accounts Companies (SAC's) legislation so the right structures were put in place to encourage the ILS market to flourish," says Demerling.

SACs are commonly used for a variety of insurance purposes, including rent-a-captives, life and annuity companies, transformer vehicles, as well as financial guarantee, securitisation and derivatives structures and special purpose vehicles.

One interesting trend that is beginning to emerge is the creation of a secondary market for ILS products, with some early signs that platforms are being developed to facilitate underlying derivative-type transactions. The upshot to this is that it could create more liquidity in the ILS market, as has been happening in PE secondaries over the past few years.

"Traditionally this type of instrument has been held to maturity. Now we are seeing investors wishing to move pieces of ILS from one sub-fund to another. There is a lot of talk about creating more liquidity and it will definitely take ILS into a whole new realm. It could create a whole new class of investors who don't necessarily want to hold these investments to maturity," confirms Taylor.

Demerling concludes: "Given where we are in terms of generational shift, we might also start to see more socially responsible investing coming in to the asset class." ■



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SAC platforms offer a compelling route

Interview with Anthony D'Silva

Incu Global operates a Segregated Account Company (SAC) umbrella structure in Bermuda, offering fund managers a cost-efficient route to launching a fund. Each manager has his own cell structure – effectively a sub-fund – whose assets and liabilities are ring fenced from all other cells operating on the platform.

“Each cell can issue its own shares and even though it doesn’t have Ltd, Limited or LP at the end of the name, that is in essence what each cell is; it’s its own legal entity,” explains Anthony D'Silva, owner and director of Incu Global and a former managing director and partner of a large fund administrator.

“There is much more compliance today and managers can easily feel overwhelmed. That is one reason for why platforms are and have become popular. A second reason is cost and speed of entry. Setting up an offshore fund can cost anywhere from USD25K to USD50K or higher depending on the structure and can sometimes take months to setup.

“When we set up a fund under Incu, the initial setup costs to the client are only USD5K and can be set-up and approved by the BMA in 4 to 6 weeks.”

Incu supervises the underlying fund managers, providing robust corporate governance, managing the funds compliance and risk without interfering in the investment strategy.

Although Incu works with a number of preferred service providers including Circle Partners, Wakefield Quin and Deloitte, managers are completely free to appoint their own counterparties to the fund. To get a sub-fund up and running quickly, the use of preferred parties is recommended.

D'Silva notes that his focus is on standardising all the processes and



Anthony D'Silva, owner and director of Incu Global

procedures in order to allow managers to focus on managing the fund and raising assets.

“This is why we work closely with firms like Circle Partners. The administrator plays an integral role in running a fund. They are the ones reconciling between the fund manager, the broker and the custodian, they value the portfolio, they act as transfer agency: they are the hub around which everything hinges.”

The Incu platform primarily focuses on liquid hedge fund strategies trading listed futures, options and FX. It also has managers running equity long/short and even long-only strategies. D'Silva says that the target returns are 10 to 15 per cent per annum with single digit volatility.

If and when a manager is ready to spin off the Incu platform to establish their own standalone fund, they retain a fully audited track record. There are no lock-in periods and no penalties are imposed for those managers who choose to spin off on their own.

“If a manager does well, builds a track record and attracts more investor capital, they can set up their standalone entity and then, at a specific date, there is an ‘*in specie*’ transfer,” explains D'Silva. “The investors will move across to the new fund structure, and that structure will own shares in the existing fund. Then in stage two, once all the investors have moved across, we transfer the fund’s positions across to the new entity. There’s a continuation in the structure – there’s no need to liquidate the portfolio and start all over again. Circle Partners, as administrator helps to make this process smooth and almost seamless for managers.

“It’s a well-planned, smooth transition and something we’ve done numerous times with clients.” ■

- 19 ► Decades ago one might have regarded Bermuda as a bit of an outlier but the way the world has changed, other jurisdictions have been forced to play catch up.

In Bermuda, therefore, it is very much a case of business as usual to uphold the standards of regulatory compliance and transparency.

Beacon's Aggarwal believes that with the introduction of enhanced new regulations, corporate governance standards have been strengthened over the last few years "and that companies doing business in Bermuda are much more aware of their requirements with the recognition that they must ensure appropriate mechanisms and controls are in place".

The BMA remains committed to maintaining the international integrity of the jurisdiction and will be subject to a Mutual Evaluation by the regional body of the Financial Action Task Force ('FATF') in 2018. Ahead of this, it has strengthened the AML/ATF regulatory environment in Bermuda and introduced updated Proceeds of Crime (Anti-Money Laundering (AML) and Anti-Terrorist Financing (ATF)) Regulations 2008, effective January 1, 2016.

"Bermuda has a strong and robust sanctions regime, where screening needs to take place to ensure that companies know their business and aren't unknowingly breaching sanctions," explains Ian Mutch, Consultant, Oyster Consulting. "It is a challenge for companies to perform regular sanctions screening and client due diligence themselves because they don't necessarily have the people or the skill set, or indeed the systems in place, to perform that ongoing monitoring. For that reason one of our most popular services is performing customer due diligence, enhanced due diligence and sanctions screening for our clients.

"Being a compliance specialist, even though we aren't involved in the initial fund set-up with managers we have decided to put together a new start-up service proposition: we can help connect them with legal support, with accounting support while we can provide all of the ongoing regulatory and compliance support. We are seeing an uptick in interest in this new service proposition.

"We are all from Bermuda at Oyster Consulting so we have a vested interest



in helping and supporting new clients who come to the island."

For platforms like Incu Global, it is vital to have effective oversight of, and transparency on, each sub-fund investment advisor. Not only to protect end investors by ensuring that each manager is operating their investment strategy in full compliance with the PPM, but also to protect Incu's own reputation.

D'Silva presently acts as director to nine funds. He is careful to control the number as his main priority is running the platform.

"I'm not a paper pusher. I get actively involved with the manager, giving them recommendations on best practices, how to market their fund, how to deal with due diligence, etc. I'll offer advice on hedging strategies in their portfolio as well, on occasion.

"I have my own board of directors at Incu; one of them is a funds lawyer, one has worked for UBS and Deutsche Bank in custody and fund administration and I have an investment adviser who also offers perspectives," says D'Silva.

Independent, split boards such as these are fast becoming the preferred option for institutional investors, particularly when investing directly with managers. Gone are the days of appointing members of the investment team, or even family members, as directors to the fund. That no longer cuts the mustard.

Unlike other jurisdictions, where jumbo directorships have been the source of media interest, Bermuda's more modest funds universe allows people like D'Silva to train their sights on a limited number of funds.

"I have seen a lot of changes in terms of governance, compliance and AML. There are still plenty of managers who take money from small family offices, for example, who may not mind if the manager sits on the board of directors of the fund. I think where the main push (for independent directors) is coming from is from larger institutional investors including endowments and pensions who want boards of directors to be 100 per cent independent, composed of a mix of complimentary skill sets and more importantly, to protect and focus on the interest of the investors," adds D'Silva.

Mutch says that one of the *raison d'être* at Oyster Consulting is to make things as simple as possible for clients.

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Outsourcing eases the pressure of regulatory compliance

Interview with Ian Mutch

That Bermuda continues to strengthen its regulatory regime is very much a selling point for those thinking of doing business on the island. This year, the Caribbean Financial Action Task Force (CFATF) is assessing Bermuda, with a possible onsite in September. This follows its assessment of the Cayman Islands in December 2017.

On the back of these visitations, offshore regulators, broadly speaking, have really ramped up their focus on compliance, and AML in particular, to make sure there is a robust and rigorous set of regulations in place.

"What we've seen over the last 18 months is that as regulators are increasing their focus, the industry is doing the same; not just financial services. We are seeing the same happening in non-profit organisations, real estate agents, corporate service providers and high value dealers. The Bermuda regulatory landscape, as a whole, has really improved and evolved," remarks Ian Mutch, Consultant, Oyster Consulting, a specialist professional in Risk and Compliance, with 20 years of global experience in the banking, insurance, foreign exchange, and payment solutions sectors.

Oyster Consulting is a compliance specialist firm, helping an array of financial services clients design their AML and compliance regimes and keep them ahead of the regulatory curve. Oyster's primary goal is to ensure its clients have the knowledge and tools to manage their future at a time when regulatory compliance demands have never been higher.

"We provide services from the ground up,



**Ian Mutch, Consultant at
Oyster Consulting**

writing procedures and designing controls for our clients, through to reviewing and testing whole compliance programs. We can provide training at all levels from board level all the way down to front line employees, not only on clients' expanded responsibilities in respect to current regulation but also advising them on impending or evolving regulations. That aspect of our work has proven very popular.

"For smaller organisations that don't have the bandwidth to handle the Chief Compliance Officer role or the Money Laundering Reporting Officer (MLRO) role internally, they turn to us to provide outsourcing services to support them in that capacity," explains Mutch.

Such are the reputational stakes at play that fund managers, regardless of their size, can ill afford to get on the wrong side of compliance. Bermuda has robust anti-bribery regulation that one could argue is even stronger than the UK Anti-Bribery and Corruption Act. For start-up managers in particular, knowing that they can turn to a trusted partner to help them navigate the regulatory landscape and establish basic compliance controls and protocols – whether those relate to corporate governance, AML, or any other areas of compliance – is a huge advantage.

"We help new managers wrap their heads around these compliance issues. What we tend to find is that their primary focus is on getting their business up and running, and managing the investment strategy. They don't necessarily have the bandwidth to assign resources and time to build their compliance

framework; that's why outsourcing is so popular.

"This allows us to build a relationship with the manager from the beginning and we can continue to support them as they grow and mature as an organisation.

"That said, we do also get larger established fund managers coming to us. Maybe they've had an independent review of their organisation and realise that they've got gaps in their compliance program. Indeed, one of our core services at Oyster is to do an independent review and testing of a manager's internal controls. We've found off the back of that, some companies need support to plug the gaps, while others use it as a good checks and balance exercise, using an independent party to assess their compliance stance," explains Mutch.

As investors increase the scope of their ODD assessments, the bar is being raised in terms of operational and compliance expectations. Preqin notes that 45 per cent of investors said they would remove managers from their screening programs if they demonstrate poor governance. Managers are attuned to this.

Forty per cent of managers surveyed in the recent EY 2017 Global Hedge Fund Survey said they plan to invest in automating manual processes and more than a quarter of managers (27 per cent) have, or will be making, investments in AI and robotics to strengthen their middle and back office. Moreover, a 2017 SEI survey found that 68 per cent of managers outsource their cybersecurity function to present themselves in a good light to investors.

These are all encouraging signs and demonstrate the urgency/seriousness with which managers are addressing ODD. This includes the business continuity plans and disaster recovery plans.

"Investors are requesting evidence of whether there is a good cybersecurity program in place and want some comfort that their data is not going to be compromised. This extends into business continuity where investors are asking for evidence that there are real plans in place and that they are being tested independently.

"The industry has evolved in that sense. Before they allocate to any fund management organisation, investors want

reassurances that they are not going to fail, either because there is a data leakage, because they don't meet compliance standards, because they are involved in an AML scandal, or because their BCP fails to work in the event of an emergency.

"Everyone is becoming more aware of the importance of these matters," outlines Mutch.

Oyster is able to build and develop cyber risk management frameworks for its clients. In addition, the team gives each client advice and guidance on the technical tools that would help strengthen their security posture.

Mutch confirms that it also has an outsourcing review and assessment program, which is particularly useful for clients who need to demonstrate good vendor management in the eyes of investors and regulators.

"This all links back to the strengthening of Bermuda's regulatory landscape," says Mutch. "There are now specific regulations around outsourcing and what companies need to perform in respect to outsourcing: how they manage each outsourced relationship, making sure there are controls in place and that regular meetings are held to review performance.

"That has been quite a new development over the last 12 to 18 months and a lot of companies are having to get to grips with it. They need to determine which are the most important material relationships to their fund(s) and then put the necessary controls in place to oversee those relationships."

At the end of the day, it all comes down to accountability. If there's a failure in a particular service, is that going to impact your ability to operate and provide the service to your clients?

"If the answer is 'Yes', then you have to put some robust controls in place to make sure that the level of service is upheld and you have a contingency plan," says Mutch.

It is good for the industry the everyone involved is taking compliance much more seriously.

"In support of the increased compliance focus, we continue to help our clients with the design and implementation of best-in-class policies, processes and controls as well as providing insight and training into the evolving regulatory and compliance environment," concludes Mutch. ■



25 ► “It’s compliance without the complexity,” he states. “We’re here to help and provide guidance to new start-ups right the way through to mature organisations.

“Every jurisdiction is different but Bermuda has all of the necessary regulations in place to help support organisations and ensure that they meet global standards. That is important because it means that clients, or investors, will be happy doing business with Bermuda-based entities. Bermuda recognises it needs a strong regulatory compliance framework to uphold its world-class reputation.”

ILS market evolution

Aside from regulatory and compliance developments, one area of continued evolution and growth is Bermuda’s ILS fund market, with 2017 proving to be another record year for the Bermuda Stock Exchange, in respect of ILS listings (see Q&A article with BSX in this report).

Bermuda’s ILS story is one that underscores Bermuda’s entrepreneurial and innovative spirit.

As it became evident that a shift began to occur in the manner in which the reinsurance industry sought/received capital, it was clear that an opportunity existed for Bermuda to leverage its depth of experience in the market and provide a commercial solution that met international standards.

“Bermuda’s success in this space is a testament to the hard-work and dedication of many people from many different organisations (some of which are competitors) to quickly build a solid platform upon which this asset class got traction and momentum,” comments Greg Wojciechowski, President and Chief Executive Officer of BSX.

Sherman Taylor is Associate Director at Estera, which over the years has become

Bermuda’s leading administrator to ILS vehicles. He notes that the types of risk that underlie ILS products have shifted away from relating purely to catastrophe events.

“We’ve started to see more discussion about things such as cyber risk and operational risk in the ILS market; indeed, there was a CHF220 million Cat Bond deal in 2016 with operational risk featuring as the underlying risk and this year, a new ILS product has come to market where financial guarantee risks are being transferred to the capital markets. I expect to see more of these new types of ILS products emerge as the ILS market continues to develop.

“Looking at the trends in own book of business, we’ve already got a sense that 2018 will match, and very likely exceed 2017,” remarks Taylor.

At Conyers Dill, Griffiths believes that many of the changes made to Bermuda’s funds regulation in 2008 were “well overdue” and in need of an overhaul to improve things such as speed to market. She says that introducing the category of registered but not regulated fund products (Exempted Funds) was a positive development given that most ILS funds fall into that category.

In regards to fund NAV calculations for ILS funds, there are any nuances that investors should be aware of compared to traditional hedge funds. ILS funds, in many cases, are investing in private transactions, which means administrators are dealing with level 3 assets in terms of valuation. As Brian Desmond, CSO and EVP Head of Fund Services at Horseshoe Group, comments: “The importance of administrator oversight when funds own hard to value assets cannot be overstated. Investors gain a lot of comfort when they know the fund they are investing substantial money in, is administered by specialists in the valuation of those hard to value assets.

“In terms of valuation, Horseshoe are well equipped to verify that our clients’ premium earnings are consistent with their portfolio’s underlying, potentially seasonal, exposure and are also well qualified to test the assumptions our clients use in determining a loss estimate and building a buffer around that estimate for additional uncertainty.”

Another difference from traditional hedge funds relates to side pocketing. When investors in traditional hedge funds

Good momentum as listings grow year-on-year

Q&A with Greg Wojciechowski

How would you summarise 2017 from a business growth perspective for BSX?

Strong global market conditions contributed to positive listing activity across most sectors of the BSX's business. Listing activity was particularly strong in international debt and insurance linked securities (ILS), both of which reached record levels.

International debt listings grew to 167 securities, up 44 per cent from 116 the previous year with their nominal value growing from USD2.0 billion to USD4.6 billion.

New ILS listings totalled 103 securities for the year with a nominal value of USD11.54 billion. This represents growth of 69 per cent in terms of the number of new securities listed in the year and an 87 per cent growth in the nominal value. At the year-end, the total number of ILS securities listed stood at 227 securities with a total nominal value of USD25.99 billion. 2017 showed a record in ILS both globally and for the BSX.

The Exchange also listed four new collective investment vehicles, three new equities and 20 new derivatives. A further nine subsequent issues were also processed by the BSX.

As of year-end there was a total of 865 listed securities on the BSX, compared to 753 in 2016.

What was demand like for new ILS listings and what trends have you seen in this area?

The BSX is particularly proud of its position as the global leader in the listing of ILS vehicles. Not only are Bermuda vehicles listed on the BSX but structures from Ireland,



Greg Wojciechowski,
President and CEO at Bermuda
Stock Exchange

the Cayman Islands are listed as well. The BSX looks forward to providing a listing platform for UK-based ILS vehicles as that market gains traction.

Currently, over 80 per cent of ILS issued globally are listed on the BSX.

The BSX is one component of the Bermuda's value proposition in respect of the global reinsurance and ILS sector. There are very few jurisdictions that can offer the full array of services required to support this exciting and developing asset class as Bermuda does.

Aside from ILS listings, what trends have you seen over the last 12 months in respect of collective investment fund vehicles?

Bermuda is well known and respected in the global asset management space. It is home to nearly 800 funds with an aggregate AUM of USD160 billion.

The well-established regulatory and commercial platform that has serviced the global asset management industry from Bermuda for years continues to evolve in an entrepreneurial fashion and is now very active in servicing dedicated fund structures whose focus is investing in ILS. In fact, Bermuda's fund growth over the last several years has been tied to the ILS space. The island is home to some of the world's largest ILS asset managers and earliest adopters.

The BSX reflects this trend and currently has over 300 collective investment fund structures listed representing a wide array of global investment strategies.

How important is it for an electronic offshore exchange like BSX to have a core platform and regulatory framework in place, in order to support innovative new products and strategies?

It is crucially important. For an exchange to be considered a platform able to support global capital market needs, it must first be able to provide key domestic capital market services to its domestic economy.

Simply put, the exchange must have the infrastructure in place to support all aspects of exchange operations if it wants to be in a position to provide capital market support in new products and market strategies to the international marketplace.

In my opinion, in order to be called an exchange, the entity must do the fundamental things that exchanges worldwide do on a daily basis for their domestic market. This includes providing an open, accessible and regulated marketplace for investors to buy and sell securities. The platform must provide the ability for price discovery for secondary market transactions. In addition, it must support the trading mechanism and crucial post-trade services such as clearing, settlement and depository services.

There are companies that provide a subset of exchange services, such as listing support but these platforms have yet to transition to an exchange structure that provides the full suite of expected exchange services as noted above.

The BSX has been operating a fully developed electronic trading clearing and settlement platform for many years. The platform plays a critical role in Bermuda's domestic economy while leveraging its solid and globally recognised stock exchange structure to support new and evolving business both locally and from international sources.

Following this, are you seeing interest among global fund managers and entrepreneurs in developing cryptocurrency strategies and ICOs?

Yes indeed. The Bermuda Government has stated its intention to develop a cyber/crypto and blockchain technology strategy for the country. That said, the strategy is likely to

be carefully designed to support a specific segment and customer demographic and very much in line with Bermuda's careful yet commercial approach to business.

The BSX is involved in discussions surrounding this space and is staying broadminded in respect of supporting the space and various products. This is a segment that is attracting significant attention from global regulators, central banks and governments in an attempt to ensure that an appropriate and functional framework exists, and all participants operate in an open, regulated and fully transparent manner.

In respect of the BSX, our entry into the crypto asset space will be carefully calibrated, measured and deliberate.

How big an opportunity does BSX regard this burgeoning asset class and what are the risks that you, as a leading offshore exchange, need to be mindful of?

The BSX view, I believe, is in alignment with most of the world's exchange operators in that crypto/cyber is viewed as an opportunity but there are challenges and specifics that will need to be addressed to attract greater institutional participation without which could stifle the growth of this segment.

Global exchange operators are actively analysing the space to determine the intersection between traditional markets and this new marketplace structure.

How has 2018 been thus far for the exchange and what are you hoping the year will bring, from your vantage point as President and CEO?

Thus far, we continue to see the momentum that developed in 2017 in the ILS and international fixed income space strengthen. As more global insurers and reinsurers view alternative capital as 'here to stay', and investors continue to find the asset class attractive, we anticipate another strong year for ILS in 2018.

The BSX will continue to offer the domestic and global capital markets exchange support for the listing and trading of its securities while keeping a watchful eye on new opportunities in existing and new lines of business. ■

Corporate governance awareness continues

Interview with Nitin Aggarwal

The Beacon Group is an independent group of companies providing management, consulting, administration, accounting and other related services to offshore and domestic hedge funds and other international entities. It is licensed by the Bermuda Monetary Authority to provide corporate secretarial services, part of which involves offering advice to promoters and fund managers on corporate governance best practices.

That Beacon is also licensed to offer fund administration services can be beneficial.

As Nitin Aggarwal, Chairman of Beacon, explains: "Our many years of knowledge and experience as fund administrators with different investment strategies and asset classes allows us to leverage that skill when we provide directorship services and related advisory services to the same client.

"We are aware of the challenges facing our industry and are constantly kept up to date with the latest regulatory requirements in the jurisdictions we do business in and as such feel that we add a lot of value to any Boards we sit on. In particular, as a result of our knowledge and experience as a professional administrator, we are very aware of the potential risks associated with an investment fund such as compliance with AML/ATF legislation."

Beacon serves a wide variety of clients both in Hedge funds and Private Equity, with a particular speciality for funds listed on exchanges requiring daily or weekly liquidity.

"We serve various types of structures including segregated portfolio companies, master-feeders, multi-class and side pockets, to name a few," confirms Aggarwal. "We cater to a wide range of client sizes and are particularly attractive to investment managers who are launching new funds as we appreciate the cost sensitivity of new startups.



Nitin Aggarwal, Chairman of Beacon

"We are also active in the area of corporate administration, providing clients with registered offices and annual corporate services which are complementary to our fund administration services."

From a corporate governance perspective, The Companies Act 1981 (as amended) together with applicable common law rules is the primary source of corporate governance that Bermuda companies are subject to. Taken with specific requirements addressed in constitutional documents, shareholders or investment agreements, will determine the fabric of corporate governance standards.

As regards investment business and fund administration, various Acts such as the Investment Funds Act 2006 and the Corporate Service Provider Business Act 2012 apply to licensed entities setting out principles of corporate governance. All such entities are required to implement adequate corporate governance policies and procedures.

The regulatory landscape has changed drastically in recent years, requiring fund directors to keep pace and stay on top of the details pertaining to the AIFM Directive, FATCA, Common Reporting Standards, not to mention the oversight of a fund's cybersecurity controls and BCP/Disaster Recovery plans.

Aggarwal confirms that Beacon generally only takes on a directorship if it is already providing that client with administration services: "When asked to provide non-executive directorship services, Beacon takes a risk-based approach ensuring that the fund is in full compliance with the latest regulations. We have become more selective before we provide directorship services, looking to satisfy ourselves that the FATCA Responsible Officer, for example, has the necessary skills and experience to fulfil the role." ■

29 ► hear about side pocketing, they generally associate the concept with poor performance and some of the emergency measures that funds had to take in dealing with the market meltdown in 2008/2009. However, in the ILS market, due to the uncertainty around the magnitude of losses and a potentially protracted settlement period associated with a catastrophic event, the creation of side pockets can be a regular occurrence. The creation of the side pocket allows for continued fair and orderly subscriptions and redemptions after a significant event.

"A third area where ILS funds can be different is in their liquidity/redemption provisions," adds Desmond. "Due to the hybrid mix of liquid and illiquid securities that ILS funds may own, ILS funds have come up with some innovative ways to deal with redemptions such as using the concept of slow pay shares. In the process, a slow pay series or class is created for the relevant investor, and the investor's share of the in-force contracts as of the redemption date are transferred to the slow pay share class and the investor is paid funds as the portfolio contracts reach maturity."

Blockchain in ILS market

One catalyst that could lead to further growth in Bermuda's ILS market is the role of technology, in particular blockchain technology, as the markets focus on building as much efficiency into the process as possible. "We recognise that this is likely to be achieved by automation in some form or another," explains Sarah Demerling, Client Director, Estera.

"The Bermuda Government is exploring ways of introducing blockchain technology into the jurisdiction in such a way that will capitalise on transactional efficiencies without sacrificing the integrity and security of the Bermuda marketplace. For example, a digital ledger could be used for record keeping and AML purposes, and to create more transparency relevant parties could easily see the entire history of an ILS instrument.

"We would certainly embrace the new technology once the proper controls and regulations are in place."

The road ahead

As alluded to earlier, Bermuda is already an attractive jurisdiction with a blue-chip



reputation. This is in part because of a well-respected regulator, a fully electronic offshore Securities Exchange, a wealth of talent and a leader on tax transparency and cooperation with the OECD, Financial Action Task Force, and G20.

Asked what further developments need to be made, Beacon's Aggarwal opines: "We believe that with a more collaborative approach, where government and regulators work closely with fund administrators, we can achieve greater speed to market and better marketing initiatives to convince the promoters of business to offshore jurisdictions that Bermuda is, indeed, a world class jurisdiction to do business in."

Certainly addressing some of the shortfalls, in terms of creating a product that has good speed to market for established and emerging managers, was a positive step forward for the island, in terms of giving it more credibility. The new exempted funds class requires filing with the BMA rather than having to go through an approval process.

"Covering that off, I think, met an important need for managers," says West. In her view, one of the issues that has yet to be fully addressed is simply for Bermuda to do a better job of getting its message out to the market. Having people think of Bermuda as a viable choice and having the investor community recognise the quality of the jurisdiction.

"Overcoming the prevailing trends and what has become 'conventional wisdom' in terms of jurisdictional choice is probably the biggest challenge right now. I do think there's a bit of a stumbling block in the sense that, with so much compliance and so much being asked of managers by investors in the ODD process, if they can avoid having to answer those additional questions then they will.

"But we are also confident that managers who are open to what Bermuda has to offer may find that the choice pays off. We have a real market on the ground here and we are easily accessible from major onshore financial centres of New York and London.

"Bermuda is on the right path. We continue to do the right things and my expectation is that more managers, over time, will pay closer attention to the advantages of Bermuda and the stability it can offer, as they look to establish funds," concludes West. ■