

Article

BVI Hedge Fund Products

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Incubator Funds and Approved (Friends and Family) Funds

With a strong desire to attract start up hedge funds and their managers, the BVI Financial Services Commission (FSC) introduced regulations to significantly ease the process to establish incubator funds (designed for managers wanting to establish a track record on a cost effective basis) and approved funds (designed for a small number of investors such as friends and family). For funds which qualify, these fund categories substantially reduce the time and costs of establishing a hedge fund. When coupled with the approved manager regime introduced in 2012, the BVI is an extremely attractive jurisdiction for start-up funds and their managers.

Incubator Fund

An incubator fund is a low cost hedge fund vehicle which allows a manager to establish a start-up hedge fund on a cost effective basis. With the increased regulatory burden on established hedge funds, the costs for a manager to launch a new fund can be significant. The incubator fund is designed to overcome this burden by allowing the manager to launch a fund with less onerous regulations.

The benefit of an incubator fund is that it does not require an offering memorandum, licenced investment manager, administrator, custodian or auditor. Rather, investors must only be provided with a written description of the investment strategy, and a written outline of the risks including the risk of investing in an incubator fund.

Otherwise, an incubator fund may only have 20 investors and its net assets cannot exceed US\$20 million. Its minimum investment must be US\$20,000 or its equivalent in another currency. Further, an incubator fund can only exist as an incubator fund for two years before it must convert to a private or professional fund, or an approved fund (discussed below), convert to closed-end fund or be wound-up. This two year period can be extended by one year.

As such, the incubator fund is designed to be a start-up fund for those managers who want to keep costs in line until they have a track record to attract sufficient subscriptions to make the fund viable for the long term.

Approved Fund

The approved fund is a low cost hedge fund vehicle which allows a manager to bring together a small number of investors (such as friends and family) on a cost effective basis. The fund is designed to avoid the regulatory burden when establishing a small fund.

An approved fund may have up to 20 investors and net assets of up to US\$100 million. There is no term limit for an approved fund and no minimum investment. An approved fund is required to have an administrator (unlike an incubator fund) but is not required to have an offering memorandum, licenced investment manager, custodian or auditor. Investors must be provided with a written description of the investment strategy, and a written outline of the risks including the risk of investing in an approved fund. The approved fund is ideally suited to managers wanting a cost effective vehicle for a small group of investors.

Other Common Requirements

In addition to the foregoing, incubator funds and approved funds benefit from and are subject to the following:

- A fund may commence business two clear business days after submitting a completed application.
- A fund must have two directors, one of whom must be an individual, and whose resume will need to be submitted to the FSC at the time of application. As well, the fund will need an authorized representative in the BVI.

- An incubator fund must submit semi-annual returns to the FSC confirming its continuing eligibility as an incubator fund. Both types of funds must submit annual returns as well as annual financial statements, although these need not be audited.
- While the fund will not receive a licence, it may obtain a certificate evidencing its status as an incubator fund or approved fund.
- An incubator fund or approved fund may at any time convert into a private or professional fund, and an incubator fund may convert into an approved fund.
- In the event a fund exceeds the threshold on net assets or number of investors as set out above over two consecutive months, the fund must notify the FSC within seven days, and (i) submit an application to convert into a

private or professional fund, or into an approved fund in the case of an incubator fund, (ii) convert the fund into a closed-end fund or (iii) commence liquidating the fund.

Conclusion

When coupled with the approved manager regime ([click here](#) for more information), the BVI is the jurisdiction of choice for new managers and for start-up hedge funds. The BVI has always been a responsive cost effective jurisdiction, and these products are continuing examples of why the BVI is a leading hedge fund jurisdiction.

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