



Bermuda: a Strong Choice for Private Equity Funds

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Bermuda's flexibility and ease of use for the creation and administration of investment funds is well recognised. As one of the world's leading offshore jurisdictions, it is a premier domicile for private equity groups. Neil Henderson of Conyers' Bermuda office and Peter Ch'ng of Conyers' Hong Kong office discuss the advantages of Bermuda for PE funds in traditional sponsor jurisdictions as well as new markets in Asia.

How popular is Bermuda as a domicile for PE funds?

NH: Bermuda has been a top choice for PE funds for many years. The figures speak for themselves – almost all of top US and European Private Equity (PE) groups have either domiciled structures in Bermuda or have interests in Bermuda funds.

PC: From an Asian perspective, it is surprising given Bermuda's lineage as a premier financial offshore centre that it has not made more of an impact in the private equity or fund management industry in Asia. Bermuda's reputation has traditionally attracted blue-chip PE sponsors from North America and Europe. With recent changes to its limited partnership laws and the introduction of limited liability companies (LLCs) as well as the lowering of government fees in line with competing jurisdictions, Bermuda is in some ways a hidden treasure awaiting greater discovery in Asia.

NH: Bermuda has demonstrated its commitment to developing the PE space. For instance, industry has partnered with the Bermuda government on a number of legislative initiatives in recent years to keep the PE product competitive while the Bermuda Business Development Agency (BDA) offers a 'concierge service' to new businesses intending to invest in Bermuda. The BDA serves as a primary point of contact to help businesses with their legal and regulatory obligations, liaising with the BMA and making introductions to key contacts in the Bermuda business community.

What form of vehicle is typically used for Bermuda PE funds?

PC: A Bermuda exempted limited partnership is comprised of at least one general partner (usually a Bermuda exempted company or LLC) and at least one limited partner. Although exempted limited partnerships are typical, there are other options to consider, depending on the type of investors targeted and the investment approach. Bermuda LLCs, segregated accounts companies and unit trusts may be more appropriate in certain circumstances and markets. They are all flexible structures and easy to set up. For example, unit trusts are historically attractive to Asia-based sponsors and investors, owing to prevalence and "pass through" tax transparency treatment at the fund and investor level.

NH: As Peter noted, in most cases Bermuda PE funds are formed as close-ended exempted limited partnerships. While Bermuda limited partnership law has its roots in English partnership legislation, it is also directly comparable with its Delaware counterpart, so the typical structure with a limited partnership and a corporate general partner is particularly popular with private equity fund sponsors in the United States targeting global investors.

Looking at other vehicles, what are the advantages of a segregated account company?

PC: Bermuda segregated account companies (SACs) may be employed to pursue multi-pronged investment strategies where assets and liabilities of one account are ring-fenced from those of other segregated accounts of the same company.

SACs are attractive because they can achieve such separation within one vehicle and so avoid the expense of incorporating separate companies in order to achieve the same effect. They can be used to establish a number of single investor portfolios designed to meet an investor's specific needs and without having to disclose the details of such portfolios to other investors in the SAC. Admittedly, these structures are much less common, perhaps partly because of the uncertainty of tax treatment given the relative novelty of the structures in the industry.

Are Bermuda PE funds or their non-resident investors liable for tax?

NH: There is no Bermuda income, profits or capital gains tax payable by an exempted Bermuda partnership or its partners, an exempted Bermuda company or its shareholders, or a Bermuda unit trust or its unit-holders. Likewise, non-Bermuda residents are not subject to any profits tax, withholding tax, capital gains tax, capital transfer tax, estate duty or inheritance tax. Private equity vehicles will usually obtain, for a minimal fee, a legally binding assurance from Bermuda's Minister of Finance confirming that in the event that any legislation is enacted in Bermuda imposing income, profits or capital gains taxes, it will not be applicable to the entity until 31 March 2035.

How easy is it to form a Bermuda PE fund vehicle?

NH: The partnership formation and company incorporation process in Bermuda is among the most streamlined of any jurisdiction, and there is a transparent pricing structure with one standard government incorporation fee. Partnerships, LLCs and companies are all typically formed or incorporated within one to two business days after completion of beneficial ownerships KYC.

PC: The formation and government fees for a Bermuda limited partnership are competitive with other offshore jurisdictions.

How easy is it to convert an existing fund to a Bermuda vehicle, or to redomicile?

PC: A notable advantage of a Bermuda vehicle is flexibility of conversion and ease of redomiciling. A typical closed-ended PE vehicle will generally not require Bermuda-specific modifications when replicating entities formed in other jurisdictions. The limited partnership agreement, bye-laws or trust deeds enjoy a high degree of freedom and flexibility in dealing with these matters and the 2015 partnership law amendments allow a partnership established in certain other jurisdictions outside Bermuda to be registered in Bermuda as an exempted limited partnership by way of continuation from those jurisdictions, and vice versa. Again, this may prove useful for future restructuring to meet any unforeseen legal, regulatory or tax changes.

How onerous are the approval and regulatory requirements?

NH: Bermuda's regulatory regime for investment funds is carefully framed to provide protection to investors while ensuring fund managers are not unduly burdened with onerous requirements. The Bermuda Monetary Authority (BMA) reviews and approves applications to form limited partnerships and LLCs and to incorporate companies, but closed-ended PE funds are outside the scope of Bermuda's *Investment Funds Act 2006* and, as such, are not regulated by the BMA. This is the case whether or not there is significant investment activity by the private equity fund in Bermuda.

PC: Generally, once the fund has been incorporated and the partners are in place, the BMA will have little direct involvement with a Bermuda private equity fund. No approval of the BMA is required for the issuance or transfer of limited partnership interests or units of a unit trust, as long as they do not carry voting rights. There are no Bermuda rules or regulations that would affect the structuring of the sponsor's compensation or profit-sharing arrangements with respect to the fund. The fund will have a free hand to negotiate these arrangements in the limited partnership agreement. Being unregulated, there are no prescribed local manager, custodian or administrator requirements in respect of the fund.

What are the requirements with regards to local presence?

PC: Every Bermuda exempted limited partnership, LLC and company is required to have a registered office in Bermuda, which cannot just be a post office box. A 'resident representative' in Bermuda may also be required. Generally, a locally based corporate administrator fulfils these roles.

NH: The register of limited partners of the fund is not open to public inspection, only to limited partners of the same fund. This degree of confidentiality is greatly valued by many investors.

How has the relationship between general partners and limited partners evolved in recent years and what effect is this having?

PC: Limited partner investors are increasingly flexing their muscle and demanding greater control and involvement in their invested vehicle without risking their limited liability status. Typically, the limited partners are not liable for the debts of the partnership beyond the amounts they have agreed to contribute as long as they do not participate in the management of the partnership. The 2015 amendments extended the statutory 'safe harbour' exceptions as to what is deemed to be 'management'. Particularly helpful safe harbour provisions include that a limited partner will not be deemed to be engaged in management by reason only of making decisions on investments; consulting or advising the general partner with respect to the business of the limited partnership; or serving on the board or committee of the partnership, a general partner, the limited partners, or any entity in which the limited partner has an interest.

NH: As Peter says, not all PE structures are funded by passive investors. The safe harbour extensions were introduced in response to industry demand and are particularly helpful to significant investors who want certainty that taking part in active advisory functions will not result in their limited liability being compromised.

What are the particular benefits of a Bermuda law partnership?

NH: Bermuda's partnership law received significant updates 2015 and 2016 in response to industry requests for specific investor and sponsor-friendly changes. The amendments included a new streamlined charge registration process. Now, any person interested in a charge on the assets of a partnership with separate legal personality may apply to have that charge registered at the Bermuda Registrar of Companies. On registrations, to the extent that Bermuda law governs the priority of the relevant security, such security will have priority over any unregistered charges, and over any subsequently registered charges, in respect of the assets which are the subject of the security. This innovation has been of particular interest to those clients looking to use offshore partnership in transactions involving secured financing.

PC: Bermuda partnerships may elect to have separate legal personality, which distinguishes Bermuda from many other offshore jurisdictions. Having separate legal personality ensures continuity of the partnership despite changes in the composition of the partners. While the partners may agree among themselves that the partnership business may continue where there is a change of partners (for example, the transfer of a partnership interest or addition of a new partner) this does not necessarily bind third parties. This is particularly relevant in respect of a partnership's entry into loan agreements, giving security or charges, and participating in master derivative contracts where there are special requirements concerning counterparty mutuality in set-off and netting of trades and transactions. Having corporate features may also lend itself to improved tax treatment in certain jurisdictions.

NH: Another benefit of a Bermuda exempted limited partnership with separate legal personality is that it may convert to an exempted company or limited liability company (LLC), or from either of these entities back to a limited partnership with legal personality. This has proved useful where the fund needs to restructure to meet a future unforeseen legal or regulatory change.

PC: A feature that has proven attractive to private equity promoters is that there is no requirement that the general partner of a Bermuda limited partnership be an entity formed in Bermuda or, for a non-Bermuda entity, that it be registered in Bermuda. The general partner of a Bermuda limited partnership could be a Delaware or even a Hong Kong company operating outside of Bermuda.

What trends have you seen recently with regards to PE fund structures in Bermuda and what do you expect for the future?

NH: The single biggest change to PE fund structures in the last few years is the introduction of LLCs. We are seeing Bermuda LLCs used increasingly as general partners and as asset holding subsidiaries of funds, and even as funds themselves. The central provisions of Bermuda's LLC legislation were closely modelled on the corresponding provisions in Delaware law, so that Bermuda LLCs look, feel and operate much like Delaware LLCs. Bermuda LLCs, like their Delaware counterparts, are extremely flexible and simple to operate. US counsel and fund sponsors know what they are getting with Bermuda LLCs with the result that they have been incorporated very quickly into Bermuda's fund structures.

PC: As for the future, close-ended PE funds form the majority of new funds in Bermuda. This has been the trend for a few years now and we expect it to continue. Who knows, perhaps we could even expect to see the use of PE fund vehicles in the ILS (insurance-linked securities) space or even in tokenized investment funds, given Bermuda's clear strengths and leadership in the reinsurance and blockchain-based digital asset/cryptocurrency industries in the future.

NH: Every sign points to established PE sponsors being happy with the refinements made to Bermuda's PE fund product. Fund groups have highlighted Bermuda's responsiveness to industry demand while continuing to enable efficient fund formations with competitive and transparent pricing structures.

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