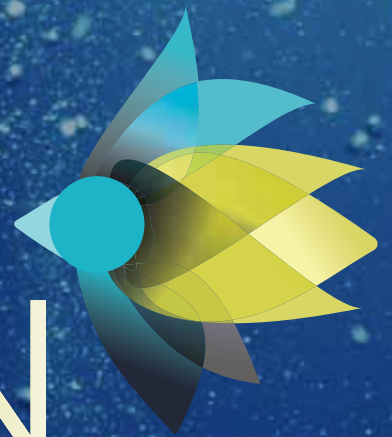


# ICON



A Guide to the Bahamas  
Investment Condominium





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# Foreword

## **The Hon. L. Ryan Pinder, M.P., Minister of Financial Services**

“ Welcome to a place that investors came to first  
that lawmakers made safe  
A sovereign nation in the heart of the Americas  
The nearest by sea or air  
Where nature roams unfettered  
Upon a crystal ocean of possibility  
Where opportunity ripens  
Under tropical skies ”

The preceding poem encapsulates the history, stability and success of The Bahamas as an ideal choice for international business and financial services and the Ministry of Financial Services of The Bahamas provides the policy directive to help sustain and grow that value proposition for the benefit of investors, clients, residents and, indeed, Bahamians. That value proposition can be further summed up in three words: stability, skill and sovereignty. These are of increasing importance in a time of near transformative unrest in economic markets, political risk in countries near and far, and the corresponding erosion of trust in governments, regulators and institutions.

The ICON is an example of The Bahamas' consistency and commitment with respect to its clients and is indicative not only of where The Bahamas is positioned now in the investment funds sector, but also of its aspirations to be the preeminent hub for funds and asset management to the Americas and beyond. That aim is furthered by the measures we've taken to ensure that the regulatory environment meets international norms and standards while retaining where possible a flexible and risk-based approach to the regulation of investment funds.

The ICON is a product of the collaborative and progressive approach to the development of new legislation in The Bahamas. With the help of the Association of International Banks and Trust Companies in The Bahamas, the Bahamas Financial Services Board and our many Brazilian advisors and partners, we have produced a sterling example of the kind of innovation that has been the touchstone of The Bahamas brand for some 90 years.

# Foreword

## **Antoinette Russell, Chairwoman of AIBT**

The Association of International Banks and Trust Companies in The Bahamas (AIBT) is pleased to partner with the Bahamas Financial Services Board and the Ministry of Financial Services in respect of this guide. AIBT has been in existence for almost 40 years and is representative of the deep ties the international banking and trust sector has maintained in The Bahamas throughout its long history as a financial centre.

It is the deep financial infrastructure, including administration, banking and custody services, that makes The Bahamas as successful as it is as a hub for funds and asset management and the Board of AIBT is pleased to be a part of assisting with the development of the newest product in The Bahamas' ever-expanding toolkit.

We believe that the ICON is another example of The Bahamas' never-ending commitment to be first in class in the provision of market responsive regulated and sophisticated products, but only the latest example of it. This commitment is evident in a host of other products, including the SMART Fund, the Bahamas Executive Entity, and the Foundation. The Bahamas has shown it is skillful in the adaptation of innovative concepts for international markets and AIBT is assured that The Bahamas will continue to be the standard bearer in this regard for financial centres for years to come.

# Introduction to the ICON

**Aliya Allen, CEO & Executive Director, Bahamas Financial Services Board**

## THE BAHAMAS INVESTMENT CONDOMINIUM IS AN “ICON”

The Bahamas recently has witnessed an upward trend in investment fund registrations which is indicative of the successful niche fund business this jurisdiction has built, largely on the back of the investment fund vehicle known as the SMART Fund. Even with more institutionally focused templates like the SMART 7, SFMs have been used as a cost-effective investment fund vehicle for families, family offices, and related investors.

The SMART Fund concept was conceived in the spirit of truly risk based regulation in recognition of the fact that depending on the structure of the investment fund, the regulation could be tailored appropriately to fit the specific business case. This is justified by the cap on the number of investors that may invest in many of the templates. As a result, the regulation accommodates agreement by a small number of investors to waive the production of audited financials in favour of semi-annual performance reports. In practice, this waiver may be utilized once or not at all but the utility is there should the investment fund require it to accommodate an illiquid strategy, or the consolidation of an audit in one jurisdiction.

While the number of SMART Funds on the register grows, The Bahamas is not content to be viewed as simply a niche fund player; it has set its sights much higher, looking to expand awareness of its entire funds offering, including its well-regarded

professional fund which may be established for sophisticated investors satisfying certain net worth qualifying criteria. Brazil has become an increasingly important market for The Bahamas, the result of a consistent and dedicated focus on assisting with satisfying the sophisticated requirements of a jurisdiction whose hedge funds number in the region of 13,000. The Brazilian multi-market fund is authorized to invest up to 100% of its assets in foreign financial assets. It would not be overreaching to estimate that a large number of the existing funds licensed in The Bahamas originated to accommodate Brazilian funds, fund managers, investors and strategies.

The condominium has been a part of the Brazilian civil code for almost 90 years. Under Brazil’s civil code the condominium was the formalization of the concept of joint ownership and administration of property (in all forms) between co-owners within an unincorporated entity that looks very similar to a partnership but operates in many respects like a company. The condominium is not a legal entity separate and apart from co-owners and the administrator is empowered to act on behalf of and represent it in all matters.

As a result of further amendments, a condominium investment fund was created; this modified the original condominium concept providing that a condominium (in the



investment funds context) was a ‘pooling of funds intended for investments in a diversified portfolio composed of financial assets and other instruments available on the financial market.’

The Investment Condominium (ICON) continues The Bahamas’ commitment to bringing to market client responsive legislation with the main purpose of the Act being to provide an alternative legal structure for investment funds that is inherently familiar to those in Brazil and indeed those in countries which have similar constructs. It was this commitment to building products that benefit from cultural and legal familiarity that saw The Bahamas introduce foundations law in 2004; the ICON is an extension of this.

The ICON is the legal structure underpinning the investment fund in the same way as investment funds are legally organized as companies, exempted limited partnerships and unit trusts. The ICON’s purpose is tied to its operation as an investment fund and is defined as the contractual relationship subsisting between participants agreeing to the pooling of assets for the purpose of investing those assets collectively.

Similar to the Brazilian condominium, the ICON possesses no distinct legal personality save that for the purposes of the legislation it is able to hold assets in its name; enter into agreements in its name; and sue and be sued in its name. The lack of legal personality is addressed by the appointment of an administrator that is empowered to transact in its name, and represent and bind the ICON.

The ICON is established by the initial participants signing “governing regulations” which is the governing document of the ICON. The initial participants engage the ICON’s administrator which must be an institution that is regulated by the Securities Commission of The Bahamas as an investment fund administrator under the Investment Funds Act. The administrator will then prepare a certificate evidencing that the ICON has been established, and which contains the information specified in the schedule to the Act. This certificate subsequently is signed by the administrator and submitted along with a prescribed fee to the Registrar General for stamping.

A unique feature of the legislation is the provision for other types of entities - e.g. companies, unit trusts and exempted limited partnerships - to convert to an ICON by following a defined procedure. The Act is clear as to the effect of conversion and it is important to note that conversion does not relieve a converted entity from liabilities or obligations incurred preceding the conversion to an ICON.

The ICON demonstrates The Bahamas’ keen understanding of the regulatory environment and the needs of the clients we service. In the current climate, success for an international finance centre (IFC) depends on a host of factors but certainly one of them is the ability to develop market-responsive, compliant and innovative products. The ICON follows in the tradition of the Bahamas Executive Entity in being the first of its kind in the common law world...and that’s quite iconic indeed.



# The Road to Becoming an ICON

## The establishment of an ICON and the conversion to an ICON

There are 3 routes to becoming an ICON:-

1. Establish an ICON and then license it as an investment fund.
2. Convert an existing Bahamian International Business Company (“**IBC**”), Exempted Limited Partnership (“**ELP**”) or Unit Trust (“**UT**”) into an ICON and then license the converted ICON as an investment fund.
3. Re-domicile a foreign company or partnership to its Bahamian counterpart, convert the entity into an ICON, or in the case of a foreign trust change its governing law to that of The Bahamas, and convert it into an ICON and then license the ICON as an investment fund.

A brief overview of each of these pathways is discussed below.

### ROUTE 1: ESTABLISHING A NEW ICON

The procedure for establishing an ICON is a streamlined one. The majority of the establishment process is facilitated by the Administrator<sup>1</sup>, though the Registrar General (“**RG**”) is responsible for keeping the register of ICONs, accepting fees and reflecting changes in the register of ICONs.

In summary, the process is straightforward and efficient, in that once the name is chosen and reserved<sup>2</sup> (the name must contain the expression “**ICON**”, “**IC**” or “**investment condominium**”) and the initial participants agree and execute the Governing Regulations, the Administrator must prepare and submit the Certificate of Establishment to the RG along with the prescribed fee. Upon receipt of the Certificate of Establishment, the RG will enter the name of the ICON on the register and then stamp the Certificate of Establishment. The date of establishment of the ICON is the date of the Certificate of Establishment reflecting the date of the execution of the Governing Regulations.

<sup>1</sup> Please note that the ICON legislation does permit for a single administrator to be appointed or both a governing administrator and a general administrator. More information relating to the division of duties where both a governing administrator and general administrator are appointed can be found on pages 8-11 and 26 of this brochure. For the purposes of this section, it is assumed, unless stated otherwise, that only a single administrator has been appointed.

<sup>2</sup> The name can be reserved with the RG for 28 days.

Within 90 days of the date of establishment of the ICON it must obtain an investment fund license (and this applies to closed-end ICONs), which may be granted by the Securities Commission of The Bahamas (“**Commission**”) or the ICON’s Administrator if it holds an unrestricted investment fund administrator’s license. An ICON may be licensed by the Commission within 72 hours, if the Commission’s requirements for fast-tracked applications are met. The ICON must comply with the requirements stipulated in *The Investment Funds Act and Regulations (as amended)* (“**IFA**”) for the particular investment fund model for which it wishes to be licensed. An ICON must have Governing Regulations, which are not required to be filed with the RG but must be filed with the Securities Commission. These Governing Regulations must include the following particulars:

- name and address in The Bahamas for service of process;
- name and address of the administrator(s);
- the number and currency of participation interests;
- provisions relating to the audit<sup>3</sup>;
- provisions for dissolution;
- the number of classes and series of participation interests;
- provisions outlining the powers, preferences, rights and liabilities of participation interests;
- the manner in which material agreements may be amended;
- provisions outlining the policies and procedures for the valuation of assets;
- provisions relating to the duration of the ICON;
- provisions addressing the division of duties between the governing and general administrator (if applicable); and
- such other provisions as may be deemed necessary by the IFA<sup>4</sup>.

**ROUTE 2: CONVERSION OF AN EXISTING BAHAMIAN STRUCTURE TO AN ICON**

The Bahamian ICON legislation allows for the conversion of an existing Bahamian IBC, ELP or UT into an ICON. The conversion process is very similar to that of establishment.

In summary, once the name is chosen and reserved (following the naming conventions mentioned above), all of the directors and majority of voting shareholders, all of the general partners and majority of voting limited partners or the trustee and majority of the voting unit holders, as the case may be, approve the Articles of Conversion which must include, inter alia, the following provisions:

- Provisions detailing the basis upon which equity interests shall be converted to participation interests in the ICON along with details of any rights attaching thereto;

<sup>3</sup> Exemptions related to SMART Funds are not affected.

<sup>4</sup> Examples include investment/borrowing restrictions, dealing policy, role of the custodian/administrator, fees etc.



- Provisions for the valuation and accounting treatment of the assets and liabilities and any retained earnings upon conversion;
- The date of incorporation, continuation, registration or establishment, as the case may be, and intended date for conversion to an ICON ; and
- An annexed copy of the Governing Regulations.

Once the Articles of Conversion have been approved, the Administrator must prepare and submit to the RG within 7 days the Certificate of Conversion along with the requisite fee. The RG will enter the name of the ICON on the register and then stamp the Certificate of Conversion.

At the date of conversion, all of the assets and liabilities of the existing Bahamian structure will be vested in the ICON and the existing Bahamian structure will be struck off the register and will cease to exist without being dissolved or wound-up, as the case may be. All of the equity interests of the structure will be converted into participation interests in accordance with the Articles of Conversion. Participants remain liable for any amount unpaid on any equity interest incurred prior to conversion.

The provisions relating to licensing apply to a converted ICON as they do to a newly established ICON.

It is important to note that conversion does not relieve officers, directors, trustees or partners from liability nor does it extinguish any debt or liability of the entity/UT prior to conversion.

### **ROUTE 3: RE-DOMICILATION OF A FOREIGN ENTITY INTO AN ICON**

The final route to becoming an ICON is to re-domicile a foreign company, ELP or UT to a Bahamian IBC, ELP or UT, respectively and then convert the Bahamian structure into an ICON as provided in ‘Route 2’ above. In relation to foreign companies and ELPs the caveat is that the foreign law and constitutional documents of the company or partnership must allow for the re-domiciliation of the entity. With respect to foreign trusts, the trust instrument must include powers to (i) change the governing law of the trust to that of The Bahamas ; and (ii) vary the provisions of the trust.

### **PRESCRIBED FEES<sup>5</sup>**

The fees pertaining to the establishment/conversion of an ICON are as follows:

- Newly Formed ICON → \$350.00 (are pro-rated).
- Converted ICON → \$350.00 (are pro-rated) plus \$150.00 for the Certificate of Conversion.
- Annual Government Registration → \$350.00 (due by 30 April of each year).

<sup>5</sup> These fees are in addition to any fees levied by the Securities Commission.

# Governance and Administration of the ICON

## **The administrative structure of an ICON and appointment and qualification of the administrator**

The role and responsibility of a typical investment fund administrator is set out in the Investment Funds Act (IFA). This role is contractual in nature and an administrator's duties under the IFA includes ensuring that the operations of an investment fund are carried out in accordance with the governing documents, ensuring the preparation of audited financial statements, and ensuring the business of the fund is not being carried on in a manner that is prejudicial to investors.

One of the most important aspects of any investment fund structure is governance. Strong governance is essential for the proper realization of the fund's investment objectives and for the fair treatment of the fund's investors. Under the IFA, governance is a function and responsibility of the fund's operators, which depending on the legal structure of the fund, may be the directors, trustee or general partner.

### **CHOICE OF ADMINISTRATIVE STRUCTURE**

The ICON will change the current paradigm in that under the ICON Act and amended IFA, the responsibility for governance of the ICON is centralized in the ICON's administrator. If the ICON chooses to engage a single administrator, that administrator performs the governance role of the operator as well as the general administration role of the administrator under the IFA.

Alternatively, the ICON may split the governing and general administrator functions between two institutions called the general administrator and the governing administrator. Where the functions are split as described above, the governing administrator is the operator of the ICON under the Investment Funds Act in the same way that a director is the operator of a company, a trustee the operator of a unit trust, or a general partner the operator of a partnership under the IFA. The governing administrator's role is critical in that it is given the power to bind the ICON in all matters and it also bears a fiduciary responsibility to the ICON's participants. The inherent risk involved in occupying such a vital role in the ICON is mitigated by the right of an administrator to call upon the indemnification extended to it under the ICON Act, except where such administrator has acted in wilful default of its duties.

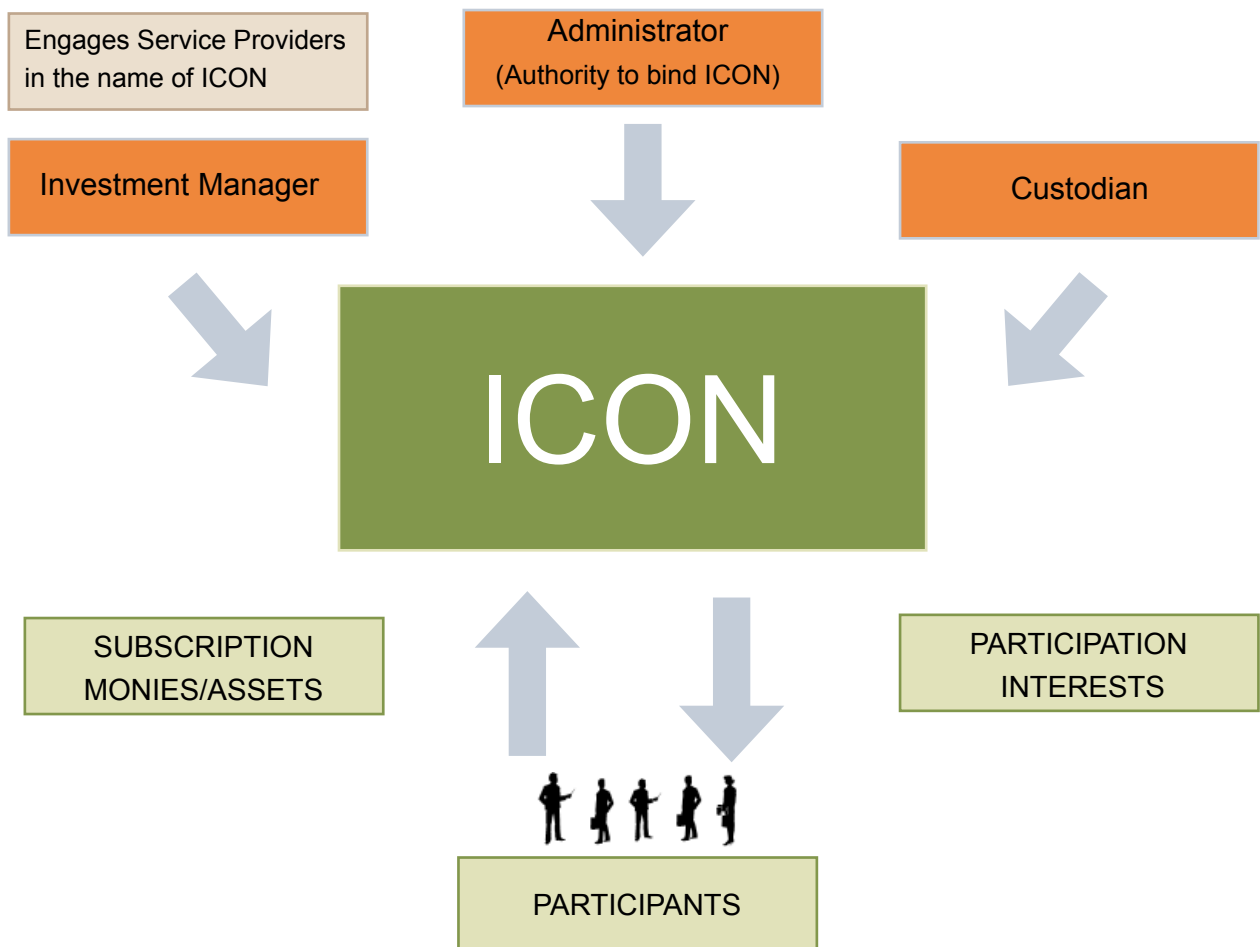
The general administrator, on the other hand, performs the duties of general administration of an investment fund with typical responsibilities of processing subscriptions, sending confirmations and providing essential and traditional activities common to fund administrators and as defined by

an administration agreement between the fund and itself. The general administrator is required to keep a record of the participants’ interests in a “Register of Participants”. The administrator is also required to keep proper books and records and provide net asset valuations. The Act allows for these administrative duties and responsibilities to be delegated to a person with appropriate expertise.

**APPOINTMENT AND QUALIFICATION OF THE ADMINISTRATOR**

The administrator(s) is appointed by the initial participants of the ICON who exercise an agreement setting out the terms upon which the ICON shall be administered. An administrator may be removed and replaced by participants entitled to vote in respect of their participation interests by way of resolution agreed or consented to by such majority as specified in the governing regulations. It is to be noted that an administrator cannot be removed unless and until a replacement administrator has agreed to act and has entered into an administration agreement.

**ICON with a Single Administrator**

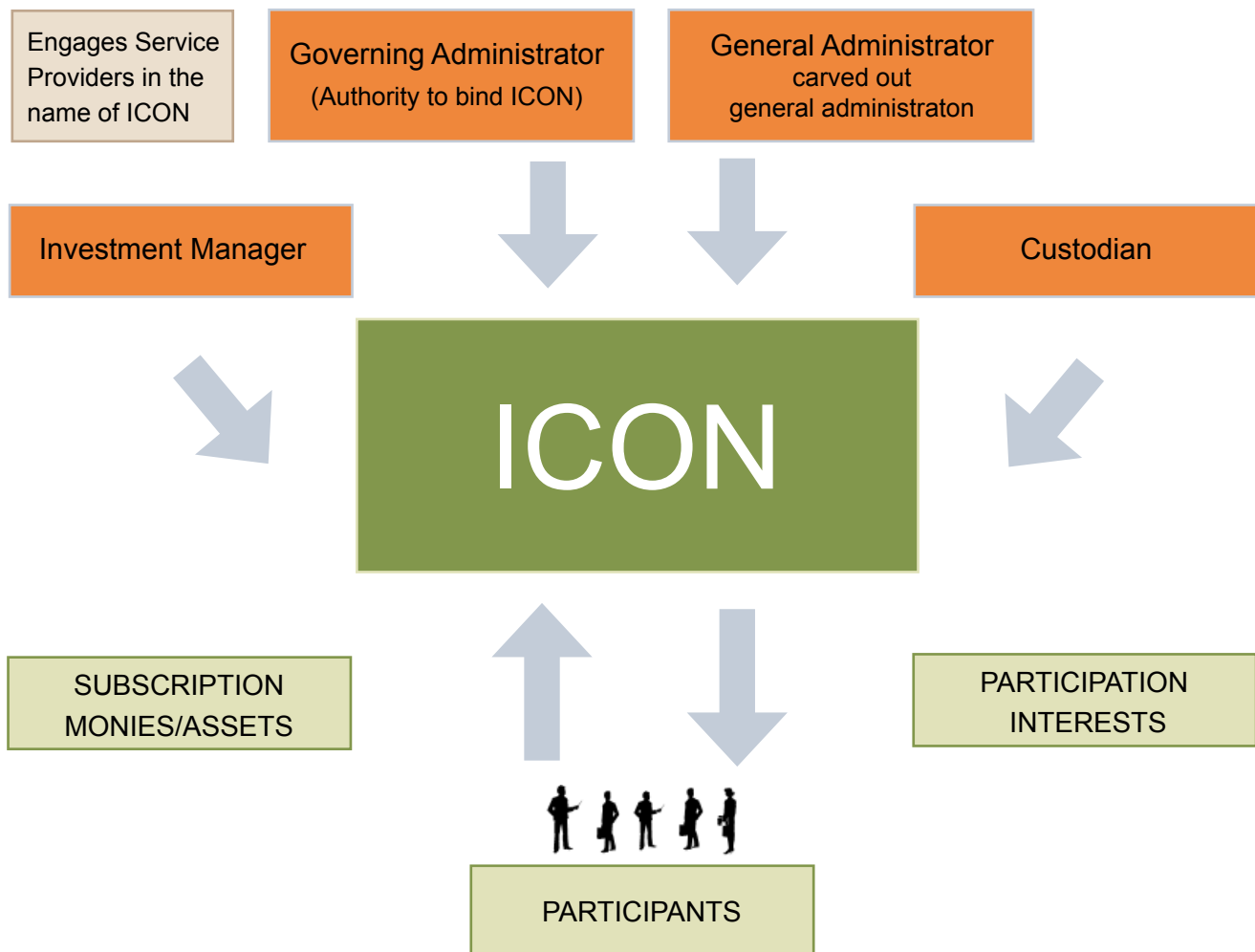




The governing administrator’s role is critical in that it is the primary interface between the fund, its services providers, and its investors. The governing administrator must be either a “financial institution” as defined in the ICON Act; or an institution licensed as a corporate services provider under the Financial and Corporate Services Providers Act (Ch.369); or an institution licensed under the Securities Industry Act (No. 10 of 2011) to deal in securities; or a bank or trust company licensed by the Central Bank of The Bahamas under the Banks and Trust Companies Regulation Act (Ch. 316); or an entity registered with or licensed by a regulatory authority in a foreign jurisdiction, which regulatory authority exercise functions that correspond to regulatory functions exercised by the Central Bank of The Bahamas or the Securities Commission of The Bahamas.

The general administrator also must be a financial institution as defined in the ICON Act. It performs the duties of administration of an investment fund with typical responsibilities.

### ICON with a Governing and a General Administrator





# The ICON-007 Fund

## The benefits of structuring your SMART Fund model 007 as an ICON

As they often say in showbiz: “good script, good location, bad actors—bad movie; good actors, good location, bad script - bad movie.” The clear logic here is that you have to match up a good script with good actors in the right location in order to make a good movie. Similar reasoning could also be extended to the investment funds business; you have to match the right legal structure in the right jurisdiction, with the right service providers, in order to create the right investment fund.

In principle, putting together the ideal combination seems simple enough. Ironically, the stark reality is that the majority of films fail to break even, and the average life span of a hedge fund is a mere thirty-six months. Notwithstanding such dire odds, both new movie and new investment fund launches are on the rise, as our art and investment cultures rapidly evolve in the midst of technological innovation and globalization.

It is the inspiring beauty of The Bahamas which gives it an allure that has been the backdrop in some of the most epic Hollywood blockbusters, such as the Jaws and James Bond Agent 007 franchises. By the same token, the sound and multifaceted Bahamian legal environment sets the scene for its dynamic financial services industry, which is driving customized investment solutions in the wealth management and asset

management sectors, particularly as it relates to the investment funds business.

Two prime examples of this sort of conscientious ingenuity in the investment funds space are outlined below: (1) the new Bahamian Investment Condominium (the “ICON”); and (2), the SMART Fund Model 007.

### The ICON

The ICON is the newest and most ground-breaking example of The Bahamas’ market-sensitivity and regulatory responsiveness. The ICON, a universal investment fund vehicle for Brazilian international investors, is a contractual relationship subsisting between investors (called participants), under which the investors agree to pool assets for the purposes of investing those assets as a collective. The structure is then licensed and fully regulated as an investment fund - as is done today using existing vehicles such as the International Business Company, the Exempted Limited Partnership, and the Unit Trust.

The ICON is simply a new offshore investment fund vehicle that can be structured and licensed as a SMART Fund, Professional Fund or Standard Fund in The Bahamas. It is not a company, not a partnership, and not a trust. It is a pooling mechanism and operating instrument for investment funds.



Although not limited to use by investors and fund managers from any one country, this new vehicle was created and tailored on the basis of Brazilian fund regulations and industry practices. The condominium has been a part of the Brazilian civil code for nearly a century and all of Brazil's approximately 13,000 funds are organized as condominiums, registered with and regulated by the Comissão de Valores Mobiliários (CVM), the Brazilian securities market regulator.

The ICON enables sophisticated Brazilian investors to access and establish offshore funds in a format to which they are already very well accustomed, where the fund administrator assumes a relatively enhanced role encompassing the traditional functions of accounting and investor relations, in addition to fund governance. Thus, a familiar legal structure can be matched up with the regulatory overlay of the Bahamian funds regime, which also has much in common with the Brazilian fund regulatory environment, considering that both countries are Members (A Signatories) of the International Organization of Securities Commissions (IOSCO). The two jurisdictions therefore share equivalent securities industry policies and standards on multiple levels. Building on this background, the Bahamian ICON offers Brazilian investors a mutually inclusive regulatory framework that is conducive to improving the efficacy of cross-border investment business. Its main advantage is that it offers an alternative way of establishing the legal nature of offshore funds, which has many implications. Since the ICON has practically the same legal profile as an onshore Brazilian condominium, and it is registered and regulated in a recognized

jurisdiction, it is potentially the ideal offshore fund vehicle for Brazilians who are looking for a way to invest overseas.

### THE SMART FUND MODEL 007

The deliberately designed SMART Fund Model 007 ("SFM 007") - the incidental name similarity to Agent 007 didn't hurt - is also known as the Super Qualified Investor Fund and was introduced in 2012 to appeal to more sophisticated investors. Industry uptake has been quite positive, with the SFM 007 representing a lion's share of all new Bahamian fund launches over the past two years. Over this short period of time, the SFM 007 has come to represent over 5% of all funds domiciled in The Bahamas and nearly 10% of all SMART Funds licensed in the jurisdiction according to data released by the Securities Commission of The Bahamas ("SCB").

This SMART Fund model serves as a regulatory wrapper for structuring private placement funds open to no more than 50 investors, each of whom is required to make a minimum initial investment of \$500,000 US dollars or the equivalent.

Some of the other features of the SFM 007 include an explicit provision for use as a single-investor fund, which makes it ideal for use as a "fund-of-one" as explained below. And similar to the other SMART Fund models, a concise term sheet is often utilized in place of the traditional long-form prospectus. In addition, waiver/deferral of the annual audit requirement is permitted, subject to unanimous investor consent. Where the waiver is in place, semi-annual financial reporting is required by the SCB.

The investment appetite of the sophisticated Brazilian investor continues to evolve. These investors are seeking to protect, diversify and sustain their wealth by expanding their search for high quality and alternative assets. This requires them to look beyond borders for asset protection and to gain access to faster growing, more stable capital markets with bigger investment capacity. In an attempt to capture these opportunities in a sustainable way, it has to be done with the right investment vehicle in order for it to be done efficiently.

Many professional asset managers and high net worth individuals are using these streamlined fund structures to better organize and consolidate their global investment portfolios, allowing for the more efficient management, reporting and control of their asset base. Among them are many sophisticated Brazilian investors who want to benefit from holding their offshore assets in a flexible and well-regulated fund, the same way they do with their onshore financial assets.

**THE ICON-007 FUND: FLEXIBLE, SOPHISTICATED AND EFFICIENT**

It is often said that the simplest approach is the best approach. However, today’s complicated cross-border environment often calls for complex solutions in order to ensure viability and safeguard against burgeoning regulatory requirements and operational risks. The opportunity to strike a balance in the private investment fund’s space is what the SFM 007, when structured as an investment condominium (the “ICON-007”), offers to sophisticated Brazilian

investors. The beauty of the ICON-007 is the flexibility to customize the fund’s operating structure in a way that efficiently provides for reduced legal and cost concerns.

Customization of a fund for asset management requires the consideration of a number of factors, including its proposed strategy, investment policy, investment restrictions, counterparties, liquidity provisions, and total expense ratio. Moreover, the most important factor from the investor’s perspective is often found to be its tax implications and how to structure the fund so that it is tax-neutral and therefore more cost-efficient.

On this basis, the SFM 007 provides for an offshore regulatory framework in several ways comparable to the onshore Brazilian multimarket super-qualified fund, which is established as a condominium and may invest up to 100% of its assets outside of Brazil, unlike other types of Brazilian funds. Currently, the minimum initial investment per investor is \$1 million Brazilian Reais, which is comparable to the minimum investment requirement for the SFM 007 (i.e. \$0.5 million US dollars). Acknowledging that such standards tend to change over time, these remain relatively high statutory thresholds shared by The Bahamas and Brazil for qualifying sophisticated investors. They are generally considered to be institutional investors, and wealthy individuals who invest like institutional investors do, and who also typically are referred to as professional or qualified investors.



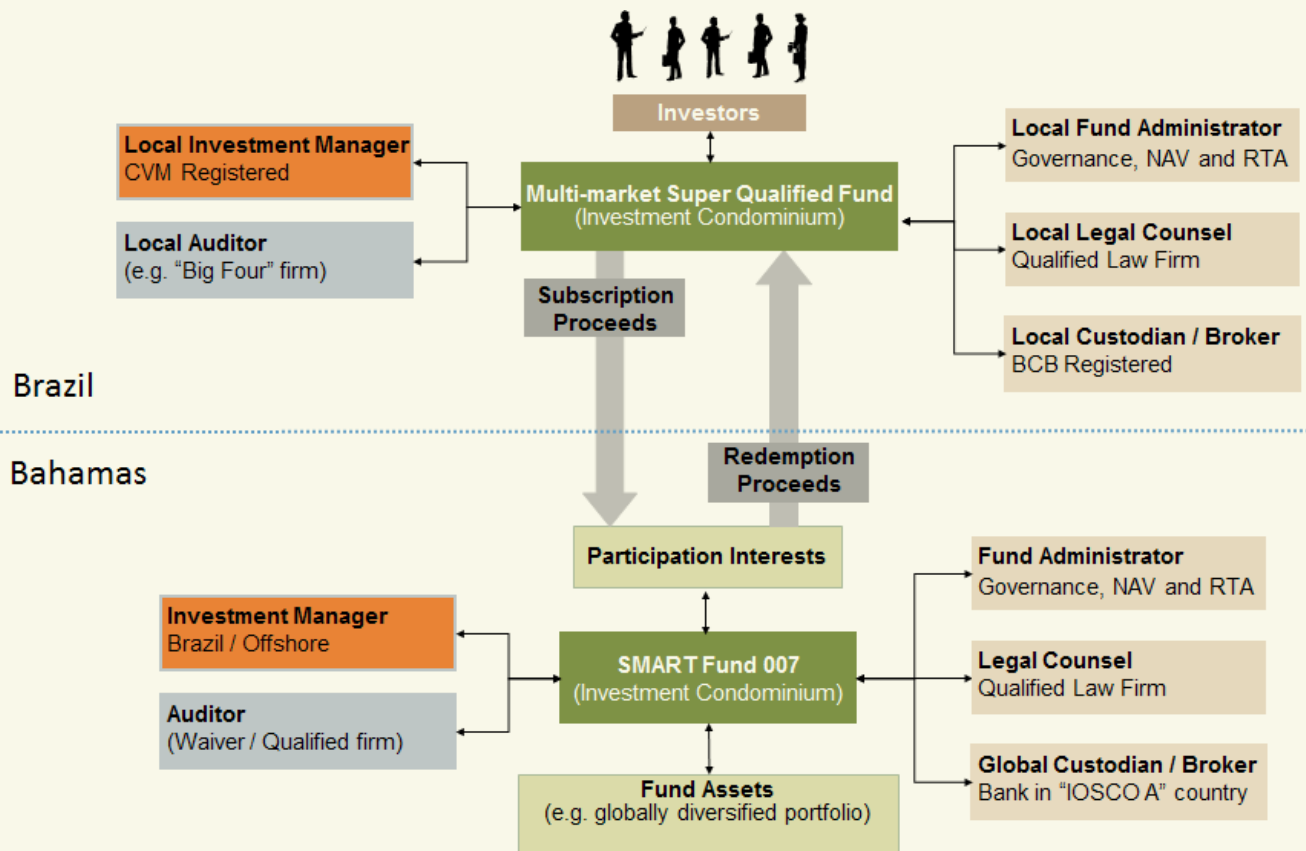
Brazilian funds can either open a foreign account directly, or the fund may open an offshore fund to hold its global investments. This dedicated offshore fund in the structure is known in the funds industry as a “fund-of-one”, as outlined in Example 1.

**(Example 1) Brazilian-Offshore Fund-of-One**

A fund-of-one is an investment structure that has become popular mainly in the fund-of-funds world, in which the investor is the sole investor in a fund. It is what it sounds like, an investment vehicle with only one investor. It can also be thought of as a hybrid investment vehicle for

high net worth investors somewhere between separately managed accounts and mutual fund vehicles. In this case, as illustrated in Fig. 1 the Multi-market Brazilian super qualified investor fund is the sole investor in the ICON-007.

**Fig. 1: Brazilian-Offshore Fund-of-One**





In its approach to offshore financial markets, the Brazilian Fund manager may decide to manage its own offshore fund directly, or opt to invest with a third-party manager by way of delegation where they have more specialized expertise in certain markets or asset classes. Allocating to offshore funds is the gateway to global capital markets for many Brazilian asset managers. As opposed to simply buying shares in various global investment funds, a Brazilian fund manager would want to establish his own fund-of-one. This international asset allocation is normally done through a fund-of-one structure because it allows the onshore fund manager to have a greater influence on the management of the offshore assets. This is a new structure in the investment world that offers investors the chance to customize the mandate, and gets the fund manager to increase allocations to a specific asset class, or to avoid it altogether.

Where management in fact is delegated to a third-party, the influence of the onshore manager helps the offshore manager avoid style drift, and maybe negotiate better fee structures. The latter is important, as fund-of-funds investors do not like the idea of paying multiple levels of fees. However, niche strategies and the addition of international access and diversification tend to compensate for the cost in a fund with adequate size. What also may happen is that an advisor will create a feeder fund for a high net worth individual,

and use that as the investor in a series of private placements - a mix and match strategy - but with much less administrative burden for both the investor and the advisor. So a fund-of-one makes customization fairly easy for such individuals looking at private placement opportunities.

Under this scenario, the ICON-007 as a fund-of-one will not be marketed to the general public so a simple term sheet and fund regulation document would suffice, as opposed to adopting a full-form prospectus. In addition, instead of waiving the fund's audit, it may make sense to consolidate the audit onshore, and have it conducted simultaneously by the same firm that preforms the onshore fund's audit. Alternative asset classes often have liquidity and valuation implications. In such cases, audit may be waived or deferred to better accommodate these investments from a purely operational viewpoint. Both the simplified offering document and consolidated audit offer some relative cost efficiencies at the start and on an ongoing basis.

While Brazilian domestic showbiz might just be nearing a tipping point as Brazilian actors and films steadily continue their thrust onto the world stage, Brazil has long-boasted a large, well-developed and highly sophisticated capital market system where the majority of investment activity is carried out via thousands of regulated investment funds. Single-investor funds, closed-ended exclusive funds, and open-ended pooled funds are all common-place fund operating models. Remarkably, it is quite normal for a wealthy individual or family to hold their financial assets via a fund; here private family funds are not

a new phenomenon as might be the case in other regions with the family office model on the rise.

As outlined in Example 2, the ICON-007 is sufficiently flexible such that a private Brazilian investor with an onshore fund as its primary investment vehicle can essentially mirror the fund model offshore with an entirely separate but analogous international wealth planning structure. The separation of the two structures provides better structural diversification, which reduces political, counterparty, legal and tax risks, amongst others.

### (Example 2) Exclusive ICON-007 Fund

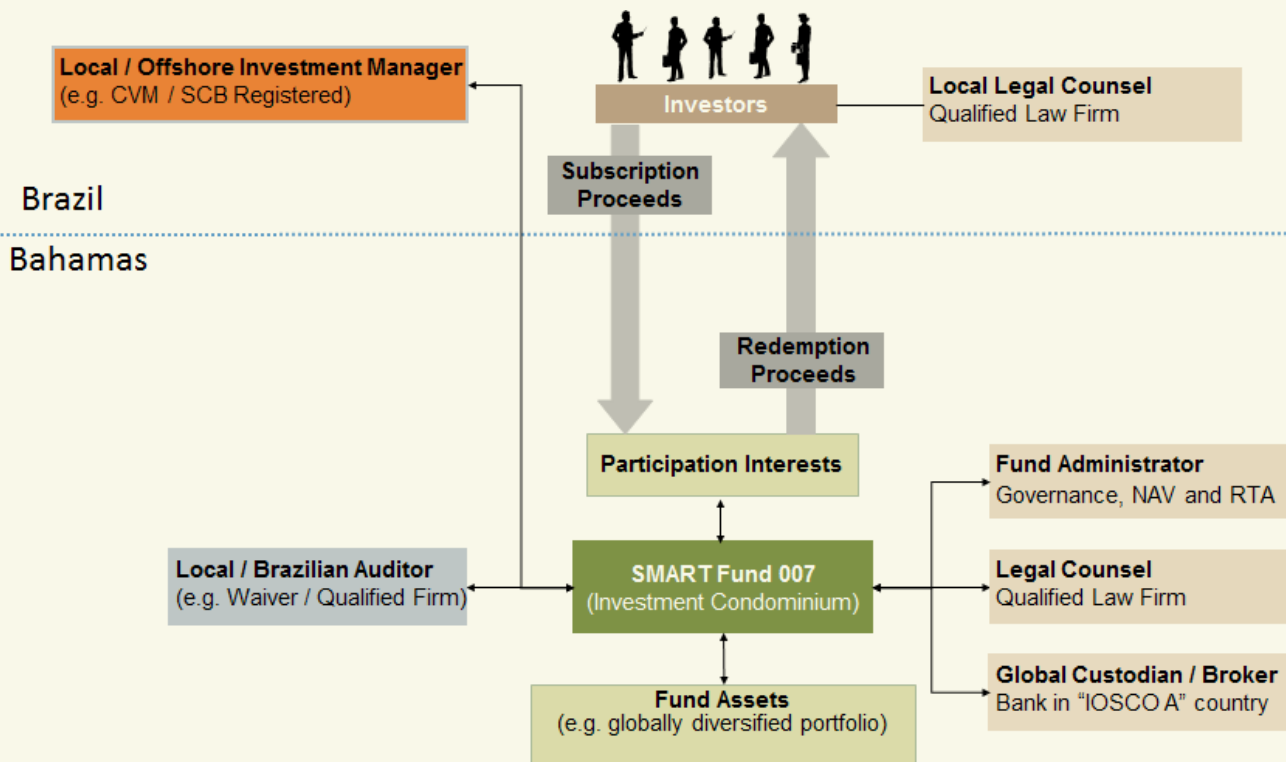
As it relates to international investing for private individuals, although some still may choose to make international allocations via their onshore funds, others will want to hold their offshore assets directly, i.e., separately from their Brazilian asset structures. For those investors who prefer a certain degree of financial segregation, some of whom may have several offshore managed accounts, a goal may be to consolidate their global holdings in order to maintain better oversight of their wealth and facilitate reporting, all of which just makes their lives easier.

An exclusive or stand-alone ICON-007 may work well for such individuals wishing to benefit from holding their international assets via their own exclusive investment

fund. Likewise, the investment scope of such investors is enriched by an exclusive ICON-007, which broadens their investment universe and raises their investment profile.

One of the greatest benefits of using an ICON-007 for private individuals is the value added by professional fund governance and management. This reduces the administrative burden on family offices and frees up the business to focus on strategic and tactical planning. Wealth managers also are making use of the streamlined nature of SMART funds to provide a one-stop-shop approach to wealth management and asset structuring by combining the fund management with succession planning and other wealth management services.

Fig. 2: Exclusive ICON-007 Fund



Wealth preservation, planning and diversification are the main drivers under this arrangement for individuals, families and small groups of investors to establish a private investment fund. Having ones wealth consolidated in a private investment fund also facilitates its transferability in terms of future restructurings or in succession planning where the participation interests in the ICON-007 would be held in a trust.

Wealth planners therefore are enabled to structure comprehensive wealth planning solutions for their clients, with the aim of managing a sustainable succession planning mandate that gives way to a formal yet flexible approach to multi-generational capital preservation, ease of transferability, and ultimately to the perpetuity of dynastic wealth under the oversight of professional administrators and trustees.





# Innovation Nation

## The ICON is just the latest example of The Bahamas’ approach to innovation

“Sustaining Innovation” and “Disruptive Innovation” are often seen as two distinct developments. The first typically is observed in mature businesses and the latter in start up enterprises. The Bahamas, an international financial centre of some 90 years, is no start up! Nevertheless, it has brought together the worlds of sustaining and disruptive innovation.

As a mature international business and financial centre with the presence of a diverse group of financial services providers and an over 80 percent long-term talent investment rate, it is not entirely unexpected that The Bahamas has demonstrated a propensity toward sustaining innovation. What is quite intriguing is its willingness to engage in disruptive innovation. Case in point and for discussion later, The Bahamas was the first major common law international financial centre to introduce a “civil law” only structure.

While this move seemed strange to some wealth management experts, it set a clear marker that The Bahamas was determined to give priority to non-traditional markets by responding to what was preferred by these markets rather than delivering traditional solutions.

At the heart of its spirit to innovate is the strength of the public-private partnership. This partnership blossomed from the trials of the onslaught of the OECD, Qualified Initiative/Jurisdiction and GAFI/

FATF in 2000. While the industry experienced some dislocation, the financial services sector - government, industry and regulators - acting together focused on their common interests; developed mutual respect for all sector-relevant roles; and perhaps most importantly, the industry understood and determined to work within the confines of the requirements of the government and regulators.

Moreover, the strict standards set and achieved in 2000 required that the nexus of all structures be grounded with a Bahamas-based regulated financial service provider responsible for gathering all due diligence information. In light of this regulatory requirement, The Bahamas can provide a level of privacy to clients whether they be founder or settlor; shareholder or beneficiaries, or in the ICON’s case, a participant.

With the strength of its public private partnership and rigorous regulatory environment, The Bahamas is able to focus - first and foremost - on adding greater value to its market proposition through sustaining innovation while seeking out solutions through non-traditional applications. Let us look first at these non-traditional applications, or disruptive Innovations.

### DISRUPTIVE INNOVATION

The **Investment Condominium**, or ICON, is not the first civil law structure adopted into the common law framework of The Bahamas.

Serious attention was first given to the adoption of the **Foundation** into The Bahamas toolkit in the late 1990s due to the important role it played in the lives of many of our clients.

What sparked this counterintuitive development? While many European clients of civil law extraction struggled with the concept of the trust it was primarily clients from Latin America who generated the greatest demand for product diversification outside of the trust context. At the core of this demand was the resistance by Latin Americans to the idea of being alienated from control of the family patrimony, a paradigm that is intrinsic to the creation of a conventional Anglo-Saxon trust. This aversion to the trust concept could not be assuaged by the many explanations that the trust pool would be safeguarded for the benefit of future beneficiaries given by European and North American financial institutions of a global stature.

As a result, a consensus developed that a foundation, a legal entity recognizable under the laws of the relevant home country, was an essential tool for both Latin American and European originating clients. The ability to accommodate the culture and custom of potential founders from Latin America and the rest of the civil law world was facilitated by the significant role played by Swiss banks that find their origins in a civil law tradition and were willing to provide banking services to this legal entity. Concurrently, a number of common law attorneys and professionals recognized that in the foundation's inherent flexibility and self-contained governance lay an array of potential solutions. The Foundations Act was enacted into

the laws of the country in 2004.

As the first major common law based financial centre to introduce foundations, and recognising its role as a path setter, The Bahamas was careful to establish a clear separation between foundations and trusts. Consistent with these efforts to mitigate the reference by the judiciary to trust law and case law precedent, the Foundation Act incorporates key provisions of The Fraudulent Dispositions Act and the Trusts (Choice of Governing Law) Act. As a result, not only is there strong asset protection in The Bahamas foundation, but in the choice of domicile which can be very important in some instances.

With this evidence of bold disruptive innovation from a common law country, a group of advisors approached The Bahamas with an idea now known as the Bahamas Executive Entity, or "BEE", in 2009. The BEE was enacted as the **Executive Entity** Act in 2011. The two year turnaround time from concept to enactment is particularly impressive when one considers that most international financial centres were focused exclusively on the execution of 12 or more tax information exchange agreements or "TIEAs". The Bahamas was able to meet evolving global standards in addition to advancing its competitiveness with this new solution.

The originators of the concept were convinced that in utilizing a "Foundation-derived entity", they had found an alternative to the use of the purpose trust as the shareholder of the private trust company. Moreover, as protectors who reside "onshore", they thought that this same

solution could mitigate the risk of contaminating the “mind and management” proposition of the client structures by their presence in onshore locations.

As a snapshot of the BEE, there are two perspectives: the legal and the practical. Giving regard to the legal definition, the BEE provides for a legal entity dedicated to the functions of the power holder and their duties, whether as an enforcer, protector, trustee or any other executive, administrative, supervisory, fiduciary or other office holding function. The BEE also provides for the ownership, management and holding of executive entity assets and trust assets.

From a practical perspective, the BEE as a legal entity effectively provides for institutionalised governance around decision-making powers that are typically held by a committee or an individual. The BEE also is permitted to own the shares of other entities dedicated to act as power holders, such as a private trust company.

In providing a greater insight into the BEE, two key features should be considered:

1. Carved out of the foundations concept, the BEE does not have a shareholder. With the absence of a shareholder, the risk that the objects and operational governance as prescribed by the founder are changed in the future is greatly mitigated. This is very important to heads of families who make decisions today regarding the governance on the family patrimony and would like the additional comfort that the protectors and advisors of the future will have

regard to their decisions.

2. The entity can only hold assets essential for operational purposes, which is expressed through the prohibition against the BEE itself accumulating assets. This means that the risks of utilizing the BEE for money laundering is stripped away, ensuring FATF/GAFI compliance. The BEE also has a very narrow purpose which further reduces the risk of money laundering while facilitating the filing of only a registration statement with the Registrar General’s Department.

In addition to the uses referenced above, the BEE also strengthens governance in family-owned businesses and family offices as well as providing for seamless transition in the members of the BEE council. The BEE can serve as a corporate director, where it is making decisions subject to and implementing the provisions of a shareholders’ agreement.

**SUSTAINING INNOVATION**

By reason of its heritage as a former colony of the United Kingdom, trusts are an important part of legal arrangements in The Bahamas. With a compelling history of jurisprudence on which to draw, the jurisdiction set about leading the way with two evolutionary changes to its trust law.

In 1998, The Bahamas paved the way with **Settlor Reserved Power Trusts** (“SRPT”). These landmark provisions were seen as an antidote to the sham doctrine which by that time had gained a great deal of traction in jurisdictions such as the UK,



Canada, the US, Guernsey, and elsewhere. This landmark change in the law of The Bahamas has been adopted by many of the jurisdictions that offer trusts to an international clientele.

At this time, The Bahamas also adopted very clear rules regarding the **access to information** relating to a trust. With limited exceptions, information is not available to third parties and non-vested beneficiaries. Other important concepts such as the protector were captured and the special company was defined and given differentiated treatment in the law. A special company is one that is not undertaking the types of activities often associated with commercial trust arrangements, for example, investing in liquid readily valued securities.

In 2011, The Bahamas took another leap forward. The role of the SRPT was further clarified through the **Directed Trust**. Developed from the Delaware statute, The Bahamas solution provides great certainty where a party wishes to have significant authority over the investment management decisions. Two classic examples are that of a professional hedge fund manager who may have greater difficulty giving over management of the family fortune to a private bank or the operators of a commercial enterprise.

This desire would appear to directly contravene trust and common law that impose substantial asset management obligations on the trustee. Essentially, the trustee must know and be accountable for the performance of the assets in the trust pool.

Given that a directed trust seeks to handcuff

the trustee with regard to the investment management decisions, it is critical that the integrity of the trust is maintained. In this regard, The Bahamas law provides for a continuing role of the trustee to respond to what are inappropriate actions based on “actual knowledge” and for the intervention of the court.

In adjusting its law against perpetuities, The Bahamas was challenged to address existing Bahamas law trusts that want to throw off the shackles of the rule against perpetuities without changing their reference to Bahamian trust law. The challenge exists in determining who could make such a fundamental decision. While the challenge was great, a solution was critical on the basis that a trust from another jurisdiction could move to The Bahamas to take advantage of the perpetual trust law environment and Bahamas existing trusts could move to another jurisdiction to take advantage of the new jurisdiction’s perpetual trust law.

After much debate, it was concluded that the courts of The Bahamas were best positioned to determine if a trust could indeed become a perpetual trust and the trustee would initiate the request to transition to a perpetual trust; the court and the trustee were given their respective powers as neither the settlors nor the beneficiaries should initiate the decision to become a perpetual trust. The court’s involvement along with the power for parties to the trust to contest the movement towards a perpetual trust - should they have particular concerns - serve to secure the integrity of the framework.

Finally, the often discussed **SMART Fund** perhaps is best recognized amongst The Bahamas' efforts at sustainable innovation. Building on the retail and professional funds, The Bahamas developed a response to one of the most dynamic markets in the world: the securities market. Predicting the direction of the market and how investors would wish to engage in these markets can be

quite difficult. The provision by Bahamian law that SMART Fund templates can be approved by the Regulator and given the effect of law once they adhere to the sound principles of regulatory integrity is evolutionary. The fact that a template has benefited from a 2 month turnaround from a well articulated market idea from the private sector to approval by the regulator is impressive.

# Fact Sheet

## Key Highlights of the ICON Act

An investment condominium is established under the Investment Condominium Act, 2014. It is a contractual relationship between one or more participants who have pooled assets for the purposes of operating as an investment fund, and an investment condominium must be licensed as an investment fund under the Investment Funds Act. It may be formed to operate as an open-ended fund (in which participants can call for redemption of their interests) or a closed ended fund (in which they may not).

It is an entity without legal personality but, when represented by its administrator, is able to hold assets in its own name, enter into agreements and sue or be sued in its own name.

### How is an investment condominium established?

When one or more initial participants execute its governing regulations, the investment condominium's administrator issues a certificate of establishment which is submitted to the Registrar General and the investment condominium's name is entered on the register. The investment condominium must be licensed as an investment fund by a licensor (the Securities Commission of The Bahamas or an unrestricted investment fund administrator) within ninety days of establishment unless an extension to this period is approved by the Securities Commission.

### What are the governing regulations?

The governing regulations set out the terms under which the investment condominium will operate. There are specific contents prescribed by law, which include the following:

- Its name;
- The name and address of its administrator;
- Its duration (which may be limited or unlimited);
- The number of participation interests it can issue and the currency in which the interests will be issued;
- Whether it will issue classes or series of participation interests, who is authorized to determine the number of classes/series and what the powers, rights and preferences of such interests are;
- How the administrator will handle its administration and whether it will have a governing administrator and a general administrator;
- Audit provisions (which are subject to the Investment Funds Act);

- How the governing regulations may be amended;
- The liability of the participants in the investment condominium, including how it is limited (if at all);
- Provisions for valuation of the investment condominium’s assets;
- Provisions for termination of the investment condominium; and
- Any other provisions required under the Investment Funds Act.

The governing regulations are not required to be filed with the Registrar General, and therefore are not a public document.

**How does the investment condominium act?**

An investment condominium, as an entity without legal personality, is represented by its administrator. The administrator, acting on its behalf, executes all letters, contracts, agreements, deeds and documents for the investment condominium. The administrator also has the power to do all other acts and things which are necessary or conducive to the investment condominium’s activities. As a general rule, the administrator’s acts bind the investment condominium.

**What are the obligations of an investment condominium’s administrator?**

The administrator’s obligations depend on the role it fills for the investment condominium. An investment condominium is required to have a general administrator and an operating administrator, and these roles may be filled by a single entity or by two separate entities.

A governing administrator is deemed to be the investment condominium’s operator for purposes of the Investment Funds Act, and has all the powers and duties of an operator for this purpose. A governing administrator must be either: (i) an administrator licensed by the Securities Commission (restricted or unrestricted); (ii) a licensee under the Financial and Corporate Service Providers Act; (iii) a licensee under the Securities Industry Act; (iv) a bank or trust company licensed by the Central Bank; or (v) a foreign entity licensed by or registered with a regulatory body with functions and powers equivalent to the Securities Commission or Central Bank. The governing administrator is therefore akin to a general partner, director or trustee of the equivalent entity licensed as an investment fund. The general administrator, by contrast, must be an administrator licensed by the Securities Commission (restricted or unrestricted) and acts as the investment condominium’s administrator for purposes of the Investment Funds Act.

If the administrator incurs any debts or obligations in conducting the investment condominium’s business, they are obligations or debts of the investment condominium and not the administrator personally.





**How does an investment condominium operate?**

An investment condominium may have an unlimited number of participants, but the minimum number is one.

Participation interests may but need not carry voting rights, and such rights are as specified in the governing regulations. Participation interests are personal property, and enforceable by the participants as a chose in action.

Books and records must be kept by the administrator, and include a register of participation interests as well as reliable accounting records retained for a minimum five year period.

Annual meetings of the participants must be called by the investment condominium's administrator, and such meetings may be held in The Bahamas or elsewhere.

Publicly available information on an investment condominium is generally limited to the information contained in its certificate of establishment, which sets out its name, the name of its administrator(s), the date of establishment, a statement that it shall be licensed as a fund and the address in The Bahamas at which the investment condominium can be served.

**Can an investment condominium make distributions?**

An investment condominium may not make or declare dividends or other distributions to its participants. Participants therefore recoup their investment only upon redemption of their participation interests, which may take place in whole or in part on the terms set out in the governing regulations.

**Is an investment condominium liable for local taxes?**

An investment condominium is not liable for estate, inheritance, succession, gift or stamp taxes, provided that its participation interests are held (directly or indirectly) only by persons deemed 'non-resident' for exchange control purposes and that the investment condominium does not own (directly or indirectly) real property situate in The Bahamas. It is intended that investment condominiums meeting these conditions will also be exempted from VAT, once implemented.

**Can an existing entity be converted to a condominium?**

Existing entities may become ICON Funds, and the conversion can be achieved without a termination event triggering a capital gain or other adverse tax consequence. Bahamian entities as well as entities presently established under the laws of other jurisdictions are able convert into an investment condominium and be licensed as a investment fund. Therefore, it is possible:

- to convert a Bahamian trust, exempted limited partnership or company to an investment condominium;
- to accommodate the re-domiciliation of an investment fund established elsewhere to The Bahamas and to permit its conversion to a condominium once successfully redomiciled; and
- to allow for unbroken continuity of the fund, while changing the character of the legal structure that underpins it.

Note that equivalent entities established under the laws of another jurisdiction must take advantage of existing continuation procedures in the International Business Companies Act or the Exempted Limited Partnership Act, or utilize the power to change governing law contained in the trust instrument.

### **How is a condominium wound up?**

An investment condominium may be dissolved either voluntarily on the terms contained in the governing regulations, or compulsorily by the court. Voluntary dissolution is permitted where the investment condominium is solvent; involuntary dissolution is required where the investment condominium is insolvent, the participants so request or the regulator so petitions, or where the court believes it just and equitable that it be so dissolved.



Bahamas Investment Condominium



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