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# THE EVOLUTION OF OFFSHORE FUND FORMATION

► **Barbara Niederkofler and Blayne Grady, partners with Akin Gump, discuss recent trends in the offshore financial sector as well as their approach to collaborating with local counsel to best serve their clients' needs in real time.**

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**CCBJ: Can you each share a bit about your background and your practice?**

**Barbara Niederkofler:** I have been practicing law since 2003. I started in Akin Gump's London office, where I worked with managers based in Europe and Asia. When the global recession hit in 2008, I was working on various funds that were being put on life support. As a result, my practice involved a lot of international structuring and regulatory issues. But depending on the economic cycle we're in, my practice consists of hedge funds, credit funds, private equity funds, as well as other more bespoke structures. Right now, my practice is focused more on closed-ended structures, but I am seeing an uptick in open-ended funds too.

I've been in New York since 2011, and while I continue to work with many international clients, I have also been working on various U.S. regulatory issues, and I have developed a practice around representing investment advisers with Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC) matters as well.

**Blayne Grady:** I've been in Akin Gump's funds practice in Washington, D.C., for 17 years. My practice is primarily focused on private equity fund formation, mostly from the sponsor side, although I have some clients on the limited partner side as well. In recent years, we've raised a number of funds with credit and credit-related strategies, renewable energy funds, and real estate funds.

**What are some trends you're seeing in the offshore financial sector?**

**Grady:** The developments have fallen into two main categories: The first involves the increasing regulatory enhancements we've seen in these jurisdictions, and the second involves developments to create more flexibility and options in fund structuring.

In the first category, we've seen enhanced know-your-customer and anti-money laundering requirements over the last few years, as well as new data privacy requirements, particularly in the Cayman Islands and in many European Union jurisdictions. As for the second category, offshore jurisdictions across the board are working to create more sophisticated legal frameworks that allow clients more flexibility to establish and operate funds in these jurisdictions. An example is the Cayman Islands' adoption of a new LLC regime that matches what's being done in the United States in terms of flexibility for entity structure and type.

**Niederkofler:** There are other regulations that are impacting these offshore jurisdictions as well. For example, the persons with significant control (PSC) regime, which aims for transparency around the ownership of entities and was originally based in the United Kingdom, has now spread to other jurisdictions, like Bermuda for instance.

**Where are most of these offshore investment funds located now? Are there significant shifts we should be aware of?**

**Niederkofler:** The main offshore jurisdiction continues to be the Cayman Islands. But it does vary based on where the investment manager is located. For U.S. managers, the Cayman Islands continues to be the preferred jurisdiction. For managers outside of the United States, we're starting to see a focus on other jurisdictions, particularly

in light of Brexit and the potential changes to the UK government and UK tax laws.

We've seen increasing interest and growth in some of the more nontraditional jurisdictions – like Jersey in the Channel Islands, for instance, and Canada. Some clients are looking at places like Malta and Scotland.

**Grady:** I agree. Cayman is still the gold standard in terms of offshore jurisdictions. The British Virgin Islands and Bermuda are generally user-friendly as well, with good local counsel. Places like the Marshall Islands and Anguilla are used less frequently, but they do pop up every now and again. As Barbara noted, it's a bit dependent on the strategy and location of the manager – and even the location of the investments. In the European Union, for fund structuring, the usual suspects have traditionally been Guernsey and Jersey. But in recent years, we've been setting up more and more funds that are actually onshore, with Ireland and Luxembourg in particular taking advantage of available tax treaties.

#### **What are some of the key issues related to the formation and structure of these kinds of investment funds?**

**Grady:** In my experience, there isn't much that can't be easily handled with the early involvement of local counsel. When deciding which offshore jurisdictions to use, the key considerations we tend to look at are making sure that the country has a well-established, sophisticated legal system to make sure that rights and obligations are enforceable. We look at cost, obviously, and then ease of formation, ease of operation, and entity administration. Dissolution is an area that often gets overlooked when you are forming vehicles for a fund, but in some jurisdictions the dissolution process can be quite formal – it takes more time and expense than anybody expects or desires. So looking into that up front is a good idea when choosing a jurisdiction.

**Niederkofler:** The operations and administration of the vehicle can also be overlooked somewhat. Managers should focus on what it actually means to have an entity formed in a particular jurisdiction, in a practical sense. Some jurisdictions require in-person meetings in that country, and that's not always easy administratively or from a governance standpoint in certain jurisdictions.

#### **What are the regulatory priorities, and what does enforcement look like? How are you advising clients in terms of compliance?**

**Niederkofler:** Whether you're looking at the United States, since the Dodd-Frank Act in 2010, or elsewhere, there have been many regulations in this industry lately – a lot of attention by the regulators. The SEC published guidance this year – its interpretation of the fiduciary duty of investment advisers – so the focus on this industry very much continues.



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On the other side of the Atlantic, in the UK, the Financial Conduct Authority is similarly focused on the alternative investment industry. In the EU, the General Data Protection Regulation has had a tremendous impact, even though it wasn't specifically focused on this industry. Then you've got other regulations like the PSC regime, which I mentioned earlier, that requires more disclosure of ownership for persons of significant control. That trend continues to grow, and other jurisdictions are doing the same. As Blayne mentioned, there have been significant developments in the Cayman Islands, Singapore and Hong Kong.

When we're working with investment managers and looking at various jurisdictions, in many ways it's a puzzle, where you have to figure out how all of the pieces are going to fit together. You have to make sure that the manager not only has the compliance manual and regulatory filings but also that they are able to ensure that

everything is in compliance with all of these regulations and practices on a daily basis.

It can be frustrating for some clients – if we are working with a client based in Asia, for instance, and we have to explain why the SEC or the National Futures Association has this long-armed jurisdiction. We have to be able to translate from one jurisdiction to another and inform clients why their country's own regulations impact that other jurisdiction. It's become very challenging.

**Grady:** Our responsibility is to make sure that we work with the key firms in the relevant jurisdictions, maintaining good relationships with them and staying abreast of all of these developments, while also making sure that we involve local counsel in these specific issues as they become relevant to our clients. And as new issues pop up, we help them decide the best ways to address those matters. ■