



BERMUDA SUCCESSFULLY FOSTERING THE FINTECH SECTOR

Stephanie P. Sanderson, of BeesMont Law, reflects on Bermuda's success in nurturing the development of fintech-related business.

"we are seeing fintech increasingly change the financial services industry including the banking, insurance and asset management sectors."

Bermuda continues to successfully foster fintech business as the market in Bermuda expands. Traditionally, Bermuda has been a successful centre for financial services, insurance, asset management and private-client business due to a sophisticated, modern and well-regulated approach to doing business. It has more recently gained a reputation as a leading fintech jurisdiction and is attracting fintech business from all over the world.

According to Accenture, venture capitalists, private equity firms, corporates and others have invested more than \$50bn into the fintech industry since 2010 as the innovative technologies redefine the way we store, save, borrow, invest, transfer, spend and safeguard money.

Bermuda's Fintech Regime

In 2018, the Bermuda government publicly announced that Bermuda would put in place a specialised legal and regulatory framework to give fintech business stability and certainty. The jurisdiction saw the introduction of Initial Coin Offering (ICO) and digital asset business legislation as well as incentives established by the Bermuda Monetary Authority (BMA) specifically to encourage fintech and insurtech growth and open innovation. Bermuda has also sought to provide a solution to the global issue of banking services for the fintech sector by amending its banking legislation.

ICOs and security token offerings continue to be a popular funding mechanism for technology-related businesses and start-ups, although fintech companies are enjoying more funding options as the market becomes established. Blockchain-based projects and platforms are prevalent in the fintech industry and larger institutions are also looking to blockchain as an underlying technology to improve existing systems.

Bermuda's digital asset business regime encompasses businesses which provide any or all of the following activities to the general public:

Issuing, selling or redeeming virtual coins, tokens or any other form of digital asset

This includes any business (incorporated or not) that provides these services to other businesses or individuals. This would include an ICO business on behalf of customers, but not ICO activities to fund one's own company or project. An example of the former that will be subject to the Digital Asset Business Act 2018 is a company that operates a facility to assist its clients to launch ICOs. This includes assistance with coin or token design and administering the ICO process. An example of the latter that will not be subject to the Digital Asset Business Act 2018 is a company that wishes to issue its own ICO for its online gaming website or other business operations.

Payment service provider business utilising digital assets

The term Payment Service Provider (PSP) is a term used globally and is defined in Bermuda legislation as: "a person whose business includes the provision of services for the transfer of funds". The intention is to capture businesses involved in the transfer of digital assets.

Operating an electronic exchange whereby digital assets of any type are exchanged for cash or another digital asset

Purchases and sales of digital assets can be made using either fiat currency or digital assets. In addition to digital assets such as bitcoin and Ether, digital asset exchanges may also facilitate the offer of new coins/tokens that are sold pursuant to ICOs/Initial Token Offerings (ITOs).

Provision of digital assets custodial wallet services

A digital assets wallet is a software programme that stores private and public keys and interacts with various blockchain technology to enable users to send and receive digital currency and monitor their balance. A digital asset itself is not actually "stored" in a wallet. Instead, a private key is stored as proof of ownership of a public key. By the wallet storing private and public keys, it allows the user to send and receive coins, and also acts as a personal ledger of transactions.

Digital assets services vendor

This category is intended to capture any business providing specific digital asset related services to the public. This would include custodial and power of attorney rights over a customer's virtual currencies or market maker in digital asset activities.

Fintech and the financial services sector

Fintech, in the general sense, impacts various industries including insurance, healthcare, tech and telecoms, as well as financial services. Generally, we are seeing fintech increasingly change the financial services industry including the banking, insurance and asset management sectors. Particularly over the past year, we have seen the finance industry becoming more comfortable and willing to invest in fintech.

Various reports have revealed that existing financial services institutions are investing, or plan to invest, in fintech and that they are largely concerned about the disruption to the industry arising from standalone fintech companies. Just recently JP Morgan announced it would be launching its own digital currency. It has also been reported that MUFG and Credit Suisse have each launched fintech funds and Standard Chartered has launched a business unit to invest in fintech.

The private equity sector has traditionally been more comfortable with fintechs, which is apparent when looking at private equity owned fintech companies, and the trend seems to be continuing.

As the industry matures and fintech companies become more established and able to create track records with respect to their business models, funding becomes more straightforward. Importantly, investor confidence is also strengthening as the market develops. This is good news for the future of the fintech sector.

Investment managers have also been able to track the progress which fintech has made with new tech being introduced which impacts the asset management industry, such as robo-advisory services. According to Statista, Assets under Management in the robo-advisory segment is expected to show an annual growth rate of 31.4% from 2019 to 2022. Mobile applications, robo-advisory services and adoption of other fintech in the asset management and wealth management sectors will likely increase rapidly in the coming years.

Risk mitigation – AML/CTF and cyber-security

One of the key concerns with digital asset business is anti-money laundering and counter-terrorist financing as well as cyber threats and systems failures.

Bermuda aims for quality versus quantity when it comes to businesses being set up in the jurisdiction. Any business which plans to establish itself in Bermuda should be aware that a vetting process will be applied. This is by design, as the jurisdiction must maintain its international reputation as a sophisticated and internationally respected place in which to do business.

Acknowledging the particular risks facing this sector, the BMA issued sector-specific guidance notes on anti-money laundering and anti-terrorist (or counter-terrorist) financing for digital asset businesses. Senior management of a digital asset business must:

- Ensure compliance with the relevant anti-money laundering and counter-terrorist financing laws and regulations;
- Identify, assess and effectively mitigate the money laundering and terrorist financing risks the business faces among its customers, products, services, transactions, delivery channels, outsourcing arrangements and geographic connections;
- Conduct an anti-money laundering and sanctions risk assessment and ensure that the risk assessment findings are maintained up to date;
- Appoint a compliance officer at the senior management level to oversee the establishment, maintenance and effectiveness of the anti-money laundering and counter-terrorist financing policies, procedures and controls;
- Appoint a reporting officer to process client disclosures;
- Screen employees against high standards;
- Ensure that adequate resources are periodically trained and devoted to the anti-money laundering and counter-terrorist financing policies, procedures and controls;
- Audit and periodically test the anti-money laundering and counter-terrorist financing policies, procedures and controls for effectiveness and address any issues uncovered adequately and timely; and
- Recognise potential personal liability if legal obligations are not met.

Digital asset businesses are also susceptible to risks such as cyber threats or systems failure. The BMA requires all digital asset businesses in Bermuda to have a comprehensive cyber-security programme in place that is commensurate with the nature,

scale and complexity of its business and must include a documented cyber-security policy. The cyber-security programme should include information security, data governance and classification, access controls, business continuity and disaster recovery planning and resources, customer data privacy, and incident response, among other requirements. The business must also appoint a Chief Information Security Officer (CISO) responsible for overseeing and implementing the cybersecurity programme and enforcing the business' cyber-security policy.

Future Development

As fintech is a relatively new industry we can expect the legal and regulatory landscape to continue to evolve as the sector develops internationally. Bermuda has the advantage of already having in place a complete legal and regulatory regime, as well as commitment from the BMA that it is focused on supporting innovative new technologies.

We will no doubt see the BMA ensuring that the framework remains fit for purpose as time goes on, which means fintech businesses should keep abreast of developments. Fintech businesses looking for certainty and stability, as well as a jurisdiction with a well-respected international reputation, will continue to choose Bermuda as their domicile of choice.



Stephanie P. Sanderson is a partner at BeesMont Law Limited. She practices in all areas of corporate and commercial law with a particular emphasis on mergers and acquisitions, investment funds, insurance, finance, corporate reorganisations, restructurings and cross-border transactions. Stephanie leads BeesMont Law's Technology & Innovation team. Sanderson's practice also encompasses Bermuda international tax transparency law, corporate governance, compliance and regulatory matters, including AML/ATF, data protection and privacy law.

As originally published by HFM Global