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Guernsey and green finance - a promising start with a bright future ahead

Guernsey has been a pioneer in facilitating environmentally-responsible investing – it was the ninth member of the United Nation's international network of financial centres for sustainability and has a longstanding relationship with the UK's Green Finance Institute.

This commitment to green finance is embodied by the work of Guernsey Green Finance - the umbrella body for green finance in Guernsey aiming to provide the broadest, most comprehensive range of green and sustainable financial services. This initiative, which draws on the collective expertise and cooperation of the Island's government, the Guernsey Financial Services Commission (the "GFSC") and wider finance industry, reinforces Guernsey's commitment to the Sustainable Development Goals ("SDG") - a collection of 17 global goals set by the United Nations to alleviate Earth's alarming environmental crisis. This is certainly an ambition objective as the International Panel on Climate Change estimates that approximately $2.4 trillion (roughly 2.5% of global annual GDP) needs to be invested in the energy sector to meet the SDG's goal of a 1.5 degree reduction in average global temperature by 2035. Through the creation of the Guernsey Green Finance initiative, Guernsey hopes to contribute its expertise as a global finance centre to help fulfil the SDG's objectives and satisfy the increasing demand for green investment options.

The Green Fund

As part of the key strategic aims of Guernsey Green Finance, the GFSC launched the Guernsey Green Fund (the "Green Fund") in 2018, the world's first regulated green investment product. The Green Fund seeks to improve access for investors to investments with an objective of tackling climate change, reducing environmental damage and achieving a net positive outcome on the planet's environment. A fund designated as a 'Green Fund' is entitled to use the Green Fund logo on all materials and documents and this 'kitemark' acts as a selling point for a fund, indicating to potential investors that it complies with the strict criteria for green accreditation. Green Funds have been very attractive to environmentally conscious investors and at the end of the second quarter of 2020, Green Funds held a total net asset value of £3.3 billion.

Eligibility requirements

All authorised and registered funds established under the Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended, are able to obtain the Green Fund designation provided they can satisfy the eligibility requirements set out in the Guernsey Green Fund Rules, 2018 (the "**Green Rules**").

The Green Rules require applicants for Green Fund designation to be established with the objectives of spreading risk and seeking a return for investors whilst mitigating environmental damage. The applying fund must also meet one of the green criteria set out in schedule 2 to the Green Rules (the "**Green Criteria**") and have at least 75% of its assets by value invested in the Green Criteria specified by such fund in its application. The current Green Criteria used is based on the Common Principles for Climate Mitigation Finance Tracking (which were calibrated by a group of 22 leading international, national and regional development finance institutions) and includes investment in the following asset classes:

- renewable energy;
- lower-carbon and efficient energy generation;
- energy efficiency;
- agriculture, forestry and land-use;
- non-energy greenhouse gas reductions;
- waste and wastewater;
- green transport;
- low-carbon technologies; and
- cross-cutting issues.

The remaining 25% of the portfolio can be invested in any other asset classes, provided they are not contrary to the Green Fund’s overall objective of mitigating environmental damage or fall under an asset class prohibited by schedule 3 of the Green Rules (e.g., uranium mining, landfill without gas capture, etc.).

To demonstrate compliance with its Green Criteria, a fund must provide the GFSC with either:

- a declaration from the fund's designated administrator together with a certificate from a suitable independent third party that the prospectus meets the chosen Green Criteria ("**Route 1**"); or
- a self-certified declaration from a Guernsey licensed entity (e.g. an administrator or fund manager) that the fund meets the notified Green Criteria ("**Route 2**").

Additionally, bolt on funds can voluntarily apply Environment, Social, and Governance (“**ESG**”) principles to the investment analysis and decision-making processes of the fund. Once accredited, Green Funds are listed on the GFSC website and can use the Green Fund logo in their various marketing and information materials (subject to the GFSC’s guidelines on use). The GFSC is currently in the process of registering the Green Fund logo as a trademark with Guernsey’s Intellectual Property Office.

Prospectus disclosures

On applying for Green Fund designation, the GFSC must receive a copy of the fund's final form prospectus. The prospectus must contain a number of disclosures, namely: (i) that the fund has been designated as a Green Fund; (ii) the Green Criteria in which the fund will be investing; (iii) the fund’s objectives and how it will meet them; (iv) whether the fund has been certified via Route 1 or Route 2 and details on that certification; (v) whether the governing body and manager of the fund will apply ESG factors when undertaking investment analysis and in its other decision-making processes; and (vi) any material risks specific to green investing reasonably required for investors to make an informed judgement on the merits of investing in the fund. The GFSC will designate a fund as a Green Fund if it is satisfied that the fund's prospectus and principal documents comply with the Green Rules. Guidance from the GFSC suggests an approval time of up to five days for Green Fund designation in respect of existing funds. The GFSC has also recently confirmed that a Green Fund can meet the requirement to disclose its designation as a Green Fund through a market announcement on a recognised stock exchange, thereby allowing greater flexibility than was previously the case in relation to such disclosures.

Ongoing obligations

A Green Fund is required to satisfy a number of ongoing obligations. First, the fund's administrator is required to ensure that the fund is monitored against its investment criteria and notified Green Criteria on a monthly basis (this has recently been extended for closed-ended funds to a quarterly basis). However, such obligation is not required until the fund is fully invested or six months from the date of the fund's Green Fund designation, whichever occurs first.

Secondly, a fund must detail how it meets its Green Criteria in: (i) a filing to the GFSC to be made within six months of the fund's accounting year-end and (ii) an annual report prepared for investors. Finally, both the GFSC and the fund's investors must be immediately notified of any changes made to the disclosures in the prospectus.

Removal of designation

Failure to comply with its investment criteria or Green Criteria for a period of over three months triggers the filing of a declaration of non-compliance with the GFSC by the fund administrator and removal of the Green Fund designation. As a result, this declaration must be published on the fund's website, the fund's administrator must ensure that the governing body of the fund removes all Green Fund designation references and logos from all documents and materials, and the fund's investors must be notified of the removal of the Green Fund designation.

In addition, the GFSC has the right to remove a fund's Green Fund designation if: (i) the fund has contravened its investment criteria or Green Criteria for a period of over three months; or (ii) the fund is being wound up; or (iii) at any time if the fund ceases to meet its investment criteria or notified Green Criteria if the GFSC considers it necessary in order to protect the interests of investors, the public or the reputation of the Bailiwick of Guernsey as a finance centre.

Success stories

There have been some notable developments in the field of green finance in Guernsey, which demonstrate the value of the product and that this is an area of growth for the Guernsey finance industry as a whole.

In 2019, Bluefield Solar Income Fund ("**Bluefield Solar**") achieved accreditation as a Green Fund and became the first fund listed on the London Stock Exchange (the "**LSE**") to do so. A Guernsey-registered, closed-ended investment fund, Bluefield Solar invests in more than 80 UK-based solar assets targeting long-life solar energy infrastructure that are expected to generate stable renewable energy output over a 25-year period. Significantly, the accreditation of such a major fund reinforced the regime's attractiveness to existing funds; Bluefield Solar was launched in 2013 and was already listed on the main market of the LSE when it successfully applied for Green Fund accreditation.

2019 also saw the launch of Greensphere Capital (a Guernsey Private Investment Fund). This fund intends to back companies and projects that help to mitigate the biggest risks facing our younger generations – resource scarcity, commodity and fuel volatility, and climate stress. More recent developments include: (i) Commercial lender Sarnia Mutual launching a new 'green loan' product, offering preferential rates for customers seeking loans for certain environmentally friendly products; and (ii) the German ESG investment manager, Aquila Capital, launching its second Green Fund, which listed on the LSE in June 2021 and raised £100 million from its IPO.

As at the date of this briefing, 12 funds have obtained Green Fund designation with the GFSC and this number continues to increase as businesses on the Island continue to support managers launching a range of sustainable funds. This is exemplified by the recent launch of Environmental & Social Impact Monitor ("**ESIM**"), a not-for-profit accreditation service for island businesses that rates businesses on environmental and social commitments. ESIM is intended to help facilitate the development of a new advisory and auditing sector within green finance and ultimately, export skills to other jurisdictions.

TISE and green finance

Guernsey is also home to The International Stock Exchange (the "**TISE**"), which is at the forefront of globally recognised exchanges adopting green finance initiatives. The TISE launched its own specialist green market segment, 'TISE GREEN', with the stated aim to 'enhance the visibility of those investments which make a positive impact on the environment'.

Similar to the Green Fund, any investment seeking admission to the TISE GREEN must meet an internationally recognised standard of green finance criteria, which is satisfied by the Green Criteria. TISE GREEN is open to issuers from any jurisdiction listing any type of green investment, including bonds, funds and trading companies provided the investment is already listed on TISE and its green credentials are verified by an appropriate third party against a globally-recognised standard.

Furthermore, like the Green Fund, TISE GREEN assists promoters who wish to attract investment into environmentally beneficial initiatives by helping to highlight their green credentials while providing easier access for ESG investors.

As the demand for ESG-focussed market makers continues to rise, the TISE stands to benefit by offering its services to funds and promoters who wish to set up structures in a way which complies with green finance criteria. A recent example of this trend is exemplified by the listing of €500 million of 'green bonds' by Novelis, the world's largest recycler of aluminium, in April 2021.

Future

Guernsey's commitment to green finance makes it well placed to benefit from the increasing focus of fund managers on ESG compliant investments. Many US investors, such as the California Public Employees' Retirement System ("**CalPERS**") a large public sector investment fund, are increasingly insisting their investment managers invest their funds in ESG-focused investments which are accredited as green by robust certification regimes. The Green Fund and the TISE GREEN could have a significant role to play in this developing trend as both products are tied to a recognised, existing set of green principles such as the Green Criteria. The Green Criteria provides flexibility for fund managers in two ways. First, since the Green Criteria does not restrict or alter existing investment principles to which they must comply or require certain management practices or processes be adopted, fund managers can continue operate their funds as they see fit.

Furthermore, the Green Criteria is likely to form the core of the EU Taxonomy Directive – an EU classification system establishing a list of environmentally-sustainable economic activities. The Green Rules enable the GFSC to add further sets of green principles to those comprising the Green Criteria. Therefore, the Green Criteria can respond and evolve to new sets of green principles as they are adopted by other jurisdictions to form the basis of their green investment regimes. Though it has yet to be adopted by the EU, the Taxonomy Directive would establish the basis for ESG investing in the EU.

Furthermore, such principles are likely to form the core of the EU Taxonomy Directive – an EU classification system establishing a list of environmentally sustainable economic activities. The Green Criteria is flexible enough to allow for differing sets of green principles to be adopted to reflect either alternative taxonomies or other areas thought suitable for the Green Fund kitemark. Though yet to be adopted by the EU, the Taxonomy Directive will establish the basis for ESG investing in the EU.

Conclusion

Guernsey remains fully committed to environmental sustainability and is primed to leverage its position as a leading international finance centre to advance in the green finance space. The jurisdiction has been administering clean technology and ESG funds for a number of years and building on this existing expertise should only serve to attract further investment. This is particularly so given the expanding interest of US and UK investment managers and pension funds in green finance and this trend is reflected in the significant rise of ESG investing in recent years, which is predicted to continue. According to the Global Sustainable Investment Alliance, sustainable investing assets in the five major markets (the US, Europe, Japan, Canada, Australia and New Zealand) stood at $30.7 trillion at the start of 2018, a 34 percent increase in two years. To further emphasise this point, over the next three decades, MSCI Inc. estimate that investments in US-domiciled ESG investments alone are estimated to range between $15 trillion and $20 trillion, approximately doubling the size of the current US equity market.

Products such as the Green Fund and the TISE GREEN market segment should give Guernsey a significant competitive advantage over competing offshore jurisdictions. The current trends toward ESG-focused investing and regulation coupled with a long history of stable government espousing high standards of administration, regulatory oversight and tax compliance makes Guernsey well placed to benefit from this shift. This is reflected in the transparent verification and certification processes applicable to the Green Fund and TISE GREEN regimes, with benchmarking against the internationally-recognised green principles, which the Taxonomy Directive should broadly follow once implemented. This, coupled with the predicted increase in ESG investing, makes Guernsey well placed to not only facilitate and benefit from the coming green finance revolution, but to be one of its key protagonists.

If you would like any further information, please get in touch with your usual Bedell Cristin contact or one of the contacts listed.

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