INSOL INTERNATIONAL

ESG IN RESTRUCTURING

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PRESIDENT'S INTRODUCTION

Environmental, social and governance (ESG) issues are rapidly changing the way that business is conducted across the world. We are witnessing new regulations on climate change, biodiversity and environmental conservation, modern slavery and workers' rights and board accountability, conflicts and stakeholder engagement.

More broadly, we are also seeing a change in social attitudes, and a growing expectation from financiers, insurers, investors and customers that the businesses they deal with must behave in a responsible and ethical manner.

These dynamic regulatory, social and economic changes will inevitably drive future restructuring activity, as companies seek to align their operational structures and business models with improved governance, labour protection, social justice goals and the reality of a net zero emissions economy and the necessity of a greener footprint.

At the same time, however, the evolution of social and economic settings – and the dominant focus on ESG – raises the question as to whether existing restructuring and insolvency laws adequately protect and uphold environmental obligations, employee entitlements and workplace health and safety obligations, and hold directors and other officers to account in relation to their responsibilities to the company and its stakeholders.

There is a delicate balancing act between the protection of these interests and the underlying assumption that restructuring and insolvency processes ought to maximise value for the collective body of creditors – and in some cases, the respective policy concerns of ESG issues and restructuring and insolvency law and practice may conflict.

This has been apparent in the controversial "Texas Two-Step" option canvassed in recent United States case law (under which it has been proposed for tort liabilities to be spun off to a new corporate entity that undergoes a restructure), as well as non-consensual third party releases and, in some jurisdictions, the potential for an insolvent entity to disclaim or otherwise evade liability for its environmental obligations.

This new publication from INSOL International – *ESG in Restructuring* – therefore comes at an important time. Project Leaders Clayton Chong and Smitha Menon, from WongPartnership, canvass the policy motivations of ESG and insolvency and restructuring law and practice, and consider the regulatory standards, soft law frameworks and practices concerning key ESG issues outlined by esteemed practitioners and academics in 31 jurisdictions.

The Project Leaders consider the manner in which restructuring law and practice may be shaped to deal with incredibly complex and emerging ESG issues – particularly environmental responsibilities, labour protection and board accountability – that can have far-reaching impacts on vulnerable claimants and broader society. They provide a "roadmap" of issues that regulators and policy makers may consider in shaping future law reform.

This book is an invaluable contribution to law reform and regulatory and policy development as we strive to ensure that restructuring and insolvency laws are modern, progressive and "fit for purpose" in relation to the underlying economic and social circumstances in which they operate.

PRESIDENT'S INTRODUCTION cont.

The book also highlights important practical issues for our members to be aware of in addressing a multitude of ESG issues in the course of an insolvency appointment. Uniquely, the book also analyses recent market developments and trends in the ESG refinancing sphere, with the aim of serving as a useful "one stop" resource for financial institutions considering the provision of finance to entities (in good times and in the event of financial distress) in the context of complex and evolving ESG obligations and liabilities.

I express my sincere thank you to the Project Leaders, and each of the jurisdictional contributors, for their significant expertise, time and commitment in completing this project over the last 12 months, as well as to our team of INSOL International technical and administrative staff for their efforts in bringing the project to fruition.

I hope you enjoy reading this publication and will find it useful in your future pursuits.

Scott Atkins
President & INSOL Fellow
INSOL International

September 2023

GUERNSEY

1. General overview of the restructuring regime

1.1 Formal restructuring procedures

1.1.1 Arrangements and reconstructions (SS.105-112 Companies (Guernsey) Law, 2008)

The Companies (Guernsey) Law, 2008 (Law) includes provisions for "schemes of arrangement", being a compromise or arrangement between a company and its creditors (or any class of creditors) or its members (or any class of members). In an insolvency situation, a scheme of arrangement can be initiated by a liquidator or administrator.

The process involves either the company, a creditor or member, the liquidator or administrator of a company or the receiver of a cell of a protected cell company (Applicant) presenting a compromise or arrangement to the company's creditors (or any class of creditors) or its members (or any class of members). The Applicant will produce a statement explaining the effect of the compromise or arrangement, including the impact on any debenture holders. The Applicant will apply to court to order the convening of meetings of creditors (or a class of creditors) or members (or a class of members), to enable them to vote on the compromise or arrangement. If a majority of 75% in value of creditors (of class of creditors) or members (or class of members) votes in favour, the court may then sanction the arrangement. The court will consider whether the majority is acting in good faith and in the interests of creditors or members, and whether the different interests of creditors or members are such that they should be treated as belonging to a different class of creditors or members. A compromise or agreement sanctioned by the court is binding on all creditors (or class of creditors) or all members (or class of members), the company, the liquidator, the administrator and any receiver.

The existing management would typically remain in control of the company during a scheme of arrangement (unless of course an administrator, liquidator or receiver is already appointed and is the Applicant), with the process being overseen by the court.

1.1.2 Administration (SS.374-390 Companies (Guernsey) Law, 2008)

The Law includes provisions for administration, which is used as a "rescue process" in Guernsey. It is a more common process in Guernsey than a scheme of arrangement.

Administration applies to a company (or cell of a protected cell company) that is insolvent or likely to become insolvent, and where the court considers that an administration may achieve the survival of the company as a going concern and / or a more advantageous realisation of the company's assets. An application for administration can be made to the court by the company, the directors of the company, any member of the company, any creditor, the Guernsey Financial Services Commission or a liquidator of the company. Following the period after presentation of an application, no resolution may be passed to wind up the company and no proceedings may be commenced or continued against the company except with leave of the court. On the making of an administration order, any application for winding up of the company shall be dismissed and during the administration period, no resolution may be passed to wind up the company and no proceedings may be commenced or continued against the company.

The administrator shall, upon appointment, take into their custody or control all property of the company and shall manage the affairs, business and property of the company.

1.2 Informal restructuring procedures

While it is possible for a company to agree to an informal restructuring plan with creditors or members, there is no guideline for such a process in Guernsey.

2. Restructuring of ESG-related liabilities

2.1 Environmental (E): restructuring environmental liabilities

2.1.1 Types of environmental liabilities

The Environmental Pollution Law (Guernsey) 2004 states the obligations all parties must adhere to under prescribed law. Although there is no separate restructuring provision in company law, there are criminal liabilities that are incumbent on company directors for committing offences against this law.[1]

Where an offence under the law is committed by a body corporate or is proven to be committed with the consent or connivance of, or is attributable to neglect on the part of, a director, that director will be guilty of the offence and proceedings will commence.

2.1.2 Priority given to environmental liabilities

There is no priority given to environmental liabilities in Guernsey.

2.1.3 Disclaimer of environmental obligations

It is possible for liquidators in Guernsey to disclaim onerous property with effect from 1 January 2023.

Onerous property includes any personal property of a company, or any property situated outside of the Bailiwick of Guernsey which is unsaleable or not readily saleable or is such that it may give rise to a liability to pay money or perform any other onerous act. An interested party objecting to a disclaimer may apply to the Guernsey court.

2.2 Social (S): restructuring health or safety-related liabilities

There is no precedent or prevailing law for allowing health and safety liabilities to be restructured at present.

2.2.1 Types of health and safety-related liabilities

The Health and Safety at Work Law, enacted by the States of Guernsey, governs an employer's responsibility in the workplace.[2]

2.2.2 Treatment of health and safety-related liabilities

There is no precedent or prevailing law for allowing health and safety liabilities to be restructured at present, and these liabilities would not receive any special priority.

2.3 Governance (G): third party releases in favour of directors and officers of the company

If an arrangement and reconstruction is successfully implemented under the law then this will as a consequence provide a third party release in favour of directors and officers of the company, on the basis that the arrangement or reconstruction will avoid an insolvency process such as administration or liquidation and therefore will avoid any investigations into the affairs of the company and its directors and officers by an administrator or liquidator.

3. Protection of stakeholders' interests

3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

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1 The Environmental Pollution (Guernsey) Law 2004.

2 States of Guernsey Health and Safety Executive – Health and Safety at Work Law (1979).

3.1.1 *Approving a restructuring plan*

See the discussion in section 1 above.

3.1.2 *Discretion to consider wider public interest concerns*

The law relating to arrangement and reconstruction does not include any provisions regarding wider public interest concerns. The court has a discretion as to whether to sanction an arrangement and reconstruction, but in exercising this discretion, the primary focus is on the financial interests of creditors.

3.1.3 *Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There is no specific influence able to be exerted by these entities.

3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

There is no specific influence, however the court has discretion as to whether to sanction an arrangement and reconstruction.

3.2.1 *Approving a restructuring plan*

The court has a discretion as to whether to sanction an arrangement and reconstruction and it could consider employees' interests.

3.2.2 *Discretion to consider wider public interest concerns*

There is no specific influence, however the court has discretion as to whether to sanction an arrangement and reconstruction.

3.2.3 *Protection of employee rights*

Employee claims have preferential status in insolvency matters. In an arrangement and reconstruction, employees would likely form a separate class of creditors for the purpose of voting on the arrangement and reconstruction. Furthermore, the court will specifically take account of the interests of the various classes of creditors in deciding to whether to sanction an arrangement and reconstruction.

3.3 Governance (G): board / management conflicts addressed in a restructuring

The arrangement and reconstruction process in Guernsey does not address any issues of conflict regarding the board / management. The arrangement might propose the issuing of shares, depending on the circumstances. The existing management would typically remain in control of the company during a scheme of arrangement (unless of course an administrator, liquidator or receiver is already appointed and is the Applicant), with the process being overseen by the court.

The Guernsey Financial Services Commission (GFSC) provides a Code of Corporate Governance for the Finance Sector.[3] The Code sets out various responsibilities directors and the company have in terms of governance, accountability, conduct and ethics.

The section on ethics states:

- boards should establish, implement and maintain an effective conflicts of interest policy which sets out standards of expected behaviour, including, among other matters, the treatment of non-compliance with the policy;

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3 Guernsey Financial Services Commission (GFSC) Code of Corporate Governance – Finance Sector, February 2016.

- directors have a duty to avoid, manage or minimise conflicts of interest and should, wherever possible, arrange their personal and business affairs to avoid direct and indirect conflicts of interest; and
- directors have a fiduciary duty to act in the best interests of the company.

The governance section of the Code states:

- the board should have a clear governance structure which reflects the demands and complexities of the company's business environment, strategy, company values, standards, risk appetite, internal controls and key policies; and
- the board should collectively comprise an appropriate balance of skills, knowledge and competence, considering its members' relevant experience.

4. "Soft law" framework

4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There is no specific guidance, best practice or precedent for applying law regarding the protection of the environment in a restructuring.

The States of Guernsey have an Environment and Infrastructure Committee. However, there is no evidence of this Committee being involved in a restructuring process.

4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The States of Guernsey provide an employment relations portal of documents which governs many aspects of employment, and the responsibility of employers.[4]

There is a specific section for "handling redundancy", which details inadmissible reasons for redundancy and also offers practical guidance to employers, employees, trade unions and employee representatives. Employers should follow a checklist of procedures before finalising plans. In particular:

- if there is a trade union or employees' association, it should be consulted and kept informed of the situation;
- employees should be consulted over proposals to put in place a redundancy when these proposals are still at the formative stage;
- employees should be given adequate information and time to comment or make representations prior to any decision to dismiss being taken;
- employers should thoroughly consider any representations from employees before making any decisions; and
- notes should be kept of any meetings and discussions concerning redundancy.

[4] https://www.gov.gg/employmentrelations.

4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Under the law, there are no restrictions on who can be appointed as a liquidator or administrator in Guernsey. Unlike many other modern jurisdictions (such as England and Wales and Jersey), there is currently no register of approved insolvency practitioners and no requirement for licensing, professional membership, qualifications, residency or any form of insurance.

However, in relation to court appointments, the court will approve the appointment of the office holders and will typically expect them to be experienced and qualified professional insolvency practitioners. Such practitioners may therefore be members of a recognised professional body (such as the Institute of Chartered Accountants in England and Wales), which will have its own guidance on professional ethics and codes of conduct.

5. ESG in financing

5.1 ESG-linked loans, bonds or investments

75% of assets of regulated funds in Guernsey are managed or administered by firms adopting the UN Principles of Responsible Investment (PRI).[5] Additionally, the GFSC has launched the world's first green fund product, which provides a trusted and transparent product for investor access to green investment. The jurisdiction is also a member of the UN Financial Centres for Sustainability Network (FC4S).

Results of a recent survey show 64% of investment managers and fund administrators have seen increased interest in ESG, 93% are aware of Guernsey green finance initiatives and 85% are aligned, or are planning to be aligned with, ESG principles.

Currently, Guernsey's green finance sector is worth £5 billion, with plans to increase this to £56 billion by 2040. This allows Guernsey to have an outsized influence on the sector.

5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The biggest theme within Guernsey funds has been ESG investing, following on from the launch of the GFSC green fund product. Following this, The International Stock Exchange (TISE) created a sustainable finance sector, as well as a transition offering.

The sector as a whole has overwhelmingly responded to the transition and its financing, with investors looking favourably upon this.

5.3 Promoting ESG by central banks and regulators

As noted above, the GFSC has been market-leading in adopting the principles of the UN PRIs as well as launching the first green fund product in 2018, which continues to grow.

The GFSC continues to develop a green approach and demonstrate its commitment to develop climate finance through regulatory tools and support of the finance sector in its transition.

The GFSC is engaged with international regulators in order to develop awareness, understanding and capabilities on how to respond to climate-related risks, and continues to contribute to the development of standards.

As noted above, the GFSC is a member of FC4S, but also holds contributory memberships to:

- the Network for Greening the Financial System (NGFS);
- the Taskforce for Nature-Based Financial Disclosures Forum (TNFD);

[5] ESG, Green and Sustainable Investing report, Guernsey Green Finance, 2022.

- the Sustainable Insurance Forum (SIF); and
- IOSCO.

The GFSC will continue to promote and develop activity in this space.

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