CADWALADER

FFF Travels to the Channel Islands: An Introduction to Jersey and Guernsey

February 4, 2022 | Issue No. 161

Cadwalader has recently seen a growth in the number of funds formed in Jersey and Guernsey that are party to subscription and NAV facilities. Trent Lindsay and Cassandra Best spoke with [Julia Keppe], Senior Counsel at Walkers in Jersey, and [Zoë Hallam], a Group Partner at Walkers in Guernsey, to learn more about the fund finance market in the Channel Islands.

Julia Keppe and Zoë Hallam

FFF: Julia and Zoë, thank you again for speaking with us and for the crash course on Jersey and Guernsey funds. To kick things off, what are recent trends in fund formation and the fund finance market in Jersey and Guernsey?

JK: Thank you so much for inviting us! Delighted to be talking with you. In terms of trends, in the Channel Islands we are of course local counsel, and so the trends we see tend to track what is going on onshore. So I'm sure a lot of this will be very familiar to your readers.

ZH: Recently, and as you've mentioned, there has been a real uptick in our deals coming out of the U.S. We regularly work with European clients and instructing counsel; however, it has been great to increasingly see Jersey and Guernsey vehicles alongside U.S. vehicles on U.S.-originated deals. I spent eight years in Walkers' Cayman fund finance team before relocating to the Guernsey office in 2019, and it's good to be back working more frequently with my U.S. network.

JK: Yes, agreed. More generally, the number of funds and amount of capital committed in both jurisdictions is increasing. Jersey Finance reported that the value of the total funds business booked in Jersey grew by 15% over the first half of 2021, with the total value of fund assets reaching a new record level of £436.3 billion at the mid-year point. This was driven by private equity, growing by 24% over the same period.

ZH: The Guernsey Financial Services Commission has published Q3 stats for 2021. Net asset value of Guernsey funds increased 6.4% in the quarter and sat at £290bn at the end of it. Of that, £238bn sits in closed ended funds, which shows the importance of closed ended funds to the industry as a whole. To briefly touch on the fund finance space, the main trend we are seeing is a rise in the number of NAV facilities. We heard a lot of talk about NAVs in 2020 but didn't see them materialise until 2021. There is no doubt now they are a strong feature of the landscape, alongside traditional sub lines.

JK: Agreed again, and they seem to be becoming more complicated as well. Definitely not complaining, as it's great to be working on the complex fund finance solutions coming into the market.

ZH: And the market across both islands continues to be innovative − we are seeing crypto funds being set up over here, which is keeping the regulators busy! And the cannabinoid healthcare market has been an area of focus since the establishment of the first fund in Guernsey in 2020.

FFF: What are the advantages or disadvantages to forming Jersey and Guernsey funds from the perspective of a sponsor or a lender to funds?

ZH: The advantages of the Channel Islands are very similar to the advantages of some of the more traditional U.S.-facing offshore markets, such as the Cayman Islands. Broadly speaking, it is tax neutrality, a stable legal environment, and the presence of all the necessary professional advisors. More specifically, there is a light touch regulatory regime in both jurisdictions, where funds can be approved within 2 days in Jersey and 24 hours in Guernsey (not that it's a competition)! Marketing Channel Islands funds in the UK and Europe under AIFMD is also a well-trodden path, and can be much cheaper and quicker than some onshore jurisdictions.

JK: Interestingly, the finance bodies in Guernsey and Jersey are reporting an increased capital flow from the U.S. into Channel Islands funds, and back into the U.S. Perhaps unsurprisingly, more than two-thirds of the inwards investment in Guernsey is in private equity. While our timezone is convenient for European managers, investors and assets, I suppose for U.S. deals, the time difference can be a disadvantage in terms of liaising with administrators and directors, but certainly not insurmountable. The professional services industry is global in its outlook and used to dealing with all timezones.

ZH: In terms of lenders, in addition to Julia's previous points, there is certainty and stability in using the Channel Islands around security and contractual rights. In particular, there is a wide body of case law for disputes and enforcement, with ultimate recourse to the Privy Counsel (should it ever be required…).

FFF: ***Are there any material differences in the way capital call security is granted and perfected with respect to subscription facilities in Jersey and Guernsey, respectively? Is***

it possible to rely on New York law-governed security documents or is it necessary for local law documents to be executed, or both?

JK: In both Jersey and Guernsey, we would require local law-governed security over capital calls and bank accounts (assuming, of course, the accounts are located here). While there is no issue with also providing New York law-governed security, on enforcement, we would rely on the local security which will have complied with the local legislation on creation and perfection.

ZH: Yes, the base position of local law security is common to both islands, although there are differences between the two jurisdictions in creation and perfection. The main conversations we have with our lead counsel on this point revolve around notices to investors. In Guernsey, the position is clear: notices are required to create security; therefore, they are sent simultaneously with the entry into the capital call security agreement. However, in Jersey, notices are not required for the creation, perfection or priority of the security, so it becomes a commercial decision.

JK: Correct, and market practice does vary, though we do tend to see notices being sent, with more discussions around timings. I'm sure most people will be very familiar with that conversation! In addition, it is worth mentioning that Jersey (unlike Guernsey) has a public security interests register, so any Jersey law-governed security, regardless of the jurisdiction of the grantor, is registered here.

FFF: ***What about perfecting security with respect to collateral accounts based in Jersey and Guernsey? Do you have a concept similar to account control agreements?***

ZH: We don't tend to use control agreements in either jurisdiction. We have the concept of 'blocked' and 'unblocked' accounts. In subscription line facilities, the account is unblocked, until an event of default. Following this, the security agent can 'block' the account so that the borrower is no longer permitted to make withdrawals or give instructions to the account bank. In terms of what is signed on a closing, for priority purposes, the grantor and secured party will send a notice to the account bank, which is usually acknowledged the same day. This is always in the relevant account bank's standard form, and is a very well established process on both islands.

FFF: ***Are there any aspects of Jersey and Guernsey law that lenders taking security under an NAV facility over equity and debt interests held by funds should consider?***

JK: Not really. Jersey and Guernsey law is fairly similar to English law when it comes to taking security over equity and debt. Share certificates, stock transfer forms and annotated registers of members are required for perfection and priority purposes. Most often, issues arise where the constitutional documents of the underlying investments don't permit (or impose consent requirements on) the granting of security – but those issues are not unique to the Channel Islands!

ZH: Perhaps one thing to flag is the inability in Guernsey to take all asset security under Guernsey law (akin to a U.S. security agreement or an English debenture). So we need to identify each relevant underlying Guernsey situs asset and take specific security over that asset. Jersey is a little more flexible in that regard.

JK: Indeed, we do the have the ability to take security over all intangible moveable property located in Jersey, though generally we tend to see asset specific security (usually, shares, contract rights or bank accounts).

FFF*: *Are there any significant differences between Jersey and Guernsey law that affect the fund finance market?

ZH: Again, not really. As noted, both laws have a lot in common with English law, and English case law would be persuasive in our courts. While there are still differences with English law and also between the two jurisdictions, none that are really significant or would necessarily steer a sponsor towards one jurisdiction or the other. It's great to be able to say that both islands offer such a stable environment for funds and fund finance.

FFF*: *What do you think the year ahead will bring?

JK: Hopefully a continual expansion of the fund finance market which has been, as is well reported, so resilient over the past few COVID-affected years. We expect ongoing innovation of the products on offer, particularly in the NAV space. Sadly, travelling to Miami is not possible for myself or Zoë this year, but fingers crossed the summer FFA symposium in London will go ahead and we will be able to cross the Atlantic again next year. We are very much looking forward to that.