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Introduction and summary

1. The Government believes the time is right to move UK Green Investment Bank plc (GIB) into private ownership. This is a natural next step for the company now it has proved itself a successful commercial enterprise. The company's Board fully supports this move and has made clear how important it considers this is to enabling the company to deliver its ambitious green business plan and have a greater impact on green investment.

2. It makes sense for GIB investment to be funded by private capital where possible and to minimise the need for public funding. This will further help to demonstrate to investors that GIB’s business model of investing in green projects can be a profitable business and is not simply the preserve of government.

3. We are confident there is strong interest in acquiring a stake in GIB from a number of large scale institutional investors such as UK pension funds, infrastructure funds and sovereign wealth funds. Many of these investors do not currently invest in individual green projects. We expect GIB therefore to provide a vehicle for them to invest in a portfolio of renewable infrastructure projects, in some cases for the first time. This fits well with our policy aim that GIB should tap into new sources of capital and mobilise maximum private investment into green sectors.

4. The Government recently announced that as a necessary part of the privatisation process, we propose to use the Enterprise Bill to repeal the legislation on GIB contained in the Enterprise and Regulatory Reform Act 2013. This move is central to achieving one of our key aims: ensuring GIB can be re-classified to the private sector following a sale so it can have the freedom to borrow and raise equity without this impacting on public sector net debt (PSND). From our discussions with the Office for National Statistics (ONS) and HM Treasury and our assessment of the regulations, it is clear to us that even if GIB was no longer owned by Government, the current legislation on GIB is highly likely to be assessed by the ONS as constituting government control over GIB, preventing it from being re-classified to the private sector.

5. The Government recognises people will be concerned about what repealing the legislation means for GIB’s ongoing focus on green investment since there would no longer be a statutory requirement for GIB to first obtain the approval of the Secretary of State and Parliament if it wished to amend or revoke the green Objects clause in its Articles of Association – this being what requires GIB to invest only in projects that achieve green impact.

6. The Government has made clear it wants and expects GIB to continue to invest in green sectors following a sale, using its larger pool of funding to carry on mobilising more private capital for the purpose of further accelerating the transition to a green economy. Potential investors in GIB will have sound commercial reasons to maintain the company’s clear focus on green investment and its robust green values and principles. Green investment is what GIB does and is where its value lies. It is clear from preliminary feedback that potential investors are interested in GIB precisely because of its unique green specialism. They will be buying into the company’s
existing forward business plan and pipeline of green projects which demonstrates exactly how GIB expects to generate returns for investors.

7. And investors will be seeking to acquire the reputational benefits that arise from owning a company with GIB’s clearly stated green principles and highly transparent and robust green reporting practices.

8. In addition, as a key part of any sale discussions, potential investors will be asked to confirm their commitment to GIB’s green values and investment principles and to set out how they propose to protect them. The Government envisages this would involve new shareholders agreeing to:

   (i) Retain the green objectives in GIB’s Articles of Association;

   (ii) Ensure GIB continues to invest in a way that achieves a positive green impact; and

   (iii) Maintain GIB’s existing standards for reporting on its green investment performance as well as continue providing for independent assurance of this.

9. We expect bidders will be willing to make such commitments and that this will be effective in securing the outcome we want - that new shareholders effectively commit to maintaining GIB’s green values.

10. The precise form of commitments cannot be specified in advance. The Government needs the flexibility to explore the matter fully with investors and secure the most appropriate package.
Part One: GIB history and policy context

GIB design and set-up

11. The previous Government began work on establishing the UK Green Investment Bank (GIB) in 2010. The overriding policy aim was to increase the UK’s ability to meet its challenging environmental targets and commitments by getting more green infrastructure projects financed more quickly than would otherwise be the case.

12. An expert Advisory Group was established under the chairmanship of Sir Adrian Montague to explore the options and make recommendations on the detailed design and structure of the Bank. As the work to design and establish GIB progressed, it became clear that the most effective way for the company to contribute to achieving HMG’s primary aim of mobilising additional private investment in key green sectors was for it to operate as an infrastructure investment bank, providing finance on fully commercial terms alongside other commercial finance providers rather than acting as a Government funding platform providing soft loans and grants or investing in more speculative early stage technologies.

13. This fully commercial approach to investing in green projects was the only way GIB would attract co-investment from other mainstream private investors and encourage them to enter green sectors. Given the scale of the financing challenge, with £200 billion of investment needed by 2020, achieving this demonstration effect (demonstrating to the wider market that green investment can be profitable business and is not the preserve of Government) would be crucial. Government funding alone would not be sufficient to achieve the transition to a green economy.

14. It was agreed, therefore, that GIB’s role would be to be both green and profitable, using its sector specific expertise to assess the risks associated with green projects accurately and giving co-investors the necessary confidence to commit finance to projects. In this way GIB would help to overcome specific finance related market failures that stifle investment activity. It would mobilise additional private investment directly alongside it into the projects GIB supports, enabling co-investors to become more familiar with the technologies and risks involved in green sectors. And it would attract additional private investment into the relevant sectors through the demonstration effect: developing a successful portfolio of investments, proving the commercial case for investment in green sectors and generating confidence in the private sector that green investment can be a profitable business.

15. The detailed proposals for GIB were set out in May 2011 in a policy document on the design of GIB:
16. This document sought to explain why it was important for direct Government intervention through GIB to be targeted at specific situations and tailored to ensure maximum ‘additionality’ and minimum market distortion.

17. It set out how the company would operate as a commercial investor to deliver both green impact and profits so as to achieve the demonstration effect and attract additional private capital into green sectors. It sought to make clear that there were already other types of Government measures in place that were designed to support policy aims such as increased venture capital and promoting early stage pre-commercial technology development. GIB’s commercial investment activities were expected to complement these other existing policy measures.

18. The policy document stated the company’s operating principles would be on the following lines:

• Green objectives, sustainable finances: Working towards a ‘double bottom line’, deploying capital to achieve significant green impact whilst generating positive portfolio returns and in doing so, preserving and building its capital base.

• Enduring impact: Building a sustainable institution that delivers the long-term impact required by the UK’s transition to a green economy.

• Strategic alignment with Government: Aligning strategic priorities with Government green policy objectives and initiatives.

• Operational independence from Government: Putting management and operational decision making at arm’s length from Government.

• Partnership with the private sector: Operating in cooperation with private sector players, enhancing private sector provision and leveraging private sector capabilities where appropriate, and not acting where Government policy objectives could be met by private sector provision alone.

• Minimising distortions: Operating consistently with EU state aid rules, minimising inappropriate competition.

19. The document also made clear that GIB was being designed specifically with a view to a possible transfer of the company to the private sector in due course stating:

“The GIB will initially be owned by the Government and will operate as a separate institutional unit at arm’s length and with full operational independence. The GIB’s proposed governance model will be designed to allow for a possible eventual transfer of ownership from Government to the private sector of some or all of its activities”.

20. Four years on, both the Government and the company itself believe that effecting such a transfer into private ownership is the best way to ensure GIB is able to build on its success to date, giving it the freedom it needs to access much greater volumes of capital and have a bigger impact.
GIB Funding

21. GIB began operating independently of HMG in October 2012. It was allocated £3 billion to invest in the period to 2015. A further allocation of £800 million was made at the last Spending Round for the year 2015-16. To date, GIB has made commitments totalling £2.3 billion. Government will fund these and any further commitments GIB enters into during the current year to March 2016 in line with its business plan.

22. Further Government funding for GIB for 2016-17 period is being considered in the current spending review. Decisions will be announced shortly but we expect the settlement will allow for full funding of GIB to the point of majority sale, assuming a sale next year.

23. The question of how much further HMG funding will be needed in order to fund GIB’s business activity in subsequent years (anticipated investment rate of circa £700m - £800m per annum) is directly related to the question of what size stake in GIB is sold and will need to be considered in that context.

State aid, sector scope and nature of investment activities

24. Using Government money to establish a commercial enterprise such as GIB involves giving state aid to that enterprise which may distort the normal operation of the markets in which it operates. Such state aid must, therefore, be approved in advance by the European Commission which must satisfy itself the aid is justified and compatible with the objectives of the European Union in that any distortion of competition in markets is kept to a minimum and is necessary to achieve a specified policy benefit of common European interest.

25. Since the intention was that GIB should leverage other sources of finance and act as a demonstrator to other commercial investors, it would operate on the basis of making investments with a balance of risk and return that is commercially acceptable. State Aid approval was therefore sought and granted on the basis that GIB would be making investments in accordance with the Market Economy Operator (MEO) principle, meaning it may only invest on terms which would be acceptable to a commercial investor.

26. GIB is required to operate in accordance with its State Aid approval including the principle of additionality which restricts it to invest only in projects where its involvement can be demonstrated to be necessary. This requirement means that GIB must withdraw from a project if the process of assessing the investment opportunity results in the project being able to attract sufficient funding from private investors. Applying this principle makes sense while GIB is investing with public money since there is no point using HMG capital to finance projects that would have happened anyway.

27. The need to demonstrate compliance with the principle of additionality would fall away if GIB was no longer subject to state aid approval. But this does not mean GIB will crowd out private investors. Investing with private capital, GIB will be adding to
competition in the market for finance and helping to drive down the cost of capital to green projects.

28. We expect interest in acquiring a stake in GIB to come from large scale institutional investors such as UK pension funds, infrastructure private equity funds and sovereign wealth funds. GIB has already successfully attracted similar investors into its managed fund for investment in Offshore Wind. Many of these investors do not currently invest in individual green projects themselves. Allowing them to acquire a stake in GIB will provide a vehicle for them to invest in this area for the first time - through GIB’s portfolio of renewable energy and green infrastructure projects.

29. A sale of GIB therefore enables this new pool of capital to be crowded in and brought to bear in investing in green sectors where the need for additional finance remains extremely high. GIB will continue to co-invest in projects alongside other infrastructure investors.

30. Operating in accordance with a state aid approval also means GIB is restricted to operate within specified sectors where the European Commission has accepted that specific market failures restrict the availability of finance. GIB considers there are a number of additional sectors where it could make an important impact if it was not so constrained (for example in the area of low carbon transport). And a state aid approval must be reviewed and renewed by the European Commission every 4 – 5 years to ensure the case for the state aid remains justified, meaning the funding and operation of GIB is always subject to obtaining the necessary clearance and a finite time period.

Focus on established, “investment ready” technologies

31. As explained in the May 2011 policy document, the key policy aim was that GIB’s activity should increase the UK’s ability to meet its challenging environmental targets and commitments. GIB’s strategic focus should therefore be on sectors and projects that are capable of having an early impact on carbon reduction and waste diversion. This has meant GIB has focused on technologies ready for deployment at full commercial scale and capable of attracting additional investment from mainstream finance providers. These finance providers would not typically be interested in participating in more high risk projects and early stage technologies with less certain or less robust commercial returns realised over much longer periods. Alternative and separate policy mechanisms were and are in place aimed at delivering policy goals in these areas.

32. Government funding in this space is provided for private sector led technology R&D through grants, procurement approaches and to a lesser extent equity interventions. Additionally, DECC, Research Councils and InnovateUK are involved in European programmes that can leverage significant funding from the EC while ensuring cross border collaboration.

33. Government spent ~£1.3billion on low carbon innovation for the period 2011-15. In addition, the Low Carbon Networks Fund which is funded by network operators is expected to allocate ~£440m over the period 2010-15. See table 1 below:
Table 1
Government low carbon innovation spend 2011-15 £m

34. Separately, the British Business Bank has three main programmes for supporting early stage technology investment, including in the clean technology area: the Enterprise Capital Funds targeted at early stage venture capital investment; the UK Innovation Investment Fund (UKIIF) which supports creation of viable investment funds targeting UK high growth technology-based businesses; and the Venture Capital Catalyst Fund, launched in 2013.

35. These types of activity do not fit with the original policy aims for GIB as set out in May 2011 and do not, therefore, fit with GIB’s existing operating model (and they are outside the terms of GIB’s State Aid approval). Offering concessionary finance would reduce GIB’s ability to achieve its green and profitable mandate and deliver its aim of mobilising much needed additional private capital into green sectors through a ‘demonstration effect’ to commercial investors.

36. The Government believed and continues to believe that this is the most effective role GIB can play: operating in green sectors that while relatively mature, nevertheless suffer from a lack of investment. It is in this more established infrastructure end of the market that the company’s expertise lies.

GIB today

37. After three years of operation and well over 50 investments, GIB has developed a good track record as an investor in green sectors with a healthy portfolio of assets (both in terms of sector and product) and a good balance of risk and reward earning a circa 10% return. In 2014-15, it entered year-on-year profitability and expects to maintain this position. This has resulted in the position that GIB is now able to attract equity investment from the private sector.

38. To date, GIB has committed £2.3 billion to 58 projects across a range of sectors mobilising an additional £7.8 billion of private capital to projects both in operation and
construction – more than £3 of additional private capital for every £1 of Government money invested.

39. Investor attitude surveys show that GIB has become a credible investment partner, capable of attracting other finance providers to relevant projects and sectors through the demonstration effect and the skills and expertise its specialist teams possess. GIB has also been innovative in developing novel finance structures to enable investment in energy efficiency, establishing funds for investment in operating offshore wind assets and financing projects that use novel technologies for the UK.

40. Routine monitoring and feedback activity shows that establishing GIB as an investment bank investing on fully commercial terms has been successful in achieving the main objective we had for it: tackling a lack of liquidity in green sectors. In particular it has helped to unlock private investment in the offshore wind sector (a key part of our aims for a low carbon energy mix), invested in innovative projects (e.g. new larger turbines in Westermost Rough OSW farm) and attracted new sources of capital into green sectors: investors that had not previously invested in this area in the UK (e.g. US private equity investor KKR and a number of UK pension funds).

41. The company has also developed a world leading approach to assessing, monitoring and reporting on the green impact of its investments. Full details can be found on the company’s website at: http://www.greeninvestmentbank.com/green-impact/. Detailed information on the green impact of the company’s portfolio of investments is also published annually as part of GIB’s annual report. GIB has also published a Green Investment Handbook with the aim of encouraging other investors to adopt similar high standards in assessing the green impact of investments.

42. At its outset, GIB was able to recruit a top class team to a new flagship institution which had access to £3bn of capital for the next three years. The collection of suitably motivated and skilled people in a securely-funded institution with a singularity of purpose is what makes GIB successful. Three years on, the company needs an up-to-date, compelling vision for the future of the company to continue attracting, retaining and motivating staff. Bringing in private capital is key to that updated vision.

43. The company also needs certainty about its future funding. The most effective way to secure this is to attract private capital into the company enabling it to access a much larger pool of capital from a wider range of sources than it would in Government ownership and removing the uncertainty attached to its current funding arrangements which are dependent on the spending decisions and limitations of government and state aid permissions.

44. The Board of GIB has sought to make clear it remains fully committed to its Edinburgh Headquarters. Edinburgh is where the Board is based as well as much of the company’s senior expertise. We see no reason to believe new owners would seek to challenge this position.
Part two: Plans for bringing private capital directly into GIB

Previous statements on moving GIB into private ownership

45. The Government’s May 2011 update paper on the design of GIB explained that GIB was being designed specifically with a view to an eventual transfer into private ownership.

May 2011 Update on the design of the Green Investment Bank

“The GIB will initially be owned by the Government and will operate as a separate institutional unit at arm’s length and with full operational independence. The GIB’s proposed governance model will be designed to allow for a possible eventual transfer of ownership from Government to the private sector of some or all of its activities.”

46. The Government first announced it was to begin working on plans to attract private capital into GIB in the 2013 Autumn Statement.

Autumn statement 2013

“As set out in the National Infrastructure Plan 2013, the government has now identified further assets with the potential for sale and the target for the sale of corporate and financial assets will be increased from £10 billion to £20 billion between 2014 and 2020. This includes (subject to value for money assessments and key policy objectives):

- a central estimate of approximately £12 billion expected from the sale of the income contingent repayment student loan book over the target period
- additional assets identified for sale, which potentially could include London and Continental Railways (LCR) property assets and the government’s shareholding in Eurostar
- considering options to bring private capital into the Green Investment Bank to enable it to operate more freely in delivering its objectives”

47. The Government re-iterated it was taking forward work on this in both the 2014 Autumn Statement and 2015 budget debate.

Autumn statement 2014

“The government is also working to bring private capital into the Green Investment Bank through a new fund for private investment in operational offshore wind assets and wider options. The government will report on progress at Budget 2015”
SofS for Business: 19 March 2015: House of Commons debate on the Budget

“I will finish with an announcement in response to a question that the Leader of the Opposition threw out yesterday about the Green Investment Bank. We have agreed that that is a successful initiative that stimulates private investment, and for £2 billion from Government there has been £3 billion extra from the private sector. We want to build on that success and are looking at a range of options for bringing private capital into the Green Investment Bank, and to give it greater operational freedom and enable it to borrow in capital markets. That will provide it with an alternative channel of funding, and ensure its future as a lasting and enduring institution.”

48. Then in June 2015, following receipt of advice on the prospects for a sale of shares in GIB from our financial advisers, Bank of America Merrill Lynch, who had been appointed in January 2015, the BIS Secretary of State announced firm plans to move GIB into private ownership. He set out the proposals in a written Ministerial Statement (text provided below) as well as in a speech to the GIB annual review event the same day (text available at: https://www.gov.uk/government/speeches/the-future-of-the-green-investment-bank).

Secretary of State for Business: 25 June 2015: House of Commons written ministerial statement

“In the debate on the Budget in March, the then Secretary of State for Business updated Parliament about work to explore options for bringing in additional capital into the Green Investment Bank (GIB) as a way to ensure it is an enduring institution and has the operational freedom for investment across the green economy. We have therefore been exploring options for how best to get that capital and, with my Right Honourable Friends the Secretary of State for Energy & Climate Change and the Secretary of State for the Environment, Food & Rural Affairs, we have concluded that the best approach is to move GIB into private ownership subject to ensuring we achieve value for money. This should bring a number of important benefits, giving GIB greater freedom to operate across a wider range of green sectors in accordance with its green purposes, which are enshrined in legislation.

It has always been our intention that GIB should leverage the maximum amount of private capital into green sectors for the minimum amount of public money. Moving the company into private ownership is a natural development for GIB that further delivers this aim. Our aim is that a transaction should result in GIB no longer being classified as a public sector body. This would mean GIB would be free to borrow capital so as to achieve its business ambitions without this having an effect on public sector net debt.

The detail and timing of any transaction will be set out in due course.”
49. This announcement was welcomed by GIB Chairman Lord Smith of Kelvin who stated in an article in the Sunday Times on 28 June 2015:

“I welcome this. You can’t keep going back to the government for more and more money. If we want to build something that is sustainable and durable, we need private capital. This was always going to happen”

50. It was separately welcomed by GIB Chief Executive Shaun Kingsbury stating in an article in BusinessGreen of 2 July 2015:

“That is why I believe the decision announced by the Business Secretary [privatisation] is the right one. It is the option that gives us the best chance of creating the greatest green impact.”

51. In October, at an event organised by the Aldersgate Group to mark the third anniversary of GIB’s launch, Bob Wigley, former Chair of the Green Investment Bank Commission which was the group originally tasked by the Chancellor in 2010 with developing proposals for a green investment bank, also commented on the plans for privatisation, saying that “the purpose and activities of the bank are well established and likely to continue in the same vein”. He also noted that private ownership would enlarge GIB’s capital base and enable it to borrow.

52. The Secretary of State’s 25 June announcement was followed in October 2015 with a further update on progress and an explanation that the Government would be repealing the GIB legislation in the Enterprise & Regulatory Reform Act 2013 to ensure GIB can be reclassified to the private sector following sale of a majority of shares.

**Secretary of State for Business: 15 October 2015: House of Commons written ministerial statement**

“My written statement of 25 June provided an update on work to move UK Green Investment Bank plc (GIB) into private ownership. It was always our intention that GIB should mobilise maximum private investment in the green economy. This reflects our policy aim of getting the market to work in tackling green policy challenges.

Bringing private ownership directly into GIB is part of this aim and a natural next step for the company now it has proved itself a successful commercial enterprise capable of operating with private sector capital rather than relying on public funding for its investments. It will allow the bank to access a much greater volume of capital than would be the case if GIB were to remain in Government ownership meaning it can grow its business, move into a wider range of sectors and have greatest possible impact in mobilising investment so that more green projects get financed more quickly than would otherwise be the case. The plans have the full support of the company and its independent Board, including Chair, Lord Smith of Kelvin.

As I said in my previous statement, a key objective in moving the company into the private sector is that it should be free to borrow and raise capital
without this affecting public sector net debt. Giving GIB this freedom is essential if the company is to invest in accordance with its ambitious green business plan.

It is now clear that to achieve re-classification of GIB as a private sector enterprise, we need to remove the public sector controls imposed on the company by the Enterprise and Regulatory Reform Act 2013. Unless we remove these controls, there is a real risk GIB would remain classified to the public sector even after a sale so would remain subject to Government control over its capital raising. This unintended effect of the legislation has only become apparent in the course of our work to facilitate GIB’s transition into the private sector.

In view of this, as a necessary part of the privatisation process, we now propose to use the Enterprise Bill, through an amendment shortly to be tabled at the Lords Committee stage, to repeal the relevant sections of the Enterprise and Regulatory Reform Act 2013 relating to GIB.

I recognise that in taking this step, people will wish to be assured GIB will nevertheless continue to invest in green sectors as Parliament envisaged. I wish to make clear that the Government also wants and expects a privately owned GIB to continue this clear focus on green sectors - mobilising more private capital and further accelerating the transition to a green economy.

It is clear from preliminary feedback that potential investors are interested in acquiring a stake in GIB precisely because of its unique green specialism and its green focused business plan. As part of any sale process, we would expect potential investors to confirm their commitment to GIB’s green values and to set out how they propose to ensure these are protected.

I will provide further updates about the transaction as soon as possible.”

53. In response to this announcement, GIB Chairman Lord Smith of Kelvin said:

“GIB has ambitious plans to double the size of our businesses over the next three years and expand into new parts of the UK green economy like energy storage, heat networks and low carbon transport. To do this we need to secure a long-term funding plan based on new investors and the ability to borrow. We can only achieve that if GIB is de-classified as a public sector body, which is the intention of the legislation proposed by the UK Government.

GIB is a global centre of expertise in green investment. Our green mission has defined our business model, it motivates our team and it will attract new investors. We will work with the Government to make sure that the mission, and the policies and procedures that underpin it, continues to play as big a part in the future of the organisation as they have in its past.”
Project governance

54. Robust project governance arrangements are in place reflecting that Ministers at the Department for Business Innovation & Skills (BIS) and the BIS Accounting Officer are accountable for the final decisions on a sale. There is a Steering Group involving senior officials from BIS, HMT and DECC and this group has an overall responsibility and accountability for delivering the project to meet HMG objectives. This Group is chaired by the official designated as senior responsible owner (SRO) of the project.

55. The project team within the Shareholder Executive in BIS (ShEx) has responsibility for working level, day-to-day delivery across all project workstreams. BIS is receiving financial advice on the project from Bank of America Merrill Lynch and legal advice from Herbert Smith Freehills. GIB is receiving its own separate financial advice from UBS and legal advice from Slaughter & May. This ensures that GIB and BIS are independently advised and protects against any proprietary issues arising.

56. ShEx is working on the project in close consultation with GIB and its board of directors, seeking their views as appropriate on matters of mutual interest. The aim is to conduct the sale process as expeditiously as possible and in a manner that will minimise disruption to GIB and its management, employees, customers and suppliers.

Informal market testing

57. Our aim is to generate interest in acquiring a stake in GIB from the widest possible number of credible potential investors to create a rigorous, competitive dynamic in the sale process and ensure we secure highest value from a sale. BIS has conducted an extensive pre-marketing exercise with sovereign wealth funds, long term institutional investors, pension funds and insurance funds based in UK, Europe, North America, Middle East and Asia.

58. GIB has already successfully attracted such investors into its managed fund for investment in Offshore Wind and other investments. An Information Memorandum will be issued to prospective bidders in due course.

Nature and timing of a transaction

59. We intend to sell a majority stake. This is important to achieve our objective of enabling GIB to be re-classified to the private sector. Decisions on the size of stake to be sold will depend on the outcome of discussions with potential investors and will be driven by what best achieves value and is in the best public interest. We need to retain flexibility about this matter in order to take into account the full range of relevant considerations, including the requirements of declassification and any future Government funding commitments.

60. While we are exploring all options for a sale, GIB is not yet at a scale that makes it suitable for sale through an Initial Public Offering. The current focus for GIB is to achieve growth. This will require significant new capital annually, requiring regular
cash calls from investors and precluding an acceptable level of regular dividends in the short term.

61. Preparation work on the sale process is ongoing. The timing of the sale is dependent on the outcome of discussions with potential investors. We will only proceed once satisfied we are able to achieve best value for money for the taxpayer.
Part Three: Re-classifying GIB to the private sector

Need to remove state control to achieve re-classification

62. One of the key objectives of moving GIB into private ownership is for it to be re-classified as a private sector company rather than a public sector body. This is essential to give GIB the freedom to borrow without this impacting on public sector net debt (PSND), but more importantly to allow it also to raise equity. If GIB continued to score to the Government’s balance sheet, any equity raised by GIB (once invested by them) would also score to PSND, as it is treated as if the private sector is providing the Government with further capital.

63. The decision on whether an organisation is classified to the public or private sector is made by the Office for National Statistics (ONS) and is considered in accordance with EU-wide regulations, set out principally in the European System of Accounts 2010 (ESA 2010) and supplemented by guidance in the accompanying “Manual on government deficit and debt” (MGDD).

64. The fundamental question to address in determining whether an organisation is classified to the public or private sector is whether the government exercises significant control over the general corporate policy of that organisation. In making its decision, ONS will look at a number of indicators of government control as set out in ESA 2010. These indicators include any legislation specific to the organisation and any other special rights the Government has which would similarly have the result of enabling the Government to exert control over the organisation (e.g. special shareholder rights to block special resolutions of the company or otherwise exercise a veto).

65. A single indicator may be sufficient to establish control, but, in other cases, a number of separate indicators may collectively indicate control. It is not the form of control but the effect which is important. In making its assessment, ONS will therefore look at all of the relationships government has with the organisation.

66. As part of the work on moving GIB into private ownership, BIS officials have consulted HM Treasury and have had substantive discussions with ONS about the classification of GIB following a sale of a majority of shares. ONS has been very helpful in engaging with us and explaining how the regulations would apply in the case of GIB following a sale. However, it should be understood that ONS would only be in a position to take a substantive decision on GIB’s classification once a transaction has actually taken place.

67. From our discussions with ONS and HM Treasury and our assessment of the regulations, it is clear to us that even if GIB was no longer owned by Government, the legislation on GIB in Part One of the Enterprise and Regulatory Reform Act 2013 is highly likely to be assessed by the ONS as constituting government control over GIB, preventing it from being re-classified to the private sector.
68. This assessment is what lies behind our conclusion that the legislation on GIB would prevent the company’s declassification and, therefore, must be repealed.

69. The Government fully appreciates that many will be concerned about this move since repealing the legislation will mean there is no longer a statutory requirement for GIB to first obtain the approval of the Secretary of State and Parliament if it wished to amend or revoke the green Objects clause in its Articles of Association. It is this green Objects clause that requires GIB to invest only in projects that achieve green impact. Had it not become clear this was a necessary, practical step to achieve our ambitions for GIB, the Government would have been content to leave the legislation in place.

Why compensatory forms of control may not be imposed

70. A number of MP’s, Lords and stakeholders have queried whether some other form of non-statutory control could be introduced to compensate for the legislative controls that are being repealed. As noted above, ONS will take into account all indicators of government control in assessing whether an organisation is classified to the public or private sector, and it is the effect and not the form of control which is important. It follows that it is not feasible simply to replace a control provided for in legislation with some other form of unique right that allows the Government to exert control over the company. Any such new form of control would be assessed in the same way and have the same effect of preventing GIB from being re-classified to the private sector.

71. Others have queried why it is possible to impose conditions on companies that operate in regulated sectors such as postal services, telecommunications or energy without these being classified to the public sector. The distinction is that in such sectors, it is the market concerned that is subject to regulation, rather than specific companies who choose to operate within the regulatory constraints that apply to the sector. This is different to a situation where government is granted unique rights to exert control over the corporate policy of a specific organisation.

72. Furthermore, this is also different to cases where a specific company like Royal Mail is designated as the “universal service provider”. Firstly, the whole mails market is subject to regulation. Secondly, there is nothing to stop Royal Mail from undertaking other non-universal service or non-mails activities, and there is nothing from a regulatory perspective that prevents Royal Mail from changing its Articles. Finally, under certain circumstances, Ofcom can designate one or more companies to act as a universal service provider.

73. Imposing regulation on GIB specifically as an alternative to the statutory provisions of the ERRA 2013, but which has the same effect, would still constitute Government control, including “control through excessive regulation” as set out in the MGDD guidance.

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1 The clause on repealing the legislation had to be introduced as a Government amendment to the Enterprise Bill because the position on this matter only became clear after the Bill had been introduced.
Part four: Maintaining GIB’s green values

GIB’s green remit

74. As noted above, the proposal to repeal the legislation relating to GIB, has led to questions and concerns about what this will mean for GIB’s focus on green investment.

75. GIB’s Articles of Association include a green Objects clause that requires GIB to invest only in a way that achieves at least one of five specified green purposes:

- The reduction of greenhouse gas emissions;
- The advancement of efficiency in the use of natural resources;
- The protection or enhancement of the natural environment;
- The protection or enhancement of biodiversity;
- The promotion of environmental sustainability.

76. Repealing the legislation does not itself alter this Objects clause. However, it does remove the statutory requirement that GIB must first obtain the approval of the Secretary of State and Parliament if it ever wished to amend or revoke the Objects clause. Removing this state control is essential to enabling GIB to be re-classified to the private sector. In the absence of this, it is reasonable to ask what basis there is to believe GIB would continue to invest in accordance with its current robust green principles and values.

Commercial case for retaining green focus

77. In his two written statements on this matter, the BIS Secretary of State sought to make clear the Government wants GIB to continue to perform its important role of mobilising more private capital into green sectors and further accelerating the transition to a green economy.

78. The main form of protection of GIB’s green remit arises from the commercial reality that GIB has been established as a green infrastructure investment company and that is what investors would be buying. The company has sought to make clear its continued commitment to its robust green values and investment principles and that it plans to continue to invest in accordance with its established green business plan.

79. It is also clear from preliminary feedback that potential investors are interested in GIB precisely because of its unique green specialism. They will be buying into the
company’s existing forward business plan and pipeline of green projects which demonstrates exactly how GIB expects to generate returns for investors.

80. And many investors will be seeking a stake in GIB specifically in order to introduce a low carbon, green element to their investment portfolios and, as part of that, will wish to acquire the reputational benefits that arise from owning a company with GIB’s clearly stated green principles and highly transparent and robust green reporting practices. We have every reason to believe potential investors will have sound commercial reasons to maintain GIB’s green focus and values.

81. We see no reason to consider investors would buy into this business unless they were actively seeking to acquire a specialist green investment vehicle. There seems no commercial rationale for buying into this unique company with the intention of transforming it into something different. If the aim was to acquire a general infrastructure investor, investors could simply buy into an alternative investment vehicle.

Assurances Government will seek

82. Nevertheless, there is a second form of protection that can be implemented through the sale process itself. The Government intends that, as a key part of any sale discussions, potential investors will be asked to confirm their commitment to GIB’s green values and investment principles and to set out how they propose to protect them. We envisage this would involve new shareholders agreeing to:

(i) Retain the green objectives in GIB’s Articles of Association;

(ii) Ensure GIB continues to invest in a way that achieves a positive green impact; and

(iii) Maintain GIB’s existing standards for reporting on its green investment performance as well as continue providing for independent assurance of this.

83. The Information Memorandum being issued to prospective investors includes text on this matter. The relevant section of text is attached at Annex A. We fully expect all bidders will be willing to make such commitments and that this will be effective in securing the outcome we want - that new shareholders effectively commit to maintaining GIB’s green values. The precise form of the commitments cannot be specified in advance – we need the flexibility to explore the matter fully with investors.

84. It should be understood that it is not open to the Government to impose binding conditions on future owners of GIB requiring them to act in a particular way. We have tested this matter with ONS and are satisfied that, whatever form such binding conditions might take (golden shares, powers of veto etc), they would have exactly the same effect as the legislation: the Government would continue to be deemed to exercise control over the company even after a sale meaning GIB could not be re-classified to the private sector.
Conclusion

85. The Government is satisfied that moving GIB into private ownership is the right step to take and that now is the right time to introduce private capital. This is fully in line with our original plans for GIB and has the full support of the company and its independent Board. It will give GIB the freedom it needs to grow in line with its ambitious green business plan, enabling the company to access much larger pools of capital than it would if it remained in Government ownership and also to mobilise more private investment into a wider range of green sectors.

86. To achieve the benefits of private ownership, we need to ensure GIB can be re-classified to the private sector following a sale so that it is no longer on the Government’s balance sheet. It has become clear that GIB can only be re-classified as a private sector enterprise if it is free from significant state controls over its corporate policy such as are provided for in the legislation and is able to operate like any other private company. This means repealing the legislation on GIB and ensuring no other specific forms of control are put in place that would have the same effect of enabling the state to exercise control over the company’s business.

87. Repealing the legislation on GIB does not mean GIB will lose its clear focus on investment in green projects and sectors. Green investment is what GIB does and is where its value lies. As we have sought to make clear, the UK Government’s intention is that GIB should continue to focus on green sectors and retain its important role in further accelerating the UK’s transition to a more sustainable, low-carbon economy.

88. In this context, it is important that we identify credible investors in GIB who will make an enduring commitment to upholding the company’s established approach to green investment and reporting.

89. It is clear from preliminary feedback that potential investors are interested in GIB precisely because of its unique green specialism and business plan and we fully expect potential investors to maintain GIB’s green focus and values. As a key part of any sale discussions, they will be asked to confirm their commitment to these values and to set out how they propose to protect them.
ANNEX A

Text on commitment to green to be included in Information Memorandum issued to prospective investors

**GIB’s continuing commitment to green investment**

It is the intention of the UK Government that the GIB group should continue to focus on green sectors, mobilising more private capital and further accelerating the UK’s transition to a more sustainable low-carbon economy.

It is important to the UK Government to identify credible investors who will make a commitment to upholding GIB’s green focus and values and to its established approach to green investments and reporting.

As a key part of any sale discussions, potential investors will be asked to confirm their commitment to these values and to set out how they propose to protect them. Bidders’ stated intentions will be taken into account in the overall assessment of bids.

As part of this, the UK Government envisages that the new shareholder(s) will agree to the continuing inclusion of the Green Objective in the Articles of GIB group companies and to the maintenance of GIB’s green focus and values as exemplified by its Green Investment Principles.

The UK Government also expects new shareholders will agree to maintain GIB’s existing standards for reporting on its green investment performance as well as continue providing for independent assurance of this.