Memorandum

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to

Mr. M. Bednall
Mr. P. Lane

from

Prof. dr. E.J. van Praag M. Jur. (Oxon)
Mr. P.B. Hoefnagels LLM

subject

SFDR legal analysis Jacobi Decarbonised Bitcoin ETF

date

8 March 2023

1. Introduction and executive summary

You (**Jacobi AM**) asked us to answer the following questions in relation to the Jacobi Decarbonised Bitcoin ETF (**the Fund**) to be listed shortly at Euronext in the Netherlands:

Question A: Can a fund qualify as art. 8 SFDR[1] if it is investing in a carbon dioxide emitting product/activity, namely Bitcoin, but is 'compensating for the negative externalities'?

Answer A: **Yes.**

Question B: Is the SFDR applicable to the Fund given it is domiciled in Guernsey and listed at Euronext in the Netherlands?

Answer B: **Yes.**

Question C: Even if the SFDR is not applicable, can you still claim art. 8 SFDR?

Answer C: **Not relevant, since Sigma Guernsey falls under the scope of SFDR.**

Question D: Can you give the Fund the name **'Jacobi Decarbonised Bitcoin ETF'** (based on the draft ESMA Fund Name Guidelines[2])?

Answer D: **We find it defendable to argue that the name 'Jacobi Decarbonised Bitcoin ETF' can be used, as it describes exactly what the Fund does.**

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[1] Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector

[2] ESMA 18 November 2022, Consultation Paper on Guidelines on funds' names using ESG or sustainability-related terms (**the Guidelines**).

Our memorandum is based on the facts as provided by you, which sources are listed in **Annex I**. For further details, we refer to the below paragraphs in this memorandum.

Please note that the draft MiCA requires from the European Commission to draft a report and where appropriate accompanied by a legislative proposal in which it addresses amongst others: "*a description of developments in business models and technologies in the crypto-asset market with a particular focus on the environmental and climate impact of new technologies, as well as an assessment of policy options and where necessary any additional measures that may be warranted to mitigate the adverse impacts on the climate and environment of the technologies used in the crypto-assets market and, in particular, of the consensus mechanisms used to validate crypto-asset transactions;*". The expected timing is not before December 2026. So you will need to monitor this, but only on the long-run.

2. Background and facts

Jacobi AM as promotor of the Fund wants to add a decarbonisation element to the Fund. To decarbonize the Bitcoin held by the Fund, Jacobi AM wants to buy Renewable Energy Certificates (**RECs**) for the estimated energy usage of the Funds' Bitcoin holdings. Jacobi AM will buy RECs on behalf of the Fund in order for the Fund to be able to claim renewable energy usage for the Fund's Scope 3 GHG emissions. By doing this, Jacobi AM wants to market the Fund as an art. 8 fund under the SFDR.

3. Classification of financial products under art. 8 SFDR

In our view, it is possible to classify a fund as art. 8 under the SFDR when it is investing in a carbon dioxide emitting product/activity but it is compensating for the negative externalities. We explain this below.

3.1. Art. 8 under the SFDR

Art. 8 products under the SFDR are financial products that promote environmental or social characteristics (or a combination of those characteristics).[3] The SFDR does not detail what is meant by the 'promotion' of 'environmental or social characteristics'.

According to the European Commission (**EC**), art. 8 of the SFDR remains neutral in terms of design of financial products:[4]

[3] When the investments are in companies, those companies must follow good governance practices. This 'good governance' criterium does not apply to other types of investments, not being companies. See EC Q&A 25 May 2022, p. 8.
[4] EC Q&A July 2021, p. 7-8.

> *"It does not prescribe certain elements such as the composition of investment or minimum investment thresholds, the eligible investment targets, and neither does it determine eligible investing styles, investment tools, strategies or methodologies to be employed."*

Art. 8 products can in fact use various types of practices and strategies to attain the environmental (or social) characteristics it promotes. As the EC explains:[5]

> *"Therefore, nothing prevents financial products subject to Article 8 of Regulation (EU) 2019/2088 not to continue applying various current market practises, tools and strategies and a combination thereof such as screening, exclusion strategies, best-in-class/universe, thematic investing, certain redistribution of profits or fees. (…)"*

> *"Financial products that fall under <u>Article 8 may pursue reduction of negative externalities caused by the underlying investments</u>, such as principal adverse impacts on sustainability factors (…)"*

It is clear from the above that financial market participants (such as fund managers) have a lot of room for interpretation by which they may classify their financial products as art. 8.

Importantly, in our view, the EC clearly explains that financial products that pursue the reduction of negative externalities caused by the underlying investments, such as GHG emissions, can qualify as art. 8 products.

As a sidenote, art. 9 products are products that have sustainable investment as their objective. Sustainable investments include investments into environmentally sustainable economic activities. The investments also may not do significant harm to any social or environmental objectives. According to the EC, art. 9 products may invest in a wide range of underlying assets, provided these underlying assets qualify as sustainable investments.[6] Hence, it is much harder to classify as an art. 9 fund compared to an art. 8 fund.

3.2. Application to the Fund

In our view, it is possible to classify the Fund as an art. 8 product under the SFDR when it compensates for the carbon impact of its Bitcoin holdings by purchasing RECs.

The EC has made it clear that art. 8 products may pursue the reduction of negative externalities of its underlying investments. Furthermore, fund managers have a lot of room for interpretation by which they may classify their funds as art. 8.

In relation to the Fund specifically, the GHG emissions of its Bitcoin holdings (e.g. the negative externality) will be reduced / compensated by the purchasing of RECs. As we understand from you, by purchasing the

[5] EC Q&A July 2021, p. 8.
[6] EC Q&A July 2021, p. 5; EC Q&A 25 May 2022, p. 7.

RECs the Bitcoin holdings of the Fund are effectively decarbonized due to the fact that RECs represents the environmental attributes of the generation of energy produced by renewable sources. Hence, the environmental characteristic the Fund tries to attain and promotes, is the neutralization of the carbon impact of its underlying Bitcoin holdings through the purchase of RECs.

4. Application of the SFDR to non-EU AIFMs

The SFDR does apply to Sigma Guernsey, as it is registered by the AFM as an Alternative Investment Fund Manager (**AIFM**) from a designated state and the Fund as an Alternative Investment Fund (**AIF**) as is apparent from the AFM register. We explain this below.

The SFDR itself by its text applies to AIFMs, but is not clear on whether it also applies to 3rd country funds marketed in the EU. The EC however has explained that the SFDR applies to non-EU AIFMs who market their funds in the EU. Specifically, the EC refers to non-EU AIFMs who market funds / enter the market on the basis of national laws set out in National Private Placement Regimes:[7]

> *"(…) access to end investors in individual Member States may be on the basis of national laws set out in National Private Placement Regimes. Where an AIFM from a third country enters the market of a given Member State by means of a National Private Placement Regime, that AIFM must ensure compliance with Regulation 2019/2088, including the financial product related provisions."*

In our view, Sigma Guernsey falls within the scope of the SFDR as it markets the Fund in the Netherlands under the Dutch Designated States Regime.[8] This is because the EC has made clear that AIFMs that market funds in the EU on the basis of national laws also fall within the scope of the SFDR.

5. ESMA Fund Name Guidelines

Jacobi AM should be aware of the upcoming ESMA Fund Name Guidelines (**the Guidelines)**, which provides guidance on the necessary proportion of investments for funds' names using ESG or sustainability-related terms. The purpose of the Guidelines is to make sure that the names of funds are fair, clear and not misleading. In our view, based on the current consultation paper, we find it defendable that Jacobi AM would be able to make use of the name 'Jacobi Decarbonised Bitcoin ETF'. The key reason is that the fund name is fair, clear and not misleading, because it describes exactly what the Jacobi Decarbonised Bitcoin ETF does, namely exposure to Bitcoin but Decarbonised. We explain this below.

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[7] EC Q&A July 2021, p. 1-2.
[8] Dutch Financial Supervision Act (**DFSA**), art. 2:66 (1) jo 2:73.

5.1. Status of the ESMA Fund Name Guidelines

ESMA has published a Consultation Paper on Guidelines on funds' names using ESG or sustainability-related terms on 18 November 2022. The Guidelines are not yet finalized and in effect. Once the Guidelines are applicable, all national supervisors and fund managers must make every effort to comply with the Guidelines. However, the Guidelines are not binding like national and EU laws.

5.2. Relevant key aspects of the ESMA Fund Name Guidelines

The purpose of the ESMA Fund Name Guidelines is to prevent the potential greenwashing risk in fund names and thereby misleading investors. Hence, ESMA introduces quantitative thresholds for the investments in funds that use ESG and sustainability-related terms in fund names.

The Guidelines introduce two different categories:

A. Funds that have ESG-, or impact-related words in their names.

   These funds must have a minimum proportion of 80% of their investments to attain their environmental or social characteristics or sustainable investment objectives in line with their investment strategy.

B. Funds that have the have "sustainable" or any other term derived from the word "sustainable" 'in their names.

   These funds must allocate, within the 80% of investments to attain their environmental or social characteristics or sustainable investment objectives, at least 50% of those investments in sustainable investments.

5.3. Application to the Fund

It is not clear what precisely falls under 'ESG' or 'impact-related' words. In our view, the word 'decarbonised' can be considered 'ESG-related'.

The investments of the Fund (e.g. Bitcoin) are not used to meet the environmental characteristics it promotes (e.g. decarbonisation of its underlying Bitcoin holdings). This means strictly speaking that the Fund does not meet the 80% quantitative thresholds ESMA introduces in its Guidelines. Nevertheless, the RECs are in fact used to attain the environmental characteristics of the Fund and these RECs relate to the full exposure of the Fund.[9] As such, the name ‘Jacobi Decarbonised Bitcoin ETF’ is fair, clear and not misleading and does not lead to greenwashing. Hence, because the Fund adheres to the purpose of the Guidelines, in our view it is defendable to use the name ‘Jacobi Decarbonised Bitcoin ETF’.

6. Other art. 8 SFDR Bitcoin products

You have informed us that there are crypto Exchange Traded Note providers that claim to offset the carbon emissions from their crypto ETPs with some claiming to be compliant with SFDR art. 8. In our view it is not possible for ETN structures to make such SFDR claims as these note structures are not on the list in art. 2 (1) of the SFDR. This means the SFDR does not apply to them and any claim as to the SFDR status is not supervised by any regulator. The more pragmatic reason is that notes have no investment strategy and therefore cannot have an investment strategy that promotes, among other characteristics, environmental or social characteristics. The entire SFDR and all its disclosure requirements are tailored towards products that actually have some kind of investment strategy and a manager executing this strategy.

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[9] In our view it should not matter at what level RECs are purchased. E.g. if a fund invests in a company that itself purchases RECs than this investment is ESG related. In our view the same should apply to a Fund that invest in the same company, but then it is not the company but the fund buying the RECs. This should be esp. the case with Bitcoin as there is no company to buy the RECs.

Annex I – list of documents

- Jacobi Decarbonised Bitcoin ETF Scheme Particulars dated March 2023.
- E-mail correspondence with Jacobi AM dated 23 and 28 February 2023.
- AFM letter of 28 January 2022 concerning the registration of Jacobi Investment Funds PCC Limited - Jacobi Bitcoin ETF.