

# STATES OF JERSEY



## STRATEGIC RESERVE FUND: USE FOR BANK DEPOSITORS' COMPENSATION SCHEME

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Lodged au Greffe on 2nd June 2009  
by the Minister for Treasury and Resources

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STATES GREFFE

## **PROPOSITION**

**THE STATES are asked to decide whether they are of opinion –**

to refer to their Act dated 5th December 2006 in which they approved a revised policy for the use of the Strategic Reserve Fund established under Article 4 of the Public Finances (Jersey) Law 2005 and agreed that the Fund should be a permanent reserve, where the capital value was only to be used in exceptional circumstances to insulate the Island's economy from severe structural decline such as the sudden collapse of a major Island industry or from major natural disaster, and –

- (a) to agree to vary that policy to enable the Strategic Reserve Fund to also be used, if necessary, for the purposes of providing funding for the Bank Depositors Compensation Scheme to be established under the Banking Business (Depositors Compensation) (Jersey) Regulations 200-; and
- (b) to agree that monies from the Strategic Reserve Fund, up to a maximum combined total not exceeding £100 million, should be made available if required to meet the States contribution to the Bank Depositors Compensation Scheme and/or to meet any temporary cash flow funding requirements of the Scheme.

**MINISTER FOR TREASURY AND RESOURCES**

## **REPORT**

### **1. Background**

- 1.1 The Minister for Economic Development is lodging the Banking Business (Depositors Compensation) (Jersey) Regulations 200- seeking States approval to a Bank Depositors Compensation Scheme to ensure that compensation would be payable (up to a maximum £50,000) if a Jersey registered bank is declared bankrupt.
- 1.2 The case for a Bank Depositors Compensation Scheme in Jersey has been made by the Minister for Economic Development in the report covering the Banking Business (Depositors Compensation) (Jersey) Regulations 200-. Political assurances have already been given that the States would provide financial assistance and support to depositors should a bank default in the Island in advance of a Compensation Scheme being formally approved.
- 1.3 The total cost of the proposed scheme is capped at £100 million.
- 1.4 The Scheme is funded by imposing a levy on banks operating in the Island; these levies may be spread over up to 5 years. Where the total bank levy is insufficient to meet the full cost of the Scheme, the States will be required to make a contribution to the Scheme.
- 1.5 The structure of the Scheme is such that income due from bank levies may not be received until after compensation payments fall due and the Board administering the Scheme may need to borrow funds to meet any short-term cash flow requirements.
- 1.6 The purpose of this report and proposition is to gain States approval to change the policy for the use of the Strategic Reserve fund so that it could, if necessary, be used to provide financial support to the Depositors Compensation Scheme.

### **2. Strategic Reserve – current policy**

- 2.1 The current States policy for the use of the Strategic Reserve was approved by the States on 5th December 2006 as –

“The Strategic Reserve should be a permanent reserve, where the capital value is only to be used in exceptional circumstances to insulate the Island’s economy from severe structural decline such as the sudden collapse of a major Island industry or from major natural disaster.”
- 2.2 The supporting report to this decision can be found in P.133/2006.
- 2.3 At the time that this policy was approved, the current financial situation was not evident and there was no call for a Bank Depositors Compensation Scheme.

2.4 The Public Finances (Jersey) Law 2005 requires that any decision on the use of the Strategic Reserve Fund is made by the States on a proposition brought forward by the Minister for Treasury and Resources.

### **3. Why fund the Depositors Guarantee Scheme from the Strategic Reserve?**

3.1 There is no indication that a Jersey Bank will fail – the Jersey banking sector is characterised by a strict licensing regime (the Top 500 rule) and is generally considered to be well controlled compared with average international requirements. Many of the banks operating in the Island are part of larger banking groups which, recent events have shown, are seen as too large to fail by the U.K. Government.

3.2 Forecasts suggest that the level of income to the Consolidated Fund will reduce over the coming years and the Stabilisation Fund is to be used to deal with the impact of the current economic downturn.

3.3 This then leaves the States' longer term Strategic Reserve Fund. Although the failure of one Jersey registered bank may not be seen as the same as the collapse of a major Island industry, as defined in the current policy, it is an issue which could result in a significant impact on the Island's major industry. The failure to have a credible compensation scheme in place could lead to a loss of confidence by investors and to the movement of cash deposits out of the Island. The States must therefore have a reasoned plan of action available to prevent this situation occurring.

3.4 In bringing this report and proposition forward it is the intent of the Minister for Treasury and Resources to gain the support of the States Assembly to use the Strategic Reserve, if necessary, to provide the appropriate financial assistance and support up to a maximum £100 million to the Bank Depositors Compensation Scheme Board.

3.5 The Bank Depositors Compensation Scheme Board may need to borrow funds to meet any short-term cash flow requirements, i.e. to pay compensation before receiving bank levy income. This proposition would include provision of this short-term loan funding within the purpose of the Strategic Reserve.

3.6 If the levies imposed on the bank are insufficient to meet the Scheme's obligations, the States will be required to contribute to the cost of the scheme. This proposition would include provision of this States contribution toward the cost of the Scheme within the purpose of the Strategic Reserve.

3.7 The total cost of the Scheme is capped at £100 million. Therefore, the total combined financial support provided to the Scheme by way of loan and contribution is also limited to £100 million.

3.8 The amendment to the existing Strategic Reserve policy to enable it to be used to meet the costs, up to £100 million, of the Bank Depositors Compensation Scheme, should provide the relevant commitment to the Scheme to enhance depositor protection and market confidence as well as maintain the Island's standing from an international competitive basis.

3.9 The Minister for Treasury and Resources will consider the most appropriate method of funding a Bank Depositors Compensation Scheme if such a need arose. The agreement of this proposal will enable the Minister to make reasoned decisions and to propose the use of the Strategic Reserve up to £100 million should it be the most appropriate approach at the time.

#### **4. Financial and manpower implications**

4.1 There are no additional manpower implications arising from this proposal.

4.2 There will be financial consequences to the Strategic Reserve Fund if a Jersey registered bank is declared bankrupt under the terms of the Banking Business (Depositors Compensation) (Jersey) Regulations 200- and there is a need to meet the States contribution to the Scheme from the Strategic Reserve fund.

4.3 If the Strategic Reserve is to provide a source of funding to support the Banking Business (Depositors Compensation) (Jersey) Regulations 200-, it will need to hold £100 million in readily marketable assets. This is within the scope of the current investment strategy and will have minimal, if any, impact on the financial return expected from the reserve.

4.4 If it is necessary to make a loan to the Depositors Compensation Scheme it is envisaged that the loan will be repaid with interest and terms and conditions agreed by the Minister for Treasury and Resources.