Consultation
Chief Minister's Department

States of Jersey

Public Consultation on Bank (Recovery and Resolution) (Jersey) Law 201-

Summary:

Jersey is developing a new bank resolution regime (**Jersey Resolution Regime**) in line with developments internationally. The aims are to ensure the continuity of critical banking functions, to avoid adverse effects on financial stability, to protect public funds by minimising reliance on extraordinary public financial support to failing banks and to protect covered depositors and clients' assets.

The international standards state that in order to avoid moral hazard, any failing bank should be able to exit the market, irrespective of its size and interconnectedness, without causing systemic disruption. A failing bank could in principle be liquidated under normal insolvency proceedings in Jersey. However, liquidation under normal insolvency proceedings may jeopardise financial stability, interrupt the provision of critical functions, and affect the protection of depositors. In such a case, it is likely that there would be a public interest in stabilising the bank rather than resorting to normal insolvency proceedings.

This draft Bank (Recovery and Resolution) (Jersey) Law 201- (**Draft Law**) closely follows the European Union's Bank Recovery and Resolution Directive 2014/59/EU (**BRRD**) and the transposition in the Banking Act 2009 into the law of England and Wales (**Banking Act**) for the sake of consistency and to adhere to international standards.

The aim of this consultation is to invite comments on the proposed Draft Law before it is submitted to the States of Jersey for debate.

Date published:
17 March 2016

Closing date:
13 April 2016

Supporting documents attached:

Bank (Recovery and Resolution) (Jersey) Law 201-

How we will use your information

The information you provide will be processed for the purpose of consultation. The Department of the Chief Minister will use your information in accordance with the Data Protection (Jersey) Law 2005 and the Freedom of Information (Jersey) Law 2011. Please note that we may quote or publish responses to this consultation but we will not publish the names and addresses of individuals. If you do not want any of your response to be published, you should clearly mark it as confidential. Confidential responses will be included in any summary of statistical information received and views expressed.

Outline of consultation

During the height of the financial crisis of 2008—2009, a number of credit institutions and investment firms in difficulty were either saved by sovereign governments, or entered bankruptcy causing or contributing to widespread financial contagion. A number of aspects of the responses of public authorities were considered unsatisfactory, for example:

a. There was no clear paradigm within which governments or public authorities decided whether to bail out a bank or whether to allow it to fail.

b. The short-term cost to the public purse has been high.

c. The rescue of a failed bank on the basis that it is "too big to fail" creates moral hazard; market participants should not be incentivised to take untenable risks with the knowledge that the price of failure will be government bail-out.

d. The financial crisis demonstrated that inadequacies in general corporate insolvency procedures which are not bespoke to bank insolvency are magnified by the differences between the approaches taken in different jurisdictions.

It therefore became apparent to policy makers that there was a lack of adequate tools available to deal effectively with failed or failing banks. It was concluded that powers were needed, in particular, to prevent insolvency or, when insolvency occurs, to minimise negative repercussions by preserving the critical economic and systemically important functions of the bank concerned. Such tools would also need to ensure that shareholders bear losses first and that creditors bear losses after shareholders provided that there are safeguards in place which normally protect

creditors with compensation payable where they endure greater losses that would have incurred under normal insolvency proceedings as set out below.

Consequently, the G20 formed the Financial Stability Board which went on to formulate and publish its Key Attributes for Effective Resolution Regimes for Financial Institutions (**Key Attributes**). Within this framework many jurisdictions have implemented resolution regimes which provide tools for addressing banks in financial difficulty within the jurisdiction. Of particular note to Jersey, is the BRRD and the implementation of the UK's Special Resolution Regime primarily through the bringing into force of the Banking Act, as subsequently amended under the law of England and Wales, and as supplemented by various policy statements and codes of practice.

The implementation of the Key Attributes will be assessed in due course as part of any Financial Stability assessment carried out by the International Monetary Fund into financial stability.

Jersey, as well as the other Crown Dependencies (Guernsey and Isle of Man) (together the **CDs**) will need to demonstrate their adequacy as leading international offshore banking centres by aligning their bank resolution framework with international development while tailoring such to the requirements of the market in Jersey. As the banks that may need resolving are mainly UK or European banks the focus has been to give a particular emphasis on the EU provisions set out in BRRD and participating in the international harmonisation of approaches to dealing with failing banks.

The Draft Law has been drafted with the aim of ensuring that Jersey is sufficiently well equipped to be able to:

a. assist a foreign jurisdiction in respect of a resolution action being taken on a bank conducting business in Jersey through a branch or subsidiary; and,

b. deal with a scenario in which a bank in Jersey were to fail and standalone powers are needed to resolve the local business (either as a result of the home jurisdiction taking action which does not satisfactorily deal with the local business, or because Jersey is the home jurisdiction of the bank in difficulty).

In practical terms the aim of the Jersey Resolution Regime is to be fit to enable the recognition of actions taken by overseas resolution authorities in respect of branches in Jersey or Jersey's Resolution Authority taking action concurrently with overseas resolution authorities to assist a group resolution in respect of a subsidiary incorporated in Jersey. There may also be cross-border issues in respect of the UK and/or other CDs where there is a bank incorporated in one island with branches in the other islands.

As part of the research and drafting process of the Draft Law, it has been concluded that current Jersey insolvency law is limited in the manner in which it provides for the recovery or resolution of insolvent banks, particularly where such banks involve a global or group nexus and the extent to which it maps out a modern mechanism for winding-up a Jersey bank. Therefore, a bespoke bank winding-up procedure (the **Bank Winding-up Procedure**) has also been drafted as part of the Jersey Resolution Regime and is incorporated within the Draft Law.

The aim of this Draft Law is to provide a new set of tools and powers relevant to particular circumstances. There is no current equivalent law in Jersey or in the other CDs. Therefore, the new Jersey Resolution Regime will not affect existing law and practice; instead it is intended to add clarity to what would happen were a bank to fail or be likely to fail in the jurisdiction.

Respondents are invited to comment generally on the Draft Law as well as answer specific questions that are raised.

Ways to respond

This consultation can be responded to electronically by the following link:

Write to: James Mews
Director, Finance Industry Development, Financial Services Unit
Chief Minster's Department
7th Floor, Cyril Le Marquand House
The Parade, St Helier,
Jersey JE48UL
Telephone: +44 (0) 1534 440413
Email: j.mews@gov.je

Responses from the finance industry may be sent to Jersey Finance at the address below:

Write to: William Byrne
Head of Technical, Jersey Finance Limited
4th Floor, Sir Walter Raleigh House
48-50 Esplanade
St Helier
Jersey JE2 3QB
Telephone: +44 (0) 1534 836021
Email: william.byrne@jerseyfinance.je

Responses sent to Jersey Finance will be shared with Government unless the respondent indicates that they wish to remain anonymous. Please indicate clearly on your response if this is the case.

This consultation paper has been sent to the Public Consultation Register.

Feedback on this consultation

We value your feedback on how well we consult or seek evidence. If you have any comments on the process of this consultation (as opposed to the issues raised) please contact Communications.Unit@gov.je

Consultation on the Draft Law

Introduction

1. The Assistant Chief Minister invites responses on the text of the Draft Law concerning creating a resolution regime. The provisions commented on in this paper are those which it is considered may be of particular note or of concern to the finance industry in Jersey or where the approach taken by Jersey significantly differs from that taken under BRRD or the Banking Act.

Article 3 – Application

2. This Article has been drafted widely in order that the Draft Law applies to a person who is registered to carry out deposit-taking business in or from within Jersey under the Banking Business (Jersey) Law 1991 (**Banking Law**), which includes subsidiaries and branches of banks, registered to carry out deposit-taking business in Jersey. Article (3)(1)(b) extends the scope to a holding company or a subsidiary of a bank that is registered to carry out deposit taking business in or from within Jersey. Article 3(1)(c) extends the scope to a branch or subsidiary of a foreign bank where the foreign bank carries out deposit taking business in or from within Jersey. This means that the Jersey Resolution Authority could, in theory, seek to resolve a branch or subsidiary of a foreign bank outside of Jersey (albeit the jurisdiction in which that branch or subsidiary of the foreign bank was located would need to recognise the action taken by the Jersey Resolution Authority).

3. It was considered preferable to include broad provisions to cover the event that the jurisdiction in which such an entity was located did not have a resolution regime and that jurisdiction would recognise a resolution action taken under the Jersey Resolution Regime in order to achieve the orderly resolution of entities in its jurisdiction. For example, a resolution action involving entities located in the other CDs might benefit from the Jersey Resolution Authority having the capability under Jersey law to extend its actions to those entities, if the recognition of such actions can be achieved in those other CDs, prior to the other CDs bringing in a resolution law.

4. Further whilst it is considered unlikely that the Jersey Resolution Authority would ever seek to resolve a branch or subsidiary of a foreign bank itself, it was considered important to ensure that Jersey retained its independence

from the home jurisdiction of a bank. For example, where a bank was incorporated in the UK and had a branch in Jersey, the most likely approach to be taken would be for Jersey to support and recognise the resolution action taken by the UK. However, if it was considered that by doing so it would have an adverse effect on the financial stability of Jersey, the Jersey Resolution Authority could, in theory, seek to resolve the branch itself.

5. It was also considered important that the Jersey Resolution Authority had a broad range of powers available in order that it could take actions to assist a foreign resolution action as deemed necessary (for example, by transferring assets located in Jersey to the foreign equivalent of a bridge bank or ensuring that liabilities governed by Jersey law can be written down in a bail-in).

6. Article 96 of the BRRD requires that where an EEA resolution authority has refused to recognise third country resolution proceedings or where the third country resolution authority has not commenced resolution proceedings which affect the branch, and action is in the public interest, the EEA resolution authority has the powers necessary to act in relation to the branch, independently of the third country resolution authority. Therefore, Jersey has taken the same approach as that set out in the BRRD.

7. The view of the Government is that cases where independent action is needed will be highly exceptional. We understand from the Bank of England that there is significant work underway at an international level, to ensure that resolution authorities co-operate in the case of cross-border banks. This includes drawing up and agreeing ex ante resolution plans which set out the roles and responsibilities of each resolution authority.

8. Powers to act independently in relation to the Jersey branch of a foreign bank would therefore be used in such exceptional circumstances as 'back-stop' powers to be used in the event that co-operation proved ineffective, and where action was required to protect the public interest of Jersey.

9. This is consistent with the Key Attributes, which recognise the need for resolution authorities to have, as a fall back option, the ability to take independent action with respect to local operations of foreign banks in certain circumstances.

10. However, it has been suggested by a member of the steering group that a simpler solution would be for the powers of the Jersey Resolution Authority to resolve a Jersey branch of a foreign bank to be 'switched off' in contrast to the position taken overseas. This would mean that the Jersey Resolution Authority would always have to seek to recognise a foreign resolution action. The rationale for such an approach is that it is highly unlikely that Jersey would seek to take resolution action on its own in respect of a branch of a foreign bank.

11. Alternatively, if it is considered that the Jersey Resolution Authority should retain broader powers and have the ability to resolve a Jersey branch of a foreign bank, there are a number of practical implications of resolving a branch of a foreign branch which would need to be considered at greater length.

12. The UK is currently in consultation to include powers to resolve a branch. It is likely that Jersey would seek to mirror the UK's approach as far as possible. The details of the proposals being consulted upon in the UK are set out below for information purposes and to demonstrate the approach that it is currently envisaged that Jersey would most likely seek to follow.

13. The UK Government is proposing to make the following stabilisation powers available to the Bank of England, when acting independently to resolve a UK branch of a third country institution:

    a. powers to transfer some or all of the assets, rights and liabilities (**the business of the branch**) to a private sector purchaser, to a bridge bank or to an asset management vehicle; and
    b. the power to bail in liabilities in connection with the transfer to the private-sector purchaser, the bridge bank, or the asset management vehicle.

14. It is considered that transferring the business of the branch could be achieved without the support of the third country authority. Following the transfer to a private sector purchaser, a bridge bank or an asset management vehicle, bail-in could be used to recapitalise that entity as necessary.

15. The UK Government would not be proposing to introduce standalone bail-in powers. Bailing in the liabilities of the branch itself would unlikely be an effective stabilisation tool, given that the branch would have no legal identity of its own. On that basis, the relevant provisions of the Banking Act would be disapplied where the Bank of England was acting independently to resolve a third country branch.

16. Similarly, the UK government would not be proposing to introduce powers to put branches into temporary public ownership. Temporary public ownership is a resolution tool intended as a 'last resort' stabilisation option for use only where there is serious risk to the financial stability of the UK (as is the case for Jersey in respect of the temporary public ownership stabilisation tool). It can only be applied to banks and holding companies, not to other banking group companies. As such, it would not be appropriate to use temporary public ownership powers for the independent resolution of a branch, which has no legal identity of its own. On that basis, the relevant provisions of the Banking Act would also be disapplied in this regard where the Bank of England is acting independently to resolve a third country branch.

17. The UK Government is not intending to extend share transfer powers to independent resolutions of UK branches, as the branch itself is not a separate legal entity.

18. For the Bank of England to have property transfer powers over the business of the branch, it would need to be specified which assets, rights and liabilities fall within such a definition. The UK Government would propose to define the 'UK branch' as 'a branch situated in the United Kingdom of a third country institution authorised for the purpose of the Financial Services and Markets Act 2000 by the PRA or FCA.' It would then look to define the 'business of a UK branch' as 'any property in the United Kingdom of the relevant third country institution, and any rights and liabilities of the relevant third country institution arising as a result of the operations of a UK branch.

19. The proposed amendments to the Banking Act would provide that the Bank of England may only exercise transfer and bail-in powers over the business of a UK branch where it is necessary to do so having regard to the public

interest in advancing the special resolution objectives. This condition would have the practical effect of limiting the scope of the Bank of England's powers to what is proportionate in order to safeguard the UK public interest. As detailed above this approach could be mirrored either as a matter of practice in the policy development side of implementing a regime or by amending the Draft Law as far as possible for use in Jersey depending on the views received as a result of this consultation.

20. However, generally speaking, the policy intent is to grant as wide powers as may be necessary for a resolution authority so that the scope of a Draft Law does not need to be changed in the future.

Question 1:

Do you agree with the scope of the Draft Law in respect to resolution under Article 3(1) of the Draft Law? If not, then please state why and what you would prefer?

21. Article 3(2) provides for the scope of the Draft Law in respect of the Bank Winding-up Procedure which is more limited compared to Article 3(1) which applies to recovery and resolution generally. Article 3(2) applies to persons registered to carry out deposit-taking business in or from within Jersey under the Banking Law which includes subsidiaries and branches of foreign banks.

22. The Bank Winding-up Procedure also extends to a company incorporated in Jersey that is a holding company or subsidiary of a person registered to carry out deposit-taking business in or within Jersey under the Banking Law.

Question 2:

Do you agree with the scope of the Draft Law in respect to the Bank Winding-up Procedure under Article 3(2) of the Draft Law?

Part 2 – Jersey Resolution Authority

23. It is a general principle of the Key Attributes, and of BRRD, that in order to ensure the required speed of action, to guarantee independence from economic actors and to avoid conflicts of interest, a public administrative authority should be entrusted with the necessary public administrative powers to perform various functions and tasks under each resolution regime. The Key Attributes state that to act as a resolution authority, the authority must be operationally independent in this role.

24. However operationally independent does not mean that other members of the financial safety net should not sit on the Board. For example, the IADI Core Principles for Deposit Insurance Systems also adopted by the Financial Stability Board, clearly sets out in Principle 3 that other members of the financial safety net are able to sit on the Board with the board remaining operationally independent provided that such members do not act as chair or constitute a majority.

25. Article 5(1) of the Draft Law provides for the States to appoint members of the Jersey Resolution Authority from various bodies (including the Chief Minister's Department and the Jersey Financial Services Commission) in order to ensure that different views from sectors of Jersey's financial industry can be heard and taken into consideration as part of the resolution process and eventual decision making in respect of a bank resolution.

26. In the event that the Minister is unable to/does not make an appointment under Article 5(1) of the Draft Law, Article 5(4) allows the Minister to appoint a public officer, public authority or other person to discharge the functions of the Jersey Resolution. For example, the Jersey Financial Services Commission or the Deposit Compensation Scheme Board could be appointed as the Jersey Resolution Authority if necessary.

27. Also this provision could be used for a pan-national body such as a CD resolution authority to be appointed. While there are many obstacles to creating a body that would govern resolution actions in more than one CD there would appear to be possibilities for cost savings and also the alignment of a common interest in working with an overseas resolution authority to resolve a globally systemically important institution.

Question 3:

Do you agree with the approach being taken in respect of appointments to a Jersey Resolution Authority?

Question 4:

Do you consider that there should be a representative of any other body/group/authority represented on the Jersey Resolution Authority?

Question 5:

Do you think that there should be best endeavours taken to create a Resolution Authority spanning more than one of the CDs?

Funding Resolution – General Approach

28. There are likely to be circumstances in which the effectiveness of the resolution tools would depend on the availability of short-term funding for a bank or bridge bank, the provision of guarantees to potential purchasers, or the provision of capital to a bridge bank. For this reason the Key Attributes and BRRD state that financing arrangements should be set up to ensure that funds are available for such purposes without the need for recourse to public funds. As a matter of general principle, the Key Attributes are clear that the finance industry as a whole must, ultimately, finance the stabilisation of the financial system.

29. The Key Attributes stipulate in general terms that jurisdictions should have in place privately-funded deposit insurance or resolution funds, or a funding mechanism with ex post recovery from the finance industry of the costs of providing temporary financing to facilitate the resolution of a bank. BRRD is more specific, setting out requirements for each European Member State to establish an ex-ante funded resolution fund. BRRD stipulates that resolution funds should have available funds of at least 1% of the amount of covered deposits of all the banks authorised in the jurisdiction.

30. It is also a general principle under the Key Attributes that where temporary funding from a resolution fund is used to accomplish the stabilisation of a bank, such funds should be recovered (i) from shareholders and unsecured creditors subject to the principle that no creditor should be worse off in

stabilisation than in winding-up; or (ii) if necessary, by way of contributions from the financial system more widely.

31. In preparing the Draft Law the Government has been cognisant of the need to balance the implementation of a Jersey Resolution Regime which is credible and in line with international standards on the one hand, with minimising the cost of the implementation of such a regime to Jersey's banking industry on the other hand. The general approach taken in respect of the funding of resolution has therefore sought to strike a balance between these considerations.

Article 16 - Annual Administration Levy

32. The approach taken in respect of the Annual Administration Levy payable under the Draft Law is similar to the approach taken in respect of the Jersey Bank Depositor Compensation Scheme (**JDCS**).

33. Banks in Jersey may be required to pay an Annual Administration Levy which would be split as necessary in order to fund the Jersey Resolution Authority's expected recurring administrative costs. Whether there is a need for an Annual Administration Levy will be the subject of further consultation in due course.

34. The Jersey Resolution Authority will also have the ability to use the Jersey Bank Resolution Fund to provide or maintain a reserve. This would provide a buffer against intial costs that might be payable in the future as a result of resolution action being taken in respect of a bank in that or any subsequent year, without having to wait for receipt of other funding.

35. The Annual Administration Levy would be used to pay for costs incurred by the Jersey Resolution Authority in respect of preparing for resolution and the standing costs of a Jersey Resolution Authority (for example, the salary of an employee of the Jersey Resolution Authority).

Article 22 – Establishment of Jersey Bank Resolution Fund

36. As detailed above, the Jersey Bank Resolution Fund mirrors the structure of the JDCS and broadly consists of the following elements:

    a. the amount that can be paid out from the Jersey Bank Resolution Fund for the costs of resolution has not been capped but is limited to the funds available;

b. the Jersey Bank Resolution Fund has the capacity to borrow from any source, including the strategic reserve fund as defined in the Public Finance (Jersey) Law 2005 and private sector sources in order to access funds;

c. the Jersey Bank Resolution Fund is able to seek to recover any funds paid out from the bank in resolution;

d. if there is any negative balance left to the Jersey Bank Resolution Fund following recovery of as much as possible from the bank in resolution, the Jersey Bank Resolution Fund is able to recover such balance from other banks, ex post, on terms which reflect the JDCS.

37. It was considered that the preferable approach for Jersey's banking industry would be for the Jersey Bank Resolution Fund to have access to immediate liquidity funding by way of a loan from the Government which could later be recouped from the bank in resolution. Whilst there is the possibility for any costs that cannot be recouped from the bank in resolution to be recouped from other banks on the island, it is unlikely that this would ever be the case when the amounts required for resolution action is compared to the balance sheets of the banks that are subject to resolution.

38. It was not considered appropriate to create a pre-funded fund as envisaged in BRRD as this would require the island's banks to pay a higher levy than they would be required to pay under the Annual Administration Levy alone. In taking this approach, the financial resources in Jersey were considered as well as the need to keep the cost of implementing the Jersey Resolution Regime proportional and cost effective. It is considered that the key backstop for the Jersey Bank Resolution Fund is to have access to liquidity from the States in order to act in a timely fashion.

39. The Jersey Bank Resolution Fund would be used to pay costs including the cost of resolution itself (valuations etc.) and potential claims for compensation.

40. Article 22(8) of the Draft Law provides a cap of £100 million to be contributed to the Jersey Bank Resolution Fund by the banks during any five year period (or such other amount or time period as may be prescribed). This cap on the amount to be contributed is aimed at providing Jersey's banking industry with some comfort as to the maximum amount of liability in respect of resolution costs.

41. Whilst the Jersey Bank Resolution Fund can be used to contribute towards compensation payable for a 'no creditor worse off claim' there is no cap specified in respect of the amount that can be claimed by way of compensation. In other words, if a creditor of a bank in resolution has a compensation claim against a bank in resolution, that creditor can claim the full amount owed and will not be capped at £100 million. However this begs the question where will the funds come from for such a claim.

42. The answer is contained in Article 22(9) of the Draft Law which provides that where a creditor's claim has exhausted the funds in the Jersey Bank Resolution Fund, that creditor will have a direct claim against the bank in resolution and the claim cannot be made against the Jersey Resolution Authority in respect of the Jersey Bank Resolution Fund. This aims to protect the other banks in Jersey and the Jersey Bank Resolution Fund while preserving creditors' rights against the party that arguably is responsible for the loss (i.e. the bank in resolution). This moves a creditor's claim away from the Jersey Bank Resolution Fund in the event that the bank in resolution cannot fund the costs of resolution, and the monies contributed by the other banks are insufficient to cover the costs of resolution. This end result is intended to be that the Fund can continue to operate and provide services to all banks even if a resolution attempt fails.

Question 6:

Do you agree with the approach being taken in respect of the Jersey Bank Resolution Fund? If not, please elaborate on your reasons as to why and how you consider this could be changed?

Question 7:

Do you agree with the approach being taken in respect of creditors' rights and the limitations of liability placed upon the Jersey Bank Resolution Fund? Could the drafting be improved to achieve the aims of transferring liability? If you do not agree with the approach taken, please elaborate on your reasons why, and state how you consider this should be changed?

Article 30 – Creditor Hierarchy

43. While eligible deposits are protected from losses in resolution, other eligible deposits are potentially available for loss absorbency purposes. In order to provide a certain level of protection for natural persons holding eligible deposits above the level of eligible deposits, such deposits have been given a higher priority ranking over the claims of ordinary unsecured, non-preferred creditors under Jersey insolvency law. The claim of the JDCS against all subrogated claims by depositors is then given an even higher ranking under the Jersey Resolution Regime than the aforementioned eligible deposits.

44. There are currently disparities between the creditor hierarchies set out in the laws of England and Wales, other European countries, Jersey and the other CDs. This is partly due to the level of protection afforded to depositors under each jurisdiction's depositor compensation scheme (**DCS**). For example, Jersey protects individual depositors up to £50,000 in comparison to England and Wales which protects individual depositors up to £75,000. Whilst this has been an accepted position in respect of the DCS, it will cause disparity under the resolution regimes because of the definition of 'covered deposit'.

45. An example is in respect of the application of the bail-in tool and the order in which liabilities can be written down or converted. Article 65(7) of the Draft Law makes provision to state that the Authority shall not exercise the write down or conversion power in respect of 'covered deposits' which is the same approach taken under the BRRD. However, the definition of 'covered deposit' itself differs in that the BRRD definition is wider than that in the Draft Law due to the difference in the deposits 'covered' by the DCS in different jurisdictions.

46. Under the Draft Law the term 'Covered Deposit' is defined as the part of eligible deposits that does not exceed the maximum amount of compensation payable to a depositor under the draft Banking Business (Depositors Compensation) (Jersey) Law 201- (**Draft JDCS Law**). In summary, the maximum amount of compensation payable under the JDCS Law is £50,000 per person, per Jersey banking group for local and international depositors. The draft JDCS Law covers private individuals, charities and Community Savings Limited. It does not extend to corporations, SMEs, partnerships or trusts.

47. Under BRRD 'Covered Deposit' is defined as the part of eligible deposits that does not exceed the coverage level laid down in Article 6 of the BRRD which confirms protection of each depositor up to EUR 100,000 (approximately GBP 77,000) and includes deposits resulting from real estate transactions relating to private residential properties and deposits that serve social

purposes and are linked to particular life events of a depositor such as marriage, divorce, retirement etc. As the law of England and Wales follows BRRD it covers private individuals, SMEs, corporate bodies, partnerships and charities (although specific rules apply in respect of turnover of charities). Therefore a wider approach is also taken by England and Wales in comparison to Jersey.

48. There is also a risk that a creditor may be worse off as a result of resolution action being taken or the recognition by the Jersey Resolution Authority of a foreign resolution authority's actions compared to the position otherwise under Jersey law. Also if the creditor hierarchy is amended there is the risk that if a bank were to fail and become insolvent, and the DCS pays out, that the recoveries might be less to the DCS as a result of the amended hierarchy.

49. As a matter of policy, the Government is working with the other CDs to achieve, as far as possible, a harmonised approach across the CDs in respect of creditor hierarchy. This is desirable in order to minimise exposure to the Jersey Bank Resolution Fund under the 'no creditor worse off' principle and to ensure that Jersey is not placed at a competitive disadvantage in respect of the level of protection afforded to depositors.

Question 8:

Are there any preferences in terms of the approach to be adopted in regard to the creditor hierarchy and as to the appropriate balance to be struck between a policy which favours maximising recoveries in the event of a DCS payout or one that reduces the chances of a 'no creditor worse off' claim by greater harmonisation with the law of England and Wales?

Article 33 – Objectives of Resolution

50. In accordance with the general principles of BRRD, the Jersey Resolution Regime does not prescribe the exact means by which the Jersey Resolution Authority should intervene with a failing bank. Rather, it maintains and gives the Jersey Resolution Authority the flexibility to use the powers available to it under the Jersey Resolution Regime. In exercising the resolution powers and measures available to it, the Jersey Resolution Authority will be required to take into account the circumstances in which the failure occurs. For example, if the problem arises in an individual bank and the rest of the financial system is not affected, the Jersey Resolution Authority will be able to exercise the

resolution powers without much concern for contagion effects, whereas greater care would need to be exercised to avoid destabilising financial markets in an economically fragile environment.

51. The Banking Act has included an objective to state that resolution action can only be taken where it is necessary in the public interest of the UK and any interference with the rights of shareholders and creditors which results from resolution actions would have to be compatible with the Human Rights Act 1998.

52. It is considered that the use of the resolution tools and powers provided for in the Jersey Resolution Regime may, by their very nature, disrupt the rights of shareholders and creditors. One example is the power to transfer the shares or all or part of the assets of a bank to a private purchaser without the consent of shareholders which will affect the property rights of shareholders. In addition, the power to decide which liabilities to transfer out of a failing bank based upon the objectives of ensuring the continuity of services and avoiding adverse effects on financial stability may affect the equal treatment of creditors. The Draft Law does not made it a resolution objective to avoid interference with property rights in breach of the Human Rights (Jersey) Law 2000. However, Article 33(5) requires the Jersey Resolution Authority to seek to minimize the cost of resolution and avoid destruction of value unless reasonable to achieve the resolution objectives. This principle is not included in the BRRD but has been included due to the comparable size of Jersey (to the EU for example) and the liability risks posed by resolution. Article 34(1)(c) also requires that a stabilization tool may only be applied if the Authority is satisfied that the application of that tool is in the public interest of Jersey. The Draft Law will be reviewed generally for compatibility with the Human Rights (Jersey) Law 2000 as a matter of course by the Law Officers.

Article 35 – General Principles of Resolution

53. The Jersey Resolution Authority will be required to take into account the nature of a bank's business; shareholding structure; legal form; risk profile; size; legal status and form and interconnectedness to other banks or to the financial system in general; the scope and complexity of its activities; whether it is a member of an institutional protection scheme or other cooperative mutual solidarity systems; whether it exercises any investment services or activities; and whether its failure and subsequent winding up under normal insolvency proceedings would be likely to have a significant negative effect on financial markets, on other banks, on funding conditions, or on the wider economy, when developing recovery and resolution plans and when using the different powers and tools at their disposal.

54. The general principles of resolution in the Draft Law closely follow the principles set out in BRRD. However, it has been proposed that the statement in Article 35(g) that: 'no creditor shall incur greater losses than would have been incurred had the bank been wound up under normal insolvency proceedings' should be constrained by the caveat unless such is necessary in the public interest. The reason for this possible amendment is to bring the 'no creditor worse principle' directly into line with Article 1, Protocol 1 of the European Convention on Human Rights in respect of interference with property rights. Compensation will be paid out of the Jersey Resolution Fund which will generally be payable by the bank in resolution. There is also a relationship with Article 78 where there is the ability for compensation to be payable following the 'difference in treatment' valuation.

Question 9:

Do you agree with the application of the 'no creditor worse off' principle as set out in the Draft Law? Should it be further constrained by a caveat unless such interference is necessary in the public interest? And if so should the principle also be linked to Article 78?

Articles 44-50 and 77-78 – Valuations

55. It is important that the Jersey Resolution Authority is able to pursue effective decision-making as regards the application of the resolution tools. The Draft Law has followed the BRRD approach in respect of the valuations to be undertaken as part of the Jersey Resolution Regime. It was considered as part of the drafting process whether a simplified approach could be taken by and in respect of banks in Jersey, however, taking a risk-based approach, it was not, subject to the views of consultees, considered sensible or feasible to amend substantially the established valuation methodologies currently used in Europe.

56. Before any resolution action is taken, a fair and realistic valuation of the assets and liabilities of the bank is required to be carried out. The valuation will be an integral part of the decision made by the Jersey Resolution Authority as to whether or not to apply a resolution tool or exercise a resolution power, or the decision to exercise the write down and conversion power.

57. Where possible, a definitive valuation will take place prior to resolution. This valuation will be undertaken by an independent valuer and the purpose of the valuation will be to (i) assess the value of the assets and liabilities of the institution/entity and ensure that the conditions for resolution are met; (ii) inform the determination as to what the resolution action to be taken should be; (iii) inform the decision on the extent to which the power should be used (depending on the resolution action taken and/or the resolution tools used); and (iv) ensure that any losses on the assets of the bank are fully recognised at the moment that the resolution tools or the power are/is applied.

58. In cases where a definitive valuation is not possible prior to resolution and the Jersey Resolution Authority considers that the urgency of the case means that it is appropriate to make a mandatory reduction instrument (i.e. an instrument by which the Jersey Resolution Authority exercises the write down and/or conversion power), or exercises a stabilisation power, before a valuation can be carried out by an independent valuer, it may carry out a provisional valuation of the assets and liabilities of the bank itself in order to understand whether the bank is failing or likely to fail. This provisional valuation will be the basis of resolution actions until a definitive valuation can be carried out.

59. Following the application of the resolution tools, a 'difference of treatment valuation' will be undertaken. This valuation will compare the treatment that shareholders and creditors have actually been afforded and the treatment that they would have received under normal insolvency proceedings. The purpose of this valuation will be to (i) ensure that any losses on the assets of the institution/entity are fully recognised in the books of the accounts of the same; and (ii) inform a decision to write back creditors' claims or to increase the value of the consideration paid where it is determined that shareholders and creditors have received in payment of, or compensation for, their claims, the equivalent of less than the amount that they would have received under normal insolvency proceedings.

60. Articles 48 and 77 of the Draft Law provides for the Jersey Resolution Authority to set or adopt standards for the purpose of the valuations to be undertaken. The Jersey Resolution Authority may therefore seek to follow the technical standards drafted by the European Banking Authority (as done in BRRD) or it may seek to produce its own.

Article 65 – Application of bail-in tool

61. There are various tools available to the Jersey Resolution Authority in the event that a bank is failing or likely to fail. However, it is considered that the tool that the Jersey Resolution Authority is most likely to apply would be the bail in tool.

62. The Jersey Resolution Regime aims to minimise the risk that the costs of the resolution of a failing bank are borne by Jersey taxpayers. It aims to ensure that systemic banks can be resolved without jeopardising financial stability. The bail-in tool is intended to achieve these objectives by ensuring that shareholders and creditors of a failing bank suffer appropriate losses and bear an appropriate part of the costs arising from the failure of the bank. The bail-in tool therefore gives shareholders and creditors of banks a stronger incentive to monitor the health of a bank during normal circumstances and meets the Financial Stability Board's recommendation that statutory debt write-down and conversion powers be included in a framework for resolution, as an additional option in conjunction with other resolution tools.

63. It is not appropriate to apply the bail-in tool to claims insofar as they are secured, collateralised or otherwise guaranteed. However, in order to ensure that the bail-in tool is effective and achieves its objectives, the Draft Law seeks to apply to as wide a range of the unsecured liabilities of a failing bank as possible.

64. Nevertheless, it is considered appropriate under the BRRD (and as transposed in the Banking Act) to exclude certain kinds of unsecured liabilities from the scope of application of the bail-in tool. This is the case to protect covered deposits but also to ensure continuity of critical functions and to reduce the risk of systemic contagion.

65. As the protection for eligible depositors is one of the most important objectives of resolution, covered deposits are not subject to the exercise of the bail-in tool. Most jurisdictions adopt the definition that is utilised under their deposit compensation regime. However, as detailed above, the current

definition of covered deposits under the Draft Law (please refer to Article 65(7)(a) and the definitions set out in Article 1) is narrower than that in the BRRD and the Banking Act. The Draft Law uses the Jersey definition under the legislation relating to JDCS, rather than that under the BRRD, which defines covered deposits to include the standard eligible depositors covered under the JDCS up to the amount that they are protected by the JDCS. Amending this provision to reflect the European approach would have the effect of parity with the UK DCS and a similarity with other European jurisdictions although it would restrict the amount of liabilities that the Jersey Resolution Authority could bail in as part of a resolution.

Question 10:

Do you agree that the definition of covered deposits should be linked to the existing Jersey definition as those covered by the Jersey Deposit Compensation Scheme? If not please state what definition should be adopted?

66. Article 65(7)(b) has the effect of excluding from bail in 'secured liabilities including covered bonds and liabilities in the form of financial instruments used for hedging purposes which form an integral part of the cover pool and which according to Jersey law are secured in a way similar to covered bonds'. Covered bonds are defined in defined in Article 2.1(96) of BRRD by reference to Article 52(4) of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities. It would need to be considered specifically by banks which liabilities held by them would fall into this category.

67. Article 65(7)(c) has the effect of excluding from bail in 'any liability that arises by virtue of the holding by the bank of client assets held on behalf of a recognized fund (within the meaning of Article 1 of the Collective Investment Funds (Jersey) Law 1988) or an AIF (within the meaning of the Alternative Investment Funds (Jersey) Regulations 2012) provided that such a client's assets are protected under normal insolvency law' which follows the approach taken under BRRD using the Jersey equivalent of UCITS as defined in in Article 1(2) of Directive 2009/65/EC or of AIFs as defined in point (a) of Article 4(1) of Directive 2011/61/EU of the European Parliament and of the Council'. Under BRRD, reference is made to 'client assets or client money' whereas the Draft Law refers only to 'client assets' (which is the same

approach taken in the Banking Act). Client assets have been specifically defined as 'assets which a bank has undertaken to hold for a client (whether or not on trust, and whether or not the undertaking has been complied with)'.

68. Article 65(7)(d) has the effect of excluding from bail in 'any liability that arises by virtue of a fiduciary relationship between the bank (as fiduciary) and another person (as beneficiary) provided that such beneficiary's interests are protected under Jersey insolvency law'. This is the same approach as that taken under BRRD.

69. Article 65(7)(e) has the effect of excluding from bail in 'liabilities to a credit institution, excluding entities that are part of the same group, with an original maturity date of less than 7 days'. Credit institutions are defined specifically as a bank or an entity that is carrying on deposit-taking business (whether or not incorporated, or carrying on business, in Jersey. This would therefore exclude bank-to-bank liabilities from bail in with an original maturity of less than 7 days which is designed to prevent the freezing up of the inter-bank lending market.

70. Article 65(7)(f) has the effect of excluding liabilities with a remaining maturity of less than 7 days, owed to payment and securities settlement systems or their participants and arising from the participation in such system. The exclusion under Article 65(7)(f) seeks to reduce the risk of systemic contagion.

71. Article 65(7)(g) has the effect of excluding certain liabilities to employees of the failing bank or to commercial claims that relate to goods and services critical to the daily functioning of the bank. In order to honour pension entitlements and pension amounts owed or owing to pension trusts and pension trustees, the bail-in tool does not apply to the failing bank's liabilities to a pension scheme. However, the bail-in tool would apply to liabilities for pension benefits attributable to variable remuneration which do not arise from collective bargaining agreements as well as to the variable component of the remuneration of material risk takers. This Article also excludes tax and social security services in Jersey and the JDCS.

72. The Jersey Resolution Authority is also able to exclude or partially exclude liabilities in a number of circumstances including where: it is not possible to bail in such liabilities within a reasonable timeframe; the exclusion is necessary and proportionate to achieve the continuity of critical functions and core business lines; and the application of the bail-in tool to liabilities would cause a destruction in value such that losses borne by other creditors would be higher than if those liabilities were not excluded from bail-in. The Jersey Resolution Authority would be able to exclude or partially exclude liabilities where necessary to avoid the spreading of contagion and financial instability which may cause serious disturbance to the economy of Jersey..

Question 11:

Do you agree with the approach being taken in respect of liabilities that are excluded under the Draft Law? If so, please explain what the issues are and how you consider they could be rectified.

Article 89 – Recognition of foreign resolution actions

73. International and European financial markets are highly interconnected with many banks operating across national borders. This is particularly noticeable in Jersey where there are no indigenous banks. The failure of a bank in Jersey is therefore likely to involve a backdrop of external economic shocks and resolution actions being taken in other home and intermediate home jurisdictions.

74. The Bank of England has stated:

"*A host authority should not seek to take action with respect to subsidiaries or branches of foreign banks in its own jurisdiction which might frustrate the orderly resolution of the group being co-ordinated by the home authority.*

In support of these principles of co-operation, the United Kingdom will co-ordinate a group-wide resolution strategy where it is the home supervisory authority of a failing cross-border firm. Regulatory authorities in other countries may need to take supporting regulatory or indeed resolution actions to assist in this. The Bank [of England] will co-ordinate with host authorities over any action that may be required.

Where the United Kingdom is a host of a foreign firm that needs to be resolved, the UK authorities will aim to co-ordinate closely with the home authorities, and only seek to take independent action in exceptional cases, in line with the approach for cross-border co-operation set out in the Key Attributes. These exceptions are set out in the BRRD, and include where the home country's proposed action, or inaction, is deemed not likely to maintain financial stability in the United Kingdom, and to ensure there is no discrimination against depositors or creditors of host subsidiaries or branches in a host jurisdiction."

75. Jersey-based subsidiaries of foreign banking groups are established in Jersey and therefore fully subject to Jersey law (including, following its implementation, the Jersey Resolution Regime). However, during the production of the Draft Law it has been considered necessary for Jersey to retain the right to act also in relation to branches where the recognition and application of foreign resolution actions would endanger financial stability in Jersey or where Jersey depositors would not receive equal treatment with depositors in the bank's home (or other) jurisdictions.

76. Therefore, the Draft Law has been drafted on the basis that the Jersey Resolution Authority has the power (after consulting with the relevant foreign resolution authority) to refuse recognition of foreign resolution actions with regard to branches of foreign banking groups operating in Jersey.

77. As detailed above, it is the Government's view that it will only ever be in highly exceptional cases that the Jersey Resolution Authority would ever refuse to recognise a parent bank's resolution action and seek to resolve the Jersey branch of a foreign bank. However, it is considered necessary to keep the power for the Jersey Resolution Authority to make an instrument refusing to recognise the foreign resolution action in the event that such an action would adversely and possibly detrimentally affect Jersey's financial stability. This point also links to the broad scope of Article 3 of the Draft Law (as discussed above).

Part 7 – Bank Winding Up

78. It is a general principle of BRRD, the Banking Act, and of policy of the Government that a failing bank be wound up through normal insolvency proceedings unless the application of one or more stabilisation tools is necessary to achieve the resolution objectives.

79. In the interests of the efficient stabilisation of a failing bank and in order to avoid conflicts of jurisdiction, in the event that the Jersey Resolution Authority takes a decision to stabilise a bank using the stabilisation tools, normal insolvency proceedings (including the bank winding-up procedure) will be excluded (or, if applicable, discontinued). This will not preclude the Jersey Resolution Authority from applying for a bank winding-up order where:

    a. the Jersey Resolution Authority has attempted to stabilise the bank but has subsequently concluded that it has failed to do so; or

    b. the Jersey Resolution Authority has successfully stabilised a failing bank but the bank winding-up procedure is required and used in conjunction with the stabilisation tool(s) to wind up the residual bank, at the initiative of, or with the consent of, the Jersey Resolution Authority.

80. Where the decision has been taken to allow a bank to become insolvent (or in the absence of a decision to take action to prevent it becoming insolvent), the bank will be wound up using an appropriate procedure to ensure that depositors who are eligible for compensation under DCS either receive payouts promptly or have their accounts transferred to another bank, and to ensure that the bank is wound up with minimum disruption to critical services. As part of the preparation of the Jersey Resolution Regime it was noted that the Banking Act sets out a bespoke procedure for dealing with insolvent banks in the UK. It was concluded that current Jersey insolvency law is limited in the extent to which it provides for the recovery or stabilisation of failed banks, particularly where such banks involve a global or group nexus.

81. It was therefore considered necessary to create a specific bank winding-up procedure in order to set out the appropriate procedure for addressing the

insolvency and liquidation of a failed bank. The intention of such a procedure is to codify the bank winding-up procedure resulting in a framework which will clearly explain the relationship between the solvent stabilisation tools of the Jersey Resolution Regime on the one hand, and the insolvent winding up of a bank under the bank winding-up procedure on the other.

82. The Bank Winding-up Procedure is one of the resolution tools (but not a stabilisation tool) that can be selected by the Jersey Resolution Authority when considering the best course of action to respond to a failed or failing bank.

83. The Bank Winding-up Procedure outlines a decision-making process that must be followed before an application may be made to Court for a bank winding-up order. The decision-making process determines whether it is appropriate to stabilise the bank through the use of one or more stabilisation tools, or whether it would be more appropriate to wind the bank up using the Bank Winding-up Procedure. In addition, the bank winding-up procedure may be used to wind up a residual bank following the transfer-out of shares, assets, rights or liabilities from a failed bank.

84. Furthermore, the Bank Winding-up Procedure is intended to achieve objectives that are consistent with the need to protect customers' access to deposits, taking into account the role of the JDCS, and which protects the provision of other critical services provided by the failed bank.

85. Government's policy is that the Bank Winding-up Procedure should not differ radically from existing Jersey insolvency practice. The Bank Winding-up Procedure is therefore modelled in part on the existing law and practice of the just and equitable winding up procedure set out in Article 155 of the Companies (Jersey) Law 1991 (**Jersey Companies Law**) (as that has been applied in insolvency matters), combined with the powers given to a liquidator under a creditors' winding up in Chapter 4 of Part 21 of the Jersey Companies Law, under the framework of principles and objectives established in the UK's Bank Insolvency Procedure.

86. The aim of the codification of case law principles established in relation to just and equitable winding up under Article 155 is to add clarity and certainty

to the process of winding up a failed bank, and provide reassurance to stakeholders in the stability of the Jersey banking industry.

87. Article 94 (Restriction of other insolvency or winding up proceedings) of the Draft Law prescribes that the commencement of the bank winding up proceedings will bar the right to commence any other normal insolvency proceedings against the bank or a winding up proceeding under Article 155 of the Jersey Companies Law. It also gives the Resolution Authority the power to veto the Court making an order for normal insolvency proceedings or proceedings under Article 155 of the Jersey Companies Law to commence.

Question 12:

Do you have any further comments on the proposals for a Bank Winding Up procedure?

Question 13:

It has been suggested that the Bank Winding-up Procedure should be the only route available to a bank in respect for winding up (in other words, none of the other normal insolvency proceedings routes will be available to a bank). Do you envisage any issues with this proposal? If so, please provide an explanation.

Next steps

88. Following the completion of the period of consultation, any final changes will be made to the Draft Law as a result of responses and the Draft Law will then be lodged for debate.

Questions

Particular questions as stated above are:

Question 1:

Do you agree with the scope of the Draft Law in respect to resolution under Article 3(1) of the Draft Law? If not, then please state why and what you would prefer?

Question 2:

Do you agree with the scope of the Draft Law in respect of the Bank Winding-up Procedure under Article 3(2) of the Draft Law?

Question 3:

Do you agree with the approach being taken in respect of appointments to a Jersey Resolution Authority?

Question 4:

Do you consider that there should be a representative of any other body/group/authority represented on the Jersey Resolution Authority?

Question 5:

Do you think that there should be best endeavours taken to create a Resolution Authority spanning more than one of the CDs?

Question 6:

Do you agree with the approach being taken in respect of the Jersey Bank Resolution Fund? If not, please elaborate on your reasons as to why and how you consider this could be changed?

Question 7:

Do you agree with the approach being taken in respect of creditors' rights and the limitations of liability placed upon the Jersey Bank Resolution Fund? Could the drafting be improved to achieve the aims of transferring liability? If you do not agree with the approach taken, please elaborate on your reasons why, and state how you consider this should be changed?

Question 8:

Are there any preferences in terms of the approach to be adopted in regard to the creditor hierarchy and as to the appropriate balance to be struck between a policy which favours maximising recoveries in the event of a DCS payout or one that reduces the chances of a 'no creditor worse off' claim by greater harmonisation with the law of England and Wales?

Question 9:

Do you agree with the application of the 'no creditor worse off' principle as set out in the Draft Law? Should it be further constrained by a caveat unless such interference is necessary in the public interest? And if so should the principle also be linked to Article 78?

Question 10:

Do you agree that the definition of covered deposits should be linked to the existing Jersey definition as those covered by the Jersey Deposit Compensation Scheme? If not please state what definition should be adopted?

Question 11:

Do you agree with the approach being taken in respect of liabilities that are excluded under the Draft Law? If so, please explain what the issues are and how you consider they could be rectified.

Question 12:

Do you have any further comments on the proposals for a Bank Winding Up procedure?

Question 13:

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