

THE STATES OF DELIBERATION
of the
ISLAND OF GUERNSEY

COMMITTEE *for* ECONOMIC DEVELOPMENT

PROPOSED AMENDMENTS TO THE PREFERRED DEBTS (GUERNSEY) LAW, 1983

The States are asked to decide:-

Whether, after consideration of the policy letter entitled 'proposed amendments to the Preferred Debts (Guernsey) Law, 1983 dated 12th March 2020, they are of the opinion:-

1. To approve the proposals to amend the Preferred Debts (Guernsey) Law, 1983 (the "**PD Law**") so that where the Guernsey Banking Deposit Compensation Board (the "**Board**") has, in respect of a qualifying deposit, exercised its right of subrogation pursuant to the provisions of the Banking Deposit Compensation Scheme (Bailiwick of Guernsey) Ordinance, 2008 the total, capped, amount paid by the Board as compensation under the Guernsey Banking Deposit Compensation Scheme takes priority (in the winding up of the defaulting bank) over all other preferred debts within the meaning of the PD Law (the "**Super Preference**").
2. To agree that any amounts recoverable in respect of a qualifying deposit in excess of the Preference, should rank behind the Preference and current preferred debts in the PD Law but above any remaining ordinary unsecured creditors.
3. To direct the preparation of such legislation as may be necessary to give effect to the above decisions.

The above Propositions have been submitted to Her Majesty's Procureur for advice on any legal or constitutional implications in accordance with Rule 4(1) of the Rules of Procedure of the States of Deliberation and their Committees.

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The Presiding Officer
States of Guernsey
Royal Court House
St Peter Port

12th March 2020

Dear Sir

1 Executive Summary

1.1 This policy letter recommends the enactment, by the States of Deliberation, of amendments to the Preferred Debts (Guernsey) Law, 1983 (the "**PD Law**"). The aim of the proposed amendments is to place the total amount paid, in respect of a qualifying deposit¹, by the Guernsey Banking Deposit Compensation Board (the "**Board**") as compensation, pursuant to the provisions of the Banking Deposit Compensation Scheme (Bailiwick of Guernsey Ordinance, 2008 (the "**Ordinance**") in respect of which the Board has a right of subrogation² as a preferred debt (in the winding up of a defaulting bank) ahead of existing preferred debts in the PD Law (after liquidation costs, fees, expenses and secured creditors)³ in the event of a bank default⁴.

2 Background

2.1 One of the responsibilities of the Board is that it must ensure that, in the event of a licensed bank⁵ default, qualifying claimants⁶, in respect of qualifying deposits, are compensated within 3 months of a declaration of default or the date of receipt of an application for compensation, whichever is later.

¹ As defined in the Ordinance.

² In accordance with section 23 of the Ordinance.

³ It is noted that there are other debts which take priority over those referred to in section 1 of the PD Law and it is not intended that they will be affected by any of the proposals in this policy letter.

⁴ As defined in section 9 of the Ordinance.

⁵ An entity which has been licensed by the Guernsey Financial Services Commission pursuant to section 6 of the Banking Supervision (Bailiwick of Guernsey) Law, 1994.

⁶ As defined in section 12 of the Ordinance.

- 2.2 In light of international developments, the Committee *for* Economic Development (the “**Committee**”) wishes to amend the PD Law so that the amounts paid by the Board as compensation under the Guernsey Banking Deposit Compensation Scheme (the “**Scheme**”), in respect of qualifying deposits subrogated to the Board, rank as preferred debts, ahead of other debts which are currently referred debts under the PD Law and unsecured creditors, on the default of a licensed bank. This would put the Board in a better position to (i) recover monies from a licensed bank in default, (ii) repay monies drawn from existing facilities and from the licensed banks (not in default) and (iii) respond to another default in the following 5 year period.
- 2.3 The EU Bank Recovery and Resolution Directive (the “**BRRD**”) was formally adopted by the European Council in May 2014 with the purpose of establishing a common framework for the recovery and resolution of credit institutions and certain investment firms throughout the EU. It also introduced a new hierarchy of creditors in respect of a bank which became insolvent, which member states were required to transpose into domestic legislation.
- 2.4 The new hierarchy now includes a mandatory ‘super preference’ for deposits protected by EU deposit guarantee schemes and the schemes themselves, such as the financial services compensation scheme (the “**FSCS**”), for amounts below £85,000. This means that, on the insolvency of a UK bank, the FSCS will be a senior class of unsecured creditor⁷ and is likely to recover more of its costs than under the previous creditor hierarchy.
- 2.5 This new hierarchy has implications for the Bailiwick, the Board and Bailiwick resident parties who hold accounts with EU banks which operate branches and/or subsidiaries in the Bailiwick.
- 2.6 The new order of creditor priorities means that depositors with deposits (up to €100,000), placed in an EU bank (including EU branches of that bank) and covered by an EU deposit guarantee scheme (“**covered deposits**”) now rank ahead of other creditors⁸. Other depositors with deposits in non-EU branches (including those covered by the Board) (“**eligible deposits**”), are ranked below these “covered deposits”, but above other debts effectively existing as a ‘secondary preference’.
- 2.7 Deposits from a Guernsey subsidiary placed with its EU parent bank (i.e. deposit monies which are “up streamed” to the EU parent bank) are treated as unsecured debts and will rank below (i) a covered deposit and (ii) a secondary preference on a bank default.

⁷ The FSCS will rank below certain creditors including, inter-alia, tax, social security and pension contributions as set out in categories 1-6 of schedule 6 of the Insolvency Act 1986.

⁸ See footnote 7.

- 2.8 The Committee has noted that the legislative changes in the UK and EU referred to above, have prioritised the claims of EU covered deposits over those held in a Guernsey branch of a UK/EU bank covered by the Board and over other unsecured deposits (such as “up-streamed” funds from a Guernsey subsidiary to an EU parent as indicated above).
- 2.9 Given the exposure of the Bailiwick and its domestic depositors, the Committee is of the opinion that the domestic regime needs to be amended to protect, as far as is possible, the interests of the Bailiwick’s depositors and the Board.

3 Debt Preference in Guernsey

- 3.1 The PD Law provides for the order of priority in which debts should be paid in the distribution of property of a person whose affairs have been declared to be in a state of “desastre” or on the winding up of an insolvent company⁹ in Guernsey, Alderney, Herm and Jethou¹⁰.
- 3.2 The Committee recommends amending the PD Law so that the initial capped amounts paid by the Board, as compensation to qualifying claimants, in respect of qualifying deposits, which have been subrogated to the Board, are the highest ranking preferred debts (the “**Super Preference**”).
- 3.3 Any amounts, in respect of qualifying deposits, in excess of the Super Preference, shall rank behind the Super Preference, and preferred debts in the PD Law, but above any remaining ordinary unsecured creditors.

4 Recognition of other Crown Dependency Deposit Compensation Schemes

- 4.1 The States of Jersey approved the establishment of the Jersey Bank Depositors Compensation Scheme (the “**Jersey DCS**”) in 2009. In 2012 Article 32 of the Bankruptcy (Désastre) (Jersey) Law 1990 was amended to give preferred creditor status to the Jersey DCS where the rights of an eligible depositor,¹¹ in respect of an eligible deposit, have vested in the Jersey DCS board, but not exceeding the total amount payable by the Jersey DCS Board in respect of that debtor as compensation. At this point in time no other depositor compensation schemes are recognised as having the same rights as the Jersey DCS though the intention is for discussions to be had in this regard.
- 4.2 On the 11th September 2015, the Isle of Man Department of Economic Development (the “**Economic Department**”) issued a consultation paper on the

⁹ Section 1 of the PD Law.

¹⁰ Section 10 of the PD Law.

¹¹ As defined in the Banking Business (Depositors Compensation) (Jersey) Regulations 2009.

introduction of preferred creditor status for bank deposits compensated under the Isle of Man Depositors Compensation Scheme (“IoMDCS”). The Isle of Man Treasury has introduced preferred creditor status for “eligible protected deposits” in respect of amounts that do not exceed compensation payable under the IoMDCS regulations.

- 4.3 The Committee’s view is that it is unlikely that a Guernsey branch, of a clearing bank subsidiary situated in a Crown Dependency, would be declared in default without the subsidiary also being declared in default in its home jurisdiction. In the event of a mutual default, both in the Bailiwick (in respect of a branch) and in another Crown Dependency (in respect of the relevant subsidiary), the intention is that the mutual recognition of each Crown Dependency’s depositor compensation schemes (in respect of subrogated qualifying deposits) would take effect providing equivalent protection¹².
- 4.4 In the case of a UK incorporated bank (with a Guernsey branch) going into default, whilst the Board would pay out to parties who had qualifying deposits in accordance with the terms of the Ordinance, the Board would rank as a party with a secondary preference as referred to in paragraph 2.6 of this policy letter as result of its right of subrogation in respect of qualifying deposits.

5 Consultation

- 5.1 A consultation paper in respect of the above proposals was issued by the Committee. Following an analysis of the responses, the policy proposals were developed which set out the changes which the Committee intends to take forward.

6 Compliance with Rule 4

- 6.1 In accordance with Rule 4(1) of the Rules of Procedure, of the States of Deliberation and their Committees, the propositions have been submitted to Her Majesty’s Procurer for advice on any legal or constitutional implications.
- 6.2 In accordance with Rule 4(4) of the Rules of Procedure, it is confirmed that the propositions above have the unanimous support of the Committee.
- 6.3 In accordance with Rule 4(5) of the Rules of Procedure, the Committee has consulted on these proposals and it is confirmed that that the propositions reflect the Committee’s mandate.

Yours faithfully

¹² Subject to any relevant caps and relevant legislative changes being made across all the Crown Dependencies.

C N K Parkinson
President

A C Dudley-Owen
Vice-President

N R Inder
D deG de Lisle
J I Mooney