

States of Jersey
States Assembly



États de Jersey
Assemblée des États

Economic Affairs Scrutiny Panel



States 
of Jersey

Jersey Innovation Fund

Presented to the States on 27th March 2013

S.R.4/2013

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1. PANEL MEMBERSHIP AND TERMS OF REFERENCE

1.1 The Economic Affairs Scrutiny Panel is comprised of the following members:

Deputy S.G. Luce, Chairman

Connétable S.W. Pallett, Vice-Chairman

Connétable M.J. Paddock

1.2 The following Terms of Reference were established for the Review:

1. To undertake an examination of key elements of the proposals to create a Jersey Innovation Fund, including:

- i. eligibility criteria and how 'innovation' is defined for the purpose of the Fund
- ii. the constitution and role of the 'Jersey Innovation Fund Board', and the associated role of the Minister for Economic Development
- iii. the appropriateness of increased risk in the investment of public funds, and how such risk will be managed
- iv. the processes to manage the Fund's income and its operational costs

2. To establish what work has been undertaken on plans to enable equity investment, and what work remains to be completed.

3. To examine how the Jersey Innovation Fund compares to similar initiatives in relevant jurisdictions.

2. GLOSSARY OF TERMS

- Application Form - Application Form in draft
- Chamber of Commerce - Jersey Chamber of Commerce
- Chief Officer, ED - Chief Officer of Economic Development
- CMD - Chief Minister's Department
- Connétable of St Brelade – Vice Chairman of the Panel
- Deputy of St Martin – Chairman of the Panel
- EDD - Economic Development Department
- EAU – Economic Advisor's Unit
- ERDF – European Regional Development Funding
- Expert Advisor – External Advisor from CIPFA
- Policy Framework – Innovation Fund Policy Framework in draft
- JIF - Jersey Innovation Fund
- Operational Terms of Reference – Jersey Innovation Fund, Operational Terms of Reference – September 2012
- Royalty Agreement – Royalty Agreement in draft
- T&R – Treasury & Resources Department
- The Minister for ED - The Minister for Economic Development
- The Minister for T&R - The Minister for Treasury & Resources
- The Panel – Economic Affairs Scrutiny Panel
- The Proposition - P.124/2012 Jersey Innovation Fund: Establishment, Funding & Operation
- TDF – Tourism Development Fund

3. CHAIRMAN'S INTRODUCTION

- 3.1 The concept of operating Innovation Funds is not new, indeed various funds have been in place not only in the United Kingdom and Europe, but also around the globe, for many years now. This doesn't mean, however, that it isn't still a concept that needs supporting, and the Economic Affairs Scrutiny Panel would certainly wish it to succeed. The fact that it is not a brand new concept means that there are a number of very successful examples for us to study, learn from, and follow. The Panel would therefore, at the outset, wish to endorse this initiative from the Economic Development Department, one that is another important part of the new Growth and Diversification Strategy.
- 3.2 Notwithstanding the above, it became apparent from the outset of this review that there were, if not contradictions, then certainly contrasting and contrary views as to how the proposed fund was going to operate. The Economic Development Minister, in the first hearing we held with him, stated that "the devil was in the detail", but it soon became clear to the Panel that "the detail" was not consistent with the Report and Proposition that have been tabled for debate by the Assembly. After six public hearings, and other meetings with civil servants held by our advisor, it is still apparent to the Panel that there are a considerable number of questions that have not been sufficiently well answered.
- 3.3 Taxpayers' money is hard earned, and it is the duty of Government to make sure it is well used. Investment in innovation can be risky, and if we are to invest in "risk" then we need to be assured that that risk is at least minimised as much as possible. This can only be done with the use of strict and consistent rules and guidelines. At present those rules and guidelines are not in place.....or at least are inconsistent across the various elements of "red tape" that the Panel were presented with. There was also a clear difference between the opinion of those people we heard evidence from, and the detailed paperwork that the Panel received during the review.
- 3.4 The Panel wish this initiative to move forward, and we wish the Fund to be a success, but both these things will only happen when there is a consistency across the whole of the Report, Proposition and the underpinning detail. The Panel look forward to reviewing

some additional amended material in the very near future, after which they are hopeful of being able to offer their full support to this new, and important, scheme.....a scheme that could prove to be hugely beneficial in these difficult economic times.

A handwritten signature in black ink, appearing to read 'S.G. Luce', with a long horizontal flourish extending to the right.

Deputy S.G. Luce

Chairman

Economic Affairs Scrutiny Panel

4. EXECUTIVE SUMMARY

- 4.1 Whilst in principle the Jersey Innovation Fund (JIF) is welcomed by the Panel, there is currently an unacceptable level of inconsistency within the proposals. The proposals also lack clarity and key details that might reasonably be in place, and available to Members and stakeholders, given the close proximity of the proposed States debate that would establish the fund. Until these issues are given consideration, reluctantly, the Panel finds itself in a position where it cannot support the establishment of the JIF. The Panel has recommended that, in this context, the Minister for Economic Development must consider and address the issues, as outlined in this report, before the JIF Proposition is debated by the States. Indeed, the Panel intends to review the Minister's response and any revised proposals in advance of their debate.
- 4.2 Although intended as a fund of £10million, it is proposed that the JIF will launch initially with £5million, with an additional £5million to be allocated at a later, undefined stage. This second tranche of funding is crucial to the prospects of the Fund. The source of the additional £5million has yet to be confirmed by the Minister for Treasury and Resources, and the Panel is clear that, for the avoidance of any doubt, the source of this second £5million should be clearly identified before the States debate.
- 4.3 The JIF is proposed to launch as a Government Fund, however, matched funding with private venture capital (i.e. a Partnership Fund) was commonly identified as a preferred model. It is suggested that serious consideration should be given by the Minister for Economic Development to adopting a Partnership Fund model, in order to harness the considerable benefits of leverage, shared risk and private sector expertise. Stakeholder organisations also agreed that basing the JIF on the principle of 'lender of last resort' was unsuitable, given its implied negativity about the quality of potential applications.
- 4.4 It is accepted by the Panel that due to the nature of the new and innovative businesses that could be supported by the JIF, not all investments would be successful, and the consequent failures could result in loans not being repaid and/or objectives not being met. A level of 'failure' would need to be accepted by the States, balanced against the positive benefits that the JIF is seeking to achieve. The Minister for Economic Development raised the potential for high percentage levels of 'failure', initially suggesting this could be as high as 70%. There is a general consensus, however, that in terms of fund recipients going out of business, such a high rate of failure would be unacceptable.

- 4.5 Looking at 'success', it was apparent there were commonly identified success criteria, such as creation of locally qualified jobs, financial return to the JIF and general taxation contributions. However, these were prioritised differently amongst the stakeholders, including the two Ministers responsible for the JIF. To address this and to provide clarity about the very purpose of the JIF, there must be a common position established by the Ministers for Economic Development and Treasury and Resources regarding the prioritisation of success criteria.
- 4.6 Indeed, greater clarity is required more generally on defining both 'failure' and 'success' as they relate to the JIF, both in an overall sense and as applied to individual, funded projects. It is recommended that this should include development of a precise framework for the monitoring of the performance of individual projects and the financial performance of the overall Fund, including a formal mechanism to establish the circumstances under which the possible temporary or permanent closure of the JIF might be considered.
- 4.7 Further clarity is also required to better define the roles and responsibilities of key external organisations and States Departments whose resources and input are required by the JIF. There should be formal discussions held at the earliest opportunity with Digital Jersey and Jersey Business regarding their roles, which in the case of Jersey Business includes a recommendation from the Panel that consideration should be given to that organisation undertaking the functions of the JIF Executive. There is concern that the roles and responsibility of other States Departments must be more clearly defined, most notably those of the Law Officers and Treasury and Resources. In addition, a number of issues relating to the work of the Law Officers Department that remain outstanding (through no fault of their own) must be resolved prior to the States debate, not least the development of the Royalty Agreement template.
- 4.8 There is clear inconsistency between the stated aim of the Fund being available to all sectors of the economy on the one hand, and the heavy emphasis placed on targeting high value, high growth opportunities on the other. In fact, there are a number of seemingly over-restrictive eligibility criteria including the need to demonstrate the ability to achieve a level of at least £65,000 GVA per employee, to demonstrate the potential for 'high growth', and the requirements relating to an applicant being a Business incorporated under the Companies (Jersey) Law 1991. These could all effectively rule out many potential applications, particularly in the third and public sectors, and traditional industries such as tourism and agriculture. If the JIF is realistically to be made available to the third and private sectors, and non-finance

industries, the proposed eligibility criteria relating to GVA per employee and high growth business should be amended to a less demanding level. Additionally, it is a conclusion of the Panel that the JIF should not adopt the principle of minimum or maximum funding levels per applicant.

- 4.9 Although the proposed JIF is intended to be self replenishing, with stakeholders agreeing that this was a sensible aspiration, it is difficult within the context of high suggested 'failure' rates, grants, costs, lender of last resort principle, differing 'success' priorities and in particular the initial absence of the equity element amongst others, to envisage that the JIF will meet this aim. There is therefore the distinct possibility of the JIF becoming a sinking Fund. It is imperative that the JIF should retain the objective of being self-replenishing. It is vital therefore to ensure that, amongst other elements, a clear financial objective and Key Performance Indicators are established, grants are only awarded absolutely 'in extremis' and that the equity element is developed, as proposed, within 6 months.
- 4.10 Costs are also a major concern of the Panel. It became apparent early in the Review that the £100,000 estimated for the operational and management costs of the JIF did not apply to anything other than the external expert advice that would be required. No full and transparent assessment of the 'invisible' costs that would be incurred by States Departments to fulfil the administration and monitoring functions of the fund has been made. Without defining the cost of the internal resource requirements, it is difficult to determine how the fund is performing and to measure its overall success relative to cost. This is taxpayers' money, and value for money must be achieved. The Panel's adviser has indicated that it is quite possible that total estimated charges to the Fund could equate to within a range of £250,000 to £400,000 per year.
- 4.11 The Panel has recommended that a best estimate of annual operating costs for the management of the JIF, including all overhead support (external and internal costs), should be provided. Additionally, it recommends an assessment of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the utilisation of the Fund. Transparency on this exercise will effectively provide an indication of the true utility of the JIF.

5. FINDINGS

- 1) The official definition of innovation for the purpose of the JIF is understandably wide ranging in scope. However, with no clear case studies identified and more restrictive eligibility criteria, a degree of uncertainty has been introduced about the type of projects the JIF aims to support. (8.2.9)
- 2) It is proposed that the JIF will launch and initially operate in the model of a Government Fund, making financial support available in the form of repayable loans or non-repayable grants. (8.3.5)
- 3) Although the JIF is proposed to launch as a Government Fund, matched funding with private venture capital (i.e. a Partnership Fund) was identified as the preferred model by stakeholder organisations, and recognised as a leverage opportunity by the Minister for Economic Development. (8.3.16)
- 4) It is proposed that the JIF is to be a fund of last resort and, in order to qualify for a loan, evidence must be produced by an applicant to show that all alternative funding has been exhausted. There is general consensus that 'last resort' terminology is unhelpful. (8.4.15)
- 5) Stakeholder organisations agreed that basing the JIF on the principle of 'lender of last resort' was unsuitable, given its implied negativity about the quality of potential applications. (8.4.15)
- 6) It is accepted that due to the nature of the new and innovative businesses that might be supported by the JIF, not all investments will be successful. Consequent failures could result in loans not being repaid and/or objectives not being met. A level of 'failure' would need to be accepted by the States, balanced against the positive benefits that the JIF is seeking to achieve. (8.5.5)
- 7) The Minister for Economic Development raised the potential for high percentage levels of 'failure' amongst those projects given funding through the JIF, initially suggesting this could be as high as 70%. There is consensus, including from the Minister, that in terms of JIF recipients going out of business, such high rates would be unacceptable. (8.5.5)
- 8) There is a lack of clarity about what defines 'failure' both in relation to the JIF overall and the individual projects receiving funding. (8.5.5)

- 9) More clarity and detail is required regarding the monitoring mechanisms that would enable, amongst other things, the possible identification of the need to discontinue the JIF before it is depleted, should it not be performing successfully. (8.5.11)
- 10) There is a lack of clarity about what defines 'success' in relation to the JIF and the individual projects receiving funding. (8.5.21)
- 11) The Economic Development Department only estimates between 5-10 full applications would be fully progressed each year, of which it is estimated 4-5 applicants would be successful in gaining funding. (8.5.21)
- 12) With regard to the overall Fund, there were common success criteria identified, such as the creation of locally qualified jobs, financial return to the JIF and general taxation contributions. However, these were prioritised differently amongst the stakeholders, including the two Ministers responsible for the JIF. (8.5.21)
- 13) To avoid becoming a sinking fund, the JIF must have a clear financial objective, and key performance indicators (KPI's) should be defined from the outset. (8.5.21)
- 14) Although intended to constitute a £10million fund, it is proposed that the JIF will launch initially with £5million, with an additional £5million to be allocated at a later, undefined stage. The source of the additional £5million has yet to be confirmed by the Minister for Treasury and Resources. (8.6.10)
- 15) It is widely agreed that, although a fund of £10million is small compared to many other such schemes, it nevertheless represents a suitable scale for Jersey and was seen by stakeholders as a positive step. (8.6.10)
- 16) The potential level of demand for the JIF has not been assessed through formal research by the Economic Development Department, and is effectively unknown. However, stakeholder organisations and the sponsoring Ministers are hopeful of introducing or attracting sufficient levels of applicants with good ideas to the Fund. (8.6.10)
- 17) Although the lodged Proposition report clearly sets out that the JIF would be available to support a wide range of activity, it is not clear to the Panel how the third or public sector would be able to access the fund based on the demanding criteria of the JIF Policy Framework and the Eligibility Guidelines found on the application form. (8.7.7)

- 18) Although the lodged Proposition, report and Operational Terms of Reference contain no indication of a minimum or maximum funding level per applicant, this is contradicted by the inclusion of minimum £20,000 and maximum £500,000 funding amounts on the draft application form and policy framework documents. (8.7.19)
- 19) Stakeholders, and initially both sponsoring Ministers, agreed that there was little or no merit in setting minimum or maximum funding levels. However, the Minister for Economic Development later suggested that a minimum level may even be set higher than £20,000. (8.7.19)
- 20) The JIF Policy Framework and the Eligibility Guidelines on the application form establish the need for an applicant to be a Business incorporated under the Companies (Jersey) Law 1991. This appears to be inconsistent with the Operational Terms of Reference, which don't indicate such a narrow scope or criteria. It raises concerns that a number of potential applicants to the JIF might be inadvertently excluded, in that Partnerships, LLP's and sole traders might be ineligible to apply. (8.7.24)
- 21) The requirement for an application to demonstrate £65,000 GVA per employee effectively rules out potential applications from the third and public sectors, and many non-finance industry related projects. (8.8.7)
- 22) The GVA levels per employee and high growth requirements could effectively rule out many potential applications, particularly in the third and public sectors, and traditional industries such as tourism and agriculture. (8.8.11)
- 23) The 'high growth' requirement states that an applicant must demonstrate the potential to double revenues or employment within four years and to employ at least ten full time equivalent staff by the end of the four year period. This appears highly restrictive. (8.8.11)
- 24) There is clear inconsistency between the stated aim of the Fund being available to all sectors of the economy on the one hand, and the emphasis placed on targeting high value, high growth opportunities on the other. (8.8.11)
- 25) The application process places considerable demands on an applicant, beginning with the initial 15 point request for a written report and supporting documentation contained on the application form. As the application process progresses, there are additional

- demands for information through the due diligence process, Funding Agreement development and post loan monitoring and reporting. (8.9.8)
- 26) A balance is required between the required quality due diligence, and the need to make the application process as free of 'red tape' as possible, in order to ensure that it is timely and not off-putting to potential applicants. (8.9.8)
- 27) Stakeholder organisations were united in their expectation of a timely and efficient, yet robust, due diligence process. The Panel has concerns about the ability of the due diligence process as currently proposed to meet those sound expectations. (8.10.6)
- 28) It is clearly proposed that grants will only be made in exceptional circumstances. (8.11.9)
- 29) Any grant or repayable loan would be the subject of a detailed Funding Agreement. Each Funding Agreement would be unique and include details of any specific clauses, including repayment terms and timing arrangements for repayment. (8.12.13)
- 30) Although the JIF Operational Terms of Reference broadly propose consultation between the Board, the Treasurer of the States and the Minister for Economic Development, the process by which loan repayment terms and interest rates are to be established is not clear, with no formal details or guidelines available. (8.12.13)
- 31) The Panel is concerned by the number of outstanding questions relating to Royalty Agreements, and the limited progress that has been made by the Economic Development Department at this stage in progressing the template document, which is currently only in early draft form. (8.12.18)
- 32) Should the States approve the first phase of the JIF, there are proposals for a second stage to be introduced within 6 months to enable the States to make equity investments in funded projects. This is a significant step and a departure from common States practice regarding loans, and requires additional expertise and also new legislation. (8.12.28)
- 33) Although the proposed JIF is intended to be self replenishing, with stakeholders agreeing that this was a sensible aspiration, it is difficult within the context of high suggested 'failure' rates, grants, costs, lender of last resort principle, differing 'success' priorities and in particular the initial absence of the equity element amongst others, to envisage that the JIF will meet this aim. There is therefore the distinct possibility of the JIF becoming a sinking Fund. (8.12.28)

- 34) The emphasis on the requirement for the JIF Executive to have considerable and specific business expertise, as outlined in the Operational Terms of Reference and identified as being crucial by stakeholders, has been reduced by the Economic Development Department to that of a basic administrative role. (9.1.18)
- 35) Some Innovation Funds in other jurisdictions are managed by external agencies who undertake all due diligence in reference to the management of the fund with no apparent conflict. In view of this and stakeholder consensus on the need for expertise and efficiency in the support provided to the JIF Board, it is conceivable that Jersey Business is well positioned to undertake the role and responsibilities of the JIF Executive. (9.1.18)
- 36) There is a discrepancy between the limited role Treasury and Resources expects to undertake in the JIF, and the level of involvement that Economic Development has envisaged for Treasury and Resources. (9.2.10)
- 37) In addition to the Economic Development and Treasury and Resources Departments, the JIF proposals establish the requirement for formal roles to be undertaken by the Economic Advisor's Unit and the Law Officers' Department. (9.2.15)
- 38) The Panel is disappointed by the level of consultation undertaken by the Economic Development Department with other relevant Departments, most notably the Law Officers. This has led to a situation where there is lack of detail and progress on key areas, such as the Royalty Agreement, despite the close proximity to the proposed debate. (9.2.15)
- 39) The JIF Board would be responsible for the management of the Fund, assessing all applications and making recommendations to the Minister for ED. It would be comprised of a minimum of two members and a Chair from the private sector, plus ex officio, non-voting representatives from the Economic Development, Treasury and Resources and Chief Minister's (Economic Advisor's Unit) Departments. This could set the Board structure as three private sector members and three public sector members. (9.3.10)
- 40) The Panel recognises the need and value of the public sector members of the JIF Board, but it is ultimately the private sector expertise recruited to the JIF Board that would be crucial to the potential success of the Fund. (9.3.10)

- 41) Although the Economic Development Department has outlined significant roles and input for both Digital Jersey and Jersey Business in the JIF, disappointingly it has not undertaken formal consultation with either organisation despite the imminent date of the States debate on the Proposition. (9.4.13)
- 42) The financial and manpower implications statement in the Proposition estimates 'the operational and management costs' of the JIF to be £100,000. However, it was soon apparent that the £100,000 did not apply to anything other than the external expert advice that would be required, and took no account of internal costs such as the resourcing of the JIF Executive by the Economic Development Department. (9.5.12)
- 43) It is quite possible that total estimated charges to the Fund could equate to within a range of £250,000 to £400,000 per year, undermining the ability of the JIF to be self replenishing. (9.5.12)
- 44) It is proposed that the operational and administration functions of the JIF would be covered by existing Departmental resources, which the Panel was told would therefore be of no cost to the Fund. This approach does not transparently account for the internal 'invisible' costs of the Fund and the man hours it requires. (9.5.22)
- 45) No full and transparent assessment of the 'invisible' costs that will be incurred by States Departments to fulfil the administration and monitoring functions of the fund has been made. Without defining the cost of the internal resource requirements, it is difficult to determine how the Fund is performing and to measure its overall success relative to cost. (9.5.22)
- 46) **Concluding Finding:**

Whilst in principle the JIF is very much welcomed by the Panel, there is an unacceptable level of inconsistency within the proposals, which also lack clarity and key details that should reasonably be in place and available to Members and stakeholders at this stage of the process. Until these issues are resolved, the Panel cannot support the establishment of the JIF.

6. RECOMMENDATIONS

- 1) It is recommended that a Partnership Fund would be a more suitable model to move to, in order to harness the considerable benefits of leverage, shared risk and private sector expertise. This should be given serious consideration at the earliest opportunity. (8.3.16)
- 2) Greater clarity is required on defining both 'failure' and 'success' as they relate to the JIF, both in an overall sense and as applied to individual, funded projects. This should include:
 - a precise framework for the monitoring of the performance of individual projects and the financial performance of the overall Fund;
 - a formal mechanism to establish the circumstances under which the possible temporary or permanent closure of the JIF might be considered. (8.5.21)
- 3) To provide clarity about the very purpose of the JIF, there must be a common position established by the Ministers for Economic Development and Treasury and Resources regarding the prioritisation of the various success criteria. (8.5.21)
- 4) The source of the second £5 million due to the Fund should be clearly identified by the Minister for Treasury and Resources. (8.6.10)
- 5) The JIF should not adopt the principle of minimum or maximum funding levels per applicant. (8.7.19)
- 6) Partnerships, LLP's and sole traders must not be excluded from applying for funding. Therefore, there should be clarification of the consequences of the requirement for an applicant to be a business incorporated under the Companies (Jersey) Law 1991. (8.7.24)
- 7) If the JIF is realistically to be made available to the third and private sectors, and non-finance industries, the proposed eligibility criteria relating to GVA per employee and high growth business should be amended to a less demanding level. (8.8.11)
- 8) Whilst ensuring effective and robust processes are established where required, such as due diligence, continued attention should be paid to ensuring that the JIF is not overburdened by red tape. (8.9.8)

- 9) Outstanding issues relating to the work required of the Law Officers Department must be resolved, not least the development of the Royalty Agreement template, prior to the States debate. (8.12.13)
- 10) The JIF should retain the objective of being self-replenishing. It is vital therefore to ensure that in addition to implementation of the Panel's monitoring and cost related recommendations:
 - a clear financial objective and Key Performance Indicators are established;
 - formal guidelines are established between the relevant Departments regarding interest rate levels, and the process for establishing loan repayment terms is clearly set out;
 - the equity element is developed, as proposed, within 6 months;
 - grants are awarded only 'in extremis'. (8.12.28)
- 11) The Minister for Economic Development should formally engage with Jersey Business, with a view to that organisation undertaking the functions of the JIF Executive. (9.1.18)
- 12) All States Departments involved in the JIF must have their roles and responsibilities more clearly defined, most notably the Law Officers and Treasury and Resources. This will require formal discussions and should result in clear guidelines outlining their particular responsibilities. (9.2.10)
- 13) It is recommended that the number of Board members recruited from the private sector, through a full and formal recruitment process, should be set at a minimum of four (inclusive of the Chairman). (9.3.10)
- 14) The Minister for Economic Development must engage in formal discussions at the earliest opportunity with Digital Jersey and Jersey Business, regarding their roles in the JIF. (9.4.13)
- 15) A best estimate of annual operating costs for the management of the JIF, including all overhead support (external and internal costs), should be provided. Additionally, an assessment should be undertaken of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the utilisation of the Fund. Transparency on this exercise will effectively provide an indication of the true utility of the JIF. (9.5.22)

16) **Concluding Recommendation:**

Due to the level of inconsistency in the proposals, and the lack of key details that could reasonably be available to Members and stakeholders at this stage, the Minister for Economic Development should consider the findings and recommendations contained within this report, and address the issues it raises, before the Proposition is debated by the States.

7. INTRODUCTION: BACKGROUND TO THE REVIEW

- 7.1 The principle of setting up a 'Jersey Innovation Fund' (JIF) was established as part of the Economic Growth and Diversification Strategy, adopted by the States in July 2012. Such funds in various forms have been established and operate in a number of countries, including the UK, Ireland, Malta and Israel, which in particular has been used as a reference point by the Economic Development Department (EDD) during the development of the JIF. The key objective of the Economic Growth and Diversification Strategy is to deliver growth, improve competitiveness, diversify the local economy and create employment. To achieve this, a key strategic aim is to encourage innovation and improve Jersey's international competitiveness. During the course of the debate last July, the Chairman outlined the Panel's intention to undertake a Review of the JIF at an appropriate time, as more detailed proposals emerged.
- 7.2 The Proposition to establish the JIF, *P.124/2012 Jersey Innovation Fund: Establishment, Funding and Operation*, (The Proposition) was lodged au Greffe on 20th November 2012 in the name of the Minister for Treasury and Resources (Minister for T&R). Although primarily an initiative of the Minister for Economic Development (Minister for ED), the Proposition has been lodged by the Minister for T&R to fulfil the requirements of Article 3(3)(a) of the Public Finances (Jersey) Law 2005, whereby the States may, on a proposition lodged by that Minister, establish a special fund for specific purposes.
- 7.3 The JIF itself seeks to support innovation through financial investment by the States in a wide range of activity, from direct business support to strategic infrastructure investments across the private, public and third sectors. Under the proposals, the £10million fund would be established with an initial allocation of £5 million coming from part of the redemption of JT Group Limited's 9% cumulative preference shares. At the time of launching the Panel's Review the source of the remaining £5 million had yet to be confirmed, and this remains the case as we present our report.
- 7.4 The Panel first received drafts of the Proposition, accompanying report and Jersey Innovation Fund, Operational Terms of Reference (Operational Terms of Reference) for the Fund on 21st September 2012, and updated versions on 16th October, along with an indication of an intention to lodge au Greffe within a week. At that stage the documents were in draft form and, therefore, understandably subject to confidentiality.

- 7.5 The Panel agreed that if the Proposition was lodged as intended, it would not have adequate time to undertake the work expected of it if the minimum six week lodging period was applied, as it needed to fully and publically explore the significant proposals with the relevant stakeholders, something that could only be achieved with publishable versions of the documents referred to above. The Panel wrote to the two relevant Ministers (see 7.2) to request that they consider agreeing that the debate should not take place before the States meeting on Tuesday 29th January 2013 (a date that has been subsequently pushed back further by the complications presented by the unplanned lodging of *P.113/2012 Tourism Shadow Board: Establishment* by the Minister for ED and the increasing concern of the Panel, as laid out in this report, that the JIF Proposition required further work before the Panel would be in a position to fully review it). Throughout the process the Panel and Ministers have maintained a constructive dialogue, and the Panel welcomes the approach of both Ministers who have been understanding of the requirements and obligations of Scrutiny, and have taken on board and agreed to the Panel's suggestions regarding the scheduling of the debate.
- 7.6 Having assessed the documentation available at the time, the Panel agreed and published the Review's Terms of Reference in December 2012 and launched a public call for evidence inviting contributions from all interested individuals and stakeholders. Targeted requests for evidence were also made to the two Ministers and to key stakeholder groups, notably Jersey Business, Digital Jersey and Jersey Chamber of Commerce who all attended Public Hearings. The Panel also secured independent expert advice from CIPFA Business Ltd, who have provided considerable assistance to the Panel, particularly on the technical aspects of the JIF. CIPFA's report on the JIF is attached to the Panel's as Appendix 2.
- 7.7 Although positive about the concept of an Innovation Fund, it soon became clear to the Panel as evidence gathering began that there seemed to be a lack of detailed planning behind the proposals, despite the imminent States debate, for instance regarding the costs associated with administering the Fund and the extent of formal consultation undertaken with key stakeholders. It also emerged that there were some worrying contradictions between the visions of the JIF held by various stakeholders, including the Ministers themselves - perhaps a symptom of the concerns regarding the level of formal consultation. Indeed, the Panel has also witnessed the 'evolving' positions of certain individuals on various elements of the JIF as the Review progressed, which has been the cause of some considerable confusion. There were a number of key

areas in which these differences were apparent, including amongst many others the scope of the JIF, defining an 'innovative' project, the purpose of the Fund, what success looked like and how risk would be managed.

- 7.8 The Panel's concerns were only intensified when it was presented with additional draft documentation as the Review progressed, notably the Innovation Fund Policy Framework (Policy Framework) and Jersey Innovation Application Form (Application form). There was further concern about the limited information provided to the Panel during correspondence with EDD requesting updates about the development of a template Royalty Agreement.
- 7.9 Although they were in draft form, once received it was reasonably expected that there would be little change to these documents given the proximity of the scheduled debate on the JIF, and because, with the exception of the Royalty Agreement, these were documents that were clearly in an advanced, apparently complete format. The Panel are concerned that further changes to the draft documents would clearly change the nature of the fund.
- 7.10 There were notable further inconsistencies and contradictions between this additional information and the lodged 'package' of the Proposition, report and Operational Terms of Reference, not least regarding minimum/maximum levels for the loans (or possibly grants) and crucially the eligibility criteria. It also raised further questions about the level of detail planning that had been undertaken, or indeed remained to be done.
- 7.11 This report presents the findings (Section 5) and recommendations (Section 6) of the Panel on the proposed Jersey Innovation Fund based on the evidence received. In Section 8 'Scope, Eligibility and Access: Key Elements Examined' there is a full exploration of who can access the fund and how (i.e. the envisaged application process), followed in Section 9 by an examination of the resource implications and costs associated with the fund.

8. SCOPE, ELIGIBILITY AND ACCESS: KEY ELEMENTS EXAMINED

8.1 Purpose and Objectives of the JIF

8.1.1 In order to achieve the key strategic aim of the Economic Growth and Diversification Strategy to encourage innovation and improve Jersey's international competitiveness, an identified priority is to establish the JIF. The aim of the Fund is to support innovation, and it will be available to support a wide range of activity, from direct business support to strategic infrastructure investments, in the private, public and third sectors.

8.1.2 The scheme is intended to be operated and managed following the Operational Terms of Reference which are attached to the Proposition. The key features are:-

- *A new independent "Innovation Board" will be established, with a minimum of 2 members and a Chair from the private sector. There will also be representatives of EDD, Treasury and Resources (T&R) and the Chief Minister's Departments (CMD) on the Board.*
- *The Board will be responsible for the management of the Fund, assessing all applications and making recommendations to the Minister for ED. The Board will be supported by a Fund Executive from EDD (from within existing establishment)*
- *The Board will assess each application on a number of economic and commercial criteria, which will require the provision of detailed information from applicants. As a minimum, this will include an economic impact assessment undertaken by the Economic Adviser's Unit (EAU).*
- *The Board will make recommendations to the Minister for ED in regard to each application*
- *Support to businesses will be by repayable loans and grants. The aim is that support will mainly be by repayable loans, as EDD's medium-term aim is for the Fund to be self-replenishing*
- *Any loans or grants to be made from the Fund will be authorised by the Minister for ED*

- *All loans and grants will be made in accordance with the Public Finances (Jersey) Law 2005 and comply with relevant Financial Directions*
- *Each loan or grant will have a formal Funding Agreement signed before funds are released. This will include any specific clauses and set out the rights and obligations of both parties*
- *Each agreement will be regularly reviewed by EDD for compliance with agreed terms, and the operation of the Fund will be subject to audit review*

8.2 What is Innovation?

8.2.1 In its broad sense, the concept of innovation can be defined as follows:

- *...not just a new idea but can be an advancement or improvement on something that is existing*
- *A new method, idea or product*
- *The action or process of innovating¹*

8.2.2 The Operational terms of Reference contains a definition of innovation for the purpose of this Fund, which reads:

Innovation encompasses a wide range of activities from research and development, to organisational change, training, testing, marketing and design. It contains products, services and other solutions that that can be new to the business or the international market.²

8.2.3 The Panel asked the key witnesses at public hearings to define what they believed innovation to be, to try to get a clear idea of the expected targeting and demand of the JIF. There were, as can be seen below, a range of responses:

Minister for ED

"...I would define innovation as a new idea, a new method or a new product, the idea being able to create high value, and importantly to create job opportunities. It is about new ideas, new methods and new products, in summary, and the execution thereof..."

³

¹ www.wikipedia.com

² Operational Terms of Reference – P.124/2012 – page 19

³ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 2

Minister for T&R

“...Innovation means securing new businesses and jobs in economic areas that are outside financial services and that are new...”⁴

President, Jersey Chamber of Commerce

“...I would be looking for natural progression...”⁵

Chairman, Jersey Business

“... it is difficult to predict. There are a number of companies here that we have come across who have ideas ranging from the mundane to what I would call the innovative to the highly innovative, and there are degrees of risk associated with all of them...”⁶

Chairman, Digital Jersey

“...it could be a completely new idea that is taken to market. It could be an extension of an existing business...the innovation fund is not just about technology and we completely understand that...”⁷

- 8.2.4 Aware that there appeared to be wide parameters to the definition of Innovation for the Fund, which could potentially cause confusion from those trying to access and those trying to run the JIF, the Panel asked the Ministers to provide a case study example of the sort of ‘successful’ application they might envisage.
- 8.2.5 A number were provided and many can be seen in the transcripts of our Hearings with the Ministers, but they have not provided the Panel with the clarity that might be expected at this stage. Instead, it appeared that many of the examples given would simply not qualify for funding based on inconsistency and incompatibility with one of more of the many eligibility criteria (see 8.7), including a sweet shop example that it was widely agreed was not innovative, and for which it is anyway difficult to envisage as being high value and high growth. Where innovation could be potentially seen, for instance in the example of a highly successful entrepreneur who, before his success, required £500 of start up funding – if he had applied to the JIF he would have been turned away for being under the £20,000 minimum (see 8.7.8) loan requirement.
- 8.2.6 The Panel also became aware of a reference that had been made by the Chief Minister at a Jersey Hospitality Association lunch in March 2013, linking the upcoming Innovation Fund and the successful Jersey Heritage ‘Forts and Towers’ project, as an

⁴ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 3/4

⁵ Public Hearing with President of Chamber of Commerce – 6th February 2013 – page 16

⁶ Public Hearing with Jersey Business – 6th February 2013 – page 5

⁷ Public Hearing with Digital Jersey – 6th October 2013 – page 3

example of the type of project that may receive funding. However, during a hearing with the Minister for ED, this example was provided by the Chief Officer, ED, but it appeared to have been contradictory to the eligibility criteria.

8.2.7 The Chief Officer, ED, explained the benefits and additional revenue this particular project had produced. The Panel explored further the eligibility criteria and asked the Chief Officer if this project would be able to show it had met the criteria of an additional 10 staff after 4 years. The Chief Officer, ED said:

Chief Officer, ED (hearing with Minister for ED on 22nd February 2013)

“...I do not know whether that particular entity has done that, but what I do know is that the level of employment associated with the forts and fortifications is certainly not zero and it is certainly quite significantly higher than ... well, it is not zero, because they were not there before...”⁸.

8.2.8 During the same hearing, the Panel Chairman asked:

Deputy of St. Martin:

“...We mentioned the development of the castles and forts around and turning them into tourist attractions, but the application form also says that the applicant has to be a high-growth business. Surely that would not qualify, because a high-growth business by definition has to double its revenue and its employment within 4 years and employ at least 10 fulltime equivalent staff by the end of the fourth year...”

Chief Officer (hearing with Minister for ED on 22nd February 2013):

“...I am not necessarily saying that the forts and fortifications fits that criteria...”⁹

8.2.9 The Panel was therefore surprised that the forts and towers scheme was still being used to illustrate the type of application that may receive innovation funding, and was concerned that inconsistency appeared to remain between the anticipated targeting of the fund and the defined eligibility criteria.

Key Finding:

The official definition of innovation for the purpose of the JIF is understandably wide ranging in scope. However, with no clear case studies identified and more restrictive eligibility criteria, a degree of uncertainty has been introduced about the type of projects the JIF aims to support.

⁸ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 11

⁹ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 10

8.3 The Type of Fund

- 8.3.1 The principle of governments encouraging, supporting and making investment into innovation is not a new concept. Jersey is unusual in not having such support available to support economic development. The UK, Malta and Singapore are 3 examples where government funds have, with significant success, been used to boost innovation. Whilst there are some common features, each jurisdiction has a unique operating model. Although Innovation Funds are operated in other jurisdictions successfully, these schemes are invariably designed to attract significant inward investment primarily focused on global markets. The Funds that are in operation in the UK, Ireland and Malta attract some regional economic support funded in part through the EU by way of European Regional Development Funding (ERDF) and channelled through the central/local government infrastructure of these respective countries.
- 8.3.2 Government funds operating in other jurisdictions follow their own operating model which is used to support the specific priorities and objectives of that jurisdiction. Within the Operational Terms of Reference, an analysis of Innovation Funds from across a number of jurisdictions allows operating models to be characterised into 3 main types:-

The Fund of Fund

A Government Fund managed by public sector fund managers who make strategic investments in a number of established private sector Venture Capital funds. The Government funding is directed towards Venture Capital funds that are of strategic importance; for example technologies or renewable energies. Coupled with private sector funding, these privately managed funds invest in private sector businesses. All investments are equity finance arrangements where a share in the company is taken in return for the investment. The returns on any government investments are linked to the overall performance of the venture capital fund and not linked to any one specific organisation.

The Partnership Fund

A Government managed fund that invites private sector Venture Capital fund managers to submit applications for co-funding to increase the availability of risk capital for early-stage and high-growth companies. Government does not own any equity in the private enterprises; this is retained by the venture capital organisation. Returns on any investments are linked to either the overall performance of the venture capital fund or a specific organisation.

The Government Fund

A fund that provides financial support in the form of repayable loans and/or non repayable grants direct into a private sector enterprise. The fund is normally managed by an independent Board with members from both the public and private sector. The returns made on loans are linked to a combination of arrangement fees, interest rates and special clauses allowing it to benefit from any increases in value, sales growth, or the licensing of any intellectual property.¹⁰

- 8.3.3 It is proposed that the JIF will launch and initially operate as a Government Fund, making available financial support in the form of repayable loans or non-repayable grants. The assumption is that the majority of support will be provided in the form of repayable loans, with conditions that allow the JIF to realise enhanced returns if the business were to be successful and/or sold for significant gain. It is envisaged that non repayable grants will only be considered in exceptional circumstances.¹¹
- 8.3.4 Following the launch of the JIF, the Minister for T&R will develop the necessary draft legislation, for States approval, that will allow the Fund to make equity investment in privately owned business. This will require an element of the JIF to be operated as a Partnership Fund. (See Section 8.12.20).
- 8.3.5 The Operational Terms of Reference makes reference to a Government Fund which is currently operating in Israel. This fund is extremely successful and references and comparisons to this fund are used throughout this report. However, the Panel's advisor has advised that whilst there is much that can be learned from the operation of Innovation Funds across the world it is important that the objectives and operating context aligned to each Fund is fully appreciated. Aspects of the funds operated in the UK and Israel have some similar attributes to the JIF although the key differences on the extent of venture capital fund matching remain. Indeed, differences in operating environment, primary objectives and underpinning funding make true comparisons difficult.¹²

Key Finding:

It is proposed that the JIF will launch and initially operate in the model of a Government Fund, making financial support available in the form of repayable loans or non-repayable grants.

¹⁰ Operational Terms of Reference – P.124/2012 – page 10

¹¹ Operational Terms of Reference – P.124/2012 - page 10

¹² CIPFA Report – page 8

8.3.6 Matched Funding

8.3.7 As outlined above, it is intended that the fund will launch initially as a Government Fund, followed in time by an equity element. It is important to note that in order for the JIF to be eligible for matched funding, it would have to move from being a Government Fund as proposed, to a Partnership Fund model. Ireland and Israel (amongst others) are two jurisdictions that operate successful Innovation Funds on this basis. It is not proposed within the JIF proposition to pursue matched funding. However, matched funding was raised by the industry stakeholders as a sensible principle with which to underpin the JIF, and the Panel has therefore explored this concept further.

8.3.8 Jersey Business suggested gaining leverage for the fund would help minimise risk and double the size of the fund. The Chairman believed it could be an opportunity to improve the fund:

Chairman, Jersey Business

“...Government could initiate it but is it the best executer of investment and investment policy? Traditionally not. Traditionally it is a very poor investor. Can it improve that through the proposed structure in the Innovation Fund proposition? Yes, it can. Can it improve that through drawing on expertise as is anticipated outside of that panel? Yes, it can. Can it do that by co-venturing with other investors? Yes, it can. I mean there is a wide open opportunity here...”¹³

8.3.9 Digital Jersey were also in favour of matched funding with the Chairman stating:

Chairman, Digital Jersey

“...I think for the future there will be ways to have a multiplier effect with the funding that comes from the States, matched funding with other Venture Capital. It is a very common model. A jurisdiction puts in X, a venture capital company or investment company comes in and matches it, and then you leverage the size altogether. So I think there are a number of models that could be considered in the near future as to how to get a greater fund to be invested in the industry...”¹⁴

8.3.10 The Panel raised matched funding with the Minister for Economic Development at the concluding public hearing. During the hearing, it became apparent that, despite its absence from the lodged proposals, the Minister and his Officers were amenable to the concept. The Chief Officer, ED, (Chief Officer of Economic Development) spoke of the model that is currently used in Ireland:

¹³ Public Hearing with Jersey Business – 6th February 2013 – page 14

¹⁴ Public Hearing with Digital Jersey – 6th February 2013 – page 18

Chief Officer (Hearing with Minister for EDD on 22nd February 2013)

“...The Irish model is quite interesting - I think we do cite this - where they have taken, I think, €125 million, which is a little bit more than we have, and have said to the venture capital community or private equity community: “If you match that with €125 million you could administer the €250 million fund, but it has to be administered with the criteria that we define.” So, yes, that is what they do. That is an alternative model...”¹⁵

8.3.11 He added:

“...if we want this thing to be generally self-sustaining the percentage of equity investments would be very high, but if that were the case that probably leads you towards having the type of model the Irish have deployed where they do match those funds with external funds and it is managed externally, because that is where the genuine investment expertise is and this is not just in the area of pre-award evaluation...”¹⁶

8.3.12 The Minister for ED (hearing on 22nd February 2013) went on to say:

“...That is quite an interesting model when you consider the amount that we do have available. As the Chief Executive (Chief Officer of Economic Development) has said we have a fund of £5 million...but the opportunity to leverage that amount by the exact model described is a very interesting opportunity in my view...But, again, even £10 million is, although a large sum of money in the context of Jersey in some respects, in the greater scheme of things, when looking at funds of this nature, is quite small. So we do need to look at opportunities for leveraging it...”¹⁷

8.3.13 However, on the Policy Framework document, it is stated that:

For the avoidance of any doubt the Fund will not compete or replace private sector funding, only to be used after all other sources of funding and security have been fully utilised, and be used to invest in innovative projects.

8.3.14 The Panel raised this issue at the final public hearing, and asked whether or not this rules out matched funding for the JIF. The Chief Officer, ED, stated that the wording did not rule out match funding and stated:

¹⁵ Public Hearing with Economic Development – 22nd February 2013 – page 35

¹⁶ Public Hearing with Economic Development – 22nd February 2013 - page 36

¹⁷ Public Hearing with Economic Development – 22nd February 2013 – page 36

Chief Officer. ED (hearing with the Minister for ED on 22nd February)

“...it is being misinterpreted and I can understand why it sounds far too draconian in this context...”¹⁸

8.3.15 The Panel’s expert advisor has stated within his report that true comparisons with other jurisdictions is difficult:

Whilst there is much that can be learned from the operation of Innovation Funds across the world it is important that the objectives and operating context aligned to each Fund is fully appreciated. Aspects of the funds operated in the UK and Israel have some similar attributes to the JIF although the key differences on the extent of venture capital fund matching remain. Indeed, differences in operating environment, primary objectives and underpinning funding make true comparisons difficult.¹⁹

8.3.16 The expert advisor continued:

We would agree that the closest Fund type to the proposed JIF, in its initial stages, is a Government Fund as outlined within the Report on the Establishment, Funding and Operation of the JIF. However, the example given of Israel should be taken with some caution given the differentials in state expansionary objectives and operating environment. At the Panel Meeting with the Minister for Economic Development on 22 February 2012 it was clear that aspirations on match funding and equity will invariably move the positioning on fund type towards a Partnership Fund type rather than a Government Fund Type.²⁰

Key Finding:

Although the JIF is proposed to launch as a Government Fund, matched funding with private venture capital (i.e. a Partnership Fund) was identified as the preferred model by stakeholder organisations, and recognised as a leverage opportunity by the Minister for Economic Development.

Recommendation:

It is recommended that a Partnership Fund would be a more suitable model to move to, in order to harness the considerable benefits of leverage, shared risk and private sector expertise. This should be given serious consideration at the earliest opportunity.

¹⁸ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 39

¹⁹ CIPFA Report – page 8

²⁰ CIPFA Report – page 8

8.4 Fund of Last Resort

- 8.4.1 The Proposition states that in order to qualify for a loan, evidence must be produced to show that all alternative funding has been exhausted (letters from bank, etc). During the public hearings with each of the Ministers, the term “fund of last resort” emerged and was used as terminology for the fund throughout the public hearing process. The Minister for ED explained the idea behind the fund of last resort:

Minister for ED (hearing 14th January 2013)

“...Clearly there is a hope and expectation that this will provide businesses with funding, funding as the last resort, as has been pointed out already, to stimulate innovative new ideas, develop businesses and, as such, give them the confidence and the requirement to employ local people...”²¹

- 8.4.2 The Minister for Treasury & Resources also informed the Panel that the JIF was explicitly intended to be a lender of last resort:

Minister for T&R

“...It is one of the criteria defined in the report, because what we want to be is a fund of last resort...”²²

- 8.4.3 The use of the term posed some issues. Jersey naturally has a significant number of bank lenders and has a well developed network of private lending. If they wouldn't lend, what did this say about the quality of the idea of applicants who would be trying to access the JIF?
- 8.4.4 There was consensus amongst the industry stakeholders that we received evidence from, that establishing a fund based on the principle of lender of last resort was not a suitable option, with the implications it carries. The President of the Chamber of Commerce raised the concern that it implied nobody else was willing to fund the idea, and therefore it may not be worthy of funding in the first place. Consequently, if the poor ideas were the ones appearing at the door of the Fund, finding the next big thing and seeing the financial rewards of that will be almost impossible. He said:

²¹ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 14

²² Public hearing with the Minister for Treasury & Resources – 10th January 2013 – page 15

President, Jersey Chamber of Commerce

“...If the private sector, and I mean this in the banks or any other form, Angel funds or anything, do not think it is great idea obviously this fund would become a fund of last resort almost. It is the last one you come to after everybody else has either told you your scheme is rubbish or it does not go and so the chances of finding a diamond in it all is quite limited. So again we have to be wary of that...”²³

8.4.5 He continued:

“...Finding that diamond is going to be a tough one to make because that diamond theoretically should have been found by a lot of other people way before the Innovation Fund got to see it...”²⁴

8.4.6 Digital Jersey were asked their view on the “fund of last resort”, and echoed the concerns raised by Chamber of Commerce:

Chairman, Digital Jersey

“...I have only just seen that comment and I could not disagree with it more. I do not see the innovation fund as being the fund of last resort at all. I would suggest that if it is viewed that way and if we ask: “Have you been to this bank? Have you been to this person?” what we will be left with is a whole bunch of dross that we are not going to invest in...”²⁵

8.4.7 He continued:

“...From what I have seen of the innovation fund it could be a really aspirational thing. What we are looking at in Digital Jersey is creating diversification in the sector, bringing in catalysts from overseas if you like. We need something that will appeal to the talent already on the Island to give them confidence that they will be able to create a new business perhaps with help from overseas...”²⁶

8.4.8 There was acknowledgement that the nature of bank lending at present was a hinderance to even good ideas accessing funding, with a more cautious attitude prevalent. Jersey Business for instance made the following point:

²³ Public Hearing with the Chamber of Commerce – 6th February 2013 – page 3

²⁴ Public Hearing with the Chamber of Commerce – 6th February 2013 – page 9

²⁵ Public Hearing with Jersey Business – 6th February 2013 – page 7

²⁶ Public Hearing with Digital Jersey – 6th February 2013 – page 7

Chief Executive, Jersey Business

“...In days gone past the banks might lend on collateral or they might lend against earnings, today, make absolutely no mistake, yes, you need those earnings and a business plan that says this is a viable business, but on top of that you need the collateral. For a lot of particularly younger business or young entrepreneurs and new ventures that collateral is not here. You have to get past it...”²⁷

8.4.9 The Chairman, Jersey Business also stated that:

“...At the moment the banks, in part because of the economy, and in a large part because of the capitalisation requirements that are being imposed on them, are simply withdrawing from the supply of credit. They are not doing that because they are not getting good propositions through the door. They are doing it because they have to reduce their own balance sheets. In that economy or in that economic situation can a fund like this assist? Can it accelerate? Can it meet the objectives that we talked about to begin with and are clearly stated in the fund? Yes, it can...”²⁸

8.4.10 At our final hearing with the Minister for ED, the Minister and the Chief Officer, ED, explained their reservations about the terminology, but not the principle, explaining:

Minister for ED (hearing on 22nd February 2013):

“...I do not like the phrase...”²⁹

Chief Officer, ED (hearing with Minister for ED on 22nd February 2013)

“...It is still a fund of last resort, is it not? The phrase is not a great phrase; I will give you that, which is what I think people are railing against. Think of the other end of the spectrum. If a company comes to us and they have a very robust balance sheet, very good cash reserves, and they come along to the Innovation Fund and say: “We have this great idea; can we have some money?” The obvious question has got to be: “Well, why?” Almost, if you go to the other end of the spectrum, the people who will come to us is probably because (a) they have not been able to raise the amount of money either privately, or (b) if they have gone into the banking system, they do not have the collateral so to do. So maybe fund of last resort, which is sort of common parlance for the way the public sector does fund, makes it sound a bit more draconian than it is...”³⁰

²⁷ Public Hearing with Jersey Business – 6th February 2013 – page 9

²⁸ Public Hearing with Jersey Business – 6th February 2013 – page 16

²⁹ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 36

³⁰ Public Hearing with Minister for Economic Development – 22nd February 2013 - page 37

8.4.11 The Chief Officer, ED, elaborated on his disagreement with the implication that last resort implied poor quality of application:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...The point I am trying to make, I suppose, is that it is about the quality of the proposal. There is nothing wrong with being the funder of last resort and it does not mean that what you are looking at ... I think the word that has been used is “dross”. Well, that is not the case. There are a lot of people with a lot of very, very bright ideas who for reasons, some of which are through no fault of their own, do not have the ability to raise funds. There is effectively a market failure...”³¹

8.4.12 The Panel followed up the issue of Jersey being in a privileged position regarding having a considerable amount of private wealth on the Island, noting that this raised further questions about the sustainability of the JIF and the potential that only the ‘poorer’ ideas would make it to the Fund once banks and private investors had been exhausted. It was acknowledged by the Chief Officer, ED, that there were a significant amount of investors in Jersey who may be willing to look at such projects, but with an important caveat that would mean this source of funding would render certain projects unviable:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...There is, absolutely, at “healthy interest rates...”³²

8.4.13 The Panel explored the intended last resort status of the JIF in the context of matched funding (see Section 8.3.6) with the Minister for ED and his Officers at the closing Hearing on 22nd February. The Chairman of the Panel explained that that all stakeholders had been positive about the JIF incorporating principles of matched funding, seeing that as the most appropriate way forward. He continued:

Deputy of St Martin

“...It doubles our money. It gets us involved with third parties who will also have an involvement and people thought it would be very attractive for third parties to get involved with Government in schemes, but we keep coming back to this fund of last resort which seems, above all, to say, “Well, no, we cannot do that because it is not the last resort...”³³

³¹ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 38

³² Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 38

³³ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 38

8.4.14 Responding, the Chief Officer, ED, said

Chief Officer (hearing with the Minister for ED 22nd February 2013)

“...If I am a private individual and I want to invest in a business and I can get Government to stump up half the money, I have halved my risk. But is that what we are seeking to do? Are we seeking to compete with the private sector and advantage them in that way or are we seeking to fund the things that may be very, very good quality opportunities but have not been able to secure that funding?...”³⁴

8.4.15 The Panel’s expert advisor has noted in his report that further clarification is needed on the fund being the lender of last resort as it could add risk if there are no other sources of funding. It was noted that the phrase “fund of last resort” was extremely unpopular with the executive and the stakeholders and could be seen as a poorly chosen one.

Key Finding:

It is proposed that the JIF is to be a fund of last resort and, in order to qualify for a loan, evidence must be produced by an applicant to show that all alternative funding has been exhausted. There is general consensus that ‘last resort’ terminology is unhelpful.

Key Finding:

Stakeholder organisations agreed that basing the JIF on the principle of ‘lender of last resort’ was unsuitable, given its implied negativity about the quality of potential applications.

8.5 Hopes of Success, Expectations of ‘Failure’?

8.5.1 All funds must have an expectation of success and failure to monitor their performance in order to achieve their objectives. The Proposition states that EDD have identified that due to the nature of the new and innovative businesses being supported, not all “investments” will be successful, and there will be failures which may result in loans not being repaid or objectives not being met. This will be a reality and runs counter to the normal inherent “risk averse” nature of public finance accountability. Therefore a level of “failure” will need to be accepted by the States and be balanced against the positive benefits that the JIF is seeking to achieve.

8.5.2 To minimise the risk of failure, it is essential that the framework for assessing applications to the Fund, as set out by EDD, must be rigorously applied and adhered to, along with robust ongoing monitoring of performance and risk. The Minister for ED

³⁴Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 38

made reference to an Innovation Fund in Israel, highlighting the fine balance between success and failure (i.e. the rate of failure of businesses that received funding), outlining clearly that high failure rates could well apply to the JIF:

Minister for ED (hearing on 14th January 2013)

“...There could well be, in terms of numbers or in percentage terms, really high percentages of failures. Now this does not mean it does not succeed of course....”

“...If you look, for example, at Israel, some of the funds created there had a very high failure rate. I think it was running at - something like 70 per cent of the projects supported failed. The key thing is that the 30 per cent that succeeded, succeeded very strongly and met the aims and the fund has been self-replenishing and indeed growing since the time that it was initially pump-primed by government...”³⁵

- 8.5.3 Responding to the potential failure rates that the Minister had originally highlighted, the Chief Executive of Jersey Business summed up the general theme of the comments on this issue expressed by stakeholders, saying:

Chief Executive, Jersey Business

“...if a venture capital fund had a 70 per cent failure rate it would not be around very long. It seems exceptionally high. I think that is a pessimistic figure...”³⁶

- 8.5.4 There was some confusion however about the level of ‘failure’ being allowed or prepared for. At the final hearing with the Minister for ED, he clarified that he was not in fact referring to 70% of businesses provided with funding failing, but making the point that 30% were high value exits (from the fund) and that 70% were still investments with the fund itself:

Minister for ED (hearing on 22nd February 2013)

“...I think the 70% failure rate was referring specifically to the Jerusalem Fund and that was referring in particular to the exits, 30% of which were high value exits. The balance, the 70% is in fact still investments that the fund itself held. They are not referring to businesses that have gone out of business in that sense but they just simply had not exited to the value that the 30% had...I would say that we would not dream of seeing 70% of businesses failing; using the definition “going out of business” that is...”³⁷

³⁵ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 15

³⁶ Public Hearing with Jersey Business – 6th October 2013 – page 10

³⁷ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 45

8.5.5 Speaking at the Public hearing with Minister for T&R on 10th January 2013, the Chief Officer, ED advised that:

“...it is only in extremis that things will fail...” “...if there are things starting to go wrong I would hope that we will be in a position to intervene and to correct that...in the event of failure it may be necessary to write those monies off because we are investing in innovation...”³⁸

Key Finding:

It is accepted that due to the nature of the new and innovative businesses that might be supported by the JIF, not all investments will be successful. Consequent failures could result in loans not being repaid and/or objectives not being met. A level of ‘failure’ would need to be accepted by the States, balanced against the positive benefits that the JIF is seeking to achieve.

Key Finding:

The Minister for Economic Development raised the potential for high percentage levels of ‘failure’ amongst those projects given funding through the JIF, initially suggesting this could be as high as 70%. There is consensus, including from the Minister, that in terms of fund recipients going out of business, such high rates would be unacceptable.

Key Finding:

There is a lack of clarity about what defines ‘failure’ in relation to the JIF overall and the individual projects receiving funding.

8.5.6 When to say “enough is enough”?

8.5.7 Given the potential failure rates identified and the issues around self replenishing and defining success, the Panel sought to establish what mechanisms were in place to potentially stop effectively ‘throwing good money after bad’. It is not stated within the Proposition, or any of the documentation behind it, when to undertake the decision to discontinue the fund through lack of performance – should this be required.

8.5.8 The Panel asked the Minister for T&R if, after 18 months there is only £3 million left in the fund and nothing to show for it, do we stop or do we carry on? He told the Panel:

³⁸ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 30

Minister for T&R

“...No, I think if that is the result then we put another shot of caffeine into the machine and we work up and say: “What has gone wrong? What can we do? What lessons can we learn?” Failure is not an option here. There is no plan B of failure. We have got to make this stuff work and we are going to make it work...”³⁹

8.5.9 The Panel asked the stakeholders what their view was on the potential discontinuation of the fund should it not be performing successfully. The President of Jersey Chamber of Commerce commented:

President, Jersey Chamber of Commerce

“...if you lose your first £5 million I think the enthusiasm for putting another £5 million in it would obviously weigh dramatically. Whether he would like to do that or not I think politically it would be very difficult to do...”⁴⁰

Deputy of St Martin

“...If we get halfway through this £5 million and we have nothing to show for it at all we need to just say: “Stop and let us look at other ways of using the money we have left”?...”

President, Jersey Chamber of Commerce:

“...I think that is a sensible approach, yes...”⁴¹

8.5.10 When the point was raised with the Chairman, Digital Jersey, he commented:

Chairman, Digital Jersey

“...I would never say you do something and that is it, you are going to do it for ever. I think initiatives like this really have to be judged on their success and if it is not working then you do not carry on doing it...”⁴²

8.5.11 The Panel’s advisor has indicated that ongoing monitoring is key to enable the fund to meet its objectives yet there are no clear areas as to what this ongoing monitoring will encompass.

³⁹ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 30

⁴⁰ Public Hearing with Chamber of Commerce – 6th February 2013 - page 4

⁴¹ Public Hearing with Chamber of Commerce – 6th February 2013 - page 4

⁴² Public Hearing with Digital Jersey – 6th February 2013 – page 19

Key Finding:

More clarity and detail is required regarding the monitoring mechanisms that would enable, amongst other things, the possible identification of the need to discontinue the JIF before it is depleted, should it not be performing successfully.

8.5.12 Defining Success

8.5.13 The JIF is linked to the overall Economic Growth and Diversification Strategy and the Proposition states that success for this Strategic Aim will be to have established a fund, and assessment framework, that could be used for strategic investments into innovation and new technologies that would deliver a competitive advantage for Jersey, attract additional private sector investment and create new high value businesses resulting in significant new job opportunities in a more diversified economy.

8.5.14 The Minister for T&R outlined to the Panel how he saw success in reaction to the JIF. He said:

“...I think we have got to be really realistic. I think there are serious economic challenges facing Jersey, and I want the Chief Officer to spend the £5 million on getting business start-ups up and running and employing people, so I want them to do it because I suspect that the scale of challenge that we have, which if we respond properly, assertively and boldly enough we can deal with, we can reduce our unemployment numbers and we can start some business start-ups that are going to be the wealth creators of the future...”⁴³

8.5.15 The Panel also asked the Minister for ED what success would look like for the JIF. Responding to whether this would perhaps be seen as being in terms of financial return to the fund, the number of jobs created, regardless of the financial return to the fund or even a combination of that and other things, the Minister said:

Minister for ED

“...It will be the latter. Clearly there is a hope and expectation that this will provide businesses with funding, funding as the last resort, as has been pointed out already, to stimulate innovative new ideas, develop businesses and, as such, give them the confidence and the requirement to employ local people. So job creation is a key outcome that I see from this...”⁴⁴

⁴³ Public Hearing with Treasury & Resources – 10th January 2013 – page 13

⁴⁴ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 14

8.5.16 The Panel asked the Chief Officer, ED, what he would define as success. He explained that success would be seen in terms of the employment creation as well as the pure commercial success of the business, adding that this in turn results in higher levels of returns through general taxation as much as it does to the loan being repaid to the fund.⁴⁵

8.5.17 The President of the Jersey Chamber of Commerce believed that small successes should be measured as equally as the larger projects as they would help build confidence in the economy. He also stated that unless the funding is given sensibly and risks are taken without recklessness:

President, Jersey Chamber of Commerce

“...There is a real danger that you turn around and go to the first guy who comes in and says: “Well, I could not get any funding anywhere else and I need £1 million and it is a great idea” and then someone sort of ...: “We have lent £1 million to something and such and it is a fantastic idea”, there is a real danger that you have tried to force the issue to say: “We have lent the money” without maybe going to: “Well did we lend the money in the right area? Was that a sensible thing to do?”...”⁴⁶

8.5.18 The Chairman of Jersey Business summed the Innovation Fund up as “venture capital with a social conscience”⁴⁷ The Chief Executive added:

Chief Executive, Jersey Business

“...I do not think you should measure success by the financial return on the fund because if that is what you want to do go and be a venture capitalist in the big wide world, in the full market. If that is the purpose of the fund then I do not understand it. But I think there should be an evaluation of the economic benefit to the Island. That would come through from directly out of the accounts that says they paid X amount of tax. The amount of payroll that it stimulated...”⁴⁸

8.5.19 Jersey Business also stressed the importance of the fund having an investment objective, and stated that unless it has a return over a set period of time it will quickly run out of funding:

⁴⁵ Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 5

⁴⁶ Public Hearing with Jersey Chamber of Commerce – 6th February 2013 – page 22

⁴⁷ Public Hearing with Jersey Business – 6th February 2013 – page 21

⁴⁸ Public Hearing with Jersey Business – 6th February 2013 – page 20

Chairman, Jersey Business

“...This fund should have an objective and it should have a return on it. Investment objective, whether that is 20 per cent or 10 per cent or 5 per cent, whether it is a return over 5 years or 10 years, is something to be determined but it must have a return on investment criteria otherwise it will have no money very shortly...”⁴⁹

8.5.20 It is perhaps important to note that any discussion of ‘success’ should be seen in the context of the number of applicants that it is anticipated will be provided funding from the JIF per annum. The Chief Officer, ED, has given a figure of 5-10 applicants per year as a guideline. The Director of Business Creation and Growth gave indication of 4-5 applicants per year as the number envisaged as being successful in gaining funding.⁵⁰

8.5.21 The Panel’s expert advisor has noted that there appears to be no clear positions/views on what successful ventures would look like and no measurements as to the quantification of success. He also stated that investment aimed at driving enterprise and innovation will inevitably invite an element of risk and the balancing of providing an optimal level of stimulus without the impediments of “red tape” together with the minimisation of risk to the fund is usually a difficult one to achieve. There are no indications as to the amount of monies that would be acceptable to write off each year.

Key Finding:

There is a lack of clarity about what defines ‘success’ in relation to the JIF and the individual projects receiving funding. Furthermore, any discussion of ‘success’ should be seen in the context of the number of applications envisaged to receive funding.

Key Finding:

The Economic Development Department only estimates between 5-10 full applications would be fully progressed each year, of which it is estimated 4-5 applicants would be successful in gaining funding.

Key Finding:

With regard to the overall Fund, there were common success criteria identified, such as the creation of locally qualified jobs, financial return to the JIF and general taxation contributions. However, these were prioritised differently amongst the stakeholders, including the two Ministers responsible for the JIF.

⁴⁹ Public Hearing with Jersey Business – 6th February 2013 – page 21

⁵⁰ Meeting with Director of Growth and Business Creation and Expert Advisor – 23rd January 2013

Key Finding:

To avoid becoming a sinking fund, the JIF must have a clear financial objective, and key performance indicators (KPI's) should be defined from the outset.

Recommendation:

Greater clarity is required on defining both 'failure' and 'success' as they relate to the JIF, both in an overall sense and as applied to individual, funded projects. This should include:

- A precise framework for the monitoring of the performance of individual projects and the financial performance of the overall Fund;
- A formal mechanism to establish the circumstances under which the possible temporary or permanent closure of the JIF might be considered.

Recommendation:

To provide clarity about the very purpose of the JIF, there must a common position established by the Ministers for Economic Development and Treasury and Resources regarding the prioritisation of the various success criteria.

8.6 Establishing Demand – is £10million enough?

8.6.1 It is proposed that the JIF will be given £10 million in its entirety, which will be provided in 2 stages of £5 million. The first £5 million will come from the redemption of the JT preference shares, but it remains unclear precisely where the second £5 million will come from. The Minister for T&R has stated that:

Minister for T&R

"...What I have said to EDD is if they get this fund up and running, if they give some good decisions, if they attract good businesses and they spend their £5 million, I will be right behind them and I will find the other £5 million. I cannot tell you where, but I have a number of options available..."⁵¹

8.6.2 The Minister for ED was hopeful that the fund would be a success and would receive the second tranche of £5 million:

⁵¹Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 12

Minister for ED (hearing on 22nd February 2013)

“...Bear in mind this is the first £5 million in what is intended, longer term, to be a £10 million fund. So we will have to...hope that the Minister for T&R remains as enthusiastic about his shot of additional funding, if required, as we move forward...”⁵²

8.6.3 Speaking to the Minister for ED at a Public Hearing, the Panel asked about the number of applications that might be seen in the first 12, 18 or 24 months, which had presumably been used to establish the resource requirements. He explained that it was not as simple as just looking at the overall number of applications, as other factors needed to be considered - such as there being one particularly complicated application requiring specific, extensive analysis. All such factors needed to be borne in mind, but his Department was working to an arbitrary figure that it felt was reasonable.⁵³

8.6.4 The Chief Officer, ED, added at the hearing with the Minister for ED on 14th January 2013:

“...I think we will get a significant number of applications when we launch the fund. Not all of those applications, however, will proceed to the point where we undertake due diligence on them, because effectively they would have to pass through the initial filtering which would be undertaken by members of the board, based on economic and commercial analysis undertaken by the department within our own resources...”⁵⁴

(See also Sections 9.1 and 9.3)

8.6.5 The Chief Officer, ED, expanded further and touched on the number of applicants per annum, and what the budget would be in terms of each application:

“...I think something that we had put together was that somewhere between 5 and 10 per annum would advance to that level and that would allow us a budget of between £10,000 and £20,000 per application to undertake that. That is not inconsistent with the type of figure that we used that we would apply to analysis of the bids for the submissions that we have from consultants...”⁵⁵

Deputy of St. Martin:

We are hoping there might be 10 to 20 applications initially?

⁵² Public Hearing with the Minister for Economic Development – 22nd February 2013 - page 16

⁵³ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 3

⁵⁴ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 4

⁵⁵ Public Hearing with the Minister for Economic Development – 14th January 2013 - page 3

Chief Officer (hearing with the Minister for ED on 14th January 2013)

“...We are hoping there will a larger number of applications than that...”⁵⁶

- 8.6.6 Stakeholders broadly concurred that until the launch of the fund it would be difficult to know the precise levels of demand. However, they were confident that there was or would be significant demand, which indeed they hoped to play their part in introducing to/accessing the Fund. The Chairman, Jersey Business highlighted his confidence in the demand, telling us:

Chairman, Jersey Business

“...I could find within a week an allocation of all £5 million...”⁵⁷

- 8.6.7 The Panel asked if the Chairman would be in a position to suggest over how many different applications that would be:

Chairman, Jersey Business:

“...We could go out and find a very good applicant who could make a business case for a £5 million investment. Absolutely. Is that the best way to invest the fund? Undoubtedly not. Would there be 50 people applying for £20,000 or £50,000 or £250,000? You do not know until you open the door and establish the fact that the funding is there and establish the criteria under which the applications will be assessed and evaluated...We do know from our direct experience that there are a considerable number of people with good ideas who are having difficulty raising finance...”⁵⁸

- 8.6.8 In addition, and specific to his sector, the Chairman, Digital Jersey explained his take on the expected demand and his organisations approach to harnessing the opportunities it may provide:

Chairman, Digital Jersey

“...I think that there is a latent demand here in the Island for business support and business start-up, but I would see it, the use of the innovation fund being to support businesses that are already here that want to extend...”⁵⁹

- 8.6.9 He continued:

“...There is demand and, in fact, I have been involved already as Chairman of Digital Jersey with a couple of local entrepreneurs, or hope to be entrepreneurs, who have

⁵⁶ Public Hearing with the Minister for Economic Development – 14th January – page 3

⁵⁷ Public Hearing with Jersey Business – 6th February 2013 – page 15

⁵⁸ Public Hearing with Jersey Business – 6th February 2013 – page 16

⁵⁹ Public Hearing with Digital Jersey – 6th February 2013 – page 4

ideas in the digital sector that they would like to see funded...I also see us using the innovation fund to help attract and support inward investment as well. I do not think we should underestimate that there are people with good ideas in the digital sector and outside that will come forward to try and access the innovation fund. I think there will be a queue for that...⁶⁰

8.6.10 Digital Jersey also made specific reference to their area of expertise and how they would be aiming their focus on targeting particular clusters of the market. The Chairman, Digital Jersey, explained that his organisation's view was that they will be seeking out and targeting particular clusters, particular areas to stimulate. He added:

'...we really believe that we will need to focus quite tightly within those and that is part of where the research comes in as to which clusters we will be focusing on and then taking the innovation fund, rather than setting up the innovation fund and waiting for people to come to it for application, targeting where we think some of the best uses of those funds could be in different areas...⁶¹

Key Finding:

Although intended to constitute a £10million fund, it is proposed that the JIF will launch initially with £5million, with an additional £5million to be allocated at a later, undefined stage. The source of the additional £5million has yet to be confirmed by the Minister for Treasury and Resources.

Key Finding:

It is widely agreed that, although a fund of £10million is small compared to many other such schemes, it nevertheless represents a suitable scale for Jersey and was seen by stakeholders as a positive step.

Key Finding:

The potential level of demand for the JIF has not been assessed through formal research by the Economic Development Department, and is effectively unknown. However, stakeholder organisations and the sponsoring Ministers are hopeful of introducing or attracting sufficient levels of applicants with good ideas to the Fund.

⁶⁰ Public Hearing with Digital Jersey – 6th February 2013 – page 4

⁶¹ Public Hearing with Digital Jersey – 6th February 2013 – page 4

Recommendation:

The source of the second £5 million due to the Fund should be clearly identified by the Minister for Treasury and Resources.

8.7 Scope of the JIF and Eligibility Criteria: Inconsistencies

8.7.1 The Proposition report states that, if established, the JIF will be available to support a wide range of activity, from direct business support to strategic infrastructure in the private, public and third sectors. The accompanying Operational Terms of Reference state that the Fund will be used to fund projects across all sectors but targeted and prioritised towards:

- *Attracting new innovative businesses to the Island*
- *Assisting early-stage high-value start-up enterprises with access to working capital to enable the Fund to invest in innovation*
- *Supporting established business with high-growth potential to invest in innovation*
- *Financing research projects that may improve the Island's competitiveness*
- *Funding enabling investments in infrastructure*
- *Seed-funding for businesses developing new products/services/processes*
- *Funding for businesses to establish better links with universities, with the objective of commercialising academic IP*⁶²

8.7.2 In addition to the Operational Terms of Reference, EDD has provided an application form (in draft) and a draft 'Policy Framework' all of which outline the scope and eligibility criteria of the JIF to a greater or lesser extent. These documents effectively establish the criteria that must be met before any applications stand the chance of being successful in receiving funding.

8.7.3 The Panel has, however, significant concerns about apparent inconsistencies between these documents and/or the evidence that we took when speaking to the Ministers and stakeholders, concerns which were particularly highlighted upon receipt of the draft application form. It should be noted that the draft application form was received following the initial hearings with the Ministers and stakeholders and, as a consequence, it was unable to be question stakeholders on this area. The Panel did however have the opportunity to raise the issues with the Minister for ED at the final Public Hearing, as seen in the following sub-sections.

⁶² Operational Terms of Reference P.124/2012 – page 14/15

8.7.4 Third and Public Sector

8.7.5 It was unclear to the Panel how the eligibility criteria and such targeting would include realistic opportunities for the third and public sectors to successfully access the Fund. Indeed, the eligibility criteria of the Application Form states that firms must be able to demonstrate the project has potential to improve the overall level of productivity of the economy with value added per employee significantly in excess of £65,000 in order to qualify for funding. In addition, they must be a high growth business with the potential to double revenues or employment within four years and to employ at least 10 full time employees at the end of the fourth year.

8.7.6 It was therefore an area that the Panel explored with the Minister for ED. He acknowledged the point, but explained:

Minister for ED (hearing on 22nd February 2013)

"...It is probably unlikely that many would qualify and it is right that the bar is relatively high when you look at the underlying core objectives of the Innovation Fund, but it is also equally right that they should be included, because it is not impossible..."⁶³

8.7.7 The Minister elaborated on the Department's objective to open the fund to all sectors, telling us in reference to the public sector that:

Minister for ED (hearing on 22nd February 2013)

"...I think it would be wrong to exclude the public sector. I would not imagine there would be very many at all potential applications from the public sector, but I do not think we should discount the fact that the public sector can also come up with innovative ideas. It is always possible..."⁶⁴

Key Finding:

Although the lodged Proposition report clearly sets out that the JIF would be available to support a wide range of activity, it is not clear to the Panel how the third or public sector would be able to access the fund based on the demanding criteria of the JIF Policy Framework and the Eligibility Guidelines found on the application form.

8.7.8 The Minimum and Maximum Amount of Loan per Applicant

8.7.9 There is no area within the lodged Proposition or Operational Terms of Reference to indicate whether the fund will operate on the basis of a minimum and maximum

⁶³ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 15

⁶⁴ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 22

amount available to applicants. At the initial hearings, both Ministers spoke to the Panel about levels of potential funding, with no suggestion of restricting the amounts through defined minimum and maximum amounts given. The Minister for T&R told us:

Minister for T&R

"...They may come to us and need £3,000, just to free up their time and get some basic equipment to get themselves going. So it is about the nature of the proposal they bring to us rather than the monetary contribution. That should not be a filter..."⁶⁵

8.7.10 The Minister for ED was very clear, commenting that there were:

Minister for ED (hearing on 14th January 2013)

"...no pre-set figures in that which is granted..."⁶⁶

8.7.11 Other stakeholders were also of the opinion that there should be no limits on the funding available. The President for the Jersey Chamber of Commerce made the point that the scheme should be for anybody and a judgement call should be made by those running the fund suggesting each opportunity presented is judged on its merits. Jersey Business also stated that they did not believe the fund should have any limitations on funding available.

8.7.12 However, significant confusion was introduced upon receipt of the draft application form. The application form states that the amount requested should not exceed £500,000 and must be greater than £20,000. This development was unexpected.

8.7.13 At the final hearing with the Minister for ED, the Panel was able to address the inconsistency on the matter of the £20,000 minimum and £500,000 maximum amounts and asked the Minister if he could clarify the issue. He suggested that the application form was still in draft format, and therefore there were details yet to be set. However, he did not dismiss the fact that £20,000 could be a minimum amount, despite this significant concept not appearing in the lodged documentation. He stated that:

Minister for ED (hearing on 22nd February 2013)

"...we see this as operating in a niche which broadly covers the range that you referred to..."⁶⁷

⁶⁵ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 20

⁶⁶ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 30

⁶⁷ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 2

8.7.14 The Panel made reference to what both Ministers had said at their previous hearings, essentially that there would be no pre set figures and figures as low as £3,000 would meet the criteria. Speaking to the Minister for ED, he told the Panel:

Minister for ED (hearing on 22nd February 2013)

"...I do not envisage applications of that level, because clearly if somebody is making an application for £1,000, £3,000 or £5,000 it is likely to be for some items of equipment as opposed to a business proposition that is going to seek to deliver on the objectives of a fund of this nature. So there is, by nature, going to be a certain minimum that is going to be considered, I would imagine, by the board as being appropriate to deliver on the objectives..."⁶⁸

Deputy of St. Martin:

"...But do you see that minimum being £20,000, as is in the application form and the policy document?..."

8.7.15 In fact, somewhat surprisingly to the Panel, the Minister for ED went on to suggest that the likelihood was that the minimum funding would be set even higher than £20,000. He told the Panel:

Minister for ED (hearing on 22nd February 2013)

"...I would think it is unlikely to be as low as that, but not necessarily..."⁶⁹

8.7.16 Following on from that comment, the Panel asked the Minister what would happen if a good, innovative idea came forward and needed funding of less than £20,000. The Minister responded:

Minister for ED (hearing on 22nd February 2013)

"...I am not saying I am ruling it out totally, I just said it was less likely I would have thought but it depends on the proposition that comes forward..."⁷⁰

8.7.17 Pressing further, the Panel asked the Minister for a yes or no answer to "are we ruling out everything under £20,000?" The Minister told the Panel that each applicant should be considered on its merit and should not have a particular financial sum attached to it stating that:

⁶⁸ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 3

⁶⁹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 3

⁷⁰ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 4

Minister for ED (hearing on 22nd February 2013)

“...it would depend on the merits of the application, so if you want a yes or no, then it falls under yes...”⁷¹

8.7.18 To illustrate the potential limitation of applying minimum/maximum amounts, the Panel reflected on the reference made by the Chief Officer, ED, to an example he gave as the sort of applicant the JIF might attract, in which the central figure required £500 finance to get started:

Chief Officer (hearing with the Minister for ED on 22nd February 2013)

“...he was in his thirties when he started business [and needed] £500 because he did not have the wherewithal to go and get that from anywhere else. He had a brilliant idea, which has turned into a brilliant idea. I think he eventually sold it to Yahoo for £30 million or £40 million or something like that. He had a brilliant idea but he did not have ability to raise the capital, regardless of where he went...”⁷²

8.7.19 However, given what the minimum and maximum levels of lending are as defined on the application form, this idea would not have received funding from the JIF as it would not have fulfilled the criteria.

Key Finding:

Although the lodged Proposition, report and Operational Terms of Reference contain no indication of a minimum or maximum funding level per applicant, this is contradicted by the inclusion of minimum £20,000 and maximum £500,000 funding amounts on the draft application form and policy framework documents.

Key Finding:

Stakeholders, and initially both sponsoring Ministers, agreed that there was little or no merit in setting minimum or maximum funding levels. However, the Minister for Economic Development later suggested that a minimum level may even be set higher than £20,000.

Recommendation:

The JIF should not adopt the principle of minimum or maximum funding levels per applicant.

8.7.20 Business incorporated under the Companies (Jersey) Law 1991

8.7.21 The Panel has noted the appearance on the draft application form eligibility guidelines of the need for an applicant to be a Business incorporated under the Companies

⁷¹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 5

⁷² Public Hearing with Minister for Economic Development – 22nd February 2013 – page 37

(Jersey) Law 1991. It raised concern that this could perhaps unnecessarily eliminate a number of potential applicants in that Partnerships, LLP's and sole traders would be unable to apply. The Innovation Policy Framework document, section 2.1 in Due Diligence, states that Memorandum and Articles of Association must be supplied. If so, this raises a key issue, as this can seemingly only relate to incorporated companies and cannot apply to Limited Liability Partnerships, Partnerships or Sole Traders.

8.7.22 The Panel raised the issue of LLP's potentially being unable to meet the criteria with the Minister for ED and his Chief Officer, who informed the Panel:

Chief Officer (hearing with the Minister for ED on 22nd February 2013)

*"...A Jersey company can be a limited liability partnership. In fact, many of the law firms are, certainly, and more and more will be so now we have changed the LLP legislation to remove the requirement for a £5 million bond..."*⁷³

8.7.23 The Minister for ED added:

Minister for ED (hearing on 22nd February 2013)

*"...Either structure or other appropriate structures would potentially qualify, so that covers that point..."*⁷⁴

8.7.24 The advice we have been given from our advisor raises a question mark about this position, suggesting that LLP's cannot produce the documents required to meet the criteria. CIPFA's report comments:

*...we would respectfully suggest that this is incorrect as a matter of Law in its strictest sense although there are some similarities within the Company law framework.*⁷⁵

Key Finding:

The JIF Policy Framework and the Eligibility Guidelines on the application form establish the need for an applicant to be a Business incorporated under the Companies (Jersey) Law 1991. This appears to be inconsistent with the Operational Terms of Reference, which don't indicate such a narrow scope or criteria. It raises concerns that a number of potential applicants to the JIF might be inadvertently excluded, in that Partnerships, LLP's and sole traders might be ineligible to apply.

⁷³ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 16

⁷⁴ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 16

⁷⁵ CIPFA report – page 14

Recommendation:

Partnerships, LLP's and sole traders must not be excluded from applying for funding. Therefore, there should be clarification of the consequences of the requirement for an applicant to be a business incorporated under the Companies (Jersey) Law 1991.

8.8 High Value Sector and High Growth Business**8.8.1 High Value**

8.8.2 There is considerable emphasis placed on targeting the Fund at high value opportunities. Within the Innovation Fund Policy Framework, high value sector is defined as a sector with a value added per employee above £65,000. This figure is based on the average per capita G.V.A. (Gross Value Added) across the whole of the Jersey economy.

8.8.3 On review of the statistics posted on www.gov.je the Panel's expert advisor has provided further detail in this area. Taking four of the key areas into consideration (Hotels, Agriculture, Construction and Finance), the advisor suggests that £65,000 GVA per employee would show finance being the only industry that met the criteria:

	Hotels	Agriculture	Construction	Finance
Total GVA 2012	£129,600,000	£46,800,000	£234,000,000	£1,476,000,000
Employees	6,320	2,230	5,100	12,500
GVA per employee	£20,506	£20,987	£45,882	£118,080

8.8.4 The Panel's expert advisor has stated that whilst these figures are broad averages and there may be extreme positions within each sector values, it does suggest that the prospectivity of applicants meeting these parameters outside the financial sector is likely to be low.

8.8.5 The Panel had the opportunity to question the Minister for ED on these figures and GVA overall at their final hearing raising the concern that if only a small section of the economy can target the fund, is it not in danger of becoming "elitist".

8.8.6 The Chief Officer, ED, made the point that the low productivity sectors are supported by EDD through grants and subsidies and stated that "elitist" was the wrong word. He went on to say:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...we would not want to support businesses that did not have the potential of performing at levels of average productivity that were lower than the average. This is not a fund to support low-productivity business...” “...the low productivity sectors are supported by what is the majority of the EDD budget through grants and subsidies and other direct marketing support for instance. That is not the intention of this fund...”⁷⁶

8.8.7 He continued:

“...there is no reason why a business in the rural economy, tourism, any other sectors, cannot develop in such a way that it has that level of productivity. Our objective is to support the broadest range of sectors possible...”⁷⁷

Key Finding:

The requirement for an application to demonstrate £65,000 GVA per employee effectively rules out potential applications from the third and public sectors, and many non-finance industry related projects.

8.8.8 High Growth

8.8.9 In addition to high value, EDD has stated this fund is targeted at areas that can deliver high value, high productivity business. The Chief Officer, ED, told the Panel:

“...The words that I would like to use is that this fund is targeted at high-productivity, high-value sector...this is not about targeting the financial services sector. It is unlikely, in my opinion, that we would be supporting businesses that are in the financial services sector...”⁷⁸

8.8.10 The Policy Framework defines a high growth business as a business with the potential to double revenues or employment within four years and to employ at least ten full time equivalent staff by the end of the four year period.

8.8.11 When raising concerns about the limitations this may place on non-finance sectors accessing the Fund, it was stressed to the Panel by the Chief Officer, ED, that there are other funds available to assist various other sectors within the economy e.g. the Tourism Development Fund for tourism initiatives, the Rural Initiatives Scheme for the

⁷⁶ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 6

⁷⁷ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 9

⁷⁸ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 7

rural economy sector and others which are funded on a recurring basis from the Department.⁷⁹

Key Finding:

The GVA levels per employee and high growth requirement could effectively rule out many potential applications, particularly in the third and public sectors, and traditional industries such as tourism and agriculture.

Key Finding:

The 'high growth' requirement states that an applicant must demonstrate the potential to double revenues or employment within four years and to employ at least ten full time equivalent staff by the end of the four year period. This appears highly restrictive.

Key Finding:

There is clear inconsistency between the stated aim of the Fund being available to all sectors of the economy on the one hand, and the emphasis placed on targeting high value, high growth opportunities on the other.

Recommendation:

If the JIF is realistically to be made available to the third and private sectors, and non-finance industries, the proposed eligibility criteria relating to GVA per employee and high growth business should be amended to a less demanding level.

8.9 Application Process – Red Tape?

- 8.9.1 It was clear speaking to stakeholders – industry representatives who will be encouraging various business sectors to use the Fund where appropriate – that a balance had to be struck between the necessary requirement for quality due diligence, with a need to make the Fund operate as free of 'red tape' as possible to ensure a timely process and to simply not put off potential applicants through an overwhelming process.
- 8.9.2 The application process does appear to place considerable demands on an applicant, as can be seen from the initial 15 point request for a written report and supporting documentation contained on the application form. As the application process progresses, there are then potential additional demands for information through the

⁷⁹ Public Hearing with Minister for Economic Development 22nd February 2013 – page 12

due diligence process, Funding Agreement development and post loan monitoring and reporting.

- 8.9.3 Commenting on the need for a sensible balance to avoid excessive demands and the consequential creep of 'red tape', the President, Jersey Chamber of Commerce explained that there has to be a clear set of procedures set out which establish very clearly how the JIF will ensure a timely process. He elaborated:

President, Jersey Chamber of Commerce

"...if it is something that is novel to the market, you know there will be 100 people behind this person who given another week or fortnight for that decision to be made may well catch up with the person who may be leading the market out there. There is a huge necessity for a fast turnaround..."⁸⁰

- 8.9.4 The Chairman, Digital Jersey concurred, clearly explaining the requirements for a sensible balance:

Chairman, Digital Jersey

"...I think we should be very sensitive to that. It is always a balance between the appropriate level of due diligence and understanding and making sure that the entrepreneurs have thought through the business plan but not tying them down in red tape. If it is going to take us 6 months of due diligence and everything else to get it going, then I think that is self-defeating..."⁸¹

- 8.9.5 The Chairman, Digital Jersey went on to discuss a successful model that was currently in operation in Israel:

Chairman, Digital Jersey

"...I refer the Panel to some very successful models. I am thinking of incubators and I had the chance to experience one in Israel where companies come in ... not companies at that point, people with ideas, and this is rather in the seed start-up, so quite heavy risk. They are provided with infrastructure, a room, connectivity, accounting support, legal support, and some upfront cash to get going, in this case £20,000, £25,000, and there was an expectation that in 6 months they will have made it. So there are models out there and if you are doing that and if the expected return

⁸⁰ Public Hearing with Chamber of Commerce – 6th February 2013 – page 6

⁸¹ Public Hearing with Digital Jersey – 6th February 2013 – page 12

time is 6 months - by the way, this is in Israel where they have been going over this for a while - you cannot take 4 months of that signing the agreement...⁸².

- 8.9.6 Once the applications have been submitted, they follow a process to undergo due diligence and economic assessment before being reviewed by the Board until finally approved/rejected. This timeline is shown on the process map within the Operational Terms of Reference. The process map states the time of the process for successful applicants as 6 weeks from submission. Applicants which are unsuccessful will be notified within 3 weeks of submission so that they can withdraw if necessary. This is shown in the process map within the Operational Terms of Reference and also on the draft application form.
- 8.9.7 The process map indicates that the first 3 weeks will be taken up with due diligence, know your client (KYC) checks and economic assessment with the following 3 weeks being used for Board review, Minister review and application approval. The Panel's expert advisor has indicated that the 3 week timeframe for the process of due diligence could be viewed as optimistic bearing in mind the amount of information that may be required and consequently, the 3 week period for Board review and Ministerial approval may seem generous.
- 8.9.8 When the Panel raised the timeframe with the Minister for ED, the Chief Officer, ED, advised that the timeframe was not set in stone but was purely an indication of their target turnaround from the point of application to the point of decision.

Key Finding:

The application process places considerable demands on an applicant, beginning with the initial 15 point request for a written report and supporting documentation contained on the application form. As the application process progresses, there are additional demands for information through the due diligence process, Funding Agreement development and post loan monitoring and reporting.

Key Finding:

A balance is required between the required quality due diligence, and the need to make the application process as free of 'red tape' as possible, in order to ensure that it is timely and not off-putting to potential applicants.

⁸² Public Hearing with Digital Jersey – 6th February 2013 – page 12

Recommendation:

Whilst ensuring effective and robust processes are established where required, such as due diligence, continued attention should be paid to ensuring that the JIF is not overburdened by red tape.

8.10 Due Diligence

8.10.1 The Operational Terms of Reference imply that the elements of the due diligence function will be undertaken by EDD with assistance from the EAU who will undertake an economic impact assessment and present a written report to the Board. It is outlined in the Proposition report that the Board, as appropriate, will also draw on other expert opinions to provide comprehensive due diligence when considering and assessing applications. The costs of this will be borne from the £100,000 currently allocated for Operational and Management costs.

8.10.2 The Chief Officer, ED, at the Public Hearing with the Minister for ED on 22nd February 2013, told the Panel that there will be two forms of due diligence or two forms of analysis undertaken. The first would be an economic impact analysis, undertaken by the EAU looking at broader impacts rather than purely commercial returns. The second level of analysis and due diligence would be on the commercial proposition put forward by the applicant, and be related in great part to the nature of the business plan presented and the 'bona fides' of the individuals presenting that. It was envisaged that this would be undertaken independently. Both of those two things would then brought together and will inform the Board's deliberations and the final decision to be made by the Minister.⁸³

8.10.3 The Minister for ED has stated that the principle of due diligence applies to whatever the amount that is being requested, and indicated that the level of due diligence is likely to change based on the size of the project and the degree of work involved.⁸⁴

8.10.4 Stakeholders were united in their expectation of there being a requirement for timely and efficient, yet robust, due diligence. Jersey Business set a very precise due diligence process consisting of 4 elements that it would expect to see apply to any investment:

⁸³ Public Hearing with the Minister for Economic Development – 22nd February 2013 - page 17

⁸⁴ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 16

Chairman, Jersey Business

“...In terms of the due diligence, you have to believe that this is a business that is likely, that the likelihood of success is there. If it is not nobody should be investing in it...due diligence consists of 4 elements in any investment. One is an investment manager or a group of people evaluating whether it is a good business proposition. The second is outside expertise, which may be required if it, for instance, is a highly scientific project...The third element of it is...legal. In other words someone has to structure the loan and the documentation that is involved. The last element is the accountant...In other words, to do checks and balances. The last 2 are a give-up, in the sense that you are going to run that expense in any investment, whether you make it or not, but you do not make that investment until you get the final stage, having done the first 2 analyses. The expert you only hire if you think there is a good business case. The good business case should be the judgment that is made by the investment panel or managers who are evaluating a sound business plan...”⁸⁵

8.10.5 The Chairman, Digital Jersey, also commented on the importance of getting due diligence right at an early stage of application, saying that for any investment there are lots of models out there and the JIF certainly should not be recreating well created wheels. He commented:

Chairman, Digital Jersey

“... I think it is a very straightforward stage gate process. One of the keys around this is a very early yes or no to determine whether you are going to spend ... because the longer you spend with due diligence the greater the cost is and then right at the end before you make the investment there will be some legal due diligence and other searches. That is where those upfront costs really build...”⁸⁶

8.10.6 The Panel’s advisor explained the importance of robust due diligence within his report stating:

Before receipt of the Policy Framework we had reservations about the absence of detailed procedure relative to due diligence. Significant importance was placed on the regulatory application of the Undertaking business licence and the requirement for the applicant to be an incorporated body under the Companies (Jersey) Law 1991, as amended. The establishment of the full identity of applicants, acquiring a history of credit and the requirement to minimise the risk of criminality is assumed to be

⁸⁵ Public Hearing with Jersey Business – 6th February 2013 – page 19

⁸⁶ Public Hearing with Digital Jersey – 6th February 2013 - page 6

fundamental. Whilst the Innovation Policy Framework effectively narrowed the range of eligible applicants to incorporated bodies only (presumably the “legal personage” of the incorporated body and Directors) which are subject to regulatory business licensing with Jersey, our thinking was that such constraints should make it easier to carry our due diligence within the application process. However, as the Minister for ED has now confirmed that there are no restrictions placed on legal entity formats that can apply, the effectiveness of Due Diligence processes are key particularly in the context of all legal business formats. In this respect, following the Panel Meeting on 22 February 2013 we now understand that Due Diligence will be externalised and fed to the JIF Board as required.⁸⁷

Key Finding:

Stakeholder organisations were united in their expectation of a timely and efficient, yet robust, due diligence process. The Panel has concerns about the ability of the due diligence process as currently proposed to meet those sound expectations.

8.11 Funding Arrangements – Loans or Grants

8.11.1 The JIF will operate on its ability to provide repayable loans or grants with the aim for support being through repayable loans. The assumption is that the majority of support offered will be through repayable loans, with grants only offered in exceptional circumstances.

8.11.2 The Operational Terms of Reference defines loans and grants as:

- **Loans** are defined as a sum of money advanced from the Fund to a party for a limited period of time and repaid with interest calculated on the balance of the outstanding.
- **Grants** are defined as a transfer of money to an individual or entity in return for future compliance with certain conditions relating to the activities of the individual/entity.

8.11.3 The condition for obtaining a loan will be based on the ability to meet the eligibility criteria. Grants will also have to follow the same criteria but with additional requirements. Grants will only be considered in exceptional circumstances and the additional requirements are defined within the Policy Framework as:

⁸⁷ CIPFA Report – page 5

- *The applicant can justify and demonstrate that the project will not generate any income within the first 5 years of the project starting;*
- *The project will result in significant economic spillovers in Jersey during the first 5 years of the project commencing;*
- *The project will deliver a significant economic competitive advantage to the Island;*
- *The project will be delivered in the Bailiwick of Jersey;*
- *The project, within the first 5 years, will result in the creation of new high value jobs (direct or indirect employment).*

8.11.4 If all of the above meet the application, assessment and approval process will follow the policies defined for loans, which include the requirement for the company receiving a grant to enter into a Royalty Agreement. The Minister for ED set out his position:

Minister for ED (hearing on 14th January 2013)

“...As far as I am concerned, the purpose of the fund is primarily that of providing funding in the first stage by loans...”⁸⁸

8.11.5 The stakeholders all held the same opinion in that they favoured loans over grants, as outlined below:

Chief Executive, Jersey Business:

“...I believe there is a place for both but it should be defined and understood why you are doing it...”⁸⁹

Chairman, Digital Jersey:

“...I think it is fair to say that Digital Jersey favour debt far above grants. I think that we should be viewing this as really, really solid business transactions and I would lean away from grants except in very exceptional circumstances towards debt...”⁹⁰

President, Jersey Chamber of Commerce:

“...Why do banks take security against loans? Because they want to make sure you get out of bed in the morning to repay the loan. What would my thoughts be? I think there is a place for grants and why do I think there is a place for a grant? I think because if you are trying to innovate into a new area and you have not quite got the

⁸⁸ Public Hearing with Minister for Economic Development – 14th January 2013 – page 21

⁸⁹ Public Hearing with Jersey Business – 6th February 2013 – page 8

⁹⁰ Public Hearing with Digital Jersey – 6th February 2013 – page 11

*cash in the bank or you have not quite got the money there to know it is a goer, kind of thing...*⁹¹

8.11.6 It can be seen above that there may be greater 'motivation' provided to the recipient of funds if the money is received in the format of a loan as opposed to a grant. The Panel is also aware that for the JIF to achieve its self replenishing aspiration (see Section 8.12) significant grant funding represents a serious hurdle.

8.11.7 The Panel's expert advisor has stated that the criteria suggests that the requirements for grant recipients are more onerous, given the additional requirements in addition to all requirements of Loan Applicants, as well as entering into a Royalty Agreement.

8.11.8 At the Hearing with the Minister for T&R, the Panel asked what the definition of exceptional circumstances would be and were informed by the Chief Officer, ED, that the base assumption was that the JIF will be able to loan the money to the venture, and it will have the capability because of the business plan that it has put forward to repay those monies over a period of time, with interest. He added:

Chief Officer (hearing with Minister for Treasury & Resources on 10th January 2013)

*"...That is what we would suggest that the majority of funding is. There may be examples where that is not appropriate and it may be more appropriate - it if is, for instance, something that a business needs as a one-off, just to support a particular piece of activity - the Innovation Fund may say: "We do not need to give them a loan which they need to repay. We can grant fund this because if they are successful it will drive more export business..."*⁹²

8.11.9 The Minister for ED explained:

*"...grants would only be in extremis. I do see very little scope for grants..."*⁹³

Key Finding:

It is clearly proposed that grants will only be made in exceptional circumstances.

⁹¹ Public Hearing with Chamber of Commerce – 6th February 2013 – page 18

⁹² Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 22

⁹³ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 33

8.12 Self Replenishing Fund?

8.12.1 The Proposition states that the medium term aim is for the JIF to be self-replenishing. The Operational Terms of Reference state very clearly that the aim of the Fund is that it should be self-replenishing and not a sinking fund. The principle means for financial returns to the Fund are to be made through interest rates, royalty agreements and equity. The process relating to interest rates is covered in Section 8.12.7, and the States is already experienced in such schemes, which are in essence relatively simple. However, we explore the less common royalty agreements and equity in more detail in this section.

8.12.2 The Minister for ED has made reference to successful innovation funds in other jurisdictions being self replenishing – namely the fund in Israel. He has indicated that in order for the fund to be self replenishing, risks will need to be taken, but was clear at our initial Public hearing that the Fund should aim to be self replenishing:

Minister for ED (hearing on 14th January 2013)

“...I think all in all there is no reason that the fund should not replenish itself as a result of the investments it makes in the businesses it supports....But I would certainly hope that it would be self-replenishing, self-sustaining...”⁹⁴

8.12.3 The Minister for T&R appeared to place less emphasis on the need for the Fund to be self-replenishing. He told us it was a fantastic principle which he hoped could be achieved:

Minister for T&R

“...I think we have got to be really realistic. I think there are serious economic challenges facing Jersey, and I want the Chief Officer to spend the £5 million on getting business start-ups up and running and employing people, so I want them to do it because I suspect that the scale of challenge that we have, which if we respond properly, assertively and boldly enough we can deal with, we can reduce our unemployment numbers and we can start some business start-ups that are going to be the wealth creators of the future...”⁹⁵

Deputy of St. Martin:

“...So you are taking your foot off the pedal when it comes to this fund being self-replenishing then, Minister?...”

⁹⁴ Public Hearing with Minister for Economic Development – 14th January 2013 – page 17

⁹⁵ Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 14

Minister for T&R:

“...No, I am delighted to hear Mike say that he thinks he can do it, but... (‘we have got to be realistic’)...”⁹⁶

8.12.4 Speaking to stakeholders, there was general consensus that self replenishing was a sensible aspiration. The Panel discussed the possible 70% failure rate aspect as quoted previously by the Minister for ED (see Section 8.5 Hopes for Success, Expectations of ‘Failure’). The President of the Chamber of Commerce outlined, however, that the success or otherwise of this aim may become apparent quite quickly, in view of the anticipated failure rates:

President, Jersey Chamber of Commerce

“...what is... critical is when that 70 per cent failure rate happens. I think if it happens at the end, in other words you have already had 30 per cent success at the very beginning and you have managed to build up that fund and recoup some of the money, but if you lose that 70 per cent at the very beginning you have a tiny fund and so you have nothing left at all to give to maybe the person who does need that money...”⁹⁷

8.12.5 The Panel asked whether the Chamber of Commerce viewed the fund as self replenishing based on this risk of failure:

President, Jersey Chamber of Commerce:

“...I do not say it will not be a replenishing fund. It just depends upon how successful those initial investments, early investments are. That is the view of Chamber, anyway...”⁹⁸

8.12.6 The Chairman, Digital Jersey, explained that he thought the JIF should be treated as an investment fund and not seen as a sinking fund; that it should absolutely seek to be replenished from the investments made. He added that it was right to identify the timing issues around that and how long it will take for the returns to be seen.⁹⁹

8.12.7 Loan Repayment Terms

8.12.8 The proposition states that the arrangements for administering the repayment of loans will be agreed between T&R and EDD. Any financial support offered (loan or grant) will comply with all aspects of the Public Finances (Jersey) Law 2005 and the States of

⁹⁶ Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 14

⁹⁷ Public Hearing with Chamber of Commerce – 6th February 2013 – page 3

⁹⁸ Public Hearing with Chamber of Commerce – 6th February 2013 – page 3

⁹⁹ Public Hearing with Digital Jersey – 6th February 2013 – page 12

Jersey Financial Directions. Any grant or repayable loan would be the subject of a detailed Funding Agreement. Each Funding Agreement will be unique to the project and include details of any specific clauses, to include repayment terms and timing and arrangements for repayment or early repayment.

8.12.9 The Proposition states that terms and interest rates will be determined through consultation between the Board, the Treasurer of the States and the Minister for ED. There has been no indication if interest rates will be set by affordability or market norm.

8.12.10 The Panel asked the Minister for T&R what responsibilities would lie within T&R regarding the fund and what level of intervention they would have in its management. The Minister responded:

Minister for T&R:

“...Well, it is we are setting up the fund and then it is over to the Minister for ED and the Chief Officer, who is legally responsible to ensure value for money...”¹⁰⁰

8.12.11 The Panel questioned the Minister for ED and his Officers on 22nd February on the overall responsibility of setting the repayment terms. The Chief Officer, ED, told the Panel that ultimately it will be for the board to recommend to the Minister, particularly the repayment terms, but that he would expect to receive an element of guidance from the Treasury with bands as to what that should be.¹⁰¹

8.12.12 The Minister for ED added:

Minister for ED (hearing on 22nd February 2013)

“...It would be wrong to leave it with Treasury or indeed ED to be making that call. It is primarily, in my view, a commercial decision and there has got to be a commercial rationale behind the proposal brought forward and the recommendation from the board to me to consider...”¹⁰²

8.12.13 Flexible payment schemes have not yet been addressed but Digital Jersey had the following to say on the importance of the fund being flexible:

Chairman, Digital Jersey

“...we need to be very careful about the repayment schedule around that because these are going to be start-up companies. You would not want to burden a company

¹⁰⁰ Public Hearing with the Minister for Treasury & Resources 10th January 2013 – page 8

¹⁰¹ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 47

¹⁰² Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 47

*with huge interest payments up front which would, in fact, stall their growth. So I think schedules of repayment of how the money is repaid, et cetera, need to be very carefully thought through...*¹⁰³

Key Finding:

Any grant or repayable loan would be the subject of a detailed Funding Agreement. Each Funding Agreement would be unique and include details of any specific clauses, including repayment terms and timing arrangements for repayment.

Key Finding:

Although the JIF Operational Terms of Reference broadly propose consultation between the Board, the Treasurer of the States and the Minister for Economic Development, the process by which loan repayment terms and interest rates are to be established is not clear, with no formal details or guidelines available.

Recommendation:

Outstanding issues relating to the work required of the Law Officers Department must be resolved, not least the development of the Royalty Agreement template, prior to the States debate.

8.12.14 Royalty Agreement

8.12.15 The Proposition report states that:

At the discretion of the Minister for ED, any project receiving support from the JIF may be required to pay royalties. The scale and scope of royalty payments will be defined in the Funding Agreement. For instance, if the Minister for ED approves a grant or repayable loan for research and development support which may lead to the commercial development of products or services, the Minister shall, based on professional advice, decide income from products or services which may be subject to royalty payments and how the amount of royalties should be calculated as a percentage of income. The products/technology on which royalties are to be paid shall be specified in the Funding Agreement. Royalty-liable revenues would be recorded separately by the company and paid in accordance with terms and conditions defined in the Funding Agreement. The sale price requiring payment of royalties would be the full price recorded by the company in its accounts and audited statements. The only

¹⁰³ Public Hearing with Digital Jersey – 6th February 2013 –page 11

expenses that would be deducted from the sale price are those due to purchase taxes.¹⁰⁴

To remove any doubt, the Funding Agreement will document the exact details of all loan and royalty payments. The Funding Agreement will be a binding agreement between the parties and must be signed by the Minister for ED before any funding is release

8.12.16 Each funded application will be subject to completion of a detailed funding agreement under the Public Finances (Jersey) Law 2005 which will include a Royalty obligation. Royalties will be paid on any income which originated in the developed product and its derivatives. The Royalty Agreement is still in draft format and is, at the time of reporting, with the Law Officers Department with the aim of developing a Jersey document for use on all loans and grants used from the Innovation Fund. We have had confirmation from EDD that the legal document will be finalised by end of May 2013, which is before the Board is appointed and in advance of the project going live. (see also Section 9.2.14 for consultation with/role of the Law Officers)

8.12.17 The Panel raised a question around how royalties could be applied to an already existing product and company. The Chief Officer, ED, stated that they would only apply the royalty to the existing product revenue stream.

8.12.18 The Panel's expert advisor has listed the Royalty Agreement as a key potential hurdle, due to possible legal issues:

The eligibility policy specifically requires that applicants agree and sign a Royalty Agreement in favour of the States – the expectation being that the States can maximise any benefit arising from ensuing success of the venture. As will be outlined within Section 5 – the objective of maintaining a Self-Replenishing or Fully Sustainable Fund is envisaged to be only achieved through maximising Royalties or equity Stake venture successes. It was confirmed at the meeting of 22 February 2013 between the Panel and the Minister for ED that Royalties would only attach to new products and not existing products or IP. The existing documentation accompanying the Innovation Fund Framework as Appendix 2 is an extract from the Royalty Agreement applied by the Chief Scientist for the Government of Israel. It is currently unclear whether States Law Officers have adapted such an agreement for the prevailing and relevant Jersey Law requirements. Provision would require to be made for enforcement – however

¹⁰⁴ Operational Terms of Reference - P.124/2012 – page 64

more fundamentally – the determination and definition of what Royalties should incorporate – within the context of the environment of Jersey should be made before such Loans or Grants can be made.¹⁰⁵

Key Finding:

The Panel is concerned by the number of outstanding questions relating to Royalty Agreements, and the limited progress that has been made by the Economic Development Department at this stage in progressing the template document, which is currently only in early draft form.

8.12.19 Equity

8.12.20 There are proposals for a second stage to be introduced to the JIF at a later date, allowing the States to make equity investments in successful applications. The Proposition report states:

*Following the launch of the JIF, the Treasury and Economic Development will develop the necessary proposals, for States approval, that will allow the Fund to make equity investment in privately-owned businesses. The aim is that the Minister for T&R will bring forward a further Proposition to the States for approval of this element, within 6 months of the launch of the Fund.*¹⁰⁶

8.12.21 This is a significant step and departure from common States practice regarding loans, and will require additional expertise and also new legislation. This second stage of the Fund has yet to be scoped in detail, and it is therefore unclear as to how the parameters will be set and how investments will be monitored on an ongoing basis. Whilst the Panel was given the impression that as the first phase did not include equity provision there was not much to be gained from discussing it at this stage, it developed the opinion that in fact there are important aspects of equity that merit being raised at this stage as, unresolved, they could have considerable impact on the longevity and success of the Fund.

8.12.22 Not least amongst these is the consensus formed amongst stakeholders, who were all in favour of aspiring to a self replenishing fund, that they were clear that without equity, self replenishing would be extremely difficult - a position clearly explained by the Chairman, Jersey Business:

¹⁰⁵ CIPFA report – page 20

¹⁰⁶ Operational Terms of Reference – P124/2012 – page 6

Chairman, Jersey Business

*"...But ultimately the fund in order to be self-sustaining is going to have to make equity investments...."*¹⁰⁷

8.12.23 Digital Jersey concurred with this position, the Chairman telling us:

Chairman, Digital Jersey

*"...I think it would be a lot easier to achieve that as a growing fund using equity than it will be with debt because I am assuming that while the debt covenants will be related to risk, I think we will be thinking about some advantageous interest rates and advantageous terms to help the business get off the ground. So hopefully you will recover capital plus a little bit offset by some of the failures that I think will happen. I think the real returns to the fund come when you have the equity structure..."*¹⁰⁸

8.12.24 The Panel raised the equity vs. self replenishing fund issue with the Minister and his Officers at our final hearing. The Chief Officer, ED, commented:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

*"...Coming back to your earlier question about the percentage of equity, if we want this thing to be generally self-sustaining the percentage of equity investments would be very high, but if that were the case that probably leads you towards having the type of model the Irish have deployed where they do match those funds with external funds and it is managed externally, because that is where the genuine investment expertise is and this is not just in the area of pre-award evaluation..."*¹⁰⁹

8.12.25 The Chief Officer, ED, made comments at the final hearing regarding equity returns, when he indicated that:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

*"...a successful equity at 20, 30, or 40 times the level of investment...is not uncommon..."*¹¹⁰

8.12.26 The Panel's adviser suggested that such aspirations of high yields on high risk investments are somewhat speculative in nature and reliance on such levels of returns are not consistent with the prudent management of public funds.¹¹¹

¹⁰⁷ Public Hearing with Digital Jersey – 6th February 2013 - page 7

¹⁰⁸ Public Hearing with Digital Jersey – 6th February 2013 – page 13

¹⁰⁹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 36

¹¹⁰ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 35

¹¹¹ CIPFA report – page 7

8.12.27 With the significance of equity to a self replenishing fund in mind, the Panel highlights at this stage that there are questions emerging about the timescale, legal ability, cost implications and expertise requirements surrounding securing an equity element to the JIF, all of which will need to be explored further as the details of the proposals emerge.

8.12.28 The Panel's expert advisor has concluded the idea of the fund being self replenishing as aspirational rather than a prudent and realistic assumption. He was clear that the fund cannot be self replenishing without significant benefits coming back to the States through Royalty Clauses:

Given that the JIF would effectively be the "lender of the last resort" after failing to secure alternative finance from Banks and Private Investor sources, we would have concern about the validity and prospectivity of the "self replenishing".¹¹²

Key Finding:

Should the States approve the first phase of the JIF, there are proposals for a second stage to be introduced within 6 months to enable the States to make equity investments in funded projects. This is a significant step and a departure from common States practice regarding loans, and requires additional expertise and also new legislation.

Key Finding:

Although the proposed JIF is intended to be self replenishing, with stakeholders agreeing that this was a sensible aspiration, it is difficult within the context of high suggested 'failure' rates, grants, costs, lender of last resort principle, differing 'success' priorities and in particular the initial absence of the equity element amongst others, to envisage that the JIF will meet this aim. There is therefore the distinct possibility of the JIF becoming a sinking Fund.

Recommendation

The JIF should retain the objective of being self-replenishing. It is vital therefore to ensure that in addition to implementation of the Panel's monitoring and cost related recommendations:

- a clear financial objective and Key Performance Indicators are established;
- formal guidelines are established between the relevant Departments regarding interest rate levels, and the process for establishing loan repayment terms is clearly set out;
- the equity element is developed, as proposed, within 6 months;
- grants are awarded only 'in extremis'.

¹¹² CIPFA report – page 6

9. RESOURCES AND COSTS

9.1 Economic Development and the Role of the JIF Executive

9.1.1 The Operational Terms of Reference accompanying the lodged Proposition state that the Board would be supported by a JIF Executive who would be provided by EDD from existing resources. The JIF Executive would be responsible for administrative and secretariat functions, and in addition have responsibility for ongoing management, aftercare and monitoring of all investment made, and for reporting to the Board on these matters on a regular basis. The Proposition report and Operational Terms of Reference set out the following manpower implications and specific lead responsibilities for the JIF Executive:

Manpower Implications

The Economic Development Department will allocate an individual to be the Fund Executive to support the Innovation Board and assist the management and ongoing operation of the Fund. This post will be from its existing establishment and budget.¹¹³

The JIF Executive will also have lead responsibility for:-

- *Receiving and coordinating all applications*
- *Undertake initial and appropriate levels of due diligence*
- *Preparing the Business Case on behalf of the Board for the Ministers consideration*
- *Preparing the Funding Agreement*
- *Providing aftercare and on-going monitoring of approved projects*
- *Establishing a risk register for all projects.*
- *Managing the risk register, which must be updated every 6 months, register every 6 months and notify the Board, Treasury Minister, Treasurer and Ministers for Economic Development of any changes.*
- *Drafting the Annual Report for the Board to approve¹¹⁴*

9.1.2 The Chief Officer, ED, discussed the resource currently being utilised within EDD for the Tourism Development Fund using it as a comparison to the JIF in terms of resourcing and said:

¹¹³ Proposition P.124/2012 – page 6

¹¹⁴ Operational Terms of Reference P.124/2012 – Page 13

Chief Officer (hearing with Minister for ED on 14th January 2013)

“...I would expect the Innovation Fund to have a greater resource than that because I think the nature and complexity of the process and the applications will be greater. I would expect us to assign one F.T.E. (full time equivalent) from EDD staff, probably at a grade 12, a fairly senior level within the organisation, because I think the person that does that will need to have an understanding of the process, an understanding of the underlying investments, not just be there as a clerical administrator...”¹¹⁵

- 9.1.3 However, at the final hearing with the Minister for ED, there was an element of confusion introduced about the role of the JIF Executive, seemingly reducing the emphasis on considerable, specific business expertise towards a basic administrative role, which was contradictory to the previous position outlined in the Operational Terms of Reference and identified as being crucial by stakeholders. The Chief Officer, ED, informed the Panel:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...What E.D.D. staff will do is provide an administrative function, end of. Not an analytical function, an administrative function. That is what we do with the T.D.F....an administrative function...”¹¹⁶

- 9.1.4 Additionally, the Panel made reference to the information that the Chief Officer, ED, had given at the previous hearing, when he stated that he would expect to have signed off for one full time employee from existing resource at grade 12 or fairly senior level to undertake the role of the JIF Executive. The Chief Officer, ED, attempted to clarify the plans for resourcing the JIF Executive in a discussion with the Chairman of the Panel:

The Deputy of St. Martin: (hearing with Minister for ED on 22nd February 2013)

“...This is where I am getting confused because, Chief Officer, you told us in a hearing not very long ago: “I would expect us to have signed off for one fulltime employee from E.D. staff probably at grade 12, a fairly senior level of the organisation...”

Chief Officer:

“...Yes, but that will not be everything that they do...That is a grade 12 person that we probably have in our existing staff complement who will discharge the administrative function to support the Innovation Fund. Now, that does not mean it takes them 24 hours a day, 5 days a week, 52 weeks a year, because the nature of the way the Innovation Fund may work, if it goes down the route of bids rather than things coming

¹¹⁵ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 13

¹¹⁶ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 24

in as and when they do, means that the periods of work are in specific timeframes and they are very concentrated. This is exactly what will happen ...We will use one of our existing F.T.Es, as we do for the T.D.F., but that is not a fulltime job. I, as Chief Officer, would not be doing my job if I assigned a resource to a task and I was over-resourcing that particular task...'¹¹⁷

- 9.1.5 The Panel's expert advisor cites the role of the JIF Executive as a key issue in section 4.7 of his report, outlining that:

Given that these reporting requirements are comprehensive it is envisaged that such requirements will require extensive practical resourcing within EDD although we were advised at the Panel Meeting with the Minister for ED on 22 February 2013 that such support will be purely administrative and only be a part of an existing officer's remit – this is in contrast to the position advocated by the Director of Business Creation and Growth relative to the recruitment and appointment of a JIF Executive with associated high level Fund Management responsibilities.¹¹⁸

- 9.1.6 The expert advisor has also stated in his report that clarity needs to be provided on actual officer support that will be provided to the JIF Board – for example what are the exact resources earmarked for JIF support role and what will the consequences be for the activities that are currently being serviced by such current resources?¹¹⁹

- 9.1.7 Given the widely agreed need for expertise identified amongst stakeholders, and indeed that lodged documentation outlines that the JIF Executive will be required to have, the Panel asked the Chief Officer, ED, if there would be a role for Jersey Business to play regarding the overall assessment process:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...There could be, but that would make them poacher and gatekeeper. If they were involved in working with the business to develop the submission and mentoring the business after, could they really provide independent due diligence on the proposal?...”¹²⁰

¹¹⁷ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 32

¹¹⁸ CIPFA Report – page 23

¹¹⁹ CIPFA report – page 9

¹²⁰ Public Hearing with Minister for Economic Development – 22nd February 2013 - page 19

9.1.8 He added:

“...The view and the discussions I had the other day with Peter Funk was about pre-application and post-award mentoring. There is a requirement for properly independent due diligence, bringing in high levels of technical and commercial expertise that is specific to that application that, to be frank, Jersey Business, good as they are, will not have...”¹²¹

9.1.9 The Panel followed this line of questioning and discussed at length the role of Jersey Business and asked what the disparity would be in assisting with the pre application advice and making the application itself to gain a clearer understanding into the role of Jersey Business. The Chief Officer, ED, outlined the Department’s position:

Chief Officer (hearing with Minister for ED on 22nd February 2013):

“...Let me give you an example from the recent Tourism Development Fund. We broadened the eligibility of the Tourism Development Fund to the private sector. We received 27 applications, we made 8 awards, so 19 bids were rejected, okay? When we looked at that, and we are re-examining the process now, one of the fundamental weaknesses was the quality of the bid that was submitted, not necessarily the underlying quality of the proposition, but it was the quality of the bid that was submitted. One of the other discussions we have with Jersey Business in the context of the TDF. (Tourism Development Fund) is whether or not they could work with potential applications to the TDF, which is a proxy for this, to make sure that the bids were of sufficient quality to allow the panel to make a positive judgment, because they have got funds to award...”¹²²

9.1.10 The Panel raised a further question around when the application pack would be presented to the Board:

Deputy of St. Martin:

“...That is exactly what I was suggesting here, because what you are saying is that in the innovation stage, Jersey Business would give the pre-application advice, and are you suggesting that once Jersey Business have finished their work with the applicant that the pack would then be in a position to go straight to the Board?...”¹²³

¹²¹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 19

¹²² Public Hearing with Minister for Economic Development – 22nd February 2013 – page 20

¹²³ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 20

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...No, no, no. The pack would then be ready to be submitted to the evaluation process, to the due diligence process. That is what I am suggesting. It is not the same thing...”¹²⁴

Deputy of St. Martin:

“...Yes, the due diligence is external anyway...”¹²⁵

9.1.11 The Chief Officer, ED, explained why he felt due diligence needed to work independently, telling the Panel:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...let us just take an I.C.T. company comes along with a proposal, works with Jersey Business, who will give them help and advice on the quality of their business plan and the quality of their proposals, may help them with some market analysis. They will submit that with the assistance of Jersey Business, so Jersey Business will have added value, because in the absence of that, that will have been a lesser quality bid, but it is still a bid which still requires from a Board and governance perspective independent commercial due diligence and economic impact analysis to be undertaken on it...”¹²⁶

9.1.12 He went on to say that it would be unusual for the people undertaking that to be the same people involved in the pre-application process, because they would not be independent, because they did not have a vested interest, but they have been involved in evolving the proposal. He explained that this would be:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

‘...like saying that Jersey Business, who do help businesses apply to one of the clearing banks for a loan, provide the bank with the due diligence that the governor of the bank makes the decision...’¹²⁷

9.1.13 This was taken up by the Chairman of the Panel, who sought clarification. He commented:

¹²⁴ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 20

¹²⁵ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 20

¹²⁶ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 21

¹²⁷ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 21

Deputy of St. Martin:

“...Sorry, I might be getting confused here, but is that not what Jersey Business is set up to do? I mean, are they not going to be administering taxpayers’ money through schemes which people will walk through their door and say: “I would like to apply under this scheme. Help me fill my form in and if it is good enough, give me some money...”¹²⁸

Chief Officer:

“...No, no. This is the whole issue. The Innovation Fund is one part of a very broad spectrum of support that is provided by the States, not just by ED for businesses. Jersey Business itself has offered services and products to small businesses, which it does so from within the funds available to it of the grant we give them, which I think is about £600,000 and something. Yes, that is the right number. That is different to helping a business, assisting a business to provide advice to make an application to the Innovation Fund, over which Jersey Business has no governance role at all. It is there to help businesses in this instance prepare, and they will use their business advice and support expertise to do that, as they do for businesses who make applications to Barclays Bank or any of the other clearers, but Barclays Bank do not go back to them and say: “Now, guys, you have helped me. Would you do the due diligence for us? ...”¹²⁹

9.1.14 The Panel asked if, due diligence aside, Jersey Business could not work up the application and present it to the Board:

Minister for ED (hearing on 22nd February 2013)

“...They can work up the application, they just cannot determine it. They cannot do the due diligence...”¹³⁰

9.1.15 The Panel asked whether in light of the expertise of Jersey Business, whilst not determining any applications, there could be a case that Jersey Business could fulfil the requirement to essentially handle the pre-determination application process. The Chief Officer, ED, responded by saying:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...I think if they fulfilled the due diligence requirement for the board of the Innovation Fund, they would be conflicted...”¹³¹

¹²⁸ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 21

¹²⁹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 21

¹³⁰ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 22

¹³¹ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 22

9.1.16 The Panel's expert advisor has queried whether this would necessarily be the case, highlighting examples of Innovation Funds in other jurisdictions which are managed by external agencies who undertake all due diligence in reference to the management of the fund with no conflict.

9.1.17 The stakeholders were clear that the assessment process required experts in order to have confidence in making quick decisions. The Chairman, Jersey Business explained his organisation's approach:

Chairman, Jersey Business:

"...We are advisers... Some of our advice is pretty sharp and short but we typically work with companies over many weeks and months to try and help them develop their plan. This could be part of the process. There is, in terms of the proposed workings of the review panel, that process as well. In other words they are obligated, as I read it, to review business plans and that is the kind of thing that we could assist with presentation or we could be a conduit for that funding, it all depend...I think we have a role internally, particularly at the executive level within Jersey Business where we should work thoroughly with organisations to get them in the right place to be making an application. It is what we do every day..."¹³²

9.1.18 Digital Jersey added weight to the point made by other stakeholders that early, informed judgement would be required for an efficient and effective process:

Chairman, Digital Jersey

"...Whoever that overview body is needs to have been there and done it, needs to know the questions to ask. I think we are seeing this in the same way. If you do not have that early very clear decision making there will be a lot of time, a lot of effort and a lot of wasted effort would go into looking at companies or ideas that are just never going to see the light of day. You need some experience to do that..."¹³³

Key Finding:

The emphasis on the requirement for the JIF Executive to have considerable and specific business expertise, as outlined in the Operational Terms of Reference and identified as being crucial by stakeholders, has been reduced by the Economic Development Department to that of a basic administrative role.

¹³² Public Hearing with Jersey Business – 6th February 2013 – page 11

¹³³ Public Hearing with Digital Jersey – 6th February 2013 – page 8

Key Finding:

Some Innovation Funds in other jurisdictions are managed by external agencies who undertake all due diligence in reference to the management of the fund with no apparent conflict. In view of this and stakeholder consensus on the need for expertise and efficiency in the support provided to the JIF Board, it is conceivable that Jersey Business is well positioned to undertake the role and responsibilities of the JIF Executive.

Recommendation:

The Minister for Economic Development should formally engage with Jersey Business, with a view to that organisation undertaking the functions of the JIF Executive.

9.2 Additional Departmental Resources/Responsibilities

9.2.1 Treasury and Resources Department:

9.2.2 The Proposition states that the arrangements for administering the repayment of loans will be agreed between States Treasury and EDD. Through Public Finances legislation, there is a requirement to report to the Minister for T&R every 6 months as to the progress of any fund.¹³⁴ The monitoring by T&R is set out on their Managing Risk Register used for Annual Reporting.

9.2.3 The Panel asked the Minister for T&R how his Department would be involved in the monitoring of the fund, and he was very clear in what he saw as his Department's important but limited position:

Minister for T&R

"...I am not going to be a non-executive and Shadow Minister for ED because we all have got to work on our priorities and I do not want them thinking I am breathing down their neck, but we are going to have a monitoring, as we do with all things, and it is set out effectively on managing risk register, updated, notifying the board..."¹³⁵

9.2.4 The Panel followed up to seek clarity on his position regarding monitoring and financial responsibility for the JIF.

Connétable of St. Brelade:

¹³⁴ Proposition P.124/2012 – page 13

¹³⁵ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 29

“...So let us be clear, the money in terms of its responsibility, in terms of looking after....

Deputy of St. Martin:

... lies in the hands of EDD?

Minister for T&R

...Absolutely....We will hold them to account, and of course in the relations that I have with my Minister Colleague Maclean, of course we will, as always, have an active interest in how they are doing, and partly because if they are successful, I hope that they are going to come and ask for some more money...”¹³⁶

- 9.2.5 The Minister for T&R also stated that there will also be informal monitoring, illustrating this with the example of how such informal monitoring worked with regard to the progress of Digital Jersey:

Minister for T&R

“...I found the money for Digital Jersey start up and I put it in the MTFP and I have kept, I can assure you a very active interest in “How is the Board selection going? Have you got very good people? Have you got good non-execs? How is that going? What has been happening? so it is the Cyril Le Marquand House bubble that is actively working, if I may say, with the Minister for ED there, with me there, with the Chief Minister...”¹³⁷

- 9.2.6 The Panel asked EDD to explain what plans they had made for the nature of involvement of the T&R Department in the JIF processes. Asking specifically about who would be tracking the performance and monitoring the fund on a regular basis or who would undertake doing the ongoing internal auditing functions, the Chief Officer, ED, explained that EDD will be tracking the performance on an investment-by-investment basis, reporting, as is the case with the TDF, on an annual basis. The Treasury would itself report on a 6-monthly basis, as it does with all the funds under its remit. ¹³⁸

- 9.2.7 The Panel asked whether, in terms of the opportunity to highlight any issues as time went on, they saw a role for T&R within that to ensure, for example, that interest

¹³⁶ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 9

¹³⁷ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 29

¹³⁸ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 29

payments were being made in order to highlight to EDD if there may be a potential problem. The Director of Business Creation and Growth explained:

Director of Business Creation and Growth: (hearing with Minister for T&R on 10th January 2013)

"...T&R have been involved...regarding development in the fund and the proposal. T&R already manage all other funds of a similar nature, housing loans, associated kind of start-up loans for purchases of property and the old agricultural loans and there is one other...They manage those on an ongoing basis and I think once the loan is approved there will be an ongoing requirement of T&R to manage that in accordance with the kind of criteria that has been set by the board. So there is absolutely a requirement for T&R to be managing that risk and be involved in the management ongoing..."¹³⁹

9.2.8 The Panel asked if a formal reporting process would be set up regarding the tracking. The Director of Business Creation and Growth advised that EDD had looked at what was already in existence. Although somewhat scheme-specific in terms of how they were being presented, there was a requirement under law to report every 6 months as to the progress and T&R had agreed that they would undertake that as part of the ongoing management of repayment of loans, interest payments and managing these points.¹⁴⁰

9.2.9 Following the Panel's hearings with industry stakeholders, the President of the Jersey Chamber of Commerce was of the view that T&R should have very little ongoing role in the fund and should be responsible solely to hand over the funding stating:

President, Jersey Chamber of Commerce

"...I think the Board themselves have to take the can. They really do have to. Treasury are just there to hand over the funding..."¹⁴¹

9.2.10 There is also a role for the Economic Advisor to play to undertake an economic impact analysis of each application. Their findings will form part of the information that will be recommended to the Board. The Panel have been advised that the cost of the Economic Advisor is a cost that is already built in to the advisor's department. This is discussed later in this report under "Invisible Costs" (see Section 9.5).

¹³⁹ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 20

¹⁴⁰ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 21

¹⁴¹ Public Hearing with Chamber of Commerce – 6th February 2013 - Page 22

Key Finding:

There is a discrepancy between the limited role Treasury and Resources expects to undertake in the JIF, and the level of involvement that Economic Development has envisaged for Treasury and Resources.

Recommendation:

All States Departments involved in the JIF must have their roles and responsibilities more clearly defined, most notably the Law Officers and Treasury and Resources. This will require formal discussions and should result in clear guidelines outlining their particular responsibilities.

9.2.11 Economic Advisor's Unit and Law Officers:

9.2.12 There is a requirement from the EAU to review each and every applicant and present an economic analysis to the board as part of the assessment process. This will need to be done for each applicant and as there are no clear indications as to the number of applicants the fund is likely to receive in a year, this could amount to numerous unallocated hours of work. In addition, the Economic Advisor will be a Board member.

9.2.13 There is also a role for the Law Officers' Department in drafting documents prior to the launch of the Fund. For successful applications the Law Officers' Department will have a role to play in the compilation of the Funding Agreements. There is an indication that the Law Officers' Department (or an external resource) may need to review the relevant draft legal documentation in relation to each successful project. The Royalty Agreement will involve part of the application package to be signed into before funding is obtained and the need for urgency on the review of these documents will be vital.

9.2.14 The extent of the consultation by EDD that has taken place to date with the Law Officers' Department is outlined below, in correspondence that the Panel was grateful to receive from the Law Officers' Department (from and with the permission of EDD) outlining their interaction with EDD. It confirmed that they had held various exploratory meetings on the subject of the fund, including the following:

- *We considered the vires question.*
- *We considered the type of legal documentation that would be required to support the operation of the Innovation Fund. You helpfully provided a precedent in relation to a royalty agreement. I understand that you also have access to various*

loan agreement templates. (Head of Investment Management, Treasury and Resources Department) ... has copies of various existing loan agreements, although it is likely that any template used later in 2013 would incorporate some enhanced safeguards.

- *We considered the outsourcing of the preparation of legal documentation. Within the indicative timeframe, it would be possible for LOD to adapt existing templates or an off-the-shelf template from an online provider (e.g.) with possible recourse to an external specialist for review. Equally, it would be possible to instruct an external firm to prepare appropriate templates e.g. a regional/national law firm with experience in acting for enterprise boards/agencies (e.g.).*
- *We considered the issue of whether the Fund is a sinking fund, self replenishing or something that sits between these concepts.¹⁴²*

9.2.15 Evidently, the requirement of such resource input from these Departments will at times (more or less so depending on number and complexity of the applications) divert that resource from existing tasks. Whether this implied cost has been transparently planned for and recognised is discussed in further detail under the section “Invisible Costs”, 9.5.13.

Key Finding:

In addition to the Economic Development and Treasury and Resources Departments, the JIF proposals establish the requirement for formal roles to be undertaken by the Economic Advisor’s Unit and the Law Officers’ Department.

Key Finding:

The Panel is disappointed by the level of consultation undertaken by the Economic Development Department with other relevant Departments, most notably the Law Officers. This has led to a situation where there is lack of detail and progress on key areas, such as the Royalty Agreement, despite the close proximity to the proposed debate.

9.3 The Board

9.3.1 The Proposition states that the Board, after completing the appropriate levels of diligence and assessment, will determine if the project should be rejected, or proceed with a recommendation to the Minister for ED to approve the project using the Business Case Template. The recommendation, signed by the Chair, will include all

¹⁴² E-mail correspondence received from EDD on behalf of Law Officers’ Department – 13th March 2013

terms and conditions, interest rates, repayment terms on loans, royalty obligations and special clauses that are to be attached to offer of support.

9.3.2 The proposed structure states that a new independent Innovation Board will be established with a minimum of 2 members and a Chair from the private sector, together with representatives of EDD, T&R and CMD. This sets the Board structure as 3 private sector members and 3 public sector members. The Board will be responsible for the management of the Fund, assessing all applications and making recommendations to the Minister for ED.

9.3.3 We asked the Minister for ED if he seen the Board as being “Government heavy”?:

Minister for ED (hearing on 22nd February 2013)

“...I think the balance is probably right in terms of the make-up of the Board at the moment. I am satisfied with what has been proposed...”¹⁴³

9.3.4 The Panel asked the various stakeholders as to their views on the make-up of the Board. The President of Jersey Chamber of Commerce told us that:

President, Jersey Chamber of Commerce

“...The point is on the Board you are going to have private sector experience, so the people who are appointed to the Board, one would hope are going to be the kind of people who are familiar with this kind of territory. Clearly the real expertise is in the private sector because these are people, whether you are a banker or whether you are getting involved in private equity finance or anything like that, this is your day job. You know exactly what to look for, you know what the risks are...so you are dealing with it on a day-to-day basis...it really does depend on the Board structure and who comes on into this Board. Are they people who are up to speed with current thinking or are they people who maybe are retired who used to do it and now coming in to help out because that is a good thing to do...the people who get appointed to the Board are absolutely critical to its potential success. I think at least if you are more to the private sector you would at least have people who are very sensitised to the necessity of speed...”¹⁴⁴

9.3.5 The Chairman, Digital Jersey explained to the Panel that whoever that overview body was needed essentially to have ‘been there and done it’, to know the right questions to ask at the right time. He advised that without early, very clear decision making there

¹⁴³ Public Hearing with Minister for Economic Development – 22nd February 2013 – page 50

¹⁴⁴ Public Hearing with Chamber of Commerce – 6th February 2013 – page 7

would be a lot of time and wasted effort going into looking at companies or ideas that were simply not viable. This would require experience. ¹⁴⁵

- 9.3.6 Jersey Business discussed the make-up of the Board they currently had in place within their own organisation, stating that each person on their Board had gone through the process of raising capital loans for a new business. The Panel asked if Jersey Business could see themselves as a “conduit” for the person with the great idea but no business experience. The Chairman, Jersey Business replied:

“...it could be, it could be very well. That is pretty much what we do day in and day out is to assist people, with their business plans and with the development of their business. We are advisers... This could be part of the process...”¹⁴⁶

- 9.3.7 He added:

“...I think we have a role internally, particularly at the executive level within Jersey Business where we should work thoroughly with organisations to get them in the right place to be making an application. It is what we do every day...”¹⁴⁷

- 9.3.8 No clear indication has been given to the amount of times the Board will meet but it seems that it will be dependent on the amount of applications received. The Chief Officer, ED, has stated that he envisaged it would be on an ad hoc basis but no less than once a month. The Minister for ED stated that in the initial establishment, the Board would sit far more often which is similar to what EDD have seen in other Boards they have set up. He also stated that:

Minister for ED (hearing on 22nd February 2013)

“...if there are more applications if they are quality and, if indeed there is a requirement for the Board to sit more often, I think we need to reappraise it in the future depending on the demand of the level of work that they have to do...”¹⁴⁸

- 9.3.9 The Panel was surprised to hear from the Chief Officer, ED, that part of the role of the Board would be to undertake initial filtering of applicants. At the initial hearing with the Minister for ED, he told the Panel:

¹⁴⁵ Public Hearing with Digital Jersey – 6th February 2013 – page 8

¹⁴⁶ Public Hearing with Jersey Business – 6th February 2013 – page 11

¹⁴⁷ Public Hearing with Jersey Business – 6th February 2013 – page 11

¹⁴⁸ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 53

Chief Officer (hearing with Minister for ED – 14th January 2013)

“...not all of those applicants, however will proceed to the point where we undertake due diligence on them, because effectively they would have to pass through the initial filtering which would be undertaken by members of the Board...”¹⁴⁹

9.3.10 The expert advisor has indicated that 12 meetings per annum could incur fees for private sector members and support costs causing a negative impact on costs to the fund. He has also stated that without officer recommendations or judgements prior to the Board reviewing applications; it was effectively a “Working Board” rather than a “Review Board” meeting regularly and solely arriving at judgements on the merits of applications.

Key Finding:

The JIF Board would be responsible for the management of the Fund, assessing all applications and making recommendations to the Minister for ED. It would be comprised of a minimum of two members and a Chair from the private sector, plus ex officio, non-voting representatives from the Economic Development, Treasury and Resources and Chief Minister’s (Economic Advisor’s Unit) Departments. This could set the Board structure as three private sector members and three public sector members.

Key Finding:

The Panel recognises the need and value of the public sector members of the JIF Board, but it is ultimately the private sector expertise recruited to the JIF Board that would be crucial to the potential success of the Fund.

Recommendation:

It is recommended that the number of Board members recruited from the private sector, through a full and formal recruitment process, should be set at a minimum of four (inclusive of the Chairman).

9.4 Stakeholder/Industry Involvement in the JIF

9.4.1 The Panel has been told that industry stakeholders will have a role to play in the Fund. The Chief Officer, ED, explained the vision of how different organisations are intended to link up to promote access to the Fund. He indicated that there will be involvement from Jersey Business to provide business advice and support to applicants together with ongoing monitoring. Additionally he told us that during the Digital Jersey Board

¹⁴⁹ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 4

recruitment process there was wide knowledge and interest in the Innovation Fund proposals, something the applicants had brought up independently. He continued:

Chief Officer (hearing with Minister for T&R on 10th January 2013)

“...I think one of the things that is interesting, You have got people there like Stephen Heppell who is one of the world leaders in education and the development of e-learning. If we had somebody that came forward with an e-learning application or e-learning business we would ally them very quickly to Stephen. An hour of his time for a business like that is hugely helpful. That is where those sorts of hook-ups can happen. We have not set up all of these things in isolation. They do all have to work together and they are established in such a way that they do work together. I think in the next few weeks we are having the first meeting of Jersey Business, Locate Jersey and Digital Jersey, all coming together to look at common issues and how they can work together...”¹⁵⁰

- 9.4.2 At the various public hearings, the Panel asked for clarification regarding the anticipated role of industry stakeholders, as it was increasingly apparent that their input, however formal or informal that might be, was becoming a key component of the JIF. The Minister for T&R told us:

Minister for T&R (hearing 10th January 2013)

“...Once they get their grant and loan, royalty arrangement...then these businesses are going to be up and running. Jersey Business is going to provide some support for that and that is going to be an added control for these guys because one of the things Jersey Business Venture did is stop people making stupid decisions and make people be realistic. Lots of people have got whacky ideas and some people just have not got the organisation to follow them through...”¹⁵¹

- 9.4.3 Appearing with the Minister for T&R, the Economic Advisor explained:

Economic Advisor

“...It might be something that they just need actual business advice and we can say: “Jersey Business, that is what they are there for.” So it can act as a catalyst between everything and get the sort of synergies moving...”¹⁵²

¹⁵⁰ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 39

¹⁵¹ Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 37

¹⁵² Public Hearing with Minister for Treasury & Resources – 10th January 2013 – page 39

9.4.5 The Chief Officer, ED, appearing at the hearing with Minister for T&R, highlighted to us that on the Board of Digital Jersey there was a lot of knowledge in the digital sector that EDD might be able to tap into for the purpose of the JIF at no cost, because of the existing relationship. In relation to Jersey Business, the Chief Officer, ED, added:

Chief Officer (hearing with Minister for T&R)

“...We established last year Jersey Business, merging Jersey Enterprise and Jersey Business Venture to provide business advice and support, fully funded so to do by EDD both in terms of preparation of applications and indeed ongoing monitoring. We would in part rely on Jersey Business to undertake that; that is their function...”¹⁵³

9.4.6 The Chairman of the Scrutiny Panel asked the Chief Officer, ED, if Jersey Business were aware of the involvement envisaged for them in or around the JIF. In response, he explained:

Chief Officer (hearing with the Minister for ED on 14th January 2013)

“...It is quite interesting that in the initial discussions around Jersey Business when we were forming this, the chair and the board members of Jersey Business were very keen to have influence over the innovation ... not influence, that is the wrong way of putting it, to make a contribution towards the work, as, interestingly, have the Board and the Chair of Digital Jersey, so again which is very valuable...”¹⁵⁴

9.4.7 The Chairman pressed further and asked if actual discussion had taken place, to which it was confirmed by the Chief Officer, ED:

Chief Officer

“...yes, very much so...”¹⁵⁵

9.4.8 The Panel spoke to Jersey Business about what they perceived their role to be in relation to the fund, asking if they might effectively be the conduit for the person with the great idea but no business experience. The Chairman, Jersey Business confirmed:

Chairman, Jersey Business

“...I must start by saying we have not had a specific conversation with Economic Development in relation to a specific role for Jersey Business Limited under the Innovation Fund. There has not been a formal conversation...”¹⁵⁶

¹⁵³ Public Hearing with Minister for Economic Development – 14th January 2013 - page 11

¹⁵⁴ Public Hearing with Economic Development - 14th January – page 11

¹⁵⁵ Public Hearing with Economic Development - 14th January – page 11

9.4.9 Nevertheless, he was keen for Jersey Business to play a role, responding to the 'conduit' scenario:

Chairman, Jersey Business

"...it could be, it could be very well. That is pretty much what we do day in and day out is to assist people, with their business plans and with the development of their business. We are advisers..."¹⁵⁷

9.4.10 He commented further:

"...I think we have a role internally, particularly at the executive level within Jersey Business where we should work thoroughly with organisations to get them in the right place to be making an application. It is what we do every day..."¹⁵⁸

9.4.11 At our final hearing with the Minister for ED, the Chief Officer, ED, confirmed that official talks had not taken place with Jersey Business, but explained:

Chief Officer (hearing with Minister for ED on 22nd February 2013)

"...As Jersey Business said, we have not formalised the discussions with them yet, but I was talking to the Chairman of Jersey Business only 2 or 3 days ago. We see their role as twofold. One is that they have a role to work with businesses in the pre-application phase to provide advice, support to them to make sure that their application is as comprehensive as it needs to be, and once the process has been gone through, an evaluation process, and let us assume the grant has been awarded, then they have a very significant role in continuing to mentor those businesses to ensure that the plan which they have helped put together, which is now being funded, is brought to fruition. That is their role..."¹⁵⁹

9.4.12 With regard to Digital Jersey, its Chairman outlined how he saw his organisation playing a series of roles in the JIF:

Chairman, Digital Jersey

"...Digital Jersey I think plays potentially several roles. If the idea is in the digital arena I would hope that Digital Jersey could provide some of that assessment to the board. I would hope also that Digital Jersey...can help a company get itself ready to make an application to the innovation fund, so some nurturing and so on. I also hope, while the

¹⁵⁶ Public Hearing with Jersey Business – 6th February 2013 – page 11

¹⁵⁷ Public Hearing with Jersey Business – 6th February 2013 – page 11

¹⁵⁸ Public Hearing with Jersey Business – 6th February 2013 – page 11

¹⁵⁹ Public Hearing with Economic Development - 22nd February 2013 – page 19

*innovation fund is not just about technology and we completely understand that, that Digital Jersey in some way would be a participant on the Board itself, understanding as well that you have to avoid any potential conflicts of interest...*¹⁶⁰

9.4.13 The Panel's expert advisor addresses an apparent lack of advancement and formality regarding negotiations with stakeholders within his report, despite EDD having seemingly 'assumed' important involvement from key organisations when developing the JIF proposals. It highlights for instance that:

*It was suggested by the Chief Officer that there was an expectation that Jersey Business and Digital Jersey would perform a mentoring role on on-going performance and that they would act as a conduit to the JIF Board on performance monitoring on a 'call-off' basis. We have some difficulty with the lack of apparent formalities within these arrangements and absence of detail relative to such defined responsibilities.*¹⁶¹

Key Finding:

Although the Economic Development Department has outlined significant roles and input for both Digital Jersey and Jersey Business in the JIF, disappointingly it has not undertaken formal consultation with either organisation despite the imminent date of the States debate on the Proposition.

Recommendation:

The Minister for Economic Development must engage in formal discussions at the earliest opportunity with Digital Jersey and Jersey Business, regarding their roles in the JIF.

9.5 Costs – Visible and Invisible

9.5.1 Visible

9.5.2 The Panel had initially understood, as it transpired some stakeholders had, that the £100,000 (which has been allocated for operational and management costs) would be the total costs of running the fund on an annual basis. This was based on the following statement contained in the Proposition report:

Financial and manpower implications

Operational costs

There will be costs associated with the operation and management of the Fund, particularly relating to assessment and approval of applications, e.g. company

¹⁶⁰ Public Hearing with Digital Jersey – 6th October 2013 – page 8

¹⁶¹ CIPFA report – page 24

searches, due diligence work, legal costs and specialist advice. These costs will be met from the Fund.

It is intended that EDD will meet these costs in the first instance, and on an annual basis recharge them to the Fund. Agreed processes will need to be put in place to manage and control this. The Economic Development Department estimates that the operational and management costs at this stage are £100,000.¹⁶²

- 9.5.3 However, it was soon apparent that the £100,000 did not apply to anything other than external advice that would be required. The Panel asked for clarification regarding the £100,000 at the Public Hearings with each of the Ministers:

Chief Officer, ED (hearing with Minister for T&R on 10th January 2013)

“...The £100,000 is our estimate, our current estimate based on the best knowledge that we have of the external due diligence, effectively the commercial due diligence that will be required based on a realistic amount of deals coming through, so that we will be required to inform the board. Now, that is a forecast, but it is very difficult to make a truly accurate forecast because we do not know at the moment until the fund would be launched, subject to approval, what the scale of applications is going to be and the nature of those applications...”¹⁶³

Minister for T&R

“...£100,000 is the estimated cost because you may need to get some additional outside ... whether that is a...bit of accounting advice or a bit of marketing analysis for somebody to check up on something...”¹⁶⁴

- 9.5.4 The Panel asked the Minister for ED how the figure of £100,000 was arrived at. He told us that there was an estimate as to the potential number of projects that might be supported and an estimate to help determine an estimate of the likely cost, bearing in mind professional advice and statistics. He acknowledged that this was not an exact science, as the complexity of the different projects that would be analysed or indeed the extent to which any external analysis may be necessary was unknown.¹⁶⁵

¹⁶² Operational Terms of Reference – P124/2012 – page 15

¹⁶³ Public Hearing with Minister for Treasury & Resources – 10th January 2013 - page 18

¹⁶⁴ Public Hearing with Minister for Treasury & Resources – 10th January 2013 - page 19

¹⁶⁵ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 3

9.5.5 He added:

“...What can be delivered in terms of support within the existing structure of EDD will be. The £100,000, as the Chief Officer has said, is designed to be utilised for what is clearly external. I mean, hopefully it is not going to be using it until it is...”¹⁶⁶

9.5.6 The stakeholders gave different points of view as to the figure of £100,000 for operational and management costs. When considering the scale of potential costs versus the size of the overall Fund, the President, Jersey Chamber of Commerce said:

President, Jersey Chamber of Commerce

“...I think it is a worry and it does make you realise how small relatively the Fund is...”¹⁶⁷

9.5.7 The Chairman, Digital Jersey highlighted one of the problems associated with the development of this Fund, which corresponded with the Panel’s broader concerns about the limited level of available firm detail, planning and research so close to the proposed debate on the Fund. He said:

Chairman, Digital Jersey

“...I do not know the answer to that question because we are dealing with things that are not defined at the moment...”¹⁶⁸

9.5.8 On a similar theme, the Chief Executive of Jersey Business outlined the difficulty any organisation might face in similar circumstances:

Chief Executive, Jersey Business

“...you are talking about a £5 million pot. You have £100,000 for external advisers. I personally think it is right to put that amount of money. You have to have a figure, does that feel about right given that nobody knows, probably. I mean in terms of our own costs and in terms of - I cannot really speak for ED - but the reality is you will only know exactly what it is the year after, at the end of the year...”¹⁶⁹

9.5.9 With the figure of £100,000 being an estimate and with no clear indication of how many successful projects will be funded in a year, it is difficult to ascertain how much specialist advice will be required. The expert advisor has stated that given the expected cost exposure of operating the Fund relative to items listed below, it is highly

¹⁶⁶ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 5

¹⁶⁷ Public Hearing with Chamber of Commerce – 6th February 2013 – page 5

¹⁶⁸ Public Hearing with Digital Jersey – 6th February 2013 – page 19

¹⁶⁹ Public Hearing with the Jersey Business – 6th February 2013 – page 20

possible that total estimated charges to the Fund could easily equate to within a range of £250,000 to £400,000 per annum making the potential sustainability from interest bearing loans - at the smaller number of 4/5 per annum (even at the maximum threshold of £500,000 at a rate of say 5%) being impossible to achieve. Areas requiring clarity include:

- *Operating Expenses*
- *Late Repayment/Repayment difficulties*
- *Bad Debt – Debt write off*
- *Valuation – Equity Investment Impairment*
- *Economic Development, Economic Advisor’s Unit, Treasury and Legal resources deployed in the management of the Fund*
- *External specialist advice and support*
- *JIF Board costs*

9.5.10 At the time of drafting this report, although initial discussions have taken place EDD was waiting confirmation from the Law Officers’ Department regarding their capacity to undertake some legal document drafting on the Royalty Agreement. If it transpires that the Law Officer’s cannot undertake this piece of work, EDD has stated that external lawyers will be used. If this is the case, legal fees will be incurred before the fund has been launched. (see section 9.5.13).

9.5.11 At the final public hearing, we asked if EDD had received a quote from any external law firms regarding a cost to provide any drafting work to which the Chief Officer, ED, stated:-

Chief Officer (hearing with Minister for ED on 22nd February 2013)

“...no we have not, but that cost would be borne by the fund...” “...that is not atypical...”¹⁷⁰

9.5.12 Digital Jersey also made a reference to external costs when discussing due diligence.

Chairman, Digital Jersey

“...the longer you spend with due diligence, the greater the cost is and then right at the end before you make the investment there will be some legal due diligence and other costs. That is where those upfront costs really build...”¹⁷¹

¹⁷⁰ Public Hearing with the Minister for Economic Development – 22nd February 2013 – page 42

¹⁷¹ Public Hearing with Digital Jersey – 6th February 2013 – page 6

Key Finding:

The financial and manpower implications statement in the Proposition estimates 'the operational and management costs' of the JIF to be £100,000. However, it was soon apparent that the £100,000 did not apply to anything other than the external expert advice that would be required, and took no account of internal costs such as the resourcing of the JIF Executive by the Economic Development Department.

Key Finding:

It is quite possible that total estimated charges to the Fund could equate to within a range of £250,000 to £400,000 per year, undermining the ability of the JIF to be self replenishing.

9.5.13 Invisible

9.5.14 The proposition does not state the costs that will be incurred for the required man hours to fulfil the administration and monitoring functions for the operation and ongoing monitoring of the Fund. The Panel questioned both Ministers on the area of resource and was informed that operational and administration would be covered by existing resource and would be of no cost to the Fund. At the Public Hearing with the Minister for T&R, the Chief Officer, ED, stated that:

Chief Officer (hearing with Minister for T&R on 10th January 2013)

"...we will provide that administration function from within our existing resource base..."¹⁷²

9.5.15 At the Public Hearing with the Minister for ED on 14th January, the Chief Officer, ED, further explained:

"...one of the advantages of EDD is, as you know, Chairman, a large proportion of our spend is discretionary. That does allow us to move resources around within the department to help with demand should it appear at any time, so we would do it from within existing resources..."¹⁷³

9.5.16 The Minister for T&R also confirmed the approach to the allocating EDD resources towards the Fund:

¹⁷² Public Hearing with the Minister for Treasury & Resources – 10th January – page 18

¹⁷³ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 13

Minister for T&R

“...The Fund is not going to be recharged any costs within EDD. All EDD services and Economic Services and Treasury where that is appropriate, that is a zero cost to the fund...”¹⁷⁴

9.5.17 Looking at the slightly broader States resources that would be required (see also Section 9.2), which includes Law Officers’ time for each Funding Agreement and Royalty Agreement, the EAU and Treasury and Resources, the Minister for ED gave the example of how the EAU in particular would be used:

Minister for ED

“...I think probably another way to look at it would be taking the example of the Economics Unit in particular. If they have the capacity to provide the advice necessary for the Innovation Fund within their existing resources, then that is absolutely fine. That is what we believe will be the case. Now, if for example, there was such a commitment of their time to look at projects coming forward to the Innovation Fund that there were things that they could not do and therefore they needed additional resource, then that is a matter outside of existing resources...”¹⁷⁵

9.5.18 The Panel asked how this time would be captured to be applied against the Fund. The Chief Officer, ED, told us:

Chief Officer (hearing with Minister for ED on 14th January 2013)

“...The EAU does not write timesheets based on how it divides its time or anything else. There are, I think, 3 at the moment ... 3, Dougie Peedle and 2 other people working there. They do not write timesheets, so it would be an estimate of the proportion of their time...”¹⁷⁶

9.5.19 The Panel also asked the Chief Officer, ED, whether EDD had calculated what the cost in man hours to the Fund is likely to be:

Chief Officer (hearing with Minister for ED on 14th January 2013)

“...it would be a proportion of the Economic Advisor’s total costs and a proportion of the EDD officer costs which are all fully provided for and covered within the existing budgets...”¹⁷⁷

¹⁷⁴ Public Hearing with the Minister for Treasury & Resources – 10th January 2013 – page 19

¹⁷⁵ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 7

¹⁷⁶ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 10

¹⁷⁷ Public Hearing with the Minister for Economic Development – 14th January 2013 – page 7

9.5.20 The Minister for ED was of the opinion that this resource would be an overall benefit to the Fund:

Minister for ED (hearing on 14th January 2013)

"...the belief is that it is going to be very very small in consideration of the overall benefits that it will deliver..."¹⁷⁸

9.5.21 Although it has been explained to the Panel that the resource already exists and has been allocated for within existing budgets, this resource will be an overhead of the relevant Department, the cost of which has not been attributed to the Fund. Without being able to ascertain how many man hours are required and at what cost, it is difficult to determine how the fund will be performing and measure its overall success.

9.5.22 Within the Panel's expert advisor's report, section 5.9 states what CIPFA would deem good practice for the management of costs. It recommends that a best estimate of annual operating costs for the management of the JIF including all overhead support (external and internal costs) is determined. In addition, it proposes that assessment is undertaken of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the utilisation of the Fund. Transparency on this exercise will effectively provide an indication of the true utility of the JIF.¹⁷⁹

Key Finding:

It is proposed that the operational and administration functions of the JIF would be covered by existing Departmental resources, which the Panel was told would therefore be of no cost to the Fund. This approach does not transparently account for the internal 'invisible' costs of the Fund and the man hours it requires.

Key Finding:

No full and transparent assessment of the 'invisible' costs that will be incurred by States Departments to fulfil the administration and monitoring functions of the Fund has been made. Without defining the cost of the internal resource requirements, it is difficult to determine how the Fund is performing and to measure its overall success relative to cost.

¹⁷⁸ Public Hearing with Minister for Economic Development – 14th January 2013 – page 10

¹⁷⁹ CIPFA report – page 27

Recommendation:

A best estimate of annual operating costs for the management of the JIF, including all overhead support (external and internal costs), should be provided. Additionally, an assessment should be undertaken of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the utilisation of the Fund. Transparency on this exercise will effectively provide an indication of the true utility of the JIF.

APPENDIX 1: EVIDENCE CONSIDERED

Written Submissions:

- Correspondence from Minister for Economic Development
- Correspondence from Minister for Treasury & Resources
- Jersey Chamber of Commerce – submission of evidence
- CIPFA report
- Jersey Innovation Fund - Operational Terms of Reference
- Innovation Fund Application Form
- Innovation Fund Policy Framework

Public Hearings:

- 10 January 2013 – Minister for Treasury & Resources
- 14 January 2013 – Minister for Economic Development
- 6 February 2013 – Jersey Chamber of Commerce
- 6 February 2013 – Jersey Business
- 6 February 2013 – Digital Jersey
- 22 February 2013 – Minister for Economic Development

APPENDIX 2: CIPFA REPORT



States of Jersey
States Assembly



États de Jersey
Assemblée des États

ECONOMIC AFFAIRS SCRUTINY PANEL

REVIEW OF THE JERSEY INNOVATION FUND

28 February 2013

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Certificate No. 5631/06

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APPENDICES

Appendix 1	Review Methodology
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1. Executive Summary

- 1.1 In December 2012, the States of Jersey commissioned CIPFA Business - Finance Advisory (the commercial arm of the Chartered Institute of Public Finance and Accountancy) to support the work of the Economic Affairs Scrutiny Panel in the Review of the Jersey Innovation Fund as outlined in its Terms of Reference. It should be noted that this report represents CIPFA Advisory's independent view, taking into account a range of evidence gathered throughout the review. The review was carried out as part of the States of Jersey's internal scrutiny processes as co-ordinated by the States Greffe.
- 1.2 Economic Development stimulus will, by its very nature, cut across a full spectrum of differing sectors, businesses and enterprises. Investment aimed at driving enterprise and innovation will inevitably invite an element of risk and the balancing of providing an optimal level of stimulus without the impediments of "red tape" together with the minimisation of risk to the Fund is usually a difficult one to achieve. However, the systematic challenge and testing of the proposed process controls through scrutiny demonstrates a commendable approach as a step towards ensuring that the key objectives of the Jersey Innovation Fund are met.
- 1.3 The Review took place between January and February 2013 and we based our assessment on a mix of evidence obtained through Direct Meetings with the Chief Officers, members of the Economic Affairs Scrutiny Panel and Document Review including transcripts of meetings held between the panel and a number of key stakeholders. This Report outlines our position to 28 February 2013.

Key Lines of Enquiry

- 1.4 Based upon our preliminary work and evidence gathered from the a range of evidential sources highlighted we categorised our approach into Key Lines of Enquiry (KLoEs):-
- Risk Mitigation – Operational and Policy Framework
 - On Going Performance Management of the Fund
 - Resourcing Fund Management;
 - Fund Sustainability; and
 - Innovation Fund Comparability;

Risk Mitigation – Operational and Policy Framework

- 1.5 The Innovation Fund policy Framework has been recently produced by EDD to provide vital detail behind the management arrangement for the operation of the Fund. These include criteria for Applicants for support including Loans and Grants. A review of the Innovation Fund Policy Framework and the Application Form Guidelines outlined the following for Loan Applications:-

- Successful applicants can only be Company formations incorporated in Jersey – so Partnerships, LLPs or sole traders would be ineligible for assistance;
- That the Loan parameters have now been fixed at a minimum threshold of £20,000 up to a maximum of £500,000;
- Repayment term parameters have been set as – maximum repayment of 5 years with a minimum repayment of 12 months;
- There would appear to be two drawdowns on loan finance;
- Successful applicant must demonstrate compliance with the definition of a ‘high value sector’.
- Improving the overall level of productivity of the economy defined as firms with value added per employee significantly in excess of £65k;
- That the Innovation Fund is a last resort for funding in that there is no other sources of funding and the project would not go ahead without such support; and
- That a Royalty Agreement will be an integral component of the assistance agreement

1.6 Such parameters were included within the Application Form itself. However, at the Panel Meeting with the Minister for Economic Development on 22 February 2013 it was confirmed that the related Application Form which had the Innovation Policy parameters included was accorded the status of draft only. By implication there must now be significant doubt over the current status of the Innovation Fund Policy Framework as currently constituted as it was suggested at the meeting with the Minister for Economic Development that the main parameters fell “broadly between the ranges...” In any event the Minister suggested that the JIF Board would play an active part in determining the criteria for successful applications and have delegated discretion to determine what that may be “by the board as being appropriate to deliver on the objectives.”

1.7 From the Innovation Policy Document and related Application Form it is clear that only an incorporated body i.e. a Limited Company incorporated by Shares would be a qualifying legal entity. However, at the Panel Meeting of 22 February 2013 with the Minister for Economic Development it was confirmed that in response to a question from the Panel Chair as to whether such parameters would preclude Limited Liability Partnerships (LLP) the Minister confirmed that “Either structure or other appropriate structures would potentially qualify..”. The Innovation Policy Framework and the Application Form refers to Memorandum and Articles of Association which can only relate to limited company incorporated bodies and not Limited Liability Partnership, Partnerships or Sole Traders.

Sectoral Restrictions on Applications

1.8 It has been correctly suggested by the Economic Affairs Scrutiny Panel that the parameters outlined within the Innovation Policy Framework may significantly limit the prospectivity of successful applicants – particularly in relation to relative to the criterion “significantly in excess of £65,000 Gross Value Added (GVA) per employee and the definition of “High Value Sector”. A very broad extrapolation of the information

produced by the Economic Statistics Unit on GVA outlines that the Financial Services Sector averages £118,000 per employee whilst Construction equates to £46,000 and, Agriculture along with Hotels/Restaurants both deliver approximately £21,000 per employee. On this crude analysis, it would be our view that the prospectivity of any applicants outwith the Financial Services Sector meeting such a GVA criterion “significantly in excess of £65,000” – in the context of the prevailing economic landscape - is likely to be low.

Application Assessment Grants

- 1.9 The Innovation Fund Policy Framework states that Grants will only be considered in “exceptional circumstances”. Our reading of the above suggests that the requirements for Grant recipients are more onerous given the additionality of the above requirements in addition to all requirements of Loan Applicants as well as entering into a Royalty Agreement.

Due Diligence

- 1.10 Before receipt of the Innovation Policy Framework we had reservations about the absence of detailed procedure relative to Due Diligence. Significant importance was placed on the regulatory application of the Undertaking business licence and the requirement for the applicant to be an incorporated body under the Companies (Jersey) Law 1991, as amended. The establishment of the full identity of applicants, acquiring a history of credit and the requirement to minimise the risk of criminality is assumed to be fundamental. Whilst the Innovation Policy Framework effectively narrowed the range of eligible applicants to incorporated bodies only (presumably the “legal personage” of the incorporated body and Directors) which are subject to regulatory business licencing with Jersey, our thinking was that such constraints should make it easier to carry our due diligence within the application process. However, as the Minister for Economic Development has now confirmed that there is no restrictions placed on legal entity formats that can apply, the effectiveness of Due Diligence processes are key particularly in the context of all legal business formats. In this respect, following the Panel Meeting on 22 February 2013 we now understand that Due Diligence will be externalised and fed to the JIF Board as required.

Performance Management of the Fund - Role of the Jif Board

- 1.11 From the material presented to us the JIF Board appear to be the anticipated body to monitor and manage the performance of the JIF. Whilst the JIF Board are best placed to make these decisions we would still have issues on the ability of the States to track financial performance of successful applicants. In order to meet the objective of Fund sustainability, the maximisation of benefits from the investment of JIF funds in successful ventures will be a requirement. To enable this to happen would require intensive and intrusive performance monitoring. Experience in the financial services industry indicates that whatever the processes and resources devoted to providing additional assurance on financial performance, it is not possible to eliminate the risk of applicant failure even when it is tracked through a core industry risk based assessment.

- 1.12 At the Panel Meeting with the Minister for Economic Development on 22 February 2013 it was suggested by the Chief Executive Officer that there was an expectation that Jersey Business and Digital Jersey would perform a mentoring role on on-going performance and that they would act as a conduit to the JIF Board on performance monitoring on a 'call-off' basis. We have some difficulty with the lack of apparent formalities within these arrangements and absence of detail relative to such defined responsibilities. Whilst such input is to be welcomed, we are not entirely convinced that such bodies were aware of these expected roles relative to relevant transcripts from previous meetings.
- 1.13 Significant Legal and Financial reporting questions surround the concepts of Royalties and Equity Stake involvement particularly in the context of a State fund and Public Law. Given the nature of these issues it would be our considered view that there are still significant detailed legal and financial issues to resolve before the JIF Board has the appropriate levers at its disposal to optimise the management of the Innovation Fund.

Sustainability

- 1.14 It is understood that the JIF will be "self-replenishing" and that "all grants and loans offered will have conditions that allow the JIF to realise enhanced returns if the business were to be successful and/or sold for significant gain." The latter secured from Royalty Agreement. Notwithstanding this objective, the JIF will be inevitably negatively impacted by the following:-
- Grants
 - Operating Expenses
 - Late Repayment/Repayment difficulties
 - Bad Debt – Debt Write Off
 - Valuation – Equity Investment impairment
 - EDD including Economic Advisor's Unit, Legal and Treasury resources deployed in the management of the JIF
 - External specialist advice and support
 - JIF Board Costs – 12 meetings per annum – including fees for Private Sector members and support
- 1.15 In view of the above, particularly in the context of risk, is the JIF realistically likely to be "self-replenishing" – even over the medium term and in terms of Financial Strategy is the financing objective of JIF as "self-replenishing" aspirational rather than a prudent and realistic assumption? During the course of our work we tried to identify the underpinning rationale for the self-replenishing assumption/objective. The Director of Business Creation and Growth unequivocally confirmed that the JIF cannot be self-replenishing without significant benefits coming back to the States through Royalty Clauses – taking benefits from Seed Investment Finance and "High Growth" propositions. Given that JIF would effectively be the "lender of the last resort" after failing to secure alternative finance from Banks and Private Investor sources, we would have concern about the validity and prospectivity of the "self-replenishing". At the

latest Panel Meeting with the Minister for Economic Development on 22 February it was conceded that without success generated by Royalties and/or Equity investments the prospects of fund sustainability at a self-replenishing level would be remote.

- 1.16 A figure of £100,000 of support costs had been originally put forward as the “operational and management” costs for the fund. We have now established that the original estimate of £100,000 is attributed to external advisors – provision of management input to the fund that is not funded within the budget envelope of the Economic Development Department. Given the expected cost exposure of operating the fund relative to items listed above it is highly possible that total estimated charges to the Fund could easily equate to within a range of £250,000 to £400,000 per annum making the potential sustainability from interest bearing loans - at the smaller number of 4/5 per annum (even at the maximum threshold of £500,000 at a rate of say 5%) being impossible to achieve.

Speculative Investments

- 1.17 Even where Royalties accrue or potential increases in Equity valuations allow a real benefit to be obtained - given the nature of support offered conditional on no other qualifying support from the Financial services market or Private Equity Investment being obtainable, the relative probabilities for high yields are likely to be low – with the practical potential to extract such benefits even lower. Mature venture capital management is not remotely core to the competencies of Government entities even where successful innovation funds are purported to operate. At the Panel Meeting with the Minister for Economic Development on 22 February 2013 the Chief Executive Officer for EDD indicated that “.a successful equity at 20, 30, or 40 times the level of investment, which is not uncommon.” Such aspirations of high yields on high risk investments are highly speculative in nature and reliance on such level of returns is clearly not consistent with the prudent management of public funds.

Fund Accounting

- 1.18 Following proper accounting practice the JIF should be charged with all external and internal management costs including overheads. In so doing, full transparency on operating the Fund would be achieved. Were full financial reporting compliance to be achieved, given the risks involved in operating such a Fund, the low probability of high yields from Equity Sharing or the acquisition of Royalties and a not insignificant number of expenditure sources (including support overheads) we would find it difficult to accept that the Fund would be sustainable or self-replenishing.

Annual Operating Cost Estimate and Outcomes

- 1.19 Given the issues highlighted above we would strongly recommend that a best estimate of annual operating costs for the management of the JIF including all overhead support (external and internal costs) is determined. We would also recommend that an assessment is undertaken of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the

utilisation of the Fund. Transparency on this exercise (including the establishment of an Opportunity Cost) will effectively provide an indication of the true utility of the JIF.

Innovation Fund Comparability

- 1.20 We have looked at a number of countries which have been cited as operating Innovation Funds – Malta, UK, Ireland, Israel and Singapore. We would be of the view that none of these examples are truly aligned to the proposed Government Fund Model highlighted within the Operational Terms. Having carefully looked at Malta, UK, Ireland, Israel and Singapore - comparisons are probably only most relevant with conditions operating in Israel and even there operating conditions do not invite favourable comparison with the operating context and conditions on Jersey. Such arrangements are invariably designed to attract significant inward investment primarily focussed on global markets with a large number of assistance strategies outwith Loans, Grants and Equity sharing. Intensive assistance can include Consultancy Support, Property Provision and relocation, locational support, Business Rates abatement, Tax incentives, direct grant funding of new employees and Marketing assistance. It is interesting to note that in respect of the UK, Ireland and Malta, some regional economic support is funded in part through the EU by way of European Regional Development Funding (ERDF) Assistance and channelled through the central/local government infrastructure of these respective countries.

Fund Type

- 1.21 Whilst there is much that can be learned from the operation of Innovation Funds across the world, it is important that the objectives and operating context aligned to each Fund is fully appreciated. Aspects of the funds operated in the UK and Israel have some similar attributes to the JIF although the key differences on the extent of venture capital fund matching remain. Indeed, differences in operating environment, primary objectives and underpinning funding make true comparisons difficult. We would agree that the closest Fund type to the proposed JIF, in its initial stages, is a Government Fund as outlined within the Report on the Establishment, Funding and Operation of the JIF. However, the example given of Israel should be taken with some caution given the differentials in state expansionary objectives and operating environment. At the Panel Meeting with the Minister for Economic Development on 22 February 2013, it was clear that aspirations on match funding and equity will invariably move the positioning on fund type towards a Partnership Fund type rather than a Government Fund Type.

Evolving Position - A 'Work In Progress'

- 1.22 During the latest aspect of our work it has become apparent that key parameters associated with the purpose and administrative management of the fund were still evolving with key management processes being a "work in progress". This position became well highlighted within the Panel Meeting with the Minister for Economic Development held on 22 February 2013. The following issues relative to an evolving position on the setting up and management of the JIF are worthy of noting:-

- There is significant doubt on the validity of the detail as contained within the Innovation Fund Policy Document and related Application Fund;
- That the restrictions outlined within the Innovation Policy Framework and related Application Form on applicants being Limited Company format have now been removed with all Business Legal Entity structures being eligible for assistance;
- That the proposed JIF Executive Post was no longer to be recruited and that the post would be purely administrative in nature and only as co-ordinating support role for the JIF Board;
- The JIF Board will be a “Working Board rather than a Review Board” meeting regularly (once per month) and solely arriving at judgements on the merits of Applications – no Officer recommendation or Judgements are within scope;
- A new and specific role has been created for Jersey Business and Digital Jersey as Mentors for aftercare and advisers to the JIF Board in relation to Performance Management on individual beneficiaries of support has been established ;
- That members of Jersey Business and Digital Jersey may be nominees within new Equity Stake Board arrangements; and
- Law Officers have yet to provide views on Royalty Agreements or the legislative changes required in order to operate Equity Stake holdings.

1.23 Outwith the above issues the Panel were advised that much of the detail behind the management of the scheme will be delegated to the JIF Board. States Members are being asked to vote on the Proposition for the establishment of the JIF. Part C of the Proposition is outlined as follows:-

“to agree that the Jersey Innovation Fund should be operated and used in accordance with the Operational Terms of Reference set out in the Appendix, under the supervision of an independent Innovation Board to be established by the Minister for Economic Development through a process overseen by the Appointments Commission and following the commission’s code on appointments to public bodies.”

1.24 Given the expectations on the delegation of the detail to the JIF Board and the level of fluidity/lack of clarity on the detail relative to the Operational Terms of Reference highlighted in section c of the Proposition, it would be our recommendation that clarity on the detail surrounding the scheme is achieved before Members are asked to vote on the Proposition.

Strengths

1.25 The creation of the Jersey Innovation Fund is a bold and very positive step towards encouraging economic growth through the promotion of specific innovation related activity. We fully recognise that in promoting/managing such objectives there is a difficult balance of competing objectives to maintain. Within the Proposition for the establishment of the JIF and associated background information, there is much to commend particularly in the desire to:-

- Targeting ventures that are most likely to succeed in relative terms;
- Ability to look beyond commercial terms to broader economic impacts;
- Setting a relatively high level of maximum Loan facility for a single applicant relative to the overall Fund - £500k to £5m;
- Creation of robust Business Case testing requirements including counterfactual positioning;
- Optimisation of any resulting benefit from the investment;
- Flexible in the approaches taken to Funding within parameters;
- Minimise bureaucracy – with a rapid turnaround; and
- Utilise key private sector business skills within the establishment of a Private Sector led JIF Board;

Further Development Challenges

1.26 Notwithstanding the advent of the Innovation Fund Policy Framework it would be our considered opinion that more clarity is needed on a number of key issues including:-

- A clear position/view on what successful venture would look like – the quantification of success;
- Clarification on the extent of delegated authority and discretion to be provided to the JIF Board for the management of the Fund;
- Clarity on the status of the Innovation Fund Policy Framework – an elimination of apparent inconsistencies between documents;
- Precision on the key support parameters;
- Clarification on Fund being final resort status;
- Clarity on actual Officer Support that will be provided to the JIF Board – for example what are the exact resources earmarked for JIF Support role and what will the consequences be for the activities that are currently being serviced by such current resources? Essentially the opportunity cost of moving resources;
- An accurate assessment of the total annual costs of running/operating the fund including all Management and overhead as well as external support including externalised legislative drafting;
- An assessment of the overall cost of running the Fund against expected Benefits/Outcomes;
- An assessment of the Opportunity Cost of running the JIF relative to standard investment;

- All outstanding Legal issues including opinion of the Law Officers on the legality of the proposals and available options, the management of Royalties and Equity Investments be fully examined and resolved including potential interventionist strategies as well as potential Equity exposure issues; and
- Resolution of differing Stakeholder expectations through closer working.

Developing a Collaborative Approach

- 1.27 It is clear that a lot is expected from the JIF Board in a number of areas within its scope including the Approval Recommendation and on-going management of the Fund including aftercare. Intuitively the operating arrangements and framework for the Fund appear to be necessarily complex and highly resourced relative to the potential number of successful applicants that may be supported – 4/5 per annum with the Board Meeting once per month. Given that key stakeholders such as Jersey Business, Digital Jersey and the Jersey Chamber of Commerce already possess access to significant sector skills and business intelligence, it would appear appropriate to consider the potential for closer collaborative involvement in the direct management arrangements for the Fund. Such involvement could potentially range from provision of complimentary resources to the JIF Board to, at the other end of the scale, carrying out support currently envisaged or Process mapped for EDD staff. We note that at the Panel Meeting of 22 February 2013 with the Minister for Economic Development that there is now an enhanced role for Jersey Business and Digital Jersey in respect of mentoring and performance management post awarding of support although, as stated, we are not entirely convinced that such bodies were fully aware of these expected roles.

Concluding Comments

- 1.28 Having carefully considered all the material made available to us, we would be of the opinion that there is considerably less clarity on the detailed management arrangements for the Jersey Innovation Fund than we would expect and indeed, less than other Public Fund Management arrangements we have seen. Implied delegation on the detailed aspects of these arrangements to a newly formed JIF Board without clear and detailed terms of reference invites significant risk.
- 1.29 At present there is a significant lack of precision on the arrangements for managing the Fund and the continuing evolving position on the management arrangements does not provide needed assurance on the critical aspects of governance and internal control required by acknowledged good practice in the stewardship of public funds. Notwithstanding this position the direction of travel taken by the States of Jersey in subjecting the proposed management arrangements for the establishment of the Jersey Innovation Fund to scrutiny is undoubtedly the right one in the quest to establish a robust framework for the operation of an Innovation Fund. A robust framework properly seeks to achieve the difficult balancing of the requirements for the appropriate stewardship of public money with the creation of a dynamic catalyst for meaningful economic opportunity and growth from the potential synergies of seed fund investment. Such an approach is highly commendable and does provide a ‘golden’

opportunity to further harness, through collaborative working, the best attributes of both Private and Public Sectors.

2. Background

2.1 In December 2012, the States of Jersey commissioned CIPFA Business - Finance Advisory (the commercial arm of the Chartered Institute of Public Finance and Accountancy) to support the work of the Economic Affairs Scrutiny Panel in the Review of the Jersey Innovation Fund as outlined in its Terms of Reference. The context for the introduction of the Jersey Innovation Fund is noted as follows:-

“The principle of the Jersey Innovation Fund is set out in P55/2012 Economic Growth and Diversification Strategy as approved by the States. The aim of the Fund is to support innovation and it will be available to support a wide range of activity from direct business support to strategic infrastructure investments, in the private, public and third sectors. Proposals will be required to improve the rate of innovation in Jersey and lead to significant employment creation.”¹⁸⁰

2.2 It should be noted that this report represents CIPFA Advisory’s independent view, taking into account a range of evidence gathered throughout the review. The review was carried out as part of the States of Jersey’s internal scrutiny processes as co-ordinated by the States Greffe.

2.3 CIPFA fully understands the significant issues relating to the promotion of economic growth, optimising available scarce resources in pursuit of this goal whilst maintaining robust levels of probity and stewardship. Strong internal controls over the management of the Innovation Fund will be critical to the maintenance of proper administration and stewardship of the fund and the level of governance associated with meeting the high level objectives as laid-out within the Report titled “Establishment, Funding and Operation of the Jersey Innovation Fund.”

2.4 Economic Development stimulus will, by its very nature, cut across a full spectrum of differing businesses and enterprises. Investment aimed at driving enterprise and innovation will inevitably invite an element of risk and the balancing of providing an optimal level of stimulus without the impediments of “red tape” together with the minimisation of risk to the Fund is usually a difficult one to achieve. However, the systematic challenge and testing of the proposed process controls through scrutiny demonstrates a commendable approach as a step towards ensuring that the key objectives of the Jersey Innovation Fund are sustained and the capability of the Economic Development Department is maximised in running the processes that underpin the Fund.

2.5 The Review took place between January and February 2013 and we based our assessment on a mix of evidence obtained through Direct Meetings with the Chief Officers, members of the Economic Affairs Scrutiny Panel and Document Review including transcripts of meetings held between the panel and a number of key stakeholders. Our methodology used in the course of this review is diagrammatically

¹⁸⁰ <http://www.scrutiny.gov.je/Pages/Review.aspx?ReviewId=176>

illustrated as Appendix 1 to this Report. This Report outlines our position to 28 February 2013.

Document Scope to Date

2.6 In relation to document review our work has included review of the following documents: -

- Proposition from the Minister for Treasury and Resources
- Report on Establishment, Funding and operation of the Jersey Innovation Fund
- Appendix 1 to “The Report” – Operational Terms of Reference and Application Assessment
- Appendix 2 – Examples of Innovation Funds
- Application 3 – Application Business case Templates
- Economic Development Department – Draft Business Case User Guide
- Economic Affairs Scrutiny Panel - Jersey Innovation Fund Review Terms of Reference
- Innovation Fund Policy Framework

Transcripts

2.7 As well as Document Review outlined above transcripts from the following meetings held by the Economic Affairs Scrutiny Panel were reviewed:-

- Minister of Treasury & Resources – 10 January 2013
- Minister of Economic Development – 11 January 2013
- Minister of Economic Development – 22 February 2013 (attended by CIPFA)
- Digital Jersey – 6 February 2013
- Jersey Chamber of Commerce – 6 February 2013
- Jersey Business – 6 February 2013

2.8 On 23 January 2013 exploratory meetings were held between CIPFA and the following Chief officers involved in the process:-

Meeting 1

Dougie Peddle – Economic Advisor

Jim Shilliday - Project Director

Meeting 2

Sean Pritchard - Director of Business Creation and Growth

Key Lines of Enquiry

2.9 Based upon our preliminary work and evidence gathered from a range of evidential sources highlighted above we categorised our approach into Key Lines of Enquiry(KLoEs).

2.10 These KLoEs were as follows:-

- Risk Mitigation
- On Going Performance Management of the Fund
- Resourcing Fund Management;
- Fund Sustainability; and
- Innovation Fund Comparability;

3. Assessment Capability and Risk

3.1 This section sets out our assessment of the arrangements for processing applications for assistance and determining the strengths of evaluating risks.

Application Assessment

3.2 It is clear that outwith the concept of Equity Sharing – which will require legislative change, that the Fund will be issued primarily for the advancing of loans with “grants only issued in exceptional circumstances”¹⁸¹. This was reiterated within the Panel Meeting with the Minister for Economic Development held on 22 February 2013. We were recently provided with the Jersey Innovation Fund Policy Framework and a copy of the application form for assistance by the EDD Director of Business Creation and Growth. It is understood that information from this form will be used as the foundation for one of two Appraisal Templates (under and over £25,000 thresholds) which will be used by staff at the Economic Development Department in the initial assessment of applications. An extract from the front page of the Application Form highlights Eligibility Guidelines for potential applicants as follows:-

- **This completed form must be returned at least 6 weeks days before any support is required.**
- **This form can be completed by both start up, established businesses and collaborative partnership**
- **Applications for projects already started will only be considered in exceptional circumstance.**
- **The information proved is critical to the assessment of your application. Make sure you provide everything that is requested.**

Jersey Innovation Fund (JIF) Eligibility Guidelines

An Applicant shall be eligible if the Applicant:

- has no available Collateral to secure finance from other sources
- clearly demonstrates that without the JIF support the project will not proceed;
- is a Business incorporated under the Companies (Jersey) Law 1991;
- has supplied all information requested;
- has obtained the required business licence in accordance with the Regulation of Undertaking Law;
- is a businesses or a project that is or will operate in a High Value Sector;
- can demonstrate the investment into the project of business has potential to improve the overall level of productivity of the economy – i.e. those firms with value added per employee significantly in excess of £65k;

The Application shall be eligible if

- the applicant is a high growth business.
- the amount requested does not exceed £500,000;

¹⁸¹ Innovation Fund Policy Framework – Page 1 Paragraph 2

- the amount requested is greater than £20,000
- the initial drawdown for the Project is made within 6 months of the support being approved
- the application is for a Loan Facility in sterling;
- the project will be delivered within the Bailiwick of Jersey;
- the applicant signs a Royalty Agreement as determined by the States of Jersey. .

Eligible costs for an Application can include:

- equipment (purchase or rental)
- facilities or systems, includes property costs;
- project implementation costs including reasonable consultant fees but excludes all in-kind labour costs;
- purchase of assets
- professional fees
- research and development costs

Please use the above as guidelines to help with your application. If you have any questions contact Economic Development Department.

3.3 A review of the document titled Innovation Fund Policy Framework the Application Form Guidelines outlined the following for Loan Applications:-

- Successful applicants can only be Company formations incorporated in Jersey – so Partnerships, LLPs or sole traders would be ineligible for assistance;
- That the Loan parameters have now been fixed at a minimum threshold of £20,000 up to a maximum of £500,000;
- Repayment term parameters have been set as – maximum repayment of 5 years with a minimum repayment of 12 months;
- There would appear to be two drawdowns on loan finance;
- Successful applicant must demonstrate compliance with the definition of a ‘high value sector’
- Improving the overall level of productivity of the economy defined as firms with value added per employee significantly in excess of £65k;
- That the Innovation Fund is a last resort for funding in that there are no other sources of funding and the project would not go ahead without such support; and
- That a Royalty Agreement will be an integral component of the assistance agreement

3.4 Such parameters were included within the Application Form itself. However, at the Panel Meeting with the Minister for Economic Development held on 22 February 2013, it was confirmed that the Application Form was currently only accorded draft status. In any event the Minister suggested that the JIF Board would play an active part in determining the criteria for successful applications and have delegated discretion to determine what that may be “by the board as being appropriate to deliver on the objectives.”

3.5 From the Innovation Policy Document and related Application Form, it is clear that only an incorporated body i.e. a Limited Company incorporated by Shares would be a qualifying legal entity. However, at the Panel Meeting of 22 February 2013 with the

Minister for Economic Development, it was confirmed that in response to a question from the Panel Chair as to whether such parameters would preclude Limited Liability Partnerships (LLP) the Minister confirmed that “Either structure or other appropriate structures would potentially qualify..”. The Chief Executive Officer further confirmed that “A Jersey Company can be a limited liability partnership.” We would respectfully suggest that this is incorrect as a matter of Law in its strictest sense although there are some similarities within the Company law framework. The Innovation Policy Framework and the Application Form refers to Memorandum and Articles of Association which can only relate to incorporated bodies as Limited Companies and not Limited Liability Partnerships, Partnerships or Sole Traders.

- 3.6 During our work it was suggested by EDD that Treasury & Resources would be recommending the relevant interest rate to apply to Loan Applications, however we understand that this has not been agreed as yet with Treasury and Resources.

Grants

- 3.7 The Innovation Fund Policy Framework states that Grants will only be considered in “exceptional circumstances” and only if all of the following are met:-

- The applicant can justify and demonstrate that the project will not generate any income within the first 5 years of the Project starting.
- The Project will result in significant economic spillovers in Jersey during the first 5 years of the project commencing
- The project will deliver a significant economic competitive advantage to the Island.
- The project will be delivered in the Bailiwick of Jersey
- The project, within the first 5 years, will result in the creation of new high value jobs (direct or indirect employment)

If all of the above are met the application, assessment and approval process will follow the policies defined for Loans, which includes the requirement for the company receiving a Grant to enter into a Royalty Agreement.

- 3.8 Our reading of the above suggests that the requirements for Grant recipients are more onerous given the additionality of the above requirements in addition to all requirements of Loan Applicants as well as entering into a Royalty Agreement.

Innovation Fund Policy Framework

- 3.9 The Innovation Fund Policy Framework has been recently produced by EDD to provide vital detail on the operation of the Fund. At the Panel Meeting with the Minister for Economic Development on 22 February 2013 it was confirmed that the related Application Form which had the Innovation Policy parameters included was accorded the status of draft only. By implication there must now be significant doubt over the current status of the Innovation Fund Policy Framework as currently constituted as it was suggested at the meeting with the Minister that the main parameters fell “broadly between the ranges...”. In respect of funder of last resort,

the Policy Framework unequivocally outlines this position in bold lettering within the first page of the policy document:-

“For the avoidance of any doubt the Fund will not compete or replace private sector funding, only be used after all other sources of funding and security have been fully utilised, and be used to invest in innovative projects.”

- 3.10 Whilst this position appears to be fairly clear at the final Panel Meeting with the Minister for Economic Development on 22 February, it was suggested by the Chief Executive Officer that match funding would be considered if “they came to us and they got partial funding but could not secure the rest of it...” Match funding is a feature of Innovation Fund Strategies employed by the Countries used within the International Comparators. However, this type of Model is a different Model to that outlined as the Fund type which the JIF purports to take as per the Report supporting the Proposition.
- 3.11 The scope outlined within Page 1 of the document does not, in our view, precisely outline the role and status of the framework – particularly in the context of the scope and wording used – “which will be used to guide” in the context of the following:-

Policy Framework

This document is a Policy Framework, presenting a range of policies which will be used to guide; eligibility criteria; the application and assessment requirements; risk management; corporate governance and reporting requirements

The Policy Framework will also be used to help manage expectations by encouraging applications for projects that can clearly demonstrate that the investment in innovative will to lead to high value-added activity and the creation of employment in businesses with high growth potential

- 3.12 At present we are not certain as to the status of this policy framework – particularly after the Panel Meeting with the Minister for Economic Development held on 22 February 2013.

Sectoral Restrictions on Applications

- 3.13 It has been correctly suggested by the Economic Affairs Scrutiny Panel that the parameters outlined within the Innovation Policy Framework may significantly limit the prospectivity of successful applicants – particularly in relation to the criterion “significantly in excess of £65,000 Gross Value Added (GVA) per employee and the definition of “High Value Sector”. A very broad extrapolation of the information produced by the Economic Statistics Unit on GVA outlines the following GVA values:-

	Hotels	Agriculture	Construction	Finance
Total GVA 2012	£129,600,000	£46,800,000	£234,000,000	£1,476,000,000
Employees	6,320	2,230	5,100	12,500
GVA per Employee	£20,506	£20,987	£45,882	£118,080

3.14 Whilst it is accepted that these are broad averages and there may be extreme positions within each sector values it does suggest that the prospectivity of applicants meeting these parameters outwith the Financial Services Sector is likely to be low – particularly within the prevailing economic environment. However, at the Panel Meeting with the Minister for Economic Development on 22 February 2013 the Chief Executive Officer for EDD stated that it was unlikely that the Financial Services Sector would be recipients of such support from the Fund.

Business Template

- 3.15 A Business Case Template has been produced by EDD differentiating the level of information required to formulate an assessment. As highlighted above, there are two templates – one for support valued at £25,000 and above and one for below that level. The extent of evaluation differs in relation to the level of support. Given the minimum threshold value of £20,000 for Loan financing we are assuming that the value of ‘lower’ level applications would fall within a narrow £20,000 to £25,000 range.
- 3.16 We understand that the templates are founded upon the HM Treasury Green Book “Best Practice”¹⁸². Whilst the ‘Green Book’ sets out the broad framework for the appraisal and evaluation of all policies, programmes and projects. It is indeed the benchmark principles for evaluating competing options by Public Bodies within the UK – usually a range of options relative to a single objective or project. A popular feature of Option Appraisal is the utilisation of Net Present Value of all cashflows associated with an option – with all Financial impacts complemented with non-financial considerations including the influence of Optimism Bias - the tendency for forecasters/appraisers to be systemically overly optimistic. Whilst the utilisation of some basic Green Book principles within the construction of the Business Templates is positive, it would be our opinion that the evaluation of Business Plans will require a more holistic approach with some form of relevant sector knowledge/experience rather than using certain components of good practice albeit within a template format.
- 3.17 In the early stages of application assessment we foresee the requirement to utilise relevant business skills in capturing the most relevant data from the application form and the construction of the Business Template. Whilst we understand that the Economic Advisor’s Office will be involved in the assessment of the economic impact for each application, we do have some reservations as to the provision of

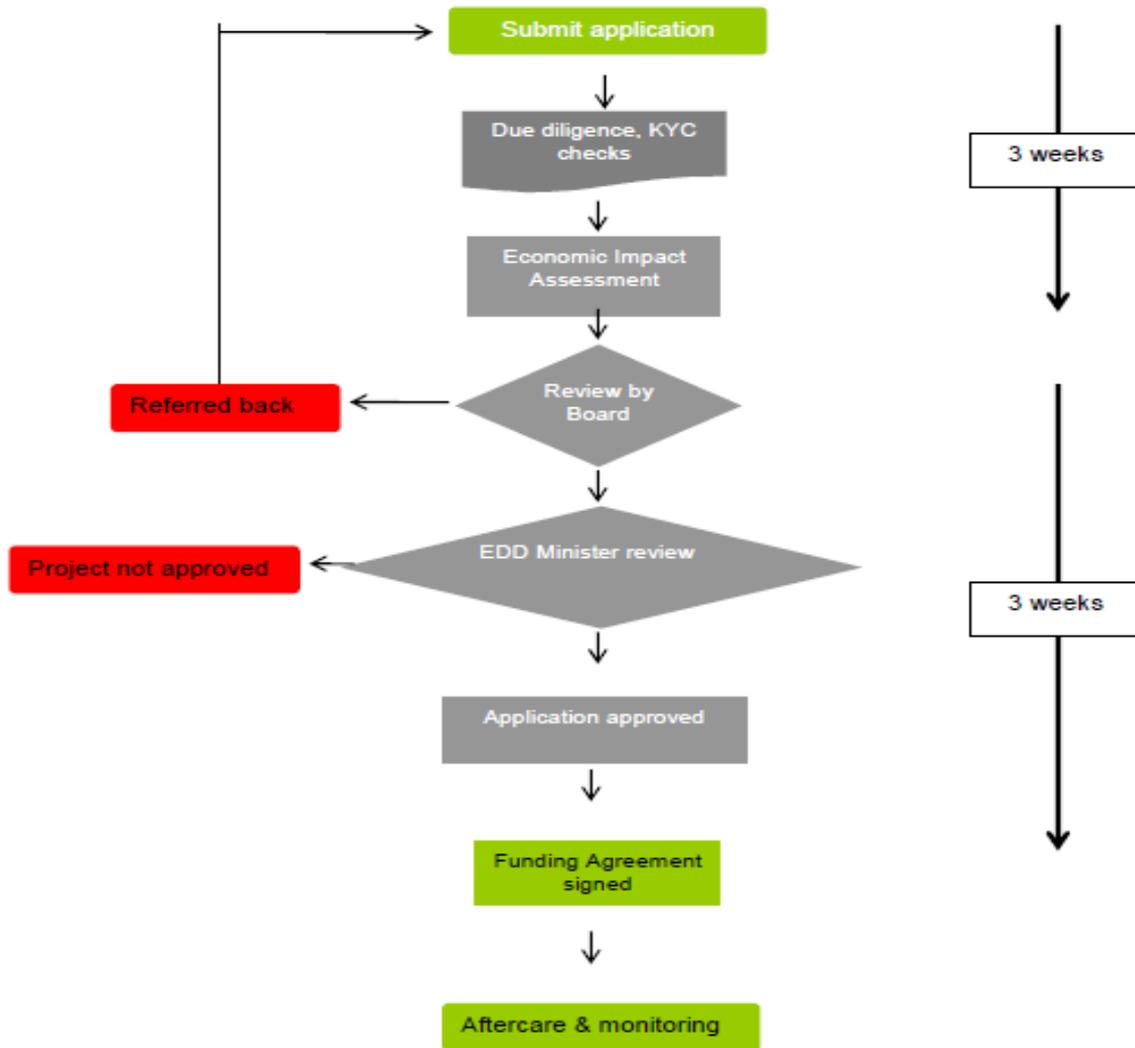
¹⁸² Jersey Innovation Fund – Operational Terms of Reference – Appendix 1

appropriate Business Analytical skills required for this process particularly within the early stages.

- 3.18 We were advised by the Director of Business Creation and Growth that an additional post of Jersey Innovation Fund Executive (to be funded from existing EDD Budgets) would be appointed to play a key role in managing the process between the administration of the Applications including aspects of primary Due Diligence and the JIF Board. This position has been substantially altered at the Panel Meeting of 22 February with the relevant Minister where it was confirmed that the support will take the form of Administrative Support, be part of the remit of an existing post at Grade 12 with costs of approximately £45,000 to £50,000 including employer costs.
- 3.19 We have been advised that it is expected that no more than 4 or 5 Applications will be successful for Loan financing within the period of one year although it was also anticipated that the JIF Board would meet once per month.

Processing Mapping

- 3.20 The actual process of application assessment and evaluation is outlined within Appendix 6 of the Operational terms of reference. This Process Map outlines the required steps along with the expected timescales from Application Submission to Ministerial Approval and Aftercare and Monitoring. What is less clear is the work that will be carried out by the JIF Board as well as the time that the application will be considered by the JIF Board. We understand that the entire process should take no more than six weeks to complete with three weeks up to a JIF Board Decision on referral to the Minister for Approval or back to the Applicant for additional information or to intimate no further progress.
- 3.21 It was the view of the Director of Business Creation and Growth that the JIF Board would take a highly interventionist approach in scrutinising applications and approving variations in the terms and conditions. Indeed, the Innovation Fund policy Framework outlines the remit and scope of the JIF Board as:-
- “JIF Board means the Board appointed by the Minister for Economic Development with management responsibility for reviewing applications, making recommendations to approve or reject applications, managing aftercare, producing reports, and all other corporate governance requirements.”
- 3.22 A copy of this Process Mapping highlighted in Appendix 6 of the Operational Terms of Reference is outlined below:--



3.23 On the 6 week timescale – we would be of the view that the period of three weeks from receipt of the Application (suitably vetted) by the Board to potential Funding being agreed by the Minister and the Funding Agreement signed is ambitious particularly in the context of the detailed level of information required and due diligence that needs to be satisfied and also the fact that the Board is due to meet only a monthly basis.

Due Diligence

3.24 The Innovation Fund Policy Framework outlines the Due Diligence Policies in Section 2 of that document. This is replicated as follows:-

2. Due diligence, Policies

2.1 Every Applicant must:

- complete and sign the JIF Application Form
- provide copies of the current Regulation of Undertaking business licence
- supply a copy of the company's Memorandum and Articles of Association

- for all collaborative applications supply copies of all partnership agreements
- provide details of all other sources of funding including copies of all agreements;
- disclose any debentures or securities taken or charges placed on the company;
- disclose full details of any guarantees provided by the Directors to secure Non-Loan Facility funding for the company and or project;
- disclose details of all shareholders and the residential address of each shareholder;
- supply a copy of the latest audited accounts (established business only)
- supply financial forecasts for a minimum of 3 years or the life of the project (if greater than 3 years)

2.2 All Applicants will be subject to financial background checks including credit rating, tax/social security and any Court judgments.

2.3 Applications made by two or more companies must be accompanied by copies of audited accounts for every partner.

2.4 Applications made by a subsidiary company must supply a copy of the parent company's accounts.

3.25 Within 2.2 – we have assumed that credit rating would include credit history.

3.26 Before receipt of the Innovation Policy Framework we had reservations about the absence of detailed procedure relative to Due Diligence. Significant importance was placed on the regulatory application of the Undertaking business licence and the requirement for the applicant to be an incorporated body under the Companies (Jersey) Law 1991, as amended. The establishment of the full identity of applicants, acquiring a history of credit and the requirement to minimise the risk of criminality is assumed to be fundamental. Whilst the Innovation Policy Framework effectively narrowed the range of eligible applicants to incorporated bodies only (presumably the “legal personage” of the incorporated body and Directors) which are subject to regulatory business licencing with Jersey, our thinking was that such constraints should make it easier to carry out due diligence within the application process. However, as the Minister for Economic Development has now confirmed that there are no restrictions placed on legal entity formats that can apply then the effectiveness of Due Diligence processes are key. In this respect, following the Panel Meeting on 22 February 2013, we now understand that Due Diligence will be externalised to a private provider and fed to the JIF Board.

Assessment Policies

3.27 The Policy Framework outlines assessment policies including the role of the Economic Advisor's Unit in relation to economic assessments and responsibilities of the JIF Board – particularly in relation to the assessment of the Business plan for applicants:-

3. Assessment policies

- Every application will be subject to a full economic assessment;
- Economic assessments will be completed by the States of Jersey Economic Advisors Unit.
- The economic assessment will be presented as a written report to members of the JIF Board.
- The JIF Board may, or if requested to do so by the Economic Advisor or the Minister for Economic Development, commission experts to provide specialist technology, financial or legal advice.

□ The JIF Board is responsible for assessing the applicant's business plan. Including its commercial viability; the market opportunity and its size; the competition if any; the capability and experience of the project team, and any identified or unidentified risks.

- 3.28 This aspect of the framework certainly highlights the “hands on” expectations in the operation of the JIF Board. It would be our view that there is a lack of clarity in the relative responsibilities between Officers preparing the Business Case Template with the initial determination of the initial “sift” at Stages 5/6 as outlined in the process mapping and the actual work carried out by the JIF Board. Indeed, whilst it is not totally clear within the Process Mapping where the JIF Board act in relation to Application Assessment, we understand from the last Panel meeting with the Minister for Economic Development that the Jif Board will exclusively undertake the assessment of each application and that this process should take no more than six weeks.

Risk Mitigation

- 3.29 Notwithstanding a full listing of Due Diligence policies as outlined above, we are still not convinced that the initial assessment process prior to Board consideration has been fully process engineered in terms of the actual resourcing of the work within EDD, the required skill sets required in the preparatory work and the requirement to collect this information within a very short period of time. Additionally, the concept of Equity Stake sharing will require some significant appreciation of the attended risks. At the Panel Meeting of 22 February 2013 with the Minister of Economic Development it was suggested that Loan Finance could be converted to Equity during the currency of the agreement if that was considered to be expedient. In order to formulate the strength of an application it will be necessary for the JIF Board to understand and agree what a positive outcome for such a JIF investment would “look like”. As highlighted above we further understand that the JIF Board will have the primary role in the assessment of applications as there will be no recommendation from EDD Officer Support. It is further understood that the JIF Board will meet at least once per month.

Legal Issues - Royalty Agreement

- 3.30 The eligibility policy specifically requires that applicants agree and sign a Royalty Agreement in favour of the States – the expectation being that the States can maximise any benefit arising from ensuing success of the venture. As will be outlined within Section 5 – the objective of maintaining a Self-Replenishing or Fully Sustainable Fund is envisaged to be only achieved through maximising Royalties or equity Stake venture successes. It was confirmed at the meeting of 22 February 2013 between the Panel and the Minister for Economic Development that Royalties would only attach to new products and not existing products or IP. The existing documentation accompanying the Innovation Fund Framework as Appendix 2 is an extract from the Royalty Agreement applied by the Chief Scientist for the Government of Israel. It is currently unclear whether States Law Officers have adapted such an agreement for the prevailing and relevant Jersey Law requirements. Provision would require to be made for enforcement – however more fundamentally

– the determination and definition of what Royalties should incorporate – within the context of the environment of Jersey should be made before such Loans or Grants can be made.

Legal Issues - Equity Stake

- 3.31 It is understood that proposal will be brought forward around six months from the practical inception of the JIF for the Fund to engage in Equity Stake Venture funding. This would most definitely require legislative change as well as an informed position/understanding on how this Equity Stake holding could be determined and measured. We understand that Law Officers have been consulted on the required legislative changes and any drafting work will be put out to private Legal Firm specialising in Public Law drafting. At this point in time it is unclear how the assessment of potential Equity Investments are made within at any application stage.

4. Governance Arrangements and Fund Management

4.1 It is understood that an “independent Innovation Board” will be established with a composition of a minimum of a Chair plus two members from the private sector together with representatives of EDD, Treasury and Resources and the Chief Minister’s Department. Key aspects of the role of the JIF Board are outlined within the Report – Establishment, Funding and operation of the Jersey Innovation Fund as follows:-

- The Board will be responsible for the management of the Fund, assessing all applications and making recommendations to the Economic Development Minister. The Board will be supported by a Fund Executive from the Economic Development Department (from within existing establishment).
- The Board will assess each application on a number of economic and commercial criteria, which will require the provision of detailed information from applicants. As a minimum this will include an economic impact assessment undertaken by the Economic Advisers Unit.
- The Board will make recommendations to the Economic Development Minister in regard to each application.

4.2 It is understood that an “independent Innovation Board” will be established with a composition of a minimum of a Chair plus two members from the private sector together with representatives

4.3 At the Panel Meeting of 22 February 2013 the Minister for Economic Development and the Chief Executive Officer for EDD confirmed that the JIF Board would:-

- ✓ Take a full “hands on” approach to the management of applications, approvals and aftercare;
- ✓ Request for additional information – e.g. additional due diligence;
- ✓ Oversee a mentoring and reporting role to be undertaken by Jersey Business and Digital Jersey on a ‘call –off basis’ in the aftercare of support; and
- ✓ Expectation to meet once a Month.

4.4 Given the complexity, volume and frequency of work it is difficult to envisage that the establishment of the JIF Board will not be achieved without some cost – particularly in respect of private sector representatives relative to the envisaged frequency of monthly meetings and other preparatory time.

Performance Management of the Fund

4.5 From the material presented to us the JIF Board appear to be the anticipated body to monitor and manage the performance of the JIF. This ostensibly includes for the

operational arrangements for the full governance and management of the fund. As outlined in Section 3 above the Innovation Fund Policy Framework defines the work of the Board post application recommendation as:-

“...managing aftercare, producing reports, and all other corporate governance requirements.”

- 4.6 In this respect we are pleased to note that the Reporting Policies(and associated responsibilities) are highlighted within the Policy Framework Document and are what we would expect to see as a robust set of reporting controls. These are highlighted in Section 8 and are composed of :-

8. Reporting Policies

8.1 The JIF Board will provide the Minister for Economic Development and the Treasurer to the States of Jersey with a written report no later than the 31st January and 30th July for every year the fund is in operation and whilst any Loan is still outstanding and remains unpaid. Each report as a minimum must include:

- a full financial statement on the income and expenditure of the Fund,
- a list of all approved Loans including information on repayment schedules,
- a report on all defaults- non repayments, repayment delays, loan restructuring or write-offs
- a progress report on every Project supported by a Loan
- details in any other changes in circumstance.

8.2 Every organisation in receipt of a Loan must provide quarterly progress reports. As a minimum each report must include

1. A progress report against the original Project plan noting all key milestones.
2. A financial analysis of spend and income compared with the original forecast
3. A progress report on all new innovation.
4. Details of any changes in Key Staff
5. Details on any change to the company's Board of Directors

8.3 All organisations in receipt of a Loan Facility must provide an annual Loan Assurance Statement to the JIF Executive Officer. Confirming how the Loan has been spent and the outcomes achieved in comparison with the original plans. (This requirement will be a condition of the Loan Agreement.) The Loan Assurance Statement must be signed by the Directors of the organisation and received by the JIF Executive Officer by the 31st March of the year following the signing of the Loan and Royalty Agreements.

Support to the JIF Board

- 4.7 Given that these Reporting requirements are comprehensive, it is envisaged that such requirements will require extensive practical resourcing within the Economic Development Departments although we were advised at the Panel Meeting with the Minister for Economic Development on 22 February 2013 that such support will be purely administrative and only be a part of an existing officer's remit – this is in

contrast to the position advocated by the Director of Business Creation and Growth relative to the recruitment and appointment of a JIF Executive with associated high level Fund Management responsibilities.

- 4.8 It is still unclear what type of Reports (format and frequency) will be presented to the Board in order to discharge its role – whilst there is a clear reporting requirement of the JIF Board to the Minister of Economic Development, what is less clear is the decision support reporting provided by EDD to the JIF Board itself in order to fulfil this requirement.
- 4.9 In addition to EDD Support, input from Treasury and Resources and Law Officers will be required to allow the JIF Board to be provided with critical support. It is also envisaged that specialist/expert advisers will be employed as required to augment skill/industry specialist needs.
- 4.10 It is noted that there are plans to provide administrative support from existing resources available to EDD supporting the application process and the JIF Board. In some respects the extensive Performance Management aspects of the work of the JIF Board in the governance of the Fund will be balanced by the relatively low level of successful applicants expected by the Director of Business Creation and Growth – being likely to be only 4 to 5 substantive Loans per annum granted and this would relate to the qualitative aspects including likelihood of success – typically high growth potential. This would suggest that such loans would be relatively high value to established business entities – this does not appear to correlate/fully reconcile with the context described on the objectives and ethos of the JIF outlined by the Minister of Treasury and Resources in his recent meeting with the Economic Affairs Scrutiny Panel or indeed, within the initial Report on Establishment, Funding and operation of the Jersey Innovation Fund and Appendix - Operational Terms of Reference and Application Assessment.
- 4.11 If there is likely to be, in contemplation, only a minimal number of applications that are likely to be given fully considered/approved – questions on the viability and the resourcing of the JIF framework including Board and Executive appointment as well as EDD, Legal and Treasury Departmental support may legitimately arise.

On-Going Performance

- 4.12 We understand that it will be up to the Board to make decisions/recommendations on Approvals/Rejections as well as on-going performance issues notably Payment Holidays and Recovery requirements. However, we are still unsighted as to the triggers which would likely precipitate intervention – for example – the extent of loan non-repayment etc.
- 4.13 Whilst the JIF Board are best placed to make these decisions we would still have issues on the ability of the States to track financial performance of successful applicants – we still have no evidence of how this is going to be achieved. Experience in the financial services industry indicates that whatever the processes and resources

devoted to providing additional assurance on financial performance, it is not possible to eliminate the risk of applicant failure even when it is tracked through a core industry risk based assessment. In this respect, even if the proper resourcing requirements could be put in place to allow the Economic Development Department to perform on-going tracking of financial performance, there is undoubtedly going to be significant limitations placed on what it can be legitimately expected to achieve. At the Panel Meeting with the Minister for Economic Development on 22 February 2013, it was suggested by the Chief Executive Officer that there was an expectation that Jersey Business and Digital Jersey would perform a mentoring role on on-going performance and that they would act as a conduit to the JIF Board on performance monitoring on a 'call-off' basis. We have some difficulty with the lack of apparent formalities within these arrangements and absence of detail relative to such defined responsibilities.

Royalties Agreement and Equity Stakes

- 4.14 In order to meet the objective of Fund sustainability, the maximisation of benefits from the investment of JIF funds in successful ventures will be a requirement. To enable this to happen would require intensive and intrusive performance monitoring. What is not clear is how that is going to be achieved.
- 4.15 Significant Legal and Financial reporting questions surround the concepts of Royalties and Equity Stake involvement particularly in the context of a State fund. Having reviewed all available evidence, including the Innovation policy Framework, we are still unclear how these are going to be dealt with. These would include:-
- Valuation/Masurement of Equity Stakes – who would ensure that accurate valuations would be obtained and any impairments/increased value assessed and incorporated within the Accounts of the States?
 - Would the States of Jersey intervene to extract Dividend?
 - Determination on when Royalties crystallise – what arrangements would flag this up?
 - Exposure to legal action from creditors – where equity stake makes the States a “Shadow Director”
- 4.16 It was suggested at the Panel Meeting with the Minister for Economic Development that consideration would be given to outsourcing the management of Equity Investments to a specialist Venture Capital organisation in order to optimise performance. Given the issues outlined above it would be our considered view that there are still significant detailed legal and financial issues to resolve before the JIF Board has the appropriate levers at its disposal to optimise the management of the Innovation Fund.

5. Sustainability

- 5.1 It is understood that the JIF will be “self-replenishing” and that “all grants and loans offered will have conditions that allow the JIF to realise enhanced returns if the business were to be successful and/or sold for significant gain.” The latter secured from Royalty Agreement.
- 5.2 Notwithstanding this objective the JIF will be inevitably negatively impacted by the following:-
- Grants
 - Operating Expenses
 - Late Repayment/Repayment difficulties
 - Bad Debt – Debt Write Off
 - Valuation – Equity Investment impairment
 - EDD including Economic Advisor’s Unit, Legal and Treasury resources deployed in the management of the JIF
 - External specialist advice and support
 - JIF Board Costs – 12 meetings per annum – fees for Private Sector members and support
- 5.3 In view of the above, particularly in the context of risk, is the JIF realistically likely to be “self-replenishing” – even over the medium term and in terms of Financial Strategy is the financing objective of JIF as “self-replenishing” aspirational rather than a prudent and realistic assumption? During the course of our work we tried to identify the underpinning rationale for the self-replenishing assumption/objective. Recent comments on topping up “another caffeine shot” suggest that expectations on retaining the initial £5m Fund is low even at a political level. At the latest Panel Meeting with the Minister for Economic Development on 22 February it was conceded that without success with Royalties and/or Equity investments the prospects of operating a “self-replenishing” Fund would be remote.

Fund Sustainability

- 5.4 The Director of Business Creation and Growth unequivocally confirmed that the JIF cannot be self-replenishing without significant benefits coming back to the States through Royalty Clauses – taking benefits from Seed Investment Finance and “High Growth” propositions. Given that the JIF would effectively be the “lender of the last resort” after failing to secure alternative finance from Banks and Private Investor sources, we would have concern about the validity and prospectivity of the “self-replenishing”. Given the “last resort funder” positioning by virtue of the qualifying criteria outlined in the Innovation policy Framework, we believe that the probability for successful high growth investments is likely to be low especially within the context of the current economic climate.

- 5.5 A figure of £100,000 of support costs had been originally put forward as the “operational and management” costs for the fund. We have now established that the original estimate of £100,000 is attributed to external advisors – provision of management input to the fund that is not funded within the budget envelope of the Economic Development Department. Given the expected cost exposure of operating the fund relative to items listed in paragraph 5.2, it is possible that total estimated charges to the Fund could easily equate to within a range of £250,000 to £400,000 per annum including all management overhead making the potential sustainability from interest bearing loans (at a rate of say 5%) - at the smaller number of 4/5 per annum being impossible to achieve.

Speculative Investments

- 5.6 Even where Royalties accrue or potential increases in Equity valuations allow a real benefit to be obtained - given the nature of support offered conditional on no other qualifying support from the Financial services market or Private Equity Investment being obtainable, the relative probabilities for high yields are likely to be low – with the practical potential to extract such benefits even lower – mature venture capital management is not remotely core to the competencies of Government entities even where successful innovation funds are purported to operate. At the Panel Meeting with the Minister for Economic Development on 22 February 2013 the Chief Executive Officer for EDD indicated that “.a successful equity at 20, 30, or 40 times the level of investment, which is not uncommon.” However, such aspirations of high yields on high risk investments are highly speculative in nature and not consistent with the prudent management of public funds.

Fund Accounting

- 5.7 Following proper accounting practice the JIF should be charged with all external and internal management costs including overheads. In so doing full transparency on operating the Fund would be achieved. Were full financial reporting compliance to be achieved, given the risks outlined above, the low probability of high yields from Equity Sharing or the acquisition of Royalties and a not insignificant number of expenditure sources (including support overheads) we would find it difficult to accept that the Fund would be sustainable or self-replenishing.

Opportunity Cost

- 5.8 It is widely recognised that the time value of money should be represented by the opportunity cost of capital. Outwith interest generated from Loans, it is understood that the JIF will earn interest on the overall remaining fund balance through normal States of Jersey Treasury Management investment practice. Given that the overall £5m set aside as the JIF would inevitably attract a standard level of “investment” interest as part of the States of Jersey's overall investment strategy for funds, there is an opportunity cost in lost interest (differential in interest on the overall £5 and the average balance of the JIF in operation) arising from the establishment and

operation of the JIF. We do not see any recognition of this position within the Report supporting the Proposition.

Annual Operating Cost Estimate and Outcomes

- 5.9 Given the issues highlighted above we would strongly recommend that a best estimate of annual operating costs for the management of the JIF including all overhead support (external and internal costs) is determined. We would also recommend that an assessment is undertaken of this estimated annual cost of operating the Fund against a measure of deliverables/outcomes arising from the utilisation of the Fund. Transparency on this exercise will effectively provide an indication of the true utility of the JIF.

6. International Comparators

- 6.1 In bringing context to the rationale for the introduction of an Innovation Fund for Jersey international comparisons were drawn within the Report on the Establishment, Funding and operation of the Jersey Innovation Fund. Such examples are outlined in Appendix 2 of that Report – Examples of Innovation Funds.

Successful Innovation Funds

- 6.2 The Operational Terms of Reference dated September that accompany the Proposition report as Appendix 1 outlines successful examples of innovation funds – “UK, Malta and Singapore are three good examples where government funds have, with significant success, been used to boost innovation. Whilst there are some common features, each jurisdiction has a unique operating model, eligibility and assessment criteria designed to support the specific priorities and objectives of the jurisdiction.” Indeed the Appendix highlights three typical types of Innovation Fund as follows:-

“3.1 The Fund of Fund

A Government Fund managed by public sector fund managers who make strategic investments in a number of established private sector Venture Capital funds. The Government funding is directed towards Venture Capital funds that are of strategic importance; for example technologies or renewable energies. Coupled with private sector funding these privately managed funds invest in private sector businesses. All investments are equity finance arrangements where a share in the company is taken in return for the investment. The returns on any Government investments are linked to the overall performance of the venture capital fund and not linked to any one specific organisation.

3.2. The Partnership Fund

A Government managed fund that invites private sector venture capital fund managers to submit applications for co-funding to increase the availability of risk capital for early-stage and high-growth companies. Government does not own any equity in the private enterprises; this is retained by the venture capital organisation. Returns on any investments are linked to either the overall performance of the venture capital fund or a specific organisation.

3.3 The Government Fund

A fund that provides financial support in the form of repayable loans and/or non repayable grants direct into a private sector enterprise. The fund is normally managed by an independent Board with members from both the public and private sector. The returns made on loans are linked to combination of arrangement fees, interest rates and special clauses allowing it to benefit from any increases in value, sales growth, or the licensing of any intellectual property.

- 6.3 The Operational Terms proposes that “... the JIF will launch and initially operate as a Government Fund (see 3.3 above) making available financial support in the form of repayable loans or non-repayable grants.” Because of the constraining prevailing legislative framework through the Public Finances (Jersey) Law 2005 it is further noted that an ambition to extend the scope of the Fund to making Equity Investments in private businesses would require legislative. This ambition being based on the premise that would allow the JIF to realise enhanced returns if the business were to be successful and/or sold for significant gain.” Whilst the Operational Terms proposes a Fund run along the mines of a Government Fund, at the Panel Meeting of 22 February 2013 with the Minister for Economic Development that sustainability of the Fund could not be maintained under this model and that Joint Funding and Equity Investment could only allow the potential for a self-replenishing model to succeed.

Innovation Fund Comparability

- 6.4 We have looked at a number of countries which were used in Appendix 2 of the Report as well as Singapore - who operate “Innovation Funds” – Malta, UK, Ireland, Israel and Singapore. We would be of the view that none of these examples are truly aligned to the proposed Government Fund Model highlighted within the Operational Terms – this point is conceded in the assertion that “each jurisdiction has a unique operating model, eligibility and assessment criteria designed to support the specific priorities and objectives of the jurisdiction.”
- 6.5 Having carefully looked at Malta, UK, Ireland, Israel and Singapore - comparisons are probably only most relevant with condition operating in Israel and even there operating conditions do not invite favourable comparison with the operating context and conditions on Jersey – effectively comparing “apples with pears.” Most of the Countries we have looked at operate an Innovation Strategy and Funding at a macro level and delegated to an Economic Enterprise Agency to administer primarily within the sole focus of promoting economic growth. The administration of this support is well embedded within government infrastructure typically discharged by specialist agencies across these countries which in itself is focussed on systematic macro-economic development and regeneration.
- 6.6 Such arrangements are invariably designed to attract significant inward investment primarily focussed on global markets with a large number of assistance strategies outwith Loans, Grants and Equity sharing. Intensive assistance can include

Consultancy Support, Property Provision and relocation, locational support, Business Rates abatement, Tax incentives, direct grant funding of new employees and Marketing assistance. It is interesting to note that in respect of the UK, Ireland and Malta some regional economic support is funded in part through the EU by way of European Regional Development Funding (ERDF) Assistance and channelled through the central and local government infrastructure of these respective countries.

- 6.7 Interestingly, even within these countries external commentators have highlighted the difficulties in demonstrating tangible outcomes for such investment.

UK - UKIIF

- 6.8 The UK Innovation Investment Fund (UKIIF) was launched in 2009 by the Department of Innovation Universities and Skills – later reorganised as business Innovation and Skills. The Fund was designed to capture match funding and was initially regarded as being unsuccessful with only limited private sector funding being raised. The initial investment of some £150 with expectations of leveraging additional funding to top £1 billion have not been realised. In its early stages the UKIIF was managed by the European Investment Fund, which itself was owned by the European Investment Bank and the European Commission. It matched the UK government’s initial £100 million contribution to the fund. Some of the latest data available from a research carried out by Middlesex University last June (2012) highlight a number of interesting facts surrounding this fund:-

Table 1 UKIIF equity finance received by funding round

Finance (£m)/Funding Round	First	Second	Third	Total
Total Project Cost	83.3	6.5	6.6	96.3
UKIIF received	38	4.3	3.3	45.7
Average UKIIF	2.9	1.4	1.7	2.9
Median UKIIF	2.6	0.8	1.7	2.4
Other VC finance	14.4	2.1	0.8	17.3
Other external equity (angels/bonds)	16.9	0	1	17.9
Internal equity (founders/employees)	3.8	0	0	3.8
Mezzanine and loan finance	8.3	0	0	8.3
Total other finance raised	43.5	2.1	1.8	47.4
% of UKIIF to project cost	46%	67%	50%	47%
% of UKIIF to total finance raised	47%	67%	65%	49%
Number of business cases	13	3	2	16

Table 2 – UKIIF Reasons for seeking further external finance

Reasons for further finance	Number	% (n=16)
Export market development	5	33%
Later stage R&D	2	12%
Corporate finance from user groups	1	6%
To build final machines	1	6%
Undertake clinical trials	1	6%
Service application	1	6%
Plant acquisition	1	6%
No need	4	25%

Table 3 - UKIIF: Ability to raise other investment, if no UKIIF

Definitely not	1 (6%)
Probably not	0 (0%)
No strong opinion	0 (0%)
Probably yes	4 (25%)
Definitely yes	11 (69%)
Definitely not	1 (6%)

UK – Regional Growth Fund (RGF)

- 6.9 Regional Aid is administered by BIS for England with the devolved administrations such as the Scottish Government through Scottish Enterprise, Welsh Assembly Government and Northern Ireland Assembly having operational responsibility for the administration of Regional Growth Funding – typically underpinned by European Regional Development Funding.
- 6.10 The latest qualifying criteria issued by the Department of Business Innovation and Skills (BIS) for English applicants included the following:-

The Regional Growth Fund will provide a mixture of direct support for private sector investments and private public partnerships. All projects should lever private sector investment for long term growth and private sector employment. The criteria for RGFasks bids to show that they would:

- create additional sustainable private sector growth
- rebalance the economy in those areas currently dependent on the public sector
- not otherwise go ahead without support from the Regional Growth Fund
- offer value for money
- be State Aid compliant

Singapore

- 6.11 Complex use of match funding – Appendix 2 is an extract from the Singapore Government’s Assistance Programme’s for SMEs. As can be seen from the different components of aid on offer, the assistance is more aligned to state economic regeneration with a mix of support options being made available – finance being a modest component.

Malta

- 6.12 Some co-financing re ERDF – European Regional Development Funding from the EC – indeed ERDF funding is at the core for underpinning Innovation Fund activity - “The EU Structural Funds, particularly ERDF, which are managed by PPCD are central both strategically and financially for the innovation policy-mix in Malta and represent the principal source of funding for innovation activities in Malta, while contributing to creating a coherent policy structure in this area.”

Israel

- 6.13 The Tmura is the Israeli Public Service Venture Fund initially founded in 2002 to increase the involvement of the high-tech community in non-profit activity in Israel, with a focus on education and other youth related initiatives. Tmura receives donations of equity stock and stock options and reallocates these to “worthy non-profit making causes in Israel. Typically Tmura asks the earliest-stage start-ups to donate 0.5% of their equity and later-stage companies to donate 0.1% to 0.5%. Tmura also generates additional funding for the community by operating matching grants programs and managing corporate foundations. In respect of the Tmura R&D Fund administered by the Chief Scientist – an outline of the Fund is illustrated as Appendix 3 of this Report.

Ireland – Innovation Fund Ireland

- 6.14 Innovation Fund Ireland is an excellent example of a Partnership fund. it was launched in September 2010, administered by Enterprise Ireland and is a key component of the National Recovery Plan 2011-2014 for Ireland. Through this initiative, the Irish Government made available €125 million for Enterprise Ireland to invest in international venture capital funds that establish a presence in Ireland and that invest, at a minimum, an equivalent amount in Irish companies or companies with a significant presence in Ireland.
- 6.15 To be considered for funding under the Innovation Fund Ireland support measure, venture capital companies must demonstrate:-
- An established global profile and network with a reputation for market leadership in venture capital investment;
 - A proven track record of raising funds and generating superior returns for investors;

- A capacity to access high potential international investment opportunities with an investment team capable of attracting world-class entrepreneurs;
- An intention to establish a new and significant presence in the venture capital market

International Comparisons

6.16 Whilst there is much that can be learned from the operation of Innovation Funds across the world it is important that the objectives and operating context aligned to each Fund is fully appreciated. Aspects of the funds operated in the UK and Israel have some similar attributes to the JIF although the key differences on the extent of venture capital fund matching remain. Indeed, differences in operating environment, primary objectives and underpinning funding make true comparisons difficult. We would agree that the closest Fund type to the proposed JIF is a Government Fund as outlined within the Report on the Establishment, Funding and Operation of the JIF. However, the example given of Israel should be taken with some caution given the differentials in state expansionary objectives and operating environment. At the Panel Meeting with the Minister for Economic Development on 22 February 2013 it was clear that aspirations on match funding and equity will invariably move the positioning on fund type towards a Partnership Fund type.

7. Evolving Policy Framework

- 7.1 The issuing of the Innovation Fund Policy Framework has provided much valuable additional information on the proposed operation of the JIF. A number of critical process issues as well as roles and responsibilities have been clarified although, as we have pointed out within section 3 of this report, the issue of the status of the Innovation Policy Framework itself requires to be clarified in the context of whether it is prescriptive or merely guidance.

Consistency and Stakeholder Expectations

- 7.2 Some evolving aspects of the Policy Framework are not fully consistent with the original stated aims of the JIF or pronouncements made by Ministers in meetings with the Economic Affairs Scrutiny Panel.
- 7.3 In relation to the report supporting the proposition – Establishment, Funding and Operation of the Jersey Innovation Fund, the introduction sets the scene with the *“aim of the Fund is to support innovation and it will be available to support a wide range of activity from direct business support to strategic infrastructure investments, in the private, public and third sectors.”* Given the level of diversity implied by this statement it is difficult to envisage how such an aim could be achieved if the qualifying applicant must be a corporate body incorporated in Jersey, operating within a high value sector – with value added per employees being significantly in excess of £65k.
- 7.4 A series of meetings were hosted by the Economic Affairs Scrutiny panel and key stakeholders such as Digital Jersey, Jersey Business and Jersey Chamber of Commerce. A review of the transcripts of each meeting revealed a number of common aspirations for the fund including legitimate expectations on risk and a number of key sectors which could leverage significant potential from the utilisation of the Fund.
- 7.5 The Innovation Fund Policy Framework highlights key qualifying criteria for Loan and Grant Applicants which clearly diverge from stakeholder expectations. For example, stakeholders were critical of the position of the fund being “Lender of Last Resort”, yet the Innovation Fund Policy Framework clearly outlines this position. The determination of what would constitute “High Value” sectors was considered by Stakeholders to be difficult and diversity of sector including Tourism could/should be actively considered.

A ‘Work In Progress’

- 7.6 During the latest aspect of our work it has become apparent that key parameters associated with the purpose and administrative management of the fund are still evolving. In many respects, evidence collected suggested that key management processes are a “work in progress” and that there is still much to do between the

Economic Development Department and the Treasury to crystallise a final working framework for the administration of the Jersey Innovation Fund.

Panel Meeting with the Minister for Economic Development - 22 February

- 7.7 This meeting with the Minister for Economic Development and the Chief Executive Officer for EDD illuminated the following issues relative to an evolving position on the setting up and management of the JIF:-
- That there is significant doubt on the validity of the detail as contained within Innovation Fund Policy Document and related Application Fund;
 - That the restrictions outlined within the Innovation policy Framework and related Application Form on applicants being Limited Company format only had been removed with all Business Legal Entity structures being eligible for assistance;
 - That the proposed JIF Executive Post was no longer to be recruited and that the post would be purely administrative in nature with scope only for effecting a co-ordinating role for the JIF Board;
 - The JIF Board will be a “Working Board rather than a Review Board” meeting regularly (once per month) and solely arriving at judgements on the merits of Applications – no Officer recommendation or Judgements are within scope;
 - A new role for Jersey Business and Digital Jersey as Mentors for aftercare and advisers to the JIF Board in relation to Performance Management
 - That members of Jersey Business and Digital Jersey may be nominees within new Equity Stake Board arrangements; and
 - Law Officers have yet to provide views on Royalty Agreements or the legislative changes required in order to operate Equity Stake holdings.
- 7.8 Outwith the above issues, the Panel were advised that much of the detail behind the management of the scheme will be delegated to the JIF Board. States Members are being asked to vote on the following Proposition:-

PROPOSITION

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

to refer to their Act dated 17th July 2012 in which they approved the Economic Growth and Diversification Strategy which, *inter alia*, proposed the establishment of an Innovation Fund, and -

- a) to approve, in accordance with the provisions of Article 3(3)(a) of the Public Finances (Jersey) Law 2005, the establishment of a special Fund to be known as the “ Jersey Innovation Fund” ;
- b) to agree, in accordance with the provisions of Article 2(4) of the Public Finances (Transitional Arrangements) (Jersey) Order 2011, to amend the expenditure approval for 2012 approved by the States on 14th September 2011 in respect of the Economic Development Department head of expenditure to permit the withdrawal of an additional £5,000,000 from the Consolidated Fund to finance the creation of this new special fund;
- c) to agree that the Jersey Innovation Fund should be operated and used in accordance with the Operational Terms of Reference set out in the Appendix, under the supervision of an independent Innovation Board to be established by the Minister for Economic Development through a process overseen by the Appointments Commission and following the commission’s code on appointments to public bodies.
- d) to agree that any loans or grants made from the Jersey Innovation Fund will be authorised by the Minister for Economic Development.

7.9 Given the expectations on the delegation of the detail to the JIF Board and the level of fluidity/lack of clarity on the detail relative to the Operational Terms of Reference highlighted in section c of the Proposition above, it would be of the considered opinion that any clear definitions on the detail of the scheme have been further obscured as a result of the Panel Meeting responses received at the meeting of 22 February 2013. In terms of transparency it would be our recommendation that clarity on the detail surrounding the scheme is achieved before Members are asked to vote on the Proposition.

8. Concluding Comments

8.1 The creation of the Jersey Innovation Fund is a bold and very positive step towards encouraging economic growth through the promotion of specific innovation related activity. We fully recognise that in promoting and managing such objectives there is a difficult balance of competing objectives to maintain. Within the Proposition for the establishment of the JIF and associated background information there is much to commend particularly in the desire to:-

- Targeting ventures that are most likely to succeed in relative terms;
- Ability to look beyond commercial terms to broader economic impacts;
- Setting a relatively high level of maximum Loan facility for a single applicant relative to the overall Fund- £500k to £5m;
- Creation of robust Business Case testing requirements including counterfactual positioning;
- Optimisation of any resulting benefit from the investment;
- Flexible in the approaches taken to Funding within parameters;
- Minimise bureaucracy – with a rapid turnaround; and
- Utilise key private sector business skills within the establishment of a Private Sector led JIF Board;

Further Development Challenges

8.2 Notwithstanding the advent of the Innovation Fund Policy Framework it would be our considered opinion that more clarity is needed on a number of key issues including:-

- A clear position/view on what successful venture would look like – the quantification of success;
- Clarification on the extent of delegated authority and discretion to be provided to the JIF Board for the management of the Fund;
- Clarity on the status of the Innovation Fund Policy Framework – an elimination of apparent inconsistencies between documents;
- Precision on the key support parameters;
- Clarification on Fund being final resort status;
- Clarity on actual Officer Support that will be provided to the JIF Board – for example what are the exact resources earmarked for JIF Support role and what will the consequences be for the activities that are currently being serviced by such current resources? Essentially the opportunity cost of moving resources;
- An accurate assessment of the total annual costs of running/operating the fund including all Management and overhead as well as external support including externalised legislative drafting;
- An assessment of the overall cost of running the Fund against expected Benefits/Outcomes;
- An assessment of the Opportunity Cost of running the JIF relative to standard investment;

- All outstanding Legal issues including opinion of the Law Officers on the legality of the proposals and available options, the management of Royalties and Equity Investments be fully examined and resolved including potential interventionist strategies as well as potential Equity exposure issues; and
- Resolution of differing Stakeholder expectations through closer working.

Developing a Collaborative Approach

- 8.3 It is clear that a lot is expected from the JIF Board in a number of areas within its scope including the Approval Recommendation and on-going management of the Fund. Intuitively the operating arrangements and framework for the Fund appear to be necessarily complex and highly resourced relative to the potential number of successful applicants that may be supported – 4/5 per annum. Given that key stakeholders such as Jersey Business, Digital Jersey and the Jersey Chamber of Commerce already possess access to significant sector skills and business intelligence, it would appear appropriate to consider the potential for closer collaborative involvement in the management arrangements for the Fund. Such involvement could potentially range from provision of complimentary resources to the JIF Board as now envisaged to, at the other end of the scale, carrying out support currently envisaged or Process mapped for EDD staff. We note that at the Panel Meeting of 22 February 2013 with the Minister of Economic Development that there is now an enhanced role for Jersey Business and Digital Jersey in respect of mentoring and performance management post awarding of support. Whilst such additional collaboration is to be welcomed, we are not entirely convinced that such bodies were aware of these expected roles relative to relevant transcripts from previous meetings.

Concluding Remarks

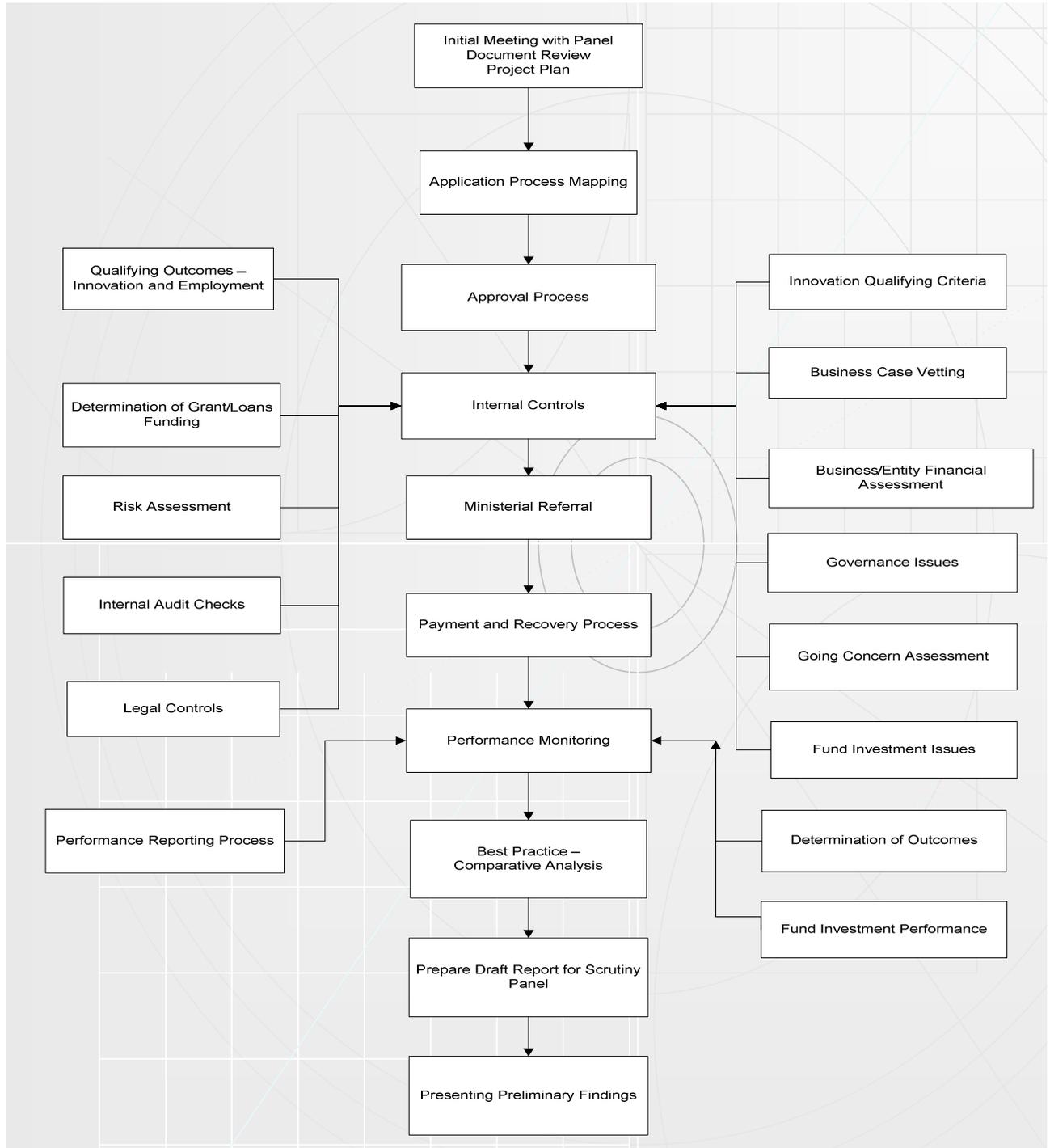
- 8.4 Having carefully considered all the material made available to us we would be of the opinion that there is considerably less clarity on the detailed management arrangements for the Jersey Innovation Fund than we would expect and indeed, less than other Public Fund Management arrangements we have seen. Implied delegation on the detailed aspects of these arrangements to a newly formed JIF Board without clear terms of reference invites significant risk.
- 8.5 At present there is a significant lack of precision on the arrangements for managing the Fund and the continuing evolving position on the management arrangements does not provide needed assurance on the critical aspects of governance and internal control required by acknowledged good practice in the stewardship of public funds. Notwithstanding this position the direction of travel taken by the States of Jersey in subjecting the management arrangements for the establishment of the Jersey Innovation Fund to scrutiny is undoubtedly the right one in the quest to establishment a robust framework for the operation of an Innovation Fund. A robust framework properly seeks to achieve the difficult balancing of the requirements for the appropriate stewardship of public money with the creation of a dynamic catalyst for meaningful economic opportunity and growth from the potential synergies of

seed fund investment. Such an approach is highly commendable and does provide a 'golden' opportunity to further harness, through collaborative working, the best attributes of both Private and Public Sectors.

- 8.6 CIPFA would like to take this opportunity to record our sincere gratitude to the members of staff at the States of Jersey who have provided extremely valuable support in the course of our work.

REVIEW METHODOLOGY

APPENDIX 1



SINGAPORE GOVERNMENT ASSISTANCE PROGRAMME FOR SMES

APPENDIX 2

Starting Up	Angel Investors Tax Deduction Scheme (AITD)	A tax incentive for business angels to invest in local startups	6
	Business Angel Scheme (BAS)	Co-invests with business angels in local early-stage companies with innovative products and/or services, for up to \$1.5 million	8
	Biomedical Sciences Accelerator (BSA)	Co-invests with pre-approved accelerator operators in local medtech startups, for up to \$4 million	10
	Work Pass for Foreign Entrepreneurs (Entrepass)	An employment pass for foreign entrepreneurs to relocate and start a business in Singapore	11
	Incubator Development Programme (IDP)	Co-funds incubators and venture accelerators to mentor and develop local startups	12
	SPRING Startup Enterprise Development Scheme (SPRING SEEDS)	Co-invests with third-party investors in local startups with innovative products and/or services, for up to \$1 million	14
	Technology Enterprise Commercialisation Scheme (TECS)	Co-funds early-stage companies to develop and commercialise innovative technology ideas	16
	Action Community for Entrepreneurship Startups (ACE Startups)	Provides funding of up to \$50,000 to entrepreneurial Singaporeans who want to start their first business	18
Building Capabilities	People		
	Management Associate Partnership (MAP)	Co-funds the training of local graduates with less than three years of working experience	22
	Enterprise Internship Programme (EIP)	Co-funds the engagement of interns from polytechnics and universities	23
	Management Development Scholarship (MDS)	Co-funds MBAs, part-time degrees and executive programmes for young executives	24
	Advanced Management Programme (AMP)	Co-funds executive programmes and EMBA for business owners and senior management	25
	Business Advisors Programme (BAP)	Co-funds the engagement of Business Advisors as qualified professionals to SME projects	27
	HR Capability Programme – Consultancy Support	Co-funds consultancy services for SMEs to customise the HR Capability Package to their needs	28
	Intellectual Property Management Programme (IPM)	Co-funds consultancy fees and project implementation for SMEs to protect and manage their intellectual property	29

Building Capabilities	Service		
	Customer-Centric Initiative (CCI)	Co-funds local companies to upgrade their service	30
	Innovation		
	Innovation and Capability Voucher (ICV) ^{New}	A \$5,000 voucher to help SMEs upgrade their business in Innovation, Productivity, Human Resources and Financial Management	31
	Technology Innovation Programme (TIP)	Co-funds technology projects which lead to new products or processes	32
	Design Engage Programme	Co-funds the integration of design strategies into business processes	34
	BrandPact	Co-funds and provides resources for local companies to build their brand	35
	Productivity		
	QQuality for Enterprises through Standards (QUEST) Programme	Co-funds the adoption of standards for increased productivity in new emerging areas	36
	Integrated Management of Productivity Activities (IMPACT)	A framework for SMEs to assess how productive they are and identify key improvement areas	37
	Productivity@Work	A dedicated online resource on how to improve productivity for SMEs	39
	Productivity Management Programme (PMP)	Provides advisory services, workshops, and clinics to help SMEs improve productivity	40
	SME Management for Action Results Initiative (SMART)	Helps SMEs develop a capability roadmap to strengthen their management systems and processes	41
Financing Schemes	Loan Insurance Scheme (LIS)	Provides insurance for short term trade financing and working capital loans	44
	Local Enterprise Finance Scheme (LEFS)	Provides factory or machinery loans for business upgrading and expansion	46
	Micro Loan Programme (MLP)	Provides working capital, factory or machinery loans for micro businesses	47
DIY Toolkits	Financial Management Toolkit	An online guide to help SMEs improve their financial management capabilities	50
	HR Capability Toolkit	An online guide to help SMEs improve their HR capabilities	51
	Interactive Customer Service Toolkit	An online guide for SMEs in service-related sectors to help them raise their service standards	53
	Marketing Toolkit	An online guide to help SMEs enhance their marketing effectiveness with and cost-effective techniques	54

TMURA – R&D INNOVATION FUND

APPENDIX 3

Tmura R&D Fund

ExpandAll | CollapseAll

Keywords	competitive R&D R&D risk sharing
Overview	<p>The R&D Fund is the main vehicle used by the Office of the Chief Scientist in the Ministry of Industry, Trade and Labour to support innovation in Israeli companies. Support for the R&D fund is based on A: an outright grant based either on the merits of the project or its relative importance to Israeli industry and B : a grant which companies have to repay in the form of royalties if the project succeeds. The maximum grant allowable in this programme is 50% of the total government support package. Royalties from successful projects form a significant part of the R&D Fund budget.</p> <p>The R&D Fund is a general framework. It approves general requests for support from all companies -- start-ups, SMEs, and larger established firms. Its decision-making body is the R&D Committee, which also makes funding decisions for other frameworks such as new firms in the incubator system and sectoral programmes such as traditional industries, biotechnology or water programmes. The role of the fund itself is in governance of the grant approval service, starting from the screening process, ensuring adherence to reporting requirements for those firms whose requests are approved, and post grant auditing to ensure repayment of success based royalties to those firms whose projects succeed and whose grants terms require payment of royalties.</p>
Background and rationale	<p>The R&D Fund was created to reduce risk in industrial innovation. This framework, with its systematic evaluation of projects by experts recruited from inside industry, has played a major part in Israeli successes in ICT innovation. The fund is export oriented and each project was traditionally judged on its own merits, if it answered the basic criteria of creating products or services that were ahead of world markets and if the firm could demonstrate that there was a market for the proposed innovation. In recent years, however, the focus has changed to a certain degree with the fund allowing for sectoral bias in fields such as biotechnology. The fund is also used to give grants for the measure "Encouraging R&D for Developing Competitive Advantages in Traditional Industries." In the latter case firms do not have to prove world wide innovation, and are allowed grants even to purchase technologies or to improve their offerings to the local market.</p>
Policy Priorities	<p>The R&D Fund supports innovation in all Israeli firms regardless of the companies size or age from the smallest start-ups to large and established firms</p> <p>Main Policy Priorities 2.3.1 Direct support of business R&D (grants and loans)</p> <p>Other Policy Priorities 2.3.1 Direct support of business R&D (grants and loans) 4.3.1 Support to innovative start-ups incl. gazelles</p>
Targeting specific sectors	0. No specific sector

Targeted research and technology fields	By law, the R&D Fund has no thematic focus. In recent years it has been used, however, to encourage innovation in specific fields such as biotechnology, nanotechnology, water industries and traditional industries.
Selected research and technology fields	No specific thematic focus
Start date	Before 1990
Expected ending	No end date planned
Relationship to other measures	Novel measure: Yes
If the measure is novel was it mainly:	Inspired by national policy debate
Geographic coverage	All of Israel
Targets or beneficiaries of the measure.	All companies All companies Technology and innovation centres (non-profit)
If more than one target group is eligible	Co-operation/networking optional (e.g. associating SMEs as users)
Overall implementation structure of the measure	Some smaller firms can submit requests throughout the year. Larger firms can apply once a year. The proposals are screened by a receiving unit, and those that pass the first hurdle are given to freelance referees, most of whom are recruited from industry. In larger grant requests two referees can be assigned. These evaluators examine the requests and also visit the firm. In some cases there is also a financial screening stage. Their recommendations are then given to the official inside the OCS in charge of the specific industry who attaches her recommendations to the Research Committee, which decides a) whether to approve the proposal and b) what percentage of the total R&D project will be funded by the government.
Management structure	The deciding body is the research committee. Under it are the officials in charge of certain industrial fields, those in charge of freelance evaluators and those in charge of finance, including receipts of royalties.
Review of progress	In most cases quarterly reports are required as well as end of year reports.
Selection criteria	

	<ol style="list-style-type: none"> 1. The project will lead to an innovative product or service 2. It has a 12-month development plan (in most cases) 3. The company agrees to IP limitations imposed by the programme. 4. The company has the human and financial resources to complete the programme 5. The project receives approval from the OCS referee 6. The company agrees to pay royalties
Openness to EU countries	No
Openness to third countries	No
Selection process of projects / participants	<p>Selection is based on:</p> <ol style="list-style-type: none"> 1. The company fills out a detailed form 2. The company is visited by an ICS referee 3. The grant request is approved by the R&D Committee
What State Aid framework is applied to the measure?	OCS budget
ModeOfFunding	<p>Grants</p> <p>Other: The grants are conditional. In most cases, if the project succeeds companies are obliged to pay back the grants gradually in the form of royalties.</p>
Elegible costs	<p>Labour costs (including overheads)</p> <p>Equipment</p> <p>External expertise (consultants, studies, etc.)</p> <p>Other: Materials##OTHERMaterials</p>
Sources of co-financing	Co-financed by the private sector
Overall budget in EUR	€304m
Exchange rate used (1 EUR = # in national	€1=5NIS

currency):	
Overall budget in national currency:	1,009,000,000
Years:	2008 €183m. 2008 €183m. 2010 €304m.
Further information	The exact amounts available for the fund are not budgeted separately and tend to change every year.
Indicators specified ex ante	No
Support Measure evaluation	Ex-Ante: No On-going/Mid-term: Yes Final/Ex-post: No
If the programme was evaluated, what were the main findings?	The programme was assessed by an in-depth study commissioned from an economic consultancy. The main findings of the study were:1. The effect of government support for industrial R&D -- the study finds a highly positive rate of 1.28, meaning that a government investment of NIS 1m. causes firms to invest another NIS1.28m. -- meaning that the economy gains NIS2.28m. Invested in industrial R&D that would have not be invested without government intervention.2. The level of spillover effects -- the economic effects of government investment in R&D -- on average are between 5 and 6 times the amount of money invested by the government, depending on the size of firm and its specialization..
If no official evaluation has been undertaken is there any evidence which allows an appraisal of the success of the measure?	See section 4.3
Results	See section 4.3
Website in original language	Website

Website in English	http://www.tamas.gov.il/CmsTamat/Rsrc/MadaanEnglish/MadaanEnglish.html
Legal basis	1984 Law for Industrial R&D
Launching Agency	OCS
Agency administering	OCS
Funding Agency	OCS
Manager(s) responsible for the measure	Avi Hasson, Chief Scientist, Ministry of Industry and Trade

APPENDIX 3: DRAFT JIF APPLICATION FORM

JERSEY INNOVATION APPLICATION FORM

- **This completed form must be returned at least 6 weeks days before any support is required.**
- **This form can be completed by both start up, established businesses and collaborative partnership**
- **Applications for projects already started will only be considered in exceptional circumstance.**
- **The information proved is critical to the assessment of your application. Make sure you provide everything that is requested.**

Jersey Innovation Fund (JIF) Eligibility Guidelines

An Applicant shall be eligible if the Applicant:

- has no available Collateral to secure finance from other sources
- clearly demonstrates that without the JIF support the project will not proceed;
- is a Business incorporated under the Companies (Jersey) Law 1991;
- has supplied all information requested;
- has obtained the required business licence in accordance with the Regulation of Undertaking Law;
- is a businesses or a project that is or will operate in a High Value Sector;
- can demonstrate the investment into the project of business has potential to improve the overall level of productivity of the economy – i.e. those firms with value added per employee significantly in excess of £65k;

The Application shall be eligible if

- the applicant is a high growth business.
- the amount requested does not exceed £500,000;
- the amount requested is greater than £20,000
- the initial drawdown for the Project is made within 6 months of the support being approved
- the application is for a Loan Facility in sterling;
- the project will be delivered within the Bailiwick of Jersey;
- the applicant signs a Royalty Agreement as determined by the States of Jersey. .

Eligible costs for an Application can include:

- equipment (purchase or rental)
- facilities or systems, includes property costs;
- project implementation costs including reasonable consultant fees but excludes all in-kind labour costs;
- purchase of assets
- professional fees
- research and development costs

Applicant's details

PLEASE WRITE IN CAPITALS AND COMPLETE ALL SECTIONS

Name of business (as registered under Part II of the Regulation of Undertakings and Development (Jersey) Law 1973):
.....

RUDL Licence No: Date business started trading:
.....

Business Contact:
Title: Mr/Mrs/Miss/Ms

Position within *Please circle most appropriate)* Business:
.....

Business Address:
.....
..... Postcode:
.....

Telephone No (Business): Fax No:
.....

Mobile No: Email:
.....

Sector.....

Country ownership of business (Local / Non-Local / Mixed- provide full details).....

Subsidiary / part of a group/partnership project provide full details.....
.....
.....

If subsidy please provide full details of parent company:.....
.....

Collaborative Partnership *(please provide details of all partners)*
.....
.....

Directors Details

How long has the company been trading?

How long has the parent company been trading?

Please send, with this signed application form, a written report and supporting documentation that covers all of the following 15 points.

1) An Executive Summary of the project that clearly explains how it will deliver some or all of the following:

- A competitive advantage for Jersey,
- Attract additional private sector investment
- Develop new high value businesses
- Created significant new job opportunities in high value sectors for local job seekers
- Diversify the local economy

2) Description of the Project that includes as a minimum

- The new products/services- The 'Innovation'
- A detailed breakdown of the total project costs
- Timescales, provide a detailed project plan
- The rationale for the project
- What alternatives have been considered to the Project
- How mobile is the project, specifically why Jersey?
- How is the project going to be managed

3) Counterfactual - what happens if the financial support from the Jersey Innovation Fund is not available

4) Market assessment

- Will the project have a local, national or international market?
- What size are the potential markets, (define with evidence)
- The market share, as a percentage, the project will/could achieve
- Provide details on competitors or competitive products – Both local and non-local
- Provide an analysis of the identified market opportunity
- Provide details of the applicants or teams knowledge of the potential markets

5) Innovation

6) Employment impacts

- Provide details of all existing employment in the organisation or collaborative partnership - Number of full time employees, roles, and wage costs.
- Provide details of each new jobs that will be created as a result of the project. Number of full time employees, roles and wage costs.
- Will there be any employment displacement concerns relating to the project/ If yes, define.

7) Experience, skills and training

- Provide detailed CV's of the key personal directing/managing the project. Include specific information on experiences, /skills, qualifications which are critical to the success of this project.
- Provide details of the type and level of any training required to deliver the project (Level of training (e.g. NVQ Level Accredited / non-accredited)
- Clearly explain how any identified training will be delivered (training, training provider, employment of specific skilled persons)

8) Knowledge transfer

- Describe any proposed collaboration or partnership opportunities or knowledge basis
- Describe any knowledge transfers to the local markets
- Describe any opportunities to develop clusters around the innovation

9) Supply chain impact

- Provide details of the supply chain spend, source, local, non-local and type of products
- Describe if any what impacts the project may have on the local supply chain

10) Business Plan

- Supply a 3-5 year Business Plan which includes the key strategic and operational factors required to deliver the project

11) Financial forecasts

- For all projects provide 5-10 year financial forecasts. This must include revenue and cost projections. (Profit & loss)
- Provide current and 5-10 year capital value forecast (Balance sheet)

12) Recent trading results. (For established business please provide)

- Copies of the last 3 years audited accounts of the applicant
- Copies of the last 3 years accounts if applicant is a subsidiary
- Copies of all the partners results if this is a Collaborative Partnership project

13) Assistance sought

- Amount and form- Loan or Grant?
- If grant- explain why the project is unable to operate using debt financing
- Over what term is the support requested- provide rationale

14) Alternative funding options

- What alternative funding option have been explored (value and lender)
- What funding options have been offered (value, lender)
- Evidence the funding gap which is required the project to proceed

15) Detail any wider economic benefits the project will deliver to Jersey

CONFIDENTIALITY/PRIVACY STATEMENT

The information you provide will be processed for economic purposes. To ensure confidentiality and privacy, all processing will be carried out under the requirements of the Data Protection (Jersey) Law 1987. This information may occasionally be disclosed and used outside of the Economic Development Department where it is considered to be in the business's best interest to do so. Should you require us to seek your individual consent to these disclosures please advise us in writing.

TO BE COMPLETED BY THE APPLICANT

I certify that the information provided on this registration form is true to the best of my knowledge and belief, and I provide the information knowing that I shall be liable to prosecution if I have stated anything I know to be false. I undertake to inform the Economic Development Department immediately of any change in circumstances which may affect this application. I understand that giving false information or withholding relevant information may lead to the recovery of any amounts paid by the Department.

Signature: Date:
.....

Name: Position within organisation:
.....

Upon completion of the activity you will be required to submit a completed claims form, together with all relevant supporting documentation to: , **Economic Development Department, Cyril le Marquand House, The Parade, St Helier Jersey The JE4 8UL**

FOR OFFICE USE

Checklist

1) An executive summary of the project that clearly explains how it will deliver some or all of the following	
2) Description of the project that includes as a minimum	
3) Counterfactual - what happens if the financial support from the Jersey Innovation Fund is not available	
4) Market assessment	
5) Innovation	
6) Employment impacts	
7) Experience, skills and training	
8) Knowledge transfer	
9) Supply chain impact	
10) Business Plan	
11) Financial projections	
12) Resent trading results	
13) Assistance sought	
14) Alternative funding options	
15) Detail any wider economic benefits the project will deliver to Jersey	

APPENDIX 4: DRAFT INNOVATION FUND POLICY FRAMEWORK

The Jersey Innovation Fund- Overview

The Jersey Innovation Fund (JIF), subject to States approval, will provide direct financial resources to encourage and support innovation. The fund will be capitalised with an initial £5 million with a promise from the Treasury Minister to add a further £5 million in 2013/14.

The Fund, once established, will award both loans and grants to encourage investment into innovation that will improve the Island's competitive advantage. Of the £5 million, it is anticipated the majority will be made available as loans with grants only issued in exceptional circumstances.

Innovation encompasses a wide range of activities from research and development to organisational change, training, testing, marketing and design resulting in products or services that are new to the market

For the avoidance of any doubt the Fund will not compete or replace private sector funding, only be used after all other sources of funding and security have been fully utilised, and be used to invest in innovative projects.

Policy Framework

This document is a Policy Framework, presenting a range of policies which will be used to guide; eligibility criteria; the application and assessment requirements; risk management; corporate governance and reporting requirements

The Policy Framework will also be used to help manage expectations by encouraging applications for projects that can clearly demonstrate that the investment in innovative will lead to high value-added activity and the creation of employment in businesses with high growth potential.

Policy Definitions

Applicant means the authorised representative of the Eligible Project in all matters related to any funds awarded through the Jersey Innovation Fund. The Applicant will be solely responsible for all project management responsibilities with respect to the Eligible Project.

Collaborative partner(s) means any subdivision, non profit entity, or for-profit entity that is identified as a partner in the Applicant's proposal for funding.

JIF Application Form means the current Economic Development Departments' Jersey Innovation Fund Application Form.

High Growth Business Defined as a business with the potential to double revenues or employment within four years and to employ at least ten full time equivalent staff by the end of the four year period.

Loan means an amount of money advanced from the Fund and due for repayment with interest within a specified period.

Loan Facility means a facility provided, or to be provided, from the Fund to an Applicant in accordance with the terms of a Loan Agreement.

Collateral means together any Security or Quasi-Security.

Eligible Business Activity means the Applicant is engaged in, or proposes to, engage in a Commercial Activity in Jersey resulting in the development of a new product or services.
'The Innovation '

Eligible Purpose means a purpose which is notified to the JIF Board by the Minister for Economic Development from time to time as being eligible for a Loan Facility.

Eligible Costs means cost of expenses agreed by the Minister for Economic Development.

Non-Loan Facility means any another financial assistance being provide to the organisation regardless of it use or link to the eligible project.

Repayment Period means the time from the date the Loan Agreement is signed and the last repayment of the Loan and any interest due.

High Value Sector means a sector with a value added per employee above £65,000.

Loan Facility Letter means a document signed by the JIF Board Chairman addressed to the Applicant confirming a Loan Facility.

JIF Board means the Board appointed by the Minister for Economic Development with management responsibility for reviewing applications, making recommendations to approve or reject applications, managing aftercare, producing reports, and all other corporate governance requirements.

Royalty Agreement means a legally binding agreement between the organisation and the States of Jersey. The agreement records the amount, how and when the organisation must pay royalties on all income including the sale, in part or whole, of the company and or any of it assets.

JIF Executive means an officer nominated by the Economic Development Department to provide support to applicants, the Board and the Ministers in all matters relating to the management of the Fund.

Initial Draw-down means the first percentage (or part) of an approved Loan Facility.

Final Draw-down mean the final percentage (or part) of an approved Loan Facility.

Interest means a fee calculated as a percentage of the Loan outstanding at the end of each calendar month.

Holiday Period means an agreement by the Minister for Economic Development to delay the repayment of a loan and interest due in respect of a Loan Facility.

Drawdown Notification means a letter sent to the Treasury Department confirming the value of every transfer of money from the Fund to the organisation.

Fund means the Jersey Innovation Fund.

Write-Offs mean an amount of a Loan and any interest due which the Board, Treasury, States of Jersey or its agents have been unable to recover from the Applicant.

Project means an initiative that has successful applied and been awarded a Loan Facility.

Key Staff mean personnel with skills or experiences which are critical to the successful implementation of an approved Project

Directors mean executives appointed to the Applicant's Board

Loan Assurance Statement means a template, signed by the Directors of the organisation receiving a loan, as determined by the States of Jersey.

Loan Agreement means a legally binding contract between the States of Jersey and the organisation awarded a Loan Facility.

Documentation means all documentation relating to the management of the Jersey Innovation Fund initiative

Loan Repayment means the organisation repaying both the loan and any interest due to the States of Jersey

Termination Date means the date the Loan Agreement is terminated.

The Policy Framework in the main refers to Loans with a specific section allocated to Grants.

LOANS

1. Eligibility policies

1.1 An Applicant shall only be eligible for a Loan Facility if the Applicant:

- has no available Collateral to secure the proposed Loan Facility or all Collateral as is available in respect of the Applicant has been fully exhausted in securing non Loan Facilities;
- is engaged or will be engaged in an Eligible Business Activity;
- clearly demonstrates that without the Loan Facility the project will not proceed, or at such a small scale that warrants support with a Loan Facility;
- has completed and signed a JIF Application Form (Appendix 1);
- is a Business incorporated under the Companies (Jersey) Law 1991;
- has supplied all information requested;
- has obtained the required business licence in accordance with the Regulation of Undertaking Law;
- is a businesses or a project that is or will operate in a High Value Sector;
- can demonstrate the investment into the project of business has potential to improve the overall level of productivity of the economy – i.e. those firms with value added per employee significantly in excess of £65k;
- is a high growth business.

1.2 The Application shall only be eligible for a Loan Facility if:

- it is to be utilised for an Eligible Purpose;
- the aggregate amount of the requested Loan Facility; and/or capable of being advanced to such Applicant under any other States of Jersey scheme is an amount which does not exceed £500,000;
- the requested Loan Facility is greater than £20,000
- the initial drawdown for the Project will be made later than six months after the date of the Loan Facility Letter;
- the application is for a Loan Facility in sterling;
- the project will be delivered within the Bailiwick of Jersey;
- the applicant signs a Royalty Agreement as determined by the States of Jersey. (Appendix 2).

1.3 Eligible cost on an Application includes:

- equipment purchase or rental;
- facilities or systems, includes property costs;
- project implementation costs including reasonable consultant fees but excludes all in-kind labour costs;
- purchase of assets
- professional fees
- research and development costs

2. Due diligence, Policies

2.1 Every Applicant must:

- complete and sign the JIF Application Form
- provide copies of the current Regulation of Undertaking business licence
- supply a copy of the company's Memorandum and Articles of Association
- for all collaborative applications supply copies of all partnership agreements

- provide details of all other sources of funding including copies of all agreements;
- disclose any debentures or securities taken or charges placed on the company;
- disclose full details of any guarantees provided by the Directors to secure Non-Loan Facility funding for the company and or project;
- disclose details of all shareholders and the residential address of each shareholder;
- supply a copy of the latest audited accounts (established business only)
- supply financial forecasts for a minimum of 3 years or the life of the project (if greater than 3 years)

2.2 All Applicants will be subject to financial background checks including credit rating, tax/social security and any Court judgments.

2.3 Applications made by two or more companies but be accompanied by copies of audited accounts for every partner.

2.4 Applications made by a subsidiary company must supply a copy of the parent company's accounts.

3. Assessment policies

- Every application will be subject to a full economic assessment;
- Economic assessments will be completed by the States of Jersey Economic Advisors Unit.
- The economic assessment will be presented as a written report to members of the JIF Board.
- The JIF Board may, or if requested to do so by the Economic Advisor or the Minister for Economic Development, commission experts to provide specialist technology, financial or legal advice.
- The JIF Board is responsible for assessing the applicant's business plan. Including its commercial viability; the market opportunity and its size; the competition if any; the capability and experience of the project team, and any identified or unidentified risks.

4. JIF Board Recommendation Policies

4.1 The JIF Board must only make a recommendation to the Minister for Economic Development to approve a Loan Facility if it is of the opinion that the:

- Applicant has a viable business proposition.
- Applicant will be able to meet its repayment obligations under the proposed Loan Facility.
- Applicant is unlikely to be successful using traditional Non-Loan Facility debt financing.
- Provision of debt financing to the Applicant is an appropriate means of financing. For the avoidance of doubt, where the provision of debt financing is only one of a number of elements of an overall financing package the JIF Board must be of the opinion, that the provision of a Loan Facility is an appropriate element of such financing package.
- Company receiving the Loan is able to meet its debts as they fall due and will not, as a consequence of entering into the proposed loan facility, cease to be able to meet its debts as they fall due;

- Economic assessment undertaken is positive and confirms the project will delivery a competitive advantage for Jersey, is of high value, and will result in the creation of high value jobs.

4.2 The JIF Board's recommendation, or not, to approve a Loan Facility must be in writing to the Minister for Economic Development and accompanied by a business case signed by the JIF Board Chairman the recommendation will include

- the amount of Loan Facility
- based on the information provide by the Treasury Department, shall recommend the interest rate for the Loan Facility
- Any holiday period for both the loan and interest repayments.
- Proposals for multiple draw downs subject to the final drawdown being no later than 12 months from the offer letter.
- Confirmation that the Applicant has a viable business proposition, or project that will deliver significant wider economic benefits to Jersey and new jobs in higher value sectors
- All information, clauses, terms and conditions attached to the Royalty Agreement.

5. Loan Offer and Notification Policies

5.1 If the Minister for Economic Development accepts the recommendation to approve a Loan Facility.

- The decision to approve a loan will be recorded by the signing of a Ministerial Decision
- The Board Chairman, subject to the above, will send a Loan Facility Letter to the applicant detailing the terms of the Loan, the Royalty Agreement, copies of all contracts, ongoing reporting requirements, and any other relevant information.
- Applicants shall have 28 Business Days from the date of such offer to accept the Loan Facility
- Offers of a Loan Facility will be subject to both the Loan Agreement and the Royalty Agreement being signed and returned to the JIF Executive Officer.

6. Loan Polices

- The minimum amount of Loan is £ 20,000
- The maximum amount of Loan is £500,000
- The maximum repayment period is 5 years
- The minimum repayment period is 12 months
- Initial draw-down of the Loan must be made within 6 months of the Loan Agreement and Royalty agreements being signed and returned to the JIF Executive Officer.
- Final draw-down must be within 12 months of the Loan and Royalty Agreements being signed.
- All Loans will be subject to an interest charge
- Interest rates will be fixed for the full term of the Loan
- Interest rates on all Loans will be set by the Treasury Department
- Holiday Repayment Period on Loan Facilities must be for no longer than 12 months after the initial draw down
- Interest rates will be calculated on the amount of capital outstanding at the end of each calendar month
- All applicants receiving a Loan will be required to enter into a Royalty Agreement

7. Notification of Initial drawdown

- As soon as reasonably practicable following the date of a Loan drawdown, but no later than the end of the tenth business day following such date, the JIF Executive shall notify the States Jersey Treasury Department of such drawdown by completing an Drawdown Notification.

8. Reporting Policies

8.1 The JIF Board will provide the Minister for Economic Development and the Treasurer to the States of Jersey with a written report no later than the 31st January and 30th July for every year the fund is in operation and whilst any Loan is still outstanding and remains unpaid. Each report as a minimum must include:

- a full financial statement on the income and expenditure of the Fund,
- a list of all approved Loans including information on repayment schedules,
- a report on all defaults- non repayments, repayment delays, loan restructuring or write-offs
- a progress report on every Project supported by a Loan
- details in any other changes in circumstance.

8.2 Every organisation in receipt of a Loan must provide quarterly progress reports. As a minimum each report must include

6. A progress report against the original Project plan noting all key milestones.
7. A financial analysis of spend and income compared with the original forecast
8. A progress report on all new innovation.
9. Details of any changes in Key Staff
10. Details on any change to the company's Board of Directors

8.3 All organisations in receipt of a Loan Facility must provide an annual Loan Assurance Statement to the JIF Executive Officer. Confirming how the Loan has been spent and the outcomes achieved in comparison with the original plans. (This requirement will be a condition of the Loan Agreement.) The Loan Assurance Statement must be signed by the Directors of the organisation and received by the JIF Executive Officer by the 31st March of the year following the signing of the Loan and Royalty Agreements.

9. Audit and provision of information

9.1 At such frequency and such times as the States of Jersey may from time to time determine, in its absolute discretion may conduct an audit of the JIF Fund

9.2 At such frequency and such times at the States of Jersey may from time to time determine, in its absolute discretion, conduct an audit or all or any approved Loans

9.3 The comptroller and Auditor General at his discretion can audit the JIF Fund.

10 Breaches and Remedies

10.1: Any Project breach, delay significant change, as determined by the States of Jersey, or the JIF Board, which is continuing unremedied and unwaived, then, if the States so requires, the JIF Board and the States shall meet with a view to agreeing what steps, if any, are to be taken by the JIF Board to remedy the relevant breach or to seek to prevent, or minimise the risk of, any possible re-occurrence of such breach. At the absolute discretion of the States of Jersey this can include the termination of the Loan Agreement

10.2 An information disclosure breach during the application process, as determined by the States, or by the JIF Board of any provision of any information that is deemed to be inaccurate or misleading in any way will result in any application being rejected. A information disclose during the term of an approved Loan Facility can result, at the absolute discretion of the States of Jersey, result in the termination of the Loan Agreement

10.3 A Loan Facility repayment breach of Loan or Royalty Agreement will result in the Treasury Department following its standard policies on debt recovery. Any change from the standard Treasury policies will require a recommendation from the Board and a Ministerial Decision from the Minister from Economic Development.

11 Termination of a Loan

11.1 Either party to an approved Loan may at any time by notice in writing, and without the need to provide any reason therefore, specify to the other party a Termination Date which shall be not less than six months from the date on which such notice is given. In all cases the Loan and any interest due will have to be repaid in full to the States of Jersey.

11.2 An organisation in receipt of a Loan may request an early repayment or settlement figure. This settlement figure will be calculated by the Treasury Department,

11.3 If a material breach, as determined by the States in their absolute discretion, by the organisation in receipt of a Loan, which is continuing un-remedied, the States may by notice in writing to the company immediately terminate the Loan agreement and make demand for full repayment of any outstanding loan and interest.

12 Liability to the States

The Loan Agreement must ensure the States of Jersey the Fund or it Board Members shall have no liability to the Organisation in receipt of a loan whether in contract, tort (including negligence or breach of statutory duty) or other otherwise.

13 Governing Laws and Jurisdictions

The Laws governing all documentation Loan or Royal Agreement shall be governed and construed in accordance with Jersey Law.

GRANTS

Grants will only be considered in exceptional circumstances and only if all of the following conditions are met:

- The applicant can justify and demonstrate that the project will not generate any income within the first 5 years of the Project starting.
- The Project will result in significant economic spillovers in Jersey during the first 5 years of the project commencing
- The project will deliver a significant economic competitive advantage to the Island.
- The project will be delivered in the Bailiwick of Jersey
- The project, within the first 5 years, will result in the creation of new high value jobs (direct or indirect employment)

If all of the above are met the application, assessment and approval process will follow the policies defined for Loans, which includes the requirement for the company receiving a Grant to enter into a Royalty Agreement.