

STATES OF JERSEY

Corporate Services Scrutiny Panel Future Hospital Funding Strategy Review

MONDAY, 20th MARCH 2017

Panel:

Deputy J.A.N. Le Fondré of St. Lawrence (Chairman)

Connétable C.H. Taylor of St. John

Deputy K.C. Lewis of St. Saviour

Senator S.C. Ferguson

Witnesses:

The Minister for Treasury and Resources

Assistant Minister for Treasury and Resources

Treasurer of the States

Director, Financial Planning and Performance

Director, Treasury Operations and Investments

[11:01]

Deputy J.A.N. Le Fondré of St. Lawrence (Chairman):

... Minister on the Future Hospital Funding Strategy Review. I will do the usual announcements. Minister, as you are aware, I would like to draw your attention to the notice that is sitting in front of you but I will be reading it out, which is that Scrutiny Panels, the proceedings of the panel are covered by parliamentary privilege through Article 34 of the States of Jersey Law 2005 and the States of Jersey (Powers, Privileges and Immunities) (Scrutiny Panels, Public Accounts Committees and Privileges and Procedures Committee) (Jersey) Regulations 2006 and witnesses are protected from being sued or prosecuted for anything said during hearings unless they say something they know to be untrue. This protection is given to witnesses to ensure they can speak freely and openly to the

panel when giving evidence without fear of legal action although the immunities should obviously be abused by making unsubstantiated statements about third parties who have no right of reply. The panel would like you to bear this in mind when answering questions. Also we do expect members of the public and the media in the public seating to remain silent at all times while the hearing carries on. Minister, as we proceed through the questions, we may stop you if we feel you have answered the question sufficiently because we do need you to try to be as concise as possible and I am sure you are aware of that, particularly as there are other things that are occurring after 1.00 p.m., but obviously we want to make sure that these questions take priority. For the avoidance of doubt if you see my hand raised that should be taken to be that we want to move on. What I am going to try and avoid is that we do not over-talk each other which can be a danger in these sorts of hearings. Should it be necessary, if you feel you wish to add something at the end of the hearing, we shall give you some time then. So for the benefit of the tape if we can start going round stating your name and position. What I would also like from the ministerial team is, if you could within that lot, identify your principal role and responsibilities as regard to the project. So, Deputy John Le Fondré, Chairman of the Corporate Services Scrutiny Panel.

Deputy K.C. Lewis of St. Saviour:

Deputy Kevin Lewis, panel member.

Senator S.C. Ferguson:

Senator Sarah Ferguson, member of the panel.

Connétable C.H. Taylor of St. John:

Constable Chris Taylor, member of the panel.

The Minister for Treasury and Resources:

Senator Alan Maclean, Minister for Treasury and Resources.

Assistant Minister for Treasury and Resources:

Assistant Minister for Treasury and Resources, John Refault, Constable of St. Peter.

Treasurer of the States:

Richard Bell, Treasurer of the States.

Director, Financial Planning and Performance:

Alison Rogers, Director for Financial Planning and Performance.

Director, Treasury Operations and Investments:

Simon Hayward, Director of Treasury Operations and Investments.

The Connétable of St. John:

Minister, what is the total budget for this project that you are working to?

The Minister for Treasury and Resources:

The hospital project that you are referring to is £466 million.

The Connétable of St. John:

What is the total level of contingency within this budget?

The Minister for Treasury and Resources:

There is a figure identified up to £90 million.

The Connétable of St. John:

You say “up to £90 million”?

The Minister for Treasury and Resources:

Yes, contingency.

Deputy J.A.N. Le Fondré:

Can I just ask, is that the present figure?

The Minister for Treasury and Resources:

I said up to £90 million because £90 million was the original figure. It is now £74,108,000.

The Connétable of St. John:

Who owns the contingency?

The Minister for Treasury and Resources:

Contingencies are managed from within Treasury.

The Connétable of St. John:

So Treasury owns the contingency, thank you.

The Minister for Treasury and Resources:

Correct.

The Connétable of St. John:

We were told during Friday's public hearing that more work will be done on how the contingency will be controlled. How do you see this working?

The Minister for Treasury and Resources:

Well, it is only Monday today.

The Connétable of St. John:

Yes, but it was not you that we were interviewing on Friday. This was the construction team from Infrastructure and Health. You are the Minister for Treasury and Resources who is controlling the contingency. We would like to know what controls you will be putting on it.

The Minister for Treasury and Resources:

Well, the controls quite simply will be that requests will come through from the team responsible for delivery at the point at which the project is progressing and they will be assessed from a Treasury perspective, those particular requests that come through, and released upon *pro formas* that will be agreed nearer the time.

The Connétable of St. John:

What if a request comes through and you say: "No, we will not supply that contingency"?

The Minister for Treasury and Resources:

Well, I think we would want more details around what the request involved. If we had some questions it would be a question of ensuring that we get satisfactory answers to those particular queries that arise in relation to it.

The Connétable of St. John:

Okay, thank you. So currently the total spend is £466 million, the contingency is £74 million, so the actual real cost of the hospital is £392 million.

The Minister for Treasury and Resources:

Well, as far as the proposition was concerned we put a capped figure of £466 million down at that time, as I have just alluded to. Even the contingency figure has changed and adjusted since then. This is a moving feast and will continue to be updated as we progress or as the project progresses.

The Connétable of St. John:

Yes. This is one of the concerns of the panel, is the contingency was £90 million, which meant that the hospital was costing £376 million. The contingency has now been reduced so that ...

Treasurer of the States:

Sorry. The contingency figure that the Minister has quoted, the contingency figure was within the paper that was lodged, P.130/2016. I know that we have had this internal discussion about is it £90 million or £74 million, so we are reading directly from the proposition.

The Connétable of St. John:

Right. So if the contingency in the proposition is £90 million ...

Treasurer of the States:

It is £74 million.

The Connétable of St. John:

It is £74 million, okay.

Treasurer of the States:

Yes. So is has not ...

Deputy J.A.N. Le Fondré:

Can we just clarify, sorry from ...

Treasurer of the States:

It is £74 million on page 6 of that proposition.

Deputy J.A.N. Le Fondré:

Yes. No, the reference we are making is the original contingency when it was originally alluded to in the M.T.F.P. (Medium Term Financial Plan) was £90 million.

The Minister for Treasury and Resources:

Correct.

Deputy J.A.N. Le Fondré:

Okay. Reference has been made to £90 million, now I accept it is £74 million so therefore there is a point that over time the contingency is changing.

The Minister for Treasury and Resources:

Yes, but that was a very early stage first cut which is why, I think we have said on many occasions, that it was £90 million because it was so early. The proposition that was lodged in November last

year was identifying the contingency at a more refined, £74 million. The point I was making was that this is going to change because the figures was still being refined and indeed the proposition that will be presented for debate at the States in the summertime will have even more detail around the cost of the project and I have little doubt that the contingency could well have moved again by that stage.

The Connétable of St. John:

So at what point will you set the various elements of the budget and in particular in relation to the controls over contingency?

The Minister for Treasury and Resources:

Well, as I said a moment ago, the figures are going to be and are continuing to be redefined and that work will be concluded in order to lodge the proposition for summer decision by the States ... around the summertime for the decision of the States.

The Connétable of St. John:

So we are looking at summertime, in other words, to fixing the particular elements of the budget?

The Minister for Treasury and Resources:

Yes. There will be a far greater clarity at that stage in order to allow the proposition to be lodged for the States to consider it.

Deputy J.A.N. Le Fondré:

Is it debated in July or lodged in July for debate in September?

The Minister for Treasury and Resources:

That is yet to be finalised. The target is the summertime for debate but that may move depending on a number of variables that could impact upon it. I do not know whether my Assistant Minister has an update on that.

Assistant Minister for Treasury and Resources:

No. I think that as the first of the programme goes through, we are looking at an 8 to 10 year programme, so obviously we have got to look forward and make sure that we have enough funds to cover that timeline as well. What we cannot predict is what R.P.I. (Retail Price Index) and material costs are going to do over that period of time so we have to put within a global amount a contingency to cover those ...

Deputy J.A.N. Le Fondré:

Yes, we understand that. We will get there.

The Connétable of St. John:

You mentioned inflation, it was confirmed to us on Friday that the inflation estimates have been reduced and that the budget was being reduced by some £13 million. However, of that saving, which was a contingency figure, a significant amount, around £11 million, has been reallocated. So when a saving has been made it is being reallocated. Now, our concern is while in this particular case the rationale behind this was sound but can you confirm what controls will be put in place that future savings of the project are banked as opposed to reallocated and spent?

Assistant Minister for Treasury and Resources:

I think it is fair to say to that, certainly Treasury, are very aware of the size of the contingency and it will robustly managed and challenged at every application that comes in. That is why we are holding it in Treasury while divesting into Jersey Property Holdings really in this project. On the point of changing the figures, of making a saving and then reallocating, then is a matter, as we go forward, for Property Holdings to decide where best they needed the monies to fulfil this project.

Deputy J.A.N. Le Fondré:

Can I come across briefly?

Assistant Minister for Treasury and Resources:

Yes, please.

Deputy J.A.N. Le Fondré:

So the point you are making is that inflation estimate is an assumption.

Assistant Minister for Treasury and Resources:

Yes, absolutely.

Deputy J.A.N. Le Fondré:

Okay. So it is an assumption that is going to change; it can go up or down. Therefore, if you have taken ... sorry, if advantage has been taken of the fact the assumption went down, so £13 million becomes free if you like, if that money has now been ... I will use the word "spent" because it has been reallocated into the project as an identified spend. If inflation goes back up again that element of, if you like, a contingent amount has now gone.

Assistant Minister for Treasury and Resources:

You are right and unfortunately that is on both sides.

Deputy J.A.N. Le Fondré:

Okay. So that is the issue we are trying to identify.

Assistant Minister for Treasury and Resources:

I understand your concern, yes, but there is ...

Deputy J.A.N. Le Fondré:

So, therefore, we accept in this instance what has happened ... what we are just looking down as a marker, going forward, is how do you then assure yourselves that bearing in mind all the work that has been done up to now that suddenly you get a change in an assumption which could change again the other way in the future that you do not erode those elements of contingency too early.

Assistant Minister for Treasury and Resources:

Absolutely. Unfortunately these are one of the unknowns because we can only speculate at what R.P.I. will do going forwards.

Deputy J.A.N. Le Fondré:

So when you robustly challenge, who is the "we"?

Assistant Minister for Treasury and Resources:

We, Treasury officers.

Treasurer of the States:

Up until the point at which we will move this into a delivery and until we get to the investment decision by the States obviously we are not into delivery, then Treasury will ... we will be present within the team but we will take our contingency decisions outside of the team. At this point in time we are in the team so we are party to the discussions as to what will happen. The chair is well aware and, as I am sure that Deputy Lewis is aware from your time at what was T.T.S. (Transport and Technical Services) and is now Infrastructure, what began as an element of contingency when you are this far out is because of the advice that has happened in the past where you will think everything will go in your favour, yes, and therefore put insufficient into the budget. It is called optimism price. So you add a budget on because you are more than likely going to be more optimistic that it will turn out to be the case. As you move through a project your optimism will either be proven or your optimism will tend to be false in which case you will have used some of the contingency. So very early on in a project you will carry a very large optimism bias and it will be sometimes you will have been right on that optimistic view and sometimes you will not have and, therefore, you will simply ... you are confusing inflation indices which will move with ...

Deputy J.A.N. Le Fondré:

I am not, because my understanding is that there are 3 figures involved. There is the contingency and the optimum bias which add up to £74 million. There is an additional assumption figure of £69 million for inflation and it is my understanding it is the £69 million that has reduced and has now been spent. So the point we ... so we are what we are ...

Treasurer of the States:

So what we are making about the Treasury rule is the Treasury rule will fundamentally alter once we get past the investment decision which is made above the Treasury in the States Assembly.

Deputy J.A.N. Le Fondré:

Okay. So as of now ...

Treasurer of the States:

As of now we are in the team, working with the team.

Deputy J.A.N. Le Fondré:

So if the assumptions change, so, for example, using this scenario so say inflation assumptions drop again and it identifies another £10 million, yes, and somebody says: "We can spend this money in a certain way and there is a really good case behind it", how robust are you in challenging that reallocation, that spending of that £10 million, particularly when we are dealing in an inflation assumption which could change in the future bearing in mind at this stage, as you say, nothing has been crystallised? How robust is the discussion or who is having that discussion because if you are in the team you are in the team? We wanted to check as to ...

Treasurer of the States:

So I am not going to use a specific example. What I ... list one recently which was, say, the upper range of £7 million or £8 million that was going to be added on.

Deputy J.A.N. Le Fondré:

Is this Westaway Court or not?

Treasurer of the States:

I am not going to say exactly what it was for, but the process that we were going through was, I had been told that in fact while that would add capital cost it will save on the revenue cost and so therefore we have laid down that there should be a business case in respect of that item that shows the revenue advantages of spending another £7 million to £8 million, okay.

[11:15]

Deputy J.A.N. Le Fondré:

Okay.

Treasurer of the States:

Once the ... and this is the point typically I, we, this Treasury, need the States to give us a maximum budget otherwise that then becomes quite hard to work within. Until you have a budget it is very difficult to say: "But the budget is this." That is why the Minister for Treasury and Resources is asking the States to set a cap otherwise those decisions become much more difficult to hold, what is to say, some control over. That is why we are asking for it.

The Connétable of St. John:

Yes. We understand the capping for the £466 million but our concern is that the hospital is £376 million. It is how that money in the middle, the £90 million, is gradually being reduced and whether, at the end of the day, the contingency will be sufficient because too much has been transferred into the project of the hospital as opposed to kept as a contingency.

The Minister for Treasury and Resources:

I would just ... sorry, I would just add that I think the important point of this is the active management of that and in particular with regard to the process which you were alluding to earlier on at the management of the contingency, which Treasury have responsibility for, and which ultimately the Minister will have responsibility to sign off or delegate if it is small sums, whatever is appropriate, in terms of that particular process ...

Deputy J.A.N. Le Fondré:

Can I just also stress, and I will get Chris back on schedule, I think the query is also a matter of mindset. In other words, if one has a budget of £466 million; that is what you set out to spend notionally. If you have a budget of £370 million, yes, you have got an envelope of £466 million, but if you, as Treasury, are saying: "Now, your budget is, I will say, £370 million or £376 million or whatever that number is", then it focuses the minds of the people who are adding in or as specifications change, that is what they have got to work to. So that is the question, what is the mindset, in other words perhaps we are asking what the budget is?

The Minister for Treasury and Resources:

Okay. I mean contingency is there for largely unforeseen circumstances which could be a number of items you have referred to, which is changing forecasts or inflationary costs or whatever it might

be, so it would have to be an exception item. That would be the position that would be the starting point for certain.

Deputy J.A.N. Le Fondré:

Okay.

The Connétable of St. John:

Which is why the question I asked at the beginning was, who owns the contingency and you said the Treasury.

The Minister for Treasury and Resources:

Correct.

The Connétable of St. John:

This is why we are concerned that the budget, that contingency, is already being spent before the spade has been put in the ground. So we have not had any unforeseen costs yet because we have not started the project and yet contingency is already being used.

Treasurer of the States:

At this point the States has not set a budget at all.

The Connétable of St. John:

No, because we have not debated it. That is why we are having this meeting ... is because we are being asked by the Assembly to scrutinise what is going on and a big concern is that already, before a spade been put in the ground, the contingency for exceptional items is already being, as it were, transferred from contingency to the build project.

Treasurer of the States:

No, except that it has not because I remind you the States decided not to make a decision.

Deputy J.A.N. Le Fondré:

Well, to be fair ...

Treasurer of the States:

It will be another period until April and then ...

Deputy J.A.N. Le Fondré:

To be fair the proposition in front of the States; it is a spend up to a maximum of £466 million. So in other words within the departments you are not going to be working to £550 million because that number is not around. I cannot remember what was in the M.T.F.P. itself. I have got a feeling it was that kind of number. So the query is, if the department is working to £466 million, what is the mindset? Is it £466 million or should it be less, £370 million or something, and the question is therefore, what is the mindset from Treasury as to what is the number they should be aiming for? Not: "Well, the States have not debated it so therefore it could be anything." We need to know what the envelope is. You have got a number. You came forward with it.

The Minister for Treasury and Resources:

Well, the mindset is not to spend the contingency unless it is absolutely needed. It is there for that purpose.

Deputy J.A.N. Le Fondré:

Thank you.

The Connétable of St. John:

Thank you, right. Number 4, what mechanism has been put in place to ensure the contingency is effectively guarded against project creep?

The Minister for Treasury and Resources:

I think we have more or less answered that hopefully. In terms of the process within Treasury, Treasury owns the contingency and contingency requests will be signed off by the Minister or delegated if smaller amounts, as we decide exactly how that will be crafted.

Deputy J.A.N. Le Fondré:

Can you define "smaller amounts"? Any suggestions at this stage? Is it, you will have anything above a million or ...

The Minister for Treasury and Resources:

I think we just need to look at that and come back in more detail later on. It also will depend on the number of requests. If there are number of smaller requests it might be more sensible to have it delegated to deal with if they are only small items but we need to really be clearer as to what that might look like.

Deputy J.A.N. Le Fondré:

Okay. So at the moment can I seek some clarity what might be in your mind as to where that split might be roughly?

The Minister for Treasury and Resources:

I am not going to speculate at this stage. What I have asked for is some profiling as to what the contingency requests might look like; the frequency and so on and so forth. Once we have got that then we will put together the exact process. But the point is primarily, and this is what I think, Chairman, you need to take away, that it will be for the Minister to sign off on contingencies, certainly anything of any substance.

Deputy J.A.N. Le Fondré:

But what I am trying to get from you is, what is substance?

The Minister for Treasury and Resources:

Yes, I know and we will ... absolutely, but we will come back and clarify that but I do not think it should be a matter of great concern for you.

The Connétable of St. John:

Our advisers have commented that it can be beneficial to have third party involved in a project from the viewpoint of controlling expenditure. So while we recognise that a public/private finance initiative may not be suitable for Jersey are there any other ways you could achieve the same level or some level of external involvement and oversight to help control expenditure?

Deputy J.A.N. Le Fondré:

That is external of the Executive.

The Minister for Treasury and Resources:

As the project ... sorry?

Deputy J.A.N. Le Fondré:

External to the Executive.

The Minister for Treasury and Resources:

To the Executive, yes. This is on the management of the funding.

The Connétable of St. John:

Yes.

The Minister for Treasury and Resources:

I mean there are external advisers which are clearly brought in who have been advising to date but there is no intention at this stage to bring anybody else in.

Deputy J.A.N. Le Fondré:

It is also not just the funding; it is the budget as well, in other words the expenditure and how it is spent. Is there no plan at this stage?

The Minister for Treasury and Resources:

No.

Treasurer of the States:

I have had discussions with other members of the delivery team recognising that Treasury no longer has Property Holdings under its domain as to how the Treasury in executing what the Assembly and the Minister is going to be asking of us in terms of control of contingency to provide some further expert advice to us in making those contingency decisions. So we are discussing that as a team as to how we can make that right without wandering into the accounting officers responsibility for ...

The Connétable of St. John:

Given this is the largest capital spend on any project to date what, in your view, is the balance between time, cost and quality? The sort of famous triangle; time, quality, cost.

Assistant Minister for Treasury and Resources:

Well, equally from a customer point of view, with my Health and Social Services hat on, we want quality, the most important part because of the long term need for the public of Jersey but equally it has got to be done on time and at cost, at the right cost. That is a matter really for the project managers but certainly from a customer point of view quality is premium.

Deputy J.A.N. Le Fondré:

Obviously we were asking the question of the Minister for Treasury and Resources.

Assistant Minister for Treasury and Resources:

You are. Sorry, about that. Possibly a slave of another hat.

Deputy J.A.N. Le Fondré:

Yes. So take that hat off, please, Constable, and put the Treasury hat on.

Assistant Minister for Treasury and Resources:

Yes, fine, thank you.

The Minister for Treasury and Resources:

The Assistant Minister is perfectly at liberty to answer if he wishes. Do you want a further comment above and beyond?

The Connétable of St. John:

Well, it leads on to basically who has overall responsibility for value for money from the project, would it be Treasury or Infrastructure?

The Minister for Treasury and Resources:

Well, I mean clearly Treasury are integrally involved in the project but one would clearly suggest that the accounting officer would be the role that would be the one responsible for value for money.

Deputy J.A.N. Le Fondré:

So that is the chief officer for Infrastructure.

The Minister for Treasury and Resources:

It is yet to be absolutely finalised who the accounting officer would be but that is the most likely role at the moment.

Deputy J.A.N. Le Fondré:

Hang on, let us just be clear, who is responsible now?

Treasurer of the States:

Me. The budget holder is the accounting officer for D.f.I. (Department for Infrastructure).

Deputy J.A.N. Le Fondré:

So that is the chief officer of Infrastructure again.

Treasurer of the States:

It is the same person at the moment.

Deputy J.A.N. Le Fondré:

Okay. But the discussions are whether that remains to be the case, is that correct? Microphones do not pick up nodding.

The Minister for Treasury and Resources:

That is likely to be the case, yes.

Deputy J.A.N. Le Fondré:

Sorry. The discussions going on are as to whether that is going to remain or not?

The Minister for Treasury and Resources:

Correct.

Deputy J.A.N. Le Fondré:

Okay, right. My little section. Minister, the Andium bond is for £250 million. Can you confirm the amount attributed to the bond for borrowing purposes?

The Minister for Treasury and Resources:

Are you talking about Article 21(3)?

Deputy J.A.N. Le Fondré:

Exactly as I asked the question, Minister.

The Minister for Treasury and Resources:

The Andium bond is held in the accounts at £243 million.

Deputy J.A.N. Le Fondré:

So for borrowing purpose, just to confirm the calculation, the figure is £243 million and can you confirm, therefore, that is based on the cash received at the time?

The Minister for Treasury and Resources:

Correct.

Treasurer of the States:

The current value in the States account is a slight difference but it is not a hundred miles away from the £ 243 million ...

Deputy J.A.N. Le Fondré:

No, no. I need some clarity because I am understanding that the accounting treatment is irrelevant to the borrowing treatment under the law and what I am asking is just confirmation ...

Treasurer of the States:

I am confirming to you the number that was given in the original calculations. It was not a million miles away from £243 million.

Deputy J.A.N. Le Fondré:

Yes, but it based on ...

Treasurer of the States:

It was £243 million.

Deputy J.A.N. Le Fondré:

Yes, it is based on the cash received. It is not an accounting treatment on the cash received. Okay. But can you confirm, Minister, that the obligation to pay is £250 million?

The Minister for Treasury and Resources:

It is.

Deputy J.A.N. Le Fondré:

Good. What I would like to refer ...

The Minister for Treasury and Resources:

So it was issued at a discount.

Deputy J.A.N. Le Fondré:

Yes, but we have the obligation to pay in the future £250 million which is the nominal value of the bond.

The Minister for Treasury and Resources:

Correct.

Deputy J.A.N. Le Fondré:

Good. What I would like to refer to, unfortunately I do not have a copy to distribute, but you will recall the schedule that you gave to States Members on 19th January and that showed a bottom line figure, which I think you labelled as "balance to borrowing limit" of £402 million, correct?

The Minister for Treasury and Resources:

Correct. I do not have it in front of me at the moment so it sounds correct.

Deputy J.A.N. Le Fondré:

No, that is okay. Now, what I was going to just ask is the original intention was to debate the proposition as I understood, the borrowing proposition, at the same time as the actual main hospital debate in November, correct?

Treasurer of the States:

It was a plan I think

The Minister for Treasury and Resources:

That was a plan, yes.

Deputy J.A.N. Le Fondré:

It was a plan at a point in time, okay. Could you confirm, therefore, that the figures, if it had been debated in November, would have been less than the £402 million if the debate had taken place at that same time?

Treasurer of the States:

I would confirm that the debate would not have taken place without a change to the Public Finances Law. The debate would not have taken place up to £400 million without a change to the Public Finances Law.

Deputy J.A.N. Le Fondré:

If it had taken place in November?

Treasurer of the States:

If it had taken place in November because the relevant year would have been 2015 not 2016.

Deputy J.A.N. Le Fondré:

Yes, and that would have meant what?

Treasurer of the States:

Pardon?

Deputy J.A.N. Le Fondré:

What would that have meant?

Treasurer of the States:

It would not have meant that you would have been able to put £400 million into the proposition.

Deputy J.A.N. Le Fondré:

So you would not have been able to borrow £400 million? It would have been less.

Treasurer of the States:

Without ... no, it would have. It would have, subject to the States decision, because had we chosen to take that path we would have changed the Public Finances Law. We would have asked the States.

Deputy J.A.N. Le Fondré:

Okay. At the point in time in November, with no changes to the Public Finances Law, we would not have been able to borrow £400 million if the debate had taken place in November, correct?

The Minister for Treasury and Resources:

We would have had to have used 2015 figures which would have meant exactly that in which case what we were discussing was, coming to the States with a possibility for changing the Public Finances Law to allow it to go ahead. As it happened, it was not going to be debated as it turned out in that year; it was going to be debated this year and the figures that you have just referred to meant that we were within the figures.

Deputy J.A.N. Le Fondré:

Are where we are, okay. So just to give my illustration, obviously you might want to verify us later, but my calculation based on the accounts was that the borrowing capacity at that point was in the order of £385 million. Does that sound about right? I can see some ...

Treasurer of the States:

A million miles away.

Deputy J.A.N. Le Fondré:

I can see sort of nods around roughly.

The Minister for Treasury and Resources:

It was short so, yes.

Deputy J.A.N. Le Fondré:

Okay. So, therefore, for example, using the capacity of the £402 million, I accept this is hypothetical, but if the bond had been valued at £250 million not at £243, for borrowing purposes we would have exceeded the borrowing limit, correct?

Treasurer of the States:

Can I clarify here then?

Deputy J.A.N. Le Fondré:

Yes.

Treasurer of the States:

We used the Q3 figures originally of £243, okay. At the time of launching, if memory serves me right, we were well over the £402 million so that, therefore, it would be a moot point as to whether you used £243 million or £250 million. By the time we get to debate you were considerably past £402 million ...

Deputy J.A.N. Le Fondré:

In April you mean, when we get to the debate, yes.

Treasurer of the States:

No.

Deputy J.A.N. Le Fondré:

That is right.

Treasurer of the States:

In January we were considerably past £402 million because we had revised income forecasts.

Deputy J.A.N. Le Fondré:

Does this mean the schedule you gave us that showed £402 million was prudent?

Treasurer of the States:

Yes, prudent based upon where we were when we were preparing as opposed to where we were at point of lodging.

Deputy J.A.N. Le Fondré:

Right. So the schedule that you gave us that showed £402 million, which I accept is after guarantees.

Treasurer of the States:

Is a Q3 forecast.

Deputy J.A.N. Le Fondré:

So based on the Q3 forecasts but was obviously the schedule that was presented to States Members.

Treasurer of the States:

Yes, based on the Q3 forecast.

Deputy J.A.N. Le Fondré:

So based on that schedule if the £243 million had been £250 million would you have not reached the £402 million on the calculations you did?

Treasurer of the States:

If you had used the £250 million based upon that, no, but I am confirming, as at November, the figures were improved on that position which is the point of lodging November.

[11:30]

Deputy J.A.N. Le Fondré:

Right. The law is, at the point of debate.

Treasurer of the States:

At the point of debate then we were well beyond the £402 million.

Deputy J.A.N. Le Fondré:

What I am trying to get to, I was assuming that this schedule that you gave us, which came down to £402 million which I add was given to States Members on 19th January was the most up to date forecast that we had available.

Treasurer of the States:

No. The most up-to-date forecast is the most up-to-date forecast at the end of the year which was considerably beyond that point. We were showing you a prudent position based upon Q3's forecast.

Deputy J.A.N. Le Fondré:

So at the time you gave it to States Members on 19th January you had a different set of figures available?

Treasurer of the States:

At the time we had the debate we used the last formal forecast that had been put in front of the Council of Ministers for the Q3 forecast in the formal reporting pack that you are well aware of. The position, however, at the time of lodging was that the income forecast was improved from that and as at the end of the year ...

Deputy J.A.N. Le Fondré:

Can we forget the time of lodging? It is the date of debate is the crucial point and all I am trying to get to is ...

Treasurer of the States:

All I am trying to say is at the time of sticking that in front of you it was the most prudent estimate we had which was based upon the Q3 figures that we had and improved the forecast that would be on that number.

Deputy J.A.N. Le Fondré:

Okay. I think an observation I would make then is when we get to the debate in April we need an up-to-date figure.

Treasurer of the States:

You probably will have had the published position for 2016.

The Minister for Treasury and Resources:

You will do, and the actual position has improved dramatically since then anyway, just as an aside, but the other confusion that arose at the time ...

Deputy J.A.N. Le Fondré:

We will come to that in a minute, yes.

The Minister for Treasury and Resources:

The other confusion that arose at the time was, as the Treasurer has been saying and which the law allows, we were using forecasts and the forecasts were being updated and so there were a range of forecasts that were being used when we were considering the preparation of the proposition and for the period from then to the lodging and for the period from then to the debate. So the numbers were changing all the time, always in a more positive way but nevertheless they were changing, and that is what caused the confusion at the time.

Deputy J.A.N. Le Fondré:

I accept that but obviously the point is that it is the figures at the time of approval, I believe, is what the law says.

Treasury of the States:

Yes. The important point, had the figures been worse then we would have told you that they were worse, but they were not worse, they were better.

Deputy J.A.N. Le Fondré:

That is okay. I think the point I was trying to make is that the States Members were working on 402 because that is what were the figures that came out of Treasury and on that basis the definition of whether it is 250 or 243 was actually quite important because if it was 250 borrowed already then £7 million would have taken you below that limit of £402 million so you would not have been able to borrow £400 million. What you are saying to us is that the figures are more positive than what was given to States Members. Correct? I am looking at the Minister. Is that correct?

The Minister for Treasury and Resources:

Yes.

Deputy J.A.N. Le Fondré:

Yes. Okay. Can we move forward because where it then becomes rather interesting is ... I am skipping around slightly. So what I just want to check then is ... I think we have covered it. You are saying the current expectation for the amount of headroom for borrowing under the Public Finances Law is now better than the £402 million that you gave to States Members on 19th January?

The Minister for Treasury and Resources:

Correct.

Deputy J.A.N. Le Fondré:

Do you have a rough indication of how much by, like £10 million, £15 million?

The Minister for Treasury and Resources:

£25 million.

Deputy J.A.N. Le Fondré:

So now we should be looking at 427 say, yes?

Treasurer of the States:

428.

Deputy J.A.N. Le Fondré:

428. Okay. So on that basis there are no plans to change the borrowing ... sorry, start again. Are there any intended plans at this stage, not necessarily linked to the hospital, to change the borrowing limit in the Public Finances Law?

The Minister for Treasury and Resources:

Not based on the position that we are currently in, no, there is not.

Deputy J.A.N. Le Fondré:

Even generally looking forward, you are not saying that we need to go out and borrow more money in the future for other capital projects?

The Minister for Treasury and Resources:

There have been no discussions of that type.

Deputy J.A.N. Le Fondré:

Okay. So no plans at this stage?

The Minister for Treasury and Resources:

No.

Deputy J.A.N. Le Fondré:

Okay. Right, what we were trying to make the point is obviously in terms of long-term care ...

The Minister for Treasury and Resources:

Sorry, just go back. Although there have been no discussions within Treasury or the Council of Ministers, of course there are those that are suggesting for student financing we should go out and borrow money, which would be an entirely different debate.

Deputy J.A.N. Le Fondré:

Okay. In other words, if that came through you would have to change the Public Finances Law to increase the ability of the States to borrow money or if any other significant project came through you would have to change the Finances Law again to increase the capacity of the States to borrow money?

The Minister for Treasury and Resources:

Yes. We would not be able to do both.

Senator S.C. Ferguson:

At the moment you are saying that the capacity to borrow is slightly over 16 per cent of G.D.P. (Gross Domestic Product). That was the figure that was mentioned.

Treasurer of the States:

That was the figure of Standard & Poor's in terms their rating, but the percentage of G.D.P. is not in the law.

Senator S.C. Ferguson

Well, it was mentioned in the debate, I think, that borrowing ...

The Minister for Treasury and Resources:

Debt to G.D.P. which was 6 per cent.

Senator S.C. Ferguson

I am sorry, debt to G.D.P. Well, borrowing debt, the hospital and so on.

The Minister for Treasury and Resources:

Yes. We were discussing ...

Senator S.C. Ferguson

So what is your figure? I am really asking what is your top figure as debt as a percentage of G.D.P.?

The Minister for Treasury and Resources:

Well, the position was 6 per cent. The view is with a bond up to £400 million I think that would take it to 16 per cent, if I am correct. What we would be very conscious of would be any impact that borrowing would have on, for example, our credit rating and we are, based on advice, significantly away from that position but we would not want to see it rise very much from the current position. As I have just pointed out to the Chairman, there are no plans for any further debt. I only made the point about student financing because it has been topical but if there were a proposal for student financing then that would have to be taken into consideration and could potentially add to those percentages we have just discussed.

Deputy J.A.N. Le Fondré:

If we can just move on then, obviously one of the things that then attracted States Members' attention, shall we say, was the treatment of long-term care, and this is around the issue of whether it is a tax or a charge. So what I want to do, Minister, is just explore that under a couple of questions

and then we will shortly move on to somebody else. When long-term care was introduced, the report that accompanied the draft law stated the following: “A new ring-fenced fund will be established based on compulsory contributions from employees, the self-employed and pensioners. The initial contribution rate of around 1.5 per cent will be fixed for 5 years. In addition, current States funding of up to £30 million a year will be paid into the fund. The scheme will be available to all eligible claimants.” The crucial bit of that, Minister, is it also states in the report: “Although there is no formal link to an individual’s contributions history, it is a condition that individuals have paid the contributions that they were liable for.” However, it appears that the final law itself makes no reference to a link between contributions and entitlement. The panel spent some time considering this and we are of the opinion that if the wording of the law had matched the wording of the report then long-term care would not have been considered as a tax for this purpose. The question, Minister, as no doubt you have had these types of discussions, is do you agree with that opinion? You may wish to defer to your chief officer who might have some experience in this.

The Minister for Treasury and Resources:

Well, I will do but before I do so I would just comment that as far as we were concerned we had some clear advice as to whether the income that is represented from long-term care could be included for the purposes of Article 21(3) and I think the Attorney General ... in fact it was the Solicitor General, correction, during the course of the discussions over this that confirmed that the understanding was ... or made clear what the understanding was for the purposes of the public finances.

Deputy J.A.N. Le Fondré:

I think you are right, Minister. What we are exploring on is that there seems to be a very fine argument as to why it is a tax and not a charge. I wonder if you were aware or do you agree that that is the lynchpin of the argument and perhaps you might direct that to the Treasurer.

Treasurer of the States:

I am not quite clear of the question, but in terms of the answer in respect of 21(3) it just goes back to we had not expected to confirm for the purposes of 21(3) that it would be deemed tax revenue and, therefore, that is another factor that said that we were looking at changing the Public Finances Law. However, once it was confirmed for the purposes of 21(3) it would be regarded that was another reason that we did not bring it forward against the Public Finances Law to change the borrowing. Obviously if it had not been included then we would not have been able to come forward with the proposition for £400 million. Within there is my previous expectation as to whether it would have been included in the calculation.

Deputy J.A.N. Le Fondré:

Initially you were approaching it that it was a charge not a tax and would not have been included?

Treasurer of the States:

Initially, yes, within the confines of how the law works and there were a number of other instances which for accountants feel like one thing but for lawyers feel like something entirely different.

Deputy J.A.N. Le Fondré:

We have had that discussion.

Treasurer of the States:

With leases and such like which for an accountant you would have in here but for the purposes of the law they are in there, does not mean that for accountants we might regard them any differently. I think it is an area that going forward we are confident that at this point within the meaning of the law going forward it would help to clarify from more of a perspective of an accountant's view.

Deputy J.A.N. Le Fondré:

Do you think that perhaps in future the Public Finances Law could warrant a bit of a review to clarify some of these errors?

Treasurer of the States:

I think the confusion that has arisen in the meantime and the comment probably demonstrates that that is the case.

Deputy J.A.N. Le Fondré:

Right, just going on then, I think this is back to the Minister. We also note from Hansard that on 16th May 2012 a statement by the former Minister for Social Security, Senator Le Gresley, said in reference to why he was recommending using the tax system to collect the charge that: "The contribution be kept completely separately and the money will be paid across to the Social Security Department for the new long-term care fund." The Minister later said in questions on a different day: "I have to repeat the fact that the fact is that this is not a tax and it is a social security contribution." Minister, would you agree that on its implementation long-term care was not considered a tax?

The Minister for Treasury and Resources:

On its implementation, that is correct.

Deputy J.A.N. Le Fondré:

Thank you. So from a policy perspective, how comfortable are you and other Ministers that the long-term care contribution has been defined as a tax for these purposes?

The Minister for Treasury and Resources:

It is a matter of law. It is an interpretation, is it not? It is what it is. The Solicitor General explained his views on it to Members of the Assembly and, therefore, publicly. I and the Ministers have noted the views that he made.

Deputy J.A.N. Le Fondré:

So you have accepted the fact that it is now a tax?

The Minister for Treasury and Resources:

I noted that for the purposes that we were discussing, which was under Article 21(3) his interpretation was as he laid out before the Assembly in the public forum. I am not one to disagree with the Solicitor General's view in that interpretation for that purpose.

Deputy J.A.N. Le Fondré:

That it is a tax?

The Minister for Treasury and Resources:

That is what he said.

Deputy J.A.N. Le Fondré:

That it is a tax?

The Minister for Treasury and Resources:

That is what he said.

Deputy J.A.N. Le Fondré:

That is a yes, Minister, is it?

The Minister for Treasury and Resources:

Yes, that is what he said, in the context.

Senator S.C. Ferguson

Have you considered amending the law to actually make it into a charge and not a tax?

The Minister for Treasury and Resources:

Well, the rules and terms are very clear. This is a matter of definition, is it not?

Senator S.C. Ferguson

It is a matter of amending the law if you feel that it should be a charge when it is a tax. I just asked if you are thinking of changing it.

The Minister for Treasury and Resources:

All I would say in answer to that is there is no need, in my view, to change anything because it is very clear how the fund is being used and how the money is being used. It is ring-fenced; it is for a specific purpose. All we were talking about was the definition under law, which the Solicitor General clarified for the purposes of Article 21(3) for the ability of the States to borrow. He made it clear that in that clearly defined, narrow term tax was appropriate and, therefore, the income could be used.

Deputy J.A.N. Le Fondré:

Can I just ask: is our tax rate now 21 per cent?

The Minister for Treasury and Resources:

The tax rate is not 21 per cent. Our basic rate of tax is 20 per cent.

Deputy J.A.N. Le Fondré:

But we now have another tax which adds 1 per cent on income.

The Minister for Treasury and Resources:

Chairman, we could have this debate for a long time. There is a definition in law, which the Solicitor General has dealt with for the purposes of this.

Deputy J.A.N. Le Fondré:

That it is a tax.

The Minister for Treasury and Resources:

This particular fund is established with clear boundaries, which is ring-fenced. The fund is going to be used for a specific purpose. That in itself is, I hope, clear.

Deputy J.A.N. Le Fondré:

Okay. What I would just point out before we move on is that I do not think it is practical to have 2 definitions of one: is it a tax or is it a charge? It is one or the other. It cannot be half a duck.

The Minister for Treasury and Resources:

I can understand the confusion. All I am simply doing is observing the position as it started out as a charge and the use of the particular fund, and that has not changed. I am pointing out in law what

the Solicitor General said for the purposes that we are discussing here of borrowing. I am making an observation.

[11:45]

Deputy J.A.N. Le Fondré:

Yes, the Solicitor General has defined it as a tax. Can we just state that irrespective of the fact that the figures have now improved in terms of we might get to £428 million in terms of the capacity to borrow, do you accept, Minister, that we are very close to if not at the limit we can realistically borrow and why do you consider that to be a prudent strategy?

The Minister for Treasury and Resources:

Well, I think the terms that were laid down for the ability for the States to borrow were probably reasonably prudent anyway. As we have stated already, the Treasurer made the point, and I will reconfirm it, that is that if we felt there was a need to alter the Public Finances Law to allow the necessary headroom to borrow, if that was going to be an issue then we would have brought a proposition to the States for consideration. We did not think that was the case. We thought there was enough headroom at the time. We thought there was enough headroom at the time of the debate or the intended debate. The position has improved considerably since then, as I have already pointed out.

Deputy J.A.N. Le Fondré:

The question I would like to ask as we were just going through, I am slightly concerned about the point of if we had not been able to borrow the amount of money we wanted to borrow we would have changed the law. The only reason I am saying it is the Public Finances Law is meant to be the framework that we operate in and is designed to set some financial rigour. How do you address the prospect that if circumstances do not set the rigour that was stated, we will just change the framework?

The Minister for Treasury and Resources:

I think it is important to clarify here that it is not the Minister for Treasury and Resources who was thinking: "Let us change the boundaries." It was a matter that we would have had to bring, quite naturally and quite correctly, to the States Assembly for a debate and that would have in itself created rigour.

Deputy J.A.N. Le Fondré:

Thank you.

Senator S.C. Ferguson

Looking at the overall bond proposals, do you still consider that the current market conditions make a straightforward bond the best option for raising the money?

The Minister for Treasury and Resources:

Based upon professional advice, yes, we do.

Senator S.C. Ferguson

Are you expecting to issue the bond for the full £400 million?

The Minister for Treasury and Resources:

We have not clarified that yet. The proposition made it clear that we were looking for flexibility up to £400 million and that will be finalised in due course.

Senator S.C. Ferguson

Bearing in mind the bond as structured, would you accept a lower capital receipt in order to obtain a lower interest rate?

The Minister for Treasury and Resources:

I think at the point of issuance one would need to consider all the necessary factors and make a decision at that particular point.

Senator S.C. Ferguson

How are you going to balance everything with the cap on what can be taken from the strategic reserve?

The Minister for Treasury and Resources:

I am not sure I understand your question.

Senator S.C. Ferguson

Well, you have made a lot of assumptions about the performance of the strategic reserve over the next so many years and obviously your proposals, your discussions on the bond need to take this into account. For instance, how much play do you think you have with the assumptions for the strategic reserve?

The Minister for Treasury and Resources:

Well, we based our proposals on, first of all, historic data going back over the last 30 years, looking at the performance of the strategic reserve over that period from 1986, and we believed that that

demonstrated that the performance was 4 per cent over R.P.I. on average through that period. The proposal that we have presented is much more cautious and prudent, 2 per cent over R.P.I. over the issuance period, which is intended to be 40 years. So we believe there is ... over that extended period in an environment where we have historically low bond rates, we believe that gives enough flexibility and safety.

The Connétable of St. John:

Could I come in here? Minister, obviously I am teaching some people how to suck eggs but bonds are issued at quarter per cents, in other words 2 per cent, 2.25, 2.5, 2.75. The capital is then either discounted in order to match the bond rate, which as we know with the Andium bond it was issued at £250 million and we actually received £243 million because the interest rate did not match the quarter accordingly. Our concern is that if a £400 million bond was issued at 2.7 per cent interest, for argument's sake, it would actually be issued as a £370 million bond at 2.5 per cent. So while the interest rate is lower, which is nice, the actual capital sum is £30 million less. Would you need to go to a £400 million bond at over market rate at 2.75 per cent or would you take £370 million at 2.7 per cent. You see the difference? The query we have is if you are £30 million short on the bond issue, as opposed to just 7 per cent in the Andium one, where would that £30 million come from?

Director, Treasury Operations and Investments:

I think your levels of discounting are rather aggressive in terms of some of the advice that we have received. We think the level of discount would probably be no more than £10 million in total.

The Connétable of St. John:

Okay. It is just the arithmetic that we have done, those are the figures we are getting. I am glad to hear it is a smaller discount than perhaps the more aggressive figures we are seeing.

Director, Treasury Operations and Investments:

A level of discount is natural, for the very reasons you stated, but certainly the advice that we have sought suggests that level of discount would be no more than £10 million.

The Connétable of St. John:

Okay, thank you.

Senator S.C. Ferguson

Are you thinking of issuing a bond of, say, £400 million but, given the level of discount, receiving cash for only £390 million? What sort of discounts are you thinking about?

The Minister for Treasury and Resources:

That is the figure that was suggested.

Director, Treasury Operations and Investments:

Yes, that is only natural that the bond will have some level of discount and the advice that we have sought suggests it would be about £10 million, so we would receive £390 million.

Senator S.C. Ferguson

Does that include all the fees?

Director, Treasury Operations and Investments:

That does include the book-building fees, yes.

The Minister for Treasury and Resources:

But you would be paying less interest over the period. That is the purpose of the discount, so you are discounting your interest over the period. That is why you get a discounted amount.

Senator S.C. Ferguson

Yes, I know, present values and things. Under the present wording of the proposition then, what stops you from issuing a bond with a nominal value of £410 million and just receiving a cash value of £400 million?

Director, Treasury Operations and Investments:

I think the wording of the proposition says that it will be up to £400 million.

Deputy J.A.N. Le Fondré:

Yes, it is to borrow up to a maximum of £400 million. The point we are making is that on the Andium bond everybody, including me, thought the borrowing was £250 million but it is now being said that the borrowing was £243 million. Therefore, we are querying that if you need to achieve cash of £400 million ... there is 2 scenarios. You are either trying to achieve cash of £400 million in debt terms and, therefore, your borrowing, because of discounting, could go higher, or you are intending that the nominal value is going to be £400 million in which case the difference below you would have to take out of the strategic reserve. The issue around the strategic reserve is that there is a cap on the strategic reserve. Hopefully £10 million is not going to make any difference but obviously you have still got £66 million that you are looking to fund anyway that you presume is coming.

Treasurer of the States:

The forecast, as the Chairman is probably aware, and the words within the amendment proposed by the Constable of St. John ...

Deputy J.A.N. Le Fondré:

Which is now incorporated.

Treasurer of the States:

... allows the borrowing to be between £300 million and £400 million.

Deputy J.A.N. Le Fondré:

Yes. So the problem is the definition that has come out recently is that the borrowing could be ... the cash that you are going to receive is not the nominal ...

Treasurer of the States:

We will go out to the market asking to borrow no more than £400 million and on the basis of that, that may well be discounted but we will go out to the market for that, £400 million, not £410 million. We will go out for £400 million. I realise you are trying to set some sort of trap around definition.

Deputy J.A.N. Le Fondré:

No, it is not a trap; it is clarity.

Treasurer of the States:

Just to be clear, we will say we will go for £400 million.

Deputy J.A.N. Le Fondré:

You are going to go for a nominal value of £400 million on the bond or up to a nominal value of £400 million. It is not going to be the equivalent, that the £400 million is going to be the equivalent of £243 million in Andium terms and the nominal is going to be higher?

Treasurer of the States:

Yes.

Senator S.C. Ferguson

We were just asking how much cash do you want in your pocket.

Deputy J.A.N. Le Fondré:

This is about clarity because ...

Treasurer of the States:

There is a trade-off here, is there not? More cash in your pocket with £400 million, less debt in the other pocket.

Deputy J.A.N. Le Fondré:

This not a trap. This is just the fact that we have now realised that the 250 is not being calculated at 250, it is being calculated at 243. If you look at the wording of the proposition, the wording is to borrow up to a maximum of £400 million. Therefore, in theory ...

Treasurer of the States:

We are clarifying here and now ...

Deputy J.A.N. Le Fondré:

There is no intention of that.

Treasurer of the States:

... we will go to the market for a nominal £400 million.

Senator S.C. Ferguson

Is it still the intention to issue the bond with a 40-year duration?

Treasurer of the States:

We are looking at between 30 to 40 at this point, yes.

Deputy J.A.N. Le Fondré:

When will you make the definition on the period?

Treasurer of the States:

The closer you get to issuance the closer these things will be defined.

Senator S.C. Ferguson

Have you considered a bond that could be drawn down in a set of tranches?

Treasurer of the States:

We have looked at the options, yes. What we have deemed is that the States would rather have certainty. With a bond that you draw down in tranches you leave yourself open to further market risk. That means that you, therefore, maybe pay a bit of a cost for carrying your bond when you do not actually need it, as is the case with the Housing Development Fund bond, but on the other hand it is a price you pay for certainty. If you take the alternative approach of drawdowns somewhat

nearer - and I am not sure you could get as near as you perhaps would ideally like to when lots of the money would be spent - you are still running the risk of the market going in the opposite way. The world has been very different post Brexit, for example. Therefore, at the point you draw down the second tranche you would be paid on the second tranche relating to the market at that point in time. So we looked at the alternatives and believed that the States generally has a view preferring certainty over market risk.

Senator S.C. Ferguson

So you have done the sensitivity analysis to compare them?

Treasurer of the States:

There are some calculations that have been done, which I think your adviser may have seen.

Director, Treasury Operations and Investments:

Yes, our advisers have provided your advisers with some calculations in that respect.

Treasurer of the States:

But of course they are only hypothetical examples. The market could move a lot further.

Senator S.C. Ferguson

Well, it is all a question of the accuracy of the assumptions, is it not, basically?

Treasurer of the States:

Yes.

Senator S.C. Ferguson

How far are you on with getting the proposal off the ground? If we approve the project on 18th April, are you ready to get your shovel in the ground, so to speak?

Treasurer of the States:

As the panel is aware, with the panel's agreement we are going through a tender process, in simple terms help sell the bond to investors, so that we will be as close to be ready to go after the States debate as possible so that we can start the process of appointing book builders. That would allow us also to execute what would ... our advisers would help to conclude on the best pre-hedging strategy at that point in time should it have changed since the point in time where we were ready to go in the couple of days after the previous ...

Senator S.C. Ferguson

What other types of funding did you consider? Why was a public-private finance initiative ruled out?

Treasurer of the States:

There are a number of reasons I think that the Senator probably shares with me on public finance initiatives. At the end of the day the advice we had was for greater complexity, including complexities relating to not owning the hospital and having to work with the landlord for the hospital, provider of the service. The pricing was not going to be cheaper than the pricing we could get through a bond, yet involved greater complexity. The one area where it would reduce some of the complexity would be perhaps through the construction phase, the first construction phase. There are plenty of examples of they do not necessarily do the work that the customer thinks they are going to do.

Senator S.C. Ferguson

Did you consider using the strategic reserve to wholly fund the project?

[12:00]

Treasurer of the States:

That is in the modelling, yes.

Senator S.C. Ferguson

What about using a larger proportion than is currently proposed?

Treasurer of the States:

We tested it at a number of different levels and that partly plays into where we will eventually advise the Minister in terms of somewhere between the £300 million and the £400 million on the position of the latest forecasts on the strategic reserve and the year end position that we have. We played with a number of different scenarios. At the end of the day where we were, and mostly still are, the historical lower cost of debt made it preferential to maximise the debt, at the same time as going through all the uncertainty we are going through out there in the world maintaining the size of the strategic reserve.

Senator S.C. Ferguson:

Given the current uncertainty as a result of Brexit, would it be an opportunity to use the income from the strategic reserve in the first few years and then to issue a bond to cover the bulk of the capital cost from 2019 onwards?

Treasurer of the States:

Then what you are doing there is you are taking the view that you are willing to carry the risk of the market moving against you and I come back to ... I do not want to use the word push back attack but I will, that the States Government or the States generally like to see certainty rather than uncertainty.

Senator S.C. Ferguson:

Yes, and where will the money raised in bond be held? In the strategic reserve?

Treasurer of the States:

The working assumption is it will be within the strategic reserve as part of the bigger investment portfolio and then release it as and when we need to for the hospital construction fund.

Senator S.C. Ferguson:

You will be investing it?

Treasurer of the States:

The £400 million ... this is conundrum which, I think, the Senator is talking about. If we put the £400 million into the wider investment portfolio then we will lose some of the capital, so this is part of the cost of wanting certainty that we will place that £400 million with the Treasury Advisory Panel's advice or listing their conclusions with their own investment advisers and lastly lower risk investments so as to minimise the risk of losing some of the capital.

Deputy J.A.N. Le Fondré:

Is that effectively in a cash type ... is that effectively cash, near cash type of investments?

Treasurer of the States:

Yes. It is not much more than that, yes.

Senator S.C. Ferguson:

What about ... we gathered on Friday that the financial directions and so on covering taking of money from the hospital construction fund and so on and so forth, the general financial controls of the project were still being put together. So when would you expect the financial directions ...

Treasurer of the States:

The general principles around managing a project that will change. In the changes here is that ...

Senator S.C. Ferguson:

Well, the scale of it is bigger, yes.

Treasurer of the States:

Yes, managing a project, the existing directions still apply to that extent, we are not rewriting the rulebook, this just relates to how we transfer the money through. It will be that we will expect to see cashflow forecasts and will plan our investment strategy based around those cashflow forecasts in respect of £400 million and any other sums that need to transfer. Those cashflow forecasts will change and we would expect to see the effects of those forecasts to help ensure that any investments we liquidate, that we liquidate them at least avoiding as much in the way of possible transaction costs.

Senator S.C. Ferguson:

You will be presumably having ... no, sorry, I will backtrack a minute. What about your oversight of the investment performance of the strategic reserve in order to make sure that you cover the risk that you do not get enough return from the strategic reserve to cover the costs of the borrowing?

Treasurer of the States:

Yes, so basically that is not the short-term view, it is a long-term view and then we have identified in the proposition that it may be the case ...

Senator S.C. Ferguson:

Are you going to have a special group, though, doing that?

Treasurer of the States:

Well, we already have a special group. It is called the Treasury Advisory Panel. The Treasury Advisory Panel is used to running with similar mandates in that it also was responsible for the advice to the management, the Minister and I in respect of the schoolteacher's pension, which is at R.P.I. plus 3 per cent.

Senator S.C. Ferguson:

Who is on it?

Treasurer of the States:

Who is on it? I am on it; it is chaired by a gentleman called Philip Taylor; it also has a gentleman by the name of Gordon Pollock on it, who is also the Chair of P.E.C.R.S. (Public Employees Contributory Retirement Scheme) and J.T.S.F. (Jersey Teachers' Superannuation Fund), an actuary by trade; and a gentleman called Paul Dentskevich, who has had a long career in investment banking, and sorry, advised by Aon Hewitt, our professional investment advisers.

Deputy J.A.N. Le Fondré:

Can I just ask will there effectively be a specific additional reference given to the Treasury Advisory Panel?

Treasurer of the States:

I think we have agreed in terms of ... we have agreed that this falls within ... after the terms of reference that says the Minister can ask them to look for anything in the sphere and that therefore they are changing terms of reference. We thought we might have to change the terms of reference but everyone is satisfied that we are using that clause within the Treasury Advisory Panel's mandate. In respect of investment, nothing needs to change, it is just anything else.

Deputy J.A.N. Le Fondré:

So what we are trying to say is there will be a specific body that will be tasked to make sure the returns to the strategic reserve will be sufficient or are on the track, rather, to meet the servicing requirements in terms of interest and capital for the borrowing.

Treasurer of the States:

If there was such a body that could confirm and ensure that the investment returns would be as much as

Deputy J.A.N. Le Fondré:

No, no, no, I said are on track.

Treasurer of the States:

Even on track, okay, this is a long-term strategy. It will have normal ones in the short term, any point within that long term ...

Deputy J.A.N. Le Fondré:

But what I am trying to say ...

Treasurer of the States:

It is a long-term strategy, yes.

Deputy J.A.N. Le Fondré:

Exactly, thank you, that is what we want. Good. Sarah? You are done, are you not? Okay. I have 2 queries. A couple of questions. One is just to give us an idea, how have bond interest rates, if at all, moved from the indicative rate of 2.61 per cent included in the proposition? That was November 2016.

Treasurer of the States:

I believe they were 2.72 when we debated, they are now 2.6.

Deputy J.A.N. Le Fondré:

So we debated at 2.7 ...

Treasurer of the States:

That is including the spread at this point. In the meantime, they have been 85 basis points.

Deputy J.A.N. Le Fondré:

So they have gone up and down and we are back where we are, they are at 2.6. Okay, just to elaborate on where we are going, at present what is the present return of C.I.F.(Common Investment Fund) in percentage terms roughly.

Treasurer of the States:

That is for you. Sixteen per cent on the C.I.F. I think.

Director, Treasury Operations and Investments:

Yes, so last year the C.I.F. was just over 16 per cent and the strategic reserve was slightly lower at 13.6 per cent.

Senator S.C. Ferguson:

That is adding income and capital together?

Treasurer of the States:

Yes.

Deputy J.A.N. Le Fondré:

We are assuming, therefore, as was just said, any funds received in advance of the project, so when the £400 million comes in, or whatever the number is, that will go into liquid or near liquid funds. What level of return do those funds generate of late, roughly?

Director, Treasury Operations and Investments:

The current forecast is about 1 per cent.

Deputy J.A.N. Le Fondré:

Okay, that will do. I think that is it for the moment. Right, in which case, Kevin.

Deputy K.C. Lewis:

Borrowing capacity. Minister, can you confirm that if this project proceeds as presently proposed I will remove our headroom for further borrowing?

The Minister for Treasury and Resources:

Well, we made it clear, I think, earlier on that if there was going to be any additional requirement for borrowing, I used the example of student financing, then that would require a change as we have currently positioned. So, yes.

Deputy K.C. Lewis:

Thank you. What impact will such a large bond have on our credit rating? I know you have touched on it earlier with Standard and Poor, we were triple A, we are now double A plus. Do you see that moving at all?

The Minister for Treasury and Resources:

The advice is that there is not likely to be any change on that situation alone based on our debt to GDP ratios which are still very low compared to the majority of places and upon advice we are nowhere near raising concerns with the credit rating agencies at current levels, or current proposed levels.

Deputy K.C. Lewis:

Okay, strategic reserve. Now, can you confirm that it is the intention to use the returns on the strategic reserve to repay the interest on the bond and eventually the capital at the end?

The Minister for Treasury and Resources:

Yes, the returns on the strategic reserve will pay during the period from draw down to maturity, which is deemed to be 2057, all interest and capital. Indeed the strategic reserve has been modelled based on 2 per cent above R.P.I over that period of 40 years to have a capital balance of £3.6 billion. So, just to be clear, in 2057 the debt for the hospital will have been repaid. That is the capital and the interest and the strategic reserve would have grown to £3.6 billion, based on an assumption of 2 per cent returns above R.P.I over the period, which is half what it has been achieving over the last 30 years.

Deputy K.C. Lewis:

The strategic reserve is our rainy-day fund, what if it rains in the near future and we need to use it?

The Minister for Treasury and Resources:

Sorry, I did not hear the question?

Deputy K.C. Lewis:

The strategic reserve is our rainy-day fund, what if it rains in the near future and we need to use it? In such a scenario, how would the coupon rate be paid?

The Minister for Treasury and Resources:

Well, I think first of all at the end of December 2016 there was a headroom of £128 million available within it. You have the core capital which would be available potentially. There is a likelihood, I suppose, that over the 40-year period there will be peaks and troughs in terms of performance but we are looking at this as an investment over a period ... an extended period, and I think it is worth noting over the last 30 years the returns to the strategic reserve has reduced, those included things like the financial crisis, the dotcom crisis and a number of other shocks to the financial system, and still produced a return. So I think there is plenty of flexibility available for a long-term vision, which is what this is. A long-term strategy.

Deputy K.C. Lewis:

Hopefully there will not be too many shocks. Does this, in effect, mean the strategic reserve will be, in effect, locked?

The Minister for Treasury and Resources:

Effectively, yes, up to the points that I have just referenced.

Deputy J.A.N. Le Fondré:

Do you mean 2057?

The Minister for Treasury and Resources:

Yes.

Deputy K.C. Lewis:

Well, taking that one stage further, what other potential capital project demands ...

The Minister for Treasury and Resources:

Sorry, could I just be clear, it is not locked for the primary purpose of course.

Deputy K.C. Lewis:

Yes. What other potential capital project demands are likely to occur during the lifespan of the bond?

The Minister for Treasury and Resources:

Well, the capital programme is defined for the current M.T.F.P. period to 2019. That is clearly defined to a medium-term plan that is in most people's horizons relatively short and there is capital set aside during the period for projects. There is a longer-term piece of work looking at capital beyond that, which defines or is defined under the long-term capital programme which is being updated and ongoing.

Deputy K.C. Lewis:

Would the investment strategy for the strategic reserve take into account requirements to service the bond?

The Minister for Treasury and Resources:

The investment strategy for the strategic reserve has been modelled, as I have already pointed out, and so obviously takes into consideration all the requirements necessary and the modelling is quite prudent. I have laid that out already.

Deputy K.C. Lewis:

I know you have touched on it slightly but how will you hedge the strategic reserve to ensure you can pay the interest on the bond?

The Minister for Treasury and Resources:

Did you say hedge?

Deputy K.C. Lewis:

Yes.

The Minister for Treasury and Resources:

There is no question of hedging the strategic reserve, it has an investment strategy which I have given the indication of what the returns are likely to be over the said period, which are quite prudent and historically are under half what the returns have been over the last 30 years.

Deputy K.C. Lewis:

How would the strategic reserve be protected if there was a market crash?

[12:15]

The Minister for Treasury and Resources:

There have been a number of market crashes or shocks over the last 30 years and the point that we have emphasised time and time again, the strategy for investments in the strategic reserve and the other investment funds like the Social Security Reserve Fund, is long term. So it will take and have occasions where returns will fall and value will fall but the investment strategy is long term and that can be seen by the average return of 4 per cent over R.P.I. over the last 30 years, despite what you might describe as crashes or shocks to the market like the financial crisis, like the dotcom bubble and so on.

Deputy K.C. Lewis:

What would the position be if the Island needs to raise a significant amount of funding in the future? Let say, if an amount over 100 million was needed, would you be unlikely to be able to borrow this amount?

The Minister for Treasury and Resources:

I think we have pointed out already that our debt to G.D.P. ratio is currently very low at 6 per cent even with a £400 million bond issuance it would get to 16 per cent or thereabouts. Countries like the U.K. (United Kingdom) are around about 100 per cent and the U.S. (United States) even higher, not that I wish to use that as an example of necessarily good practice. But I think it is fair to say that, upon advice, it is unlikely to concern, for example, the rating agencies if we were to need increase our debt to G.D.P. ratio, and I hasten to add again that is not a strategy that is being considered or is very likely, but there is therefore headroom if, in the future, somebody should decide that they wish to do so.

Deputy K.C. Lewis:

What plans have been put in place for the impact of the project going over £466 million due to an extremely impact on the contingency?

The Minister for Treasury and Resources:

I did not get the final part of the question.

Deputy K.C. Lewis:

What plans have been put in place for the impact of the project going over £466 million due to an extremely large impact on the contingency?

The Minister for Treasury and Resources:

Again, we have said this on a number of occasions, that there is a fairly significant contingency built into the project anyway and your Panel Member, the Constable of St. John, is at pains to point out the actual cost of the project on a number of occasions and I would hope at this stage that that

contingency would be more than sufficient to deal with any additional costs that may arise if they are deemed to be justifiable to fund.

Treasurer of the States:

Sorry, just to clarify, we have a contingency model there in the papers that are accessible by the panel.

Deputy J.A.N. Le Fondré:

Sorry, can you just repeat that?

Treasurer of the States:

There is contingency modelling on different costs that you can go over.

Deputy J.A.N. Le Fondré:

Okay, I am not aware that we have seen that, unless it has gone to the adviser. Can you make sure we receive a copy?

Director, Financial Planning and Performance:

Yes, it was in the pack that was provided with the EY report.

Deputy J.A.N. Le Fondré:

Okay, I will check on that. Just pursuing this a little bit further because one of the concerns at present is, so for example following Brexit, we could find ourselves in a position where we are in direct competition with the United Kingdom due to their lower of corporation tax rates, for example. That has not just been dreamed up, that has been mentioned a couple of times since the statement by the U.K. Chancellor, I believe.

The Minister for Treasury and Resources:

Chairman, no, that is not likely to be a serious risk, having been assessed on the basis of affordability for the U.K. to reduce their rates to a level that would be competitive.

Deputy J.A.N. Le Fondré:

I would hope that is the case, Minister, absolutely. Has one looked at, for example, that kind of scenario where for some reason, it could be anything, some form of political risk, that our tax revenues start reducing - be that the deficit positions for whatever reason - and that has to be funded out of the strategic reserve? Have you stress tested that?

Treasurer of the States:

We did some catastrophic type modelling in there. Clearly I think you come to back to where you first talked about this, you could, at this point in time, with all that money in the bank, still decide that what you wanted to do is raise taxes to pay for this. Given the existence of the strategic reserve, given the capacity within the strategic reserve and given the investment return from the strategic reserve, with what is known at the moment, it makes good sense to use this strategy. I cannot predict it, neither can the Minister or the panel, therefore my take on this position if something changed in the future then the States would probably have to change, if we are talking about significant draw downs on the strategic reserve, to see, of which this would be one, how it would be funded on an ongoing basis. So that is based upon ... we do not know what the future would hold but when you come to do the future that £400 million, it was going to be £10 million to £11 million per annum on investment on coupon and it would probably be within a whole host of other numbers that you have to deal with and you would set your budget accordingly at that point.

Deputy J.A.N. Le Fondré:

Okay, so just expanding out, maybe not from a Brexit perspective, but have you, for the sake of it, modelled within your figures or stress tested the equivalent of a 2008 financial crash happening in, I do not know, 5 years' time? Just a yes or no really.

Treasurer of the States:

We did a number ...

Director, Financial Planning and Performance:

A hundred million, one off in 2018.

Treasurer of the States:

A hundred million, one off, decreasing in 2018, I think that was an E.U. (European Union) one and that still ended up with this balance of this strategic reserve at the end of a further £3 billion, which was a surplus of £550 million over the capital value ...

Deputy J.A.N. Le Fondré:

That is still funding ... and that is still funding with coupons?

Treasurer of the States:

Yes, that is all in there. Obviously we take these matters very ...

Director, Financial Planning and Performance:

Yes, 42 million between 2020 and 2055. A 42 million shortfall over 2020 to 2055 was one of the scenarios that we looked at.

Treasurer of the States:

In which case you would still have ... that would entirely overdraw considerably the strategic reserve, and that I think would put you in a position of having to draw down £42 million every year, it was just to illustrate. It was not anything we ever thought would ever happen, it is to understand the limit of the ...

Deputy J.A.N. Le Fondré:

I know. That would be every year up to 2057?

Treasurer of the States:

By that time you would have seen a less technical background.

Deputy J.A.N. Le Fondré:

But in that sort of scenario, have you got 10 or 20 years to play with, as it were?

Director, Financial Planning and Performance:

Yes, obviously it does not happen overnight and you can see from the graph about where it starts to affect and where you would start to alert them.

Deputy J.A.N. Le Fondré:

Right, I think that probably covers strategy. As we said, what would happen if you started having to use the capital balance to support the economy and that is effectively what you are testing there. And what you are saying is that in the initial years it is okay but then after that you have to take some steps? That is a summary, depending on the magnitude of the ...

Treasurer of the States:

It is sufficient to take instances of shocks but under any scenario where you said significant deterioration in the fund, is obviously not, in that event you would have to be thinking about ... we would have to be changing the strategy regardless of what you were paying on the bond.

Deputy J.A.N. Le Fondré:

Right. Anybody else got anything at the moment?

Senator S.C. Ferguson:

Just a quick one. You talked about the C.I.F. and the investment returns, what was the capital return and what was the income return?

Director, Treasury Operations and Investments:

I do not have that breakdown here in terms of capital and income.

Senator S.C. Ferguson:

If we could have it?

Deputy J.A.N. Le Fondré:

Okay, just some questions to get a couple of points on the record as well. What are the total interest costs on the bond?

The Minister for Treasury and Resources:

Ten and a half million.

Deputy J.A.N. Le Fondré:

Over the lifetime of the bond?

Director, Treasury Operations and Investments:

Over the lifetime of the bond based on a price of 2.46, the interest cost is £393.6 million.

Deputy J.A.N. Le Fondré:

Okay, now just a clarification, I anticipate the response here. The proposition states that we are agreeing to expenditure up to a maximum of £466 million, the main construction project and all associated costs, including relocation costs and including contingencies for the new Jersey General Hospital. Now, in theory on that wording that should take account of the interest during construction but obviously it seems that that has been presented in the project as being netted off the returns in the strategic reserve rather than capitalised as part of the overall project costs. Would you like to comment?

Treasurer of the States:

Yes, I disagree.

Deputy J.A.N. Le Fondré:

So the total associated costs obviously did not include the finance costs?

Treasurer of the States:

No, I think that is laid out separately in the proposition.

Deputy J.A.N. Le Fondré:

Okay, thank you. Next one, can you confirm that the £466 million includes all fitout and equipment costs and basically the £466 million and all the figures within that will produce a fully operational hospital on day 1 of opening?

Treasurer of the States:

I will not say that in case it is day 2, but, yes, that is the ...

Deputy J.A.N. Le Fondré:

That is the principle, yes? So what I mean is there is not significant chunks being funded by the departments ...

Treasurer of the States:

No, it is not a shell, no.

Deputy J.A.N. Le Fondré:

Okay. What is the projected life of the assets, i.e. the hospital?

Treasurer of the States:

I think it is in the proposition working on the basis that we were looking at the ongoing lifetime costs over 60 years, that is probably excessive working within the bounds that equate to the length of the bond. It appeared elsewhere that someone suggested 25 years. We have done some forecasts based on lifetime costs over 60 years. Taking it to 60 years that is quite an ancient hospital. Who knows what healthcare looks like in 30, 40, 50, 60 years.

Deputy J.A.N. Le Fondré:

So what would your reasonable expectation be: 40 years, 30 years, 50 years?

Treasurer of the States:

Thirty, 40 years.

Director, Financial Planning and Performance:

For the building.

Deputy J.A.N. Le Fondré:

No, the equivalence, we would accept that. I think we have covered the point about the Public Finances (Jersey) Law.

Senator S.C. Ferguson:

So say it had a 30-year life and we have a bond for 40 years, we will carry on paying for it when you are talking about thinking about replacing the building?

The Minister for Treasury and Resources:

No, we are talking about 40 years for the building. Forty years for the building is what the expectation is. They are aligned.

Deputy J.A.N. Le Fondré:

How are we going to fund capital replacement and renewal through the life of the hospital? That will be things like equipment, maintenance, anything else that comes through. Is that all built into the funds?

The Minister for Treasury and Resources:

About £1.8 million a year, I think.

Director, Financial Planning and Performance:

It is a normal capital programme.

The Minister for Treasury and Resources:

Yes, normal capital programme.

Deputy J.A.N. Le Fondré:

How much?

Treasurer of the States:

The normal capital programme and the normal revenue programme.

Deputy J.A.N. Le Fondré:

Yes, sorry, I thought the Minister cited a figure. That is fine.

Treasurer of the States:

That was costs related to the current hospital.

Deputy J.A.N. Le Fondré:

Right, okay, I thought you cited a figure, Minister, that was all.

The Minister for Treasury and Resources:

Sorry?

Deputy J.A.N. Le Fondré:

Did you say a figure?

The Minister for Treasury and Resources:

No, I was talking in relation to the existing.

Deputy J.A.N. Le Fondré:

Okay. One question, Minister. We accept that the estimated inflation forecast has gone down, correct?

The Minister for Treasury and Resources:

I am sure that is right, yes.

Deputy J.A.N. Le Fondré:

Yes, good. At the start of the year you claimed, Minister, that the rise in construction costs due to inflation were a key reason not to delay the January debate. Would you like to elaborate on your comments you made in January?

The Minister for Treasury and Resources:

Figures go up and down and they will continue to go up and down, I have no doubt. Particularly in this very volatile environment that we are living in at the moment. There have been some big shocks recently that you will be familiar with, in regard to, for example, sterling. Which has caused import costs to rise and the construction industry has been impacted or was impacted by that at one point.

Deputy J.A.N. Le Fondré:

But obviously the forecast for the moment is relative to the assumptions that were in the forecast that inflation costs would be lower than originally predicted.

The Minister for Treasury and Resources:

Yes, there are many factors that come into ...

Deputy J.A.N. Le Fondré:

I have one question left. Kevin, are you happy? Are we all happy? Good. Well, really I think just to try and nail it down, the figure that has been used most commonly in association with the future hospital costs for £466 million. But can you confirm that is a worst-case scenario at the end of the day and that is not the cost that is being worked to?

The Minister for Treasury and Resources:

That was a cost, a prudent cost, put in at the early stages when there were an even larger number of uncertainties and it includes, or it certainly did at the beginning, a substantial contingency figure. As I have made clear, our views are that the contingencies are there not to be spent but to be used in exceptional circumstances.

Deputy J.A.N. Le Fondré:

Would it be fair to say only exceptional circumstances?

The Minister for Treasury and Resources:

I think as I phrased it was probably about right.

Deputy J.A.N. Le Fondré:

Okay, I think on that basis we can conclude the hearing. Thank you very much, Minister, and your team. Where we have asked for information, we will just double check what we have but if we do have any further requests can we try and get it really by Wednesday so we do not have anything outstanding. Thank you very much. I call the hearing to an end.

[12:29]