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Guernsey—Crown Dependency of the United Kingdom: Assessment of the Supervision and Regulation of the Financial Sector Volume II—Detailed Assessment of Observance of Standards and Codes

This detailed assessment of observance of standards and codes in the financial sector of **Guernsey** in the context of the offshore financial center program contains technical advice and recommendations given by the staff team of the International Monetary Fund in response to the authorities of Guernsey's request for technical assistance. It is based on the information available at the time it was completed in **October 2003**. The staff's overall assessment relating to financial sector regulation and supervision can be found in Volume I. The views expressed in these documents are those of the staff team and do not necessarily reflect the views of the government of **Guernsey** or the Executive Board of the IMF.

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ASSESSMENT OF THE SUPERVISION AND REGULATION OF THE FINANCIAL SECTOR

Volume II: Detailed Assessment of Observance of Standards and Codes

Guernsey

October 2003

Contents Page

Text Tables

ACRONYMS

AML	anti-money laundering
AML/CFT	anti-money laundering and combating the financing of terrorism
APM	Annual Prudential Meeting
CFT	combating the financing of terrorism
CIS	collective investment scheme
CISX	Channel Islands Stock Exchange
COBO	Control of Borrowing Ordinance, 1959
Committee	Advisory and Finance Committee
CP	Core Principle
CSP	company service provider
CTP	common trading practices
DT	drug trafficking
EC	European Community
EU	European Union
FIS	Financial Intelligence Service
FNCC	Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules, 1998
FSB	Financial Services Business
FT	Financing Of Terrorism
GAAP	Generally Accepted Accounting Principles
GAAS	Generally Accepted Auditing Standards
GFSC	Guernsey Financial Services Commission
GFSC Law	Financial Services Commission (Bailiwick of Guernsey) Law, 1987, as amended
IAIS	International Association of Insurance Supervisors
IB Law	Insurance Business (Bailiwick of Guernsey) Law, 2002
IMII Law	Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002
IOSCO	International Organization of Securities Commissions
KYC	know your customer
LBG	limited by guarantee
LEG	Legal Department
LI Code	Licensed Insurer's Code of Conduct
LOC	letters of credit
MFD	Monetary and Financial Systems Department[1]
ML	money laundering
MOU	Memorandum of Understanding
OGBS	Offshore Group of Banking Supervisors
PCC	protected cell company
POC	proceeds of crime

[1] The IMF's Monetary and Exchange Affairs Department (MAE) was renamed the Monetary and Financial Systems Department (MFD) as of May 1, 2003. The new name has been used throughout the report.

POI Law	Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended
PQ	personal questionnaire
ROSCs	Reports on Observance of Standards and Codes
SIS	shared intelligence system
SRO	self-regulating organization
States Assembly	Guernsey Parliament
STR	suspicion transaction report
TSP	trust service provider

I. BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

A. General

1. This assessment of Guernsey's compliance with the Basel Core Principles for Effective Banking Supervision has been completed as part of the IMF Offshore Financial Sector (OFC) assessment program. Completion of a formal assessment serves several purposes. First, it benchmarks the current state of banking supervision, recognizing that there have been extensive changes in the last years. Second, it suggests a number of further improvements or changes. Thus, this report provides a key input for the development of an action plan to move toward full compliance with the Core Principles. The assessment team[2] expresses its thanks to the staff of the Banking Division who cooperated in the completion of the assessment.

Information and methodology used for assessment

2. This assessment of the effectiveness of banking supervision was based on a review of the legal framework, both generally and as specifically related to the financial sector, the self-assessment of the Core Principles, and extensive discussions with the staff of the Guernsey Financial Supervision Commission (GFSC) the external auditors and the management of commercial banks.

Institutional and macroprudential setting, market structure overview

3. There are 69 banks licensed to take deposits under the Banking Supervision (Bailiwick of Guernsey) Law, 1994. These banks are subsidiaries or branches and come from Europe; Asia; the Middle East; North America; and South Africa. Total deposits stood at £71.8 billion at the end of September 2002, the largest source being fiduciary deposits.

4. Licensed banks carry out private banking services for nonresidents, corporate banking, deposit gathering for funding parent operations, and retail banking for the local population. Some banks also carry out custody work for mutual funds, and others provide banking services to the captive insurance sector.

[2] The assessment was undertaken by Marcel Maes and Jack Heyes (Consultants MFD).

5. Financial sector supervision is undertaken by the GFSC which was established as a statutory body under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as a unitary regulator responsible for the regulation of financial services business. The Advisory and Finance Committee of the parliament (States Assembly) is mandated to oversee the financial services sector and to monitor and act as the channel of communication with the GFSC.

6. The Banking Supervision Law, 1994, as amended, provides for the regulation of deposit-taking business. It gives the GFSC the ability to set out conditions for issuing licenses. The Law restricts the acceptance of deposits to licensed institutions and provides for the regulation and supervision of such institutions. It also gives the GFSC the ability to impose conditions on licensees, to give directions to institutions, and to provide for penalties for breach of the legislation and for the revocation of licenses.

General preconditions for effective banking supervision

7. The GFSC operates within a context of a generally strong legal and regulatory framework and effective implementation of supervisory processes. An effective licensing authority is in place supplemented by fair and equitable criteria to ensure a consistent approach is applied to permissible activities, ownership, and investment criteria. Prudential regulations and requirements compare favorably with international standards and best practices.

8. The GFSC applies an effective supervisory process that blends off-site assessment of internationally active banking organizations and regulatory agencies with a visitation program to confirm the results of the off-site assessment process. It is the policy of the GFSC to grant licenses only to banks or branches that have parent organizations with an acceptable international presence in accordance with criteria established by the Commission.

9. The GFSC has emphasized the importance and need for transparency of accounting policies and practices and conformance with international standards. Legal provisions are in place, which enable the GFSC to take regulatory action against a noncompliant bank.

10. The GFSC has a range of gateways to enable it to share information domestically and internationally.

B. Detailed Assessment

Table 1. Detailed Assessment of Compliance with the Basel Core Principles

Principle 1.	**Objectives, Autonomy, Powers, and Resources** An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks. Each such agency should possess operational independence and adequate resources. A suitable legal framework for banking supervision is also necessary, including provisions relating to the authorization of banking establishments and their ongoing supervision; powers to address compliance with laws, as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Principle 1(1)	An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks.
Description	The Financial Services Commission (Bailiwick of Guernsey) Law, 1987 (the FSC Law) and the Banking Supervision (Bailiwick of Guernsey) Law, 1994 (BSL) lay out the GFSC's objectives. The objectives and responsibilities of the GFSC are restated annually in appendix 1 of the GFSC's annual report. The GFSC is the sole agency in Guernsey responsible for banking supervision. The responsibilities are divided into "general functions and statutory functions." These are set out respectively in sections 2 and 3 of the GFSC Law. The general functions of the GFSC include: (a) to take such steps as it considers necessary or expedient for development and effective supervision of finance business in the Bailiwick; (b) to provide for the Advisory and Finance Committee or the Policy and Finance Committee of the States of Alderney or the General Purposes and Finance Committee of the Chief Pleas of Sark, when either of such committees so request, reports, advice and assistance on any matter connected with finance business; (c) to prepare and submit to the Advisory and Finance Committee or the Policy and Finance Committee of the States of Alderney or the General Purposes and Finance Committee of the Chief Pleas of Sark, either at the request of one of those committees or on its own motion, recommendations and schemes for the statutory regulation of finance business and generally for the revision of legislation appertaining to companies and other forms of business undertakings; (d) the countering of financial crime and of the financing of terrorism; and in this paragraph "financial crime" includes any offense involving – (i) fraud or dishonesty; (ii) misconduct in, or misuse of information relating to, a financial market; or (iii) handling the proceeds of crime; and "offense" includes an act or omission which would be an offense if it had taken place in the Bailiwick; and (e) all other such functions as the States may by Resolution assign to the Commission. In the exercise of its functions the GFSC may take into account any matter which it considers appropriate, but shall in particular have regard to:

	(a) the protection of the public interest, including the protection of the public against financial loss due to dishonesty, incompetence or malpractice by persons carrying on finance business; and (b) the protection and enhancement of the reputation of the bailiwick as a financial center. The GFSC's statutory functions include, inter alia, the regulation and supervision of deposit taking business. For the purposes of the GFSC's function in relation to the development of finance business in the Bailiwick (see above) the 2002 Amendment Law defines "development" to include, among other things, "without limitation:" "the establishment and ongoing support of bodies and organizations the functions of which include or are important or relevant to: (i) the development of finance business in the Bailiwick and of that sector of the Bailiwick economy which carries on finance business; (ii) the improvement of the infrastructure of or serving that sector of the Bailiwick economy which carries on finance business; (iii) the protection of the public; or (iv) the protection and enhancement of the Bailiwick as a financial center." Schedule 3 to the BSL sets out minimum criteria for licensing of banks. Various other regulations and guidance notes set out supplementary minimum prudential standards. These include: • Principle 1/1994/24 on large exposures; • guidance on verification of prudential returns (April 1998); • guidance on trilateral discussions (March 1997); • the Banking Supervision (Bailiwick of Guernsey) Regulations 1994 as amended; • the Banking Supervision (Accounts) Rules 1994; • guidelines to Banks and their Auditors issued under s1(a) and s1(b)(ii) of the Banking Supervision (Accounts) Rules, 1994; • Guidance Note 1996/1: Flows of Information To Parent Banks; • Guidance Note 1997/1 on Bank Auditor's Reports on GFSC returns used for prudential purposes; • Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism; • guidance to prudential and statistical returns; • Code of Conduct on deposit advertisements; • principles of conduct of finance business; • principles of conduct of derivatives business; • Code of Practice for banks; and • Guidance Note 2002/1 on Procedures for On-Site Visits to Overseas Operations of Guernsey Banks.

	• Principles for the Management of Credit Risk • Guidelines for Corporate Governance and Risk Management which is currently out for consultation and will be issued some time during August 2003. Problem bank situations have, to date, only arisen as a result of failure of the parents of Guernsey banks. In each case the GFSC has actively participated in deciding when and how to affect an orderly resolution of the problem. Examples of cases in Guernsey have included subsidiaries of the British and Commonwealth Merchant Bank and Baring Brothers & Co. The BSL was introduced in 1994 and was amended most recently in 2003. The GFSC has established an encompassing program to revise and update laws, regulations and the system for protecting depositors. In that context, the GFSC also conducted a detailed review of the compliance of the Bailiwick's law and the supervisory practices with the Basel Core Principles for Effective Banking Supervision. The GFSC reviews annually its performance against that plan. The regulatory structure in the island was also subject to a major review in 1998 by the UK home office ('Edwards Review'). The recommendations that were formulated have set in motion a change process. The GFSC is audited annually by external auditors and has undergone an internal audit by the States (of Guernsey) Audit Commission. The GFSC intends to employ the services of external audit firms to provide assistance in assessing internal audit and corporate governance issues. The GFSC's annual report is laid before the States (Parliament) of Guernsey each year and is available free of charge from the GFSC or on the web. The report details not just financial information but also the current approach to topical issues and the results of the GFSC's activities. The executives of the GFSC are answerable to the five non-executive commissioners who meet regularly and each have a particular expertise in financial services. Statistics on the size of the Guernsey banking sector are published at least quarterly. The annual report reproduces detailed data along with a summary and commentary. Regulated entities are required to produce audited accounts that are available to the public. The GFSC also works closely with the two other crown dependencies to achieve a consensus approach in the prevention of money laundering. The primary purpose is to ensure greater consistency, to address observations made previously by FATF and to commit to the Basel document entitled "Customer Due Diligence for Banks." A position paper entitled 'Overriding Principles for a Revised Know your Customer Framework' was issued in February 2002 and is now being discussed with the industry prior to a redrafting of the relevant Guidance Notes.
	Largely compliant.
Comments	The GFSC is to be commended for its continuous proactive attitude taken in order to enhance the Bailiwick's regulatory and supervisory regime and its endeavor to meet international standards. The GFSC also undertakes discussions with the industry on how to formulate guidance notes, which are critical in ensuring that implementation is practicable. The GFSC also identified the need to address the question of how the island's limited resources can be used more efficiently. As a first step, a survey of the finance sector is being undertaken with the objective of obtaining information which will inform the debate aimed at utilizing Guernsey's resources more efficiently by increasing the value added by the sector.

	The development function given to the GFSC may give rise to a possible conflict with its other functions. A regulator is called on from time to time to make difficult decisions affecting the finance sector or its individual members. It is therefore essential that the regulator's judgment or freedom of action should not be affected by other considerations. The team has not seen any evidence that the development function has indeed caused problems with conflicts of interest. The GFSC has assured the review team that in the event of a potential conflict, supervisory and regulatory duties would take precedence over the development function. The GFSC Law should establish safety, soundness, and integrity of the financial system as the objectives of the GFSC and eliminate "development" as one of the GFSC functions. The GFSC should be able to continue its support of the activities of the Training Agency that are consistent with the revised mandate.
Principle 1(2)	Each such agency should possess operational independence and adequate resources.
Description	In April 1986, the States (Parliament) of Guernsey resolved to establish the GFSC as a statutory body. The following year, 1987, the FSCL was passed and, on February 1, 1988, the GFSC came into being. According to section 4(1) of the FSCL, the GFSC is not a committee of the States, or a servant or agent of the States. The GFSC consists of five members. The policies and procedures pursuant to which they are appointed and removed are described in the law. The States elect the members from persons nominated by the Committee. Commissioners shall be persons having knowledge, qualifications or experience appropriate to the development and supervision of financial business in the Bailiwick. They are elected for a period of three years. The legal provisions as to the resignation and removal of the Commission members warrant their independence. The GFSC has explicit functions and responsibilities about advice and recommendations including those on the revision of legislation. It also has rule making powers. It is expected to consult with industry and others on much of its policy work. It is independently accountable for this work. This seems appropriate. However, a question arises for us under section 7 of the GFSC Law which provides that the Advisory and Finance Committee may, "after consulting the GFSC, give to the GFSC: (a) written guidance of a general character; and (b) written directions of a general character, concerning the policies to be followed by the GFSC in relation to the development and supervision of finance business in the Bailiwick and the manner in which any function of the GFSC is to be carried out." Fees paid by the finance sector fund the GFSC. Banks are required to pay this fee under a provision in secondary legislation (the Financial Services Commission (Fees) Regulations). In 2002 these fees were raised by more than 20 percent. The GFSC sets its own fees, after consultation with the relevant political bodies in the Bailiwick. During 2001, the GFSC commissioned a comprehensive review of staff terms and conditions of employment. The review covered a wide range of issues and led to a number of recommendations for change. All divisions have seen an increase in staff numbers during 2001 (total staff as at August 30, 2002 amounts to 75). The number of staff in the Banking Division has increased to ten. Five have been employed by the GFSC for more than five years, three have professional qualifications (including one Barrister) and six are graduates (three at master's degree level).

	The director has worked for the Bank of England for over 20 years including secondments in Bermuda as economic adviser to the Government of Bermuda (1974–1977) and Bahrain as an adviser to the Bahrain Monetary Agency (1982–1984). He has worked for the GFSC for five years. The deputy director has worked at the GFSC for 14 years including 7 years in the Investment Business Division and an 18-month secondment to a fund management company. Both the director and his deputy hold Masters degrees in Economics from British Universities. The deputy director is a Certified Fraud Examiner and is an affiliate of the Securities Institute. He is a member of the Associates Program of the Toronto International Leadership Center for Financial Sector Supervision. He has also attended the Basel Committees International Banking Supervisory Course and has received training from the U.S. Securities and Exchange Commission and the UK's Investment Management Regulatory Organization. Staff is encouraged to undergo relevant training. In 2001, the GFSC spent over £31,000 on training with the Banking Division spending £6,788. In addition, the Banking Division receives training either free of charge or at reduced rates when attending courses put on by bodies such as the Financial Stability Institute, the Toronto Center, the FDIC or the FSA. Access to all of the facilities of the Guernsey Training Agency is also available to the division and staff attend many of the courses put on through the agency free of charge. One member of the Banking Division is studying for an MSc degree through the Training Agency. The GFSC's budget for IT costs is more than adequate with 1999 seeing an entirely new computer system installed with PCs for all staff. In addition, heavy expenditure is made on software designed specifically for the GFSC and the GFSC subscribes to several databases (such as Lexus-Nexus and the SIS) (and the internet) to enable it to carry out adequate monitoring and intelligence gathering. The GFSC has a substantial travel budget. The Banking Division currently only has supervisory responsibility for banks in Guernsey, Alderney and Sark and for subsidiaries in Jersey and the Republic of Ireland. However, in 2001 supervisory visits have been made to group offices and head offices of Guernsey banks in Germany and Switzerland. During that year, supervisors have been visited in Jersey, Gibraltar, Switzerland, and the United Kingdom. The Banking Division is always represented at the annual meeting of the Offshore Group of Banking Supervisors and the biennial International Conference of Banking Supervisors. All of these visits are to enable the GFSC to ensure that the other regulators have sufficient information to carry out their consolidated supervision. They also provide useful intelligence on banking groups represented in both jurisdictions. There are no cost constraints on the Banking Division traveling to carry out supervisory on-site visits as this is a part of its statutory function and as such is an expense, which cannot be avoided.
Assessment	Largely compliant.
Comments	The Advisory and Finance Committee's power to give guidance and directions to the GFSC has the potential of intruding on its operational independence. It is recommended that the law be amended to remove these powers. Notwithstanding these comments we consider that broadly speaking the existing power of general guidance and directions has not affected the GFSC's operational independence. As to the staffing of the Banking Division the need for additional resources should be examined. The diversification and growing complexity of the financial products should thereby be acknowledged. The Banking Division, subsequently in June 2003, recruited an additional person. In addition, subsequent to the mission the division carried out a "zero-based" analysis of its staffing needs going forward taking account of the projected number of licensed banks. The existing GFSC manpower plan for 2003–2007 anticipates that over the period there will be a number of additional staff. The anticipated enhancement of the Banking Division's supervisory direction coupled through the need for a more in-depth visitation program will have to be considered in the allocation of the envisioned staff complement. More detail concerning

	the extended Banking Division supervisory direction is indicated in more detail under CP 16. The case for additional resources should benefit from an in-depth analysis of the supervisory objectives and the means needed to fulfill those objectives. The frequency and scope of the on-site visitations, which is pivotal in this issue, will be addressed in detail under CP 16. The Island will also need to continue to have due regard to other developments in international standards, whether arising from pronouncements by the international regulatory bodies or through other international initiatives.
Principle 1(3)	A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision.
Description	The BSL specifies that the GFSC is responsible for granting and withdrawing (revoking) banking licenses. If a person is aggrieved by a decision of the GFSC he may appeal under section 18 of the BSL to the Royal Court (of Guernsey) sitting as an Ordinary Court. The Banking Division regularly issues policy and guidance and there are provisions in the BSL for introducing guidance, principles and rules (by the GFSC) and regulations or ordinances (made by the States of Guernsey and/or its Advisory and Finance Committee) without the need to change the primary Law. The GFSC may impose conditions on bank licenses as it thinks fit (BSLs.9 (1). The amended BSL contains provisions for the GFSC to obtain information and documents BSL s25) and to enter premises in order to obtain that information and documents (BSL s26). In practice banks freely make all relevant information available to the GFSC and provide copies of documents when requested to do so. All banks have a condition imposed on their license requiring them to provide the GFSC with quarterly prudential returns and to inform the GFSC of material adverse developments. The suspension and removal of directors or officers is also addressed by s67A of the Companies Law. The application for a disqualification order by the Court can be made by the Advisory and Finance Committee, the GFSC, the Procurer, any corporate body of which the person in question is or has been an officer, a liquidator or creditor of the corporate body, or with leave of the Court, any other interested party. The person may be prohibited from being a director or officer of any company or any specified company, and from participating in, directly or indirectly, the management, formation or promotion of any company or any specified company.
Assessment	Compliant.
Comments	Pursuant to the provisions of the Human Rights (Bailiwick of Guernsey) Law, 2000 (the HRL), Guernsey is adopting the European Convention for the Protection of Human Rights and Fundamental Freedoms 1950 (the Convention) into domestic Guernsey law. The Convention contains various provisions, which are of particular relevance to the GFSC in the discharge of its responsibilities. These provisions include the following: • Article 6: Right to a fair trial; • Article 8: Right to Respect for Private and Family Life; and • The First Protocol-Article 1: Protection of Property. Article 6 states that "in the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law…" The GFSC has received clear legal advice that it should not be "judge and jury in its own cause." Guernsey has therefore resolved to establish a Financial Services Tribunal. The Tribunal has commenced by considering the cases of applicants for licenses under The Regulation of Fiduciaries, Administration Businesses and Company Directors (Bailiwick of Guernsey) Law, 2000 who are dissatisfied with GFSC decisions. However, the GFSC has introduced the concept of a Shadow Tribunal across all Divisions and cases where an Enlarged

	Assessment Committee cannot make a positive decision can, in the first instance, be heard by the Shadow Tribunal. The statutory establishment of the Tribunal will require an amendment to the legislation but, in the meantime, the Tribunal will be established on a voluntary basis and will be known as a Shadow Tribunal. An independent Chairman who ensures that the Tribunal will conduct itself in a strictly impartial manner chairs it. The Tribunal considers afresh the evidence relating to the application. Pending the establishment of a statutory tribunal and any consequent amendment to the FSC Law the tribunal will issue recommendations to the GFSC. The tribunal normally holds its hearings in public but will have the discretion to hold a hearing in private if it considers it appropriate in any particular case.
Principle 1(4)	A suitable legal framework for banking supervision is also necessary, including powers to address compliance with laws, as well as safety and soundness concerns.
Description	The BSL enables the GFSC to address compliance with laws by carrying out on-site visits, prudential meetings with management and analysis of monthly statistical and quarterly prudential and locational returns. Schedule 3 to the BSL sets out minimum criteria for licensing which include, inter alia, several criteria requiring banks to conduct their business in a prudent manner. The GFSC may not grant a banking license (BSL s6(2) or may revoke a banking license (BSLs8 (1)(a) if these minimum criteria are not fulfilled. The GFSC has unfettered and routine access to all bank's files and carries out file sampling techniques during on-site visits to banks. This includes the verification that banks meet internal rules and limits as well as external laws and regulations. The GFSC may take (or require banks to take) a wide range of remedial actions under the BSL if necessary. This includes imposing conditions on a license (BSLs.9) (there is no constraint on the nature of the condition which may be imposed); revocation of a license (BSLs8); give institutions directions (BSLs12); obtain information and documents (and gain entry to do so) (BSLs25 and 26); appoint inspectors (BSLs27); investigate suspected offenses (BSLs28).
Assessment	Compliant.
Comments	
Principle 1(5)	A suitable legal framework for banking supervision is also necessary, including legal protection for supervisors.
Description	The FSC Law, s22 provides that no member, officer or servant of the GFSC is personally liable in any civil proceedings in respect of anything done or omitted to be done in the discharge or purported discharge of any function (statutory or general) of the GFSC under the Law unless the thing is done or omitted to be done in bad faith. Similarly: The Financial Services Commission (Limitation of Liability) Ordinance, 1990; and The Protection of Investors (Limitation of Liability) Ordinance, 1990 made by the States in exercise of powers under s23 of the FSC Law together with BSL s55 and s57 of the Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law, 2000, The Insurance Business (Bailiwick of Guernsey) Law, 2002 (s93) and the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002 (s70) provide variously that no liability shall be incurred by the States, the Committee or the GFSC in respect of anything done or omitted to be done in the discharge of the GFSC's various statutory functions unless the thing is done or omitted to be done in bad faith. The GFSC has adequate financial resources to cover the costs of defending its actions and, under the FSC Law (s15) the GFSC may borrow from the government (States General Revenue Account) to assist it to carry out its functions. Following the coming into force of the FSC

	Amendment Law, 2002 the GFSC will additionally be able to borrow from any person provided that it may not borrow monies at any time to the extent that the aggregate amount outstanding by way of principle in respect of monies so borrowed would exceed one third of the GFSC's fee income for the preceding calendar year.
Assessment	Compliant.
Comments	
Principle 1(6)	Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Description	The GFSC is the only body responsible for the soundness of the Guernsey financial system. In carrying out these duties it shares information with government committees where appropriate and with Police, Customs and Excise and the Financial Intelligence Service. Cooperation and information sharing by the Banking Division is common and can take place under the following pieces of legislation: **The BSL** The BSL provides for the disclosure of information by the GFSC of bank information for the purpose of enabling or assisting a relevant supervisory authority in a country outside the Bailiwick to exercise its supervisory function (see s44). **The FSCL** The FSC Law constitutes the GFSC and defines its regulatory functions. It provides for the disclosure of information to foreign countries in circumstances specified in the legislation (see s21). The Money Laundering (Disclosure of Information) (Guernsey) Law, 1995; the Money Laundering (Disclosure of Information) (Alderney) Law, 1998; and the Money Laundering (Disclosure of Information) (Sark) Law, 2001. These laws facilitate the disclosure of information to Guernsey law enforcement agencies in relation to the proceeds of criminal activity. They give statutory protection to an informant who would otherwise be subject to an obligation of secrecy, confidence or other restriction on disclosure of information. In addition regular meetings are held (at least annually) with the Financial Services Authority in the U.K. and communication with the U.K. regulators is frequent. Meetings are held with Swiss regulators annually and Dutch regulators regularly. Other offshore regulators (e.g., Bermuda, Gibraltar) are met at the Offshore Group of Banking Supervisors annual meeting. Close contact is maintained with the Isle of Man Financial Supervision Commission and the Jersey Financial Services Commission; an MOU has been signed with Jersey and the U.S. Federal Deposit Insurance Corporation. Regular meetings are held in Guernsey between the GFSC, Police, Customs and Excise, the Financial Intelligence Service and the office of the Attorney General in a forum called The Bailiwick Financial Crime Committee. Meetings are held with senior representatives from all of these bodies regularly. Financial Crime Group meetings are also held regularly between individuals from each of these organizations at an operational level. The Financial Crime Group reports to the Bailiwick Financial Crime Committee. There is also a Guernsey Terrorist Finance Team, which includes representatives of the GFSC, the Financial Intelligence Service, Customs and Excise, Police Special Branch and the Attorney General's office. Finally, the three Crown Dependencies (Jersey, Guernsey and the Isle of Man) meet regularly at meetings attended by senior representatives of the three Islands' Police, Customs and Excise, FIUs, Attorneys General and commissions.
Assessment	Compliant.
Comments	

Principle 2.	**Permissible Activities** The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined, and the use of the word "bank" in names should be controlled as far as possible.
Description	"Bank," "banking license," "deposit" and "deposit-taking business" are all clearly defined in the amended BSL. Section 37 of the BSL prohibits persons carrying on business in the Bailiwick from describing himself or so holding himself out, so as to indicate or reasonably be understood to indicate (whether in English or any other language) that he is a bank, banker or carrying on a banking business unless he has a license under the BSL or he has permission from the GFSC. In addition, any Guernsey company wishing to use a name that would reasonably be taken to indicate that it is a bank or banker or is carrying on banking business would have to apply under Control of Borrowing Ordinances to the GFSC for permission to incorporate or, under Company Law, for permission to change its name. (The same is true of any financial term.) Any use of 'bank' or a similar term in a name would be referred to the Banking Division for permission under BSL. The BSL states that no person shall accept a deposit in the course of carrying on a deposit taking business except under the authority of a banking license. However, banking licenses do not specify which particular activities are permissible for each bank. The GFSC follows other common law jurisdictions (such as the UK) in this matter. Section 37 of the BSL states (inter alia): "(1) No person carrying on any business in the Bailiwick, other than a licensed institution, a person specified in paragraph 2, 3, 4, or 5 of Schedule 1 or a person who has first obtained the permission of the GFSC in that behalf under section 38 and who is acting in accordance with the conditions of that permission, shall so describe himself or so hold himself out, as to indicate or reasonably be understood to indicate (whether in English or any other language) that he is a bank or banker or is carrying on a banking business. (2) No person carrying on any business in the Bailiwick, other than a licensed institution, a person specified in paragraph 2, or 3 of Schedule 1 or a person who has first obtained the permission of the GFSC in that behalf under section 38 and who is acting in accordance with the conditions of that permission, shall use any name which indicates or may reasonably be understood to indicate (whether in English or in any other language) that he is bank or banker, or is carrying on a banking business."
Assessment	Compliant.
Comments	
Principle 3.	**Licensing Criteria** The licensing authority must have the right to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the banking organization's ownership structure, directors and senior management, its operating plan and internal controls, and its projected financial condition, including its capital base; where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.
Description	When granting a license, or any time thereafter, the GFSC may impose such conditions as it thinks fit (s9 of the BSL). There is only one type of bank license: this is unrestricted as to what the bank can do so long as it has the appropriate systems, expertise and controls in line with the BSL and the Code of Practice. There is only one category of banking license so banks are licensed to conduct banking business with local residents and overseas residents alike. There is no special category of license which restricts activity to offshore business only.

	The GFSC has specific powers to impose on banking licenses conditions which (BSL s9(4)(g): "require the furnishing to the Commission, at such times, intervals, and places as may be specified by the Commission, of such information and documents, and of accounts of such description, in such form and containing such information and particulars, as may be so specified." Applicants for a banking license have to transmit information as to the group structure, staff and management, financial information and business plan, external funding and comfort letter. In meeting its policy of permitting only established banks of high reputation and standing to establish in Guernsey, the GFSC ensures that major shareholders, ownership structure, and source of capital are transparent. Schedule 3 to the BSL sets out minimum criteria for licensing which include, inter alia, several criteria requiring banks to conduct their business in a prudent manner. The GFSC may not grant a banking license (BSL s6 (2) or may revoke a banking license (BSLs8 (1) (a) if these minimum criteria are not fulfilled. The criteria are consistent for both issuing licenses and ongoing supervision. The same staff at the GFSC carries out both activities. Section 8 of the BSL states that in considering whether to revoke a banking license failure to meet the criteria established in schedule 3 to the BSL may be a valid reason to revoke. The minimum criteria for licensing banks outlined in schedule 3 to the BSL includes the following headings: • Integrity and skill; • Economic benefit; • Directors etc., to be fit and proper persons; • Business to be directed by at least two individuals; • Composition of board of directors; and • Business to be conducted in prudent manner. The GFSC makes these criteria freely available. Copies of the BSL are included as an appendix to the Banking Guide and are available on the GFSC website. . The fit-and-proper criteria have also been published in GFSC's Annual Reports and Financial Statements and are also on the website. By requiring banks to comply with these criteria the GFSC is ensuring that the banks' structures are such that they do not hinder effective supervision. A bank without appropriate legal and management structures would not meet these criteria. The Code of Practice for Banks (September 9, 2002) sums up sound principles to be observed by banks regarding integrity, know your customer, competence and effective management, credit procedures, trading procedures, risk management, responsibilities of the board of directors, audit, capital adequacy and co-operation with regulatory bodies. All Guernsey incorporated banks are required to keep a minimum risk asset ratio of at least 8 percent (most have higher minima) calculated in accordance with the Basel Capital Accord. The overall risk asset ratio for Guernsey subsidiary banks as at the end of 2001 was approximately 20 percent. This is subject to an absolute minimum capital policy requirement of £1million upon incorporation. All but two Guernsey banks have capital over £5m. The two, which have less capital, are inactive and have risk asset ratios of 18 percent and 122 percent. All managers, directors, money laundering reporting officers and company secretaries of banks are required to complete a detailed personal questionnaire (form PQ) including questions on personal details, relationship with the bank (and with former employees and other third parties),

	experience, qualifications, other business interests and good reputation and character. The GFSC uses the information declared in forms PQ and consequential checks on the information (and the individual) to ensure that the requirements of schedule 3, paragraph 3 of the BSL are met prior to that person carrying on his or her duties. A detailed business plan and application form must be submitted to and approved by the GFSC prior to the licensing of a bank. These are examined carefully to ascertain, inter alia, that corporate governance will be effective and appropriate and that the plans are acceptable and achievable. The application form requires banks to provide a full account of how the applicant will satisfy itself that any possibility of money laundering will be avoided. Procedures for assessing applications require an assessment of the system of corporate governance to be in place. The business plan submitted to the GFSC and early meetings with representatives of the shareholder / head office will ensure that operational policy / procedures, internal control and oversight are adequate and reflect the scope and degree of sophistication of the proposed activities of the bank. This is explicitly stated in Banking Division procedures. The application form requires a business plan to include "an outline of the nature and scale of the proposed business, plans for the future development of that business, and particulars of the arrangements for the management of that business. The operational structure outlined in the business plan should include, inter alia, adequate operational policies and procedures, internal control procedures and appropriate oversight of the bank's various activities including management of the bank's risk. The operational structure should reflect the scope and degree of sophistication of the proposed activities of the bank" (q. 4(c)(I) of form BA/1). The application requires latest audited accounts of the parent bank (shareholder) and (if different) of the ultimate parent organization. It also requires a three-year projection of estimated profits / tax and a three-year projection of the balance sheet. It also asks for details of external funding. All of this is analyzed by the GFSC as part of the application process. As a matter of course and policy the GFSC always requires prior consent of the home country supervisor prior to granting a license to an applicant for a banking license. Section 8(1)(d) of the BSL states that the GFSC may revoke a bank's license if: "The Commission has been provided with false, misleading, deceptive or inaccurate information by or on behalf of the institution or, in connection with an application for a banking license, by or on behalf of a person who is or is to be a director, controller or manager of the institution." The GFSC routinely requires "letters of comfort" from shareholders of Guernsey banks. The application form also asks for details on external funding guarantees, indemnities or other commitments given to the applicant for a license. In the amended BSL (s36C) requires banks to review annually whether any activity has been entered into in the course of the bank's business in respect of which no director of the bank has a sound knowledge. If this review identifies any shortcomings in this respect then the bank is required to immediately report the shortcomings or deficiencies to the GFSC together with details of the steps it proposes to take to remedy the position. The progress of new entrants in meeting their business and strategic goals and their ability to meet supervisory requirements are monitored through monthly statistical and quarterly prudential reporting along with annual prudential meetings with the bank's senior management and on-site visits where discussion is held with bank management and their staff. In the past the concept of administered or managed banks has also been promoted. The objective was to allow new entrant banks to operate a relatively simple spread of business from Guernsey without incurring the full cost of essential overheads: the administering banks

	providing the administration on a cost-effective basis. In the past, seven banks, which started out as administered banks, have evolved into stand-alone banks with their own full staff. Hence the administered bank concept in some cases has allowed banks to start a business slowly and then take a decision whether they wish to fully support it and go independent of the original administrator. At the time of the review there were seventeen managed banks (out of sixty-nine in total). Twelve are subsidiaries and five are branches of foreign banks. Managed banks are subject to the same legal and supervisory process. The policy for new entrants from 2002 is that a branch manager or managing director should be employed directly by the banking group (i.e., not seconded from the administering bank) and should be resident in the Bailiwick.
Assessment	Compliant.
Comments	
Principle 4.	**Ownership** Banking supervisors must have the authority to review and reject any proposals to transfer significant ownership or controlling interests in existing banks to other parties.
Description	"Significant shareholder" and "shareholder controller" are defined in the BSL: "For the purposes of this Law, a "significant shareholder," in relation to an institution, means a person who, alone or with associates, is entitled to exercise, or control the exercise of, 5 percent or more but less that 15 percent of the voting power in general meeting of that institution or of any other institution incorporated in the Bailiwick of which that institution is a subsidiary." "Shareholder controller," in relation to an institution, means a person who, alone or with associates, is entitled to exercise, or control the exercise of, 15 percent or more of the voting power in general meeting of that institution or of any other institution of which that institution is a subsidiary." S23(1) of the amended BSL states: "A person who becomes a significant shareholder in relation to a licensed institution incorporated in the Bailiwick shall, within a period of 14 days immediately following the day of that event, give notice in writing of the event to the Commission." S14(1)of the BSL states that: "No person shall become a shareholder controller or an indirect controller of a licensed institution incorporated in the Bailiwick unless he has notified the Commission in writing of his intention to become such a controller and the Commission has notified him in writing that there is no objection to his becoming such a controller." S14(3) of the BSL states: "The Commission may serve notice of objection under this section if it is not satisfied that the person concerned is a fit and proper person to become a controller of the description in question of the licensed institution; (a) that the person concerned is a fit and proper person to become a controller of the description in question of the licensed institution; (b) that the interests of depositors and potential depositors of the licensed institution would not in any other manner be threatened by that person becoming a controller of that description; or (c) without prejudice to paragraphs (a) and (b), that, having regard to that person's likely influence on the licensed institution as a controller of the description in question, the criteria of Schedule 3 would continue to be fulfilled in relation to that institution or, if any of those criteria is not so fulfilled, that that person is likely to undertake remedial

	action." As all Guernsey banks are 100 percent subsidiaries of existing overseas banking groups it is clear who is the shareholder of Guernsey banks and any change in significant shareholder (or shareholder controller) will be transparent (as it will be a matter of public record in the parent bank's jurisdiction and be announced to shareholders) as well as being notified to the GFSC. The Banking Division undertakes periodic surveys to confirm the ownership of all Guernsey banks. Shareholders of Guernsey banks are also identified in the bank's annual audited accounts and are discussed at prudential meetings.
Assessment	Compliant.
Comments	
Principle 5.	**Investment Criteria** Banking supervisors must have the authority to establish criteria for reviewing major acquisitions or investments by a bank and ensuring that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Description	The Banking Division undertakes periodic surveys to confirm which subsidiaries banks have and this information is also drawn from banks' audited accounts. Schedule 3 to the BSL includes ample minimum criteria for licensing by which to judge individual proposals. For example, the first three sub-paragraphs of paragraph 6 of schedule 3 state: "6. (1) The institution conducts or, in the case of an institution which is not yet carrying on deposit-taking business, will conduct its business in a prudent manner. (2) An institution shall not be regarded as conducting its business in a prudent manner unless it maintains or, as the case may be, will maintain a capital base (a) of an amount commensurate with the nature and scale of the institution's operations; and (b) of an amount and nature sufficient to safeguard the interests of the institution's depositors and potential depositors, having regard to the particular factors mentioned in sub-paragraph (3) and any other factors appearing to the Commission to be relevant. (3) The particular factors mentioned in sub-paragraph (2)(b) are- (a) the nature and scale of the institution's operations; and (b) the risks inherent in those operations and in the operations of any other institution in the same group so far as capable of affecting the institution." The GFSC verifies that any new acquisitions and investments do not expose the bank to undue risks or hinder effective supervision. This is part of the process carried out by the GFSC in considering whether the bank still complies with the minimum criteria as set out in schedule 3 to the BSL. It is also part of the procedures for approving large exposures if such an acquisition were to be a large exposure. Large investments are also apparent from quarterly prudential data collected from banks. Significant changes in volume or the nature of such investments would be queried as part of the analysis of such returns. Investments over 25 percent of the capital base of a bank must be notified to the GFSC in advance. However paragraph 10 of the Principle 1/1994/24 states: "If an exposure which exceeds 25 percent of capital base has been entered into without prior notification to the Commission notification must be made within two working days of entering such an exposure. A bank would not be expected to enter such exposures without notification unless the nature of the business is such that prior notification would be commercially disadvantageous but it would be expected that such possible

	circumstances are discussed with the Commission and outlined in the bank's large exposures policy." Large exposures of more than 10 percent of a bank's capital base are reported quarterly in arrears on form BSL/1. There is also a condition imposed on all bank licenses that they: "should not establish a branch outside the Bailiwick or invest in any company, which after such investment would be a subsidiary, associate or joint venture without the prior consent in writing of the Commission." A breach of a condition imposed on a license under the BSL is an offense.
Assessment	Compliant.
Comments	
Principle 6.	**Capital Adequacy** Banking supervisors must set minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. For internationally active banks, these requirements must not be less than those established in the Basel Capital Accord.
Description	A condition is imposed on bank licenses requiring them to complete quarterly returns (Form BSL/1). These returns include specific prescribed minimum risk asset ratios for each bank. The BSL/1 Form is freely adapted from the Bank of England antecedents of the current FSA Capital Adequacy forms (BSD3) and from the current FSA Liquidity Returns. All the concepts and calculation methodology are the same as the UK. However, certain analyses and statistical items that are required to be reported in the UK are not relevant to the jurisdiction. The Capital Adequacy returns are substantially the same. Tier 3 capital is not completed for trading books because Guernsey banks, except one, do not have a material number of trading books. Similarly the GFSC does not require supplementary information on trading book counterparty risk, derivatives trading or commodity trading. Given the absence of market makers the equity position risk is not captured. Any bank falling below the minimum will call into question its ability to meet the minimum criteria for licensing in schedule 3 to the BSL (which includes a requirement to have sufficient capital commensurate with the nature and scale of the bank's operations (paragraph 6). All banks are required to keep a minimum risk asset ratio of at least 8 percent calculated by the method established in the Basel Capital Accord. The minimum risk asset ratio applied to a Guernsey bank reflects each bank's risk profile and that of its parent bank taking into account both on and off-balance sheet risks. As stated above, only one Guernsey bank has a material trading book. This has been confirmed from the results of questionnaires completed by each bank in 2002 (the Bank Trading Book Review). The GFSC has therefore decided not to routinely measure market risk but the bank with a material trading book has its prescribed minimum risk asset ratio set at a level to reflect the risk in the business (12 percent). The minimum risk asset ratio for all banks is 8 percent but all but two have higher minima. In addition, for all banks the current risk asset ratio measure does include the following: off balance sheet risks; foreign currency exposure, interest rate related contracts and foreign exchange related contracts. Being primarily intra-day positions and client trading, they only represent 1.19 percent of total weighted assets of the bank subsidiaries in Guernsey.

	Components of capital are defined clearly in the GFSC's quarterly prudential return (BSL/1) and the accompanying Guidance to Prudential and Statistical Returns. The measures of capital follow those laid down by the Basel Committee. Although it is rare for Guernsey banks to have subsidiaries with significant balance sheets, some do have nonbank subsidiaries with assets and these are consolidated into the calculation of the capital adequacy ratio. To date no Guernsey bank has had a banking subsidiary. The GFSC has a range of penalties at its disposal (such as imposing conditions on licenses and appointing reporting accountants or inspectors) but ultimately it may revoke a banking license if, inter alia, any of the criteria of Schedule 3 to the BSL are or have not been fulfilled. Breaching a condition imposed on a banking license is an offense under BSL. One of the criteria of Schedule 3 is that: "(2) An institution shall not be regarded as conducting its business in a prudent manner unless it maintains or, as the case may be, will maintain a capital base (a) of an amount commensurate with the nature and scale of the institution's operations; and (b) of an amount and nature sufficient to safeguard the interests of the institution's depositors and potential depositors, having regard to the particular factors mentioned in sub-paragraph (3) and any other factors appearing to the Commission to be relevant. (3) The particular factors mentioned in sub-paragraph (2)(b) are (a) the nature and scale of the institution's operations; and (b) the risks inherent in those operations and in the operations of any other institution in the same group so far as capable of affecting the institution." Banks are required to report quarterly to the GFSC on their risk asset ratios and their components and a sample of these returns are verified by external audit. The definition of capital is the same for all banks in Guernsey and it is consistent with the Basel Capital Accord. If capital falls below the minimum required for a bank, or approaches the minimum level for the risks taken by the bank, the GFSC would be aware of this through monthly and quarterly reporting. The GFSC makes it clear to a bank in such instances what remedial action is required. This is either to reduce the number of risk assets held or (more usually) a requirement for a capital injection (or subordinated loan) from the shareholders. During annual prudential meetings with banks the procedures and mechanism for monitoring levels of capital are discussed, in particular in cases where banks are operating close to their minimum prescribed risk asset ratio. This is a requirement of the Code of Practice for Banks, which requires banks to have an internal process to assess their overall capital adequacy in relation to their risk profile. In addition, the GFSC reviews quarterly returns produced by banks, which calculate a bank's risk asset ratio. These quarterly returns are verified on a sample basis (chosen by the GFSC in arrears) by external audit. In light of the potential for off-balance sheet, litigation and operational risk in many Guernsey banks (as a factor of operating in the field of private banking) the minimum risk asset ratio for a bank is 8 percent but most banks have minima prescribed at higher levels. There are 47 Guernsey banks that operate as subsidiaries. Only two have a prescribed minimum risk asset ratio of 8 percent. Seventeen have 10 percent; five have 11 percent; seventeen have 12 percent; three have 14 percent; one has 15 percent and two have 16 percent. For 2001 the weighted average risk asset ratio for the industry remained at 20.52 percent.

	No Guernsey bank has a subsidiary with a banking license. If a banking subsidiary were to be established solo and consolidated risk asset ratios would be calculated. The Guidance to Prudential and Statistical Returns states (par A (e) that, assets and liabilities of reporting banks and their subsidiaries/branches should be included. In the event of a banking subsidiary being established the GFSC would also require solo reporting for the licensed bank and its banking subsidiary. Bank branches of Guernsey banks established overseas submit solo returns also. The GFSC policy is for a bank to have at least £1million in capital. This is cited in the Guernsey Banking Guide: "It is likely that any new subsidiary (whether stand-alone presence or administered) would be required to have a net worth of not less than £1million." and is repeated on the GFSC's website. The amended BSL stipulates a minimum capital of 1 million pounds sterling for Guernsey banks." A legislative change, requiring a minimum capital of 1 million pounds sterling, is expected to take place at the end of 2002/early 2003.
Assessment	Compliant.
Comments	It is recommended that the GFSC monitors future developments of market risk. A specific capital charge should be introduced if significant changes of the present situation should occur.
Principle 7.	**Credit Policies** An essential part of any supervisory system is the independent evaluation of a bank's policies, practices, and procedures related to the granting of loans and making of investments and the ongoing management of the loan and investment portfolios.
Description	An independent internal evaluation of a bank's credit policies, practices and procedures is a requirement of the Code of Practice for Banks. During prudential meetings the make up of the bank's credit committee and reporting lines are discussed. In addition, the overall condition of the loan book and credit granting process is discussed as are the individual credit limits of management, local credit committees, and large exposures and staff discretionary limits. The practice is for the GFSC to confirm approval of very large loans from Head Office credit committee or to require a specific risk transfer letter from the parent bank. A certified minute, an internal memorandum or letter from a credit committee representative can evidence the confirmation being requested. The GFSC checks, during on-site visits, whether such decisions are made at managerial level. Also, the condition of investment portfolios is discussed at length as part of the visitation program focusing on credit risk particularly in periods of volatile markets. The expectation is that all this information is available to management to enable them to complete quarterly returns and answer questions at prudential meetings. The GFSC Code of Practice and the policy document on large exposures include comments on the need for banks to ensure that credit decisions are free from conflicting interests. For example, the policy document states: "Exposures to companies or persons connected with the lending banks, its managers, directors or controllers require special care to ensure a proper objective credit assessment is undertaken. Such exposures may be justified only when undertaken for the clear commercial advantage of the lending bank, and when they are negotiated and agreed in an arm's length basis." In addition, the Banking Division carries out on-site credit reviews of banks. This includes verifying that credit granting / investment criteria etc., are approved by the management and the board. Verification of the existence and application on sound credit risk policies and procedures takes place periodically during on-site credit reviews. An on-site credit review questionnaire has been developed for use in credit risk assessments.

	The Banking Division issued to all Guernsey banks a copy of the Basel Committee's paper "Principles for the Management of Credit Risk." A covering memorandum from the GFSC stated, inter alia, a statement that the Commission endorses the principles contained in the paper and expects banks to have taken account of them. It also stated that the extent to which banks have taken account of those principles will be reviewed when the Commission carries out on-site credit reviews. Access to information is freely available to GFSC staff and the ten largest exposures/nonbank investments and all large exposures are reported to the GFSC (along with the ten largest money market placements) quarterly. Lending officers are available during prudential meetings and on-site visits. They are questioned on their roles and procedures by GFSC staff on a case-by-case basis and during on-site credit reviews. Credit and investment portfolios are also reviewed during on-site credit reviews.
Assessment	Compliant.
Comments	Bank assets devoted to loans, advances and market loans as at year-end 2001 was approximately Stg. 5.3 billion or approximately 6.6 percent of the jurisdiction's total banking assets. The recently implemented and focused credit risk assessment visitation program has been designed to address the quality of a credit risk process. The visitation questionnaires are sound. Working papers supporting the visitation program and the management letters completed at the end of the visitation are reflective of the degree of risk noted. Required remedial action is followed up on a timely basis. The GFSC should be commended for the introduction of the credit risk focused on-site visitation program. However, the on-site credit risk assessment visitation program has been carried out under the direction of the Director, Banking Division. The Director in taking an active role in the process is using the on-site visitation process to provide training in credit risk assessment techniques and practices to subordinate staff. (See also comments re C.P. 8).
Principle 8.	**Loan Evaluation and Loan-Loss Provisioning** Banking supervisors must be satisfied that banks establish and adhere to adequate policies, practices, and procedures for evaluating the quality of assets and the adequacy of loan-loss provisions and reserves.
Description	See also comments C.P. 7 The BSL currently states in schedule 3: "(6) An institution shall not be regarded as conducting its business in a prudent manner unless it makes or, as the case may be, will make adequate provision for depreciation or diminution in the value of its assets (including provision for bad or doubtful debts), for liabilities which will or may fall to be discharged by it and for losses which it will or may incur." If a bank does not conduct its business in a prudent manner it fails to meet the essential for licensing under the BSL. The amended BSL requires banks to review, at least annually, their individual loans, asset classification and loss provisioning (including on and off balance sheet exposures). If this review identifies any shortcomings in this respect then the bank is required to immediately report the shortcomings or deficiencies to the GFSC together with details of the steps it proposes to take to remedy the position. Loan classifications including provisions are reported to the GFSC in form BSL/1 on a quarterly basis. The regulatory report includes on and off balance sheet exposures. The classification and provisioning policies are reviewed by external audit and discussed during on-site credit risk visitation programs.

	Provisions are analyzed off-site as part of the GSFC's bank risk assessment program. Banks are required, by a condition on their license, to report to the GFSC promptly, any loan loss provisions or write offs. The GFSC can raise the prescribed minimum risk asset ratio if it perceives a bank's risk profile has deteriorated. In order to meet paragraph 6 of schedule 3 to the BSL a bank will have to satisfy the GFSC that it is acting prudently and has adequate provisions given the risk profile of the loan book. If an on-site credit review brings to light sub-standard practice the GFSC requires a bank to take remedial action. The need for ensuring banks have the mechanisms in place to continually assess the strength of guarantees and the quality of collateral is a requirement of the Code of Practice for Banks. Principle 1/1994/24 also states that the GFSC requires banks entering into exposures greater than 10 percent of capital base to have a policy on such exposures. The GFSC requires banks to have taken account of the following in establishing policy: "the standing of the counterparty, the nature of the bank's relationship with the counterparty, the nature and extent of security taken against the exposure, the maturity of the exposure, and the bank's expertise in the particular type of transaction." (Principle 1/1994/24 para. 2)." Collateral and guarantees taken to support loans are discussed at prudential meetings and banks are expected to have close control over loan-to-value ratios. During periods of volatile markets this is particularly closely monitored. Impaired loans are defined in the Guidance to completing the quarterly return (see Guidance to lines 37.3 to 37.5). Banks are also required to report impaired loan values and write-offs in quarterly returns to the GFSC and in maturity analyses they are required to report overdue assets and liabilities. The need to reflect the net realizable value of collateral is a requirement of the Code of Practice. In addition, in the case of large exposures, Principle 1/1994/24 provides guidance on exposures secured by cash deposits including margin requirements where FX risk exists, right of set off, and the need for appropriate margin requirements where exposures are secured by market value based securities.
Assessment	Largely compliant.
Comments	Refer also to comments C.P. 7. As indicated, the GFSC has taken a constructive step in ensuring that banks establish and adhere to effective credit risk policies and procedures. The prescribed reporting requirements include the need for banks to report: (1) the quality of their loan portfolio in accordance with a specified risk rating system, (2) details of impaired loans, and (3) specific loan provisions allow for credit risk trends to be monitored on a regular and consistent basis. The introduction of the on-site credit risk visitation program adds to the off-site review process. The quality of the loan portfolios as reported by the industry indicated the following: Grade A – Satisfactory 98.7 Grade B - Watch List 1.2 Grade C - Substandard 0.1 Grade D - Loss 0.0 Total 100.0 The GFSC does not risk rate individual exposures as part of the credit risk visitation program. The on-site visitation focuses on the credit risk process. Nor do the audited financial statements make any reference to the integrity of risk ratings required to be reported to the GFSC.

	To add further value to the on-site credit review process the GFSC may want to consider extending the on-site review to include: • additional focus on the out of order reporting process; and, • the assessment of a sample of loans to confirm or otherwise the integrity of the bank's own credit risk rating system and ultimately the appropriateness of the provisioning methodology to ensure that deteriorating situations are recognized in a timely manner. The mission recognizes that in developing a more prescriptive approach to loan evaluation and provisioning due consideration has to be given to ensuring that the GFSC has staff capable of carrying out this type of specialized review. Additional training in this area will be required. Refer also to comments C.P. 7.
Principle 9.	**Large Exposure Limits** Banking supervisors must be satisfied that banks have management information systems that enable management to identify concentrations within the portfolio, and supervisors must set prudential limits to restrict bank exposures to single borrowers or groups of related borrowers.
Description	Principle 1/1994/24 (Para. 14) defines a "closely related counterparty." The requirement to refer to the GFSC in this definition allows the GFSC to exercise discretion in determining this on a case-by-case basis. This principle also prescribes exposure limits. Paragraph. 6 states: "A bank may not incur exposures which exceed 10 percent of capital base to individual counterparties or groups of closely related counterparties which in aggregate exceed 800 percent of the bank's capital base without prior agreement of the Commission." In addition, section 24 of the BSL prescribes the requirements of the Reports of Large Exposures. Key elements of the section include: ▪ A report to the GFSC is required prior to funding where the exposure would result in an exposure exceeding 25 percent of the capital base; and, ▪ The GFSC may require the institution concerned and any relevant subsidiary thereof to make such arrangements within such time as may appear to the GFSC to be desirable for the protection of the institution's capital base. The requirements included in this section of the BSL afford the GFSC with wide discretion in interpreting the definition on a case-by-case basis. In addition, the GFSC requires, in its quarterly prudential returns, all banks to report on bank exposures over 10 percent of capital base. The requirement to submit a return is a condition on banks' licenses. The ten largest interbank exposures must also be reported quarterly. The GFSC selects one quarterly return per annum from each licensed bank, to be verified by the bank's external auditor against the bank's books and records. Any misreporting (including misreporting of large exposures) would be noted by auditors and included in their report which is copied to the GFSC. Banks are also required to report large exposures to the GFSC quarterly. In this way the GFSC ensures that the 10 percent and 25 percent limits have not been breached. Geographical statistics for all assets (and liabilities) are provided to the GFSC quarterly.
Assessment	Compliant
Comments	

Principle 10.	**Connected Lending** In order to prevent abuses arising from connected lending, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.
Description	BSL defines a related party at s25(6) as: "a 'related company,' in relation to an institution, means any body corporate (other than one which is a group company in relation to that institution) in which that institution holds for a significant period a qualifying capital interest for the purpose of securing a contribution to that institution's own activities by the exercise of any control or influence arising from that interest." Principle 1/1994/24 (Para.16) clearly defines "A connected counterparty**"** in annex 1 of the Document. Para. 17 of the Principle affords the GFSC discretion in making judgments about the existence of connections between the banks and other parties. The GFSC has prescribed in Principle 1/1994/24 limits on exposures to connected parties. The Principle states: "Exposures to companies or persons connected with the lending bank, its managers, directors or controllers require special care to ensure a proper objective credit assessment is undertaken. Such exposures may be justified only when undertaken for the clear commercial advantage of the lending bank, and when they are negotiated and agreed on an arm's length basis. The Commission will examine particularly closely all exposures to companies or persons connected to a lending bank and will deduct them from the bank's capital base if they are of the nature of a capital investment or are made on particularly concessionary terms." Principle 1/1994/24 (Para. 8) also emphasizes that situations involving connected lending with the lending bank, its managers, directors, or controllers require special care to ensure a proper and objective credit assessment is undertaken. The GFSC retains the option, where appropriate, to deduct such exposures from the bank's capital base if the findings are of the nature of a capital investment or are made on particularly concessionary terms. See also comments C.P. 9 for the process in place to verify the accuracy of the information contained in the regulatory reports.
Assessment	Compliant
Comments	Going forward the GFSC may want to consider further augmenting existing legislation relating to related and connected party exposures by referring to prescribed limits.
Principle 11.	**Country Risk** Banking supervisors must be satisfied that banks have adequate policies and procedures for identifying, monitoring, and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining appropriate reserves against such risks.
Description	Principle 1/1994/24 states that: "The Commission does not believe that a common limit should be applied to the aggregate of banks' exposures to counterparties in the same country; nor does it consider it appropriate to publish guideline percentages for the acceptable level of exposure to counterparties in particular countries. There may be circumstances where the Commission will insist on a limitation on a bank's country exposure. Banks likewise will be expected to set limits for country exposures on the basis of their own risk assessments which should be set out in their policy. The nature of the exposure (for example, whether it is trade finance or longer term balance of payments finance) will be relevant in considering an acceptable level of exposure."

	Certain banks in Guernsey have had limits placed on their exposure to certain countries. This risk area is also addressed during on-site credit risk visitations. See C.P. 7 and 8 for the techniques and practices applied by the GFSC when assessing credit risk process. Transfer risk is identified in focused on-site credit reviews and reviewed in annual prudential meetings as part of the Banking Division's discussions with banks.
Assessment	Compliant
Comments	
Principle 12.	**Market Risks** Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor, and adequately control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposure, if warranted.
Description	The Code of Practice for Banks (September 9, 2002) requires banks to ensure that they have suitable policies and procedures related to the identification, measuring, monitoring and control of market risk. In addition, schedule 3 to the BSL states that: "An institution shall not be regarded as conducting its business in a prudent manner unless it maintains or, as the case may be, will maintain adequate accounting and other records of its business and adequate systems of control of its business and records." External auditors of banks are required (under s.3(2)(a) of the Banking Supervision (Bailiwick of Guernsey) Regulations, 1994) to communicate to the GFSC if they have reasonable cause to believe: "That any of the criteria specified in Schedule 3 of the law is not or has not been fulfilled, or may not have been fulfilled…" Where banks have a material-trading book, the GFSC requires the banks to instruct their external accountants to verify the adequacy of banks' policies and procedures. The general scope of the work to be carried out in this respect has been agreed upon with the Technical Committee of the Guernsey Society of Chartered and Certified Accountants. The GFSC meets with the auditors in order to finalize the scope of their review and the timetable for completion. This procedure has been applied on one occasion. The Code of Practice for Banks requires that banks set appropriate limits for various market risks, including their foreign exchange risk. Foreign exchange exposures are reported quarterly to the GFSC on form BSL/1 (which is verified on a sample basis in arrears by external auditors for each bank) and are discussed, where appropriate, at annual prudential meetings. The GFSC is given the power to impose a specific capital charge on market risk under the terms of s.6(2) of schedule 3 to the BSL which states: "(2) An institution shall not be regarded as conducting its business in a prudent manner unless it maintains or, as the case may be, will maintain a capital base (a) of an amount commensurate with the nature and scale of the institution's operations; and (b) of an amount and nature sufficient to safeguard the interests of the institution's depositors and potential depositors, having regard to the particular factors mentioned in sub-paragraph (2) and any other factors appearing to the Commission to be relevant." The external auditors of banks are required (under s.3 (2)(a) of the Banking Supervision (Bailiwick of Guernsey) Regulations, 1994) (the BSR), to communicate to the GFSC where they have reasonable cause to believe that any of the minima criteria for licensing specified in Schedule 3 of the GBL is not or has not been fulfilled, or may not have been fulfilled.

	These broadly defined criteria require bank management to have regard to the circumstances of the institution and the nature and scale of the operations. These systems are a matter-of-routine discussion during annual prudential meetings and on-site visits.
Assessment	Compliant.
Comments	The GFSC should be commended for its bank trading book review and the discussions undertaken with the external auditors in order to define the general scope document of the work to be carried out by them. Issuing additional specific guidelines or best practices papers on how to manage these risks should complete the existing framework. Reference could thereby be made to guidelines issued by the Basel Committee.
Principle 13.	**Other Risks** Banking supervisors must be satisfied that banks have in place a comprehensive risk management process (including appropriate board and senior management oversight) to identify, measure, monitor, and control all other material risks and, where appropriate, to hold capital against these risks.
Description	Schedule 3 of the BSL states that a bank "shall not be regarded as conducting its business in a prudent manner unless it maintains adequate systems of control of its business and records" (paragraph 6 (7). The Code of Practice includes a requirement that a bank must have an effective process of control for monitoring risks such as liquidity, interest rate, foreign exchange and operational risk. A liquidity gap report is required as part of the regulatory returns. The quarterly report also requires banks to report currency exposure and interest rate and foreign exchange-related contracts. Undrawn commitments and other off-balance sheet liabilities are also included in the quarterly liquidity report. Guidance on the completion of the quarterly return states in connection with the maturity analysis: "the Commission would not normally expect a maturity mismatch at one month of more than 20 percent." External accountants verify the accuracy of the regulatory report on a sample basis, annually. Audited financial statements contain tables providing interest rate sensitivity gap analysis, foreign exchange and interest rate contracts and currency exposure. Risk management reporting lines and processes are evaluated during on-site visitations. Capital requirements and liquidity guidelines are monitored as part of the off-site supervisory process.
Assessment	Largely compliant.
Comments	Section 7 of the Code of Practice, which has been updated and came in force 9 September 2002, sets out sound principles for practice covering the need for banks to have in place comprehensive risk management processes to identify, measure, monitor, and control material risks. In general, banks in this jurisdiction are not position takers. Banks are primarily deposit gatherers who normally place surplus funds with "group" members. To support off-site analysis the GSFC has required banks to complete an internal questionnaire designed to confirm or otherwise the GSFC's assessment of the trading risk appetite of banks. During annual prudential meetings the responses to the Trading Book questionnaire are reviewed. Where trading risk situations exist the GSFC has assessed the quality of trading risk management practices on a one-off basis. As indicated above, under s31 of the BSL, Banking Supervision (Accounts) Rules 1994 Reporting Accountants are required to report management's comments on the risk profile of banks as part of their presentation of the annual financial statements. A note to the financial statements covering this issue is provided, without audit.

	A gap analysis schedule of the bank's position risk is also required to be presented in the notes to the financial statements. As reported, external auditors verify the accuracy of the regulatory report on a sample basis, annually. This complimentary verification technique allows GFSC staff to confirm or otherwise the recommended gap management guidelines. In December 1999 the reporting requirements as prescribed in the BSL were reaffirmed in guidance notes to all banks based upon the rationale that greater transparency of financial information is an essential part of promoting greater reliance on the disciplines of the market place. As the on-site visitation program is extended to address safety and soundness issues the mission would recommend that the GFSC develop on-site visitation techniques and practices designed to confirm or otherwise the existence and application of an effective and comprehensive risk management process and control culture.
Principle 14.	**Internal Control and Audit** Banking supervisors must determine that banks have in place internal controls that are adequate for the nature and scale of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding its assets; and appropriate independent internal or external audit and compliance functions to test adherence to these controls, as well as applicable laws and regulations.
Description	The Companies (Guernsey) Law, 1994 as amended includes Part XI on directors. This includes a section on "liability of directors who misrepresent company position," "fraudulent trading" and "wrongful trading." More specifically in Guernsey (and English) law directors' responsibilities are prescribed as a matter of common law. In the BSL it states at s49: "Where an offense under this Law is committed by an institution and is proved to have been committed with the consent or connivance of, or to be attributable to any neglect on the part of, any director, chief executive, controller, manager, secretary or other similar officer of the institution or any person purporting to act in any such capacity, he as well as the institution is guilty of the offense and may be proceeded against and punished accordingly." The amended BSL requires banks to review, at least annually, the responsibilities and conduct of the bank's board of directors with respect to corporate governance principles. If this review identifies any shortcomings in this respect then the bank is required to immediately report the shortcomings or deficiencies to the GFSC together with details of the steps it proposes to take to remedy the position. The Code of Practice for Banks requires that: "The board of directors of banks is responsible for banks having in place internal controls that are adequate for the nature and scale of the bank's business." Schedule 3 of the BSL also includes the following minimum criteria for licensing: "Business to be conducted by at least two individuals"; and "Business to be conducted in prudent manner." Furthermore, the Banking Supervision (Bailiwick of Guernsey) Regulations, 1994 require Bank's auditors to communicate to the GFSC circumstances of a material nature that could adversely impact the ongoing viability of the Bank. Emphasis is placed on a mixture of off-site analysis and on-site prudential visitations at least annually. The prudential meetings are used to examine reporting lines, organizational structures as well as internal control and operational activities. During the course of these meetings the GFSC is able to reach an opinion on the quality of senior management as well as the quantity of

	resources available to sustain an effective process of control over the bank's operations. The GFSC requires there to be an external audit carried out by a competent audit firm for all banks incorporated in Guernsey. As Guernsey banks are all subsidiaries of international banks they are normally subject to internal audits on a regular basis from the Head Office of licensed banks. The GFSC meets with internal audit groups as required and addresses matters of significance raised by internal audit during annual prudential meetings and on-site visits. All external audit reports are copied to the GFSC. GFSC also reviews the annual management letter provided to the board of directors of a bank by external auditors as part of their "fairness" opinion on the financial statements. The quality of senior management and the board of directors are closely monitored by the GFSC. Section 22 of the BSL prescribes the need for a bank to advise the GFSC of changes in the content of the board of directors as well as senior management. The small population of banks and their proximity to the GFSC allows for close and ongoing contact to be maintained. The GFSC has issued for consultation a paper entitled "Guidelines for Corporate Governance and Risk Management" to all Guernsey Banks. This guideline when issued in final form is expected to articulate the GFSC's expectation of a sound corporate governance regime.
Assessment	Largely compliant.
Comments	As part of the evolution of the on-site visitation program, the Banking Division plans to extend the existing focused on-site visitation program to areas of assessment that will include an assessment of a bank's corporate governance regime and through this assessment process confirm or otherwise the existence of a sound and sustainable process of control. The Banking Division is to be commended for moving in this direction. The legislative change noted in the descriptive comments when promulgated will add further emphasis to the need for banks to have a sound corporate governance process in place at all times. The Banking Division is of the view that the planned legislative change would benefit from having a guideline developed that would more clearly articulate the GFSC's expectations of a sound corporate governance regime. The mission would support the development of such a guideline and would also suggest that as part of this process consideration be given to having senior management and the board of banks confirm compliance with the guideline on an annual basis.
Principle 15.	**Money Laundering** Banking supervisors must determine that banks have adequate policies, practices, and procedures in place, including strict "know-your-customer" (KYC) rules that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.
Description	Banks are required to comply with a range of laws designed to prevent and detect criminal activity and report suspicion of criminal activity to the Guernsey Financial Intelligence Service (FIS which is Guernsey's FIU) and, in some cases, the GFSC. These laws are: • the Money Laundering (Disclosure of Information) (Guernsey) Law, 1995; • the Money Laundering (Disclosure of Information) (Alderney) Law, 1998; • the Money Laundering (Disclosure of Information) (Sark) Law, 2001; • the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999; • the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 (the Regulations); • the Drug Trafficking (Bailiwick of Guernsey) Law, 2000;

	• the Terrorism (United Nations Measures) (Channel Islands) Order 2001; • the Al Qa'ida and Taliban (United Nations Measures) (Channel Islands) Order 2002; and • the Terrorism and Crime (Bailiwick of Guernsey) Law, 2002. In addition banks are required to comply with the GFSC's Guidance Notes on the Prevention of Money Laundering and Countering the Financing Terrorism (the Guidance Notes). These notes are designed to assist license holders in complying with the anti money laundering legislation by specifying best practices in this regard. The GFSC carries out on-site visits to ensure that banks are complying with these requirements. In 2000, 15 such on-site visits were carried out (covering 19 bank licenses), 19 in 2001 and, as at 31 July 2002, 22 have been carried out (covering 25 bank licenses). There are 69 licensed banks in Guernsey. During its program of on-site visits the GFSC verifies banks' compliance with the Regulations and the Guidance Notes. Sections 3 and 5 of the Regulations require banks to have obtained satisfactory evidence of identity for all applicants for business and have specific requirements for the retention of customer verification documents and customer documents. The Guidance Notes provide detailed guidance on these areas also. (See paragraphs 37–39 and 121–130). In addition, the GFSC (along with its Jersey and Isle of Man counterparts) has issued a Position Paper on a Revised Know Your Customer Framework, which provides further guidance in this area. This paper's status is a statement of best practice, which the GFSC expects banks to be moving towards. During its program of on-site visits the GFSC verifies banks' compliance with the Regulations and Guidance Notes. Section 6 of the Regulations requires banks to establish clear and comprehensive internal and external reporting procedures for suspicious transactions. The Guidance Notes provide detailed guidance on this area (see paragraphs 94 to 120). Appendix G and paragraph 139A provides examples of what might be considered to be unusual transactions and refers to cash withdrawals and deposits. On-site visits focus on unusual transactions and cash transactions are a matter for close scrutiny by the GFSC. Financial services businesses are also required by the Regulations (Regulation 7) and the Guidance Notes (131–133) to train staff in recognizing potentially suspicious transactions. By arranging courses (with the Training Agency and the FIS), the GFSC assists banks in fulfilling these requirements. The Guidance Notes also state: "(5) The Commission also actively encourages financial services businesses to develop modern and secure techniques of money management as a means of encouraging the replacement of cash transfers." So large cash deposits or withdrawals are unusual for banks. All banks are required by the GFSC to have a Money Laundering Reporting Officer. The Regulations require that banks identify a person as the reporting officer and provide the name to the GFSC and FIS (s.6(1). The Guidance Notes state: "…The Reporting Officer should be a senior member of staff with the necessary authority to ensure compliance with these Guidance Notes." The Guidance Notes require reporting of suspicion to the GFSC (as well as the FIS) in the circumstances laid out in Guidance Note 118. In addition there is close liaison between the GFSC's Banking Division, Enforcement Division, Policy and International Affairs Division and the Director and officers of the FIS and police and customs fraud officers.

	All banks also have a condition imposed on their licenses to report material adverse events to the GFSC. The GFSC regularly shares information related to suspected or actual criminal activities with both domestic and foreign financial sector supervisory (and law enforcement) authorities. This is carried out using the gateways contained in the Money Laundering (Disclosure of Information) Laws (MLDIs) section 44 of the BSL and section 21 of the FSC Law. In 1999, Guernsey had an Offshore Group of Banking Supervisors FATF-style Mutual Evaluation Report on the anti-money laundering system in Guernsey. It stated, inter alia, that "the standards set by Guernsey are close to complete adherence with the FATF's 40 Recommendations" Since that review, the Bailiwick has continued to improve and enhance its adherence to the FATF 40 Recommendations. A number of legislative, policy and operational changes have been made since 1999. In their Noncooperative Countries and Territories review of Guernsey in June 2000 FATF stated that the Bailiwick has "comprehensive anti-money laundering systems." They concluded that the Island was cooperative. The GFSC employs several people with specialist expertise on financial fraud and anti-money laundering obligations.
Assessment	Compliant.
Comments	The Bailiwick of Guernsey and the other Crown Dependencies have to be commended on their joint position paper entitled: "Overriding Principles for a Revised Know Your Customer Framework." It is acknowledged that the process set in train to move towards implementing the conclusions set out in the document has been started and the GFSC has discussed the paper with the industry. The GFSC is expected to amend its existing guidance notes on this matter in the near future.
Principle 16.	**On-Site and Off-Site Supervision** An effective banking supervisory system should consist of some form of both on-site and off-site supervision.
Description	The Banking Division carries out both on and off-site supervision. (See also comments C.P. 19) On-site visits are risk based with a panel (consisting of the Director, his Deputy and the Assistant Director) considering prudential inputs, feedback from the FIS (Financial Intelligence Service), copies of disclosures made by banks to the FIS and other information such as fraud incidents and operational problems. The target cycle is carry out an on-site visit to each bank once every two years with higher risk banks visited more frequently. Where other regulatory disciplines (Insurance or trust providers) are involved feedback is requested to assist with better understanding of the overall risk profile of the bank. Occasionally, staff from other divisions accompany the banking division during on-site visits where either their special knowledge is helpful or where that division wishes to carry out its own visit concurrently. Higher risk situations will result in re-visits within six to twelve months (or shorter if necessary). The program is dynamic and is responsive to new data. On-site visits can also improve understanding of a bank's basic business, which will provide input to the prudential process. Ad hoc meetings are held as situations require. On-site risk focused visitations, for particular business reasons have emphasized anti-money laundering (AML), KYC and account opening policies and practice. Credit risk reviews have been carried out in banks where lending is considered to be a significant business line. Proforma

	questionnaires are used for these visits and staff at various levels are interviewed. Customer files are examined as part of the on-site methodology. External auditors are used to determine that prudential and statistical data provided by banks is reliable and to examine trading books. Trilateral meetings are held as required. Off-site work includes annual prudential meetings with management (which actually take place at the bank's premises) and analysis of monthly and quarterly statistical and prudential returns. The quarterly prudential returns are verified, in arrears, on a sample basis by external auditors. Other off-site supervision includes monitoring media and the market place; exchanging information with other supervisors and law enforcement agencies and visits from head office personnel, directors, compliance officers, MLROs, external auditors, and visiting regulators. Analysis of quarterly prudential returns and audited accounts (with audit reports) provides information to check that banks meet their requirements for large exposures, capital requirements and loan provisioning. It also ensures that they are meeting their requirements to produce audited accounts in a manner and at a time determined by the GFSC. See also C.P. 18 for additional information on off-site supervisory activities.
Assessment	Largely compliant
Comments	The long-standing off-site supervisory process coupled with the Annual Prudential Meeting (APM) program has been effective. Feedback from the industry also confirmed that senior management of the Banking Division are respected for their understanding of the risk profile of the industry and other interests affecting the banking industry. The GFSC has made progress in its efforts to enhance the structure and approach to on and off-site supervision. Contributing factors to the enhanced supervisory process include: • A comprehensive manual covering on and off-site supervisory activities has been developed. The manual is also available to Banking Division staff through intranet facilities; • A standardized assessment and reporting process is in place for use when carrying out the annual prudential meetings and when completing the off-site analysis; • A portfolio approach has been put in place that in effect assigns responsibility for off-site supervision of a portfolio of banks to specific staff. As the on-site visitation process evolves it is expected that the portfolio approach will be expanded to include on and off-site supervision; • A risk rating system has been introduced for banks and is being applied on an ongoing basis. Senior officers of the banking division, in the form of a panel, review the risk ratings applied in order to ensure a quality control mechanism is in place when assigning individual risk ratings; • Detailed questionnaires have been developed for the two areas of on-site concentration which have been carried out to date (AML/Credit Assessment); • The existing technology platform provides for statistical comparisons to be made. Unusual items are followed up. A summary report is prepared on a quarterly basis outlining issues identified as part of the off-site analysis completed; and, • Existing reporting formats are standardized and focused. Production of reports and follow-up is timely. In the year 2000, the GFSC identified the need to ensure that licensed banks had an effective anti-money laundering regime in place. Since this date almost all Banks have had a special focus AML/KYC visitation. It is expected that all banks will have had an AML/KYC on-site visitation prior to the end of this calendar year. The APM process has been retained.

	The on-site AML/KYC work was well documented. Industry representatives and auditing firms also confirmed that the focused visitations were effective. The GFSC has also conducted follow-up visitations where the findings of the AML/KYC visitation programs revealed operational and control weaknesses. The mission welcomes the GFSC's recent emphasis on the assessment of the source and application of funds when completing AML/KYC assessments. Refer also to comments C.P. 8 regarding areas where the GFSC may want to consider when expanding their credit-review-visitation program. As a result of the focused visitation program, which was well founded, no full scope safety and soundness visitations have been carried out. For example, the effectiveness of the overall corporate governance regime in banks has yet to be subject to an independent assessment during visitations. In the mission's opinion the on-site visitation program must be expanded. The Banking Division shares this view. Significant risk areas should be assessed to confirm that an effective process of control exists throughout all areas of the bank's operations and that the corporate governance regime is reflective of the risk appetite and profile of the bank. The GFSC has indicated that as part of the evolution of the division it plans to develop a detailed methodology covering corporate governance and the overall process of control plus other risk areas as required. Despite the progress being made we are concerned that the GFSC may not be able to achieve their departmental objectives particularly in the area of on-site safety and soundness visitations. The visitation objective, that is to ensure that higher risk banks are subject to more in-depth visitations on a timely basis, may be difficult to achieve with the existing complement. Central to our concerns is that it appears that while the staff employed is well qualified and supportive of the directional statements being made, the Banking Division has a resource deficit. Extrapolating the estimated person days for scheduled on and off-site supervision developed by the Banking Division and taking into consideration the planned extension of on-site programs, it would seem to confirm that there will be a significant shortfall. Other issues that will have an impact on the effectiveness of the Banking Division include: • In general, feedback from the industry particularly feedback relating to the capabilities of senior management of the Banking Division was positive. However, there were some concerns raised regarding the ability of the States Advisory and Finance Committee's staff to assess some of the products and services (and the associated control practices being developed or already in place) in the industry; • There has been some new staff recruited to the Banking Division over the past twelve months. While recruited staff are well qualified they will need time and guidance to be able to assume their new accountabilities. In addition to a complement increment, the GFSC would benefit from adding a further degree of discipline to the on and off-site supervisory process. Examples of the types of additional discipline that the mission believe would add value to the process include: • Accelerate the plan to finalize the on-site examination methodology; • Training programs focused on the expectations of the enhanced on-site methodology would be of benefit. As well, training programs designed to address the dynamic knowledge gap that can occur as a result of the accelerated changes that have and continue to occur within the industry should be considered; and • The quality control or assurance process be formalized; and,

	In general, the mission is of the view that unless the Banking Division department is adequately resourced the progress made to date will not be sustained.
Principle 17.	**Bank Management Contact** Banking supervisors must have regular contact with bank management and a thorough understanding of the institution's operations.
Description	The APMs with directors, managers and, often, nonexecutive directors are held with all Guernsey-licensed banks. Operational matters such as strategy, group structure, corporate governance, performance, capital adequacy, liquidity, asset quality, risk management, and others are all discussed during those meetings. The GFSC achieves a thorough understanding of the banks and their activities through off-site surveillance, on-site reviews and regular (prudential and ad hoc) meetings. Furthermore, the deliberate close physical proximity of the GFSC to all the banks and their management allows the GFSC to monitor industry and systemic issues in a timely manner. The GFSC has imposed certain conditions on banks including: "there shall be no significant change in the nature of the business conducted without prior consultation of the Commission"; and "Senior management should notify the Commission as soon as they become aware of any material adverse development surrounding the bank's operations…." In addition, auditors are required to communicate to the GFSC on significant circumstances and or issues that come to their attention in the course of their audit work. The quality of management is assessed by personal contact and by requiring directors, company secretaries, money laundering reporting officers and managers reporting directly to the Board to complete and submit a Personal Questionnaire.
Assessment	Compliant
Comments	
Principle 18.	**Off-Site Supervision** Banking supervisors must have a means of collecting, reviewing, and analyzing prudential reports and statistical returns from banks on a solo and consolidated basis.
Description	The regulatory returns require statistical data, on and off balance sheet liabilities and assets, capital adequacy, liquidity, large exposures, loan loss provisioning, foreign and exchange rate related contracts, loan classification, staffing, gap positions and deposit currencies. Information on the geographical location of asset and liabilities is also required. Information is obtained on the scale of bank's trading books by each bank having to complete a questionnaire for the GFSC. Section 1(a) of the Banking Supervision (Accounts) Rules, 1994 state that audited accounts of Bailiwick of Guernsey incorporated banks must be: "containing at least the information (including notes and statements) set out in guidelines issued from time to time by the Commission." The GFSC has issued as guidelines covering proforma financial statements detailing precisely how audited accounts should be produced and include guidance on producing consolidated accounts. The Banking Supervision (Accounts) Rules, 1994 require that accounts for Bailiwick of Guernsey incorporated banks be submitted to the GFSC within 90 days of the banks fiscal year-end. A breach of these Rules constitutes an offense under the BSL. Returns are required to be signed by a person considered to be senior enough to commit the bank. Quarterly returns are verified annually in arrears on a sample basis by external audit. Standardized forms are used for regulatory reporting requirements.

	Inaccurate returns are required to be re-submitted if errors are significant. If returns are not completed accurately or there is deliberate misreporting, this could be constituted as a breach of the minimum criterion for licensing that bank. The amended BSL requires banks to review, at least annually, whether they have in place control systems which are effective to ensure – i. that all returns and other documents required by or under the BSL to be submitted to the GFSC are duly submitted; and ii. that any inaccuracies in any such returns and other documents are identified, corrected and reported to the GFSC expeditiously, And if this review identifies any shortcomings in this respect then the bank is required to immediately report the shortcomings or deficiencies to the GFSC together with details of the steps it proposes to take to remedy the position." The GFSC has not introduced a program that would include the possibility of fines being levied against banks for incomplete, inaccurate, or late regulatory returns. The GFSC has under section 25 of the BSL the power to obtain information and documents as required. Section 26 provides the right of entry by the GFSC to obtain information and documents. A five quarterly comparison of prudential returns is carried out along with a system that flags any movements in figures over a percentage (e.g., 10 percent) from quarter to quarter. Data is collected from all banks at the same dates which represent the same periods. This includes monthly and quarterly returns. Ratio analysis is also carried out. In addition, analysis of data on an ad hoc basis is often carried out and used as a factor to determine on-site planning. For example, an analysis of loan books of banks was used in 2001/2002 to plan the 2002 on-site credit reviews.
Assessment	Compliant.
Comments	The mission would suggest that the GFSC consider developing legislation or regulations that would allow the GFSC to fine banks that continually fail to meet reporting guidelines.
Principle 19.	**Validation of Supervisory Information** Banking supervisors must have a means of independent validation of supervisory information either through on-site examinations or use of external auditors.
Description	The process for planning on-site visitations is detailed in the Banking Division's Procedures Manual including guidance for on-site visits and required revisits. The manual allows for a consistent methodology to be applied. (See also comments C.P. 16). The guidance outlines the scheduling process following the annual risk assessment, requirements for the pre-visit analysis, evidence gathering, scoring, post visit analysis and on-site re-visits. As indicated, proforma questionnaires are used to assist with ensuring the application of a consistent methodology and quality control process. The Director and/or the Deputy Director review the findings and proposed correspondence emanating from an on-site visit. Supervisory work carried out by external auditors on behalf of the GFSC is always carried out under detailed guidance and scope from the GFSC. Only international audit firms with an appropriately skilled workforce in Guernsey will be used. In July 1996 Guidance was issued to auditors requiring them to report to the GFSC on the up streaming of information from banks to their parent organization. In February 1997 (and updated in April 1998) the GFSC issued Guidance on Verification of Prudential Returns for auditors to follow. In March 1997 Guidance on Trilateral Discussions was issued to auditors to cover the occasions when they are required to be present during meetings held between a bank and the GFSC. It also covers policy in connection with other relationships with auditors and reporting accountants. Trilateral discussions with individual banks are rarely held.

	The power to appoint reporting accountants is detailed in s5 (5) and s25 (1) of the BSL and the roles and responsibilities of reporting accountants will be laid out by the GFSC in a scope provided to the reporting accountant prior to the carrying out of the examination. All major accounting firms are represented in Guernsey and their partners are members of a U.K. professional body.
Assessment	Largely compliant.
Comments	The GFSC is to be commended for obtaining reasonable assurance through independent audit opinions which confirm the accuracy of regulatory reports. In addition, the letter required from external auditors indicating that nothing has come to their attention that would indicate noncompliance with sections of the Code of Practice adds further value to the supervisory process. An important degree of reliance is being placed on the work and opinions provided by external auditors. However, the GFSC has not put in place a process to monitor the quality of work carried out by external auditors in order to confirm or otherwise the reliance being placed on this source of regulatory support. The type of assurance sought may be able to be achieved if the GFSC was able to review the audit working papers supporting the opinion provided covering the correctness of regulatory returns or where appropriate, the work undertaken as part of the Reporting Accountant process. In discussions with representatives of the Guernsey Association of Chartered and Certified Accountants concerning the aforementioned subject, the representatives indicated that they understood the need for the GFSC to obtain the necessary quality assurance. They also indicated that they were willing to work with the GFSC to develop a methodology to achieve the desired results. The mission also believes that additional benefits can be achieved by the GFSC through having regular bilateral or trilateral meetings with external auditors. Bilateral meetings have in other jurisdictions been of benefit to supervisors when discussing systemic or industry trends or when developing policy issues (refer C.P. 12). Trilateral meetings can address the expectation of the supervisor on bank or topic specific issues and can be useful on an ad hoc basis.
Principle 20.	**Consolidated Supervision** An essential element of banking supervision is the ability of the supervisors to supervise the banking group on a consolidated basis.
Description	All activities of the banks are discussed during annual prudential meetings. Any investment, insurance or fiduciary business carried on by banks in Guernsey requires a license from the GFSC and that business is regulated by the GFSC. The Banking Division works closely with the other Divisions of the GFSC and is aware of the risks that those activities might bring to the bank. (An example is trust business carried out within a bank. The Banking Division monitors the risks to the bank surrounding such an arrangement). The risks of nonbanking activities carried out by the parent of a bank are also considered (in light of potential reputational risk to the group). Nonbanking risks in non-Guernsey subsidiaries are also closely monitored. Where activities of such subsidiaries are significant, accounts of subsidiaries are required and Guernsey management are expected to know the risks to the bank in their non-Guernsey entities. Bilateral discussions with regulators of subsidiaries of Guernsey banks are held where those subsidiaries are overseas. On-site visits are also carried out to overseas nonbank subsidiaries of Guernsey banks on a periodic basis. Under guidance issued under s1 (a) of the Banking Supervision (Accounts) Rules, 1994 banks are required to produce (and submit to the GFSC) annual audited accounts containing a consolidated balance sheet, consolidated cash flow statement, consolidated profit and loss account, consolidated statement of total recognized gains and losses and notes relating to the bank and its subsidiary companies. The GFSC measures capital on a consolidated basis and where subsidiaries have had large exposures they have been treated as large investment exposures of the bank.

	Section 25 of the BSL permits the GFSC, with the prior written authority of not less than two ordinary members (of the GFSC) to require information or documents to be supplied to the GFSC. See also comments C.P. 18. Sections 25(5) to 25(8) provide additional guidance on this subject. The GFSC measures capital on a consolidated basis. Where subsidiaries have had large exposures they have been treated as large investment exposures of the bank. The GFSC may impose conditions on a bank's license circumscribing a branch or subsidiary's range of activities. This has not yet been necessary given the limited activities of branches and subsidiaries of Guernsey banks. The amended BSL (S9(4)(h) gives the GFSC explicit power to prohibit, restrict or impose (limitations on the carrying on of deposit-taking business without the need to impose a condition on a bank's license.
Assessment	Compliant.
Comments	The GSFC has established MOUs with 12 regulatory bodies. The GSFC has adopted a policy that it will enter into a MOU when requested by another regulator. The need for a MOU is not a precursor to providing an exchange of information with a "home" or "host" regulator. While the key elements of the essential criteria are being applied the mission has recommended that the GFSC obtain on an annual basis confirmation from the "home" regulator that nothing has come to their attention that could impact the operations of the regulated bank. The format of the confirmation could parallel the confirmation requested as part of the licensing criteria.
Principle 21.	**Accounting Standards** Banking supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with consistent accounting policies and practices that enable the supervisor to obtain a true and fair view of the financial condition of the bank and the profitability of its business, and that the bank publishes on a regular basis financial statements that fairly reflect its condition.
Description	Forms BSL/1 (prudential returns including required capital calculation scheme) and MA/1 (Monetary Aggregates data) must be submitted within 28 calendar days of the reporting date. Form LOC/1 (Quarterly Locational Statistics) has to be submitted two months from the reporting date. In this connection all banks have the following condition imposed on their license that: "completed prudential returns are provided to the Commission and any other such similar routine returns that may from time to time be required. The Commission will on occasion require an institution to provide confirmation from an external auditor that prudential returns accurately reflect the business on the reporting date" The BSL also states (under schedule 3 – Minimum Criteria for Licensing) that: "(7) An institution shall not be regarded as conducting its business in a prudent manner unless it maintains or, as the case may be, will maintain adequate accounting and other records of its business and adequate systems of control of its business and records. (8) The records and systems described in sub-paragraph (7) shall not be regarded as adequate unless they are such as to enable the business of the institution to be prudently managed and the institution to comply with the duties imposed on it by or under this Law; and in determining whether those systems are adequate the Commission shall have regard to the functions and responsibilities in respect of them of any such directors of the institution as are described in paragraph 5." And that: "(1) Every person who is, or is to be, a director, controller or manager of the institution is a fit and proper person to hold that position.

(2) In determining whether a person is a fit and proper person to hold a particular position, regard shall be had to his probity, competence and soundness of judgment for fulfilling the responsibilities of that position, to the diligence with which he is fulfilling or likely to fulfill those responsibilities and to whether the interests of depositors or potential depositors of the institution are, or are likely to be, in any way threatened by his holding that position."

Furthermore, Guidance Note 1997/1 on Bank Auditors' Reports on GFSC returns used for Prudential Purposes recalls that the management of licensed institutions and bank auditors should be aware of s47 of the BSL regarding the knowing or reckless provision to the GFSC of information which is false or misleading in a material particular. This section is particularly relevant in underlining management's responsibility for the preparation and submission of returns and confirms the importance, which the GFSC expects management to attach to their preparation.

Section 31 of the BSL requires audited accounts to be made publicly available. In addition, the Banking Supervision (Accounts) Rules, 1994 state:

"1. In the case of a licensed institution incorporated in the Bailiwick –

(a) audited accounts of the institution containing at least the information (including notes and statements) set out in guidelines issued from time to time by the Commission shall be drawn up to dates at intervals not exceeding twelve months unless other arrangements have been specifically agreed in writing with the Commission.

(b) not later than three months after each date to which the said audited accounts are drawn up, except with the prior specific written consent of the Commission:

(i) a copy thereof shall be delivered to the Commission; and

(ii) either those audited accounts or abridged accounts containing at least the information set out in guidelines issued from time to time by the Commission shall be available to any person on request; and

(c) the auditor's report on the accounts of the licensed institution shall include, inter alia, statements on the following matters:

(i) the basis of the auditor's opinion;

(ii) whether, in the auditor's opinion, the accounts (and, in the case of group accounts submitted by a holding company, the group accounts) show a true and fair view and have been properly prepared in accordance with applicable accounting standards and also in accordance with the provisions of the Law and of the Companies (Guernsey) Law, 1994; and

(iii) as regards the abridged accounts as described in paragraph (b)(ii) of this rule, a statement to the effect that they have been drawn up in accordance with the provisions of the Law and in a manner authorized by the Commission; and in the case of such abridged accounts the auditor's report shall also include a verbatim copy of the auditor's report on the audited accounts.

2. In the case of a licensed institution whose principal place of business is outside the Bailiwick the latest audited accounts of the main group shall be:

(i) delivered to the Commission not later than one month following publication; and

(ii) available to any person on request."

Guidance issued by the GFSC under paragraph s1(a) of the above Rules requires a director's report to be included in the audited accounts of Guernsey banks.

From December 1999 the banks were also required to provide risk management policies and practices for the detailed pro forma annual statements submitted to the GFSC. The rationale for this is rooted in developments in the international supervisory community, particularly the Core Principles for Effective Banking Supervision published by the Basel Committee for Banking Supervision, and also the new Basel Capital Accord published earlier that year which views enhanced bank transparency as a means to more effective market disciplines.

A legislative change, to make management explicitly responsible for all of this, is expected to take place at the end of 2002/early 2003.

Banks are all subject to an annual audit and are periodically subject to on-site visits by the GFSC. Quarterly prudential returns have to be verified by external audit once a year with the returns being selected on a sample basis, in arrears, by the GFSC. The returns (form BSL/1) are to be verified against the bank's books and records. On-site credit reviews also review bank records concerning loans granted.

There is regular and open communication between the GFSC and external auditors. Some of that is detailed in the Banking Division's Guidance Note 1997/2 on Trilateral Discussions.

Auditors also have to verify prudential returns and copy their findings to the GFSC annually. Audited accounts and auditor's management letters are submitted to the GFSC each year.

In addition BSL states:

"33. (1) No duty to which an auditor of a licensed institution or a person appointed to make a report under section 5(5) or section 25(1)(b) is subject is contravened by reason of his communicating in good faith to the Commission, whether or not in response to a request made by it, any information or opinion on a matter to which this section applies and which is relevant to any function of the Commission under this Law."

And the Banking Supervision (Bailiwick of Guernsey) Regulations, 1994 state the following:

"Matter to b e Communicated to the Commission"

3. (1) Matters are to be communicated to the Commission as mentioned in section 33(1) of the Law [BSL] by an auditor or other person described in that section in the circumstances specified in paragraph (2).

(2) The circumstances referred to in paragraph (1) are circumstances which are such as to give the auditor or other person reasonable cause to believe :

(a) that any of the criteria specified in Schedule 3 of the Law [BSL]is not or has not been fulfilled or may not have been fulfilled in respect of the licensed institution of which he is auditor or in relation to which his report is made, as the case may be; or

(b) that the circumstances are likely to be of material relevance to the exercise, in relation to the said licensed institution, of the Commission's functions under the Law [BSL] or under these Regulations.

The provisions of this regulation shall also apply in relation to former licensed institution..

The GFSC's Guidance on Verification of Prudential Returns (Guidance Note 1997/1) states that reports by auditors should be (paragraph 7(d):

"prepared, in the case of Guernsey subsidiaries, using the same accounting policies as those applied in the current period of statutory accounts;"

In addition, Guidance issued by the GFSC under s1(a) of the Banking Supervision (Accounts) Rules, 1994 requires that audited accounts state that the accounts show a true and fair view and

	that the audit was conducted "in accordance with Auditing Standards issued by the Auditing Practices Board" (GAAS). The GFSC will consider requests to follow other internationally accepted accounting standards (e.g., IAS) if it receives a request from a banking group. Guidance issued by the GFSC under s1(a) of the Banking Supervision (Accounts) Rules, 1994 requires auditors preparing audited accounts to value investments as follows: "Debt securities are held for long term investment and included at cost adjusted for amortization of premium and accretion of discounts. Other investments held for the long term are included at cost. Other instruments are included in the balance sheet at market value with any resultant profits and losses included in the profit and loss account." and require profit and loss accounts, which include provisions for loan losses. They also require auditors to provide an opinion that accounts are prepared in accordance with Auditing Standards issued by the Auditing Practices Board (see above) i.e. GAAS (Generally Accepted Accounting Standards). When auditing under GAAS, one of the auditor's objectives is to assess asset valuation (recoverability). If the auditors do not agree with the directors that the assets are appropriately valued then the ultimate recourse to the auditor is to qualify the accounts on the grounds of disagreement with the directors and specify the nature and extent of the disagreement. By auditing the valuations of assets the auditors are also assessing (under GAAS) the related provisions which are included in the profit and loss account. Thus profits are stated net of provisions. The Accounts Rules and Guidance issued by the GFSC under s1 (a) of those Rules provide detail on the contents of annual audited accounts and on when they should be produced. The GFSC may introduce Rules under the following provision of the BSL, which would make public issuance of individual bank's financial statements subject to its prior approval. However, no such rules have been introduced to date: "31. (2) The Commission may make rules prescribing the form in which the accounts and reports described in subsection (1)(a) are to be, the information and particulars to be contained in them and the times or intervals at which they are to be drawn up; and rules under this subsection may also make provision in respect of the delivery of such accounts and reports to such persons and at such times or intervals as may be prescribed." As to the ability to treat certain types of sensitive information as confidential, s43 of the BSL states (subject to gateways in s44): "(1) (a) no person who under or for the purposes of this Law receives information relating to the business or other affairs of any person; (b) no person who obtains any such information directly or indirectly from a person who has so received it; shall disclose the information without the consent of the person to whom it relates and (if different) the person from whom it was so obtained. (2) A person who discloses information in contravention of this section is guilty of an offense." The penalties for such an offense are, on summary conviction, a fine or a term of imprisonment not exceeding three months or both and, on conviction on indictment, to a fine, to imprisonment for a term not exceeding two years or both.

	Section 17A of the amended BSL provides the GFSC with powers to prohibit an individual from performing any function in connection with a bank if it considers that a person is not a fit and proper person to perform that function. In the amended BSL (s36C) makes management explicitly responsible for all of this. As all Guernsey banks are owned 100 percent by banks or holding companies in banking groups, the market price of the shares in Guernsey banks is not relevant or a consideration. However, audited accounts of Guernsey banks include (inter alia) all the requirements of the accounting standard on "Derivatives and other Financial Instruments: Disclosures," namely FRS 13. They are drawn up to GAAS and are to be made available in full (or in an abridged form prescribed by the GFSC) to the public upon request.
Assessment	Compliant.
Comments	The GFSC has to be commended for requiring banks to publish their risk management policies and practices in the detailed pro forma annual statements. However, ways should be explored of how to enhance the synergies between the GFSC supervisory process and the operations of the external auditors. This is especially recommended given the tight labor market situation of the Bailiwick.
Principle 22.	**Remedial Measures** Banking supervisors must have at their disposal adequate supervisory measures to bring about timely corrective action when banks fail to meet prudential requirements (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the ability to revoke the banking license or recommend its revocation.
Description	Oral and written communication with bank management is a common form of remedial action by the GFSC. The GFSC has powers under sections 9 and 10 of the BSL to impose conditions on licenses and to revoke a banking license. Conditions may be imposed "at any time" after granting a banking license and may be "such conditions in respect of the license as it (the Commission) thinks fit" (s9(1). The GFSC may vary or rescind any condition. In this respect s9 of the BSL states, inter alia: "(4) Without prejudice to the generality of subsection (1), the conditions which may be imposed in respect of a banking license may make provision as to the duration of the license and for the protection of the institution's depositors or potential depositors; and such conditions may : (a) require the institution to take certain steps, to refrain from adopting or pursuing a particular course of action or to restrict the scope of its business in a particular way; (b) impose limitations on the acceptance of deposits, the granting of credit or the making of investments; (c) prohibit the institution from soliciting deposits, either generally or from persons who are not already depositors; (d) prohibit the institution from entering into any other transaction or class of transactions; (e) require the removal of any director, controller or manager; (f) specify requirements to be fulfilled otherwise than by action taken by the institution; and (g) require the furnishing to the Commission, at such times, intervals and places as

	may be specified by the Commission, of such information and documents, and of accounts of such description, in such form and containing such information and particulars, as may be so specified." or by applying to the Court for an injunction under s35 of the BSL which states, inter alia: "(3) An injunction under subsection (1) or (2) may be granted on such terms and conditions, and may contain such incidental, ancillary, consequential or supplementary provision, as the Court thinks fit including, without prejudice to the generality of the foregoing, provision for the appointment of a receiver or other person to exercise such powers as the Court may consider necessary or expedient for the purpose of ensuring that any assets subject to the injunction are not disposed of or otherwise dealt with in contravention of the injunction, including powers to locate, ascertain, hold, gather in, sequester or take possession or control of any such assets." The GFSC may also withhold approvals of controllers/shareholders under s14 and 15 of the BSL and of the use of the words "bank," "banker" etc., under s37. Time scales are always placed on remedial actions and diary notes used (electronic) to follow up implementation. File reviews are also carried out periodically to ensure matters have not been overlooked. It is an implicit requirement of the FSC and BSL Laws that the GFSC carries out remedial actions in a timely manner. Other than imposing conditions on a licensee, the amended BSL also gives the GFSC explicit powers to prohibit an individual from performing any functions in connection with a bank if it considers that a person is not a fit and proper person to perform that function. Any institution, which contravenes any condition of a banking license, is guilty of an offense under the BSL (s9(5). In serving notice to revoke a banking license the GFSC has powers to give the bank such directions: "as appear to the Commission to be desirable in the interests of the institution's depositors or potential depositors, whether for the purpose of safeguarding its assets or otherwise." In refusing or revoking a banking license the GFSC must give written notice to the bank of the intention to refuse or revoke a license. Any contravention of a direction is an offense under BSL. The GFSC also has powers in the BSL to object to potential controllers / shareholders of banks (s.14) or to existing controllers / shareholders (s.15) and the GFSC may obtain information and documents (s25) appoint inspectors (s27) and require a person to furnish information/ documents to the GFSC and attend a meeting (s28). The GFSC may also apply to the Court to have unauthorized deposits and profits repaid (s34) and to issue an injunction to restrain unlawful deposit taking (s35) or to wind up a Guernsey or Alderney company under certain circumstances (s36). The GFSC may impose conditions on a bank's license to "require the removal of any director, controller or manager" (s9 (4)(e) of the BSL). Directions from the GFSC when serving notice to refuse or revoke a bank's license may also "require the removal of any director, controller or manager" (s12 (2)(e) of the BSL). With reference to injunctions issued by the Court under s35 of the BSL on the application of the GFSC, the following is stated: "(35)(2) If on the application of the Commission the Court is satisfied that a person may have been guilty of a contravention mentioned in subsection (1)(a), the Court may grant an injunction restraining him or any of his associates or controllers from disposing of or otherwise dealing with any assets or class or description of

	assets while the suspected contravention is investigated." This range of actions has been seen, over the 15 years of the GFSC existence, to be adequate and effective in the enforcement of the GFSC's instructions and requirements. It is an implicit requirement of the law that the GFSC should carry out its actions without unduly delaying appropriate corrective actions. This has been confirmed in writing by the Attorney General's office.
Assessment	Compliant.
Comments	Legal provisions are in place, which enables the GFSC to take regulatory action against a noncompliant bank. The GFSC has also taken the policy decision to introduce powers to fine and powers to publicly report institutions or individuals that are found to be not in compliance with regulatory or legal requirements. However, given the size of the constituency and the possible repercussions on its reputation one may wonder whether the latter powers are not to be considered as impracticable. Of far more importance seems to be the implication of the revision of the Companies (Guernsey) Law, 1994 and the proposed amendment to introduce administrative provisions. To quote the draft provisions, "an administration order is an order directing that, during the period for which the order is in force, the affairs, business and assets of the company shall be managed by a person (an administrator) appointed for the purpose by the court. The GFSC would have the power to apply for an administration order and would be entitled to receive notice of any such application made by another person such as a creditor. On the GFSC's application for an administration order, it would nominate the person to be appointed as administrator and, on another person's application, it would be entitled to object to the identity of the proposed appointee. The purpose for which an administration order could be made would include the survival of the company as a going concern, or a more advantageous realization of its assets than would be achieved on a winding up. During the administration of the company, it would not be possible for creditors or others to force the company into liquidation or receivership, to take or continue with legal proceedings against the company or to repossess goods. The enactment of the amendment would provide for an important modern legal tool. The Banking Division agrees that such a provision is invaluable.
Principle 23.	**Globally Consolidated Supervision** Banking supervisors must practice global consolidated supervision over their internationally active banking organizations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organizations worldwide, primarily at their foreign branches, joint ventures, and subsidiaries.
Description	The GFSC has the authority to supervise the overseas activities of locally incorporated banks. The powers to obtain adequate information are provided under s25 of the BSL. They extend to overseas subsidiaries in sub-sections 5 to 8. "(5) If it appears to the Commission to be desirable in the interests of the depositors or potential depositors of a licensed institution to do so, the Commission may also exercise the powers conferred by this section in relation to any body corporate which is or has at any relevant time been : (a) a holding company, subsidiary or related company of the licensed institution; (b) a subsidiary of a holding company of the licensed institution; (c) a holding company of a subsidiary of the licensed institution; or (d) a body corporate in the case of which a shareholder controller of the licensed institution, alone or with associates, is entitled to exercise, or control the

	exercise of, more than 50 percent of the voting power at a general meeting. (6) For the purposes of this Law a "related company," in relation to an institution, means any body corporate (other than one which is a group company in relation to that institution) in which that institution holds for a significant period a qualifying capital interest for the purpose of securing a contribution to that institution's own activities by the exercise of any control or influence arising from that interest. (7) For the purposes of this Law a "qualifying capital interest" means, in relation to any body corporate, an interest in shares comprised in the equity share capital of that body corporate of a class carrying rights to vote in all circumstances at general meetings of that body corporate. (8) Where: (a) an institution holds a qualifying capital interest in a body corporate; and (b) the nominal value of any relevant shares in that body corporate held by that institution is equal to 20 percent or more of the nominal value of all relevant shares in that body corporate; the institution shall be presumed to hold that interest on the basis and for the purpose mentioned in subsection (6), unless the contrary is shown; and in this subsection "relevant shares" means, in relation to any body corporate, any such shares in that body corporate as are mentioned in subsection (7)." In practice the GFSC does obtain information on and visits overseas subsidiaries of Guernsey incorporated banks. There are only two active overseas subsidiaries of Guernsey banks. Those companies have been subject to visits (in Jersey and Dublin) in 2002 and are a trust company and a fund custodian. The visits were carried out in conjunction with GFSC staff from the Fiduciary Services and Investment Business Divisions respectively. There are no banking subsidiaries of Guernsey banks. There are branches of Guernsey banks in Jersey and they have been subject to on-site visits by the GFSC in 2002. No other branches exist outside the Bailiwick. During these overseas on-site visits information reporting, compliance, internal controls and oversight are considered. In addition, during prudential meetings and on-site visits in Guernsey oversight of foreign branches and subsidiaries is discussed. Overseas operations are also subject to oversight by the host supervisor and external audit. Bilateral meetings with the Jersey Financial Services Commission include discussion of these branches and subsidiaries. In the limited number of cases where Guernsey banks have active overseas subsidiaries, the GFSC has ensured that sufficient management information is provided to the Guernsey bank's management. The GFSC obtains information on the senior management of subsidiaries and branches of Guernsey banks and satisfies itself that they are fit and proper. Active subsidiaries of Guernsey banks are required to submit copies of their audited accounts to the GFSC. Conditions may be imposed on banks' licenses "to restrict the scope of its business in a particular way" (s9 (4)(a) of the BSL). This could include the closure, where necessary, of a subsidiary or branch. All banks already have the following condition imposed on their license: "You should not establish a sub-branch outside the Bailiwick or invest in any company, which after such investment would be a subsidiary, associate or joint venture without the prior consent in writing of the Commission."
Assessment	Compliant
Comments	

Principle 24.	**Host Country Supervision** A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved, primarily host country supervisory authorities.
Description	As stated above the only jurisdictions where Guernsey banks have significant overseas operations is Jersey and the Republic of Ireland. The GFSC reportedly has a close and good working relationship with the Jersey Financial Services Commission. In addition, a Memorandum of Understanding (MOU) was agreed with the Jersey Commission during October 1998. Findings of on-site visits are to be shared under paragraph 9 of the MOU which states: "The main findings of on-site visits made by the GFSC or the JFSC to institutions in the others jurisdictions will be made available in summary form to the other authority after the conclusion of the visit." A good close working relationship also exists with the Irish regulators and a meeting has been held with them in Dublin in 2002. All banks have the condition imposed on their license that they: "should not establish a sub-branch outside the Bailiwick or invest in any company, which after such investment would be a subsidiary, associate or joint venture without prior consent in writing of the Commission." The GFSC would not give such prior consent if a proposal was made to establish a subsidiary, branch or joint venture in a jurisdiction where laws or regulations prohibit flows of information deemed necessary for adequate supervision. Bilateral meetings are regularly held with host (and home) country supervisors concerning the specific offices in the host countries, concerning the overall framework of supervision in which the banking group operates, and, if appropriate, concerning significant problems.
Assessment	Compliant.
Comments	
Principle 25.	**Supervision Over Foreign Banks' Establishments** Banking supervisors must require the local operations of foreign banks to be conducted with the same high standards as are required of domestic institutions and must have powers to share information needed by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.
Description	There are no domestic banks in Guernsey and all Guernsey licensed banks are supervised in the same manner. As a matter of policy, a letter is always sent to the home country supervisor before licensing a bank in Guernsey requiring the home country supervisor to confirm (inter alia): "(a) that you have no objection to the establishment of the branch / subsidiary in Guernsey;" (and a license is never granted until the home country supervisor has confirmed that it has no objection) "(c) that in supervising the bank you will be taking into account its transactions in Guernsey and satisfying yourselves as to the overall prudential soundness of the group on a consolidated basis." (and a license is never granted prior to receiving a satisfactory response from the home supervisor).
Assessment	Compliant
Comments	

Table 2. Summary Compliance with the Basel Core Principles

Core Principle	C[1/]	LC[2/]	MNC[3/]	NC[4/]	NA[5/]
1. Objectives, Autonomy, Powers, and Resources					
1.1 Objectives		**X**			
1.2 Independence		**X**			
1.3 Legal framework	**X**				
1.4 Enforcement powers	**X**				
1.5 Legal protection	**X**				
1.6 Information sharing	**X**				
2. Permissible Activities	**X**				
3. Licensing Criteria	**X**				
4. Ownership	**X**				
5. Investment Criteria	**X**				
6. Capital Adequacy	**X**				
7. Credit Policies	**X**				
8. Loan Evaluation and Loan-Loss Provisioning		**X**			
9. Large Exposure Limits	**X**				
10. Connected Lending	**X**				
11. Country Risk	**X**				
12. Market Risks	**X**				
13. Other Risks		**X**			
14. Internal Control and Audit		**X**			
15. Money Laundering	**X**				
16. On-Site and Off-Site Supervision		**X**			
17. Bank Management Contact	**X**				
18. Off-Site Supervision	**X**				
19. Validation of Supervisory Information		**X**			
20. Consolidated Supervision	**X**				
21. Accounting Standards	**X**				
22. Remedial Measures	**X**				
23. Globally Consolidated Supervision	**X**				
24. Host Country Supervision	**X**				
25. Supervision Over Foreign Banks' Establishments	**X**				

[1/] C: Compliant;
[2/] LC: Largely compliant;
[3/] MNC: Materially noncompliant;
[4/] NC: Noncompliant;
[5/] NA: Not applicable.

Recommended actions and authorities' response to the assessment

Recommended actions

Table 3. Recommended Actions to Improve Compliance with the Basel Core Principles

Reference Principle	Recommended Action
1.1 Objectives	The GFSC Law should establish safety, soundness, and integrity of the financial system as the objectives of the GFSC and eliminate "development" as one of the GFSC functions. The GFSC should be able to continue its support of the activities of the Training Agency that are consistent with the revised mandate.
1.2 Independence	The Advisory and Finance Committee's power to give guidance and directions to the GFSC has the potential of intruding on the operational independence of the latter. It is recommended that the law be amended to remove these powers. An in-depth analysis of the supervisory objectives and the means to fulfill those objectives should be made. The existing Banking Division Manpower Plan for 2003–2007 should be revisited accordingly.
8 Loan Evaluation & Loan Loss Provisioning	Extend current on-site credit risk assessments to include additional emphasis on credit quality and provisioning levels.
14 Internal Control and Audit	Confirm formalization and distribution of Corporate Governance Guideline.
16 On-site and Off-site Supervision	Prioritize the completion of the examination methodology to allow for full scope safety and soundness visitations to be carried out supplemented by more defined quality control procedures. A dedicated training program directed at assisting Banking Division staff with the enhanced accountabilities would be beneficial. Explore increased synergies with external auditors.

Authorities' Response to the Recommended Action Plan to Improve Compliance with the Basel Core Principles

Overview

11. The authorities welcome the IMF's assessment and confirmation that the Bailiwick of Guernsey has achieved a high level of compliance with the Basel Committee Core Principles on Banking Supervision.

Objectives (CP 1.1)

12. Currently, the GFSC has a responsibility under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 to develop and effectively supervise finance business in Guernsey. The IMF's recommendation that the GFSC should be provided with a statutory obligation for the safety, soundness and integrity of the financial system in place of its responsibility to develop the finance sector has been noted. The States of Guernsey Advisory and Finance Committee and the GFSC agree with the IMF's view that formalising the GFSC's approach in this manner better expresses the GFSC's current and continuing objectives and will enhance the reputation and contribute to the continuing development of the financial system in Guernsey. The Committee proposes to seek amendment of the law at an early stage.

Independence (CP 1.2)

13. The IMF's conclusion that the States of Guernsey Advisory and Finance Committee's ability under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 to give guidance and directions of a general character to the GFSC has not interfered with the GFSC's capacity to carry out its functions is noted. As stated by the IMF, the Committee has never unilaterally provided guidance or directions to the GFSC. As is also acknowledged, the law permits the Committee to give the GFSC guidance and directions only of general character. Both the Committee and the GFSC consider that this provision provides proper accountability by the GFSC to the Committee, which is the senior political body of Guernsey's parliament. The Committee and the GFSC consider that the ability to give guidance and directions of general character is in compliance with the international standard which applies to the independence of regulatory bodies.

14. Staff resources of the GFSC have continued to grow in line with the size of the finance sector and the responsibilities of the GFSC. The IMF has recommended that the GFSC's Banking Division should carry out a "zero based" analysis of its staff needs based on the expected number of banks. This has been completed and, as a consequence, an additional analyst has been recruited since the assessment in order to assist the Division to carry out a systematic programme of corporate governance and full scope safety and soundness on-site visits to banks.

Loan Evaluation and Loan Loss Provisioning (CP 8)

15. Following the introduction of the Banking Supervision (Bailiwick of Guernsey) (Amendment) Law, 2003, it is a legal requirement for all Guernsey banks to review, at least annually, their individual loans, asset classification and loss provisioning (including on and off balance sheet exposures). Should the review identify any shortcomings, the bank is required to report any findings to the GFSC, together with the details of how it proposes to address the shortcomings.

16. With regard to policies followed by the GFSC, the scope of on-site credit assessments of banks was extended in early 2003 to give additional emphasis to credit quality and provisioning levels.

On-Site and Off-Site Supervision (CP 13 and 16)

17. The GFSC's Banking Division is planning full safety and soundness on-site visits for 2004. Additional training of staff in this field of work will continue. The visits will include techniques and practices to confirm or otherwise the existence and application of an effective and comprehensive risk management process and control culture.

18. Meetings by the GFSC with external bank auditors will be more frequent and scope for increasing synergies will be explored.

Internal Control and Audit (CP 14)

19. Following the introduction of the Banking Supervision (Bailiwick of Guernsey) (Amendment) Law, 2003, it is a legal requirement for each Guernsey bank to review, at least annually, the responsibilities and conduct of the bank's board of directors with respect to corporate governance principles. Should the review identify any shortcomings, the bank is required to report any findings to the GFSC, together with the details of how it proposes to address the shortcomings.

20. GFSC guidance notes entitled "Guidelines for Corporate Governance and Risk Management" are being revised in light of comments received during consultation with banks and will be formally issued as soon as possible, following consideration of the comments arising from the consultation.

Validation of Supervisory Information (CP 19)

21. Meetings will be held with the Guernsey Society of Chartered and Certified Accountants to explore the possibility of the GFSC having access to working papers in connection with the verification of quarterly returns and preparing audited accounts. Where necessary, the GFSC will also consider the benefits of bilateral and trilateral meetings with auditors.

II. FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism

A. General

Information and methodology used for the assessment

22. A detailed assessment of the anti-money laundering (AML) and combating the financing of terrorism (CFT) regime of Guernsey was prepared by a team of assessors that included staff of the International Monetary Fund (IMF) and an expert not under the supervision of IMF who was selected from a roster of experts in the assessment of criminal law enforcement and nonprudentially regulated activities[3]. IMF staff reviewed the relevant AML/CFT laws and regulations, and supervisory and regulatory systems in place to deter money laundering (ML) and financing of terrorism (FT) among prudentially regulated financial institutions. In addition, the IMF staff reviewed the framework in respect of trust and company service providers, which were in a transitional stage towards full prudential regulation. The expert not under the supervision of IMF reviewed the capacity and implementation of criminal law enforcement systems.

23. This assessment is based in part on discussions on AML/CFT issues that were held with officers and other representatives of the following offices among others, all of whom were most helpful in the preparation of this assessment: the GFSC; the Bailiff's Chambers; Attorney General's Chambers; Customs and Excise Department; Guernsey Police and the Financial Intelligence Service (FIS). In addition, the assessors met with a number of financial sector parties, including banks, investment management companies, fiduciaries, insurance companies, lawyers, and associations representing these sectors.

24. Information used for the assessment was obtained from the following:

The Money Laundering (Disclosure of Information) (Guernsey)[4] Law, 1995 (the "1995 Law"); the Money Laundering (Disclosure of Information) (Alderney) Law, 1998 (the "1998 Law"); the Money Laundering (Disclosure of Information) (Sark) Law, 2001 (the "2001 Law"); the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999 as amended (the "POC Law"); the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations 2002 (the Regulations); the Criminal Justice (International

[3] The team consisted of Ian Carrington, (Senior Financial Sector Expert, MFD) and Ross Delston, (Consulting Counsel, LEG), with Washington-based assistance from Stuart Yikona, (Technical Assistance Officer LEG). Messrs. Carrington and Delston were part of a Fund-lead mission to Guernsey during the period November 13–26, 2002. The expert not under the supervision of the IMF was Detective Chief Superintendent Felix Mc Kenna of Ireland's Criminal Assets Bureau.

[4] References in names of laws to 'Guernsey' refer to that island only, as opposed to references to "the Bailiwick of Guernsey," which refer to the islands of Alderney, Guernsey and Sark.

Cooperation) (Bailiwick of Guernsey) Law, 2001 (the "CJIC Law"); the Criminal Justice (Fraud Investigation) (Bailiwick of Guernsey) Law, 1991 (the "Fraud Investigation Law"); the Terrorism and Crime Law (Bailiwick of Guernsey) Law, 2002 (the "Terrorism Law"); the Terrorism (United Nations Measures) (Channel Islands) Order 2001 (the "Terrorism Order") and the Al-Qa'ida and Taliban (United Nations Measures) (Channel Islands) Order 2002 (the "Al-Qa'ida Order"); the Drug Trafficking (Bailiwick of Guernsey) Law, 2000 (the "DT Law"); the Banking Supervision (Bailiwick of Guernsey) Law, 1994 (the "Banking Law"); and the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism issued by the Guernsey Financial Services Commission (the "Notes");[5] Position Paper entitled Overriding Principles for a Revised Know Your Customer Framework issued in February 2002 jointly by the Guernsey, Jersey and Isle of Man Commissions (the "Position Paper"); Business from Sensitive Sources Notices issued by the Guernsey Financial Services Commission; The Protection of Investors (Bailiwick of Guernsey) Law, 1987 and associated rules and regulations (the "POI Law"); The Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law, 2000 and associated Codes of Conduct (the "Fiduciary Law"); the Insurance Business (Bailiwick of Guernsey) Law, 2002 (the "Insurance Business Law"); the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002 (the "Insurance Managers and Intermediaries Law"); the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended (the "Commission Law"); the Control of Borrowing Ordinance, 1959 as amended (the "Control of Borrowing Ordinance); the Companies (Guernsey) Law, 1994 as amended (the "Companies Law"); the Data Protection (Bailiwick of Guernsey) Law, 2001 (the "DP Law"); the Data Protection (Transfer in the Substantial Public Interest) Order, 2002; the Interpretation (Guernsey) Law 1948 (the "Interpretation Law"); the Misuse of Drugs (Bailiwick of Guernsey) Law, 1974 (the "Misuse of Drugs Law") Law; Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 (the "Investment Licensees Rules"); the Policy Letter dated September 26, 2002 with respect to Amendments to Regulatory Legislation (the " Policy Letter"); Projet de Loi (draft law) entitled The Prevention of Corruption (Bailiwick of Guernsey) Law 2003 (the "Draft Corruption Law"); Project de Loi entitled The Criminal Justice (Miscellaneous Provisions)(Bailiwick of Guernsey) Law, 2003, (the "Draft Miscellaneous Provisions Law"); The United Kingdom Recording and Dissemination of Intelligence Material, Code of Practice (the "Intelligence Material Code of Practice"); The Royal Court (Bar Administration) Order, 1993 (the "Royal Court Order"); the Rules of Professional Conduct for Guernsey Advocates.

25. For purposes of this assessment, the term Financial Institution (FI) has the definition found in the Schedule to the POC Law, as follows:

- Any person or body carrying on or providing services in or from within the Bailiwick of Guernsey in relation to the business of: (i) lending (including, but not limited to,

[5] The Notes do not meet the definition of 'law' contained in the Methodology since they are not 'mandatory.' The Attorney General agrees with this conclusion. Hence, the Notes were not included in the detailed assessment in any discussion of laws or legal requirements.

consumer credit, mortgage credit, factoring with or without recourse, financing of commercial transactions (including forfeiting) and advancing loans against checks); (ii) financial leasing; (iii) money service business including money or value transmission services, currency exchange (bureaux de change) and/or cheque cashing; (iv) provision of services for, and/or the facilitation of, the transmission of money or value through an informal money or value transfer system or network; (v) issuing, redeeming, management and/or administration of means of payment (for example, credit, charge and debit cards, checks, travelers' checks, money orders and bankers' drafts); (vi) providing financial guarantees and/or commitments; (vii) trading for account of customers (spot, forward, swaps, futures, options etc) in: money market instruments (for example checks, bills, certificates of deposit); foreign exchange; exchange, interest rate and/or index instruments; commodity futures, transferable securities and/or other negotiable instruments and/or financial assets, including bullion; (viii) participating in securities issues, including underwriting and/or placement as agent (whether publicly or privately) and/or the provision of services related to such issues; (ix) settlement and/or clearing services for financial assets including securities, derivative products and/or other negotiable instruments; (x) providing advice to undertakings on capital structure, industrial strategy and/or related questions and/or advice as well as services relating to mergers and/or the purchase of undertakings; (xi) money broking/changing; (xii) providing individual and/or collective portfolio management services and/or advice; (xiii) providing safe custody services; (xiv) providing the services of safekeeping and/or administration of cash or liquid securities on behalf of clients; (xv) credit unions; and/or (xvi) accepting repayable funds other than deposits.

- 'Deposit taking' as a deposit-taking business as defined in Section 3 of the Banking Law.

- 'Controlled investment business' as defined in Section 1, and Schedules 1 and 2 of the POI Law.

- 'Insurance business' as defined in Section 2 and Schedule 1 of the Insurance Business Law and Sections 1 and 2 of the Insurance Managers and Intermediaries Law.

- 'Regulated activities' as defined in Section 2 of the Fiduciary Law.

- Section 1 above applies to lawyers,[6] accountants and actuaries providing non-incidental financial services.

[6] Section 1(a) of the Royal Court Order makes the Rules of Professional Conduct binding on Guernsey Advocates. Rule 23A of such Rules state that an Advocate "is under a duty at all times to observe the provisions of all Guernsey laws." The Commentary on this rule refers to "guidelines – for example in respect of money laundering," which refers to the Notes. Consideration should be given to amending relevant laws to include all activities of

26. The main institutions in Guernsey in the AML/CFT area are the Financial Intelligence Service, which is an independent unit of the Guernsey Police and Customs and Excise Department jointly staffed by each and is the FIU for Guernsey; the Police and the Customs and Excise Department, each of which investigate criminal activities; the Attorney General's Chambers, which prosecutes ML and FT, defends Guernsey authorities against any suit, and advises the States Assembly (Parliament) and the government on legal issues; the GFSC, which is the financial regulator for Guernsey and is responsible for monitoring compliance for FIs that are regulated by it; and the Advisory and Finance Committee of the States Assembly (the "Committee), which issues regulations on AML/CFT and other matters.

Overview of measures to prevent money laundering and terrorism financing

Legal and Institutional Framework

27. Guernsey has a developed legal and institutional framework generally, particularly with respect to confiscation of the proceeds of criminal conduct, exchange of information, and international cooperation. The broad regulation of the financial sector, including banking, investment companies, insurance business, and fiduciaries (company and trust service providers), is another strength. However, Guernsey's legal and institutional framework falls short in a number of areas outlined in greater detail below.

Implementation of the Legal and Institutional Framework, and Financial Sector-specific Issues

28. The general framework for AML/CFT in Guernsey has been implemented well. The GFSC has devoted an appropriate level of resources to this issue. Detailed Guidance Notes have been developed and the GFSC has established a program of on- and off-site surveillance of financial service businesses to assess compliance with required standards. There is a strong relationship amongst the principal institutions involved including the GFSC, the FIS, the Attorney General's chambers, and prudentially regulated financial institutions (FSBs). Visits to FIs revealed a high level of awareness and, in general, the existence of appropriate AML/CFT policies and procedures. However, there are a number of areas in which the implementation of the AML/CFT framework could be strengthened as set forth in greater detail below.

B. Detailed Assessment

29. The following detailed assessment was conducted using the October 11, 2002 version of Methodology *for assessing compliance with the AML/CFT international standard, i.e., criteria issued by the Financial Action Task Force (FATF) 40+8 Recommendations* (the Methodology).

Advocates that would be covered by the amended European Union Anti-Money Laundering Directive, in addition to those activities covered under current Guernsey law.

Assessing criminal justice measures and international cooperation

Table 4. Detailed Assessment of Criminal Justice Measures and International Cooperation

I—Criminalization of ML and FT (compliance with criteria 1–6)
Description
1. The Vienna Convention was ratified on Guernsey's behalf by the United Kingdom on 9 April 2002. The Council of Europe Convention on Laundering, Search and Seizure was extended to Guernsey from on January 2003. Guernsey, by letter dated 15 August 2002, asked the United Kingdom to effect ratification of the Convention for the Suppression of the Financing of Terrorism. The application is now in the hands of the Foreign and Commonwealth Office. All necessary legislation to ratify the Convention has been enacted. The laws of Guernsey meet most of the provisions of the Palermo Convention, however additional implementing legislation will be needed prior to ratification, as follows: (i) Guernsey's current law concerning corruption is not wide enough to meet the Convention requirements. The States of Guernsey (the island's parliament) have agreed in principle to enact a comprehensive anti-corruption law which is expected to be laid before it in the autumn of 2003. A Bill has been drafted and comments received from the Home Office. The authorities have indicated that the Bill is expected to become law in early 2004; and (ii) to meet the terms of Article 3 of the Protocol on Trafficking Persons it will be necessary to enact provisions similar to sections 30 and 31 of the English Sexual Offenses Act 1956; and (iii) legislation might be required to implement the Convention Article on Extradition and the Protocol on Trafficking in Human Beings. The authorities have advised that legislation will be enacted as required to implement the Palermo Convention. 2. Money laundering has been criminalized, as follows: • Drug trafficking money laundering is criminalized under the provisions of sections 57–59 of the DT Law. • Money laundering for terrorism is criminalized by section 11 of the Terrorism Law. • Money laundering for other crimes is criminalized by sections 38–40 of the POC Law. • The financing of terrorism is criminalized by sections 8–10 of the Terrorism Law. Offenses relating to money laundering extend to proceeds of all serious offenses, including financing terrorism, and are consistent with provisions of the Vienna and Palermo Conventions and the FATF Recommendations. The definition of the financing of terrorism is also consistent with the definition set out in the Convention for the Suppression of the Financing of Terrorism. According to the authorities, in Guernsey's courts, the intentional element of ML and FT may be inferred from the totality of the evidence submitted to the court. The offense of ML extends to persons who have committed ML as well as both the laundering and predicate offense (sections 38(1) of the POC Law and section 57(1) of the DT Law). It is not necessary that a person be convicted of a predicate offense to establish that assets were the proceeds of a predicate offense (Sections 38–40 of the POC Law, sections 57–59 of the DT Law and Section 11 of the Terrorism Law). All serious crimes are predicate offenses for money laundering, including the financing of terrorism. (Section 1 of the POC Law, Section 1 of the DT law, Section 1 of the Terrorism Law). The offense of ML extends to any property which represents the proceeds of criminal conduct (Sections 38(1)(a), 38(2), 39(2) and 40(1) of the POC Law, sections 57(1)(a), 57(2), 58(2) and 59(1) of the DT Law, and sections 7(2)(a) and 11(1) of the Terrorism Law). In each provision, reference is made to property which "in whole or in part directly or indirectly represents....." The predicate offenses for ML extends to conduct that occurred in another country and which would have constituted such an offense had it occurred domestically (Section 1(b) of the POC Law, section 1 of the DT Law and section 1(4) of the Terrorism Law).

3. FT has been criminalized on the basis of the Convention for the Suppression of the Financing of Terrorism (Sections 8, 9 & 10 of the Terrorism Law). The predicate offense for FT extends to terrorists or terrorist organizations located in another country and to conduct that occurred in another country (Section 1 of the Terrorism Law).

4. The offenses of ML applies to individuals and legal entities that engage in ML activities (Section 49(4)(d) of the POC Law); the offense of FT extends to those who should have reasonable cause to suspect that money or other property may be used in terrorism activities (Sections 8(3) & 10(b) of the Terrorism Law).

According to the authorities, in Guernsey's courts, the intentional element of ML and FT may be inferred from the totality of the evidence submitted to the court. In Guernsey, the offenses of money laundering and financing of terrorism extend to all entities. Section 2 of the Interpretation Law states that 'person' includes a body corporate.

All of Guernsey's money laundering offenses and those relating to the financing of terrorism apply at least to those knowingly engaged in money laundering or terrorist financing. Section 38(2) of the POC Law, section 57(2) of the DT Law and section 11 of the Terrorism Law include the objective test within their terms. Therefore, where an individual has reasonable grounds for suspicion, but fails to disclose such a suspicion, and it is subsequently established that a reasonable person would have suspected and disclosed that suspicion, an offense has been committed.

The offense of FT extends to those who should have reasonable cause to suspect that money or other property may be used in terrorism activities (Sections 8 & 10(b) of the Terrorism Law).

5. (see response to criterion 64)

6. *Guernsey falls marginally short of having an adequate number of law enforcement personnel who are tasked with providing the resources to effectively combat money laundering and financing of terrorism. This process, is supervised by the offices' of the Attorney General and Solicitor General in Guernsey and prosecuted by experienced personnel who have also worked for the Crown Prosecution Service in the United Kingdom. The Guernsey Police and Customs & Excise approach to financial crime is coordinated and directed by a Service Authority which is staffed by Senior Commanders of Police and Customs and Excise. The Financial Intelligence Service (FIS) which is the FIU in Guernsey carries out the immediate tasks in respect of money laundering. On the investigation stages matters are then referred to the agencies (A) Police Commercial Fraud and External Affairs, (B) Customs and Excise Fraud and International Team. In Guernsey the total authorized establishment of the police force is 177 and total number of Customs and Excise Law Enforcement officers is 51.*

The Guernsey Commercial Fraud and External Affairs Department is staffed by a D/Inspector, D/Sergeant and 2 D/Constables with part-time administrative support. Their mandate is:

1. *To assist external law enforcement agencies to obtain evidence in relation to financial crime within the Bailiwick of Guernsey.*
2. *Investigate serious and complex fraud and financial crime committed within the Bailiwick of Guernsey.*
3. *Investigate, identify and restrain proceeds of crime and drug trafficking, in Guernsey.*

The Customs and Excise Fraud and International Team is staffed by a senior investigating officer, two investigating officer's, an office manager/analyst with secretarial support.

This unit is mandated to:

1. *Investigate Customs and Excise related fraud and identify, then restrain proceeds of crime and drug trafficking.*
2. *Assist external law enforcement agencies to obtain evidence within the Bailiwick in relation to Customs related offenses and Money Laundering.*
3. *Conduct and support local money laundering investigations.*
4. *Investigate suspected breaches of UN and EU sanctions within the Bailiwick.*

The Financial Intelligence (FIS) is headed by a director and is staffed equally by Police and Customs and Excise. Its current staff complement comprises two Senior Intelligence Officers, four Intelligence Officers, a Financial Analyst, an Office Manager and an Administrative Assistant. At the time of the assessment two of the Intelligence Officer posts and the positions of Financial Analyst and Administrative Assistant were vacant. The FIS was in the process of advertising the Analyst and Administrative positions (these posts have now been filled). The vacant positions of Intelligence Officers are expected to be filled in early 2004. Therefore there is a shortage of personnel in the unit.

The aim of the FIS/FIU is to:

- *Provide quality in financial crime intelligence particularly money laundering.*
- *Ensure full international cooperation.*
- *Enhance the coordination and development of financial crime intelligence within Guernsey.*
- *Gather, collate and evaluate all Bailiwick financial crime intelligence, i.e. suspicious transaction reports (STR).*
- *Lawful and proper dissemination of financial crime intelligence.*
- *Providing strategic and tactical intelligence with regard to financial crime.*

Analysis of Effectiveness

Measures taken to criminalize money laundering and terrorist financing are generally adequate. Present arrangements will be enhanced when Guernsey implements legislation to give effect to the Palermo Convention and the Convention for the Suppression of the Financing of Terrorism is extended to Guernsey.

Recommendations and Comments

Legislation will be required to implement the Palermo Convention as follows:

i) Guernsey's current law concerning corruption is not wide enough to meet the Convention requirements. The States of Guernsey (the island's parliament) have agreed in principle to enact a comprehensive anti-corruption law to be presented to the States Assembly for approval in September 2003;

ii) To meet the terms of Article 3 of the Protocol on Trafficking Persons, it will be necessary to enact provisions similar to sections 30 and 31 of the English Sexual Offenses Act 1956; and

iii) Legislation might be required to implement the Convention Article on Extradition and the Protocol on Trafficking in Human Beings.

Implications for compliance with FATF Recommendations 1, 4, 5, SR I, SR II

Full compliance will be achieved when the Convention for the Suppression of the Financing of Terrorism is extended to Guernsey.

II—Confiscation of proceeds of crime or property used to finance terrorism (compliance with criteria 7–16)

Description

7. Laws provide for the confiscation of laundered property, proceeds from and instrumentalities used in or intended for use in Guernsey with respect to any ML offense (Sections 2 of the POC and DT Laws). In addition, laws do provide for the forfeiture of property that is the proceeds of or intended for use in FT (Section 18 of the Terrorism Law). Parts I of the POC Law and the DT Law provide for the confiscation in criminal cases of the proceeds of crime and include any income gains from the proceeds of crime. Both laws provide for the enforcement of confiscation orders which are made in countries which are designated in secondary legislation. Guernsey designates those countries which are designated by the United Kingdom under the Criminal Justice Act 1988 and the Drug Trafficking Act 1994. It is likely that the need for designation will be abolished in the proposed proceeds of crime legislation. Laws do not provide for the confiscation of property of equivalent value.

The instrumentalities of crime may be forfeited by a court by the use of its power under common law and statutory powers such as those contained within section 26 of the Misuse of Drugs Law 1974 which provides for the forfeiture and destruction of anything found to the satisfaction of the court to relate to an offense under the Law.

Forfeiture orders concerning the instrumentalities of crime that are made by courts in another jurisdiction may be enforced locally under section 8 of the CJIC Law. The Law contains a provision concerning the designation of countries which is similar to that contained in the POC Law and the DT Law.

Section 18 and schedule 2 of the Terrorism Law provides for the forfeiture of any property connected with terrorism; paragraphs 8–10 provide for the enforcement of orders made elsewhere.

With respect to confiscation of property of corresponding value, AML laws in Guernsey provide for the appointment of a receiver for all property owned by a defendant, and for the sale of such property to satisfy a confiscation order (POC and DT Laws Sections 5, 6, 29–31). However, the Terrorism Law does not contain comparable provisions.

The law does provide for restraint orders against all realizable property whether described in an order or not (Section 26 of the POC Law). Freezing orders may also be made with respect to FT (Sections 20 & 21 of the Terrorism Law). Restraint orders may be obtained under sections 25 and 26 of the POC and DT Laws. Applications for restraint orders may be made by ex parte applications. Orders may apply to all realizable property as defined by section 6 of both laws. Realizable property includes "any property held by the defendant." A restraint order under the POC and DT Laws may be obtained if proceedings have been instituted against a defendant or when a person is to be charged with an offense.

With regard to terrorism, under section 18 and schedule 12, paragraph 3 of the Terrorism Law, a restraint order may be made by ex parte applications in respect of any property liable to forfeiture. An order may be made if proceedings have been instituted and not concluded or an investigation has been commenced and in both cases it appears to the court that a forfeiture order may be made in proceedings for the offense. Sections 20-29 and schedule 4 of the Terrorism Law provide for the making of freezing orders by the Committee if certain criteria are met. Under Article 6 of the Terrorism Order and Article 8 of the Al-Qa'ida Order, freezing orders may be made by the Attorney General.

The proceeds of crime and terrorist property held by members of a criminal organization or a company used as a vehicle to commit crime may be confiscated by the Royal Court (trial court equivalent to the Crown Court in England) following conviction under the POC Law, DT Law and the Terrorism Law.

In the event of an order being made under the POC Law or the DT Law, the court may make an order that the convicted person must pay a monetary amount. No reference is made by the court to specific assets (sections 5(1) of POC Law and 5(1) of DT Law).

Section 29 of both the POC Law and the DT Law and section 18 and Schedule 2 of the Terrorism Law give power to the Royal Court to appoint a receiver to gather in a convicted person's assets, sell them and put the proceeds towards settling a confiscation order.

It is currently not possible for the authorities to apply for confiscation orders using the civil process. Consideration is being given to the introduction of civil forfeiture powers based upon the United Kingdom's Proceeds of Crime Act or the equivalent legislation in the Republic of Ireland. According to the authorities, it is however open to a person who has lost any property as a result of a person's unlawful act to seek the return of the assets and damages through the civil courts.

8. Production Orders and warrants may be obtained to identify and trace property. (Sections 45 and 46 of the POC Law; sections 63 and 64 of the DT Law and sections 36 and schedule 5, section 37 and schedule 6 and section 39 and schedule 7 of the Terrorism Law). Section 37 and schedule 5 and section 39 and schedule 7 of the Terrorism Law provide for the obtaining of information about bank accounts and the monitoring of accounts respectively. Police and Customs Officers, by virtue of these laws, may apply to the Court for orders to gain access to material so as to identify and trace property that is, or may become, subject to confiscation. Such powers are exercisable where there are sufficient grounds to suspect and where it is in the public interest to do so. Police and Customs Officers have no power of discovery outside of the judicial process.

9. There are protections for the rights of bona fide third parties in the case of restraint orders (Section 25(5) (c) of the POC Law). In addition, under section 2(6) of the POC Law, where the Court is satisfied that a victim of any relevant criminal conduct has instituted, or intends to institute, civil proceedings against the defendant in respect of loss, injury or damage sustained in connection with that conduct, the Court does not have to make a

confiscation order in the total sum which is available to be realized.

When a restraint order is made under the POC, DT or Terrorism Laws notice of the order must be given to persons affected by the order. Any person affected by the restraint order may apply for its discharge or variation. (Sections 25(5) (c) and (7) of the POC and DT Laws and section 18 and schedule 2 paragraphs 4(1) (c) and 4(4) of the Terrorism Law).

Under the POC Law (Section 8(1)(a) and the DT Law (Section 8(1)(a), only assets held by a defendant or gifts made during the previous six years may be considered when calculating the amount of a confiscation order. Under Section 31(4) of the POC and DT laws, a receiver appointed to enforce a confiscation order must exercise their powers with a view to allowing any person other than the defendant or the recipient of a gift to retain or recover the value of any property held by him.

10. According to the authorities, it is likely that the Guernsey courts would declare as void any contract whose purpose was to frustrate the authorities from recovering the proceeds of crime, thereby making the value of the assets concerned liable to be included in any confiscation order.

11. *Statistics on amounts of property frozen, seized, and confiscated relating to proceeds of crime, drug trafficking, money laundering, and financial terrorism are kept by the FIS.*

12. *The Judiciary, law officers and Crown Advocates who are involved in administering the law and mounting all prosecutions in Guernsey are familiar with applications made in respect of money laundering, production orders and freezing orders, as these people are involved in the formulation of the existing Guernsey laws relating to this subject. They have obtained their experience and training through basic law studies for many years, they attend training courses in the UK routinely and also attend seminars and conferences and discuss the matter with experts and keep themselves abreast of all money laundering legislation.*

The police and customs officers who are involved in the financial investigation matters in Guernsey have undergone training courses in the UK and are required to attain the same standards applicable to UK counterparts. All law enforcement officers engaged in the area of Financial Investigations are required to be accredited as "Financial Investigators" by UK Home Office' Center of Excellence.

13. There are measures for freezing of funds and/or property of terrorists (Article 6 of the Terrorism Order and Article 8 of the Al Qa'ida Order).

I am satisfied from the records produced to me which are confidential at this point of time, that the Guernsey authorities do keep records and statistics.

14. Under Article 10 of the Terrorism Order, information may be obtained to secure compliance with the Order or detect evasion of the Order. Article 6 of the Order provides for the freezing of funds connected with terrorism.

Section 36 and Schedule 5 of the Terrorism Law allow information to be obtained in connection with terrorist investigations; section 37 and Schedule 6 are concerned with the collection of information relating to bank accounts and Section 39 and Schedule 7 permit the monitoring of accounts.

Section 18 and Schedule 2 of the Terrorism Law provides for the restraint of assets which are or may be liable for forfeiture. Freezing orders may be made under section 20 of the Terrorism Law.

In addition, the Terrorism Order allows for the obtaining of information by the Attorney General (Article 10) and the freezing of funds by order of the Attorney General (Article 6).

All the above provisions may apply to persons or entities not included on lists maintained by relevant Committees of the UN Security Council.

15. There is no statutory asset forfeiture fund. In a number of cases, assets have been shared by other jurisdictions with Guernsey. The money received has been paid into accounts in the name of the Receiver General (who is the Attorney General). These funds were used by the Receiver General following consultation with the Chief Officers of Police and Customs, senior members of the States of Guernsey and senior civil servants to fund special projects connected with law enforcement that are not covered by general revenue. The Bailiwick Financial Crime Committee is currently considering whether legislation should be drafted to formalize

the fund. 16. There is no statutory asset sharing mechanism. However, in the event of a confiscation order made in another jurisdiction being enforced by Guernsey, the authorities have indicated that they would be prepared in appropriate cases to share a proportion of the funds realized with the other jurisdiction. Unless agreed, no conditions would be imposed on the jurisdiction recovering the shared property.
Analysis of Effectiveness
The framework in place for the confiscation of the proceeds of crime or property used to finance terrorism is generally adequate. The framework would however be improved by the adoption of legislation to provide for an asset forfeiture fund and for asset sharing with other jurisdictions.
Recommendations and Comments
Consideration should be given to amending the Terrorism Law to provide for the appointment of a receiver for all property owned by a defendant to satisfy a confiscation order. Consideration should be given to adopting legislation that would provide for an asset forfeiture fund and for asset sharing with other jurisdictions. The authorities have informed us that such consideration will take place in connection with the consideration of an amended Proceeds of Crime Act in early 2004.
Implications for compliance with FATF Recommendations 7, 38, SR III
Compliant
III—The FIU and processes for receiving, analyzing, and disseminating financial information and other intelligence at the domestic and international levels (compliance with criteria 17–24)
Description
17. The FIS is the FIU and is an independent unit of the Guernsey Police Force and Officers of the Customs and Excise office, jointly staffed by both the Police and Customs. Police Officers. FIs are required to report to a police officer (a defined term which includes customs officers) transactions suspected of stemming from a criminal activity or used to finance terrorism (Regulation 6(5) of the Regulations; Sections 39(3) and 40(5) of the POC Law; Sections 58(3), 59(5) and 60(1) of the DT Law; Sections 12 & 13 of the Terrorism Law). There is no requirement in law that STRs must be submitted to the FIS. Guernsey has had an FIU since 1989. In 1998 Guernsey's FIU became a member of the Egmont Group in which it plays an active role. On 2 April 2001, and following a Financial Crime Review conducted by two Senior Managers from Police and Customs, the FIU became known as the Financial Intelligence Service (the "FIS"). The mandate and mission statement of the FIS states as follows: In order to enhance this joint policy the Financial Intelligence Service shall, as far as possible, stand alone from either of its parent organizations but will remain within both Police and Customs responsibilities. The Financial Intelligence Service shall be staffed equally by Police and Customs Officers seconded for a fixed tenure under a clear line management system. The Financial Intelligence Service shall be responsible to a Service Authority constituted equally from Senior Operational Police and Customs Managers who shall in turn, be directly responsible to their respective Chief Officers. The Financial Intelligence Service will have its own budget funded equally by Police and Customs and dedicated accommodation. A Director shall be appointed from Police and Customs on the basis of a three year contract. The post of Director of the Financial Intelligence Service will be independent of both Police and Customs. Reporting parties are required to submit suspicious reports where such party knows or suspects that a person is engaged in money laundering or the financing of terrorism (Regulation 6(5) of the Regulations; Sections 39(3) and 40(5) of the POC Law; Sections 58(3), 59(5) and 60(1) of the DT Law; Sections 12 & 13 of the Terrorism Law). Although the Notes (paras. 101 and 109) state that STRs should be submitted to the FIS by FIs, there is no requirement in law to do so, and it is not clear whether the GFSC has the requisite legal authority to impose a more specific requirement than the law. The GFSC has issued Notes which include sections on the identification of complex and unusual transactions although the authority for the GFSC to do this is unclear. The FIS assists the GFSC in preparing the Notes by

providing typologies relating to money laundering (ML) and the financing of terrorism (FT).

The Notes provide examples of suspicious transactions, for example: paragraphs 92 (general indicators of suspicious activity), 136 and 139A (relating to banking), 163 (investments), 167 (fiduciary business) and 184 (insurance). Appendices B and BB outline case studies of money laundering and terrorist financing. In addition, the FIS also publishes via the GFSC's website other typologies and case studies.

There are reporting procedures prescribed by the Regulations and FIs have been provided with guidance regarding the manner of reporting (Regulation 6 of the Regulations, and Section 109 together with Appendix I of the Notes. There is no requirement in law or in the Notes that a standard form of STR be used, since the Notes state that "[i]t would be of great assistance to the FIS if disclosures were made in standard form" (Appendix I, I.1, Part 5, first bullet). However, the States Assembly (Parliament) has approved in principle the enactment of legislation that would allow the Committee to prescribe by regulation the form and manner in which STRs may be made (Clause 5(1) of the Draft Miscellaneous Provisions Law). This law will be presented to the States Assembly for approval in early 2004.

18. The FIS does not have the power in law to demand additional information from reporting parties. According to the authorities, in practice it does request such information and in most cases the required information is provided. In addition, FIs, relying on Tournier v. National Provincial and Union Bank of England (1924), are permitted to disclose information in order to protect the public and their own interests.

If the requisite information fails to be forthcoming, the FIS may seek to obtain a production order in serious or complex fraud cases from the Attorney General (Section 1 of the Fraud Investigation Law) or in other types of cases from a judge (Sections 45 and 46 of the POC Law, Sections 63 and 64 of the DT Law, and Section 36 and Schedule 5 of the Terrorism Law). To obtain a production order there must be reasonable grounds for doing so and depending on the legislation other criteria may also need to be met prior to the order being granted.

Finally, the Draft Miscellaneous Provisions Law (Clause 5(2) states that regulations made under the Law may provide that such regulations may include a request as part of the STR form to the submitter of an STR to provide additional information.

19. Real time searches are possible on the Customs and Police databases by virtue of the fact that the FIS is staffed by Police and Customs Officers. Immigration details are also available as the Immigration Department is under the same management structure as the Customs Department and has a common Chief Officer. The FIS is able to search using the Police National Computer. The FIS also has access to records such as vehicle registration, company records, court judgments, passport, land and property title documents, and many other government departments. In addition, the Draft Miscellaneous Provisions Law (Clause 21) provides that the States Income Tax Authority will be permitted to disclose information for the purpose of, for example, facilitating a determination of whether any criminal investigation should be initiated or terminated (Clause 21 2)(e).

The FIS also subscribes to commercial databases through which credit reporting and other records can be obtained. The FIS can call for an individual's credit records for a fee through the various commercial databases it subscribes to. In addition, the FIS liaises with the GFSC's Fiduciary Services and Enforcement Division in order to obtain information from the GFSC.

20. Although the FIS is not authorized by law to order sanctions or penalties, the GFSC may do so under its broad administrative powers with respect to FSBs. See response to Criterion 5.

With respect to criminal sanctions, failure to disclose knowledge or suspicion of ML connected with drug trafficking is an offense punishable with up to five years imprisonment (Section 60 of DT Law). Failure to disclose knowledge or suspicion of other crimes is not currently an offense but will become so in the near future (Sections 1 and 2 of Draft Miscellaneous Provisions Law).

21. The FIS is authorized to disseminate financial information and intelligence to domestic authorities for investigation when there are grounds to suspect ML or FT (Section 43 of the POC Law). The FIS routinely disseminates intelligence to various agencies within Guernsey for the purposes of the investigation of crime in Guernsey whether on its own initiative or upon request.

22. The FIS is authorized to share financial information, either on its own initiative or upon request, outside Guernsey with respect to all crimes other than drug trafficking and terrorism (Section 44(1) of the POC Law) and, according to the authorities, common law would so allow for other disclosures. The FIS primarily exchanges intelligence with other FIUs within the Egmont Group.

The FIS also seeks to enter into memoranda of understandings with other FIUs should this be a requirement of their domestic legislation in order to facilitate an exchange of intelligence (although the FIS locally does not have any such pre-condition in order to cooperate with third parties), such as Belgium and France.

There are adequate safeguards to protect any information disclosed outside Guernsey under the POC Law (Section 44(1) of the POC Law). Information may be exchanged outside Guernsey for the purposes of the investigation of crime or criminal proceedings to a 'competent authority.'

In general, information exchanges by law enforcement authorities are governed by codes of practice, such as the Intelligence Material Code of Practice, and the DP Law. The codes of practice set out procedures for the recording and dissemination of information. In addition, the codes set out the principles that govern these functions, which, for example, require that where it is necessary to keep the source of intelligence confidential, a record will be kept separately of the source's identity. Under the Data Protection Law, law officers are required to undertake risk assessments prior to intelligence being released externally. The risk assessment is required to consider issues such as the source, subject and content of the intelligence paying due regard to the human rights and security of all concerned, while taking into account the jurisdiction to which the material may be sent. For example, the eighth principle of the DP Law prohibits the transfer of personal data outside Guernsey unless that country "ensures an adequate level of protection for the rights and freedoms of data subjects in relation to the processing of personal data" (para. 8, Part I, Schedule I of DP Law).

23. Statistics are kept by FIS as part of its function relating to amounts of property frozen, seized and confiscated relating to proceeds of crime, drug trafficking, money laundering and financial terrorism.

	2000	2001	2002
Number of Disclosures	482	605	777

- **STRs resulting in investigation, prosecution, or convictions;**

Statistics and records are kept. There is a number of ongoing money laundering investigations. However, no company or person has been convicted of Money Laundering in Guernsey.

- **Requests for assistance received by the FIS or other competent authorities, from both domestic and foreign authorities, as well as the number of responses provided to the requests received;**

The FIS maintains good records in relation to this information.

Example:

	2000	**2001**	**2002** (Half Year)
Request for Assistance	154	170	139
Of which:			
Internal	84	87	90
External	70	83	49

- **Spontaneous referrals made by the FIU or other competent authorities to both domestic and foreign authorities;**

Records are kept on all referrals made by the FIS to other competent authorities. Following examination of STRs the FIS refers most of them (50-60 percent) to NCIS. If the STR referred to a resident of Ireland for example.

The STR would be forwarded to the FIU in Ireland.

- **If the jurisdiction requires the reporting of large currency transactions, statistics should be kept on the number of reports filed.**

The Bailiwick of Guernsey has no legislation which requires reporting large currency transactions. However cash seizures occur under the Drug Trafficking (Bailiwick of Guernsey) Law 2000. This law covers the seizure and detention of cash both import and export. It empowers Law Enforcement/Customs and Excise to forfeit and confiscate cash on a civil standard of proof i.e. the balance of probability in respect of cash suspected to be involved in drug trafficking. A soon to be enacted Miscellaneous Provisions Law will provide for the seizure of cash on an 'all crimes' basis.

24. The FIS as currently structured and funded is capable of performing its functions, however it is not working at maximum capacity due to shortage of staff as outlined in Criteria 6 and a dramatic increase in work load (the number of STRs rose by 100 percent over last 5 years). The FIS requires two further Financial Investigators, to bring the unit to the recommended and approved strength and the support of a Financial Analyst and an administrative assistant.

Following a review of the FIS's first year of operations the Service Authority recommended to the Chief Officers (Police and Customs) that the resources allocated to it be increased. In addition, the Service Authority also sought additional increases in staff to their respective Commercial Fraud Departments. The Chief Officers supported the recommendations and subsequently obtained the necessary approval of the relevant Government departments to increase the FIS's staff and that of the Custom & Excise Fraud and International team. In addition, the Chief Officer of Police secured a five year housing license for a former Metropolitan Police Financial Investigator who is now supplementing the established complement of the Police's Fraud and External Affairs Department.

The Director of FIS is accountable to the Chief Officers of Police and Customs and Excise through the Service Authority. The Director of FIS manages the operations/investigations and ensures that its functions are properly executed. All staff appointed to FIS from Police/Customs and Excise, are on a fixed tenure basis. The organizational structure is of high standard, with very good work practices. Where the FIS becomes aware of an institution's failure to report suspicions, the FSC is informed.

The Guernsey FIS/FIU unit has sufficient independence and autonomy to ensure its functions are performed without interference on its day to day activity as it is controlled and directed by a Director whose position allows a certain amount of independence for Police and Customs and Excise.

The situation with all law enforcement FIS/FIU there are matters and decisions to be made from time to time that require advice from the law officers or senior personnel within the Police Authority and Customs Authority, which is readily available to the Director.

The procedures used in recording analyzing and disseminating information ensures that the information and intelligence is properly protected and lawfully disseminated to investigation units or exchanged with international law enforcement authorities in accordance with the laws of the Bailiwick of Guernsey.

The FIS/FIU publishes from time to time articles in the Compliance Officers Association Newsletter and on the Guernsey Financial Commission website on its role, statistics, typologies and trends. The unit submits periodic reports to the Egmont website. The FIS submits an annual report to the Bailiwick Financial Crime Committee. A less detailed version of the report was circulated to other external bodies and interested parties.

Analysis of Effectiveness

Arrangements for processing, receiving, analyzing, and disseminating financial information are generally adequate. The framework would be strengthened if the law required the reporting of suspicious transactions to the FIS, made failure to report, a crime and gave the FIS the power to require additional information from reporting parties without a production order. The general arrangements would also be strengthened if the staff complement of the FIS was increased by at least two persons.

Recommendations and Comments
Legislation should be adopted along the lines of the Draft Law (Sections 1 and 2) to make it a crime to fail to report a suspicious transaction, as in the DT Law, rather than as a defense to the crime of money laundering. In addition, legislation should be considered along the lines of the Draft Miscellaneous Provisions Law (Section 5) to provide that STRs should be submitted to the FIS on a form to be prescribed by law, with appropriate penalties. This draft law is expected to be considered by the States Assembly by the end of 2003. Finally, consideration should be given to providing authority in law to the FIS to require additional information from reporting parties, without the need to meet the burden of proof required for a production order. The provision in the Draft Miscellaneous Provisions Law that such regulations may include a request as part of the STR form to the submitter of an STR to provide additional information does not appear to be sufficient for this purpose. Consideration should be given to amending the relevant laws to provide explicit legal authority for the GFSC to issue guidance notes. *The Guernsey authorities should implement plans to increase the staff of the FIS by two intelligence officers as soon as is practicable.*
Implications for compliance with FATF Recommendations 14, 28, 32
Compliant
IV—Law enforcement and prosecution authorities, powers and duties (compliance with criteria 25–33)
Description
25. *The responsibility to ensure that ML and FT offenses are properly investigated rests with the Police and Customs and Excise. The FIS/FIU is also able to carry out this task as it is staffed with personnel from Police and Customs and Excise.* *Prior to obtaining/serving production orders or warrants, the consent/authority of a Law Officer is required. The structure of Law Enforcement ensures that all offenses are properly investigated.* 26. The use of covert and investigative measures are permitted by common law and governed by codes of practice (internal guidelines) issued by the Police and Customs. Courts in Guernsey have accepted the use of a wide range of investigative techniques, such as controlled delivery, undercover operations and covert and intrusive surveillance. The States of Guernsey have agreed in principle to the enactment of a law based upon the UK's Regulation of Investigatory Powers Act 2000. The proposed law will provide for the interception of communications, the carrying out of surveillance, and the use of covert intelligence sources. The UK Act does not contain provisions relating to controlled deliveries, and therefore such provisions are not contained in the Guernsey proposal. *The Guernsey FIS/FIU and other law enforcement units tasked with enforcing ML and FT matters use all investigative techniques including covert, overt and intrusive measures that are legally at their disposal in the Bailiwick of Guernsey. These matters are dealt with on a case by case basis and the investigation teams consult regularly with their Attorney General for directions and advice.* 27. Law enforcement authorities are able to compel production of bank records and other records maintained by FIs through lawful process (Sections 45 & 46 of the POC Law; Sections 43 & 44 of the Terrorism Law). Law enforcement authorities are also able to compel production of bank records and other records maintained by FIs through lawful process (Sections 45 & 46 of the POC Law; Sections 63 and 64 of DT law; Section 36 of the Terrorism Law and Section 1 of the Fraud Investigation Law). 28. *The FIS/FIU is an inter-agency type unit, therefore "Task Force" style enquiry teams, are a regular feature of how Guernsey investigate/prosecute ML/FT and predicate offenders, where the need arises. There is a culture of partnership work and clear understanding that this style of enquiry team is necessary to achieve results in complex investigations of ML/FT.* 29. *This has been addressed at Criteria 24 and I am satisfied that the FIS/FIU Service Authority conduct reviews annually which has resulted in increased resources of FIS/FIU and commercial fraud departments of Police and Customs and Excise.* *Resources are in place to prosecute/enforce the legal means for effective implementation of the ML and FT laws. It is however clear that the number of STRs and external request for assistance in relation to ML and FT continue to increase annually. The Islands Authorities should therefore continue to review and support requests*

from the FIS's Service Authority for any additional resources that are considered necessary to maintain current levels of effectiveness.

The FIS/FIU have secured some funding and consultants to develop their IT needs, those being the need for a rationalization and introduction of a new computer system in order to enhance and streamline their capabilities of monitoring the receipt, analysis and dissemination of STRs which will benefit them in their overall investigations.

30. *Statistics of the number of ML and FT investigations, prosecutions and convictions where the investigation was initiated on the basis of an STR are recorded, by FIS.*

Due to lack of feedback from Foreign Jurisdictions to the Bailiwick of Guernsey, the FIS/FIU is unable to give an accurate figure in respect of convictions for ML and FT investigations.

Despite several money laundering investigations, no domestic prosecution has taken place in Guernsey. Following the arrest/charge of persons for predicate offenses, a preliminary financial investigation is carried out in every case where an offender is being tried on indictment.

This investigation is conducted in order to aid the gathering of additional evidence to support the predicate offense and also to ascertain if the criminals concerned have benefited financially from criminal conduct and have assets that could be confiscated.

31. *The Guernsey FIS and Law Enforcement units examine typologies and trends on regular reviews on an interagency basis in the financial crime group and terrorist financing team and new typologies or trends identified are then disseminated to the operational people at the coal face and in a limited number of cases new typologies may well be published via the Commissions website.*

32. *Members of the FIS are skilled in the administrative, investigative, prosecutorial and judicial aspects of enforcing the law on ML and FT. All law enforcement officers have undergone training that's available to financial investigators in the UK. Additionally local training courses are conducted to increase the investigation/technical knowledge that is needed in Guernsey, e.g., areas relating to trust funds. The key personnel appear to have all the skills and technical knowledge to enable them to perform their functions adequately and are in a position to train and pass on their skills. Officers are encouraged to attend lectures given on the Bailiwick from the private sector.*

Law enforcement personnel in the Bailiwick of Guernsey are professional in their approach, to tracing property suspected of being the proceeds of crime or used in the finance of terrorism and they are skilled in obtaining seizure, freezing and confiscation orders to remove those assets.

A number of officers in the Guernsey FIS/FIU units have undergone special training in financial investigations and have obtained accreditations on a level of the financial investigators provided by the Home Office Center of Excellence in the UK.

33. *The Financial Crime Committee and the Financial Crime Group play an important role in providing advice and guidance on best practices to the FIS. This includes guidance that is based on evolving international standards and best practice.*

Additionally the Bailiwick of Guernsey law enforcement publish their financial crime strategy annually, which is circulated to all relevant parties including the Attorney General's chambers and the Commission. This document identifies problems encountered and indicates how they were addressed.

In order for the authorities and investigation units of the Bailiwick of Guernsey to be successful, the personnel involved attend international conferences to keep themselves abreast of current trends of combating money laundering and identifying methodologies used to finance terrorism,

The law enforcement agents in the Bailiwick of Guernsey make use of the partnership approach, to identifying proceeds or property to finance terrorism.

Analysis of Effectiveness

The general framework for the powers and duties of law enforcement and prosecution authorities is considered to be adequate. The framework would be strengthened if sufficient funding were made available for technical support requirements of the FIS *and if the planned legislation on investigatory powers included provision for*

controlled delivery.
Recommendations and Comments
Consideration should be given to including controlled delivery in the proposed legislation on investigatory powers. *Funding should be made available for the development of the FIS' IT resources. This technical support is essential for its future effectiveness and success especially in light of the continuing increase in STRs.*
Implications for compliance with the FATF Recommendation 37
Compliant
V—International Cooperation (compliance with criteria 34–42)
Description
34. There are laws and procedures which provide for mutual legal assistance regarding the use of compulsory measures including the production of records, search of persons and premises (Sections 4 & 7 of the CJIC Law). The following laws allow for the widest possible range of mutual legal assistance in AML/CFT matters: • The Fraud Investigation Law, Section 1; • The POC Law, Sections 45 and 46; • The DT Law, Sections 63 and 64; • The Terrorism Law, Section 36 and Schedule 5, paras. 1 and 4; • The CJIC Law, Sections 4 and 7; • The Terrorism Order, Article 10; and • The Al-Qa'ida Order, Article 18. Production orders or warrants may be issued to obtain records from FIs or private individuals (section 1 of the Fraud Investigation Law, sections 45 and 46 of the POC Law, sections 63 and 64 of the DT Law and section 36 and schedule 5 of the Terrorism Law). If a warrant is issued searches may be made of business premises and private dwellings. These laws do not contain provisions which compel persons to make witness statements for use in court proceedings. However, in practice many financial services businesses permit their employees to make full witness statements. Testimony under oath for use in another jurisdiction can be obtained under section 4 of the CJIC Law in connection with all types of criminal investigations and prosecutions. Search warrants can be obtained under section 7 of the 2001 Law. The only restriction is that, before a warrant is issued, it must be shown that the conduct constituting the offense under investigation would have constituted a criminal offense punishable with imprisonment if it had occurred in Guernsey. There are appropriate laws and procedures relating to the following: (i) Production or seizure of information: Section 1 the Fraud Investigation Law; Sections 45 and 46 of the POC Law; Sections 63 and 64 of the DT Law; Section 36 and Schedule 5 of the Terrorism Law; and Sections 4 and 7 of the CJIC Law. (ii) Taking of statements: Witnesses are required to provide information and documents (the Fraud Investigation Law (Section 1), POC Law (Section 45), DT Law (Section 63) and Terrorism Law (Section 36 and Schedule 5 (para. 4). They cannot be required to make formal witness statements under the law of the requesting state. However, many FIs do allow their employees to make formal witness statements under the law of the requesting state. In cases where a formal witness statement is not made, evidence under oath which can be used in a foreign court can be obtained in connection with all types of criminal investigation under section 4 of the CJIC Law. (iii) Identification, seizure etc: The identification of assets can be achieved under the legislation referred to under (i) above.

The freezing and confiscation of assets may be achieved under Part I of both the POC and DT Laws, and Section 18 and schedule 2 of the Terrorism Law.

The provisions of section 8 of the CJIC Law may be used to freeze instrumentalities.

Assistance may be provided in connection with criminal proceedings or criminal investigations (Section 4 of the CJIC). Assistance may also be provided in investigations and proceedings where persons have committed both the money laundering and the predicate offense under the provisions of sections 45 and 46 of the POC Law, sections 63 and 64 of the DT Law and sections 4 and 7 of the CJIC.

35. *The Guernsey FIS has procedures and structures in place that use all available legislation to provide assistance to foreign authorities on the question of international investigation of ML/FT. The publication entitled "Mutual Legal Assistance" and the Bailiwick of Guernsey clearly sets out guidelines and notes, to obtain mutual legal assistance in Guernsey. In order that mutual assistance is achievable the FIS/FIU in Guernsey is capable of sharing information and intelligence with FIUs in other jurisdictions as they are members of the Egmont Group.*

There is no impediment within the Bailiwick of Guernsey and their legislation makes no distinction in the mental element of an offense and does not preclude assistance being given by the Bailiwick of Guernsey. Therefore dual criminality is not a precondition in mutual legal assistance.

Arising from statistics produced, all appropriate efforts are taken by the investigation agencies in the Bailiwick of Guernsey to provide a uniform and effective response to requests. It is obvious from the statistics that the investigation units in Guernsey respond to follow-up requests in the most expeditious manner possible.

Statistics on request are by the FIS and other relevant agencies.

36. On September 30, 2002, a letter was lodged with the Council of Europe by the United Kingdom's representative to the Council indicating that the 1990 Convention on Money Laundering etc., will extend to Guernsey as from 1 January 2003. On 15 August 2002, Guernsey's authorities asked by letter that the United Kingdom seek ratification on Guernsey's behalf of the United Nations Convention for the Suppression of Terrorist Financing. Ratification will be sought for the Palermo Convention, the Council of Europe Convention on Corruption and the OECD Convention on Corruption as soon as the necessary legislation has been passed by the States of Guernsey. The FIS has MOUs with TRACFIN in France and CTIF in Belgium. Generally, however international cooperation is supported through informal mechanisms.

The GFSC has entered into a number of MOUs. Please refer to the response to criterion 67 for further details. However, the GFSC does not require an MOU to have been executed with foreign supervisors/regulators or law enforcement bodies before exchanging information with them.

37. According to the authorities, the law enforcement authorities are permitted under common law to exchange information regarding the subjects of investigations with their international counterparts. No agreements or MOUs are needed for this purpose.

Appropriate statistics are maintained, however information on the resolution of cases is not up to date. This is due in part to poor feedback from the requesting countries.

38. Law enforcement authorities in Guernsey are able freely to cooperate with investigations being conducted in other jurisdictions. Foreign investigators are able to come to Guernsey and accompany local officers when production orders and warrants are served. Although not expressly provided by statute, controlled deliveries, particularly in connection with drug trafficking, are used in connection with enquiries.

Production orders in fraud investigations are issued by the Attorney General (section 1(2) of the Fraud Investigation Law). Production orders issued under section 45 of the POC Law, section 63 of the DT Law and section 36 and schedule 5, paragraph 4 of the Terrorism Law are issued by a judge. In all cases warrants are issued by judges (section 1(4) of the Fraud Investigation Law, section 46 of the POC Law, section 64 of the DT Law and section 36 and schedule 5, paragraph 1 of the Terrorism Law).

39. *The authorities in the Bailiwick of Guernsey are more than anxious/capable to coordinate action locally and internationally to coincide with law enforcement action in any jurisdiction.*

On the question of sharing of confiscated assets there is no legislation in Guernsey for the sharing of assets, however, the Bailiwick of Guernsey has on a case by case basis entered into agreements to share assets with other jurisdictions, for example assets voluntarily repatriated to the USA where a proportion has been shared with the Bailiwick of Guernsey. *Guernsey law enforcement authorities have partaken in joint investigation teams with other jurisdictions. This involved the execution of warrants in Guernsey simultaneously with law enforcement conducting operations elsewhere.* 40. The Extradition Act 1989 (United Kingdom) as extended to Guernsey permits the extradition of those wanted in other jurisdictions for money laundering and terrorist financing offenses. All persons resident in Guernsey, if wanted in connection with criminal activity in another jurisdiction, are liable for extradition under the Extradition Act 1989. 41. *Guernsey's Immigration Act sets out certain requirements for non-European nationals wishing to take up residence in the Bailiwick. If immigration officials are satisfied that applicants are not conducive to the public good for permanent residency in Guernsey they are refused admission.* *Special Branch and customs officers monitor all persons arriving in Guernsey and are familiar with any wanted posters on criminals or on known terrorist or suspected terrorists. Therefore these persons are closely monitored and policed at points of entry to Guernsey.* *Any person identified with residence in Guernsey who is wanted in connection with a terrorist related crime is liable to extradition under the provisions of the Extradition Act 1989.* *Any foreign national from outside the EU area of common travel is required to seek permission to enter or leave the island and in a number of cases a visa is required by foreign nationals before permission is granted for them to enter the island. Prior to the granting of such visa all law enforcement data based on criminal/terrorism connections will be examined in order for the authorities to make a decision.* *42. Guernsey has adequate resources that are committed to fully investigating and dealing with requests for assistance from other jurisdictions that are involved in the international fight of money laundering and financing terrorism.*
Analysis of Effectiveness
There is an adequate framework for international cooperation.
Recommendations and Comments
Implications for compliance with FATF Recommendations 3, 32, 33, 34, 37, 38, 40, SR I, SR V
Compliant

Assessing preventive measures for financial institutions

30. In order to assess compliance with the following criteria assessors must verify that: (a) the legal and institutional framework are in place and (b) there are effective supervisory/regulatory measures in force that ensure that those criteria are being properly and effectively implemented by all financial institutions. Both aspects are of equal importance.

Table 5. Detailed Assessment of the Legal and Institutional Framework for Financial Institutions and its Effective Implementation

I—General Framework **(compliance with criteria 43 and 44)**
Description
43. There is no obligation of secrecy or confidence or other restriction on the disclosure of information related to money laundering or the proceeds of criminal activity (Section 1 of the 1995, 1998 & 2001 Laws). It is an implied term of the contract between a banker and his customer that the banker will not divulge to third persons, without the express or implied consent of the customer, either the state of the customer's account, transactions made etc. unless the banker is compelled to do so: a) on order of a Court; b) the circumstances give rise to a public duty of disclosure; or c) the protection of the bank's own interests requires it (Tournier v. National Provincial and Union Bank of England [1924] IKB461). Guernsey laws contain provisions which state that a person does not breach any confidentiality obligations when a disclosure is made to a police officer (Sections 39(3) (b) and 40(5) (b) of the POC Law; Sections 58(3) (a) and 59(5) (a) of the DT Law; Section 16 of the Terrorism Law; and Section 1 of the 1995 Law). 44. The Commission Law provides the GFSC with general powers to combat money laundering, the financing of terrorism and financial crime, as follows: 2. (2) The general functions of the Commission are: (d) the countering of financial crime and of the financing of terrorism; and in this paragraph "financial crime" includes any offense involving . . . (i) fraud or dishonesty; (ii) misconduct in, or misuse of information relating to, a financial market; or (iii) handling the proceeds of crime. . . . 4. In the exercise of its functions the Commission may take into account any matter which it considers appropriate, but it shall in particular have regard to – (a) the protection of the public interest, including protection of the public against financial loss due to dishonesty, incompetence or malpractice by persons carrying on finance business; and (b) the protection and enhancement of the reputation of the Bailiwick as a financial center. The GFSC is the sole agency in Guernsey responsible for supervision of FSBs.
Analysis of Effectiveness
Guernsey has an adequate mechanism for the implementation of its AML/CFT framework. The GFSC has authority to ensure effective implementation of AML/CFT policies for all regulated FIs. While the GFSC has power under the Regulations to monitor compliance of businesses that engage in bureau de change activities, check cashing and money transmission services ("MSBs"). It does not currently have the authority to regulate MSBs, except to the extent that a bank or other regulated financial institution engages in such activities.
Recommendations and Comments
Consideration should be given to enacting a law to regulate MSBs.
Implications for compliance with FATF Recommendation 2
Compliant
II—Customer identification **(compliance with criteria 45-48 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 68-83 for the banking sector, criteria 101-104 for the insurance sector and criterion 111 for the securities sector)**
Description

45. The Regulations require FIs to establish and maintain procedures for customer identification (Article 3). However, the Regulations contain no explicit requirement that such procedures be followed by FIs, although such a requirement is clearly implied from the language of the Regulations. While there is no explicit requirement in law prohibiting anonymous accounts or accounts in fictitious names, Regulation 3(1) of the Regulations requires customer identification for the forming of a business relationship, a significant one-off transaction (over £10,000), or two or more linked transactions.

Paragraph 67B of the Notes states that, FSBs must not open or operate financial services products held in obviously fictitious names. Anonymously operated financial services products should similarly not be allowed

46. FIs are required to identify their customers whether long term or occasional over a specified threshold, on the basis of evidence of identity which is reasonably capable of establishing that the applicant is who he claims to be and record the identity (Regulation 3 of the Regulations; see also Sections 38, 39 & 75 of the Notes).

While legal entities are covered by the customer identification requirements of the Regulations as they are for any applicant for business (Regulation 3 and Section 2 of the Interpretation Law), there is no explicit provision in law relating to obtaining information on (a) the legal entity's legal form and directors; (b) whenever it is necessary, in order to know the true identity of the customer, requiring FIs to request information from the customer concerning the principal owners and beneficiaries; and (c) provisions regulating the power to bind the entity, and requiring FIs to verify that any person purporting to act on behalf of the customer is so authorized, and to identify those persons.

Paragraph 38 of the Notes states that:

> "A financial services business undertaking verification should establish to its reasonable satisfaction that every verification subject relevant to the application for business actually exists. All the verification subjects of joint applicants for business should normally be verified. However, where the guidance implies a large number of verification subjects it may be sufficient to carry out verification to the letter on a limited group only, such as the senior members of a family, the principal shareholders, the main directors of a company, etc."
>
> Paragraph 75 indicates that valid passports, national and armed forces identity cards and drivers' licenses with photographs are the best form of identification. The paragraph indicates that documents which can be easily obtained such as birth certificates, credit and business cards, national health or insurance cards, provisional drivers' licenses and student union cards should not be accepted uncritically.

Paragraphs 84 and 85A of the Notes indicate that the relevance and usefulness of the following documents should be carefully considered :

- certificate of incorporation;
- details and identification documentation of beneficial owners;
- Memorandum and Articles of Association;
- Powers of Attorney (including identification documentation); and
- resolution, bank mandate, signed application form or any valid account-opening authority, including full names of all directors and their specimen signatures.

Paragraph 62 of the Notes stresses that, "the best time to undertake verification is not so much at entry as prior to entry." Wherever possible, verification should be completed before any transaction is undertaken.

Paragraph 30 of the OPP indicates that relationships should be reviewed for any deficiency in verification documentation following the occurrence of a trigger event. Appendix 2 lists a number of possible trigger events.

There is no specific requirement to record the customer's identity when undertaking transactions over a specified threshold.

Paragraph 141C of the Notes deals with Powers of Attorney and states:

"Verification should be made on the holders of Powers of Attorney as well as the client, and financial services businesses should ascertain the reason for the granting of the Power of Attorney."

Paragraph 39 indicates that a financial services business should primarily carry out verification in respect of the parties operating the financial services product. Where there are underlying principals, however, the true nature of the relationship between the principals and the signatories should be established and appropriate enquiries performed on the former, especially if the signatories are accustomed to act on their instruction. In this context principals should be understood in its widest sense to include, for example, beneficial owners, settlors, controlling shareholders, directors, major beneficiaries etc, but the standard of due diligence will depend on the exact nature of the relationship.

Paragraphs 57–60 of the Notes outline practices to be followed where "reliable introductions" are used. Under the regime a reliable introducer may maintain introduction records but must undertake to supply copies of such records to the FSB on demand.

The language "the relevance and usefulness ...of the following documents... should be carefully considered" does not clearly indicate what standard the GFSC expects licensees to meet. The GFSC has issued draft revised Notes which will address this concern.

Guernsey, the Isle of Man and Jersey have jointly issued a paper outlining the direction to be taken in the AML legal and regulatory frameworks in each jurisdiction. This paper which does not replace the existing Guidance Notes focuses on issues related to the verification of customer identity. Among the many aspects of identity verification addressed in the paper are the issues of introduced business and the verification of identity of customers whose relationship with financial institutions pre-dates the all-crimes anti-money laundering legislation (Progressive Program). Unlike the existing framework where an introducer can hold verification documents to be made available to the "accepting party" on request, the paper envisages that an "accepting party" will always hold either originals or copies of these documents. In terms of the Progressive Program the paper envisages that where FIs discover any deficiencies in existing verification documents they should seek to obtain necessary information to address the deficiency. It proposes that this work be undertaken on the basis of risk prioritization and trigger events.

47. FIs are required to take reasonable measures to obtain information about the true identity of applicants who appear to be acting otherwise than as principals (Regulations 3 and 4 of the Regulations; see also Section 48 of the Notes). With respect to "an applicant for business that is or appears to be acting otherwise than as principal" (Regulation 4(1), Regulation 4(2) states that "[i]dentification procedures maintained by financial services businesses in respect of applicants to whom this paragraph applies shall require reasonable measures to be taken (as prescribed in the Notes) for the purpose of establishing the identity of any person on whose behalf the applicant for business is acting."

Paragraph 38 of the Notes states that, a financial services business undertaking verification should establish to its reasonable satisfaction that every verification subject relevant to the application for business actually exists.

Paragraph 48 of the Notes adds that:

Where a financial services business suspects that there may be an undisclosed principal (whether individual or corporate), it should monitor the activities of the customer to ascertain whether the customer is in fact merely an intermediary. If a principal is found to exist, further enquiry should be made and that principal should be treated as a verification subject. A financial services business should also consider carefully whether the existence of an undisclosed principal raises suspicion that it is dealing with the proceeds of criminal conduct.

48. There is no provision of law that requires FIs to include accurate and meaningful originator information on funds transfers and related messages that should remain with the transfer or related message through the payment chain. Originator information should include name, address, and account number (when being transferred from an account). The Commission has issued draft revised Regulations and Notes for consultation which will incorporate provisions on funds transfers and other messages into legislation.

The Notes do not explicitly provide for recording originator information, but Section 126 refers to the retention of records for electronic or wire transfers with sufficient detail to enable the identification of the remitting customer and "as far as possible" the identity of the ultimate recipient. The section also requires that in all cases wherever possible the originator's details should remain with the transfer or related message throughout the payment chain. Full records of the originating customer and address should be retained by the financial services business.

Institutions visited generally had comprehensive procedures for verification of customer identity. In most cases there were more stringent requirements in respect of persons from Non-Appendix C countries. All institutions required the verification of identity of beneficial owners. In general the procedures adopted by institutions complied with the requirements of the Notes. None of the procedures reviewed covered the "progressive programme" of verification (i.e. verification of identity for persons who were customers of financial institutions prior to the enactment of money laundering legislation. There were also varying approaches adopted by institutions in respect of the progressive programme.
Analysis of Effectiveness
Measures in place for the verification of the identity are generally adequate although there are some concerns. relating to instances in which the language of the Notes could be strengthened to better communicate the standard which the Commission expects of licensees, the program for introduced business and the variation in practices used by institutions in relation to the progressive program for verification of customer identity.
Recommendations and Comments
The relevant laws should be amended to explicitly require that customer identification procedures be followed. The language of paragraph 84 and 85A "the relevance and usefulness ...should be carefully considered" as well as the language of paragraph 75 "documents that can be easily obtained ...should not be accepted uncritically" should be amended to clearly communicate the standard that is expected of FSBs. The GFSC has issued draft revised Guidance Notes for consultation which will address this concern. Since the Notes require the originator details to remain with the transfer throughout the payment chain, it is recommended that they be clarified and strengthened to specifically require the inclusion of the information in the first place. The GFSC has issued draft revised regulations and Notes for consultation which will address this concern. The GFSC should communicate to banks that decisions taken on establishing relationships with higher risk customers should be taken by senior management. The GFSC has issued draft revised regulations and Notes for consultation which will address this concern. The exception provided in section 63 which provides that a senior staff member may give appropriate authority to open an account where identity has not been verified is vague and should be redrafted to clarify the kind of circumstances in which the GFSC expects this discretionary power to be used. The GFSC has issued draft revised Notes for consultation which will address this concern. The GFSC has already undertaken considerable work to direct FSBs towards the customer identification standards required by the Position Paper. It is nevertheless recommended that these efforts be redoubled to ensure a greater degree of consistency in the approach adopted by licensees.
Implications for compliance with FATF Recommendations 10, 11, SR VII
Full compliance will be achieved when FSBs have immediate access to all customer verification documents under the regime for introduced business.
III—Ongoing monitoring of accounts and transactions **(compliance with Criteria 49–51 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 84–87 for the banking sector, and criterion 104 for the insurance sector)**
Description
49. Although Regulation 6(2) of the Regulations requires an STR be filed if there is "knowledge or suspicion that another person is engaged in money laundering or that he is providing financial assistance for terrorism . . ." there is no explicit legal requirement that FIs should pay special attention to all complex, unusual large transactions, or unusual patterns of transactions, that have no apparent or visible economic or lawful purpose, to examine as far as possible the background and purpose of such transactions, to set forth their findings in writing, and to keep such findings available for competent authorities. The Commission has issued revised draft Regulations for consultation which will address this concern. Paragraph 22 of the Notes states that: Vigilance systems should enable key staff to react effectively to suspicious occasions and circumstances (for example, complex, unusual, large transactions and all unusual patterns of transactions which have no apparent

economic or visible lawful purpose) by reporting them to the relevant personnel in-house and to receive training from time to time from the FSBs to equip them to play their part in meeting their responsibilities.

Paragraph 25 of the Notes indicates that "financial servive businesses may find it useful to delegate responsibility for maintaining vigilance policy to a prevention officer. Rather than reserve to the reporting officer all such day-to day responsibility."

Paragraph 92 and Appendix G of the Notes provide general examples of unusual or questionable patterns of activity which should give rise to suspicion. This is supplemented by industry-specific examples of suspicious transactions in Part 4 of the Notes.

In addition, Appendices B and BB provide real life case studies of laundering schemes uncovered and examples of terrorist financing.

There is no specific requirement for concerns to be put in writing, and kept available for competent authorities although draft revised regulations issued by the Commission for consultation, include such a requirement. However paragraph 97 indicates that key staff should be required to report suspicion of money laundering. An appendix to the Notes provides examples of reporting forms.

50. There is nothing in the law that requires FIs to give special attention to business relations and transactions with persons (including legal entities and other financial institutions) in jurisdictions that do not have adequate systems in place to prevent or deter ML or FT. If those transactions have no apparent economic or visible lawful purpose, the background and purpose of such transactions should, as far as possible, be examined, and written findings should be available to assist competent authorities such as supervisors, law enforcement agencies and the FIU, and auditors. The Commission has issued draft revised Regulations for consultation which will address this concern.

Appendix C of the Notes refers to sensitive jurisdictions and states, that from time to time the Commission issues Business from Sensitive Sources Notices (BSSNs). Transactions to or from the jurisdictions specified in such Notices should be subject to a greater level of caution."

The Commission has issued four BSSNs which have dealt with terrorism, FATF Noncooperative Countries or Territories and other key issues. Business from Sensitive Sources Notice 4 was circulated to financial services businesses on August 22, 2002 and this highlights FATF's work to identify noncooperative countries and territories (NCCT's). It states that:

The Commission encourages money laundering reporting officers and other interested parties to visit FATF's website and apprise themselves of FATF's work on NCCT's. Financial services businesses should take particular account of the descriptions of the AML systems of all of the jurisdictions considered in the review and FATF's current attitude to those jurisdictions.

In the Commission's Position Paper entitled 'Overriding Principles for a Revised Know Your Customer Framework' jointly issued by the three Crown Dependencies the importance of risk prioritization and monitoring was acknowledged. Appendix 2 of the Position Paper gives guidance on risk profiling and trigger events and indicates that issues such as the geographical origin of the customer or the customer's activities should be taken into account.

There is no specific requirement for concerns to be put in writing, and kept available for competent authorities. The authorities have issued draft revised Notes for consultation which will address this issue.

51. There is nothing in the law that requires FIs to give enhanced scrutiny to wire transfers that do not contain complete originator information. The GFSC has issued draft revised regulations for consultation which will address this concern.

Paragraph 135 of the Notes states that vigilance should govern all stages of a bank's dealings with its customers and this includes transactions into and out of accounts generally, including by way of electronic transfer (wire transfer).

Paragraph 126 of the Notes states that:

In the case of electronic transfers (or wire transfers), financial services businesses should retain records of payments made with sufficient detail to enable them to establish the identity of the remitting customer, and, as far as possible, the identity of the ultimate recipient. In all cases wherever possible the originator's details should remain with the transfer or related message throughout the payment chain. Full records of the originating customer and address

should be retained by the financial services business.

While the procedures used by institutions visited addressed the issue of suspicious transaction reporting, in a number of instances the issue of first understanding a customer's likely pattern of activity was not satisfactorily addressed. All procedures gave examples of suspicious transactions. Most institutions provided staff with information on jurisdictions considered to have weak AML/CFT frameworks.

Analysis of Effectiveness

There are generally satisfactory arrangements in place for the monitoring of transactions. However there are concerns with respect to enhanced scrutiny for wire transfers and the reporting of unusual or complex transactions. The GFSC has issued draft revised regulations for consultation which will address this concern.

Recommendations and Comments

Within the two-year period referred to by FATF, the relevant laws should be amended to require that accurate and meaningful originator information on funds transfers remain with the transfer throughout the payment chain, and that FIs give enhance scrutiny to wire transfers that do not contain complete originator information. The GFSC has issued draft revised regulations for consultation which will address this concern.

The language of paragraph 25 of the Notes "may find it useful ... to delegate responsibility for maintaining vigilance policy" does not clearly indicate the standard that the Commission expects of licensees and should be amended. The GFSC has issued draft revised notes for consultation which will address this concern.

Implications for compliance with FATF Recommendations 14, 21, 28, SR VIII

Compliant re 14, 21 and 28. Compliance re SR VII will be determined at the end of the two year period established by FATF or at such time when required laws are in place.

IV—Record keeping (compliance with Criteria 52–54 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criterion 88 for the banking sector, criteria 106 and 107 for the insurance sector, and criterion 112 for the securities sector)

Description

52. FIs are required to retain each customer verification document in its original form for at least the minimum retention period (Regulation 5 of the Regulations). Regulation 10 defines 'customer verification document' as "a customer document obtained or created by a financial services business during a customer verification process," and 'minimum retention period' as being six years. Regulation 5 of the Regulations imposes a requirement for all records to be maintained for such period.

Paragraphs 122–129 of the Notes state what documents should be kept, for how long and cover records relating to verification. The Notes indicate that in order to facilitate any investigation it must be possible to follow the audit trail of the funds under question and this therefore necessitates adequate record keeping standards.

The records must be in a readily retrievable form and must be able to be accessed without undue delay. The retention period for all records is the minimum retention period which is defined in the regulation as 6 years from the date of the last transaction. There is provision for the FIS to require an institution to keep a record until further notice.

53. The Regulations provide for retention of all customer documents, defined in Regulation 10 as any document "relating to a customer of a financial services business' dealings with a customer or a person or entity acting on a customer's behalf." Although the term 'dealings' would appear to cover customer transactions, there is no explicit reference to customer transaction records in the definition. The GFSC has issued draft revised regulations for consultation which will address this concern.

With respect to reconstruction of transaction records, the definition of 'customer document' in Regulation 10 states that "The retention of customer documents must ensure, in so far as it is practicable, that in any subsequent investigation a financial services business can provide the relevant authorities with its section of the audit trail."

Paragraphs 122–129 of the Notes state what documents should be kept, for how long and cover records relating to verification. The Notes indicate that in order to facilitate any investigation it must be possible to follow the audit trail of the funds under question and this therefore necessitates adequate record keeping standards.

The records must be in a readily retrievable form and must be able to be accessed without undue delay. The retention period for all records is the minimum retention period which is defined in the regulation as 6 years from the date of the last transaction. There is provision for the FIS to require an institution to keep a record until further notice. Section 125 requires that the following information be maintained on transactions: Identity of the customer, beneficial owner, and any counterparty. Details of financial services product including the nature of the product, valuation, memoranda of sale and purchase, destination of funds and bearer securities, memoranda of instruction, book entries, custody of title documentation, nature and date of transaction, the forms in which funds are offered and paid. Section 127 indicates that FSBs should keep all relevant records in readily retrievable form and be able to access records without undue delay. There is no specific requirement for records to be maintained of the currency involved, and the type and identifying number of any account involved in the transaction. The draft revised regulations issued for consultation will address this concern. 54. Regulation 5(3) of the Regulations requires that "[d]ocuments retained under this Regulation shall be retained in a manner that makes their retrieval readily practicable." The Notes do not specifically require that records be available to domestic competent authorities for AML/CFT investigations and prosecutions. The GFSC however has the power to request information and undertake on-site inspection of licensees other than investment business. Most institutions visited documented requirements for the retention of records in accordance with the requirements of the Notes. In some cases there was insufficient description of the types of information that should be maintained and in one instance the AML guidelines contained no reference to a record retention policy.
Analysis of Effectiveness
The framework for record keeping is generally adequate.
Recommendations and Comments
Consideration should be given to including a reference to customer transactions in the definition of customer documents in the Regulations. The Draft Law will be considered for approval by the States Assembly in September. The GFSC has issued draft revised regulations and Notes for consultation which will address this concern. The Notes should be amended to require that records of the currency involved, and the type and identifying number of any account involved in the transaction be maintained. The GFSC has issued draft revised regulations and Notes for consultation which will address this concern.
Implications for compliance with FATF Recommendation 12
Compliant
V—Suspicious transactions reporting **(compliance with Criteria 55–57 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 101–104 for the insurance sector)**
Description
55. With respect to drug-related crimes and terrorism related crimes FIs are required to report to a police officer (a defined term which includes customs officers) transactions suspected of stemming from a criminal activity or used to finance terrorism; Sections 58(3), 59(5) and 60(1) of the DT Law; Sections 12,13, 14 and 15 of the Terrorism Law)**.** However, with respect to other serious crimes covered by the POC Law, there is no provision making failure to report a crime; Sections 39(3) and 40(5) of the POC Law. The Draft Miscellaneous Provisions Law is expected to be presented to the States Assembly for approval by the end of 2003. FIs are required to institute and maintain internal reporting procedures with respect to the filing of STRs (Regulations 6(1)–(4) of the Regulations).

Paragraph 102 of the Notes indicates that if a reporting officer decides that information substantiates a suspicion of money laundering he should disclose this information promptly to the FIS. Paragraph 97 indicates that key staff should be required to report any suspicion of laundering of the proceeds of crime either directly to their reporting officer or if the FSB so decides to their line manager for preliminary investigation in case there are known facts which negate suspicion. The GFSC has issued guidelines to assist FIs in detecting suspicious patterns of behavior by their customers (Sections 90–93 of the Notes and Appendixes B & BB to the Notes). These are drafted with the assistance of the FIS and the Attorney General's Chambers. The recognition of suspicious customers and transactions are acknowledged in paragraph 19 of the Notes as an essential part of the duty of vigilance which all financial services businesses are expected to exercise. Paragraph 92 and Appendix A of the Notes provide a general description of the relevant laws and Appendix G provides examples of unusual or questionable patterns of activity which should give rise to suspicion. This is supplemented by industry specific examples of suspicious transactions in Part 4 of the Notes. 56. FIs are protected from any liability for breach of any restriction on disclosure of information in good faith to the FIU (Sections 1 & 2 of the 1995, 1998 & 2001 Laws, sections 39 and 40 of the POC Law, sections 58 and 59 of the DT Law, section 16 of the Terrorism Law, Article 10 of the Al Qa'ida Order and Article 9 of the Terrorism Order). 57. FIs are prohibited from tipping off their customers when information relating to them is reported to competent authorities (Section 41 of the POC Law; Section 61 of the DT Law and Section 40 of the Terrorism Law). There is no explicit requirement in law that provides legal authority for the FIS or any other competent authority to give instructions to FIs or to require FIs to observe those instructions. All procedures reviewed at institutions included guidelines on the procedure for reporting suspicions to the MLRO and ultimately to the FIS.
Analysis of Effectiveness
The framework for the reporting of suspicious transactions is generally adequate except with respect to the criminalization of failure to submit a suspicious transaction report under the POC and Terrorism laws.
Recommendations and Comments
Legislation should be adopted along the lines of the Draft Law (Sections 1 and 2) to make it a crime to fail to report a suspicious transaction under the POC Law, as in the DT Law, rather than as a defense to the crime of money laundering. Consideration should be given to providing the FIS with the authority to give instructions to reporting entities or to require FIs to observe instructions of the FIS. The wording of Section 102 of the Notes should be amended to address suspicion that funds have been used to finance terrorism. The GFSC has issued draft revised Notes for consultation which will address this concern. The use of the term "key staff" in paragraph 97 of the Notes in reference to the reporting of suspicions may suggest that only certain staff have a duty to report. The wording should be amended to make it clear that all staff have a duty to report suspicions. The GFSC has issued draft revised Notes for consultation which will address this concern..
Implications for compliance with FATF Recommendations 15, 16, 17, 28
Full compliance will be achieved when there is legislation along the lines of the Draft Law (Sections 1 and 2) to make it a crime to fail to report a suspicious transaction, as in the DT Law, rather than as a defense to the crime of money laundering. It is expected that the draft law will be considered by the States Assembly by the end of 2003.

VI—Internal controls, Compliance and Audit
(compliance with Criteria 58-61 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 89-92 for the banking sector, criteria 109 and 110 for the insurance sector, and criterion 113 for the securities sector)

Description

58. FIs are required to establish and maintain internal procedures and policies including employee training programs (Regulations 1(1) (a) and 7 of the Regulations). However there is no explicit reference in the law to an audit function to test the system. The GFSC has issued draft revised Regulations for consultation which, will include an explicit reference in law.

Regulation 7 of the Regulations requires that FIs "ensure that key staff receive comprehensive training in (1) the relevant laws; (2) vigilance policy (including vigilance systems); (3) the recognition and handling of suspicious transactions; and (4) the personal obligations of all key staff under the relevant laws."

The Notes require FSBs to establish internal procedures to protect themselves from abuse through money laundering and the financing of terrorism. Paragraph 20 indicates that FSBs perform their duty of vigilance by having in place systems which enable them to ensure that internal audit and compliance departments regularly monitor the implementation and operation of vigilance systems.

Section 131 indicates that FSBs are required to ensure that both existing and new employees receive comprehensive training in relevant laws, vigilance policy (including related systems, the recognition and handling of suspicious transactions and the personal obligations of all key staff under relevant laws. There is no specific requirement for staff to be informed of new developments, trends and techniques of money laundering and financing of terrorism. The GFSC has issued draft revised Guidance Notes for consultation which will address this concern.

59. FIs are required to institute and maintain procedures to identify a person to whom a suspicious report can be made (Article 6 of the Regulations). However, the Regulations contain no explicit requirement that such procedures be followed by FIs, although such a requirement is clearly implied from the language of the Regulations. FIs are required to "institute and maintain clear internal reporting procedures which . . . identify a person as the reporting officer and provide the name and title of that person" to the GFSC and FIS (Regulation 6(1) of the Regulations). The definition of a 'reporting officer' is "a senior manager . . . [with] responsibility for vigilance policy and vigilance systems, to decide whether suspicions should be reported and to report to the police if he so decides." (Regulation 10 of the Regulations).

As part of its licensing requirements the GFSC requires each licensed entity to have a designated Compliance Officer and a Money Laundering Reporting Officer.

Paragraph 24 of the Notes states that:

> Financial services businesses must appoint a Reporting Officer. The designated person should be the point of contact with the FIS in the handling of cases of suspicious customers and transactions. The Reporting Officer should be a senior member of staff with the necessary authority to ensure compliance with these Guidance Notes. The name of the Reporting Officer must be communicated to the FIS and also to the Commission.

The GFSC requires the prior notification of the appointment of a designated Compliance Officer and Reporting Officer and a Personal Questionnaire (Form PQ) must be completed and submitted to the Commission for approval. Any changes in the designated Compliance Officer/Reporting Officer must be notified to the Commission together with an explanation as to the reason for the changes.

60. Financial services businesses which carry on investment business licensed by the GFSC are covered by the Investment Licensees Rules which have been issued pursuant to Section 12 of the POI Law. Part 5.01(3) of the Rules states that:

> "A licensee should establish and maintain systems to ensure that its employees are suitable, adequately trained and properly supervised, and these systems should include arrangements –
>
> (a) to cover recruitment procedures, including the vetting of applicants for employment and the taking up of references. . . ."

Financial services businesses other than investment business are not covered in this regard by the Rules or by any other law. However, a number of banks, insurance companies, insurance intermediaries, and fiduciaries are licensed to do investment business and therefore covered by the Rule. The GFSC has issued draft revised Regulations and Guidance Notes for consultation which will impose similar requirements for all financial services businesses.

A personal questionnaire must be completed and submitted to the Commission with regards to any individual to be appointed as either a director or controller of an entity (which includes directors, relevant managers, compliance officers, reporting officers and company secretaries). This form asks for personal details, relationship with the institution (and with former employees and other third parties), experience, qualifications, other business interests and includes a requirement to provide details of any criminal convictions. The Form requires that any future changes to the answers provided are to be notified to the Commission.

The GFSC reviews and assesses the quality of financial services business' staff during its on-site visits.

There is nothing in the law that requires FIs to ensure that their foreign branches and subsidiaries observe appropriate AML/CFT measures consistent with the home jurisdiction requirements, to the extent that local laws and regulations permit, or that FIs should inform their home jurisdiction supervisor/regulator when a foreign branch or subsidiary is unable to observe the appropriate AML/CFT measures of the home jurisdiction. The GFSC has issued draft revised Regulations for consultation which will address this concern.

61. There is nothing in the law requiring that where the minimum AML/CFT requirements of the home and host jurisdictions differ, branches and subsidiaries in host jurisdictions should be required to apply the higher standard. The draft revised Regulations issued for consultation by the GFSC will address this concern.

Paragraph 6 of the Notes is entitled 'Group Practice' and states:

Where a group whose headquarters are in Guernsey operates branches or controls subsidiaries in another jurisdiction, it should:

Ensure that such branches or subsidiaries observe these Guidance Notes or adhere to local standards if those are at least equivalent;

Keep all such branches and subsidiaries informed as to current group policy; and ensure that each such branch or subsidiary informs itself as to its own local reporting point equivalent to the FIS in Guernsey and that it is conversant with procedures for disclosure equivalent to Appendix I [Disclosure to the FIS].

Most institutions have adopted adequate internal AML/CFT procedures. A large percentage of the institutions have training programs for new staff and refresher course at least annually. In most instances staff such as the MLRO and compliance received more intensive training. FSBs appear to take full advantage of training available at the GFSC funded training facility. In most instances the anti-money laundering compliance function was a part of institution's overall compliance function.

While most institutions screened prospective employees to determine suitability for employment most of them did not apply specific test that would reveal past criminal activity.

Most of the institutions had no policy for the application of AML/CFT standards on a global basis since in general they have no branches or subsidiaries outside of Guernsey.

Analysis of Effectiveness

The framework for internal controls and compliance is generally adequate. However there are some concerns with respect to issues related to consolidated supervision and the adequacy of screening of employees. The draft revised Regulations and Notes issued by the GFSC for consultation will address these concerns.

Recommendations and Comments

Consideration should be given to amending the appropriate laws to require FIs to appoint a person to receive suspicious reports, and to require FIs to notify the GFSC of any change in such position.

Consideration should be given to amending the relevant laws to require all FIs to put in place adequate screening procedures to ensure high standards when hiring employees along the lines of Part 5.01(3) of the Investment Licensees Rules, which applies to investment business only. The GFSC has issued draft revised Regulations for

consultation which will address this concern.

Consideration should be given to a requirement that all Guernsey FIs apply Guernsey legal and regulatory requirements in respect of AML/CFT to their branches and subsidiaries outside of Guernsey. The GFSC has issued draft revised regulations and Notes for consultation which will address this concern.

The Notes should be amended to require that where the minimum AML/CFT requirements of the home and host jurisdictions differ, branches and subsidiaries in host jurisdictions should be required to apply the higher standard. The GFSC has issued draft revised Notes for consultation which will address this concern.

Implications for compliance with the FATF Recommendations 19, 20

Compliant

VII—Integrity standards (compliance with Criteria 62 and 63 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criterion 114 for the securities sector)

Description

62. Although there is no explicit provision of law prohibiting criminals from holding or controlling a significant investment in a FI, or from holding any qualified management functions therein, including in the executive or supervisory boards, councils, etc., the relevant supervisory laws require that such individuals be fit and proper, defined in all of the supervisory laws to include any evidence that such person has "committed any offense, and in particular any offense involving fraud or other dishonesty or violence" (Schedule 3(3) to the Banking Law; Schedule 1(3) to the Fiduciary Law; Schedule 7(3) to the Insurance Business Law; Schedule 4(3) to the Insurance Managers and Intermediaries Law). Promoters and all parties connected with open-ended funds (formed under the POI Law) and closed-ended funds (formed under the Control of Borrowing Ordinance) are similarly vetted. Under Section 8(1) of the Control of Borrowing Ordinance, the GFSC has the legal authority delegated by the Committee to review all applications to form Guernsey companies, even when they are not regulated by the GFSC, and equity and debt offerings over £500,000. In addition, Regulation 8(a) of the Regulations requires financial services businesses not regulated by the GFSC to notify the GFSC with information relating to directors, partners, senior officers, beneficial owners and controllers. Finally, according to the authorities, there is also scrutiny of each company by the Attorney General's Chambers before it is allowed to be incorporated pursuant to an agreement with the United Kingdom.

According to the authorities, individuals or legal entities attempting to operate, control or acquire a significant investment in a regulated financial institution cannot do so without formal vetting by the Commission.

In conducting its review the Commission utilizes not only its own databases but also has access to information held by the Shared Intelligence System (SIS), Lexis/Nexis, the Financial Fraud Information Network (FFIN) and various websites such as those of the SEC and FBI. The Commission also utilizes, where appropriate, Guernsey Police and the databases and contacts to which the Guernsey Police have access.

As a matter of policy, a Personal Questionnaire (Form PQ) must be completed and submitted to the Commission with regard to any individual to be appointed as either a director or relevant member of senior management of an entity (which includes compliance officers, money laundering reporting officers and company secretaries where they are not members of the Board of Directors). This form asks for personal details, relationship with the institution (and with former employees and other third parties), experience, qualifications, other business interests and questions to ascertain good reputation and character. The Form requires that any changes to the answers provided are to be notified to the Commission.

The Commission uses these provisions to actively monitor the fitness and propriety of major shareholders and influencing parties on an ongoing basis. The Commission has the right to object to such a person where, in its opinion, such a person no longer meets the fit and proper criteria.

Comprehensive due diligence checks are performed on the controllers of the financial services business and the institution. In licensing or approving new financial services businesses the Commission liaises with the home supervisor and other relevant regulators and bodies. This is a means of alerting the Commission to any issues of concern. Detailed checks of databases are also carried out as described above.

The Commission holds meetings with the management of licensed entities as well as conducting on-site visits. During on-site visits the Commission assesses an entity's key staff and directors to assess their fitness and propriety.

63. Although there is no explicit provision of law to prevent unlawful use of entities identified as vulnerable to use as conduits for criminal proceeds or FT, such as shell corporations or charitable or not-for-profit organisations, uunder Section 8(1) of the Control of Borrowing Ordinance, the GFSC has the legal authority delegated by the Committee to review all applications to form Guernsey companies, even when they are not regulated by the GFSC, and equity and debt offerings over £500,000. In addition, Regulation 8(a) of the Regulations requires financial services businesses not regulated by the GFSC to notify the GFSC with information relating to directors, partners, senior officers, beneficial owners and controllers, and to notify the GFSC with any such information prior to any changes. Finally, Section 96(b) of the Companies Law provides authority for the GFSC and the Committee to petition a court to wind up a company "for the protection of the public or of the reputation of the Bailiwick of Guernsey." The Notes do not specifically address the use of entities such as shell companies. However in the context of correspondent banking relationships paragraph 139D indicates that Guernsey banks should not establish relationships with shell banks. Paragraph 85 of the Notes provides guidance for dealings with charities. The Notes provide guidance for the verification of corporations (including corporate trustees). Under paragraph 45 the Notes indicate that where an applicant for business is an institution but not a firm or company (such as an association or institute) all signatories should be treated as verification subjects. It further provides that in the case of clubs societies and charities all signatories on accounts should be treated as verification subjects.
Analysis of Effectiveness
The framework related to integrity standards is adequate.
Recommendations and Comments
Implications for compliance with FATF Recommendation 29
Compliant
VIII—Enforcement powers and sanctions (compliance with Criteria 64 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 93-96 for the banking sector and criteria 115–117 for the securities sector)
Description
With respect to explicit statutory authority to impose administrative or civil sanctions, the GFSC has the following powers relating to banks, investment business, fiduciaries, and insurance business (except as indicated): (i) issuance of a written directive or order, which does not apply to investment business and which may only be done as a last resort after the GFSC has decided to revoke or suspend (with respect to investment business) a license (although the functional equivalent of such authority is found in the placement of conditions on a license, see para. (iii) below)(Sections 12 of the Banking Law; 12 of the Fiduciary Law; 16 of the Insurance Business Law; 11 of the Insurance Managers and Intermediaries Law); (ii) issuance of a public statement, which is not available under Guernsey law; (iii) placing conditions on a license, which includes the authority "to require the institution to take certain steps . . ." (see, for example, Section 9(4)(a) of the Banking Law) and therefore is the functional equivalent of the issuance of a written directive r order (Sections 9 of the Banking Law; 9 of the Fiduciary Law; 5 of the POI Law; 12 of the Insurance Business Law; 7 of the Insurance Managers & Intermediaries Law); (iv) suspension or removal of directors and officers of any company, where the court considers that a person is unfit to be concerned in the management of a company on application by the Committee, the GFSC, the Attorney General, any corporate body of which the person in question is or has been an officer, a liquidator or creditor of the corporate body, or, with leave of the court, any other interested party. The person may be prohibited from being a director or officer of any company or any specified company, and from participating in, directly or indirectly, the management, formation or promotion of any company or any specified company (Section 67A of the Companies Law); in addition, conditions placed on a license may be used to remove a director as explicitly provided in the relevant laws (Sections 9(4)(e) of the Banking and Fiduciary Laws; 12(4)(e) of the Insurance Business Law; and 7(4)(e) of the Insurance Managers Law; (v) objections to controllers, defined as a managing director, chief executive, shareholder or shareholder group with 15 percent or more of voting power, and any person who exercises control over a director, which applies to all regulated sectors other than investment business (Sections 14 and 15 of the Banking and Fiduciary Laws; 25 and 26 of the Insurance Business Law; 36 and 37 of the Insurance Managers Law and sections 28A and 28B of the POI Law) (vi) appointment of a special auditor at the expense of the licensee, other than investment business (Sections 27

of the Banking Law; 24 of the Fiduciary Law; 69 of the Insurance Business Law and 46 of the Insurance Managers & Intermediaries Law); (vii) appointment for a defined period of a provisional or temporary administrator (typically with court approval), not applicable to any FSB; (viii) imposition of a range of civil penalties (administrative fines) on the licensee, its directors and senior managers, not applicable to any FSB; and (ix) revocation of license (Sections 8 of the Banking Law; 8 of the Fiduciary Law; 6 of the POI Law; 13 and 14 of the Insurance Business Law; and 8 and 9 of the Insurance Managers and Intermediaries Law).

Paragraph 3 of the Notes state that "the Commission is entitled to take such failure to follow the Notes or an equivalent standard into consideration in the exercise of its judgment as to whether directors and managers are fit and proper persons."

Analysis of Effectiveness

The framework for supervisory enforcement powers is generally adequate. It would be strengthened if the POI gave the GFSC the legal authority to enter a licensee's premises for the purpose of obtaining information and undertaking an assessment of its business

Recommendations and Comments

With respect to administrative sanctions, consideration should be given to amending the relevant laws to provide that all FSBs are subject to the same set of sanctions, particularly with respect to two powers available to the GFSC for all regulated sectors other than investment business: the issuance of a written directive or order and the appointment of a special auditor at the expense of the licensee. In addition, the relevant laws should be amended to provide for additional powers for the GFSC not currently in the law, in the areas of civil money penalties or administrative fines which may be imposed on companies and controllers and the ability to petition a court to appoint a provisional or temporary administrator or conservator for a defined period.

Consideration should be given to amending the POI to provide the legal authority for the Commission to enter a licensee's premises for the purpose of obtaining information and undertaking an assessment of its business. The authorities have indicated that they will promote this change to the legislation.

IX—Cooperation between supervisors and other competent authorities (compliance with Criteria 65–67 for the (i) banking sector; (ii) insurance sector; (iii) securities sector; and (iv) other financial institutions sector, plus sector-specific criteria 97–100 for the banking sector and criteria 118–120 for the securities sector)

Description

65. The Policy and International Affairs Division acts as a core resource upon which the regulatory divisions can draw and it is also responsible for the drafting of relevant AML/CFT regulations and the Guidance Notes. The Deputy Director is assisted by a consultant at the level of Assistant Director who is devoted to AML/CFT issues on a full time basis. Subsequent to the mission this officer left the GFSC. A senior analyst has joined the staff of the Division and is devoted fully to matters related to AML/CFT. GFSC has retained the services of an external consultant. The regulatory staff includes several people with specialist expertise in the financial fraud and anti-money laundering field including 2 ex-police officers (both in the Department of Fiduciary Services and the Enforcement Division) and two Certified Fraud Examiners.

The Banking Division commenced on-site assessments of licensees in 1999. The other divisions commenced reviews in 2000. Files were well documented and suggested that AML/CFT reviews were thorough. The current resources devoted to AML/CFT appear to be adequate. AML/CFT surveillance undertaken by the FSC may however have been at the expense of surveillance activity related to other areas of risk. However subsequent to the mission's visit staff resources have been increased.

The Regulations require the GFSC to train its staff on anti-money laundering issues. The GFSC has held formal in-house training for its staff, with the most recent training prior to the mission having taken place in July 2002. Follow-up training is scheduled for January 2003. The GFSC also makes use of a computer based training package which regulatory staff must undertake. This incorporates an accreditation module where key aspects are tested to ensure adequate comprehension.

66. Section 21 of the Commission Law permits the GFSC to cooperate under certain circumstances, including "to enable the Commission to carry out any of its functions" (Section 21(2)(a), one of which is "the countering of financial crime and of the financing of terrorism" (Section 2(2)(d), and "for the purposes of the investigation, prevention or detection of crime with a view to the instigation of, or otherwise for the purposes of, any criminal proceedings" (sections 21(2)(b) and 21A(b). The GFSC also relies on broad disclosure powers contained in the

various supervisory laws (Section 34B of the POI Law, Section 4 of the Banking Law, Section 44 of the Fiduciary Law, and Section 57 of the Insurance Managers and Intermediaries Law and Section 80 of the Insurance Business Law).

According to the authorities, the GFSC routinely provides the FIS, Police and Customs with intelligence and equally as routinely responds to requests for information from them where relevant. For example, the FIS liaises with the GFSC's Fiduciary Services and Enforcement Division in order to obtain information from the GFSC. In addition, the GFSC provides advice to the FIS with respect to intelligence-gathering and, more broadly, the operations and commercial activities of FSBs, including on issues raised in STRs.

67. There are laws and procedures allowing the provision of the widest possible range of international cooperation between supervisors/regulators. The GFSC relies on the provisions of the Commission Law, which provides that the GFSC may cooperate under certain circumstances, including "for the purposes of the investigation, prevention or detection of crime with a view to the instigation of, or otherwise for the purposes of, any criminal proceedings" (section 21A (b) of the Commission Law). The GFSC also relies on broad disclosure powers contained in the various supervisory laws (Section 4 of the Banking Law, Section 34B of the POI Law, Section 44 of the Fiduciary Law, Section 57 of the Insurance Managers and Intermediaries Law and Section 80 of the Insurance Business Law).

For supervisory/regulatory purposes, the GFSC has entered into Memoranda of Understanding with the following:

- Australian Securities Commission (1996);
- United States Commodity Futures Trading Commission (1994);
- De Nederlandsche Bank NV (1993);
- United States Federal Deposit Insurance Corporation (1999);
- International Association of Insurance Supervisors (1994);
- International Organization of Securities Commissions (1991 and 1996);
- Jersey Financial Services Commission (1998);
- Hong Kong Securities and Futures Commission (1992 and 1994);
- The London Stock Exchange (1998);
- Commissione Nazionale per le Società e la Borsa (an Information Exchange Agreement in1994 replaced by an MOU in 2002); and
- Isle of Man Financial Supervision Commission (2002).

The GFSC is currently negotiating memoranda of understanding with four European regulators. Two of these were finalized subsequent to the mission.

According the authorities, however, the GFSC does not require a memorandum of understanding to have been executed with foreign supervisors/regulators or law enforcement bodies before exchanging information with them. The most frequent exchange of information takes place with the United Kingdom's Financial Services Authority and the United States Securities and Exchange Commission, notwithstanding that there are no memoranda of understanding in place. Court authorization is not necessary for the exchange of information, nor is there any requirement that the exchange of information should be reciprocal or that the requesting authority should be subject to an obligation of secrecy.

In addition, the Director General and the Directors of the various Divisions of the GFSC sit on international committees which involve them in the dissemination of information on economic crime and criminals to other bodies internationally. Particular examples of this include:

- The Director General and the Deputy Director (Policy and International Affairs) sit on the Crown Dependencies Anti-Money Laundering Group which is comprised of senior regulatory, legal and enforcement personnel from Guernsey, Jersey and the Isle of Man;

• The Director of Fiduciary Services sat on FATF working group B concerned with enhancing the transparency of trusts and other corporate vehicles; • The Director of Banking has participated in the ongoing work of the joint Basel/Offshore Group of Banking Supervisors Working Group on Cross-border Banking; • The Director of Insurance has been the Chairman of the Insurance Fraud Sub-Committee of the IAIS which issued 'Anti-Money Laundering Guidance Notes for Insurance Supervisors and Insurance Entities" during his chairmanship.
Analysis of Effectiveness
The general framework in respect of international cooperation is generally adequate.
Recommendations and Comments
Implications for compliance with FATF Recommendation 26
Compliant

Description of the Controls and Monitoring of Cash and Cross-Border Transactions

Table 6. Description of the Controls and Monitoring of Cash and Cross-Border Transactions

FATF Recommendation 22:
Description
At present, money above a prescribed sum (currently £10,000) that is suspected of being the proceeds of Drug Trafficking or intended for use in drug trafficking can be seized at the borders on import and export then detained for up to two years (section 52 of the DT Law). Forfeiture can then be sought under Section 53. Under the DT Law 'money' means cash (including coins and notes in any currency) or any negotiable instrument. By way of a recent example, in August 2002, one such seizure of cash was made under the current DTL, with regard to a convicted drug trafficker. This case is still pending. To enhance this, a comprehensive Guidance document has been issued to Customs Law Enforcement staff with regard to seizure of cash in the controls. **Terrorism** Similar provisions exist under Section 19 and Schedule 3 of the Terrorism Law. These provisions relate to '***cash,'*** which is defined as coins and notes of any currency, postal orders, checks of any kind including travelers checks, bankers drafts, bearer bonds or bearer shares, or any negotiable instrument found at any place in the Bailiwick (para. 1 of schedule 3). Terrorist cash anywhere in the jurisdiction can be seized as with the DT Law, the period of detention can be extended for up to two years pending forfeiture proceedings. **Future Legislation** Amendments to current AML legislation have been approved by the States of Guernsey to extend cash seizure and detention to cash believed to be the proceeds or represent the proceeds of crime or intended for use in criminal conduct (sections 6–19 of the draft Miscellaneous Provisions Law). The new law will provide for detection and forfeiture of cash which is over the prescribed amount of £10,000. Under the draft law it will be possible to seize cash anywhere in the jurisdiction. The law is expected to be approved by the States Assembly by the end of 2003.
FATF Recommendation 23:
Description
There is no requirement to report currency transactions beyond a specified threshold. Financial institutions are required by law to report suspicious transactions. In practice, the financial sector is encouraged to report suspicious cash transactions both through training that is given to them by Law Enforcement and paragraph 15B of the Notes states that:

Interpretative Note to FATF Recommendation 22:
Description
(a) From time to time Customs & Excise in partnership with their counterparts in the UK conduct exercises to assess the risk posed by the placement of cash in the Bailiwick. One such exercise was conducted in the last year and was initiated by HM Customs & Excise in the UK. This operation, which took place in April 2001, failed to identify passengers traveling to or from the Bailiwick carrying large quantities of cash.
(b) There is a requirement under the European Communities law 1973 for the Customs Department to cooperate with other Customs Services on matters of mutual concern. In addition, the Department exchanges intelligence world wide with Customs Authorities and have disseminated intelligence accordingly, when the need has arisen on matters of cash movements, and goods of high value.

Ratings of Compliance with FATF Recommendations, Summary of Effectiveness of AML/CFT efforts, Recommended Action Plan and Authorities' Response to the Assessment

Table 7. Ratings of Compliance with FATF Recommendations Requiring Specific Action

FATF Recommendation	Based on Criteria Rating	Rating
1 – Ratification and implementation of the Vienna Convention	1	Compliant
2 – Secrecy laws consistent with the 40 Recommendations	43	Compliant
3 – Multilateral cooperation and mutual legal assistance in combating ML	34, 36, 38, 40	Compliant
4 – ML a criminal offense (Vienna Convention) based on drug ML and other serious offenses.	2	Compliant
5 – Knowing ML activity a criminal offense (Vienna Convention)	4	Compliant
7 – Legal and administrative conditions for provisional measures, such as freezing, seizing, and confiscation (Vienna Convention)	7, 7.3, 8, 9, 10, 11	Compliant
8 – FATF Recommendations 10 to 29 applied to non-bank financial institutions; (e.g., foreign exchange houses)		Largely Compliant
10 – Prohibition of anonymous accounts and implementation of customer identification policies	45, 46, 46.1	Largely Compliant
11 – Obligation to take reasonable measures to obtain information about customer identity	46.1, 47	Largely Compliant
12 – Comprehensive record keeping for five years of transactions, accounts, correspondence, and customer identification documents	52, 53, 54	Compliant
14 – Detection and analysis of unusual large or otherwise suspicious transactions	17.2, 49	Compliant
15 –If financial institutions suspect that funds stem from a criminal activity, they should be required to report promptly their suspicions to the FIU	55	Largely Compliant
16 – Legal protection for financial institutions, their directors and staff if they report their suspicions in good faith to the FIU	56	Compliant

FATF Recommendation	Based on Criteria Rating	Rating
17 – Directors, officers and employees, should not warn customers when information relating to them is reported to the FIU	57	Compliant
18 – Compliance with instructions for suspicious transactions reporting	57	Compliant
19 – Internal policies, procedures, controls, audit, and training programs	58, 58.1, 59, 60	Compliant
20 – AML rules and procedures applied to branches and subsidiaries located abroad	61	Compliant
21 – Special attention given to transactions with higher risk countries	50, 50.1	Compliant
26 – Adequate AML programs in supervised banks, financial institutions or intermediaries; authority to cooperate with judicial and law enforcement	66	Compliant
28 – Guidelines for suspicious transactions' detection	17.2, 50.1, 55.2	Compliant
29 – Preventing control of, or significant participation in financial institutions by criminals	62	Compliant
32 – International exchange of information relating to suspicious transactions, and to persons or corporations involved	22, 22.1, 34	Compliant
33 – Bilateral or multilateral agreement on information exchange when legal standards are different should not affect willingness to provide mutual assistance	34.2, 35.1	Compliant
34 – Bilateral and multilateral agreements and arrangements for widest possible range of mutual assistance	34, 34.1, 36, 37	Compliant
37 – Existence of procedures for mutual assistance in criminal matters for production of records, search of persons and premises, seizure and obtaining of evidence for ML investigations and prosecution	27, 34, 34.1, 35.2	Compliant
38 – Authority to take expeditious actions in response to foreign countries' requests to identify, freeze, seize and confiscate proceeds or other property	11, 15, 16, 34, 34.1, 35.2, 39	Compliant
40 – ML an extraditable offense	34, 40	Compliant
SR I – Take steps to ratify and implement relevant United Nations instruments	1, 34	Largely Compliant
SR II – Criminalize the FT and terrorist organizations	2.3, 3, 3.1	Compliant
SR III – Freeze and confiscate terrorist assets	7, 7.3, 8, 13	Compliant
SR IV – Report suspicious transactions linked to terrorism	55	Compliant
SR V – provide assistance to other countries' FT investigations	34, 34.1, 37, 40, 41	Compliant
SR VI – impose AML requirements on alternative remittance systems	45, 46, 46.1, 47, 49, 50, 50.1, 52, 53, 54, 55, 56, 57, 58, 58.1, 59, 60, 61, 62	Rated where applicable
SR VII – Strengthen customer identification measures for wire transfers	48, 51	Not being assessed in light of the two year compliance period provided by FATF.

Table 8. Summary of Effectiveness of AML/CFT Efforts for Each Heading

Heading	Assessment of Effectiveness
Criminal Justice Measures and International Cooperation	
I—Criminalization of ML and FT	Measures taken to criminalize money laundering and terrorist financing are generally adequate. Present arrangements will be enhanced when Guernsey implements legislation to give effect to the Palermo Convention and the Convention for the Suppression of the Financing of Terrorism is extended to Guernsey.
II—Confiscation of proceeds of crime or property used to finance terrorism	The framework in place for the confiscation of the proceeds of crime or property used to finance terrorism is generally adequate. The framework would however be improved by the adoption of legislation to provide for an asset forfeiture fund and for asset sharing with other jurisdictions.
III—The FIU and processes for receiving, analyzing, and disseminating financial information and other intelligence at the domestic and international levels	Arrangements for processing, receiving, analyzing, and disseminating financial information are generally adequate. The framework would be strengthened if the law required the reporting of suspicious transactions to the FIS, made failure to report, a crime and gave the FIS the power to require additional information from reporting parties without a production order. The general arrangements would also be strengthened if the staff complement of the FIS was increased by at least two persons.
IV—Law enforcement and prosecution authorities, powers and duties	The general framework for the powers and duties of law enforcement and prosecution authorities is considered to be adequate. *The framework would be strengthened if sufficient funding were made available for technical support requirements of the FIS. Further,* the planned legislation on investigatory powers included provision for controlled delivery would also strengthen the legal framework.
V—International cooperation	There is an adequate framework for international cooperation.
Legal and Institutional Framework for All Financial Institutions	
I—General framework	Guernsey has an adequate mechanism for the implementation of its AML/CFT framework. The GFSC has authority to ensure effective implementation of AML/CFT policies for all regulated FIs. While the GFSC has power under the Regulations to monitor compliance of businesses that engage in bureau de change activities, check cashing and money transmission services ("MSBs"),. it does not currently have the authority to regulate MSBs, except to the extent that a bank or other regulated financial institution engages in such activities.

Heading	Assessment of Effectiveness
II—Customer identification	Measures in place for the verification of the identity are generally adequate although there are some concerns. relating to instances in which the language of the Notes could be strengthened to better communicate the standard which the Commission expects of licensees, the program for introduced business and the variation in practices used by institutions in relation to the progressive program for verification of customer identity.
III—Ongoing monitoring of accounts and transactions	There are generally satisfactory arrangements in place for the monitoring of transactions. However there are concerns with respect to enhanced scrutiny for wire transfers and the reporting of unusual or complex transactions,
IV—Record keeping	The framework for record keeping is generally adequate.
V—Suspicious transactions reporting	The framework for the reporting of suspicious transactions is generally adequate except with respect to the criminalization of failure to submit a suspicious transaction report under the POC and Terrorism laws.
VI—Internal controls, compliance and audit	The framework for internal controls and compliance is generally adequate. However there are some concerns with respect to issues related to consolidated supervision and the adequacy of screening of employees.
VII—Integrity standards	The framework related to integrity standards is generally adequate. However it would be strengthened if the POI law was amended to allow the GFSC to take into account the criminal history of applicants for licenses, directors and senior officers, as part of the definition of 'fit and proper."
VIII—Enforcement powers and sanctions	The framework for supervisory enforcement powers is generally adequate. It would be strengthened if the POI gave the GFSC the legal authority to enter a licensee's premises for the purpose of obtaining information and undertaking an assessment of its business.
IX—Cooperation between supervisors and other competent authorities	The general framework in respect of international cooperation is generally adequate.

Table 9. Recommended Action Plan to Improve the Legal and Institutional Framework and to Strengthen the Implementation of AML/CFT Measures in Banking, Insurance and Securities Sectors.

Criminal Justice Measures and International Cooperation	**Recommended Action**
I—Criminalization of ML and FT	Legislation will be required to implement the Palermo Convention as follows: iv) Guernsey's current law concerning corruption is not wide enough to meet the Convention requirements. The States of Guernsey (the island's parliament) have agreed in principle to enact a comprehensive anti-corruption law to be presented to the States Assembly for approval in September 2003. v) To meet the terms of Article 3 of the Protocol on Trafficking Persons, it will be necessary to enact provisions similar to sections 30 and 31 of the English Sexual Offenses Act 1956; vi) Legislation might be required to implement the Convention Article on Extradition and the Protocol on Trafficking in Human Beings.
II—Confiscation of proceeds of crime or property used to finance terrorism	Consideration should be given to amending the Terrorism Law to provide for the appointment of a receiver for all property owned by a defendant to satisfy a confiscation order. Consideration should be given to adopting legislation that would provide for an asset forfeiture fund and for asset sharing with other jurisdictions.
III—The FIU and processes for receiving, analyzing, and disseminating financial information and other intelligence at the domestic and international levels	Legislation should be adopted along the lines of the Draft Miscellaneous Provisions Law (Sections 1 and 2) to make it a crime to fail to report a suspicious transaction, as in the DT Law, rather than as a defense to the crime of money laundering. In addition, legislation should be considered along the lines of the Draft Miscellaneous Provisions Law (Section 5) to provide that STRs should be submitted to the FIS on a form to be prescribed by law, with appropriate penalties. According to the authorities, this draft law is expected to presented to the States Assembly for approval in September 2003. Finally, consideration should be given to providing authority in law to the FIS to require additional information from reporting parties, without the need to meet the burden of proof required for a production order.

Criminal Justice Measures and International Cooperation (continued)	**Recommended Action**
	The provision in the Draft Miscellaneous Provisions Law that such regulations may include a request as part of the STR form to the submitter of an STR to provide additional information does not appear to be sufficient for this purpose. Consideration should be given to amending the relevant laws to provide explicit legal authority for the GFSC to issue guidance notes. *The Guernsey authorities should implement plans to increase the staff of the FIS by two intelligence officers as soon as is practicable.*
IV—Law enforcement and prosecution authorities, powers and duties	Consideration should be given to including controlled delivery in the proposed legislation on investigatory powers. *Funding should be made available for the development of the FIS' IT resources. This technical support is essential for its future effectiveness and success especially in light of the continuing increase in STRs.*
V—International cooperation	
Legal and Institutional Framework for Financial Institutions	
I—General framework	Consideration should be given to enacting a law to regulate MSBs.
II—Customer identification	The relevant laws should be amended to explicitly require that customer identification procedures be followed. The language of paragraphs 84 and 85A "the relevance and usefulness...should be carefully considered" as well as the language of paragraph 75 "documents that can be easily obtained...should not be accepted uncritically" should be amended to clearly communicate the standard that is expected of FSBs. The GFSC has issued draft revised Notes for consultation which address this issue. Since the Notes require the originator details to remain with the transfer throughout the payment chain, it is recommended that they be clarified and strengthened to specifically require the inclusion of the information in the first place. The GFSC has issued draft revised Notes for consultation which address this issue. The GFSC should communicate to banks that decisions taken on establishing relationships with higher risk customers should be taken by senior management. The GFSC has issued draft revised Notes for consultation which address this issue.

Legal and Institutional Framework for Financial Institutions (continued)	Recommended Action
	The exception provided in section 63 which provides that a senior staff member may give appropriate authority to open an account where identity has not been verified is vague and should be redrafted to clarify the kind of circumstances in which the GFSC expects this discretionary power to be used. The GFSC has issued draft revised Notes for consultation which address this issue. The GFSC has already undertaken considerable work to direct FSBs towards the customer identification standards required by the Position Paper. It is nevertheless recommended that these efforts be redoubled to ensure a greater degree of consistency in the approach adopted by licensees.
III—Ongoing monitoring of accounts and transactions	Within the two-year period referred to by FATF, the relevant laws should be amended to require that accurate and meaningful originator information on funds transfers remain with the transfer throughout the payment chain, and that FIs give enhance scrutiny to wire transfers that do not contain complete originator information. The GFSC has issued draft revised Notes for consultation which address this issue. The language of paragraph 25 of the Notes "may find it useful ... to delegate responsibility for maintaining vigilance policy" does not clearly indicate the standard that the Commission expects of licensees and should be amended. The GFSC has issued draft revised Notes for consultation which address this issue.
IV—Record keeping	Consideration should be given to including a reference to customer transactions in the definition of customer documents in the Regulations. The GFSC has issued draft revised Notes for consultation which address this issue. The Notes should be amended to require that records of the currency involved, and the type and identifying number of any account involved in the transaction be maintained. The GFSC has issued draft revised Notes for consultation which address this issue.
V—Suspicious transactions reporting	Legislation should be adopted along the lines of the Draft Miscellaneous Provisions Law (Sections 1 and 2) to make it a crime to fail to report a suspicious transaction under the POC Law, as in the DT Law, rather than as a defense to the crime of money laundering. The draft Miscellaneous Provisions law will be presented to the States Assembly for approval in September.

Legal and Institutional Framework for Financial Institutions (continued)	Recommended Action
	Consideration should be given to providing the FIS with the authority to give instructions to reporting entities or to require FIs to observe instructions of the FIS. The wording of Section 102 of the Notes should be amended to address suspicion that funds have been used to finance terrorism. The GFSC has issued draft revised Notes for consultation which address this issue. The use of the term "key staff" in paragraph 97 of the Notes in reference to the reporting of suspicions may suggest that only certain staff have a duty to report. The wording should be amended to make it clear that all staff have a duty to report suspicions.
VI—Internal controls, compliance and audit	Consideration should be given to amending the appropriate laws to require FIs to appoint a person to receive suspicious reports, and to require FIs to notify the GFSC of any change in such position. Consideration should be given to amending the relevant laws to require all FIs to put in place adequate screening procedures to ensure high standards when hiring employees along the lines of Part 5.01(3) of the Investment Licensees Rules, which applies to investment business only. The GFSC has issued draft revised Notes for consultation, which address this issue. Consideration should be given to a requirement that all Guernsey FIs apply Guernsey legal and regulatory requirements in respect of AML/CFT to their branches and subsidiaries outside of Guernsey. The GFSC has issued draft revised Notes for consultation that address this issue. The Notes should be amended to require that where the minimum AML/CFT requirements of the home and host jurisdictions differ, branches and subsidiaries in host jurisdictions should be required to apply the higher standard. The GFSC has issued draft revised regulations and Notes for consultation which address this issue.
VII—Integrity standards	Consideration should be given to amending the POI Law to allow the GFSC to take into account the criminal history of applicants for licenses, directors and senior officers, as part of the definition of 'fit and proper' along the lines of the Banking, Fiduciary and Insurance Laws. The authorities have indicated that such will receive royal assent the end of July 2003.

Legal and Institutional Framework for Financial Institutions (continued)	Recommended Action
VIII—Enforcement powers and sanctions	With respect to administrative sanctions, consideration should be given to amending the relevant laws to provide that all FSBs are subject to the same set of sanctions, particularly with respect to two powers available to the GFSC for all regulated sectors other than investment business: the issuance of a written directive or order and the appointment of a special auditor at the expense of the licensee. In addition, the relevant laws should be amended to provide for additional powers for the GFSC not currently in the law, in the areas of civil money penalties or administrative fines which may be imposed on companies and controllers and the ability to petition a court to appoint a provisional or temporary administrator or conservator for a defined period. Consideration should be given to amending the POI to provide the legal authority for the GFSC to enter a licensees premises for the purpose of obtaining information and undertaking an assessment of its business. The authorities have indicated that an enabling provision has recently been added to the FSC Law and they intend to proceed with an Ordinance providing for a specific power to enter licensees' premises at an early stage.
Banking Sector based on Sector-Specific Criteria	
II—Customer identification	
III—On-going monitoring of accounts and transactions	Banks should ensure that documented procedures stress the importance of staff understanding the nature of a clients' business and the likely pattern of activity.
IV—Record keeping	Banks should ensure that their procedures provide detailed guidance on the type of customer transaction information that should be retained.
Securities Sector based on Sector-Specific Criteria	
VII—Integrity standards	
VIII—Enforcement powers and sanctions	The POI should be amended to provide for the Commission to enter a licensee's premises for the purpose of obtaining information and undertaking an assessment of its business.

Authorities' Response to the Recommended Action Plan to Improve Compliance with the FATF Recommendations

Overview

31. The authorities welcome the IMF's assessment and confirmation that the Bailiwick of Guernsey has a sound legal and institutional AML/CFT framework with a high level of compliance with the Financial Action Task Force Recommendations on Money Laundering and the Special Recommendations on Terrorist Financing.

Criminalization of ML and FT

32. The Prevention of Corruption (Bailiwick of Guernsey) Law, 2003, which will introduce a statutory offence of corruption, was approved by the States Assembly in September 2003. Once it has received Royal Assent this law will supersede the existing common law on corruption and will assist the Bailiwick to adopt the UN Convention Against Transnational Organized Crime (the Palermo Convention). The authorities will maintain their programme of legislation so that the Convention can be extended to Guernsey.

Confiscation of Proceeds of Crime or Property Used to Finance Terrorism

33. Consideration will be given to amending the Terrorism and Crime (Bailiwick of Guernsey) Law, 2002 to provide for the appointment of a receiver for all property owned by a defendant and for the sale of such property to satisfy a confiscation order.

34. During 2004, consideration will be given to new legislation based on the UK Proceeds of Crime Act in respect of the introduction of a statutory asset forfeiture fund and legislation for asset sharing with other jurisdictions.

The FIU and Processes for Receiving, Analysing, and Disseminating Financial Information and Other Intelligence at the Domestic and International Levels

35. The States Assembly approved a policy letter incorporating drafting instructions for the Criminal Justice (Miscellaneous Provisions) (Bailiwick of Guernsey) Law in 2002. This law is intended to be presented to the States Assembly for approval early in 2004 and it will include provisions making it an offence if a financial services business fails to report a suspicious transaction to the Financial Intelligence Service. This will replace the existing legal provision whereby the reporting of a suspicion is a defence against committing the crime of money laundering. The new law will also include provisions which permit the Financial Intelligence Service to prescribe the format of suspicious transaction reports.

36. During 2004, consideration will be given to a requirement for information to be provided by reporting entities on an intelligence basis to the Financial Intelligence Service as part of the drafting of the Guernsey equivalent of the UK Proceeds of Crime Act.

37. The Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 provide that a court may take account of the Guidance Notes and any other guidance issued, adopted or approved by the GFSC. It is proposed to amend the Regulations to state explicitly that the GFSC must issue guidance notes under the Regulations.

38. Training of two investigators for the Financial Intelligence Service has been approved. In addition, an intelligence analyst and an administrative assistant were appointed earlier in 2003.

Law Enforcement and Prosecution Authorities, Powers and Duties

39. The Regulation of Investigatory Powers (Bailiwick of Guernsey) Law, 2003, which was approved by the States Assembly in September 2003, contains provisions that regulate the component parts of controlled delivery. This law includes the legal authority required in order to conduct directed and intrusive surveillance, property interference and the use of covert human intelligence sources.

40. The Financial Intelligence Service has given consideration to the development of its information technology resources and tenders have been issued. Work on the new computer system will commence as soon as possible.

General Framework

41. Consideration will be given to the extension of the application of the AML/CFT framework to MSBs (bureau de change activities, cheque cashing and money transmission services) as part of the current consideration of the introduction of new Regulations and Guidance Notes.

Customer Identification

42. The Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 already contain detailed customer identification requirements, which must be followed by financial services businesses. Failure to comply with the Regulations is an offence. The IMF's comment about the documentary requirements for legal entities will be considered as part of the changes to the Regulations and the Guidance Notes arising from the Financial Action Task Force's new Recommendations (issued in June 2003).

43. With regard to the other comments made by the IMF, the GFSC has issued draft revised Guidance Notes to the finance sector for consultation.

44. The GFSC routinely communicates its policies to the finance sector and is consulting with the finance sector in connection with the publication of a statement on the FATF's June 2003 Recommendation on introduced business.

Ongoing Monitoring of Accounts and Transactions

45. The GFSC has issued draft revised Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism for consultation which address the enhancement to the framework on ongoing monitoring of accounts and transactions recommended by the IMF.

Record Keeping

46. The GFSC has issued draft revised Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism for consultation which include the specific recommendations on record keeping made by the IMF.

Suspicious Transactions Reporting

47. See paragraph 35 for the response to the recommendation to introduce a new offence for failure to report a suspicious transaction.

48. Consideration will be given to providing the Financial Intelligence Service with the authority to give instructions to reporting entities and to require financial services businesses to observe instructions of the Financial Intelligence Service as part of the drafting of the Guernsey equivalent of the UK Proceeds of Crime Act.

49. The GFSC has issued draft revised Guidance Notes for consultation which address the issue of the use of the term “key staff”.

Internal Controls, Compliance and Audit

50. Amendments to the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 and the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism have been issued for consultation, which will require all financial services businesses to put in place adequate screening procedures to ensure high standards when hiring employees. They also include additional detail on the application of AML/CFT standards to the branches and subsidiaries of Guernsey financial services businesses.

51. With regard to the requirements for financial services businesses to appoint a person to receive suspicious transaction reports and to require financial services businesses to notify the GFSC of any change in such position, amendments to the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 have been issued for consultation, which require the designation of a reporting officer who should be resident in the Bailiwick of Guernsey and whose name and title must be provided to the GFSC.

Integrity Standards

52. The Protection of Investors (Bailiwick of Guernsey)(Amendment No. 2) Law, 2003 requires the GFSC to take into account the criminal history of applicants for licences, directors and officers as part of the definition of "fit and proper".

Enforcement Powers and Sanctions

53. It is intended that legislation will be promoted in 2004 to provide the GFSC with the power to issue a written directive or order in respect of persons undertaking investment business. A similar power is already contained in the other regulatory legislation administered by the GFSC.

54. It is intended an amendment to the Protection of Investors (Bailiwick of Guernsey) Law, 1987 will be promoted in 2004, which will provide for the appointment by the GFSC of inspectors to investigate investment licensees. A similar power is already contained in the other regulatory legislation administered by the GFSC.

55. The GFSC will report to the States of Guernsey Advisory and Finance Committee during 2004 in respect of civil money penalties and administrative fines.

56. An enabling provision has been included in the Financial Services Commission (Bailiwick of Guernsey) (Amendment) Law, 2003, which permits the States Assembly to introduce by Ordinance separate, explicit, legal provisions for on-site visits to be undertaken by the GFSC. An Ordinance is expected to be laid before the States Assembly for approval early in 2004.

Banking Sector based on Sector-Specific Criteria III – On-going Monitoring of Accounts and Transactions

57. The GFSC has issued draft revised Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism for consultation, which address the enhancement to the framework on ongoing monitoring of accounts and transactions recommended by the IMF.

Banking Sector based on Sector-Specific Criteria IV – Record Keeping

58. The GFSC has issued draft revised Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism for consultation, which address the specific recommendations on record keeping made by the IMF.

Securities Sector based on Sector-Specific Criteria VIII – Enforcement Powers and Sanctions

59. See paragraph 102 for the response to the recommendation to provide the GFSC with separate, explicit, statutory on-site inspection powers with regard to investment licensees.

III. INSURANCE CORE PRINCIPLES

A. General

60. This assessment of Guernsey's compliance with the IAIS Core Principles has been completed as part of the IMF Offshore Financial Sector (OFC) assesment program. Completion of a formal assessment serves several purposes. First, it benchmarks the current state of insurance supervision, recognizing that there have been extensive changes in the last years. Second, it suggests a number of strengthening measures to aid in the development of an action plan to move toward full compliance with the Core Principles.

Information and methodology used for assessment

61. The review of the IAIS Core Principles involved comparison with the Core Principles and the Core Principles Methodology, the Standards and Principles already adopted, and a review of the necessary parts of the insurance laws.

Institutional and macroprudential setting—overview

Markets

62. Guernsey is the leading European insurance captive domicile with 382 captives and protected cell companies licensed for insurance purposes. It is number one in Europe before Luxembourg, Ireland, and the Isle of Man. The insurance sector employs nearly 1,000 persons. It has a strong and comprehensive legal framework, which is implemented by a supervisory authority, the Insurance Division of the GFSC. The legal framework is one of the most modern in the world. The Insurance Business (Bailiwick of Guernsey) Law, 2002 (IB Law) and the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law 2002 (IMII Law) came into effect on November 5, 2002.

63. The GFSC distinguishes between international and domestic insurance companies. International insurance companies are captive, life insurance companies or protected cell companies. Domestic companies are local domestic insurers or overseas insurers writing Guernsey risks.

64. Captive insurance companies were originally established to provide insurance coverage to all or some of the risks of its parent (industrial or commercial companies for instance). Broad captives occasionally cover more risks from third parties than from their parent and consequently become similar to commercial insurers.

65. A protected cell company (PCC) is a new form of company vehicle designed to make the advantages of captive insurance available to smaller companies by reducing costs and to also provide benefits for investment funds. The basic idea is that the PCC's sponsor, instead of setting up separate captives for the businesses of each insured entity, sets up a single company vehicle and writes the various businesses into separate cells within the single vehicle. The assets of one cell are protected from the liabilities of another. The Protected Cell Companies' Ordinance, 1997, allows the creation and the carrying of insurance business in Guernsey by these companies. The regulation provides segregation and protection of the individual cell assets. Two classes of assets are consequently identified: noncellular (attributable to the PCC or to the "Core") and cellular (attributable to the cells).Creditors of any one cell shall have no entitlement to recourse to assets of any other cell, but, if the assets of that cell prove insufficient, they may have recourse to the PCC's noncellular (core) assets. A formal process is provided in the regulation for liquidation, and for receivership or administration of any individual cell. The PCC may create both its own (core) shares and cell shares.

66. The capital and solvency requirements of the IB Law are applicable to insurance PCCs. If the core capital and net worth is intended to support the cell business, the usual solvency ratios will apply to the whole in a consolidated manner. Where each cell will be capitalized (with a minimum in the core) each cell will have to satisfy the ratio.

67. The GFSC supervises PCCs like all other insurers on a risk basis. The board of directors and management have to fulfill the requirements (fit and proper-test, accounting procedures, financial reporting, business plan, etc.) of the IB Law and its additional regulations regarding the special "cell nature" of these companies.

68. Guernsey was the first jurisdiction to introduce by law the concept of PCCs. It has proven extremely successful. It is, for instance, used by big industrial groups for their different subsidiaries or within a company for the different profit centers or by accountancy firms for the different professional liability coverage of their different partnerships, etc.

69. At the end of 2002 there were 50 licensed PCCs with 214 cells. The experiences with this new vehicle in the last five years since its introduction were good. There have not been any known negative reactions from courts outside Guernsey as at the date of this report. The structure seems to be recognized. Other countries like Bermuda (segregated account companies), Cayman Islands (segregated portfolio companies), and some jurisdictions in the United States have also introduced this concept.

70. International insurance companies (captives and PCCs) are mainly managed by 30 management firms. The biggest among them are managing between 50 and 140 companies (Aon Insurance Managers (Guernsey) Limited, Marsh Management Services Guernsey Limited, Willis Management Guernsey Limited). The management has to fulfill the directions of the board of directors of the insurance company. Tasks that need special knowledge (investment, auditing, actuarial duties, etc.) are usually outsourced by the board of directors. The managers need to be licensed by the GFSC under the IMII Law.

71. Domestic insurers are local insurance companies or overseas insurers writing Guernsey risks.

72. Local insurers are organizations incorporated in Guernsey writing, wholly or primarily business for the resident market. These include several mutuals, which date back as far as the early 1800s.

73. Overseas insurers are companies domiciled outside Guernsey (mostly from the United Kingdom) to write domestic insurance business. Where an overseas insurer advises or arranges contracts through a branch or its agent resident in Guernsey, the insurer is deemed to have a physical presence in Guernsey and is required to be licensed by the GFSC. Prudential supervision of these companies, including solvency, is the responsibility of the home supervisor. Where an insurer does not maintain a physical presence, the GFSC must be notified, and that insurer is classed as a recognized insurer. The GFSC relies on the home supervisor for supervision of the insurer. An insurer cannot be added to the recognized list without being licensed in its home jurisdiction.

General preconditions for effective insurance supervision

74. Within the GFSC supervision of insurance is carried out by the Insurance Division which is highly specialised and allows the GFSC to accumulate a deeper and broader knowledge and experience in the insurance business.

75. The bases of the insurance supervision are primarily the IB Law, IMII Law, and several regulations, ordinances, codes, and guidelines relating to insurance business (Box 1).

B. Detailed Assessment

Table 10. Detailed Assessment of Observance of the IAIS Insurance Core Principles

Principle 1.	**Organization of an Insurance Supervisor** The insurance supervisor of a jurisdiction must be organized so that it is able to accomplish its primary task, i.e., to maintain efficient, fair, safe, and stable insurance markets for the benefit and protection of policyholders. It should, at any time, be able to carry out this task efficiently in accordance with the Insurance Core Principles. In particular, the insurance supervisor should: • be operationally independent and accountable in the exercise of its functions and powers; • have adequate powers, legal protection, and financial resources to perform its functions and exercise its powers; • adopt a clear, transparent, and consistent regulatory and supervisory process; • clearly define the responsibility for decision-making; and • hire, train, and maintain sufficient staff with high professional standards who follow the appropriate standards of confidentiality.
Description	The Insurance supervisor in Guernsey is the GFSC, which is a statutory body established under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 (as amended), (the FSC Law). The GFSC is the regulatory body responsible for all financial services (banking, insurance,

	investment business and fiduciary services). Under the FSC Law the GFSC's general functions include: • to take such steps as the GFSC considers necessary or expedient for the development and effective supervision of finance business in Guernsey; and • the countering of financial crime and the financing of terrorism. In the exercise of these functions the GFSC may take into account any matter which it considers appropriate but shall particularly have regard to: • The protection of the public interest, including the protection of the public against financial loss due to dishonesty, incompetence, or malpractice by persons carrying on finance business; and • the protection and enhancement of the reputation of Guernsey as a financial center. The supervisory process of the insurance supervisor is clear and objectively stated: (i) in relation to the supervision of insurance business, in the IB Law; (ii) in relation to insurance intermediaries, in the IMII Law; (iii) in relation to the supervision of financial services business generally, in Sections 2 and 3 of the FSC Law. These responsibilities are divided into "general functions and statutory functions." The GFSC has to be operationally independent from government and industry. Section 4 of the FSC Law provides that: "the GFSC is not a committee of the States, or a servant or agent of the States, and, except to the extent that this Law or any enactment otherwise provides: (a) is not subject to any rule of law relating to committees of the States; (b) does not have any right or privilege vested in committees of the States." ▪ The senior government committee, the States Advisory and Finance Committee, must ensure that the GFSC is managed under good governance. Whilst Section 7 of the FSC Law provides that the States Advisory and Finance Committee may, after consulting the GFSC, give to the GFSC: (a) written guidance of a general character; and (b) written directions of a general character, concerning the policies to be followed by the GFSC in relation to the development and supervision of finance business in Guernsey and the manner in which any function of the GFSC is to be carried out. The GFSC is not subject to any external controls on specific matters such as licensing or enforcement matters. The Insurance Division has confirmed that until now the Committee has not given guidance or directions on matters related to insurance. The overall activity and policy of the GFSC is overseen by the five commissioners. The GFSC is required to report annually on its activities. That report is required to be delivered to the Parliament of Guernsey (States) and is debated in a States meeting. The report is published and made available to the general public free of charge. It is also published on the GFSC's website.

	The GFSC is mainly funded by fees paid by the licensees. It also receives a small grant from the States of Guernsey for the administration of the Control of Borrowing Ordinance, 1959 as amended (COBO), along with a further grant for the development of the financial services sector in Guernsey. The development grant assists the GFSC's part funding of the Training Agency. The GFSC has budgeting processes designed to predict the level of staff and other resources required to achieve their regulatory objectives. Regulatory fees are then considered and, if necessary, adjusted by the GFSC following consultation with the Advisory and Finance Committee in Guernsey and the relevant committees in Alderney and Sark, in order to cover the costs of regulation. As to insurance supervision the GFSC has a wide range of adequate powers to perform its functions. The IB Law as well as the IMII Law provides the supervisory authority with all rights necessary for information and intervention. The IB Law and the IMII Law protect GFSC staff from any liability in respect of anything done or omitted in the discharge of any function of the GFSC under the Laws unless it is done in bad faith. As to human resources, the GFSC has the power to appoint such officers and servants as it considers necessary for carrying on its functions. Budget constraints have not been an issue in the resourcing of the Insurance Division. As of 30 August, the GFSC employed 79 staff (9 of which have been seconded to the Training Agency), of which 20 have been employed by the GFSC for more than five years. Fourteen staff work within the Insurance Division, comprising a Director, Deputy Director, an actuary, a consultant, four senior analysts, four analysts, and two support staff. Personnel within the Division possess a wide number of professional qualifications and, additionally, a wide variety of finance sector and regulatory experience. Senior staff in the Insurance Division are highly professionally qualified and members of the relevant national and international professional bodies. Guernsey has a Training Agency which was established by the GFSC and which is jointly funded by the GFSC and the States of Guernsey. The Agency provides training across the range of financial and business areas, from data protection to the prevention of money laundering, as well as sector-specific programs for banking, fiduciary, insurance and investment businesses. In 2001 there were 715 licensed students and 254 training events. Through its own participation in seminars, and through its support for the Training Agency, the GFSC plays an important part in ensuring the education of members of the financial services industry and interested members of the public. The GFSC uses a variety of media to develop and explain its policies in operational areas. These include: information circulars to the insurance industry and the media; articles of general interest in the GFSC's publication "Update"; as well as in the GFSC's annual report. These are available to the public free of charge, both in printed form from the GFSC's offices, and in the case of the annual report, via the GFSC's website. The GFSC frequently speaks to the industry to inform them of developments and challenges facing the insurance sector. The general criteria for the GFSC's approach for the granting or denial of a license are publicly available. Applicants for a license of authorization are entitled to make written or oral representations in the event of an adverse decision. The GFSC's policies and the insurance legislation under which it operates are also available on the GFSC's website or directly from the GFSC. During revision of the Insurance Laws the draft laws were made available on the GFSC's website during the consultation process. In addition, a number of workshops were held to explain the changes to the Insurance Law with industry.

	Similarly, the regulations and Codes have been made available on the GFSC's website during the consultation process. The decision-making is structured in a clear and efficient way. The Insurance Division reports directly to the Director General, in the event of a matter requiring immediate action by the Division. Where necessary, matters are referred to the commissioners for assistance. Urgent decisions needing commissioners' approval are dealt with by telephone, email or fax. In addition to the above, the Insurance Division has a comprehensive procedures manual, dealing with each departmental procedure. This facilitates the rapid and consistent operation of procedures. The procedures manual documents action to be taken in an emergency situation. Furthermore, Sections 13 and 14 of the IB Law (Sections 8 and 9 of the IMII Law) clearly show the sanctions, which may be invoked, and the steps that may be taken in an emergency situation. The GFSC's employment system is routinely considered by the Director General, Directors, the Deputy Director (Operations) and the Assistant Director (Personnel). Similarly, the employment system is considered at meetings of the senior executive with the commissioners. Their aim is to ensure the GFSC operates to the highest professional standards. A human resources officer joined the GFSC in September 2002. In 2001, third party consultants were used to undertake a major survey of the GFSC's employment system. Their survey resulted in, amongst other matters, new remuneration structures in order to remain competitive with industry. The GFSC's staff costs for 2001 were £2.183million. Salary levels at the GFSC are now competitive compared with those in the Finance Sector it regulates. Staff are encouraged to undertake training. Access to the facilities of the Training Agency is also available to the Division and staff attend many of the courses facilitated by the Agency. The FSC Law imposes duties of confidentiality on the GFSC and its staff. For details see Principle 17. Rules regarding dealings between supervisory staff and licensees (e.g., gifts, invitations, etc.) as well as rules relating to avoidance or resolution of conflicts of interests are contained in the GFSC's staff handbook. The GFSC is able, and has the necessary funding available, to use third parties, where it is recognized that the GFSC does not have sufficient capacity or sufficient knowledge of certain matters. Where specialist support is considered desirable lawyers, accountants and actuaries are the most commonly used third parties. Such assistance may be by direct provision or by the use of secondments from appropriate firms. In all circumstances, whilst the activity may be outsourced, responsibility and accountability for it, as well as oversight remains with the GFSC. Prior to the employment of its own actuary, the GFSC outsourced this work to a firm of consulting actuaries. Annually, the GFSC uses the services of an insurance auditor for a period of eight weeks to assist in the timely review of annual insurance returns. This extra assistance is recruited because the majority of financial year-ends of the licensees occur in December, resulting in most of the annual insurance returns being submitted at the end of April. Third parties are subject to the same confidentiality provisions as the staff of the GFSC and a breach of these provisions constitutes an offense. Furthermore, prior to engaging a third party, the GFSC requires a confidentiality clause to be signed, if one of equivalent standing is not included within a contract/engagement letter.
Assessment	Largely observed.
Comments	The mission acknowledges the State Advisory and Finance Committee's power to give guidance and directions has not interfered to date with the GFSC's capacity to carry out its functions, and

	that development and effective supervision can be complementary objectives. However, a supervisor is called on from time to time to make difficult decisions affecting the finance sector or its individual members. The current Law has the potential to compromise the judgment and, therefore, the independence of the supervisors. In order to strengthen the operational independence of the GFSC, the mission recommends that the FSC Law be amended to remove the power of the Advisory and Finance Committee to provide guidance and direction to the GFSC. The FSC Law should establish safety, soundness, and integrity of the financial system as the objectives of the GFSC, and eliminate "development" as one of the GFSC functions. Further, there should be no provisions in the Law that could potentially compromise the above stated objectives. This would provide a clear legal framework that would avoid potential conflicts in the functions of the GFSC. The attainment and sustainability of these objectives will enhance the reputation and contribute to the development of the financial system in Guernsey. The GFSC should be able to continue its support of the activities of the Training Agency that are consistent with the revised mandate. The staff of the Insurance Division has been increased in the past. That was absolutely necessary. The new Insurance Laws have the target to strengthen the supervision. New responsibilities are given to the GFSC. The insurance has become more volatile and the competition has hardened. The number of insurance companies has increased. On-site inspections have to be intensified. Under these circumstances, it seems necessary to increase the number of staff once more (second actuary, some more analysts). Since the dates of the mission the staff was increased by the addition of trainee actuary and two analysts.
Principle 2.	**Licensing** Companies wishing to underwrite insurance in the domestic insurance market should be licensed. Where the insurance supervisor has authority to grant a license, the insurance supervisor: • in granting a license, should assess the suitability of owners, directors, and/or senior management, and the soundness of the business plan, which could include proforma financial statements, a capital plan, and projected solvency margins; and • in permitting access to the domestic market, may choose to rely on the work carried out by an insurance supervisor in another jurisdiction if the prudential rules of the two jurisdictions are broadly equivalent.
Description	The legal mechanism for the licensing of insurance business, insurance managers, and insurance intermediaries in or from within Guernsey is provided by the IB Law and the IMII Law. The IB Law provides that all persons carrying on insurance business in or from within Guernsey must be licensed by the GFSC. In respect of those persons carrying on domestic business in or from within Guernsey or in the case of a Guernsey body carrying on insurance business outside Guernsey such activities are also required to be licensed by the GFSC. There is no difference between domestic and foreign insurers as to the licensing requirement or the application process. Only where a foreign insurer wishes to carry on insurance business in Guernsey through licensed insurance intermediaries and does not maintain a physical presence in the country (through a branch or agents), the GFSC must be notified and that insurer is deemed to be a recognized insurer. Then there is no requirement for that insurer to be licensed. The GFSC relies on the home supervisor for supervision of the insurer. If the insurer is considered unsuitable, it is excluded from the recognized insurer list and licensed insurance intermediaries are unable to place business with that insurer. The information required by an applicant when applying for a license to carry on insurance business is contained in the Insurance Business Licensing Regulations, 2002 (IBL Regulations), and Insurance Intermediaries' and Insurance Managers' Licensing Regulations, 2002 (IIIML Regulations), which came into effect in November 2002. These regulations and guidelines are

	available in hard copy and from the GFSC's website. The Laws contain a range of definitions. Insurance business is defined in Schedule 5 (Glossary of expressions) of the IB Law and is subdivided into long term business and general business. The definitions of long term and general business are contained in Sections 2(2), (3) and (4) and Schedule 1 of the IB Law. Similarly, under the IMII Law an insurance manager is defined in Section 1(3) and an Insurance intermediary is defined in Section 2(5). Licensing provisions, responsibilities, and tasks specified are conferred upon the GFSC. In practice an Assessment Committee meets on a regular basis to discuss each application to form a view as to whether or not a license should be issued. The Committee is made up of the Director of Insurance, the Deputy Director of Insurance, and staff from the relevant team who have conducted the initial review of the application. Schedule 5 (Glossary of expressions) of the IB Law (Schedule 3 in the IMII Law) defines the GFSC as the Guernsey Financial Services Commission established by the FSC Law. Schedule 7 (Minimum criteria for licensing) of the IB Law (Schedule 4 in the IMII Law) contains detailed minimum criteria for licensing. The GFSC will not grant a license unless it is satisfied that the minimum licensing criteria have been met. The licensing requirements are laid down in the IBL Regulations and the IIIML Regulations, (which are effective from November 2002). Legal forms are expressed as "persons," the definition of which is contained in Schedule 5 (Glossary of expressions) of the IB Law (Schedule 3 of the IMII Law) as including "a body of persons" (whether a company or an unincorporated body like for instance a partnership). There are three mutual companies carrying on insurance; these were founded a long time before the establishment of insurance supervision in Guernsey. Provisions governing fitness and propriety of key functionaries i.e., directors, controllers, partners, managers, and general representatives, are contained in the IB Law and the IMII Law. These minimum criteria cover the following: • integrity and skill; • economic benefit to the Bailiwick; • fit and proper persons; • business to be directed by at least two individuals; • position of the board of directors; and • business to be conducted in prudent manner. The IBL Regulations and the IIIML Regulations require that each application for a license includes the names and addresses of the applicants' current and proposed directors, officers, managers, general representative, and consultants. In addition, these regulations permit the GFSC to request details on any other person connected with the application. The IB Law and the IMII Law require personal questionnaires (PQs) for directors and controllers and the IBL Regulations and IIIML Regulations permit the GFSC to ask for details, in the form of a PQ, in respect of any other person connected with the application. The PQ is designed to assist the GFSC to form an opinion on the suitability of an individual. In essence, the individual should be honest, competent, and solvent. The fit and proper criteria were originally set out in the GFSC's annual report of 1989, further explained in 1991 and reissued in 1998. The IAIS Fit and Proper Principles were based on the Guernsey model.

	The Licensed Insurer's Corporate Governance Code (LICG Code) requires the directors to annually consider their PQs and advise the GFSC of any material changes.
	
	As regards owners, both the IBL Regulations and the IIIML Regulations provide a requirement, as part of the application process, to notify the GFSC of the names of the natural and legal persons holding a direct or indirect qualifying participation in the applicant company.
	
	The IB Law and the IMII Law require prior approval for any changes in directors, controllers, etc.
	
	Similar notification and approval procedures are required for changes in those holding a qualifying participation post licensing (see Principal 3).
	
	As to the fit and proper requirements see also Principal 4.
	
	The IBL Regulations and IIIML Regulations require an applicant to produce and submit a three year regulatory business plan.
	
	This plan has to include for insurance companies:
	
	• for the first three years after licensing financial projections as follows:
	  • forecast profit and loss account, broken down into technical account and nontechnical account;
	  • forecast balance sheet;
	  • forecast statement of solvency; and
	  • for long-term insurance business, forecast statement approved by a qualified actuary.
	• Description of the nature of the risks which the applicant intends to write;
	• Explanation of the firm's strategy for managing the risks associated with carrying on insurance business, particularly in relation to reinsurance;
	• Details of any loss history, identifying the source of the information, and past actuarial studies (where appropriate);
	• Confirmation that the financial projections are and should be consistent with the loss history and actuarial studies;
	• Details of the rationale for setting up a company in Guernsey and for not establishing the company in the parent's jurisdiction;
	• Summary of any proposed portfolio transfers, together with actuarial valuations establishing the transfer value;
	• The investment policy to be adopted and the names of the investment managers where applicable;
	• Details of exposures to be underwritten, reinsurance arrangements and dividend policy;
	• Details of any fronting arrangements;
	• Details of parties providing services in relation to policyholder protection arrangements (long term business only); and
	• For protected cell companies, where the cell is reliant on the core for solvency, a solvency projection.
	
	In the case of applicants under the IMII Law, the IIIML Regulations details the information to be included within the business plan, and includes:

	• financial projections for the first three years after licensing; • a narrative setting out the rationale for setting up the company in the Bailiwick; • in respect of insurance intermediaries, a list of the insurance companies intended to be used for the next 12 months; • details of other forms of business to be undertaken; and • details of the jurisdictions in which they intend to conduct business. In addition to the above, the Insurance Division's procedures manual sets out detailed requirements concerning the submission of business plans for both types of applicant. The GFSC has, since 1988, operated a risk based supervisory approach. However, the IB Law sets out minimum capital requirements for an insurance company which will be licensed. The minimum capital required is as follows: Insurers writing general insurance business: £100,000 Insurers writing long term insurance business: £250,000 Insurance managers and insurance intermediaries: £10,000 A person shall not be regarded as conducting his business in a prudent manner unless he maintains a capital base of an amount commensurate with the nature and scale of his operations, and of an amount and nature sufficient to safeguard the interests of his clients and policyholders. In many cases, the risks and exposures of the insurer are such that a higher capital and funding is required by the GFSC (details see Principle 8). The IB Law and IMII Law confer powers upon the GFSC to request and obtain any information and documents required for the performance of its supervisory and regulatory functions. In this context, material outsourcing contracts have been inspected by the GFSC. Checks with respect to outsourcing are conducted as part of the on-site inspection and include persons to whom functions have been outsourced. The IB Law and the IMII Law confer powers upon the GFSC to request and obtain information and documents as may reasonably be required for the purpose of determining an application. The IBL Regulations and the IIIML Regulations contain the details which are required to be completed as part of the application process. Furthermore, it is usual for the GFSC to hold pre approval meetings with the proposed management of an applicant to discuss any outstanding matters or other issues prior to the granting of a license. Where there are material contracts about which the GFSC is concerned, it is normal practice to obtain an independent legal opinion as to their validity and use. In any case the GFSC has the authority to require information about the products offered by the insurer (part of the business plan already mentioned). In the case of long-term business, the GFSC requires a certificate from the Actuary confirming that he has approved any new product having regard to the financial circumstances of the company and the reasonable expectations of potential policyholders. Among a range of other documents and information the GFSC requires: • Copies of the memorandum and articles of association of the applicant; • A copy of its certificate of incorporation; • A copy of the auditor's acceptance to act as auditor of the applicant; and • In the case of an applicant applying to carry on long-term insurance business, a copy of

	the actuary's acceptance letter. Only those auditors approved by the GFSC can carry out audits of licensed insurers. The GFSC will only approve auditors with the necessary insurance auditing expertise and knowledge of the local insurance laws. Similar requirements are valid for actuaries. Under the IB Law applicants seeking a license to carry on both life and general insurance business are prohibited from doing so. It is possible for composites to operate under the PCC legislation, where assets are legally separated both on a going-concern and a winding-up basis, and the business must be written in separate cells. However, the GFSC will allow those insurers already lawfully carrying on both life insurance and general insurance business to continue to do so. The GFSC will take account of, and determine what weight should be given to reports from third parties, including auditors and other regulators. Relevant matters include the quality of regulation in the regulators' jurisdictions, and, whether that regulator applies international standards. The GFSC is routinely in contact with other regulatory bodies. It is the GFSC's policy not to rely totally upon the reports of others but rather undertake its own assessment of an applicant. In support of the above, both the IBL Regulations and the IMIIL Regulations require the applicant to support the details relating to its ownership by including within the application pack, copies of the latest audited financial statements for itself, its ultimate holding company and its controller where different. In addition to this requirement, the GFSC may under the IB Law and IMII Law require the applicant to provide a report by a person who has the relevant professional skills. Furthermore, as stated above, in vetting fit and proper status, the GFSC utilizes not only its own data but also has access to information held by commercial databases such as Lexis Nexis, various regulatory websites such as that of the U.S. SEC and certain other nonpublic regulatory databases maintained in the UK. The LICG Code requires all conflicts of interest either of the directors or the appointed managers to be declared to the board when they arise. In addition, a declaration of any conflicts of interest or their absence is required to be made at each annual review of Corporate Governance issues by the Board. The requirement for the GFSC to provide prior approval to those persons intending to be directors, controllers, partners, managers or general representatives, and notification of authorized insurance representatives, will also act as a means of identifying any material conflicts. The GFSC may provide to the insurance supervisors in other jurisdictions and receive from such insurance supervisors information in connection with applications from foreign regulated insurers. Such information is given and received in confidence. It is standard practice for the GFSC to contact overseas authorities if the application contains reference to an overseas financial services company. Whilst the GFSC will take information from other regulators into account, it will only do so as part of its own assessment. For example, approval by an insurance supervisor in another jurisdiction will not automatically result in approval by the GFSC. However, refusal to grant a license by another regulator will almost undoubtedly result in similar refusal by the GFSC (details about cooperation and confidentiality see Principle 16 and 17). The GFSC has the power to revoke or suspend a license in a variety of circumstances including where the insurer has been involved in substantial irregularities. The same measures under the same circumstances can be taken under the IMII Law regarding insurance managers and/or insurance intermediaries.
Assessment	Observed.

Comments	
Principle 3.	**Changes in Control** The insurance supervisor should review changes in the control of companies that are licensed in the jurisdiction. The insurance supervisor should establish clear requirements to be met when a change in control occurs. These may be the same as, or similar to, the requirements which apply in granting a license. In particular, the insurance supervisor should: • require the purchaser or the licensed insurance company to provide notification of the change in control and/or seek approval of the proposed change; and • establish criteria to assess the appropriateness of the change, which could include the assessment of the suitability of the new owners as well as any new directors and senior managers, and the soundness of any new business plan.
Description	The IB Law and IMII Law place an obligation on controllers and proposed controllers to notify the GFSC of any changes in control and to seek prior approval by the GFSC for such a change. Failure to notify the GFSC is an offense under the IB Law. "Controller" is defined in Schedule 5 (Glossary of expressions) of the IB Law as: " in relation to a company, means: (a) a managing director or chief executive of that company or of any other company of which that company is a subsidiary; (b) a shareholder controller* or an indirect controller** in relation to an unincorporated body, means; (a) a partner; (b) a managing director or chief executive of that body or of any other body which that body is controlled by; or (c) a person in accordance with whose instructions any director of that body or of any other body which that body is controlled by, or any controller of that body, is accustomed to act." *A shareholder controller is defined as: (a) in relation to a company, and subject to paragraph (b), means a person who, alone or with associates, is entitled to exercise, or control the exercise of, 15 percent or more of the voting power in general meeting of that company or of any other company of which that company is a subsidiary; (b) in relation to a protected cell company, means a person who, alone with associates, beneficially owns 50 percent or more of the cell shares issued in respect of any cell of that company. **An indirect controller is defined as: (a) in relation, to a company means a person in accordance with whose directions or instructions any director of that company or of any other company of which that company is a subsidiary, or any controller of that company, is accustomed to act. The IMII Law requires a licensee to give notice to the GFSC where any person has become or ceased to be a director, controller, manager or auditor of a licensee. Where there are material changes in control a new business plan is required. Any changes in existing thresholds would be reviewed as part of the annual return that is required to be deposited with the GFSC under the IB Law and the IMII Law. Information regarding ownership is routinely checked by on- site inspection. Additional information may be requested under the IB Law and

	the IMII Law. The above mentioned Laws empower the GFSC to assess any proposed change of control and either approve or object to the proposed change. Changes in control are assessed by reviewing Personal Questionnaires, company accounts and conducting regulatory checks with other regulatory authorities. In conducting its review the GFSC utilizes not only its own data but also has access to information held by commercial databases such as Lexis Nexis, various regulatory websites such as that of the U.S. SEC and certain other nonpublic regulatory databases maintained in the UK. The GFSC will notify its acceptance or objection to a change of control in writing and in the case of its objection will specify the reasons why it has refused the change and include the particulars available for a right of appeal under the IB Law and the IMII Law.
Assessment	Observed.
Comments	
Principle 4.	**Corporate Governance** It is desirable that standards be established in the jurisdictions which deal with corporate governance. Where the insurance supervisor has responsibility for setting requirements for corporate governance, the insurance supervisor should set requirements with respect to: • the roles and responsibilities of the board of directors; • reliance on other supervisors for companies licensed in another jurisdiction; and • the distinction between the standards to be met by companies incorporated in this jurisdiction and branch operations of companies incorporated in another jurisdiction.
Description	The LICG Code, which came into effect in November 2002, sets out sound principles of practice relating to Corporate Governance for licensed insurers. A failure to comply with this Code is an offense under the IB Law. The GFSC requires the board of directors of a licensed insurer to adopt the provisions of the LICG Code at its inaugural meeting and to make an annual review of its compliance with the Code. Compliance with the LICG Code by all licensed insurers is required by 31st December 2003. In submitting its annual regulatory return, the company is required to include a declaration statement certifying that, for the period covered by the return, the licensed insurer has complied with the provisions of the LICG Code. In addition, disclosure regarding the level of adherence to the Code is required to be made in a statement contained in the licensed insurer's annual report and accounts. There is a requirement on the board of directors, under the LICG Code to define its strategic objectives, which may, as a minimum, consist of a business plan which has to be submitted to the GFSC, to ensure that it receives adequate and timely management information to enable it to monitor and evaluate fulfillment of these objectives. The LICG Code requires that the memorandum and articles of association should set out procedures for the election and de-selection of the board of directors. In addition: • the board at the end of every third year (or more frequently if circumstances demand), should invite the shareholders to give careful consideration to the construction of the board and give particular attention to the balance between directors who are also employees of the shareholder or appointed licensed insurance manager of the insurance company and those who are independent of those organizations. • all insurance companies shall appoint at least one person as a director who is neither an employee of the shareholder, or the company itself, or the appointed licensed insurance

	manager unless the GFSC has consented to waive this requirement in writing. The LICG Code provides for a balance of power and authority by virtue of the board ensuring that the management clearly understands that they are to take instructions from the board of directors collectively rather than from individual directors. The exception to this is where the board has already ratified this and requested a director to implement it or appoint a sub-committee to act on a particular issue with the authority of the board as a whole. Furthermore, where the company employs its own management rather than contracting with an independent management company, the board should impose levels of authority and reporting such that it can ensure management is sufficiently accountable to the board and is not operating upon the authority of one individual. Where it may appear to the GFSC that this criteria is not being met, the GFSC has the ability to impose conditions under the IB Law. Furthermore, the GFSC can suspend or revoke the license if necessary. The LICG Code requires the board to identify the key operational risks of the business and to develop suitable risk management systems over them which will identify, measure, monitor, and control underwriting risk, credit risk, and other risks. The need for separate risk assessment functions will depend on the scale and complexity of the business. However, in the case of a business carrying on long term insurance business a licensed insurer must under the IB Law, appoint an actuary whose duties include aspects of risk assessment. Where the GFSC considers it appropriate it may require an actuarial valuation of the technical provisions of general insurance. The LICG Code requires all licensed insurers to have an external audit and the board or committee appointed by the board shall consider meeting with the external auditors where necessary. In addition the board of directors is required to establish internal control procedures (see Principle 5). The LICG Code requires that where a licensed insurer is issuing policies to members of the public, the licensed insurer must be able to demonstrate that it has in place procedures for dealing with customer's complaints (see Principle 11). The Principles of Conduct of Finance Business require licensees to avoid conflicts of interest, or where they exist, they should ensure fair treatment of all customers. The LICG Code requires that all conflicts of interest either of the directors or the appointed managers are declared to the board when they arise and a declaration of conflicts of interests or their absence is required to be made at each annual review of corporate governance issues by the board. The LICG Code states that licensed insurers are not permitted to unreasonably withhold information from its shareholders or customers. In considering the request to disclose information on a case by case basis the board should apply the relevant Laws governing disclosure and the rights to obtain information. Where considered appropriate or necessary, the board is required at its inaugural meeting to adopt a policy that private transactions, self dealing, preferential treatment of favored internal and external entities, covering trading losses and other inordinate trade practices of a non-arms length nature, should not be conducted by the company without the prior approval of the board. Management should be advised and required to report to the board where such practices arise. The LICG Code states that if individual directors were to be subjected to influence from outside concerns these are required to be declared as conflicts of interest as noted above and considered by the board. If it is felt that these outside influences are impairing the proper functioning of a director or the board, then the composition of the board will need to be considered and changes

	recommended to the shareholders in order to address the situation. Furthermore, a licensee whose board was subject to undue influence would be viewed by the GFSC as not carrying out its business in a sound and prudent manner and would be carrying on in breach of the requirements of the IB Law. In addition, the licensee would not be viewed as continuing to be fit and proper. If a breach was committed the licensee would be subject to the GFSC's range of powers which may include the GFSC revoking the insurer's license. The GFSC has the powers to object to existing controllers and directors who are no longer fit and proper under the IB Law. Where a person continues to be a controller or director after a notice of objection has been served, that person is guilty of an offense under the IB Law. The LICG Code provides that a review of directors' fees should be a standing item at the Annual General Meeting of the licensed insurer and should be considered by the shareholder(s). The Code further provides that in the case of executive directors, the Board must be able to demonstrate that procedures are in place for the review of employment contracts and remuneration of executive directors. The IB Law and LICG Code require a licensed insurer to appoint a compliance officer. In addition, where a licensed insurer employs the services of a licensed insurance manager, the board will charge the licensed insurance manager to deal with issues of compliance relating to the relevant laws and standards of business conduct. In doing so the licensed insurance manager is required to submit regular compliance reports to the board for their review. As part of its on-site inspections the GFSC reviews a firm's compliance with its legal obligations and the GFSC's Codes and the adequacy of its internal review systems.
Assessment	Observed.
Comments	
Principle 5.	**Internal Controls** The insurance supervisor should be able to: • review the internal controls that the board of directors and management approve and apply, and request strengthening of the controls where necessary; and • require the board of directors to provide suitable prudential oversight, such as setting standards for underwriting risks and setting qualitative and quantitative standards for investment and liquidity management.
Description	The LICG Code which came into effect in November 2002, requires the board of directors to establish internal control procedures for the purposes of conducting the business, having regard to the nature and scale of its business. In establishing such procedures, the Board is required to provide the GFSC with copies of the extracts from its Inaugural Meeting identifying such internal controls as required to be adopted by the aforementioned Code. In particular this Code requires the establishment of internal controls in relation to: • prudential oversight in respect of insurance matters, including controls for underwriting risks, valuation of technical provisions, investment and liquidity management and reinsurance, including credit status of reinsurers; • the monitoring of its capital resources; • the oversight of market conduct activities; • the oversight of divisions of responsibilities; • the oversight of custody or similar arrangements to safeguard the assets of the company; • the oversight of compliance issues.

	The Code requires the board to provide internal controls in relation to the oversight of custody or other arrangements put in place to safeguard the assets of the company and to review from time to time, if thought appropriate, the internal controls of such service providers. The board should give careful consideration to the controls imposed through signing authorities and bank mandates with regard to the assets of the company. These should be clearly set out by the board, reviewed regularly and compliance with them checked at the board's direction. At the application stage details of the bank mandate are required to be submitted so the GFSC can verify where control of the assets lies. Under the Policyholder Protection requirements life companies must keep assets representing at least 90 percent of policyholder liabilities under the control of an independent Guernsey trustee (see Principle 6) who, in turn, approves and appoints custodians to hold the assets. A trustee is required to report the value of assets held to the GFSC quarterly, and must inform the GFSC if the company instructs that assets representing more than 5 percent of the market value are withdrawn in any calendar month. The LICG Code requires an oversight of Market Conduct activities where the Company concerned is dealing directly with customers of the public in accordance with the Licensed Insurer's Code of Conduct (LI Code) and other relevant regulations from time to time used by the GFSC. Insurance Intermediaries and Insurance Managers are required to carry out their business in line with the Conduct of Business Rules and the Code of Conduct for Authorized Insurance Representatives (AIR Code), which deal with Market Conduct activities. The Principles of Conduct of Finance Business identify how to treat customers fairly and have appropriate procedures in place. In addition, the LI Code and the Codes under the IMII Law all set out the minimum standards of good practice which all licensees are required to comply with in carrying out their insurance business (see Principle 11). The Code requires the board to provide internal controls in relation to the oversight of divisions of responsibilities between the board and/or members of the board and third party service providers. Furthermore, it requires the insurers to have in place internal controls to address accounting procedures, reconciliation of accounts, control lists and information for the management. Clear reporting lines are required to be fixed. Having regard to the size, nature, and scope of the business of licensees in Guernsey, it is not a requirement under the Insurance Laws to have an internal audit function. Nevertheless, some of the large licensees, subsidiaries of major insurance companies and brokers, have an internal audit function or other similar process in place for reporting to their group. The GFSC has the legal ability to obtain copies of internal audit reports where an internal audit function exists. Instead of internal audits, all licensees are subject to external audits by auditing firms approved by the GFSC where audited accounts are submitted to the GFSC annually together with the auditor's management letter where one has been supplied. External auditors are registered with the Institute of Chartered Accountants in England and Wales and all satisfy the criteria outlined above. The GFSC checks whether an internal audit function has been set up as part of its on-site inspection and will check the scope of such an audit. It has the authority under the IB Law to impose a condition on a licensed insurer to require the substitution of an external auditor, if the GFSC has the impression that the auditor does not comply with its duties. Not only life insurance companies (see Principles 7, 12) but also insurers writing nonlife insurance business may under the IB Law be required by the GFSC to produce an independent actuarial report. Classes of insurance where this would be required include mortgage indemnity guarantee, airline liability, asbestos liability, and other long-term insurance business. As with an external auditor, an actuary must be substituted if the GFSC has the impression that the actuary

	does not comply with its duties; the GFSC can then impose an appropriate condition. All licensees are subject to the anti-money laundering provisions contained in the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999, the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002, the Terrorism and Crime (Bailiwick of Guernsey) Law, 2002 and the guidance notes (the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism) issued pursuant to the Regulations and the Terrorism and Crime Law. The Regulations require compliance with a wide range of anti-money laundering and anti-terrorism legislation. Licensed insurers in Guernsey have a unicameral board structure. The LICG Code requires the Memorandum and Articles of a licensed insurer to set out procedures for the election and de-selection of the board of directors. In particular, all licensed insurers are required to appoint at least one experienced person as director who is neither an employee of the shareholder or the company itself nor the appointed licensed insurance manager unless the GFSC waives the requirement in writing. All subsequent changes are subject to approval by the GFSC under the IB Law and the IMII Law. Failure to comply with the LICG Code is an offense under the IB Law. In addition, the GFSC has the authority to impose a condition on an insurer for it to strengthen its controls where considered necessary. Contravention of any condition of a license is a criminal offense under the IB Law, and grounds for suspension or revocation of the license. Internal control checks form part of the on-site inspection.
Assessment	Observed.
Comments	
Principle 6.	**Assets** Standards should be established with respect to the assets of companies licensed to operate in the jurisdiction. Where insurance supervisors have the authority to establish the standards, these should apply at least to an amount of assets equal to the total of the technical provisions, and should address: • diversification by type; • any limits, or restrictions, on the amount that may be held in financial instruments, property, and receivables; • the basis for valuing assets which are included in the financial reports; • the safekeeping of assets; • appropriate matching of assets and liabilities; and • liquidity.
Description	Legal basis for the asset management of an insurance company are the IB Law, the Insurance Business (Approved Asset) Regulations, 2002, and the Insurance Business (Asset and Liability Valuation) Regulations, 2002. Approved assets are principally restricted to trading assets and high quality investments readily realizable in recognized markets. This approach ensures that liquidity is maintained. The LIALV Regulations impose restrictions on approved assets valuations where there is concentration of risk to a counter party, the assets are not freely realizable on recognized markets, and a trading asset has not been realized within 90 days of its due date. The GFSC further restricts the assets through the use of "recognized territory," "recognized bank" and "recognized stock exchange" restrictions. This allows the GFSC to exclude investment in sensitive areas from the approved assets lists. Furthermore the lists can be amended quickly by

	the GFSC in response to market events. In carrying on its business in a sound and prudent manner a licensed insurer must ensure that it maintains an appropriate asset liability management and an adequate level of liquidity in accordance with the requirements of the Law. In addition, the LICG Code, which came into effect in November 2002, provides that in considering the firm's investment strategy, the board should consider issues of mismatching between the assets and liabilities of the licensed insurer and adopt internal guidelines with regard to the acceptability and extent of any such mismatch. These guidelines should be reviewed periodically and reports made to the board as to compliance with these guidelines. A condition is imposed on life companies when licensed whereby such a company must not deliberately mismatch assets against liabilities unless a mismatching reserve is also set up (following the Guidance Notes of the Faculty and Institute of Actuaries in the United Kingdom).The Code requires the board to develop and implement an appropriate investment strategy that is approved and monitored by the board on at least an annual basis. In addition, the investment strategy, having regard to the size and nature of the operation, should consider undertaking regular resilience testing for a range of market scenarios and changing investment and operating conditions in order for the board to assess the appropriateness of asset allocation limits. The Code also deals with controls over the safeguard of assets in that it proposes firms establish internal controls over the oversight of custody and ensures other arrangements are put in place to safeguard the assets of the company. Under the Policyholder Protection requirements, international life companies are required to keep assets representing at least 90 percent of policyholder liabilities under the control of an independent Guernsey trustee who, in turn, approves and appoints custodians to hold the assets. A trustee is required to report the value of assets held to the GFSC quarterly and must inform the GFSC if the company instructs that assets representing more than 5 percent of the market value are withdrawn in any calendar month. A trustee can be e.g., a bank or a specialized trustee company. The LICG Code assists the licensed insurer in complying with this requirement by requiring the implementation of an appropriate investment strategy that is approved and monitored by the board at least on an annual basis, and which addresses the main elements of these criteria. Illiquid assets, whether due to their own illiquidity or that of the market generally, would not fall within approved assets and be subject to the overall restriction, as well as assets that do not have independent verification of pricing. Assets under lien (pledged assets) are unapproved and subject to the unapproved asset restriction. Trading in derivatives is prohibited under Section 11(1)(b) of the IB Law without the specific consent of the GFSC. Most licensed insurers invest in bank deposits or certificates of deposits issued by local banks. There is limited diversification into equities and other markets. The LICG Code requires the board to identify the key operational risks of the business and to develop suitable risk management systems over them which will identify, measure, monitor, and control underwriting risk, credit risk, and other risks. Furthermore, the standard requires the board to identify its key "Operational Risks" and to develop suitable controls over them. In addition, the board should give careful consideration to the controls imposed through signing authorities and bank mandates with regard to the assets of the company. These should be clearly set out by the board, reviewed regularly and compliance with them checked by the board.

	The LICG Code of Conduct provides that in developing and implementing its investment strategy appropriate stress and scenario tests should be carried out for a range of market scenarios and changing investment and operating conditions in order to assess the appropriateness of asset allocation limits**.** The Code requires the board to establish internal control procedures and checks that are, in the opinion of the directors, necessary and sufficient for the purposes of the conduct of the licensed insurer's business having regard to the nature and scale of its business. The LICG Code requires a licensed insurer to take reasonable care to maintain a clear and appropriate apportionment of significant responsibilities amongst its directors and senior executives. It requires that the apportionment should be such that it is clear who has which of those responsibilities so as to enable the affairs of the business to be adequately monitored and controlled by the directors and senior executives. Licensed insurance managers manage almost all licensed insurers. Insurance Managers are not Investment Managers and would not seek to provide investment advice to the licensed insurers. Regulated professional Investment Managers would carry out any investment of funds, apart from placing funds with regulated banks. Such arrangements would be contractual arms length arrangements. The Investment Manager would typically take over the whole investment role in accordance with the terms of the management agreement. The annual audited regulatory return and financial accounts as required by the IB Law are two of the GFSC's principal supervisory tools for regulating a licensed insurer and monitoring its asset/liability position. Where the GFSC is of the opinion that the investment activities and asset position are not appropriate to the licensed insurer's liability profile it may, amongst other things, impose restrictions under the IB Law, on the types of investments the firm may deal in and/or require it to submit its returns on a more frequent basis so as to monitor the licensed insurer's activities more closely. Actuarial reviews are conducted on life and nonlife business, where appropriate. The GFSC uses its own actuary and firms of independent actuaries to perform these reviews. Furthermore investment policies and procedures are reviewed by the GFSC during an on-site inspection.
Assessment	Observed.
Comments	
Principle 7.	**Liabilities** Insurance supervisors should establish standards with respect to the liabilities of companies licensed to operate in their jurisdiction. In developing the standards, the insurance supervisor should consider: • what is to be included as a liability of the company, for example, claims incurred but not paid, claims incurred but not reported, amounts owed to others, amounts owed that are in dispute, premiums received in advance, as well as the provision for policy liabilities or technical provisions that may be set by an actuary; • the standards for establishing policy liabilities or technical provisions; and • the amount of credit allowed to reduce liabilities for amounts recoverable under reinsurance arrangements with a given reinsurer, making provision for the ultimate collectability.
Description	The rules relating to the valuation of liabilities are detailed in Schedule 2 of the IB Law, which provides that liabilities are to be determined in accordance with Recognized Accounting Standards (see Principle 12).

	In the case of long term insurance, the IB Law provides that an annual actuarial investigation and report is made in accordance with Relevant Professional Standards of the Institute of Actuaries in London. This report accompanies the audited financial report and accounts. It has to be delivered to the GFSC. Under the IB Law, the GFSC may require an actuarial valuation of the technical provisions in general insurance if considered appropriate. It may impose a requirement on the insurer to establish and maintain technical reserves on whatever basis it determines prudent, over and above those required by Recognized Accounting Standards. The GFSC has the right to override the accounting result if it is considered inappropriate for regulatory purposes. Debts, including the reinsurer's share of the technical account, are to be considered on a gross basis unless any legally enforceable right of offset exists. Details of the reinsurance program have to be provided at the application stage; and, if there are any subsequent changes, these will be notified to the GFSC prior to the change being effected (see Principle 10). This allows the GFSC to intervene if the proposed arrangements are deemed unsuitable. Where the GFSC is of the opinion that the reinsurance conditions are unsuitable with respect to the insured risks, the premiums ceded or the suitability of the reinsurer, the GFSC may, when granting a license or at any time thereafter, impose conditions in respect of the license as it sees fit. That allows the GFSC to impose a condition to refrain the licensed insurer from adopting or pursuing a particular course of action (e.g., to renew or increase the cover with this reinsurer). The GFSC may also require any receivables, or amounts offset against reserves in respect of a particular reinsurer, be removed from the regulatory accounts using its powers in Schedule 2 of the IB Law. This is useful where the GFSC wants to restrict the use of reinsurers in a particular location or individual reinsurers who may be financially impaired. The IB Law requires a declaration of reliance on reinsurers to be completed by all licensed insurers which is available on the GFSC's website. The GFSC, in the performance of its supervisory and regulatory functions, conducts on-site inspections for the purposes of ascertaining whether or not the insurer is complying with the requirements of the IB Law, and in carrying out these visits analyses the adequacy of the technical provisions. In relation to off-site monitoring, the requirement to submit audited financial accounts, annual returns and in the case of long term insurance business, actuarial reports, act as off-site supervisory tools for monitoring and assessing the adequacy of a licensed insurer's technical provisions. Furthermore, the IB Law enables the GFSC to obtain additional information as may reasonably be required for the performance of its review.
Assessment	Observed.
Comments	
Principle 8.	**Capital Adequacy and Solvency** The requirements regarding the capital to be maintained by companies which are licensed, or seeking a license, in the jurisdiction should be clearly defined and should address the minimum levels of capital or the levels of deposits that should be maintained. Capital adequacy requirements should reflect the size, complexity, and business risks of the company in the jurisdiction.

Description	The IB Law and the supporting Regulations contain the legal provisions governing the solvency requirements (technical provisions, assets, capital adequacy). The IB Law together with the Insurance Business (Approved Assets) Regulations, 2002 and the Insurance Business (Assets and Liability Valuation) Regulations, 2002 provided the detailed requirements for a licensed insurer to secure that its liabilities under contracts of insurance entered into by it, are covered by assets of appropriate safety, yield and marketability (details see Principles 6 and 7). As to capital adequacy, Section 30 of the IB Law requires a licensed insurer to maintain a margin of solvency. The margin of solvency being the excess of the value of the assets of a licensed insurer over the value of its liabilities, those values being determined in accordance with the provisions of Schedule 2. In addition, Section 32 requires the paid up share capital of a licensed insurer to be maintained at not less than the Minimum Capital Requirement. The IB Law provides that a person shall not be regarded as conducting his business in a prudent manner unless he maintains a capital base of an amount and nature sufficient to safeguard the interests of the policyholders. In addition, the LICG Code requires a licensed insurer to monitor at all times the adequacy of its capital resources such that it is able to demonstrate that it knows at all times its capital adequacy position. The systems and controls which an insurer has in place are expected to be appropriate to enable it to be certain that it has adequate capital resources. Also, the combination of premium based and reserve based margin of solvency calculations and risk gap calculations ensures that the insurers' obligations will be met. The GFSC has the authority to monitor the mentioned three components. The business plan contains details of exposures, reinsurance, and capital and solvency. Under the IB Law, if there are any material changes during the year, the GFSC has to be notified in advance. This is the GFSC's principal prospective tool for the supervision of licensed insurers. The annual return required under the IB Law is the GFSC's principal retrospective tool for regulating licensed insurers. The information contained in the return enables the GFSC to monitor the level of technical provisions, the required minimum margin and the licensed insurer's overall solvency position. Where the GFSC wishes to monitor a licensed insurer's activities more closely, it imposes a requirement under Section 12 of the IB Law, for example, a requirement for a licensed insurer to submit its financial returns on a more frequent basis than required usually. The IB Law provides that a licensed insurer shall maintain paid up share capital of not less than the Minimum Capital Requirement. The basis for determining the Minimum Capital Requirement is contained in the Minimum Capital Requirement Regulations and is as follows: Licensed Insurers writing general insurance business: £100,000 Licensed Insurers writing long-term insurance business: £250,000 The calculation of the margin of solvency is laid out in Schedule 2 of the IB Law. For general business the margin of solvency is based on the higher of (i) the sum of 18 percent of the first £5 million net premium income and 16 percent of the value of its net premium income exceeding £5 million; or (ii) 5 percent of the value of its loss reserves. For long-term business, the margin of solvency is based on the greater of (i) £250,000 (the minimum capital requirement); or (ii) 2.5 percent of the value of the fund required to be maintained under Section 42(1) as does not comprise such a separate part of that fund referred to in Section 42(2). (The Section 42(1) fund includes assets designated to cover the technical provisions for long term business). Schedule 2 1 (2) permits the GFSC to modify the solvency requirements taking into account the "size, complexity of business, and business risks of the insurer." This risk based approach, which the GFSC has applied since 1988, enables the supervisor in most cases to require a higher amount

	of capital where the net exposures indicate that this is necessary. The principal tool for assessing this is the business plan which analyses the gross and net exposures per class of business and shows the aggregate exposure for the licensed insurer on the basis of expected losses, a worst case scenario, and a maximum exposure basis. The GFSC may, however, in reviewing the nature and classes of business involved, the spread of risk, and the historic and industry based claims data, modify the percentages used in the calculation of a general insurer's margin of solvency under Schedule 2 1(2) of the IB Law. The same procedure is possible for long term insurance by imposing a corresponding condition if necessary. The IB Law details the capital elements which are considered as appropriate for the buffer function of the solvency. The Law does not generally permit any asset under lien securing any derivative contract or other such encumbrance to be treated as an approved asset for the purposes of counting towards an insurer's margin of solvency. The exception being where the GFSC consents in writing to allow it to be regarded as such. It is very common in the captive sector for some assets of a captive reinsurer to be pledged to the insurer as security. The GFSC requires that, if there are other creditors (other than the insurer) there are sufficient unencumbered assets to discharge its liabilities. It is normal practice in the captive sector to allow letters of credit (LOC) to be established: (a) to support capital in order to allow the captive to take on extra risks, and (b) in favor of the insurer, in the case of a captive reinsurer. In the former case the LOC is secured by assets owned by the shareholder, but in the latter case the security is usually a relevant proportion of the assets of the captive reinsurer. It is relatively easy when there is only one insurer and there are no other policyholders; but, where a captive reinsures more than one insurer then care is taken that the amounts of encumbered assets are not excessive, so that the captive reinsurer can discharge its liabilities in a worst case scenario. The Law provides that an insurer must at all times maintain a margin of solvency. In submitting its annual return, the IB Law requires the insurer to include a certificate confirming that the firm has maintained a margin of solvency throughout the period covered by the annual return. A licensed insurer which cannot state compliance is guilty of an offense. The GFSC has the power to determine how any particular asset or liability is valued for regulatory purposes in any particular set of accounts. In the event that double-gearing arises, the GFSC would consider exercising its powers to eliminate the effect of this. The GFSC is very aware of double/multiple gearing techniques and licensed insurers are required to seek explicit approval for any loans to group companies. Based on the GFSC's practice, OGIS has produced guidelines on loanbacks. The GFSC always consults with overseas authorities when there is a possibility of these transactions occurring, for example, it informs the U.K. FSA of securitizations involving U.K. regulated banks utilizing a Guernsey insurance vehicle. The GFSC may in granting a license or at any time thereafter impose conditions in respect of the license as it thinks fits. For example in certain circumstances the GFSC may consider it necessary to monitor the solvency of an insurer more closely by imposing a requirement to prepare and submit its solvency calculations on a more frequent basis than that required usually. The LICG Code requires that if an insurer's margin of solvency falls below its required margin of solvency it must within seven days of the firm becoming aware of this event, advise the GFSC of this. Under the IB Law the GFSC may require the submission of a recovery plan in a form to be

	determined by the GFSC. The form and content of such a plan is not restricted in any way and the GFSC would seek a plan for the restoration of a sound financial position, which should include an explanation of how, if at all and by when it expects its margin of solvency to be adequately restored to the required margin of solvency. The plan should cover a period which is sufficient to demonstrate that the licensed insurers' margin of solvency will be adequately restored**.** The GFSC is entitled to share information and to cooperate with other supervisory authorities (details see Principles15, 16, and 17).
Assessment	Observed.
Comments	The minimum capital requirements as well as the minimum solvency margin, mentioned in the IB Law and the relevant Regulations are rather low in comparison with the minimum level for instance in the EU. However the GFSC regularly use the legal possibility to modify these solvency requirements taking into account the size, complexity of business and business risk of the insurer, for the licensing procedure as well as for ongoing supervision. In doing so, the solvency requirements are in practice usually much higher than the minimum amounts. Nevertheless, it should be considered to increase these minima from time to time following the economic environment and development worldwide.
Principle 9.	**Derivatives and 'Off-Balance Sheet' Items** The insurance supervisor should be able to set requirements with respect to the use of financial instruments that may not form a part of the financial report of a company licensed in the jurisdiction. In setting these requirements, the insurance supervisor should address: • restrictions in the use of derivatives and other off-balance sheet items; • disclosure requirements for derivatives and other off-balance sheet items; and • the establishment of adequate internal controls and monitoring of derivative positions.

Description	An insurer can only trade in derivatives if they are "Approved." Derivatives which fall within the definition of approved assets include:
	
	• Exchange Traded Derivative Contracts (ETC) or schemes resulting in an equivalent arrangement if, and only if, they are not leveraged and to the extent that they are in order to:
	
	  • apply an index tracking strategy to part or all of a portfolio;
	  • apply capital protected strategies to part or all of a portfolio;
	  • apply efficient portfolio management techniques to a portfolio.
	
	• Reduce investment risk currently employed on a portfolio.
	
	The IB Law together with the Insurance Business (Approved Assets) Regulations, 2002 detail the criteria which must be met for a derivative to be treated as an approved asset.
	
	These assets would need to be disclosed as class 4 items in the insurer's annual regulatory return.
	
	To protect against valuation and realization risk from over the counter transactions, the IB Law prohibits trading in over-the-counter derivatives; they do not come within the definition of approved assets.
	
	Any insurer who trades in derivatives in breach of the Law is guilty of an offense.
	
	The application of Recognized Accounting Standards (see Principle 12) ensures that any off-balance sheet activities are appropriately disclosed.
	
	The LICG Code requires insurers to ensure that controls over derivatives and other complex investment instruments have been implemented and are adequate to ensure that risks are properly assessed, regularly reviewed in the light of changing market conditions and experience, and consistent with the company's overall investment strategy. In addition, the LICG Code lays out provisions for directors dealing in derivatives. It provides that directors should take all reasonable

	steps to satisfy themselves that those dealing in derivatives: • fully understand the nature of derivatives trading being undertaken by the company and the related risks, and are suitably qualified and competent to transact the range and type of transactions being undertaken, and understand the nature of their exposures which their use will create; • have clearly documented the objectives and policies for the use of derivatives and monitor to ensure that their use is in line with those objectives and policies; • are capable of analyzing and monitoring the risk of all transactions undertaken by the organization individually and in aggregate; • have ensured that those responsible for the control of derivatives investment are sufficiently independent of the day-to-day operators to ensure effective control; and • are satisfied that sufficient systems and controls relevant to derivative products are in place. In addition there is a requirement under the LICG Code for directors collectively to have sufficient expertise to understand the important issues to enable them to satisfy themselves on the above points. All licensed insurers are subject to external audits by auditing firms approved by the GFSC. The auditing firms are all registered with the Institute of Chartered Accountants in England and Wales whose standards cover the criteria outlined above. Furthermore, the LICG Code requires the board of directors to carry out an annual review of the firm's overall investment strategy, including the use of derivatives. In addition, the LICG Code expects that in order for the board to satisfy itself that the investment activity is carried out in accordance with the approved strategy and that adequate controls are in the place, the board should receive frequent reports detailing the investment activities and controls in place. In addition the IB Law requires the general representative to include a certificate with the annual return confirming compliance throughout the financial period with the LI Code or any other code issued under the IB Law. The GFSC in ensuring that the licensed insurer is complying with the requirements of the LIALV Regulations, 2002, undertakes compliance reviews by requesting evidence of compliance from a licensed insurer as permitted under the IB Law and/or carrying out on-site inspections.
Assessment	Observed.
Comments	
Principle 10.	**Reinsurance** Insurance companies use reinsurance as a means of risk containment. The insurance supervisor must be able to review reinsurance arrangements, to assess the degree of reliance placed on these arrangements and to determine the appropriateness of such reliance. Insurance companies would be expected to assess the financial positions of their reinsurers in determining an appropriate level of exposure to them. The insurance supervisor should set requirements with respect to reinsurance contracts or reinsurance companies addressing: • the amount of the credit taken for reinsurance ceded. The amount of credit taken should reflect an assessment of the ultimate collectability of the reinsurance recoverable and may take into account the supervisory control over the reinsurer; and • the amount of reliance placed on the insurance supervisor of the reinsurance business of a

company which is incorporated in another jurisdiction.	
Description	The reinsurance program as part of the business plan includes all details of the reinsurance arrangements. Under the IB Law any changes in the business plan (which includes the reinsurance program) require prior notification to the GFSC. The business plan, which is submitted with every change, is designed to ensure that the level of funds available is appropriate to the risks underwritten. The IB Law requires a declaration of reliance on reinsurers, in such form, containing such particulars and accompanied by such information and documents (which shall be in such form) as the GFSC may require. Where the amount receivable from a reinsurer is more than 10 percent of the licensed insurer's shareholder funds, the following information is required to be submitted to the GFSC at the same time as the insurer's annual regulatory return: • the name and address of the reinsurance company; • whether (and if so, how) the insurer is connected with the reinsurer; • details of the reinsurer's credit rating; • the amount receivable, including the amount of any offset against reserves; • the due date of the amount receivable; • the amount of receivable in dispute; • the treatment of the amount receivable and disputed in the audited financial statements; and • the status of recovery. The GFSC subscribes to Standard & Poors and Fitch rating services which are always used to check the appropriateness of reinsurers. In practice, licensed insurers use highly rated reinsurers. Most licensed Insurance Managers utilize their U.K. based security divisions to monitor the security of reinsurers. If a proposed reinsurer was unacceptable to the GFSC, a condition would be imposed on the licensed insurer to require it to change its proposed reinsurer. In relation to the amount of ceded reinsurance the GFSC imposes no fixed limit; rather it monitors each licensed insurer's reinsurance arrangements and imposes individual limits where it considers it necessary and appropriate to do so. The GFSC considers that this method is specific and more appropriate to the Guernsey insurance sector. A primary insurer, which is also carrying out also active reinsurance, is supervised relating to its whole business (insurance as well as reinsurance). A pure reinsurer carrying on or holding itself out as carrying on business in or from Guernsey will require a license from the GFSC and in being granted a license will be subject to the same regulations and rules as those governing a direct insurer. At the present time there are no pure reinsurers licensed in Guernsey.
Assessment	Observed.
Comments	
Principle 11.	**Market Conduct** Insurance supervisors should ensure that insurers and intermediaries exercise the necessary knowledge, skills, and integrity in dealing with their customers. Insurers and intermediaries should: • at all times act honestly and in a straightforward manner; • act with due skill, care, and diligence in conducting their business activities; • conduct their business and organize their affairs with prudence;

	• pay due regard to the information needs of their customers and treat them fairly; • seek from their customers information which might reasonably be expected before giving advice or concluding a contract; • avoid conflicts of interest; • deal with their regulators in an open and cooperative way; • support a system of complaints handling, where applicable; and • organize and control their affairs effectively.
Description	The IB Law as well as the IMII Law provides that "every person who is, or is to be, a director, controller, partner, manager or general representative (or authorized insurance representative, in the case of IMII Law) of the applicant or licensee is a fit and proper person to hold that position." In the Principles of Finance Business the GFSC requires a licensee to observe high standards of integrity and fair dealing in the conduct of its business and to act with due skill, care and due diligence. In order to comply with the Principles, the key functionaries must be fit and proper. If that is not the case the GFSC is authorized to refuse to grant or to revoke a license. The IB Law and the IMII Law require a licensee in conducting its business to act in accordance with the Principles issued by the GFSC, together with any Codes issued under the Laws. The Principles require licensees to treat customers fairly and have appropriate procedures in place. In addition, the LI Code, and the Codes issued under the IMII Law set out the minimum standards of good practice which all licensed insurers, insurance managers and insurance intermediaries are required to comply with in the carrying out of their insurance business. The Codes deal with, amongst other things, advertisements, maintenance of client accounts and records, fair treatment of customers, disclosure and confidentiality of information. The various codes covering insurers, intermediaries and insurance managers (outlined in Box 1, paragraph 26), all set out these standards of good practice in detail. In particular, the Codes set out the minimum standards relating to the disclosure of relevant, timely and meaningful information to customers. In addition, the AIR Code requires information to be disclosed regarding charges, benefits, risks etc. The Principles require licensees to seek any information about their customers' circumstances and investment objectives, which might reasonably be expected to be relevant in enabling the licensee to fulfill its responsibilities to the customer. The above Codes require a licensee to include, within the proposal form, a statement drawing the attention of the proposer to the consequences of the failure to disclose all material facts that an insurer would regard as likely to influence the acceptance and assessment of the proposal. Furthermore, in relation to the issue of renewal notices, a licensed insurer is required to ensure that all renewal notices contain a warning concerning the duty to disclose any changes in information which are relevant to the renewal of a policy (e.g., increase of risks). The Principles require all licensees to deal with conflicts of interests and to protect the interests of their customers at all times. This requirement is supported by the LI Code, the LICG Code, and the AIR Code which do not allow the disclosure of any information acquired from clients except in the normal course of negotiating, maintaining or renewing a contract of insurance or in handling claims unless the written consent of the client has been obtained beforehand or disclosure of the information is required in the public interest or is compelled by law. The LICG Code requires that where a licensed insurer is issuing policies to customers, the licensed insurer must be able to demonstrate that it has in place procedures for dealing with customer complaints. In such circumstances, the complaints procedure should as a minimum set out the following:

	• In the event of complaint, this should be first reported to the appointed managers (or management if self managed). • If a satisfactory response is not issued within 30 days of complaint, the complaint should then be directed to a member of the board. • If a satisfactory response is not issued within 30 days of complaint to the board, the company should inform the complainant of his rights and the procedures to pursue the complaint further. • If a satisfactory response is not issued within 90 days of the receipt of the complaint, the directors should notify the GFSC of the complaint. The licensed insurer must ensure that the appropriate information is supplied to the customer detailing the procedure to be adopted and the parties to be contacted in the case of a complaint. There are similar requirements for Insurance Managers and Insurance Intermediaries included in the Conduct of Business Rules. An insurer or an intermediary who fails to comply with a Code issued under the Laws is guilty of an offense. The GFSC conducts on-site inspections for the purposes of assessing whether the licensee or any associated party (or any person acting for or on behalf of the licensee or associated party) is complying with the provisions concerning market conduct in the IB Law and/or IMII Law or any Ordinance, Regulation, rule or code, condition, or direction under these Laws. The GFSC has a range of procedures available to stop persons or entities failing to comply with the mentioned Laws, Codes, and Principles. Insurance intermediaries (and insurance managers) are directly regulated by the GFSC under the provisions contained in the IMII Law. Details of the regulatory structure relating to the areas required by these criteria are covered by the responses to the relevant sections of this report. The GFSC does not act as Ombudsman or Arbitrator where complaints arise but follows up the complaint with the licensee and ensures that it is dealt with at a senior level. The GFSC reviews the complaint and response provided for any matters of a regulatory concern. The process of dealing with complaints is outlined in the Insurance Division's procedures manual. The position of a financial services ombudsman is in the process of being created. The Advisory and Finance Committee issued a consultation paper in February 2002—–the GFSC is closely involved with the establishment of the Ombudsman.
Assessment	Observed.
Comments	
Principle 12.	**Financial Reporting** It is important that insurance supervisors get the information they need to properly form an opinion on the financial strength of the operations of each insurance company in their jurisdiction. The information needed to carry out this review and analysis is obtained from the financial and statistical reports that are filed on a regular basis, supported by information obtained through special information requests, on-site inspections, and communication with actuaries and external auditors. A process should be established for: • setting the scope and frequency of reports requested and received from all companies licensed in the jurisdiction, including financial reports, statistical reports, actuarial reports, and other information;

	• setting the accounting requirements for the preparation of financial reports in the jurisdiction; • ensuring that external audits of insurance companies operating in the jurisdiction are acceptable; and • setting the standards for the establishment of technical provisions or policy and other liabilities to be included in the financial reports in the jurisdiction. In so doing, a distinction may be made: • between the standards that apply to reports and calculations prepared for disclosure to policyholders and investors, and those prepared for the insurance supervisor; and • between the financial reports and calculations prepared for companies incorporated in the jurisdiction, and branch operations of companies incorporated in another jurisdiction.
Description	The IB Law requires an insurer in respect of each of its financial years to prepare an annual return and financial accounts and to submit these along with the related auditor's report and actuarial report (if applicable) to the GFSC within four months of the financial period to which the accounts relate. Similar information is required from licensed insurance managers and licensed insurance intermediaries by the IMII Law within six months of the financial period to which the accounts relate. Such information may be either on a solo or consolidated basis as determined by the GFSC. The accounts are required to be drawn up in accordance with Recognized Accounting Standards (U.K. GAAP or other internationally accepted Standards) The GFSC has authority to specify which accounting standards will be Recognized Accounting Standards for the purposes of complying with this section. The format, contents and the principles for completing a licensed insurer's return are detailed in the Licensed Insurer's Asset and Liability Valuation Regulations, 2002 (LIALV Regulations) and the Licensed Insurer's Approved Asset Regulations, 2002 (LIAA Regulations). Furthermore, under the IB Law and the IMII Law the GFSC is able to exercise its authority to vary the scope and frequency of reports as it sees fit. Life insurers and certain other insurers have to submit management accounts on a quarterly basis. Two directors must sign the audited accounts of the licensed insurer. Similar requirements exist under the IMII Law for insurance intermediaries and insurance managers, although the lodgment period is six months from the financial period to which the accounts relate. It is the responsibility of the general representative to make any return, deposit any accounts, reports and other documents to the GFSC. In submitting the licensed insurer's annual return, the general representative is required to include a signed declaration certifying that the licensed insurer: • has complied with its margin of solvency and approved assets requirements; • has complied with the LI Code, the LICG Code, and any other codes or rules issued under the IB Law; • has complied with the general restrictions and requirements for licensed insurers set out in Section 11 of the IB Law; • has complied with all conditions and directions imposed by the GFSC; • has prepared and deposited accounts in accordance with the IB Law; and

	• has in the case of long term business, deposited the actuarial report with the GFSC in accordance with the IB Law. The application of Recognized Accounting Standards will ensure that any off-balance sheet activities are appropriately disclosed. The submitted documents are one of the GFSC's principal retrospective tools for regulating and monitoring the financial condition of a licensee. For a licensed insurer the GFSC will also review and consider the 12 months, or in the case of those carrying on long-term business, three years, financial projections that all licensed insurers are required to submit with their annual regulatory return. All financial information is kept on the GFSC's computer system where certain ratio calculations provide further checks. The annual regulatory returns and financial statements are also supported by information obtained through special information requests, on-site inspections and communication with insurance managers, external auditors and actuaries or other skilled persons. Under the IB Law, a licensed insurer is required to notify the GFSC prior to any material changes to the business plan (material changes include but are not limited to: excessive losses; diminution of asset values; and changes to the nature and size of premium income). In this way the GFSC is able to monitor the condition and performance of the licensed insurers prospectively as well as on a retrospective basis. Furthermore, the GFSC may request any additional information and documents necessary to assist it in its review. A licensee who fails to comply with the above requirements is guilty of an offense under the IB Law and the IMII Law. Both Laws further provide that where a document appears to be inaccurate or deficient in any respect, the GFSC has the authority to request the correction and making good of any such deficiency. The IB Law and the IMII Law requires a licensee to appoint an external auditor who is required to audit, and include a report on the financial accounts periodically. Where special conditions have been attached to a licensee, or if the GFSC has concerns over all or part of a licensee's business, the GFSC may impose a requirement for more frequent audits. In the case of a licensed insurer carrying on long term insurance business, the IB Law requires the appointment of an actuary to the licensed insurer, who is required to carry out an annual investigation and report into the financial condition of the licensed insurer. This report is required to be submitted at the same time as the returns required to be deposited under the IB Law. The existing on-site program is structured so that licensees are visited regularly. In addition, the IB Law and the IMII Law permit the GFSC to carry out or appoint a person with relevant skills to carry out on-site inspections as considered necessary in the performance of its supervisory and regulatory functions. A person who fails to cooperate or obstructs the performance of an on-site inspection is guilty of an offense. The GFSC has procedures in place covering on-site inspections and these are detailed in Principle 13 below. Under the IB Law the GFSC has the power to appoint one or more persons (referred to as inspectors) to investigate and report to the GFSC on any particular aspect of a licensee's business as instructed by the GFSC. The costs, fees and expenses associated with any such inspection are required to be met by the licensee.
Assessment	Observed.

Comments	
Principle 13.	**On-Site Inspection** The insurance supervisor should be able to: • carry out on-site inspections to review the business and affairs of the company, including the inspection of books, records, accounts, and other documents. This may be limited to the operation of the company in the jurisdiction or, subject to the agreement of the respective supervisors, include other jurisdictions in which the company operates; and • request and receive any information from companies licensed in its jurisdiction, whether this information be specific to a company or be requested of all companies.
Description	The GFSC has the power to conduct on-site inspections at such times and intervals as it thinks fit, and where it considers it desirable to do so for the protection of the interests of the public or policyholders or the reputation of Guernsey as a financial center. Routine on-site inspections are conducted for the purposes of assessing whether the licensee or any associated party (or any person acting for or on behalf of the licensee or associated party) is complying with the provisions of the IB Law, IMII Law, or any Ordinance, Regulation, Rule or Code, Condition or Direction made under the Laws. In practice, the GFSC carries out visits on a 3 year rolling program for all licensees, with the exception of insurance intermediary sole traders, who are subject to annual inspections. Sole traders are single persons, who were allowed to intermediate insurance contracts as brokers until 1998; now only partnerships or companies are licensed as brokers. Ad hoc inspections where matters of concern are raised are conducted as and when necessary. Where a joint inspection with another department is undertaken, these are coordinated so as to minimize duplication of effort by the GFSC and the institution. The on-site team will usually be made up of a senior analyst (or in the case of a life insurer, an actuary), and an analyst plus additional technical support as considered necessary. In carrying out their inspection, the team will be required to complete a number of standard forms which provide structure to the inspection. The number of forms to be completed will be dependant on the nature of the licensee's business and include the following areas: • money laundering; • captive insurance company and protected cell company; • life insurance company; • domestic insurance company; and • insurance intermediary. Whilst there is no obligation on the GFSC to give advance notice of a compliance visit, for routine inspections it is normal practice to give one-month's advance notice and to require the provision of standard information prior to the commencement of the inspection, which the on-site team will use in preparing for its inspection. Following the receipt and assessment of this information, as well as other information in the possession of the GFSC, a pre inspection meeting is held internally with the on-site team, Assessment Committee and representatives from other divisions, where appropriate, to discuss the key areas to be covered in the inspection and any initial concerns the GFSC has about the quality of the information provided. The Assessment Committee will depend upon the licensee to be visited and the members of staff available. Generally, the members will be made up of the Director, Deputy Director, and the staff who work in the relevant areas on a daily basis. At the commencement of the inspection, the agenda is explained to the licensee and the on-site team answers any queries. This process promotes openness and ensures that the GFSC's approach

	is fully transparent. It also reduces the risk of misunderstanding and its consequent reduction in the effectiveness of the review. Detailed records are kept of all material during an on-site inspection. Summary Recommendations are drafted and any major concerns arising from the inspection would be discussed with the Assessment Committee. The final Summary Recommendations are then issued to the licensee. The licensee will be expected to provide a progress report one month after the date of issuing the Summary Recommendations. A reminder will be issued by the GFSC requesting such an update. Otherwise, the licensee may be given a specific time to address the Summary Recommendations, with a revisit being scheduled at the end of the time given. The Deputy Director may attend a re-inspection with the on-site team to review how the licensee has addressed the issues raised. Following the re-inspection, the on-site team will refer to the Assessment Committee in order to form a conclusion as to whether to report the issue to the commissioners. It may be decided that an undertaking from the licensee to appoint an independent third party to help the licensee address the issues is required. In some cases, the GFSC may appoint an independent third party to inspect the licensee, at the expense of the licensee, to assess how the issues raised by the GFSC have been addressed. In the normal practice, where an inspection identifies deficiencies, to require the licensee to take remedial action within a specified time and to report to the GFSC that is has done so. Where serious failings are apparent, the GFSC may take action to attach a condition to the license (for instance prohibition of new business) until the situation has been rectified. The GFSC may extend its on-site inspections to include those parties associated with the applicant or acting for, or on behalf of, the licensee or associated party. Where associated parties are located in a different jurisdiction to the licensee, the GFSC will liaise with the insurance supervisor in that jurisdiction so that any inspection is either carried out by that supervisory authority or on a joint basis. Insurance Intermediaries licensed by the GFSC are subject to routine on-site inspections. The treatment of customers by the licensee, the nature of any disputes/litigation between a customer and the licensee, and observance of consumer regulations, are all part of the normal on-site review procedures. Prior to all on-site inspections, standard information is requested which includes details of any complaints and litigation against the licensee. This information is reviewed prior to the inspection and is discussed with the licensee during the inspection where the complaints register is also examined. Compliance with the relevant laws and regulations is reviewed during an on-site inspection. Policyholder files are reviewed to ensure fair treatment of customers during on-site inspection to Insurance Intermediaries, domestic insurers and other insurers dealing directly with the general public. The GFSC schedules its planned inspections on an annual basis for implementation the following year, although this program of inspections is reviewed where matters of concern arise with a licensee. The first inspection is used to gain an overview of the licensee's business and procedures; subsequent inspections will tend to be more specific to include a review of any regulatory issues raised during the previous inspection, changes to regulatory environment and licensee changes.

	All of the above activities are evaluated as part of the on-site inspection. In 2001 a total of 18 inspections were undertaken. The inspections also included 1 follow up inspection to confirm remedial action had been undertaken and 2 special reviews in response to specific issues which had come to the GFSC's attention.
Assessment	Observed.
Comments	
Principle 14.	**Sanctions** Insurance supervisors must have the power to take remedial action where problems involving licensed companies are identified. The insurance supervisor must have a range of actions available in order to apply appropriate sanctions to problems encountered. The legislation should set out the powers available to the insurance supervisor and may include: • the power to restrict the business activities of a company, for example, by withholding approval for new activities or acquisitions; • the power to direct a company to stop practices that are unsafe or unsound, or to take action to remedy an unsafe or unsound business practice; and • the option to invoke other sanctions on a company or its business operation in the jurisdiction, for example, by revoking the license of a company or imposing remedial measures where a company violates the insurance laws of the jurisdiction.
Description	Where the GFSC considers that the ownership and the organizational structure of the applicant may hinder the effective supervision of the licensee, the GFSC has power to refuse a license. Therefore the Insurance Business (Licensing) Regulations, 2002 (IBL Regulations) and the Insurance Managers and Insurance Intermediaries (Licensing) Regulations, 2002 (IMIIL Regulations) require the applicant to submit a copy of its group organization chart detailing the holdings between itself and its ultimate holding company (and controller, where different), together with a brief summary outlining the background of these related parties. The GFSC will consider such information and any other documents that it may require for the purpose of determining the application. Furthermore the GFSC may revoke a licensee's license where the GFSC has been provided with false, misleading, deceptive, or inaccurate information. The IB Law and IMII Law authorizes the GFSC to refuse to grant or revoke a license where it considers that the key functionaries of an applicant are not fit and proper for their roles. Should members of the board or officers or other key functionaries of the company prove not to be fit and proper or to have the required technical knowledge, the GFSC may impose a requirement to remove any director, controller, manager, partner, employee, general representative, auditor, or actuary of the licensed insurer for the purpose of protecting the interests of the policyholders and the public. The GFSC possesses a range of powers to take remedial actions in the interests of the policyholders. The IB Law as well as the IMII Law enables the GFSC, for instance, to suspend or to revoke a license, to prohibit or impose limitations upon the carrying on of insurance business, to object to someone becoming a controller of a licensee, to appoint inspectors at the expense of the licensee, for the purpose of investigating and reporting to the GFSC on the nature, conduct or state of the licensee's business or its ownership and control, to petition the court for the winding up of a company for the protection of the public or to safeguard the reputation of Guernsey, require the licensee to deposit within a short period of time a recovery plan in a form determined by the GFSC including an explanation of how the situation of the company will be improved, etc. Restrictions to the free disposal of assets or the suspensions of payments can be reached by conditions imposed by the GFSC. A temporary administrator, substituting the management, can be appointed only by the court on application by the GFSC. The same procedure is necessary in the case of the transfer of a portfolio.

	The GFSC does not follow a "ladder of compliance" as the nature of noncompliance and the appropriate remedies varies too much from case to case to allow a formula-driven response to be effective. Instead the GFSC relies upon having detailed information about its licensees, proactive supervision, and a significant range of possible remedial action to enable it to take effective, timely, and appropriate action. For serious offenses, fines and prison sentences, as well as compulsory winding up are available, the GFSC has to require the intervention of the Royal Court. The GFSC does not have the power to issue itself civil money penalties (sometimes called administrative fines).
Assessment	Observed.
Comments	It is recommended to complete the range of sanctions by the power of the GFSC to impose civil money penalties (administrative fines) following the international standards of financial services supervision. It is desirable that all supervisors have consistent enforcement powers.
Principle 15.	**Cross-Border Business Operations** Insurance companies are becoming increasingly international in scope, establishing branches and subsidiaries outside their home jurisdiction, and sometimes conducting cross-border business on a services basis only. The insurance supervisor should ensure that: • no foreign insurance establishment escapes supervision; • all insurance establishments of international insurance groups and international insurers are subject to effective supervision; • the creation of a cross-border insurance establishment is subject to consultation between host and home supervisors; and • foreign insurers providing insurance cover on a cross-border services basis are subject to effective supervision.
Description	Under the IB Law everybody carrying on insurance business in or from Guernsey must be licensed and supervised by the GFSC. There is one exception: Where a foreign insurer wishes to carry on insurance business in Guernsey through licensed insurance intermediaries and does not maintain a physical presence in the Bailiwick (through a branch or agents), the GFSC must be notified and that insurer is deemed to be a recognized insurer; in this case there is no requirement for that insurer to be licensed. The GFSC relies on the home supervisor for supervision of the insurer. If the insurer is considered unsuitable, it is excluded from the recognized insurer list and licensed insurance intermediaries are unable to place business with that insurer. In other words it is permitted for a broker licensed in Guernsey to place Guernsey risks with an overseas insurer, provided that insurer is on the GFSC's recognized insurer list. That insurer cannot however write business in Guernsey without being licensed in its home jurisdiction. In all other cases, where a license in Guernsey is necessary, the GFSC will take into account any information supplied to it by the relevant overseas authority in which it currently carries on business. Information between supervisors is exchanged on a confidential regulator to regulator basis as discussed at Principles 16 and 17. However, the powers of the GFSC to grant or refuse an application for a license to carry on insurance business from a foreign insurer and the application procedure, are the same as those for Guernsey based companies. In granting a license to an overseas insurer wishing to carry on similar business in Guernsey, the GFSC will have regard to the description of insurance business and the jurisdiction in which it is currently regulated, along with any information supplied to the GFSC by the relevant overseas authority. The powers of the GFSC all apply to insurance subsidiaries or branches of foreign institutions. The GFSC can refuse to grant a license to a foreign insurer wishing to carry on insurance business in or from within Guernsey under the same circumstances given in the case of a

	domestic insurer. It is also possible under Section 12 of the IB Law for the GFSC to impose conditions on a licensed insurer where appropriate. The GFSC is able to suspend or revoke a license or issue directions to a licensee under the IB Law. If there were concerns regarding an existing licensee, the Assessment Committee would meet to decide on the most appropriate action. The Committee is made up of the Director of Insurance, the Deputy Director of Insurance, and the relevant team involved in the day-to-day supervision of the licensee. A Guernsey insurer should not carry on insurance business of any description in or from within a country outside Guernsey unless: • it is licensed by the GFSC as an insurer in respect of that description of insurance business; and • that business is carried on outside Guernsey with the written consent of the GFSC and in accordance with any conditions subject to which that consent has been granted. The GFSC will not provide its consent unless it considers the licensee has the necessary skills and capability to undertake the business in the other jurisdiction and it has the appropriate authorization in that other jurisdiction. The LICG Code requires the board of an insurer with its head office in Guernsey and which carries on business overseas to ensure that its systems and controls are adequate to ensure the maintenance of a sound and verifiable system of reporting to its head office. As for the exchange of information, the GFSC currently has formal arrangements in place regarding cross-border information sharing under a Memorandum of Understanding with the following supervisors: • Australian Securities Commission (1996); • United States Commodity Futures Trading Commission (1994); • De Nederlandsche Bank NV (1993); • United States Federal Deposit Insurance Corporation (1999); • International Association of Insurance Supervisors (1994); • International Organization of Securities Commissions (1991 and 1996); • London Stock Exchange (1998); • Jersey Financial Services Commission (1998); • Hong Kong Securities and Futures Commission (1992 and 1994); • Commissione Nazionale per le Società e la Borsa (an Information Exchange Agreement in 1994 replaced by a MOU in 2002); and • Isle of Man Financial Supervision Commission (2002); MOUs with the U.K. Financial Services Authority and the French Commission des Operations de Bourse were signed subsequent to the mission. Each of the above MOUs apply to different regulatory activities undertaken by the GFSC. Currently, the GFSC is in the process of arranging two further Memoranda of Understanding. The Director of Insurance holds regular meetings with his counterpart from the Isle of Man to discuss specific supervisory matters. He meets the South African FSB regularly, and the insurance division regularly meets with the U.K. FSA to discuss specific supervisory matters. The

	GFSC has always been the proactive party in setting up these arrangements. Even when there are no cross-border arrangements in place, exchange of information between the GFSC and relevant other supervisory authorities for the purposes of enabling or assisting them to discharge/exercise their functions are provided under the IB Law. The GFSC has the power to and will cooperate with the home state supervisor should they wish to undertake on-site inspections within Guernsey. To date, only the regulators from the Netherlands have undertaken an on-site inspection in the insurance area. On the other hand, the GFSC has undertaken on-site inspections in several other countries.
Assessment	Observed.
Comments	
Principle 16.	**Coordination and Cooperation** Increasingly, insurance supervisors liaise with each other to ensure that each is aware of the other's concerns with respect to an insurance company that operates in more than one jurisdiction, either directly or through a separate corporate entity. In order to share relevant information with other insurance supervisors, adequate and effective communication should be developed and maintained. In developing or implementing a regulatory framework, consideration should be given to whether the insurance supervisor: • is able to enter into an agreement or understanding with any other supervisor both in other jurisdictions and in other sectors of the industry (i.e., insurance, banking, or securities) to share information or otherwise work together; • is permitted to share information, or otherwise work together, with an insurance supervisor in another jurisdiction. This may be limited to insurance supervisors who have agreed, and are legally able, to treat the information as confidential; • should be informed of findings of investigations where power to investigate fraud, money laundering, and other such activities rests with a body other than the insurance supervisor; and • is permitted to set out the types of information and the basis on which information obtained by the insurance supervisor may be shared.
Description	The GFSC has a full range of statutory gateways to enable it to share information both domestically and internationally. Indeed, the GFSC has a long experience of cooperation with regulators in other jurisdictions in matters of investigation and enforcement; for example, it has memoranda of understanding with numerous foreign supervisory authorities of different financial sectors (see Principle 15). In the GFSC itself, information sharing and other cooperation across the regulated sectors is set up efficiently. The regulatory divisions responsible respectively for banking supervision, insurance supervision, investment supervision, and the regulation of fiduciary services, company administrators and company directors have identified where institutions conduct activities in more than one sector, which of them is the primary regulator. The directors of each division meet on a weekly basis and, at this meeting, discuss issues relating to licensees of more than one division. Furthermore the GFSC's data system, containing details of licensees including directors and controllers is centralized and therefore accessible to all the divisions. Correspondence relating to licensees is also circulated to officers in all the divisions. These processes, combined with the GFSC's overall understanding of its licensees, enable consistent and comprehensive regulatory standards. Domestic gateways exist to enable the GFSC to provide and receive information, inter alia, to/from the domestic law enforcement agencies in connection with the investigation of suspected

	offenses or the institution of criminal proceedings, or with the Attorney General, and any police officer where it suspects a money laundering offense. The GFSC is permitted by Law to exchange information with other regulators regardless of whether they are in the course of a civil or criminal investigation or are simply at an enquiry stage (see Principle 17). As a result of these "gateways" the GFSC has wide powers to disclose confidential information where they consider it appropriate to do so. Information-sharing arrangements do not require the execution of a specific Memorandum of Understanding with a foreign regulator, but such Memoranda mentioned above are an increasingly common feature of the GFSC's arrangements. They are designed to promote the efficiency of information exchanges by detailing the content, nature, and frequency of such exchanges as well as providing a formal agreement concerning the confidentiality of information provided. There are no legislative requirements relating to reciprocity of confidential information; the GFSC is able and willing to cooperate with overseas regulators without a Memorandum of Understanding in place. The GFSC is able to communicate to relevant supervisory authorities information that is in its possession, whether or not as a result of the exercise of any of its powers, at the request of another authority. The GFSC recognizes that information exchange is a two way process and will always consult with an overseas regulator where problems of any kind exist with a regulated person licensed in both jurisdictions. Where information comes into the possession of the GFSC, which may indicate that an offense is or potentially could be committed in another jurisdiction, that information is sent to the GFSC division responsible for intelligence. The individual responsible in that division will consider, as an automatic part of the assessment process, whether the information should be forwarded to the Law Officers if the issue is a domestic one, or to a relevant overseas agency if the issue has international implications. Although information sharing with other agencies is coordinated by the intelligence gathering function, there is close cooperation between regulatory divisions and overseas regulators to ensure that information is shared with or transferred to the most appropriate regulatory agency outside.
Assessment	Observed.
Comments	
Principle 17.	**Confidentiality** All insurance supervisors should be subject to professional secrecy constraints in respect of information obtained in the course of their activities, including during the conduct of on-site inspections. The insurance supervisor is required to hold confidential any information received from other insurance supervisors, except where constrained by law or in situations where the insurance supervisor who provided the information provides authorization for its release. Jurisdictions whose confidentiality requirements continue to constrain or prevent the sharing of information for supervisory purposes with insurance supervisors in other jurisdictions, and jurisdictions where information received from another insurance supervisor cannot be kept confidential, are urged to review their requirements.
Description	The FSC Law imposes duties of confidentiality on the GFSC and its staff. In Section 21 the Law says that: "Any information from which an individual or body can be identified which is acquired by the GFSC in the course of carrying out its duties shall be regarded as confidential by the Commission and by its members, officers and servants." The Section also sets out those circumstances where it is legitimate for the GFSC to disclose information. Those are: (a) to enable the GFSC to carry out any of its functions;

	(b) for the purposes of the investigation, prevention or detection of crime or with a view to the instigation of, or otherwise for the purposes of, any criminal proceedings; (c) in connection with the discharge of any international obligation to which Guernsey is subject; (d) to assist in the interests of the public or otherwise, any authority which appears to the GFSC to exercise in a place outside Guernsey., functions corresponding to any of the functions of the GFSC; or (e) to comply with the directions of any division of the Royal Court. A person who, without reasonable excuse, discloses information or who, without reasonable excuse, causes or permits the disclosure of information in contravention of this section is guilty of an offense and liable on conviction on indictment to imprisonment for a term not exceeding two years, or to a fine, or to both; and on summary conviction to a fine not exceeding £5,000, to imprisonment for a term not exceeding 3 months or to both. On appointment, GFSC staff are also required to sign an undertaking that they have read and understood the provisions of this section of the FSC Law. Signed undertakings are renewed annually. Restrictions on the disclosure of information without the consent of the person to whom it relates or from whom it was obtained are also contained in the IB Law and the IMII Law. The cases in which the supervisor is permitted to disclose or share confidential information are set out in the IB Law and the IMII Law. These include the disclosure and sharing of information to other supervisors, on public interest grounds, for the purpose of investigating, preventing or detecting crime or for the purpose of criminal proceedings. The confidentiality requirements apply also to information that the GFSC receives from other insurance supervisors abroad.
Assessment	Observed.
Comments	

Table 11. Summary Observance of IAIS Insurance Core Principles

Assessment Grade	Principles Grouped by Assessment Grade	
	Count	List
Observed	16	2–17
Largely observed	1	1
Materially nonobserved		
Nonobserved		
Not applicable		

Table 12. Recommended Actions to Improve Observance of IAIS Insurance Core Principles

Reference Principle	Recommended Action
ICP 1	In order to strengthen the operational independence of the GFSC, the mission recommends that the GFSC Law be amended to remove the power of the Advisory and Finance Committee to provide guidance and direction to the GFSC. The GFSC Law should establish safety, soundness, and integrity of the financial system as the objectives of the GFSC, and eliminate "development" as one of the GFSC functions. Further, there should be no provisions in the Law that could potentially compromise the above stated objectives. This would provide a clear legal framework that would avoid potential conflicts in the functions of the GFSC. The attainment and sustainability of these objectives will enhance the reputation and contribute to the development of the financial system in Guernsey. Increase number of staff of the Insurance Division.
ICP 8	Increase the legally required solvency minimum.
ICP 14	Complete the range of sanctions by the power of the supervisor to impose penalties (administrative fines).

Authorities' Response to the Recommended Action Plan to Improve Observance of IAIS Core Principles

Overview

76. The authorities welcome the IMF's assessment and confirmation that the Bailiwick of Guernsey has achieved a high level of compliance with the IAIS Core Principles.

Organisation (ICP 1)

77. See paragraphs 12 and 13 for the response on the recommendations concerning the GFSC's objectives and independence.

78. Since the IMF's assessment the staff of the GFSC's Insurance Division has increased to include an assistant actuary and two analysts, as recommended by the IMF.

Prudential Rules (ICP 8)

79. With regard to solvency requirements, provisions exist within the Insurance Business (Bailiwick of Guernsey) Law, 2002 for the GFSC to modify the solvency requirements of

each insurer depending on the size, nature and complexity of the risks being written. Solvency levels for individual insurers are set on this basis. The GFSC's requirements can be imposed at the licensing stage as well as on an ongoing basis. In practice, this means that solvency requirements are much higher than the minimum legal levels set under the law. The solvency of individual insurers is continually monitored by the GFSC.

Imposition of Penalties (ICP 14)

80. The GFSC will report to the States of Guernsey Advisory and Finance Committee in 2004 on the recommendation concerning the imposition of penalties.

IV. IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

A. General

81. This assessment of Guernsey's compliance with the IOSCO Objectives and Principles of Securities Regulation has been completed as part of the IMF Offshore Financial Sector (OFC) assesment program[7]. In the report the mission reviews the rules of law and practice about the regulation of securities and investments and, for this purpose, considers whether the Bailiwick has implemented the principles. The IOSCO, when adopting these Objectives and Principles, stated its commitment to high regulatory standards and effective international cooperation and these are central to the present assessment.

82. The GFSC is a statutory body responsible as a single regulator for the regulation and supervision of financial services business in the Bailiwick. It is a member of IOSCO and was a party to the IOSCO resolution adopting the statement of Objectives and Principles in September 1998. Company law is administered by the Law Officers. The Greffier maintains the register of companies.

Information and methodology used for assessment

83. The assessment has been undertaken by analyzing law and regulations, statements of best practice, and evidence of current practice in the Bailiwick and evaluating them against the 30 IOSCO Principles. Compliance with individual principles is rated according to the following; (i) implemented; (ii) broadly implemented; (iii) partially implemented; (iv) not implemented; or (v) not applicable.

84. In the course of this assessment the mission made a number of judgments. We report on these in Table 1 of the report.

85. The mission reviewed many background documents before or in the course of the assessment. These included the IMF's own guidance notes on assessment process and

[7] The assessment was undertaken by John Farrell.

procedures, various IOSCO reports and resolutions, relevant publications of OECD, selected Bailiwick legislation, regulations, ordinances, rules, codes and guidance statements, various documents on the GFSC website, the IOSCO self-assessments prepared by the GFSC, and various operational documents of the GFSC. In reviewing this material, the mission paid close attention to the explanatory notes accompanying the IOSCO statement of Objectives and Principles. It also considered the MFP Transparency Code. The mission had extensive discussions with representatives of the government, the FSC, professional bodies (including those representing independent auditors and legal advisers of firms licensed by the GFSC), industry associations, and a number of firms representative of the various categories of firms licensed to undertake securities and investment business. In the time available, the mission did not have the opportunity to confer with independent commentators.

86. There were no factors that impaired the assessment process. The mission received extensive briefings from GFSC staff on relevant matters and helpful answers to its many questions. The GFSC has a great deal of useful written material available, both on its website and in hard copy. The legislation, regulations, ordinances, rules, guidance statements and GFSC operational files were readily accessible. GFSC staff organized an extensive program of visits for team members. The mission is grateful for this.

Institutional and macroprudential setting, market structure

87. The core Bailiwick's law for the regulation of securities and investments relate to:

- the functions and powers of the GFSC;
- the licensing and supervision of those who undertake controlled investment business, whether in relation to collective investment schemes (CISs) or to general securities and derivatives;
- the authorization and supervision of CISs; and
- the conduct of controlled investment business by licensees.

88. A person may not carry on a controlled investment business in or from within the Bailiwick unless licensed to do so. A "Bailiwick body" may not carry on controlled investment business outside the jurisdiction without a license. A person carries on controlled investment business if, by way of business, it engages in a restricted activity in connection with a controlled investment. The term "restricted activity" is defined to cover the various activities associated with the conduct of investment business including the issue of securities for subscription. The term "controlled investment" appears to cover the full range of securities and investment products; the most important of which for the Bailiwick are interests in CISs. In the most general terms and subject to a number of important exceptions a CIS is "any arrangement relating to property of any description (including money)." Life insurance policies that have the character of investments are excluded. They are regulated as insurance products. They are dealt with elsewhere in the mission's overall report.

89. The most important types of investment business carried on in the Bailiwick are:

(i) management, administration, and custody of collective investment funds (open and closed-ended);

(ii) discretionary asset management;

(iii) nondiscretionary asset management;

(iv) stock broking; and

(v) provision of investment advice.

90. As at June 30, 2002, there were 428 entities licensed to carry on investment business, of which 403 were companies incorporated in the Bailiwick, one Bailiwick partnership and 24 branches of international institutions. Clients of investment businesses include local and overseas residents and local and overseas institutions and professional firms. The geographical spread of clients is diverse.

General preconditions for effective securities regulation

91. The GFSC has adopted as its primary objective:

> "to regulate the Bailiwick's finance sector to international standards and, by doing so, to protect depositors, investors, policy holders, other customers and the public."

92. Market access is determined by reference to the securities regulatory system and the decisions of the GFSC. The mission is not aware of any particular barriers to the entry or exit of market participants other than those which are incidental to the operation of the regulatory system. The Bailiwick does not have explicit rules of statute law about competition. It is nevertheless the team's impression that there is a diversity of market participants engaged in investment business.

93. As noted above, the Bailiwick has a conventional framework of general business law including a common law system. Securities law is backstopped by rules of law about contract, tort and property, and about serious fraud and other crimes involving fraud and deceit. Securities law is also dependent on mature rules of law about the constitution of entities which issue securities for subscription, in particular, company law and partnership law. Guernsey and Alderney both have mature rules about the formation and administration of companies and partnerships.

94. Some industry representatives consider that the cost of compliance with securities regulation is higher in Guernsey (and in Jersey and the Isle of Man) than in competitor jurisdictions. In the main they appear to accept this. They do so on the basis that a key determinant of success for the Bailiwick as an international finance center is its reputation. We routinely encountered a general understanding in this context of the importance of the regulatory system and broad support for the regulatory policies of the Bailiwick authorities.

95. The Bailiwick depends for its ability to develop as an international finance center on the quality of its regulation, the expertise of its people, the cost of doing business there and its tax regime. It has encountered criticism in the past, particularly from neighboring countries, about its tax regime. The Bailiwick authorities consider it all the more important in the circumstances to have and to be seen to have soundly based law and procedures for the supervision and regulation of market participants and to cooperate and to be seen to cooperate with equivalent authorities in other jurisdictions.

96. The Bailiwick also depends for its ability to develop as a finance center on its willingness to cooperate more generally with others on regulatory matters. The GFSC has direct bilateral relations with a number of regulators in overseas jurisdictions under MOUs on cooperation in the regulation of financial markets and institutions.

97. It is against the background of these general comments that we proceed to examine the extent to which the Bailiwick has implemented the IOSCO Principles.

B. Detailed Assessment

Table 13 Detailed Assessment of Observance of the IOSCO Objectives and Principles of Securities Regulation

Principles Relating to the Regulator	
Principle 1.	The responsibilities of the regulator should be clear and objectively stated.
Description	The responsibilities of the GFSC are set out in the Financial Services Commission (Bailiwick of Guernsey) Law, 1987, and amendments (the GFSC Law) and are restated annually in Appendix 1 of the GFSC's annual report. The responsibilities are divided into "general functions and statutory functions." These are set out respectively in Sections 2 and 3 of the GFSC Law. The general functions of the GFSC include: (a) to take such steps as it considers necessary or expedient for the development and effective supervision of finance business in the Bailiwick; (b) to provide to the responsible Committee of the States, when requested, reports, advice and assistance on any matter connected with finance business; and (c) to prepare and submit to the responsible committee recommendations for the statutory regulation of finance business and the revision of legislation about companies and other forms of business undertakings. The Financial Services Commission (Bailiwick of Guernsey) (Amendment) Law, 2002, adds to the GFSC's general functions: "the countering of financial crime and of the financing of terrorism." The GFSC's statutory functions include administering the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (the POI Law). The POI Law sets out the responsibilities and powers of the GFSC in connection with investment business. In addition the GFSC is responsible for the regulation of deposit taking, insurance business, the provision of fiduciary services, company administration, and acting as a company director by way of business.

	The GFSC is also responsible for administering the Borrowing (Control)(Bailiwick of Guernsey) Law,1946 which applies in respect of • the raising of money by the issue of shares; • the issue of company shares and debentures; and • the circulation of an offer of company shares or debentures. In the exercise of its functions the GFSC may take into account any matter which it considers appropriate but shall in particular have regard to: "(a) the protection of the public interest, including the protection of the public against financial loss due to dishonesty, incompetence or malpractice by persons carrying on finance business; and (b) the protection and enhancement of the reputation of the Bailiwick as a financial center." For the purposes of the GFSC's function in relation to the development of finance business in the Bailiwick (see paragraph 2 above) the 2002 Amendment Law defines "development" to include, among other things, "without limitation": "the establishment and ongoing support of bodies and organizations the functions of which include or are important or relevant to- (a) the development of finance business in the Bailiwick and of that sector of the Bailiwick economy which carries on finance business; (b) the improvement of the infrastructure of or serving that sector of the Bailiwick economy which carries on finance business; (c) the protection of the public; or (d) the protection and enhancement of the Bailiwick as a financial center."
Assessment	Implemented.
Comments	We note that the IOSCO Principles are backed by the three IOSCO Objectives are : • the protection of investors; • ensuring markets are fair, efficient, and transparent; and • reducing systemic risk. The Bailiwick may wish to consider in any review of its statement of responsibilities whether any aspect of its commitment to these objectives should be more explicitly recognized. We consider that the GFSC would be better placed to undertake work under the Borrowing (Control) Law if its powers were more up-to-date and better integrated with its other powers. The GFSC has informed us that it is proposing to review this Law, in the context of a more general review of Company Law. We recommend that the GFSC proceed to undertake this work. We have expressed concerns about the inclusion of development in the functions of the GFSC, particularly in the context of the enlarged definition of this term (see para 6 above). The GFSC has informed us that it will propose a change in the law to meet our concerns. The GFSC should be able to continue its support of the activities of the Training Agency that are consistent with the revised mandate.

Principle 2.	The regulator should be operationally independent and accountable in the exercise of its functions and powers.
Description	The GFSC has been established on the basis that it is operationally independent and fully accountable for its actions. The government is nevertheless responsible for the performance of a number of essential tasks : • to secure the enactment of appropriate rules of law about its establishment and constitution and about the regulation of markets and institutions; • to appoint and remove commissioners; • to arrange appropriate sources and levels of funding; • to afford the GFSC as an expert body which is continuously engaged with the private sector the opportunity to make recommendations on the laws which it administers and to receive and consider these recommendations; and • as the primary stakeholder to be concerned for the reputation and good standing of the GFSC and for this purpose to ensure that the GFSC is able to maintain appropriate standards of independence and accountability and perform its statutory functions. In addition, the Bailiwick relies to a considerable extent on the finance sector and its professional advisers for people who are qualified to serve as commissioners. Appropriate arrangements need to be in place to ensure that the GFSC is able to act independently in its dealings with the finance sector. We consider that any question about the independence and accountability of the GFSC needs to be answered in the context of these matters and the transparency with which they are addressed. **Operational independence** ***The law*** There are extensive rules of law about the GFSC and its responsibilities. These are described elsewhere in this report. They are enacted by or under the authority of the States. The States also have a continuing role in respect of secondary legislation. The States have an active and commendably large program of law reform work. The GFSC consists of five members. The policies and procedures pursuant to which they are appointed and removed are described in the law. The members are elected by the States from persons nominated by the committee and "having knowledge, qualifications or experience appropriate to the development and supervision of finance business in the Bailiwick." The members hold office for three years and are eligible for reelection. The Chairman is selected annually by the States from among the members. In the past the President of the Advisory and Finance Committee was required to be Chairman but this requirement ceased to apply with effect from February 1, 2003. We do not consider that the appointment of members under the law as amended raises questions for us on the independence of the GFSC. We consider, however, that difficult questions would arise on any proposal to appoint a person as a commissioner who was a member of the States. Both the States and the Advisory and Finance Committee have responsibilities under the laws which the GFSC administers and, to the extent practicable, need to be independently responsible and accountable in performing their respective functions. We think this might be all the more important where, as in the Bailiwick, there are close constitutional links between the legislature, the government, and the judiciary. We understand, however, that the present policy

	of the government is not to appoint a politician to the GFSC. A member may be removed from office for cause by the Chairman or by the States on the recommendation of the Advisory and Finance Committee. We query whether the Chairman of a statutory GFSC should have a personal discretion to remove other members from office. We think the Bailiwick should review this discretion. **Funding** The present institutional arrangements adopted by the States for the funding of the GFSC appear to work well and do not affect the GFSC's capacity to perform its work independently. Comment on funding more generally is dealt with elsewhere in the mission's report. Recommendations on the law—General policy The GFSC has explicit functions and responsibilities about advice and recommendations including those on the revision of legislation. It also has rule making powers. It is expected to consult with industry and others on much of its policy work. It is independently accountable for this work. This seems appropriate. However, a question arises for us under Section 7 of the GFSC Law which provides that the Advisory and Finance Committee may, "after consulting the Commission, give to the Commission (a) written guidance of a general character; and (b) written directions of a general character, concerning the policies to be followed by the Commission in relation to the development and supervision of finance business in the Bailiwick and the manner in which any function of the Commission is to be carried out." In principle, in the context of optimum arrangements about accountability and transparency, the power to give guidance and directions to a securities regulator should not be necessary. The policy of the law should be clear and the responsibilities of the regulator clear and objectively stated. If there is to be a power, it should be crafted to apply squarely within the core functions and responsibilities of the regulator, to be of a general character and not to intrude on operational independence. In the present case we have three comments: • the power applies not only to matters of policy but also to the manner in which the GFSC carries out its functions; • the power applies in respect of the GFSC's development function; and • acknowledging that any exercise of this power would be profoundly important in the life of the GFSC and, potentially, the license holders and others, we consider that the power should be exercised publicly. Notwithstanding these comments, we conclude that broadly speaking the power of guidance and directions conforms with Principle 2. We record moreover as a practical matter that we have seen no evidence of a lack of independence on the part of the GFSC in its dealings with others. There is a code of conduct regulating the conflicts of interests of commissioners. This was formally approved at a meeting of the GFSC. There is an equivalent code in the Staff Handbook applying to all staff. There are procedures for ensuring adherence to these. **Accountability** The commissioners are elected by the States under the GFSC Law. The GFSC is required to report annually to the Advisory and Finance Committee on its activities and financial affairs. This report must include a review of:

	• the adequacy and application of its systems of internal control; • the effective, efficient and economical management of its assets and resources; and • its compliance with such generally accepted principles of good corporate governance as it is reasonable to regard as being applicable to it. The report is published and is made available on the GFSC's website. Important decisions must be made in accordance with prescribed procedures. Section 35 of the POI Law requires that on any decision of the GFSC: • to refuse an application for a license; • to impose a condition on a license; • to cancel or suspend a license otherwise than at the request of the licensee; • to refuse authorization to a collective investment scheme; • to impose any condition on an authorization of a collective investment scheme; or • to revoke or suspend the authorization of a collective investment scheme otherwise than at the request of the manager, trustee or custodian. The GFSC must notify the applicant in writing of a proposed decision, offer the applicant up to 28 days to make oral or written submissions and, on request, furnish written reasons why it is considering taking the decision. The applicant may appeal to the Court against the decision on the grounds that it was ultra vires or was an unreasonable exercise of the GFSC's powers. The Court may quash or confirm the decision or may substitute any other decision which the GFSC could have made. In addition, the Court may review administrative decisions of the GFSC under its general power of judicial review. We query whether a court of law should have a general power to substitute its decisions for the decisions of an independent regulator which is bound by the rules of fairness, particularly where appeal rights are limited to ultra vires and unreasonable grounds. It might be better if the Court's power were limited to referring the matter back for redetermination. In addition from the time of institution of an appeal, the decision ceases to operate against the appellant. This is subject to a direction to the contrary by the Court on the application of the GFSC. The interests of investors and potential investors may be seriously at risk and we consider that the GFSC decision should continue to operate subject to any order of the Court on the application of the appellant. We understand it to be an accepted principle of the Common Law and associated jurisdictions that the decision of a tribunal or court should remain effective subject to the exercise by the court of an explicit power to stay the decision for good reason by interim order. Otherwise, these procedures for appeal and judicial review seem appropriate. The Director General and his staff regularly exercise certain of the powers of the GFSC on behalf of the commissioners. The Director General reports back to the commissioners on the exercise of these delegated powers. This is appropriate. The commissioners have powers of delegation and they have exercised them. **Conclusions** We consider that the Bailiwick has broadly implemented Principle 2 as it relates to operational independence. We consider that the Bailiwick has implemented Principle 2 as it relates to Accountability.
Assessment	Broadly implemented.
Comments	We raise questions about the following matters: • the discretion available to the Chairman of the GFSC to remove other members from

	office (para 7 above); • the terms and conditions under which a direction or guidance may be given to the GFSC (para 10 above); and • the consequences of an appeal to the Court against a decision of the GFSC on the grounds that it is ultra vires or unreasonable (para 15 above).
Principle 3.	The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.
Description	**Powers** The GFSC Law confers certain general powers which it describes as relating to the capacity of the GFSC as a corporate body. Section 8 of the Law provides that the GFSC may do anything which appears to it to be conducive to the carrying out of its functions. It may: • obtain information on development and supervision; • consult and seek advice; • publish information relating to its functions; and • provide advice, assistance and services with a view to securing the general well being of finance business in the Bailiwick. In addition to these general powers, the GFSC has power under the GFSC Law: • to levy fees and charges (Section 13); • to cooperate with foreign regulators including to share information which it may lawfully disclose (Section 21A); • to disclose confidential information where necessary: (a) to enable it to carry out a function under the GFSC Law; and (b) to assist an authority in another jurisdiction with functions corresponding to its own. The GFSC has powers under the POI Law. These include: • to grant or refuse a license to carry on a controlled investment business (Section 4); • at any time on or after the issue of a license to impose such conditions as appear to the GFSC to be necessary or desirable (Section 5); • to cancel or suspend a license (Section 6); • to authorize a CIS (Section 8); • to impose conditions on an authorization (Section 9); • to revoke or suspend an authorization (Section 11); • to make rules about controlled investment business and authorized CISs (Sections 12 to 20); • to obtain information from licensees and those appearing to require a license (Sections 27 and 30); • to report an auditor to a disciplinary body (Section 27B); • to apply to the Court for an injunction (Section 33); • to apply to the Court for a restitution order (Section 33);

	• to request the Law Officers to apply to the Court to prohibit a company director or manager (Companies (Guernsey) Law, Section 67A); • to request the Law Officers to bring criminal proceedings against any person. In addition, the Advisory and Finance Committee has power to regulate in particular cases. The GFSC exercises powers under the Borrowing (Control) (Bailiwick of Guernsey) Law, 1946 and the 1959 Control of Borrowing Ordinance (COBO) made under it, on transfer from the Advisory and Finance Committee. These include: • consent to the raising of money by the issue of shares; • consent to the issue of partly paid shares; • consent to the issue of securities other than shares if the body corporate is incorporated under the laws of the Bailiwick or the securities are to be registered in the Bailiwick; • consent to the circulation of a public offer of securities for sale or subscription; and • authorize the registration of a limited partnership. The GFSC's powers under the POI Law are extensive. It makes extensive use of the rule making powers in respect of CISs and those engaged in investment business. It makes extensive use of the operational powers in the ongoing regulation of licensees. The GFSC does not have power to issue directions to licensees. However, it has power to impose conditions on a license (section 5 POI Law). This power is expressed in the Law in terms that render it in substance, we consider, a power to give directions as well as a power to impose conditions. The power is described under Principle 9 paragraph 1 below and procedures relating to the exercise of the power under Principle 2 paragraph 14 above. The GFSC does not have power to impose administrative fines. However, we think the power to impose conditions on a license in the terms in which it is expressed in the Law can be an effective procedure for regulating licensees on a continuing basis. There are powers in the POI Law for dealing with a person who engages in investment business without a license. These are less effective than those which apply to a licensed person. One additional power which the GFSC might find useful, which is not provided in the present Law or in the proposed amendment law on misleading statements and practices, is the power to prohibit promotional statements by administrative process where in the opinion of the GFSC they are misleading or do not comply with the law. There are precedents for such a power in other jurisdictions. It would apply particularly to unlicensed persons but may also be a valuable supplementary procedure for dealing with uncooperative licensees. The GFSC does not have power to make rules under the Borrowing (Control) Law. It has power to consent to an issue of securities. This applies to investment products other than CISs, most importantly, interests in closed-ended investment schemes, interests in the cells of what are called protected-cell company and securities issued by trading companies, in the form of shares and debentures. The GFSC issues administrative guidance. It expects shortly to have explicit power under COBO to issue guidance on its COBO based policies. Moreover, the managers of an investment company based in the Bailiwick will need to hold an investment business license. The GFSC does not have an explicit power to review market practice and comment publicly on it. We refer to this matter under Principle 8. It does not have power to require a person, other than a licensee, to produce information for the purpose of communicating to an offshore regulator, merely to communicate the information which it has already acquired. We refer to this matter under Principle 13.

	The GFSC does not have full on-site inspection powers or the power of entry and search. We consider this under Principle 8. **Resources** The GFSC has the following divisions: banking, investment business, insurance, fiduciary business and enforcement, operations and personnel, and policy and international affairs. It also jointly funds a Training Agency the development of which it has taken responsibility for. The GFSC has a current complement of staff of 72. There are 19 people in the Investment Business Division including the director. The director expects to have an establishment of 24 people in the New Year. The present establishment is one secretary, 12 analysts, 4 senior analysts, a deputy director and a director. The division is subdivided into three teams, one for authorizations, one for off-site review and one for on-site inspections. The arrangements for the funding of the GFSC as described elsewhere in this report appear sound and reliable. The forward program of work for the Investment Business Division as described to the mission seems robust and the level of resources available for securities and investment work seem appropriate to the jurisdiction. The mission has met with a number of people in the financial services industry. It is our impression that the efforts of the GFSC are well supported in the community, reinforcing its capacity to perform its functions and exercise its powers effectively as an investment business regulator.
Assessment	Implemented.
Comments	The GFSC may find it useful to have statutory power to prohibit promotional statements which in its opinion are misleading or do not comply with the law (see para 8 above). We comment further on the powers of the GFSC under Principles 8 and 13 below in relation to • on-site inspection and entry and search, • GFSC public comment on investment business management and marketing practice, and • obtaining information for the purpose of communicating to an overseas regulator.
Principle 4.	The regulator should adopt clear and consistent regulatory processes.
Description	As noted above the GFSC has wide power to issue rules about investment business and has made extensive use of this. It consults widely on all its proposals for new rules. Indeed, it is required to do so under the POI Law (Section 13). There appears to be a wide-spread support in the finance sector for this rule-making power. The GFSC may give advice on the operation of the law or its own functions. These include general circulars to the investment industry and the media, articles in its publication « Update » and the annual report. The GFSC also produces guidance notes which are available on its website or directly from the GFSC. These include: • Investment Business in Guernsey—A Regulatory Overview; • Guidance Note—Outsourcing of Administration Functions in respect of Authorized Collective Investment Schemes; • Incorrect pricing of Authorized Collective Investment Schemes—Guidance Note on Correction and Compensation; • Guidance Notes on UK Public Offers and Promotional Activities; and • Guidance Notes on the Prevention of Money Laundering and the Countering of the Financing of Terrorism.

	It publishes general conclusions arising from investigations and, indeed, from routine monitoring. We have found a great deal of useful material on the website. In formulating its policies and processes, the GFSC has said that it aims to adhere to high regulatory standards following extensive industry consultation. Any person who is aggrieved by a decision of the GFSC on designated matters relating to the administration of the Law may appeal to the Court on the grounds that the decision was ultra vires or an unreasonable exercise of its powers. The GFSC is required under the POI Law to follow certain prescribed steps when taking various decisions about licensing or authorization matters. It must give notice that it is considering taking the decision and offer to state its reasons in writing on request. More generally, the staff handbook provides for GFSC staff to observe standards of fairness in performing the GFSC's regulatory and supervisory work.
Assessment	Implemented.
Comments	
Principle 5.	The staff of the regulator should observe the highest professional standards including appropriate standards of confidentiality.
Description	Section 18 of the GFSC Law requires the GFSC to review in each year, by the appointment of appropriately qualified and independent professional persons or otherwise, its "compliance with such generally-accepted principles of good corporate governance as it is reasonable to regard as being applicable to the Commission." The commissioners are required to satisfy themselves about the conclusions of this review. The staff handbook sets standards for the staff including standards about the confidentiality of information. The GFSC is required to review annually its professional standards, including its standards of confidentiality. **Avoidance of conflicts of interest** The commissioners and GFSC staff are required to be aware of actual and perceived conflicts of interest arising from the use of confidential information in their possession or to which they have access. commissioners and GFSC staff are required to submit details of investment holdings to a designated officer of the GFSC and, if necessary, explain any transactions. A commissioner or member of staff who becomes aware of a conflict of interest must inform a Director or the Director General as soon as possible. Staff are not permitted to present themselves for election to any significant public office including that of States Deputy. The commissioners are also required at each meeting of the commissioners to disclose any potential conflicts of interest arising at the meeting. All potential conflicts of interest as disclosed are minuted. **Observance of confidentiality and protection of data** The GFSC maintains standards of confidentiality in accordance with its standing policies. The GFSC Law protects the name of an individual or body and certain other information. The GFSC is subject to the confidentiality provisions of the GFSC Law. In addition it is subject to the Data Protection (Bailiwick of Guernsey) Law, 2001 which specifies the framework for the holding and disclosure of personal data. Procedures on compliance with this law are contained in the Staff Handbook. **Observance of procedural fairness** We refer to the GFSC's procedures under Principle 4 above.
Assessment	Implemented.
Comments	

Principles of Self-Regulation	
Principle 6.	The regulatory regime should make appropriate use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, and to the extent appropriate to the size and complexity of the markets.
Description	There is one SRO in the Bailiwick, the Channel Islands Stock Exchange (CISX).The CISX was established in March 1998 as a company limited by guarantee (LBG), with shares, under the Companies (Guernsey) Law, 1994. The objects of the CISX as set out in its Memorandum of Association include: • to carry on the business of an investment exchange and clearing house; to provide, manage and regulate markets in, and to provide clearing and settlement services with respect to transactions in, investments of all kinds, whether direct or derivative, including financial instruments and currencies; and to provide facilities for the transaction of the businesses of broking, dealing, market-making, stock lending, investment management and advice and other businesses in the field of financial services; • to act as an authority for the admission of investments to be traded or dealt in on any exchange or market and to maintain any official list for the time being required or recognized by the law of any country; • to provide information, depository and nominee services; • to provide, maintain and operate, systems for and in connection with the evidencing and transfer of investments without a written instrument and to regulate the use thereof; • to enter into arrangements of any kind and to cooperate and share information with governmental and nongovernmental authorities, bodies and persons in any part of the world, and in particular with those having responsibility for the supervision or regulation of financial services; • to promote high standards in the financial services industry and in particular to make, administer, monitor and enforce rules governing access to and use of any services and facilities provided by the CISX and the qualification and conduct of persons engaging in the financial services industry or any part thereof, and to make arrangements for the investigation of complaints in respect of business transacted by means of the CISX's services and facilities; • to establish and maintain, by the levying of contributions, by insurance or otherwise, compensation schemes for the benefit or protection of the public or of any class of persons; and • to carry on business as a general commercial company. The CISX is licensed by the GFSC under the POI Law to carry on the restricted activity of "operating an investment exchange" and is subject to GFSC regulation and supervision. The CISX has power under its Articles of Association to make Rules. It has made Membership Rules and Listing Rules. It monitors compliance with and enforces them. The rules require the members to be appropriately regulated. We consider this to be an appropriate use of an SRO.
Assessment	Implemented.
Comments	
Principle 7.	SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.
Description	There is one SRO, the CISX. The GFSC reviewed the CISX's constitution, structure, staffing plans, proposed rules and internal procedures before issuing a license and assessed them against

	equivalent arrangements in other jurisdictions, notably the United Kingdom. The CISX aims to ensure, among other things, that it observes standards of fairness and confidentiality. The GFSC maintains a program of on-site and off-site supervision and aims to verify this. The CISX has power, among other things, under its Articles of Association to make rules respecting: • the admission of members; • the conduct of disciplinary proceedings and the imposition of sanctions; • appeals against refusal of membership, expulsion, exclusion or suspension and other disciplinary sanctions; and • the admission of securities to the Official List. It has exercised this power in making Membership Rules and Listing Rules. The Articles establish a Market Authority "for the purposes of managing, operating and regulating the Company" and confer on it wide powers including the power "to apply and enforce Rules" and "to supervise compliance with the Rules." If the Market Authority rejects an application the Rules provide for a right of appeal to the board of directors and prescribe the procedure for this. There is a Disciplinary Committee which is responsible for considering reports from the Market Authority on disciplinary matters and there is a right of appeal from its decisions to a Disciplinary Appeals Committee. The Market Authority is effectively a senior management team. It is responsible for both operational and compliance matters. There is no formal separation at the decision making level within management between these two broad functions. Similarly there is no formal separation at the Board level when it is acting as an appeal authority. There is a Disciplinary Committee and a Disciplinary Appeals Committee which, like the Market Authority, are required to act fairly. These committees are described as sub-committees of the Board. There is no further statement in the CISX Rules about the structure or composition of these committees. This procedure appears to work well in practice in the Bailiwick and to have the confidence of the finance sector. CISX Directors have established clear rules about conflicts of interests, the confidentiality of information and the need to act in good faith. Staff at the CISX has equivalent obligations. Pursuant to their contracts of employment they sign an annual employee code of conduct. The Investment Exchange (Notification) Rules 1998 provides that the CISX must, in the case of: (a) the chairman, chief executive and board members; (b) the persons responsible for compliance and for finance; (c) the members of any body to which the CISX has delegated rule- making powers; (d) the members of any disciplinary body; (e) any arbitrator or member of an arbitration panel; and (f) the members of any complaints body, notify the GFSC of any: (a) change of name; (b) conviction for any offense concerning fraud or other dishonesty; (c) conviction for any offense under any legislation relating to finance business; (d) initiation of bankruptcy or similar proceedings; (e) refusal of any application for, or revocation or suspension of any license authorization or registration under any finance legislation;

	(f) disciplinary measures or sanctions by a regulatory authority or professional body; and (g) Court order disqualifying the person from acting as a director or manager of a company. The CISX is required to submit an annual regulatory plan in draft to the GFSC, the annual budget, any proposal to change the CISX rules, any proposal to change the Memorandum or Articles of Association and any proposal to delegate monitoring to a body outside the CISX. The GFSC monitors the operations of the CISX by off-site review and on-site inspections.
Assessment	Implemented.
Comments	We comment further on the structure and operations of the CISX under Principles 25 and 26.
Principles for the Enforcement of Securities Regulation	
Principle 8.	The regulator should have comprehensive inspection, investigation and surveillance powers.
Description	The GFSC's powers of inspection and investigation are set out in Section 27 of the POI Law. The GFSC may require a licensee and certain other persons : (a) to attend before the GFSC and answer questions and otherwise furnish information; (b) to furnish the GFSC with such information as it may reasonably require about any specified matter; and (c) to produce books or papers. The obligation to comply extends to any person who appears to the GFSC to be carrying on controlled investment business (Section 30). It is an offense to provide a misleading response to an enquiry by the GFSC under Sections 27 and 30 of the POI Law. The GFSC conducts on-site visits for the purpose of ensuring that licensees comply with the POI Law and the rules and regulations made under it. All licensees are subject to on-site visits. The GFSC does not have statutory on-site inspection powers and powers of entry and search. These are particularly useful powers in dealing urgently with an investment business which should be licensed but is not or which is unwilling to respond to a license condition. We consider it may be difficult to deal efficiently with this type of situation under the present law. Under a 2003 amendment to the GFSC Law which received royal assent after the mission the States can by Ordinance provide for the making by the Commission of site visits in respect of licensees and any other class of person. While it may not be necessary for the GFSC itself to have a power of entry and search an associated regulator such as the Law Officers should be able to act on its behalf in appropriate circumstances. The GFSC has indicated that it expects to see the Ordinance made in early 2004. Section 27(A) of the POI Law requires audit firms to report to the GFSC on any matter relating to a licensee, to a fund or to a client which appears to the auditor to be of material significance for determining whether a person is fit and proper to carry on controlled investment business, or whether the GFSC should exercise its powers under the POI Law to protect investors from significant risk of loss. As observed under Principle 3 the GFSC does not have an explicit power to review investment business management and market practice and to comment publicly on it. It would afford statutory backing to its practice of publishing conclusions arising from its investigation and monitoring work (see Principle 4 para 2 above). It would empower the GFSC to undertake case studies and publish reports in circumstances where an intermediary has engaged in an undesirable practice less than a breach of the law or a license term. It is in the context of this wide power of review that any power of the GFSC to publicly report institutions or individuals that are found to be not in compliance with regulatory or legal requirements can be most

	effective. In the absence of statutory on-site inspection powers and powers of entry and search we do not consider that the Bailiwick has fully implemented Principle 8.
Assessment	Partially implemented.
Comments	We recommend that the Government review the GFSC's powers and secure statutory powers of on-site inspection and entry and search. We also recommend that the GFSC consider whether to seek a general power to comment on investment business management and market practice.
Principle 9.	The regulator should have comprehensive enforcement powers.
Description	The GFSC has power under the POI Law to attach conditions to, suspend, cancel or revoke a license or authorization and to compel the production of information about a controlled investment business or a CIS. As we have noted elsewhere we consider that the power to impose conditions has very much the character of a power to issue a direction to licensees as well as a power to impose conditions (see Section 5 of the POI Law). For example, the GFSC may in the exercise of this power, prohibit a licensee from: • entering into transactions; • soliciting business; • carrying on business in a specified manner; • disposing of or otherwise dealing with any asset; or require a licensee; • to transfer assets to a trustee; and • to maintain assets in the Bailiwick. The GFSC Rules about investment business and CISs seem comprehensive and the GFSC has the power to enforce them as they apply to the individual licensee. It is a criminal offense to conduct a controlled investment business without a license, or to operate an unauthorized fund. It is also a criminal offense to provide misleading information to the GFSC in response to a statutory request. The GFSC may request the Law Officers to prosecute those who do not comply with the law. The GFSC inform us that they take into account a failure to respond to an information request when considering a licensee's status as a fit and proper person. The GFSC may commence proceedings in the court for a restitution order where there has been a breach of named laws and profits have accrued to any person or an investor has suffered loss. The GFSC may request the Law Officers to apply to the Court to prohibit a person from acting as a company director or manager. The CISX has the power to investigate and discipline its own members, including the power to levy fines and administrative sanctions. It may also direct the suspension of trading in individual trading in securities.
Assessment	Implemented.
Comments	
Principle 10.	The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.
Description	The Investment Business Division has a staff of 19 people and is expected to increase to 24 in 2003. It plans and implements an annual supervision program in relation to investment business licensees and CISs. For this purpose it maintains a program of off-site and on-site supervision. It utilizes off-site supervision to monitor compliance with the rules made under the POI Law, namely: • The Collective Investment Schemes Rules 1988;

	• The Collective Investment Scheme (Class A) Rules 2002; • The Collective Investment Schemes (Class B) Rules 1990; • The Collective Investment Schemes (Designated Persons) Rules 1988; • The Collective Investment Schemes (Qualifying Professional Investor Funds) (Class Q) Rules 1998; • The Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998; • The Licensees (Conduct of Business and Notification) (Non-Guernsey Schemes) Rules 1994; • The Investment Exchange (Notification) Rules 1998; • The Investor Protection (Designated Countries and Territories) Regulations 1989; • The Investor Protection (Designated Countries and Territories) (Republic of Ireland) Regulations 1992. These rules impose extensive requirements on licensees, most importantly for the purposes of off-site inspections, the notification of information to the GFSC. Licensees must submit routine notifications, annual compliance reports, audited annual reports and analyses of investor complaints. A licensee is required to notify the GFSC if at any time its financial resources fall below the minimum prescribed level. The GFSC aims to monitor compliance with any conditions imposed on a license or a fund authorization. The GFSC undertakes both routine inspections and inspections initiated in response to specific matters brought to its attention. In 2001, a total of 21 inspection visits were undertaken. Of these 11 were to designated managers and 6 to designated custodians/trustees. The visits also included two follow-up visits to confirm remedial action had been undertaken and one special review in response to specific issues which had come to the GFSC's attention. From January to mid-September 2002, the GFSC has made 18 on-site inspections to a range of licensees, including one inspection made to a firm in a foreign jurisdiction which is a subsidiary of a Guernsey financial institution. The GFSC is not obliged to give advance notice of an inspection, although it is normal practice to do so. It requests the licensee to provide standard information before the inspection and additional information during the visit. We are informed that the inspectors generally request copies of: • minutes of board meetings; • compliance reports; • management accounts; • procedures manuals; • complaints procedure; • disaster recovery plans; • anti-money laundering and counter terrorist financing policy; and • report on staff awareness. In addition there are categories of information which relate specifically to the type of business under review (e.g., stockbroker, designated custodian/trustee or designated manager). Following the receipt and assessment of this information and the assessment of other information in its possession, the GFSC holds a pre-visit meeting with the senior management of the licensee to discuss the key areas to be covered in the visit and any initial concerns the GFSC may have about the quality of the information provided. The GFSC aims to be open with

	the licensee about its areas of interest or concern, in order to reduce the risk of misunderstanding and to improve the effectiveness of the on-site review. There is a closing meeting after the inspection. Significant matters arising from an inspection visit are notified in writing to the board of directors of the institution concerned, while less significant procedural matters are referred to the senior management of the institution. The GFSC keeps detailed records of all matters covered during an inspection visit. The GFSC's practice, where it identifies deficiencies in the course of an inspection is to require the licensee to take remedial action within a specified time and to report back to the GFSC when it has done so. The GFSC maintains a diary system to check that the firm is meeting the timetable. Where serious control failings are apparent, the GFSC may attach a condition to the license until the situation has been rectified. It has done so on a number of occasions in the recent past. Notice periods for non-routine inspections have tended to be short. In determining the prioritization of visits to an individual licensee and their frequency, the GFSC inform us that they take account of a range of criteria including the nature of the licensee's business and its clients, the risks associated with the business, the quality and timeliness of statutory notifications, and the incidence of complaints.
Assessment	Implemented.
Comments	
Principles for Cooperation in Regulation	
Principle 11.	The regulator should have authority to share both public and nonpublic information with domestic and foreign counterparts.
Description	The Bailiwick does not have secrecy laws. Information held by the GFSC is subject to Section 21 of the GFSC Law. This states that "any information from which an individual or body can be identified" shall be regarded as confidential. The GFSC may disclose this information if it appears to the GFSC to be necessary: • to enable the GFSC to carry out any of its functions; • for the purposes of the investigation, prevention or detection of crime or with a view to the instigation of, or otherwise for the purposes of, any criminal proceedings; and • in connection with the discharge of any international obligation to which the Bailiwick is subject; • to assist in the interests of the public or otherwise, any authority which appears to the GFSC to exercise in a place outside the Bailiwick functions corresponding to any of the functions of the GFSC; or • to comply with the directions of the Royal Court. In addition, Section 21A of the GFSC Law requires the GFSC to: "take such steps as it considers appropriate to cooperate with any person or body : (a) who or which appears to the Commission to exercise in a place outside the Bailiwick functions corresponding to any of the functions of the Commission; or (b) for the purposes of the investigation, prevention or detection of crime or with a view to the instigation of, or otherwise for the purpose of, any criminal proceedings." The GFSC clearly has wide powers to disclose information. In addition, it does not require the execution of an MOU with a foreign regulator to be able to share information. However, such a memorandum is an increasingly common feature of the GFSC's arrangements (see Principle 12).

	In addition to the GFSC's powers, the Law Officers have powers under the Insider Dealing Law to obtain information and to share it with other regulators. We consider that the Bailiwick has implemented Principle 11.
Assessment	Implemented.
Comments	
Principle 12.	Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts.
Description	The GFSC has entered into the following MOUs in relation to investment business : • Australian Securities Commission (1996); • United States Commodity Futures Trading Commission (1994); • De Nederlandsche Bank NV (1993); • International Organization of Securities Commissions (1991 and 1996); • Jersey Financial Services Commission (1998); • Hong Kong Securities and Futures Commission (1992 and 1994); • London Stock Exchange (1998); • Commission Nazionale per le Societa e la Borsa (an Information Exchange Agreement in 1994 replaced by an MOU in 2002); and • Isle of Man Financial Supervision Commission (2002). These MOUs typically aim "to establish a framework for mutual assistance and to facilitate the exchange of information between the commissions to enforce or secure compliance with any laws or regulations of their respective jurisdictions." The GFSC informs us that it is currently negotiating MOUs with four other regulatory bodies. Two of these were finalized subsequent to the mission. The GFSC is able to share information without an MOU. However, the MOU represents an important public statement on cooperation and sets out the understandings of the parties on such practical matters as the type of information to which it applies, the procedures for making a request, the uses to which the information may be put and the understandings on confidentiality. Under the Data Protection (Transfer in the Substantial Public Interest) Order 2002, the GFSC is required to obtain an undertaking that personal information will be kept confidential but, subject to that, is able to agree to the disclosure of personal information where it considers it is in the substantial public interest to do so.
Assessment	Implemented.
Comments	
Principle 13.	The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.
Description	The GFSC did not at the time the mission visited Guernsey have explicit statutory powers to require the production of information for communication to an offshore regulator. We thought it should. The GFSC's statutory powers were limited to the sharing of information already in its possession as described under Principle 12. Suitable powers are now contained in a 2003 amendment to the FSC Law. We are informed that this received royal assent in July 2003. We note that the Law Officers have power under the Company Securities (Insider Dealing) (Bailiwick of Guernsey) Law, 1996 to appoint inspectors where there are circumstances suggesting that an insider dealing offense under the laws of another country may have been committed and that a person in the Bailiwick may have been concerned or may have

	information or documents. The Law Officers have power to transmit material obtained under statutory authority to the prosecuting or supervisory authorities in the other country. We considered that the Bailiwick had partially implemented Principle 13 at the time of the mission visit. We consider that it has now fully implemented the principle with the coming into force of the 2003 amendment to the FSC Law.
Assessment	Implemented.
Comments	
Principles for Issuers	
Principle 14.	There should be full, accurate and timely disclosure of financial results and other information that is material to investors' decisions.
Description	The disclosure requirements for public offerings arise in three ways: • by GFSC discretion, through the exercise of its powers under COBO, in respect of offerings other than Guernsey open-ended funds; • under the various POI Rules in respect of the offer of interests in Guernsey open-ended funds; and • by the CISX under the listing rules about disclosure. Securities—other than Guernsey open-ended funds—offered in or from within the Bailiwick of Guernsey must have GFSC consent under COBO. The GFSC is, at present, conferring with the finance industry on the terms of a detailed guidance note on the disclosure of information in an offer by a closed-ended fund. The directors of the issuer take responsibility for the content of the prospectus or other offer document. For open-ended fund approvals, a lawyer's certificate is also required, confirming that the relevant disclosure requirements have been met. Promotion to private investors must be carried out under the authority of a Guernsey licensee who must take responsibility for the content of any local presentation. In the case of an offer under COBO, the GFSC does not have power to supervise the issuer but may take action against the responsible licensee, for example, by imposing a condition on the license. The Companies (Guernsey) Law, 1994 provides for the keeping of accounting records, the appointment of auditors, the preparation of financial statements and distribution to shareholders. There are similar provisions in the Companies (Alderney) Law, 1994. The GFSC, as a matter of policy, will not permit a public offer to be made without an undertaking from the issuer in the prospectus to provide for the regular disclosure of information, including the preparation and timely distribution of audited financial statements. The disclosure requirements for open-ended funds are set out in the relevant class rules (the Collective Investment Schemes Rules 1988, and the Collective Investment Scheme (Class A) Rules 2002 (the Class A Rules), the Collective Investment Schemes (Class B) Rules 1990 (the Class B Rules) and the Collective Investment Schemes (Qualifying Professional Investors Funds) (Class Q) Rules 1998 (the Class Q Rules). No offering may proceed until the GFSC has issued its consent. The GFSC maintains an active compliance program in respect of these obligations of issuers. We have confirmed this by inspection of GFSC files and discussions with GFSC officers. The program is described under Principle 10 above. There is at present a Closed-Ended Fund Working Party comprising representatives of the GFSC and the finance sector which has prepared and published detailed proposals for ongoing reporting by closed-ended fund managers. The GFSC expects to formalize these shortly in a formal policy statement.

	Where a company is listed on the CISX, the listing rules require regular and timely reporting of financial information and of matters significant to the company. Listed companies are required to publish annual and semi-annual reports. This is backed by Guernsey company law where there is a requirement for the preparation and distribution of audited annual financial statements.
Assessment	Implemented.
Comments	
Principle 15.	Holders of securities in a company should be treated in a fair and equitable manner.
Description	There are a number of provisions in the Companies Laws in force in the Bailiwick which aim to ensure that holders of securities are treated in a fair and equitable manner. While, as we understand the position, the GFSC is not responsible for enforcing company law, investment company managers based in the Bailiwick will hold an investment business license and will be subject to GFSC supervision. There is a very small number of trading companies with members of the general public as shareholders and the ongoing management of these will be regulated under the Companies Laws. In either case, the GFSC will have been involved under COBO at the time of issue of securities and the terms of the investment contract as contained in the offer document will have been settled before the COBO consents were issued. Investors benefit from this GFSC involvement. The Companies (Guernsey), Law 1994 contains a number of provisions which are material to the treatment of holders of securities. These relate largely to the constitution, corporate governance and reporting to shareholders. They are rather more for the benefit of shareholders than debenture holders. The debenture holders will particularly benefit, we think, from the GFSC review of the investment contract at the time the securities are first issued. There are rules of law about insider dealing which establish an offense of insider dealing and powers of investigation (see under Principle 28). In addition the London City Code on Takeovers and Mergers applies to listed companies which are resident in Guernsey, Jersey, the Isle of Man as well as the United Kingdom.
Assessment	Implemented
Comments	
Principle 16.	Accounting and auditing standards should be of a high and internationally acceptable quality.
Description	Subject to exceptions, in particular in relation to 'dormant companies' and 'asset holding companies', all companies are required under the Companies (Guernsey) Law, 1994 and the Companies (Alderney) Law, 1994 to prepare, and deliver to their members annual financial statements audited by an external auditor. In addition, the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 (the FNCC Rules) require all licensees to maintain accounting records and to prepare audited annual financial statements. They regulate the appointment of qualified auditors and a change of auditors. The Collective Investment Schemes Rules 1988, the Collective Investment Scheme (Class A) Rules 2002, the Collective Investment Schemes (Class B) Rules, 1990 and the Collective Investment Schemes (Qualifying Professional Investors Funds) (Class Q) Rules 1998 also contain rules on the preparation of annual reports and financial statements and the auditing of accounting information by qualified auditors. The auditors' report will state whether in their opinion the financial statements have been properly prepared in accordance with the law and whether they give a "true and fair" view. Bailiwick companies will normally adopt generally accepted accounting principles (GAAP) in the United Kingdom and the audit will be conducted on this basis. However under a Statement of Channel Islands Accounting Practice, it is recognized that the financial statements of companies incorporated other than in the Channel Islands may be drawn up to comply with the standards of the jurisdiction, e.g., United States GAAP, or International Accounting Standards. The accounting standards adopted will be identified in the audit report to the financial statements.

	A person is not qualified for appointment as an auditor unless a member of: • the Institute of Chartered Accountants in England and Wales; • the Institute of Chartered Accountants of Scotland; • the Institute of Chartered Accountants in Ireland; or • the Chartered Association of Certified Accountants, and eligible for appointment under the rules of the body as an auditor. Qualified auditors who are members of any one of the above bodies will be subject to its independence and audit rules and guidelines and subject to its disciplinary authority. There has been some consideration in the Bailiwick in recent times about the best source of authority for audit standards and the review of auditor performance, particularly in the context of evidence of unsatisfactory practice overseas. The GFSC should continue to review policy in this area. For the present the mission considers it appropriate for the Bailiwick to work to maintain satisfactory standards through the present institutional links between the profession and the offshore institutes and the links between some firms and their affiliates in the United Kingdom and elsewhere.
Assessment	Implemented.
Comments	The source of authority for financial reporting and audit standards and for the review of auditor performance is under careful review internationally. We consider that the GFSC, the accounting profession and others should continue their ongoing consideration of this matter.
Principles for Collective Investment Schemes	
Principle 17.	The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.
Description	Any person who carries on restricted activities in connection with a collective investment scheme as defined by the POI Law must have a license. This includes the promoter, the administrator, the manager and the trustee or custodian of a collective investment scheme. Section 4 of the POI Law sets out the criteria which the GFSC must apply in considering an application. These include: (a) the general nature and specific attributes of the controlled investment business to which the application relates; (b) whether or not the applicant is a fit and proper person to carry on that business; (c) the manner in which it is proposed to organize the carrying on of controlled investment business to which the application relates, the number of persons who will be responsible for carrying on each aspect of that business and the relationship between those persons; (d) what, if any, economic benefit the Bailiwick is likely to derive from the carrying on of that business; and (e) any other factors which the GFSC thinks it appropriate to consider. The GFSC may grant or refuse a license and may attach conditions to a license. The GFSC has made Rules relating to the conduct of investment business and the operation of the various classes of CISs. The Rules are supplemented by published guidance on certain aspects of fund operations, often based on matters which it has observed in the course of its monitoring programs. Licensees must have appropriate resources and experience to act and meet requirements under the Collective Investment Schemes (Designated Persons) Rules 1988 in connection with financial records, financial statements, financial resources, audit, financial notifications, best execution, arrangements for indirect payment for services, product bias, gifts, benefits in kind and reciprocal arrangements, the allocation of transactions, records relating to transactions, contract notes, the inspection of records, client money, compliance arrangements and

	complaints and other notifications. Licensees must also comply with equivalent requirements in connection with financial resources, notifications and records, fitness and properness, and compliance arrangements under the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998. In addition, section 8 of the POI Law requires that Bailiwick collective investment schemes must be authorized by the GFSC. The GFSC has made rules – the Class A Rules, the Class B Rules and the Class Q Rules – which regulate the operation of funds. The Class A Rules are the most detailed, with less detailed arrangements applying to the Class B and Class Q funds which are normally offered to more sophisticated or institutional investors. These scheme-based Rules do not apply to closed-ended funds which are promoted under the authority of COBO. The GFSC maintains an active compliance program in respect of those who market or operate a CIS. We have confirmed this by inspection of files and discussions with GFSC officers. The program is described under Principle 10 above. In December 1988 the Bailiwick was granted "designated territory status" under Section 87 of the United Kingdom Financial Services Act. Class A funds are therefore freely marketable in the United Kingdom. Similar arrangements are in place with Australia, Belgium, Hong Kong, Isle of Man, Japan, Jersey, the Netherlands, the Republic of Ireland, South Africa and Switzerland.
Assessment	Implemented.
Comments	
Principle 18.	The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.
Description	Collective investment schemes may be formed as trusts, bodies corporate, or as limited partnerships. The Trusts (Guernsey) Law, 1989, the Companies (Guernsey) Law, 1994 and the Limited Partnerships (Guernsey) Law, 1995 provide the basic framework for the establishment of the scheme structures. The POI Law and the rules made under it establish additional controls on the legal form and structure of schemes. The Rules provide for the segregation and protection of client assets. The Bailiwick also promotes the PCC. The GFSC attributes the following characteristics to this type of company: • is one legal entity; • provides, for each cell, legal segregation and protection of assets and liabilities; • may create its own core shares and cell shares, providing two classes of assets—core (or noncellular), attributable to the PCC directly, and cellular attributable to the cells; • can provide an unlimited number of cells; • can be converted from an existing company; • offers flexibility in the allocation of capital between the core and individual cells; and • offers a wide range of potential applications. We are informed that creditors of an individual cell of a PCC have no recourse to the assets of another cell, but will have recourse to the core assets. Provision is made in the Protected Cell Companies Ordinance, 1997 for the incorporation of such a company, or the conversion of an existing company into such a company, with the consent of the GFSC. The Ordinance allows for the PCC to be a CIS. The vehicle was originally developed, we understand, for captive insurance business within a group of

	companies. The GFSC also allows for the use of umbrella funds, subject to the Rules. It considers the PCC a more secure investment vehicle than the umbrella fund. For all CISs client assets must be held in a segregated pool under the control of a separate custodian. In the case of Class A schemes the custodian must not only be separate but also independent from the manager's group. The Collective Investment Schemes (Designated Persons) Rules 1988 also require subscription monies received from investors and redemption monies due to investors to be segregated from the assets of the fund. In addition to the custody function, the custodian's duties under the Class A and Class B Rules but not the Class Q Rules extend to overseeing the operation of the fund by the manager and administrator and satisfying itself that the manager and administrator operate the fund in accordance with the POI Rules and with the objectives disclosed to investors. In this sense, the custodian's role is akin to that of a trustee. This trustee function applies irrespective of the legal form of the fund. The segregation and protection of client assets are evaluated by the GFSC during on-site visits to the administrators, managers and custodian/trustees of collective investment schemes.
Assessment	Implemented.
Comments	
Principle 19.	Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.
Description	Every fund authorized under the POI Law must offer to investors a prospectus or statement of scheme particulars or equivalent document setting out prescribed information, including the objectives and policies of the fund; the names of the manager, custodian, registrar, auditor and any other functionaries appointed to operate the fund; the manner and frequency of valuations; subscription and redemption arrangements; the fees and charges to be paid by investors; the level of fees and charges which will be met by the fund; and other information – such as suitable risk warnings. The detailed requirements are specified at Schedule 4 to the Class A Rules, the Schedule to the Class B Rules and the Schedule to the Class Q Rules. The GFSC is required to approve the Scheme Particulars. The manager must revise the Scheme Particulars annually and any changes must be submitted to the GFSC for consideration before they are implemented. The manager (and, in the case of a company based scheme, the directors) have a responsibility to ensure that the prospectus/scheme particulars do not contain any untrue or misleading statements. The CIS Rules also require scheme annual reports and financial statements (and, additionally, interim reports for Class A schemes) to be prepared and distributed to investors. The rules prescribe detailed contents for the reports and accounts, which must be published within six months of the end of the period to which they relate. For Class A and B schemes, the designated custodian/trustee must report on the management of the scheme. The CIS Rules provide for the periodic valuation of property, to be carried out on both offer and bid basis, and for the pricing of units. The Scheme Particulars must describe the arrangements for this. The GFSC maintains an active compliance program in respect of those who market or operate a CIS. We have confirmed this by inspection of files and discussions with GFSC officers. The program is described under Principle 10 above.
Assessment	Implemented.
Comments	

Principle 20.	Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.
Description	The CIS Rules set out the requirements for the valuation of CISs and the arrangements for pricing, subscription and redemption of units in a scheme. As noted under Principle 19, the pricing basis must be disclosed in the Scheme Particulars or equivalent document. The GFSC has also issued guidance on the steps to be taken by operators and custodians to ensure that valuation and pricing is conducted in an efficient and controlled manner so as to minimize the risk of error. Compliance with the rules and guidance notes on asset valuation and pricing are monitored by the GFSC during on-site visits (see also under Principle 10 above). The CIS Rules set out the requirements for the redemption of units. The Scheme Particulars must describe the procedures for redemption and the circumstances in which the redemption of units may be suspended. The GFSC must be informed of the suspension of redemption rights. Fund administrators' policies, in connection with the redemption of units are monitored by the GFSC during on-site visits.
Assessment	Implemented.
Comments	
Principles for Market Intermediaries	
Principle 21.	Regulation should provide for minimum entry standards for market intermediaries.
Description	All market intermediaries and investment advisers require a license under the POI Law. The minimum entry standards are set out in the Law as noted under Principle 17. The GFSC requires as a matter of policy that new entrants demonstrate that they have an already established track record in their sphere of activity, that they are persons of integrity, honesty and competence, and that they have adequate financial resources. They must also have an appropriate business plan. Section 4(3) of the POI Law states: "In considering whether to grant an application made under Section 3 the Commission shall have regard to the need to protect the public and the reputation of the Bailiwick as a financial center; and to that end the Commission shall consider : (a) the general nature and specific attributes of the controlled investment business to which the application relates; (b) whether or not the applicant is a fit and proper person to carry on that business; (c) the manner in which it is proposed to organize the carrying on of the controlled investment business to which the application relates, the number of persons who will be responsible for carrying on each aspect of that business and the relationship between those persons; (d) what, if any, economic benefit the Bailiwick is likely to derive from the carrying on of that business; (e) if the applicant has stated that he proposes to carry on controlled investment business in, or from within, Alderney or Sark, any opinion expressed, in response to a notice given under subsection (2), by the Policy and Finance Committee of the States of Alderney or by the Greffier (registrar of companies) of Sark as the case may be; and (f) any other factors which the Commission thinks it appropriate to consider." Licensees must be "fit and proper," that is, in accordance with a GFSC policy paper on the website, they must have: • integrity; • solvency; and

	• competence. The GFSC describe their more detailed expectations of a licensee in the policy paper. To meet the competence requirement the business must among other things be directed by at least two individual people (the "four eyes" policy). The Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 (the FNCC Rules) apply to market intermediaries and investment advisers. Among other matters, these rules require the appointment of a qualified independent auditor and the production of annual audited financial statements. These must include a statement of financial resources certified by the auditor. The GFSC maintains an active compliance program in respect of CIS disclosure. We have confirmed this by inspection of files and discussion with GFSC officers. The program is described under Principle 10 above.
Assessment	Implemented.
Comments	
Principle 22.	There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.
Description	Paragraph 8 of Schedule 2 to the FNCC Rules states "A licensee should ensure that it maintains adequate financial resources to meet its investment business commitments and to withstand the risks to which its business is subject." Part 2 of the FNCC Rules sets out minimum capital requirements for the various categories of investment business including market intermediaries and investment advisers. Client money and client assets must be segregated from a firm's assets at all times. Most market intermediaries are branches or subsidiaries of firms regulated in other jurisdictions–particularly the United Kingdom—and subject to capital adequacy standards in those jurisdictions. As described under Principles 11 and 12, the GFSC is able to share information with the relevant foreign regulator. The GFSC reviews and evaluates the capital and other prudential standards as maintained by market intermediaries during on-site visits.
Assessment	Implemented.
Comments	
Principle 23.	Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.
Description	Market intermediaries and investment advisers must comply with the FNCC Rules. They must observe the following 10 Principles set out in Schedule 2: (a) integrity (principle 1); (b) skill, care and diligence (principle 2); (c) conflicts of interest (principle 3); (d) information about customers objectives (principle 4); (e) information for customers (principle 5); (f) segregation of customer assets (principle 6); (g) high standards of market conduct (principle 7); (h) adequacy of financial resources (principle 8); (i) internal organization (principle 9); and (j) relations with GFSC.(principle 10). The FNCC Rules contain obligations relating to a licensee's conduct of business. These obligations include requirements relating to:

	(a) customer relations: • customer agreements; • suitability of investment; • disclosure of risks and charges; • inducements; and • complaints, (b) dealing, managing, and advising: • order priority; • best execution; • timely and fair allocation; • churning and switching; and • the content of contract notes, (c) and safekeeping of customer assets and client money. The licensee must undertake an annual review to determine the effectiveness of its compliance and monitoring procedures. It must have a written procedure for the handling of complaints and must submit an annual report to the GFSC on significant complaints received, settled and outstanding. The GFSC informs us that in its monitoring work, it emphasizes the responsibility of senior management for the quality of the internal control environment and the importance of proper segregation and reconciliation of customer asset holdings and client money holdings. The GFSC undertakes off-site monitoring and on-site inspections of all licensees. These are described under Principle10 above.
Assessment	Implemented.
Comments	
Principle 24.	There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.
Description	Where the GFSC considers that a licensed investment business has insufficient financial resources it may impose a condition on the license. Such a condition may have important consequences. It may have the character of a direction to the licensee, for example, that the licensee should not dispose of any asset or class of assets or that it should transfer assets into a trust account (see Section 5 of the POI Law). There is an investor compensation scheme in place in respect of Class A CISs (that is, schemes which are for offer to the general public), to mitigate the effect of a failure. Moreover the GFSC is at present conferring with the Law Officers on possible amendments to the Companies Law on corporate rescue provisions. Nevertheless the GFSC does not have special powers to intervene to deal with a failure.
Assessment	Partially implemented.
Comments	We recommend that the Bailiwick consider the powers which should be available to the GFSC to deal with the failure of an intermediary.
Principles for the Secondary Market	
Principle 25.	The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.
Description	The operation of an investment exchange is a restricted activity requiring a license from the GFSC under the POI Law. The expression “operating an investment exchange” applies both to an exchange and to an alternative trading system. There is one exchange currently established in Guernsey, the CISX. The CISX was established in March 1998 as a company limited by guarantee, with shares. It is licensed by the GFSC. The GFSC monitors the CISX through on-site and off-site supervision. The number of securities admitted to the CISX Official List as at October 31, 2002 was 280. The market capitalization as at 31 October 2002 was U.S.$17 billion. Prior calendar year figures were:

YTD	31 Oct. 2002	2001	2000	1999
Trading companies		2	-	1
Closed-ended investment funds				
Primary	3	5	4	-
Secondary	11	22	27	8
Open-ended investment funds	16	28	60	54
Specialist debt securities (Bonds)	2	14	6	4
SPVs	1	-	3	-
Warrants	2	7	10	-
Total:	**35**	**93**	**110**	**67**

Trading figures were:

(In pounds sterling)

YTD	08 Nov 2002	2001	2000	1999
Shares traded	76,955,496	75,327,426	31,676,148	32,598,695
Value	72,102,762	76,262,293	47,032,605	52,420,553
Transactions	672	620	367	267

The trading system

The key features of the trading system are:

- an electronic bulletin board is maintained by Reuters on which market makers may input two-way prices and other brokers may enter orders in real time;
- all trading is done by telephone;
- trades are reported to the exchange using the bulletin board and must be published within three minutes of execution;
- information on corporate actions, net asset value, historical price information (12 month period), recent trade history and current background information on listed securities is available on Reuters;
- information about listed entities is reported to the CISX and disseminated by Reuters on a continuous basis; and
- information on all quotes, orders and trades is stored at the exchange, both to facilitate market surveillance and to provide a historical record.

The market is screen-based with no trading floor.

The trading hours are from 8.00am until 4.30pm, Monday to Friday. All Trading Members have access to the trading platform as a condition of their membership. All securities transactions must be reported to the Market Authority within three minutes of the trade. The CISX requires information on trades, counter-party ID, security, price, date, time and size.

The price of all deals reported is distributed immediately by the CISX via Reuters. The Market Authority sets and publishes the normal market size for each security within the CISX pages on Reuters. The GFSC and any user of Reuters have access to the CISX pages (CISXINDEX).

The CISX does not provide clearance and settlement facilities. The Market Authority in consultation with the issuer's sponsor designates an approved clearance system for each security (see Principle 30).

	Supervision The CISX must, under the Investment Exchange (Notification) Rules 1998, notify the GFSC of information relating to: • key individuals; • regulatory plans and rules; • auditors; • fees and charges; • annual report, accounts and budgets; • directors' annual statement of opinion on sufficiency of financial resources; • quarterly management accounts; • the constitution; • delegation of monitoring; • complaints; • trading hours; • force majeure; • listings; • membership; • investigations; • defaults; and • insolvency and legal proceedings. The CISX has a continuing requirement under the law to maintain: • sufficient financial, human and technical resources; • monitoring and enforcement; • investigation of complaints; and • promotion and maintenance of standards. The CISX rulebook contains rules about trading and settlement, admission of products to trading, admission of participants to the trading system, the provision of trading information, the routing of orders, trade execution, past trade reporting and publication, supervision of system and participants, dispute resolution and appeals procedures, operational failure and trading disruptions. The GFSC's on-site inspection procedures are generally as described under Principle 10. **The members** A member may be a Trading Member or a Listing Member. A member must: • be a corporate, partnership or legal entity which is regulated by the CISX or a regulatory body in a recognized jurisdiction approved by the CISX or, in the case of a Listing Member that is not licensed, by a member of a professional body approved by the CISX; • satisfy the board that it is of good financial standing and integrity; • satisfy the Board it is fit and proper to be a member; • not carry on any business inconsistent with its membership of the exchange; and • comply with the rules of the exchange. As at September 30, 2002 there were 32 Members, three of which were Trading Members, Collins Stewart (CI) Ltd (regulated by the GFSC), and Dresdner Kleinwort Wasserstein Securities Ltd and Winterflood Securities Ltd (regulated by the UK Financial Services Authority), and 29 were listing members.

	The Membership Rules contain a Code of Conduct which includes Principles of Best Practice, and rules about Conduct of Business and Forbidden Market Practices. These apply to all members. In addition the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 contain detailed conduct of business rules which also apply to members who are licensed. A Trading Member may register as a market maker in listed securities specified by the Trading Member, and will be required to comply with the CISX's obligations of a market maker. Trading Members are subject to visits by the CISX and Reuters to confirm the necessary systems are in place to enable trading to occur. A Listing Member must be established as an entity in the Channel Islands and must have suitably qualified staff. An issuer wishing to have its securities listed on the exchange is required to engage the services of a Listing Member who will act as a sponsor. There are two categories of sponsors, those who may sponsor all types of securities to listing and those who may only sponsor the listing of investment funds. There are currently 29 Listing Members, of which one third are law firms providing corporate services, one Member is an accountancy firm, and the balance are investment fund managers or administrators. A listing member is required to: • confirm to the exchange that it has satisfied itself as to compliance with the relevant requirements of the listing rules; • communicate and deal with the exchange on all matters arising in connection with the application for listing and the continuing obligations of the issuer; • prepare and lodge with the exchange a formal application for listing together with all supporting documentation; and • seek the approval of the exchange for the listing prospectus or other disclosure document. **Listings** Listings are covered by the Listing Rules. The Rules cover: • general requirements and market authority; • compliance and market enforcement; • sponsors and authorized representatives; • application procedures and special categories of procedures; and • the rules are subject to review by the members and by the GFSC before they are adopted. A listing member of the CISX sponsors applications. The listing member is required to carry out a program of due diligence on the issuer and its directors before submitting an application for listing. Directors' declarations are provided. The CISX may at its discretion confer with the GFSC and ask it to carry out further search. All listed funds are regulated in a jurisdiction recognized by the CISX. There are a number of securities that are seldom if ever traded. The open-ended funds are a case in point. The primary purpose of the listing appears to be for the issuer to establish a respected and independent source of information on the affairs of the fund which is available to investors and to those who promote or advise on the fund. The objective is achieved by entering into continuous disclosure obligations with a stock exchange of good standing. There may be circumstances in which the listing of interests in a closed-ended fund not otherwise traded may be important for trading purposes, in particular, to provide an exit mechanism to interest

	holders. Nevertheless that appears to be a lesser consideration. **Financial resources** The available clearance and settlement systems are in other jurisdictions. Both the CISX and the GFSC, in supervising the CISX, are expected to satisfy themselves that the systems are subject to adequate regulation in the home jurisdictions. The GFSC is responsible for monitoring the financial resources of both the CISX and the members who are its license holders. An approved offshore regulator is responsible for monitoring the financial resources of the system operators and the CISX members who are based offshore. The CISX is not responsible for monitoring the resources of its members. The present scheme of regulation may be appropriate for the size, level of activity and exposure of the CISX and those who trade on it but the board of directors of the company and the GFSC will need to keep its systems and activities under continuing review. As at December 31, 2001, the CISX had net assets of GBP869,167. Operating expenditure for the year was GBP612,286. All elected members of the company have undertaken to contribute up to GBP10,000 each in the event of a winding up. The maximum aggregate value of the present undertakings is GBP320,000.
Assessment	Implemented.
Comments	
Principle 26.	There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.
Description	We have reviewed the material relevant to this Principle under Principle 25. We consider that the Bailiwick has implemented Principle 26.
Assessment	Implemented.
Comments	
Principle 27.	Regulation should promote transparency of trading.
Description	The CISX market is established as a public market (see Principle 26) and it is operated and supervised on this basis. The Membership Rules impose obligations on those undertaking transactions including obligations about the reporting of information. They also impose a Code of Conduct including provision for such matters as Client Order Priority, Timely Execution and Best Execution. The Listing Rules impose Continuing Obligations on the Listed Issuers including the fundamental obligation to keep the public, the CISX and the holders of securities informed of material information. The FNCC Rules, which apply to all licensees, contain provisions about dealing, managing, and advising, in particular: • customer order priority; • timely execution; • best execution; • timely and fair allocation; • churning and switching; and • dealing ahead of published research or analysis.
Assessment	Implemented.
Comments	
Principle 28.	Regulation should be designed to detect and deter manipulation and other unfair trading practices.
Description	Insider dealing is a criminal offense under the Company Securities (Insider Dealing) (Bailiwick of Guernsey) Law, 1996. It applies to transactions on the CISX but also on any of a lengthy list of overseas exchanges. It confers investigation powers on the Law Officers. It does not impose transaction reporting obligations on insiders who engage in transactions. It does not apply

	generally to manipulation and unfair dealing and is not in itself sufficient to meet the needs of Principle 28. The Law Officers administer this Law. They may appoint inspectors to investigate a suspected offense. GFSC officers may be appointed as inspectors. These powers may not be used for the purpose of assisting a prosecuting or supervisory authority in another jurisdiction in respect of a contravention or suspected contravention of insider trading law in that jurisdiction. They may nevertheless be used by the Law Officers for communicating information which the Law Officers have already acquired in the course of their work. The City Code on Takeovers and Mergers and the Rules Governing Substantial Acquisitions of Shares also apply to listed companies resident in Guernsey, Jersey and the Isle of Man as well as the United Kingdom. The Protection of Investors (Bailiwick of Guernsey) (Amendment) Law, 2003, extended the law by establishing new offenses relating to misleading statements and practices and a new offense of market abuse. It extended the GFSC's power to obtain information to apply to the circumstances of a suspected offense although it did not appear to extend it to apply to a person who was not a licensee or associate or was otherwise engaged in investment business as defined. Market manipulation is difficult to detect and difficult to prove in a court. Clear powers to obtain information are essential to the process of detecting and deterring manipulation and unfair trading as contemplated by Principle 28. A clear power to share information with other regulators is equally important and is dealt with under Principle 11. A 2003 amendment law now covers manipulation and unfair trading, although it does not prescribe procedures for obtaining information from those people who are not carrying on investment business as defined such as professional investors or intermediaries. The GFSC inform us that it will rely on the Law Officers to take enforcement action in these cases. The 2003 amendment has received royal assent and we consider that the Bailiwick has now fully implemented Principle 28.
Assessment	Implemented.
Comments	Should there be a significant increase in turnover on the CISX, particularly in equities, the Government may need to consider whether there should be transaction reporting requirements for directors and other insiders under the law. In the meantime there are reporting provisions in the Listing Rules which bind listed issuers but not directors or other insiders personally.
Principle 29.	Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.
Description	As noted under Principle 22, all licensees, including the CISX and its members, are subject to the FNCC rules, which include minimum solvency requirements. Those solvency requirements are supplemented by the requirement that all client assets and money be segregated from the licensees' own assets. The FNCC rules are being reviewed by a joint commission/industry working party and public consultation is expected to commence shortly on a planned revision to the FNCC rules in a number of areas including solvency and client money/asset segregation issues. At present, of the three broker/dealers domiciled in Guernsey two are branches of UK firms and subject to United Kingdom FSA capital adequacy requirements. The third provides the GFSC with monthly statements, on the UKFSA basis, on solvency and the control of large exposures. In the meantime, the GFSC is at present preparing a consultation document on these matters. It intends to issue new rules during 2004. In the meantime the present procedures for the regulation and supervision of the exchange appear to provide a solid if incomplete coverage.
Assessment	Partially implemented.
Comments	

Principle 30.	Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.
Description	The Investment Exchange (Notification) Rules 1998 require the CISX to "either itself provide satisfactory procedures (including default procedures) for the settlement of transactions on the exchange or ensure such provision by means of services provided under clearance systems approved by it." The Rules relating to the settlement of transactions are set out in Chapter 6 of the CISX Rules. They deal among other things with: • trade confirmation; • the method of settlement including designation of clearance system; • timing of settlement; • responsibility for settlement; • partial settlement; • late settlement; • buying-in; and • the appointment of settlement agents. Trading in the shares of local companies may be settled via Crest or Crest Residual International. Debt securities and other eligible securities may be settled through either Cedel Bank or EuroClear. The Rules state this is unless otherwise agreed by the parties to the transaction at the time of transaction. The CISX must consent to any such non-standard settlement. Under the CISX Rules the Market Authority determines the standard settlement period for each security, in general following London market practice for the type of security concerned. Current market practice is for the settlement of domestic and foreign equities on a T+3 basis. The CISX and the GFSC must reassure themselves that these systems are subject to satisfactory regulatory oversight in their home jurisdiction. In addition the GFSC's oversight responsibilities apply on a continuing basis.
Assessment	Implemented
Comments	

Table 14. Summary Observance of the IOSCO Objectives and Principles of Securities Regulation

Assessment Grade	Principles Grouped by Assessment Grade	
	Count	List
Implemented	26	1, 3, 4, 5, 6, 7, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 25, 26, 27,28 ,30
Broadly implemented	1	2,
Partially implemented	3	8, 24, 29
Not implemented	...	...
Not applicable	...	...

Table 15. Recommended Plan of Actions to Improve Observance of the IOSCO Objectives and Principles of Securities Regulation

Reference Principle	Recommended Action
Principles Relating to the Regulator (CP 1–5)	
CP 1	1. We note that the IOSCO Principles are backed by the three IOSCO Objectives are : • the protection of investors; • ensuring markets are fair, efficient, and transparent; and • reducing systemic risk. We recommend that the GFSC consider in any review of its statement of responsibilities whether any aspect of its commitment to these objectives should be more explicitly recognized. We consider that the GFSC would be better placed to undertake work under the Borrowing (Control) Law if its powers were more up-to-date and better integrated with its other powers. The GFSC has informed us that it is proposing to review this Law, in the context of a more general review of Company Law. We recommend that the GFSC proceed to undertake this work.
Principles for the Enforcement of Securities Regulation (CP 8–10)	
CP 8	We recommend that the government consider whether the GFSC should have access to powers of entry and search, directly or through another agency such as the Law Officers. We recommend that the GFSC consider whether to seek a general power to comment on investment business management and market practice.
Principles for Issuers (CP 14–16)	
CP 16	The source of authority for financial reporting and audit standards and for the review of auditor performance is under careful review internationally. We recommend that the GFSC, the accounting profession and others should continue their ongoing consideration of this matter.
Principles for Market Intermediaries (CP 21–24)	
CP 24 There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.	We recommend that the Bailiwick consider the powers which should be available to the GFSC to deal with the failure of an intermediary

Authorities' Response to the Recommended Plan of Actions to Improve Observance of the IOSCO Objectives and Principles of Securities Regulation

Overview

98. The authorities welcome the IMF's assessment and confirmation that the Bailiwick of Guernsey has achieved a high level of compliance with the IOSCO Objectives and Principles of Securities Regulation.

Principles Relating to the Regulator (Principle 1)

99. See paragraph12 for the response to the recommendation concerning the GFSC's objectives.

100. The Control of Borrowing regime is being reviewed as part of a review of company law and a consultation document will be issued in 2004.

Principles Relating to the Regulator (Principle 2)

101. See paragraph 13 for the response on the recommendation concerning the GFSC's independence.

Principles for the Enforcement of Securities Regulation (Principle 8)

102. The States Assembly approved the drafting of separate, explicit, statutory on-site inspection powers with regard to investment licensees in 2002. Consequently, the Financial Services Commission (Bailiwick of Guernsey) (Amendment) Law, 2003 provides the States Assembly with an enabling power to make an Ordinance covering this matter. It is intended that the States Assembly will consider the Ordinance in early 2004. The Protection of Investors (Bailiwick of Guernsey) Law, 1987 already provides the GFSC with comprehensive powers to obtain information and interview investment licensees' staff; on-site inspections have been conducted since 1989.

103. In addition, it is intended to promote an amendment to the Protection of Investors (Bailiwick of Guernsey) Law, 1987, which will provide the GFSC with powers of entry and search after obtaining a warrant from the Bailiff. A similar provision is already found in the other regulatory legislation administered by the GFSC.

104. With regard to the recommendation that the GFSC should possess a general power enabling it to comment on investment business management and market practice, the GFSC will report to the States of Guernsey Advisory and Finance Committee on the recommendation in 2004. There is nothing in the current framework which prohibits the GFSC from commenting on investment business management and market practice should it see fit.

Principles for Issuers (Principle 16)

105. The Bailiwick of Guernsey does not issue its own accounting or auditing standards; it follows internationally recognised accounting standards. The GFSC monitors the changing international standards and will continue to liaise with the local accounting profession, investment industry and other interested parties in respect of accounting and auditing matters that impact the Guernsey investment industry.

Principles for Market Intermediaries (Principle 24)

106. The GFSC intends to liaise with the finance sector with a view to promoting an Ordinance under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 in 2004, which will include specific legislative provisions for dealing with the failure of a market intermediary.

Principles for Secondary Market (Principles 29)

107. The GFSC intends to publish a consultation document on the management of large exposures, default risk and market disruption and to issue new rules during 2004.

V. REVIEW AGAINST THE OGBS STATEMENT OF BEST PRACTICE FOR TRUST AND COMPANY SERVICE PROVIDERS

A. General

108. In August 2002 , a Working Group established by the Offshore Group of Banking Supervisors (OGBS) produced a draft "Statement of Best Practice" (Statement) for trust and company service providers (CSP). The Fund agreed with the Commission that the Statement will be used for the review of trust and company service providers in Guernsey[8]. Subsequent to the mission the statement was formally adopted by the OGBS.

Methodology

109. The OGBS Working Group did not develop a methodology to accompany the Statement. Reviewers working for the Fund, who use the Statement in their work, developed the methodology used for the review.

110. The Statement is applicable to trust and company service providers whether or not they are based in a jurisdiction that has a formal licensing and supervisory regime. Thus, unlike the principles applicable to banking, insurance and securities, the Statement does not require that trust and company service providers are licensed or that they are subject to ongoing supervisory or enforcement procedures.

[8] The assessment was undertaken by Neville Grant

111. Even though Guernsey licenses and supervises trust and company service providers , the mission concluded that, to ensure consistency between this and future reviews of other jurisdictions, some of which may not have a formal system of licensing and supervision in place, it was not appropriate to review issues such as the independence, accountability and resources of the regulator, the licensing process, ongoing supervision or enforcement except to the extent necessary to review compliance with the Best Practice Statement.

112. Furthermore, the mission has had to make certain assumptions in the way that it has interpreted the Best Practice Statement.

113. The Best Practice Statement is expressed as a set of general principles rather than a set of detailed criteria. In the circumstances, the mission has provided an indication of how the regulation of fiduciaries in Guernsey compares with the Best Practice Statement but has not attempted to provide a specific measure of compliance as it has in respect of the Basle, IAIS, and IOSCO Principles.

114. The Statement includes consideration of the following:

- fit-and-proper criteria;
- conduct of business;
- the holding and sharing of information;
- cessation of business; and
- misleading statements.

Additional issues

115. The assessment team has, of course, had the opportunity of examining the regulation of trust and company service providers as undertaken in Guernsey. Although the report contains recommendations to the Commission, it should be appreciated that it is not, and should not be considered to be, an assessment.

B. Detailed Assessment

Table 16. Detailed Assessment Against the OGBS Statement of Best Practice for Trust and Company Service Providers

Definition of Trust and Company Service Business	
Principle 1.	**The scope of trust and company service business should be adequately defined**.
	1.1 The scope of activities subject to the requirements of a jurisdiction should cover at least the following (when provided in the course of business): Company service provider • acting as company or partnership formation agent; • acting as (or arranging for another to act as) a director or secretary of a company or a partner of a partnership; • providing a registered office, business address or accommodation, correspondence or administrative address for a company, partnership or for any other person; • acting as, or arranging for another to act as, a nominee shareholder or unit holder for another person. Trust service provider • acting as (or arranging for another to act as) a trustee of an express trust.
Description	In Guernsey, company and trust service provider business is regarded as fiduciary business and is defined under the Fiduciary Law (s.2) as: • the formation, management or administration of trusts, and the provision of advice in relation to the formation, management or administration of trusts, including: • acting as corporate or individual trustee or protector for trusts; • the provision to trusts of corporate or individual trustees or protectors; • company or corporate administration including: • the formation, management or administration of companies, partnerships or other unincorporated bodies, and the provision of advice in relation to the formation, management or administration of companies, partnerships or other unincorporated bodies, whether incorporated or established in or under the laws of the Bailiwick or elsewhere; • the provision to any such companies, partnerships or other unincorporated bodies of: • corporate or individual directors; • individuals or companies to act as company or corporate secretary or in any other capacity as officer of a company, partnership or other unincorporated body other than a director; • nominee services, including (without limitation) acting as or providing nominee shareholders; • registered offices or accommodation addresses (the expression "address" in this subparagraph including any postal, telecommunication or electronic address); • acting as director of any company or unincorporated body, or as partner of any partnership, whether incorporated, registered or established in or under the laws of the

	Bailiwick or elsewhere; • the provision of executorship services including (without limitation) acting as, or accepting an appointment made by will as, an executor of a will or administrator of an estate. A significant number of persons are exempted from the licensing requirements, see explanatory note and exempted activities following principle 1.4 below.
Comments	
	Additional Criteria 1.2 Many jurisdictions provide that companies must appoint a registered agent. It is desirable that in such jurisdictions acting as registered agent is incorporated within the definition of company service business.
Description	There is no such requirement in Guernsey. There is a requirement to have a registered office and the provision of that is regulated (see Fiduciaries Law s.2(1)(b)(ii).
Comment	
	1.3 The trust law of many jurisdictions recognizes enforcers, protectors and custodians. It is desirable that the provision of these services is, as far as necessary, also covered by the definition of trust service business.
Description	This is covered in the Fiduciaries Law section 2(1)(a) "the formation, management or administration of trusts, and the provision of advice in relation to the formation, management or administration of trusts, including (without limitation): • acting as corporate or individual trustee or protector for trusts; and the provision to trusts of corporate or individual trustees or protectors.
	1.4 It is also desirable for the definition of trust business to include the provision of trust management and administration services, insofar as those activities are not otherwise regulated.
Description	See response to principle 1.1 above.
Comments	
	Explanatory note Countries and jurisdictions may provide for limited exceptions to the requirements set out in this Methodology in respect of CSPs that do not provide director or nominee shareholder services and that do not handle or manage client assets or funds. *The exceptions could include lesser standards covering:* • the span of control covering the number of persons engaged in the business; • the level of qualifications/experience of the persons engaged in the business; • the capital/professional indemnity insurance requirements; and • the audit requirements. **Exempted activities** The Fiduciary Law encompasses a very wide range of activities, and as a result there are a number of exemptions for activities where regulation is not appropriate or necessary. *The following are not regulated activities (Fiduciaries Law s.3):* (a) acting as trustee or custodian of a collective investment scheme authorized by the GFSC under section 8 of the Protection of Investors (Bailiwick of Guernsey) Law,1987; (b) acting as a director of a company which has an established place of business within the Bailiwick provided that no services consisting of or comprising a regulated activity are supplied to the company by the director (other than acting as director); (c) acting as a director of a company which is quoted on a stock exchange recognized by

	the GFSC for the purposes of this paragraph; (d) acting as a director of a company where more than half in nominal value of the equity share capital of that company is held by: (i) the director, as beneficial owner; (ii) any close relative of the director, as beneficial owner; or (iii) the trustees of a trust of which a person mentioned in subparagraph (i) or (ii) is a beneficiary; (e) acting as a director of a supervised company; (f) acting as a director of a company which is a subsidiary of a company described in paragraphs (b), (c), (d) or (e); (g) acting, where the person so acting is an individual, as a director of not more than six companies, being directorships which are not the subject of an exemption contained in any other paragraph of this subsection, except in any case where the GFSC does not apply the exemption contained in this paragraph in respect of any person on the grounds that, having regard to the criteria of Schedule 1, the GFSC is not satisfied that he is a fit and proper person to be or to become a director of a company; and, where the GFSC decides not to apply the exemption contained in this paragraph, it shall serve notice to that effect on the person concerned, giving particulars of the right of appeal set out in section 19; (h) acting as bookkeeper or company secretary of a company which has an established place of business within the Bailiwick provided that no services consisting of or comprising a regulated activity are supplied to the company by the person concerned (other than acting as bookkeeper or company secretary); (i) acting as a partner of a partnership which has an established place of business within the Bailiwick provided that no services consisting of or comprising a regulated activity are supplied to the partnership by the partner (other than acting as partner); (j) acting as a partner of a partnership: (i) which holds a license to carry on controlled investment business under section 4 of the Protection of Investors (Bailiwick of Guernsey) Law, 1987 or which is exempt from licensing under section 29 of that Law; or (ii) which holds an authorization under section 8 of that Law; (k) acting as a limited partner in a limited partnership; (l) acting as bookkeeper of a partnership which has an established place of business within the Bailiwick provided that no services consisting of or comprising a regulated activity are supplied to the partnership by the person concerned (other than acting as bookkeeper); (m) the acceptance of money on terms under which the money: (i) is paid by way of advance or part payment under a contract for the sale, hire or other provision of property or services and is repayable in the event of the property or services not in fact being sold, hired or otherwise provided; (ii) is paid by way of security for the performance of a contract or by way of security in respect of loss which may result from the nonperformance of a contract; or (iii) without prejudice to subparagraph (ii), is paid by way of security for the delivery up or return of any property, whether in a particular state of repair

	of otherwise; (n) acting as guardian of a minor or person under legal disability where the appointment is made by, and where the discharge of the functions of guardian is subject to the supervision of, the Royal Court, the Court of Alderney or the Court of the Seneschal; (o) acting as executor of the will of, or administrator of the estate of, a person who was resident or domiciled in the Bailiwick at the time of the execution of the will or at the time of death, provided that the person so acting is a lawyer; (p) acting as trustee of testamentary trusts created by the will of a person who was resident or domiciled in the Bailiwick at the time of the execution of the will or at the time of death, provided that the person so acting is a lawyer; (q) the provision of advice or the drafting of documents by a lawyer, accountant or actuary in the ordinary course of carrying on the profession of lawyer, accountant or (as the case may be) actuary; (r) the incorporation of companies by an advocate and the drafting of minutes of meetings by a lawyer, accountant or actuary; (s) the preparation and auditing of accounts; (t) activities undertaken in the course of a profession or business: (i) which are undertaken without separate or additional remuneration (whether from the client concerned or from a third party); and (ii) which are incidental to the carrying on of that profession or business; provided that the person carrying on the profession or business does not hold himself out as undertaking those activities; (u) the activities of the Ecclesiastical Court and Registrar thereof in relation to the granting of probate and letters of administration; (v) the provision of accommodation addresses (within the meaning of section 2(1)(b)(ii)(D): (i) by the States of Guernsey Telecommunications Board or the States of Guernsey Post Office Board (or any company succeeding to the undertaking of either of those Boards) or by an internet or telecommunications service provider; or (ii) where the address is provided solely for the service of process or the service of notice under a contract; (w) any activity carried on under the authority of and in accordance with the conditions of a license, registration or authorization granted under any of the regulatory Laws; (x) the following activities when carried on by a registered insurance intermediary within the meaning of section 49A of the Insurance Business (Guernsey) Law, 1986: (i) the formation of, and the provision of advice in relation to the formation of, a retirement annuity scheme or retirement annuity trust scheme approved by the Administrator of Income Tax under the provisions of part XIII of the Income Tax (Guernsey) Law, 1975; or (ii) the formation of, and the provision of advice in relation to the formation of, a pension scheme or trust of a life assurance policy; (y) any particular activity, transaction or appointment specifically exempted from the operation of section 2 by written instrument of the GFSC; and for the purposes of this paragraph:

	(i) an application for such an exemption shall be made in such form and manner, and shall be accompanied by such information and documents, as the GFSC may require; (ii) the application shall be accompanied by such fee as may be prescribed by regulations under section 7; (iii) the application may be refused or granted subject to such conditions as the GFSC may consider necessary or expedient; (iv) the GFSC may at any time after receipt of the application require the applicant to furnish such additional information and documents as it considers necessary or desirable; and (v) the exemption may be revoked or varied at any time by the GFSC by written notice to the person to whom it was granted.
Fit-and-Proper Criteria	
Principle 2.	**All countries/jurisdictions should require that those individuals holding key positions in a trust or company service provider ("key persons") should be fit and proper.**
Description	With regard to key persons the Fiduciary Law Section 6 by implication considers certain persons to be "key persons." The Law provides that where the application is for a full fiduciary license, the GFSC must be satisfied that the criteria are satisfied by the applicant itself and in relation to anyone who is to be a director, controller, partner or manager. A controller includes: • a managing director or chief executive of the applicant; • a shareholder controller—someone who, alone or with associates, controls or is entitled to control the exercise of at least 15 percent of voting power at general meeting; or • an indirect controller—someone in accordance with whose instructions the directors are accustomed to act. The minimum criteria for licensing are contained in Schedule 1 to the Fiduciary Law. These minimum criteria cover the following: • integrity and skill; • economic benefit to the Bailiwick (full fiduciary license holders); • fit-and-proper persons; • business to be directed by at least two individuals (full fiduciary license holders); and • business to be conducted in prudent manner. The GFSC does not have the power to vary the standards applied in determining whether an applicant meets these criteria. However, the GFSC will determine whether any conditions should be attached to a license, for example restricting the activities the fiduciary can undertake. All applications are independently verified by the GFSC. The verification process involves a detailed review of the application, including a review of certain databases. Each controller, director and manager of the applicant is required to submit a personal questionnaire. This requires background information on the person, including experience, details of current and previous employment and any disciplinary action taken against them. It also contains a request for details of any membership/licensing by other regulators. Such references are taken up with these regulators. The GFSC also, where it considers it desirable on risk-based analysis to do so, conducts on-site visits to applicants before deciding whether to grant a license. This occurs in approximately one third of cases and involves verification of the information provided in the application on the

	applicant's take-on and other procedures. A visit at this stage also allows the GFSC to probe the competence of the applicant or its staff. Those applicants who are licensed will all be subject to an on-site inspection program.
Comments	
	2.1 In assessing whether a key person is fit and proper, the country/jurisdiction should consider his: • honesty, integrity and reputation; • competence and capability; and • financial soundness.
Description	This will require a consideration of all relevant matters including the specific criteria set out in principles 2.2, 2.3 and 2.4. The Fiduciary Law (Schedule 1) at subsections 3 (2) and 3 (3) is relevant. Subsection 3.2 states that in determining whether a person is fit and proper to hold a fiduciary license or a particular position, regard shall be had to: (a) his probity, competence, experience and soundness of judgment for fulfilling the responsibilities of a licensed fiduciary or (as the case may be) of that position; (b) the diligence with which he is fulfilling or likely to fulfill those responsibilities; (c) whether the interests of clients of the applicant or licensed fiduciary are, or are likely to be, in any way threatened by his holding a fiduciary license or that position; (d) his educational and professional qualifications, his membership of professional or other relevant bodies and any evidence of his continuing professional education or development; (e) his knowledge and understanding of the legal and professional obligations to be assumed or undertaken; and (f) his procedures for the vetting of clients and his record of compliance with any provision contained in or made under the Criminal Justice (Fraud Investigation) (Bailiwick of Guernsey) Law, 1991 or the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999. and Subsection (3) states that: Without prejudice to the generality of the foregoing provisions, regard may be had to the previous conduct and activities in business or financial matters of the person in question and, in particular, to any evidence that he has: a) committed any offense, and in particular any offense involving fraud or other dishonesty or violence; (b) contravened any provision contained in or made under this Law, the regulatory Laws or any other enactment appearing to the GFSC to be designed for protecting members of the public against financial loss due to: (i) dishonesty, incompetence or malpractice by persons concerned in the provision of regulated activities, banking, insurance, investment or other financial services; or (ii) the conduct of discharged or undischarged bankrupts or persons who are otherwise insolvent; (c) engaged in any business practices appearing to the GFSC to be deceitful or oppressive or otherwise improper (whether unlawful or not) or which otherwise reflect discredit on his method of conducting business or his suitability to carry on regulated activities; (d) engaged in or been associated with any other business practices or otherwise conducted

	himself in such a way as to cast doubt on his competence and soundness of judgment.
Comments	
	2.2 In the case of the person's honesty, integrity and reputation, the following matters are relevant and should be considered: (a) any criminal offense of which he has been convicted or any criminal charges outstanding, particularly where the offense concerned is an offense of dishonesty or an offense relating to financial crime or committed under any financial services legislation.
Description	The Fiduciaries Law (Schedule 1 para. 3(3)(a) states that regard may be had to the previous conduct and activities in business or financial matters of the person in question and, in particular, to any evidence that he has (a) committed any offense, and in particular any offense involving fraud or other dishonesty or violence;
Comments	Although the Law does not mention criminal charges the GFSC does not believe that this prejudices the generality of fit and proper considerations. The GFSC notes that pending charges would raise questions of integrity, probity or soundness of judgment under para. 3(2)(a) of Schedule 1 of the Fiduciaries Law.
	(b) any adverse finding, settlement or fine in civil proceedings, particularly in connection with a company or a financial services business;
Description	The Fiduciary Law Schedule 1 para. 3(2)(c) requires the GFSC in assessing applicants for a license to consider the previous conduct and activities in business or financial matters of the person in question and, in particular, to any evidence that he has contravened any provision contained in or made under this Law, the regulatory Laws or any other enactment appearing to the GFSC to be designed for protecting members of the public against financial loss: (see response to principle 2.1 above–Fiduciary Law (Schedule 1, para. 3.3, b–d).
Comments	
	(c) any association, past or present, with a firm, company or other person that is or has been the subject of a regulatory investigation or disciplinary or enforcement proceedings;
Description	See response to principle 2.1 above—Fiduciary Law (Schedule 1) para. 3.3.d.
Comments	
	(d) any disciplinary, enforcement, disqualification or similar proceedings to which he has, or may be, subject or any professional or administrative reprimands;
Description	See response to principle 2.1 above—Fiduciary Law (Schedule 1) para. 3.3.d.
Comments	
	(e) any previous regulatory breaches committed by him or by a person with whom he is or has been associated and any complaints made against him; and
Description	Breaches of regulatory law by the individual are covered by Schedule 1 para. 3(3)(b). See also principle 2.2.b above. The GFSC noted that association with someone who has committed such breaches would be approached as in 2(c) and (d) above. Complaints against an applicant are covered by the Fiduciaries Law Schedule 1 para.5(9) (c) which provides that the GFSC shall have regard, in determining whether a person is to be regarded as conducting his business in a prudent manner, to the complaints history of the applicant or licensed fiduciary.
Comments	
	(f) whether he has been candid and truthful in his dealings with the Director and/or any other regulatory body.
Description	The Fiduciaries Law s.46 (1) creates an offense of providing misleading information in connection with a fiduciary license application. It states that: A person who:

	(a) in connection with an application for a fiduciary license under this Law; (b) in purported compliance with a requirement imposed by or under any provision of this Law or of any Ordinance, regulation or rule made under it; or (c) otherwise than as mentioned in paragraph (a) or (b) but in circumstances in which he intends, or could reasonably be expected to know, that the statement, information or document provided by him would or might be used by the GFSC for the purpose of exercising its functions conferred by or under this Law: (i) makes a statement which he knows or has reasonable cause to believe to be false, deceptive or misleading in a material particular; (ii) dishonestly or otherwise, recklessly makes a statement which is false, deceptive or misleading in a material particular; (iii) produces or furnishes or causes or permits to be produced or furnished any information or document which he knows or has reasonable cause to believe to be false, deceptive or misleading in a material particular; or (iv) dishonestly or otherwise, recklessly produces or furnishes or recklessly causes or permits to be produced or furnished any information or document which is false, deceptive or misleading in a material particular; is guilty of an offense. In addition, Section 46(2) states that: A licensed fiduciary which fails to provide the GFSC with any information in its possession knowing or having reasonable cause to believe: (a) that the information is relevant to the exercise by the GFSC of its functions under this Law in relation to the licensed fiduciary; and (b) that the withholding of the information is likely to result in the GFSC being misled as to any matter which is relevant to and of material significance to the exercise of those functions in relation to the licensed fiduciary, is guilty of an offense.
Comments	
	2.3 In the case of the person's competence and ability, the following matters are relevant and should be considered: (a) the extent of that person's relevant experience; and (b) where the person is an individual, his or her knowledge and professional and other relevant qualifications.
Description	The Fiduciaries Law, Schedule 1 para. 3(2) refers to competence and experience. It states that in determining whether a person is a fit and proper person to hold a fiduciary license or a particular position, regard shall be had to his probity, competence, experience and soundness of judgment for fulfilling the responsibilities of a licensed fiduciary or (as the case may be) of that position; and paragraph 3(2)(d) refers to educational and professional qualifications membership of professional or other relevant bodies and any evidence of continuing professional education or development.
Comments	
	2.4 In the case of a person's financial soundness, the following matters are relevant and should be considered: (a) any insolvency proceedings that have been instituted against the person;
Description	The GFSC does request this information on its application form...
Comments	The GFSC stated that it looks at resources under Fiduciaries Law, Schedule 1, para. 5 and would become concerned about any relevant matter. In addition, question 27 of the PQ asks for confirmation that there was no pending winding up application or any receivership or

	composition with creditors.
	(b) where the person is an individual, any adverse credit rating.
Description	The GFSC do not routinely make credit ratings enquiries.
Comments	The GFSC stated that it would refuse an applicant on resources grounds using the prudent business criteria under the Fiduciaries Law, Schedule 1, para. 5.
	Additional criteria 2.5 It is also desirable for jurisdictions to require that those persons who hold an interest in a service provider, whether legal or beneficial, should be fit and proper applying the criteria set out in paragraphs 2.1 to 2.4 above, with suitable modifications where the person is a corporate body.
Description	The GFSC considers this as essential because someone who is not fit and proper could otherwise control a licensee. The application forms for a full fiduciary license require information on the directors, partners and managers and on beneficial ownership/control. All such persons are required to submit a detailed personal questionnaire. (Fiduciaries Law, Schedule 1). The Fiduciaries Law s.14 also provides the GFSC with the power to object to transfers of control of a service provider. It. requires a person to notify the GFSC in writing of his intention to become a controller (or partner in a service provider which is a partnership). In the case of a company, a controller is someone holding at least 15 percent of a company's shares. The GFSC requires that all such persons complete a personal questionnaire detailing their experience and background. Following such notification the GFSC may require the person to furnish additional information or documents in order to enable the GFSC to decide whether or not to serve a notice of objection. The criterion used in determining whether to issue a notice of objection is whether the GFSC is satisfied that: • the person is fit and proper; • the interests of the clients of the service provider would not be threatened by that person becoming a controller; and • the minimum criteria for licensing of the service provider will continue to be met. Section 22 of the Fiduciary Law requires that anyone becoming a significant shareholder (i.e., holding between 5 percent and 15 percent) notify the GFSC within 14 days of becoming so.
Comments	
Conduct of Business	
Principle 3.	**All countries/jurisdictions should require that those providing the service of trust or company service provider exhibit evidence that their business will be or is being conducted in accordance with the proper corporate governance, customer due diligence, conduct of client business, financial soundness, and systems and controls requirements**.
	Corporate Governance 3.1 Trust and company service providers should comply with recognized standards of corporate governance in respect of both the business itself and clients' corporate vehicles, trusts and other legal entities.
Description	The application forms for a full fiduciary license require information on a number of areas regarding the strategic and operating plan of an applicant. This includes succession and disaster recovery plans, as well as plans for staff training and development. The GFSC pays close attention to the question of whether the applicant complies with the requirement for "four eyes" and considers the relative experience and ownership interests of the persons put forward as fulfilling that test. Where the GFSC is not convinced that there are "four eyes," it has refused to license an applicant until additional executive personnel are taken on at a suitable level. Where the GFSC is dissatisfied with any response or where it has decided to undertake an on-site visit, it asks additional questions, including questions covering the operation of the

	applicant. The GFSC examines procedures, controls and reporting lines as part of on-site visits with respect to fiduciary business and with respect to administered trusts and companies with particular reference to the director or trustee applying its own judgment to the issues.
Comments	There are still a number of fiduciaries operating under the "transitional provisions" of the law. These companies and individuals are fully covered by the supervisory and enforcement provisions of the legislation, but some have not yet been licensed because the GFSC is not fully satisfied that they meet all of the licensing criteria. The GFSC believes that it is making every effort to complete the process as effectively and efficiently as possible consistent with the need for decisions to be based on a detailed consideration of each individual application that must involve proper respect for due process. It has set up a Shadow Financial Services Tribunal and within the next few months, the licensing process will be substantially complete. If the transitional process is not complete within the next few months, the mission would be concerned about the risks to the reputation of the jurisdiction and would recommend in those circumstances the setting of a cut-off date for completion of the licensing process.
	3.2 Trust and company service providers should comply with the FATF Recommendations concerning money laundering and the financing of terrorism.
Description	Service providers are subject to the Bailiwick's anti-money laundering provisions contained in the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999, the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002, the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism issued under those Regulations and the Terrorism and Crime (Bailiwick of Guernsey) Law, 2002. These have been supplemented by the Position Paper on Overriding Principles for a Revised Know Your Customer Framework. Suspicious transactions must be reported to the Financial Intelligence Service (FIS) and also to the GFSC where they might cause regulatory concern, for example if the institution's systems failed to detect a relevant matter or there is a serious reputational risk to Guernsey or the institution. The application forms for a fiduciary license require a full account of the applicant's procedures for complying with the anti-money laundering requirements to which it is subject and in many cases, copies of procedures manuals are obtained and reviewed before the licensing decision is made. Noncompliance with the law or a regulation is a criminal offense. Furthermore such a failure may result in disciplinary action by the GFSC (including the revocation of a license). A breach of the Guidance Notes, whilst not a criminal offense may also be grounds for regulatory action. The GFSC has obtained and reviewed procedures for the prevention of money laundering and countering the financing of terrorism from applicants for licenses. Examination of the adequacy of those procedures and how they are followed in practice is one of the areas reviewed during on-site inspections.
Comments	See also AML/CFT assessment in this report.
	3.3 Trust and company service providers should comply with any relevant financial regulatory standards.
Description	The Fiduciaries Law s.29, gives the GFSC the authority to make rules prescribing the form in which a licensed fiduciary's accounts and the auditors reports on those accounts are to be, and the information and particulars contained in them, and the times or intervals at which they are to be drawn up and furnished.
Comments	
	3.4 Trust and company service providers should comply with all relevant domestic statutory obligations, for example the legislation governing the formation and administration of companies.
Description	On-site visits review these issues.
Comments	
	3.5 Trust and company service providers should comply with recognized standards in respect of the responsibilities of directors and trustees.

Description	The GFSC has published a Code of Practice for Company Directors under the Fiduciaries Law, s.35. The Code states that directors should understand and act in accordance with their legal duties and requires them to act in good faith and in the best interests of the company. Separate Codes of Practice have also been issued for Trust Service Providers and Corporate Service Providers.
Comments	
	Additional criteria 3.6 Trust and company service providers should have adequate internal controls that provide at least four eyes control.
Description	This is a statutory criterion for full licensees. In the case of a full fiduciary license, at least two individuals, resident in the Bailiwick and of appropriate standing and experience, shall effectively direct the business of the licensed fiduciary. (the Fiduciaries Law, schedule 1 para.). In applying this test the GFSC considers the independence of senior management and, where necessary, requires additional appointments to be made before a license is granted. As part of its on-site inspections, the GFSC reviews the institution's compliance with its legal obligations and the GFSC's Codes of Practice and the adequacy of its internal review systems. Reporting lines and business controls are also considered during on-site inspections.
Comments	
	Customer due diligence 3.7 Trust and company service providers should be required to satisfy standards equivalent to those set out in the Basel Committee's CDD Paper, published in October 2001, to the extent that the recommendations in that paper are relevant to nonbanks.
Description	Applicants and licensees must satisfy the requirements of the GFSC's Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism.
Comments	
	3.8 Customer due diligence procedures should cover the following: (a) customer identification; (b) verification of identity of customer; (c) risk profile (e.g., politically exposed persons); (d) source of wealth; (e) source of funds; and (f) ongoing monitoring.
Description	In this report, these issues are covered in the AML/CFT review. The money-laundering Guidance Notes cover these matters.
Comments	
	Conduct of client business 3.9 Trust and company service providers should be required to have systems and procedures in place for the conduct of client business covering: (a) the identification and segregation of clients' assets from the assets of the business;
Description	TSP Code of Practice para. 4 states that: TSPs should treat the interests of beneficiaries as paramount subject to their legal obligations to other persons or bodies. In particular, TSPs should: • invest, distribute or otherwise manage each trust's assets in accordance with the law and the trust deed; • manage the investment and custody of trust assets professionally and responsibly; • maintain confidentiality except where disclosure of information is required or permitted

	by an applicable law or by guidance published by the GFSC, or authorized by the person(s) to whom the duty of confidentiality is owed; • provide promptly to clients information to which they are entitled about a trust; • ensure that the funds of different trusts are kept separately from each other and from the TSP's own funds; • agree a clear fee structure in advance of taking an appointment and charge fees in accordance with that and in a fair and transparent manner; • notify clients that the TSP is licensed by the GFSC; • avoid setting up or participating in discretionary trusts where the trustees merely carry out the settler's instructions and exercise no significant discretion; and • deal in a timely manner and in the best interests of the beneficiaries with any transfer to other trustees. The CSP Code of Practice, para. 6 states that: A CSP should, through its staff: • identify and act in each client company's best interests and avoid or deal properly with any conflict of interest between clients or client companies or between itself and a client or a client company; • keep the funds of each client company separate from each other and from the CSP's own funds. The GFSC monitors compliance with these requirements during on-site visits. The GFSC states that any inadequacy of systems can be tied to the general licensing criterion in the Fiduciaries Law Schedule 1, that require adequate accounting and other records and adequate systems of control. In addition, the external auditors are required to identify any clients' assets that were not being segregated from each other or from those of the licensee and report the matter to the GFSC.
Comments	
	(b) the effective handling of clients' assets, which should include both safe custody and proper management procedures;
Description	See response to principle 3.9.a above.
Comments	
	(c) the maintenance of adequate and orderly accounting records of clients' affairs;
Description	See response to principle 3.9.a above. In addition, the Guernsey Society of Certified and Chartered Accountants' Guidance Note, with which licensees' auditors have to comply, requires them to "make preliminary assessment of control risk by reviewing client administration controls" that include client accounting.
Comments	
	(d) the maintenance of adequate client documentation (e.g. trust deeds);
Description	See response to principle 3.9.a and 3.9.c above. These are examined during on-site visits.
Comments	
	(e) the appropriate authorization and handling of all transactions and decisions by persons with the knowledge, experience and status required to effect such transactions or make the required decisions according to the nature and status of the transactions/decisions involved.
Description	This is reviewed during on-site reviews as part of client assets questions
Comments	
	Explanatory note

	Examples of the type of issue raised by paragraph (e) are set out below: • where discretion is exercised for or in relation to clients, all reasonable steps should be taken to obtain sufficient information in order to exercise that discretion or other powers in a proper manner and such discretion should only be exercised for a proper purpose; • any actual or perceived conflict of interest should be avoided or, where conflicts arise, such conflicts should be covered by disclosure, internal rules of confidentiality, rules on when or when not to act, or otherwise as appropriate; • all business (including the establishing, transferring or closing of business relationships with its customers) should be transacted in an expeditious manner. The GFSC's comments • Re adequacy of information, see principle 3.4 above; • Re conflicts of interest, the Code of Practice for CSP's requires licensees to "identify and act in each company's best interests and avoid or deal properly with any conflict of interest between clients or client companies or between itself and a client or client company (para. 6). The equivalent obligation relating to trusts can be found in para. 5 of The TSP Code; • Re transacting business in an expeditious manner. This would be covered under general competence criterion if there were unacceptable delays or under adequacy of systems if the delay arose from a failure of the licensee's systems.
	Financial soundness 3.10 Trust and company service providers should be required to: (a) maintain adequate and orderly accounting records of their business and their clients' affairs;
Description	The Fiduciary Law, Schedule 1, para. 5(6) states that in relation to both own business and clients' affairs, a person shall not be regarded as conducting his business in a prudent manner unless he maintains or, as the case may be, will maintain adequate accounting and other records of his business and adequate systems of control of his business and records. Auditors would also pick up any lack of either type of accounting records during their audit.
Comments	
	(b) maintain adequate financial resources including adequate paid up capital and adequate liquid capital to enable the business to continue and to enable clients' affairs to be managed properly for an appropriate period;
Description	The Fiduciaries Law Schedule 1, para. 5(2) states that "A person shall not be regarded as conducting his business in a prudent manner unless he maintains or, as the case may be, will maintain a capital base and insurance cover: (a) of an amount commensurate with the nature and scale of his operations; (b) of an amount and nature sufficient to safeguard the interests of his clients and any other factors appearing to the GFSC to be relevant. For trust companies the GFSC requires paid up share capital of at least £25,000 and there is a three months' expenditure test. Post-licensing the GFSC monitors capital on an annual basis through the submission of annual accounts. The GFSC believes that it is effectively able to impose whatever level of capital and resources are considered appropriate under the law."
Comments	
	(c) comply with any relevant financial regulatory standards and international accounting standards;
Description	In relation to accounting standards, the audit must be conducted in accordance with Auditing standards issued by the Auditing Practice Board and the financial statements must be prepared

	in accordance with U.K., U.S. or International Accounting Standards, unless the GFSC agrees to accept another standard. The GFSC informed the mission that so far it has not agreed to any other standard.
Comments	
	(d) maintain adequate professional indemnity insurance cover.
Description	The Fiduciaries Law, Schedule 1, para. 5, imposes a statutory requirement for all licensees to have adequate cover for their activities. It states that: A person shall not be regarded as conducting his business in a prudent manner unless he maintains or, as the case may be, will maintain a capital base and insurance cover: (a) of an amount commensurate with the nature and scale of his operations; and (b) of an amount and nature sufficient to safeguard the interests of his clients and any other factors appearing to the GFSC to be relevant. The GFSC noted that it has generally required full licensees to have cover of greater of £1million and three times turnover, and personal licensees £1million or, where small-scale activities only, £500,000.
Comment	
	Systems and procedures 3.11 Trust and company service providers should be required to: (a) have in place effective compliance functions which include the designation or appointment of an appropriately skilled and experienced person as compliance officer;
Description	There is at present no requirement in the law for such an appointment. The GFSC noted, however, that in practice most Money Laundering Reporting Officers, a post which must exist, act as compliance officer. In addition, compliance with regulatory and other legal requirements is the responsibility of the Board and the designation of an individual at director or other level would not affect the current situation. In summary, the functions are being covered under current legislation.
Comments	
	(b) have in place effective reporting requirements which include the designation or appointment of an appropriately skilled and experienced person as an anti-money laundering reporting officer
Description	The Criminal Justice (Proceeds of Crime) Regulations, 2002, require the appointment of MLRO. While there is no explicit requirement on experience, the GFSC noted that it would comment if it thought that a MLRO was not sufficiently experienced for the job.
Comments	
	(c) have in place an effective complaints handling system which should include the maintenance of a record of complaints and the actions taken to resolve them;
Description	The Code of Practice requires licensees to record, investigate and, as appropriate, act on complaints. The Code of Practice for TSPs states that: TSPs should, through their staff, record; investigate; and, as appropriate, act on complaints (para. 5). The Code of Practice for CSP, similarly states that: CSP's should, through their staff, record; investigate; and, as appropriate, act on complaints (para. 6). The GFSC noted that through on-site visits, it reviews these records.
Comments	

	(d) maintain adequate, orderly and up to date records of all business transactions and instructions at an appropriate location in the jurisdiction, including: • accounting records of the business; • accounting records of clients' affairs; • records of the internal organization and risk management systems; • client documentation (e.g. client requirements).
Description	With respect to accounting records—See the response to Principle 3.10(a) above. The business records would include records of meetings and other communications with settlors/beneficiaries/ beneficial owners. The GFSC noted that it expects to see such communications on files during visits and has had occasion during visits to report on inadequate records.
Comments	
	3.12 Trust and company service providers should be required to retain records for a period appropriate to the business and in line with relevant legal obligations.
Description	The Criminal Justice (Proceeds of Crime) Regulations, 2002 imposes a six-year period. During on-site inspections the GFSC questions licensees about these matters.
Comment	
	3.13 Trust and company service providers should be required to maintain a manual of appropriate policies and procedures; including business take on procedures, and documenting systems and procedures intended to safeguard the business and clients' assets and ensure that only authorized and proper transactions are undertaken.
Description	The Fiduciaries Law, Schedule 1, para. 5(6) requires the licensee to maintain adequate accounting and other records of his business and adequate systems of control of his business and records. The GFSC noted that it reviews procedures before visits and compliance with them during on-site visits.
Comments	
	3.14 Trust and company service providers should be required to ensure: (a) that they have an adequate span of control with a sufficient number of appropriately skilled and experienced persons able to exercise independent judgment; and
Description	The Fiduciaries Law, Schedule 1, para. 4, states that at least two individuals of appropriate standing and experience shall effectively direct the business of the licensed fiduciary.
Comments	
	(b) that those engaged in the business have a minimum relevant experience and qualifications.
Description	In addition to the requirement under 3.14.a, the GFSC must be satisfied that the directors and managers are sufficiently experienced and qualified (the Fiduciaries Law, Schedule 1, paras. 3(2)(a) and (b). The GFSC noted that the levels of experience are factored into its risk-profiling for post licensing visits.
Comments	
	Explanatory Note Exceptions may apply to this criterion in respect of sole practitioners where, for example, an individual trustee function is controlled by the court.

	3.15 Trust and company service providers should be required to ensure that professional development requirements are satisfactorily met.
Description	The GFSC believes that this is the responsibility of professional and industry associations.
Comments	
	3.16 Trust and company service providers should be required to ensure that their officers and staff have a full understanding of the duties arising under the laws relevant to the affairs of client corporate vehicles, trust and other legal entities for which they are acting in the jurisdictions in which they are carrying on business and in which the assets being handled/managed are held.
Description	See the response to Principle 3.14 above. In addition, the Fiduciaries Law, para. 3(2) requires the GFSC to take account of the individual's knowledge and understanding of the legal and professional obligations to be assumed or undertaken.
Comments	
Holding and Sharing of Information	
Principle 4.	**All countries/jurisdictions should ensure that there is proper provision for the holding, having access to and sharing of information.**
	4.1 Information on the ultimate beneficial owner and/or controllers of corporate vehicles, and the trustees, settler, protector/beneficiaries of trusts should be known to the service provider.
Description	The money laundering Guidance Notes require licensees to keep this information.
Comments	
	4.2 Any changes of client control/ownership should be promptly monitored, particularly where a service provider is administering a corporate vehicle in the form of a "shelf" company or where bearer shares or nominee share holdings are involved.
Description	The Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism, para. 39 would require the service provider to verify the identity of a new beneficial owner.
Comments	
	4.3 There should be an adequate, effective and appropriate mechanism in place for information to be made available to all the relevant authorities.
Description	The Fiduciaries Law s.23 enables the GFSC to obtain information and documents. The Fiduciary Law s.43 sets out the confidentiality provisions relating to information within the GFSC's possession. It states that: • no person who under or for the purposes of this Law receives information relating to the business or other affairs of any person; • no person who obtains any such information directly or indirectly from a person who has so received it; shall disclose the information without the consent of the person to whom it relates and (if different) the person from whom it was so obtained; and • a person who discloses information in contravention of this section is guilty of an offense. The Fiduciary Law s.44 provides gateways for onward transmission to other regulators, investigating and prosecuting authorities (see Principle 4.4 below).
Comments	
	4.4 There should be no barrier to the appropriate flow of information.
Description	There is no particular barrier, for example, no requirement for the Attorney General's consent before disclosure to the GFSC. (There is in section 44(1) a requirement for AG's consent in very limited circumstances where information has gone from the GFSC to the Police and the Police want to disclose for investigation and prosecution outside Guernsey.)

	The Fiduciary Law s.44 specifies the cases where disclosure is permitted. These include: • information which at the time of disclosure is or has already been made available to the public from other sources; • information in the form of a summary or collection of information so framed as not to enable information relating to any particular person to be ascertained from it; • the disclosure of information for the purpose of enabling or assisting the GFSC to discharge its functions conferred by or under this Law; • information by the GFSC to the auditor of a licensed fiduciary or former licensed fiduciary if it appears to the GFSC that the disclosure would enable or assist the GFSC to discharge its functions conferred by or under this Law or would otherwise be in the interest of the public; • where, in order to enable or assist it to discharge its functions conferred by or under the Law, the GFSC considers it necessary to seek advice from a qualified person on any matter of law, accountancy or valuation or any other matter requiring the exercise of professional skill, the disclosure by the GFSC to that person of such information as appears to the GFSC to be necessary to ensure that he is properly informed as to the matters on which his advice is sought; • information in the interests of clients or the public interest; • information for the purpose of enabling or assisting a relevant supervisory authority in a place outside the Bailiwick to exercise its functions; • the disclosure of information for the purposes of the investigation, prevention or detection of crime or with a view to the instigation of or otherwise for the purposes of any criminal proceedings; • the disclosure of information to a person or body responsible for a scheme for compensating clients or investors (whether in the Bailiwick or elsewhere): (i) if it appears to the GFSC that the disclosure would enable or assist the recipient of the information or the GFSC to discharge its functions; and (ii) if the recipient has given to the GFSC a written undertaking that the information will not be further disclosed without the prior consent of the GFSC.
Comments	
	4.5 Information regarding the clients of the service provider should be kept in the jurisdiction in which the service provider is located.
Description	The Criminal Justice (Proceeds of Crime) Regulations, 2002 (Regulation 5) require licensees to retain customer documents and customer verification documents "in a manner that makes their retrieval readily practicable." In addition, the requirement under the Fiduciary Law, Schedule 1, para. 5(6), to keep adequate records and have adequate systems of control is relevant.
Comments	
	4.6 There should be no legal barrier to the flow of information or documentation necessary for the recipient of business from a provider who is an acceptable introducer to satisfy itself that adequate customer due diligence has been undertaken in accordance with the arrangements set out in the Basel customer due diligence paper.
Description	The GFSC noted that it does not prevent financial services businesses in the Bailiwick from supplying verification documents to other jurisdictions.
Comments	

Audit and Compliance Reviews	
Principle 5.	**All countries/jurisdictions should require proper provision to be made for audits and compliance reviews.**
	5.1 External auditors with relevant experience and appropriate track record should be appointed to carry out a full audit of the trust and company service providers' businesses in accordance with international standards.

Description	The Regulation of Fiduciaries (Accounts) Rules, 2001, para. 10.1, requires:
	• a person shall provide to the GFSC financial statements for each accounting period at any time during which it held a full fiduciary license;
	• the statements shall be provided to the GFSC within four months of the end of the accounting period to which they relate;
	• the financial statements shall be accompanied by:
	  • an auditor's report on the financial statements;
	  • any report prepared by an internal or external auditor which is available to the licensed fiduciary and addresses a relevant matter; and
	  • brief details of any report prepared by an accountant or consultant, which is available to the licensed, fiduciary and addresses a relevant matter (relevant matter means a breakdown or material weakness in a licensed fiduciary's internal control procedures);.
	• a licensed fiduciary shall forthwith provide to the GFSC a copy of any management letter received from his external auditor.
	The Fiduciary Law s.58 defines an auditor as one approved by the GFSC. The GFSC only approves auditors who confirm that they will perform audits of fiduciary licensees in accordance with the GSCCA Guidance Notes on the audit of fiduciaries. The Guidance Notes require the auditor to review client files and to form a view on risks facing the licensee.
	In addition, the Companies Law s.63(1) states that:
	"A person is not qualified for appointment as an auditor unless he is (a) a member of (i) the Institute of Chartered Accountants in England and Wales, of Scotland or in Ireland; (ii) the Chartered Association of certified Accountants; or (b) for the time being authorized by the Committee to audit the accounts of companies as having similar qualifications obtained outside the United Kingdom."
	It goes on to state that:
	"The audit must be conducted in accordance with Auditing Standards issued by the Auditing Practices Board and the financial statements must be prepared in accordance with U.K., U.S., or International Accounting standards, unless the GFSC agrees to a different standard."

Comments	
	5.2 External auditors should have the statutory authority and protection necessary to report to the competent authorities any breaches of relevant legislation or other material concerns.
Description	Auditors are protected by Section 31, which provides that communications of information relevant to the GFSC's functions do not constitute a breach of any duty by the auditor. This is the case whether or not the communication is in response to a request from the GFSC. The Fiduciaries Law s.31 states that: "No duty to which an auditor of a licensed fiduciary is subject is contravened by reason of his communicating in good faith to the GFSC, whether or not in response to a request made by it, any information or opinion on a matter relevant to any function of the

	GFSC. The section applies to any matter of which he becomes aware in his capacity as auditor and which relates to the business or affairs of the licensed fiduciary." The protection also applies to the auditor of a former licensed fiduciary as it applies in relation to the auditor of a licensed fiduciary.
Comments	
	5.3 Adequate procedures should be implemented to ensure that regular independent reviews are conducted of compliance with the Statement.
Description	The GFSC reviews compliance during on-site visits.
Comments	
Cessation of Business and Misleading Statements	
Principle 6.	**All countries/jurisdictions should have proper provisions for the ceasing of business and for prohibiting misleading statements.**
	6.1 The interests of customer/clients should be able to be adequately safeguarded when the service provider is no longer able to carry on the business for any reason.
Description	This is currently not covered. However, legislation introducing the Office of Public Trustee has been agreed by Guernsey, Alderney, and Sark legislatures and sent to the Privy Council in the week of November 4, 2002 for the Royal Sanction.
Comments	.
	6.2 All countries/jurisdictions should ensure that trust and company service providers do not provide false or misleading information (including advertisements
Description	The Fiduciary Law s.20 gives the GFSC the power to make regulations on fiduciary advertisements. It states that the regulations that have been made (The Regulation of Fiduciaries (Fiduciary Advertisements and Annual Returns) Regulations, 2001) prohibit personal fiduciary licensees from advertising but do not impinge on advertising by holders of full licenses. However, even without such regulations, the GFSC can under Section 20(7) give a direction prohibiting a fiduciary advertisement or requiring its modification. The GFSC may make regulations in respect of the issue, form, and content of fiduciary advertisements and may prohibit the issue of advertisements of any description (whether by reference to their contents, to the persons by whom they are issued or otherwise); make provision as to the matters which must or which may not be included in fiduciary advertisements; provide for exemptions from any prohibition or requirement imposed by the regulations. A person who issues or causes to be issued, in or from within the Bailiwick or (in the case of a Bailiwick company) in or from within any place whatsoever, an advertisement the issue of which is prohibited by regulations under this section or which otherwise contravenes any provision of such regulations is guilty of an offense. In addition to the annual return, the service provider is required, pursuant to section 46(2), to provide the GFSC with any information in its possession that is relevant to the GFSC in the exercise of its powers. Failure to do so is an offense. In furtherance of this, the Codes of Practice for Trust Service Providers and Corporate Service Providers set out the events about which the GFSC would expect to be notified. These include the commencement of proceedings against the service provider in any country and serious or prolonged breakdown of the service provider's administrative systems. The guidance that accompanies the Code confirms that the list in the Code is not exhaustive but rather indicative of the type of events of which the GFSC would expect to be notified. The GFSC reviews whether on-site inspections reveal that any matter, such as a complaint, should have been but has not been notified to the GFSC. Section above sets out the other requirements in the Fiduciary Law for notification to or approval by the GFSC.
Comments	

Authorities' Response to the Review against the OGBS Statement of Best Practice for Trust and Company Service Providers.

116. The authorities welcome the IMF's assessment and confirmation that the Bailiwick of Guernsey's standards of trust and company service provider regulation are fully consistent with the OGBS Statement of Best Practice for Trust and Company Service Providers.