Guernsey Financial Services Commission

# ANNUAL REPORT AND FINANCIAL STATEMENTS

For the year ended 31 December 2012

Guernsey Financial Services Commission



**Appendix**

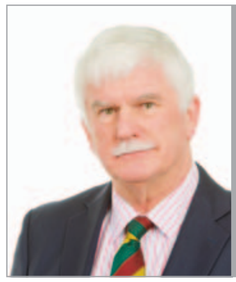


This report, including the financial statements as required by section 18 of the Financial Services Commission (Bailiwick of Guernsey) Law, 1987, as amended (the Commission Law), is made in pursuance of section 6 of the Commission Law to the States Policy Council and submitted by the Chief Minister for consideration by the States of Guernsey.

*Note: Throughout this report the Guernsey Financial Services Commission is referred to as "the Commission". The Chairman and other members are referred to collectively as "the Commissioners".*

# STRUCTURE OF THE COMMISSION

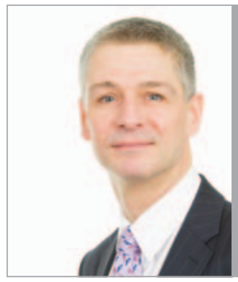
COMMISSIONERS



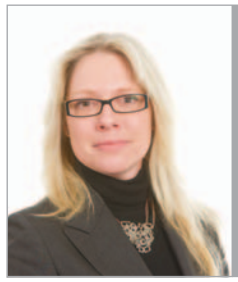
**Nik van Leuven QC**
Director General

DIRECTOR GENERAL'S DIVISION

**Richard Walker**
Director
Policy and International Affairs



**Kevin Bown**
Deputy Director
Intelligence Services



**Samantha Sheen**
Legal Counsel

**Fionnuala Carvill**
Commission Secretary

**Philip Marr**
Director
Banking Division

**Philip Nicol-Gent**
Director
Fiduciary Services Division

**Neville Johnson**
Chief Operating Officer

**Dr Jeremy Quick**
Director
Insurance Division

**Carl Rosumek**
Director
Investment Business Division

**Tim Loveridge**
Chief Transformation Officer

# COMMISSIONERS

**Drs. Cees Schrauwers**
**Chairman of the Commission**

Drs. Schrauwers [Cees] is a Dutch citizen and has more than 35 years' financial services experience. He has served as Managing Director of Aviva International, CGU Insurance and Commercial Union covering both the general insurance and life sectors. He was instrumental in the mergers with General Accident and Norwich Union which resulted in the creation of Aviva plc. Following the mergers he was appointed Managing Director of Aviva International, gaining valuable experience in dealing with regulators across the globe, including North America. Prior to this, he was a Partner with Coopers & Lybrand in charge of insurance consultancy. In the past he has served as Chairman of Drive Assist Holdings Limited, Senior Non-executive Director of Brit Insurance Holdings Plc. and Brit Syndicates Limited, Non-Executive Director of Canopius Holdings UK Limited and Canopius Managing Agents Limited and as a Director of Munich Re (UK) Plc. He is currently Chairman and Commissioner of the Guernsey Financial Services Commission. Cees was appointed as a Commissioner in 2008 and Chairman in 2012 and is the Senior Non-Executive Director of Record Plc since November 2007. In May 2012 he was appointed as an Independent Director at Scottish Widows Group. He was educated at the Vrije Universiteit Amsterdam and Nautical College Den Helder. He lives with his wife near London.

**Susie Farnon FCA**
**Vice-Chairman of the Commission**

Susie Farnon was appointed as a Commissioner in February 2006. She was a Banking and Finance Partner with KPMG Channel Islands from 1990 until 2001. She has served as President of the Guernsey Society of Chartered and Certified Accountants and as a member of the Guernsey Audit Commission and the Guernsey Public Accounts Committee. She is also director of a number of private and listed companies.

**Richard Hobbs MCIPD**
**Commissioner**

Richard Hobbs was appointed as a Commissioner in January 2012. His first career was in the UK Civil Service where he concentrated on a variety of consumer protection and European issues. Latterly, he was a director of the Department of Trade and Industry's Insurance Division where he was responsible for overall supervision of the Lloyd's insurance market during its reconstruction in the mid-1990s. He has been Head of Life and Pensions at the Association of British Insurers, and for the past decade has been a consultant advising a wide range of clients in financial services on regulatory, risk and governance issues. He is also chairman of Faber Global Limited, a wholesale insurance broker, and a non-executive director of Barbican Managing Agency Limited, a Lloyd's managing agent.

**Alex Rodger MCIBS**
**Commissioner**

Alex Rodger was appointed as a Commissioner in February 2008. He spent over 40 years with the Royal Bank of Scotland ("RBS") Group. Prior to moving to Guernsey in 1989 as Island Director, he occupied senior posts in relationship management and credit control in London and New York. He was executive director of RBS International from its formation in 1996 and was appointed Managing Director of RBS International Securities Services Group in April 2002. Later that year his responsibilities were increased to that of Managing Director of RBS International Corporate Banking Division with responsibility for corporate banking operations in each of Jersey, Guernsey, the Isle of Man and Gibraltar. He was also Chairman of RBS International Employees Pension Trust. Alex Rodger is the non-executive Chairman of advocates Collas Crill.

**Lord Flight MA (Cantab) MBA, FRSA**
**Commissioner**

Howard Flight was appointed as a Commissioner in 2005. He was the Conservative Member of Parliament for Arundel and South Downs from 1997 to 2005, during which time he was Shadow, Economic Secretary, Paymaster General and Chief Secretary to the Treasury. From 1999 to 2004 he had Shadow Treasury responsibilities for the Finance Acts, the financial services industry, financial regulations and pensions. He has worked for over 40 years in the financial services industry, starting his career at Rothschilds. In the second half of the 1970s he worked for HSBC's merchant bank in Hong Kong and India. In 1979 he joined Guinness Mahon and established what became Guinness Flight Global Asset Management, of which he was joint Managing Director until it was acquired by Investec in 1998. He formed, and is Chairman of, Flight & Partners, which is the manager of the Flight & Partners Recovery Fund, and is currently a director of Investec Asset Management Limited, Metrobank plc, Aurora Investment Trust plc and a number of other companies and investment funds.

**Bob Moore**
**Commissioner**

Bob Moore was appointed as a Commissioner in February 2012. He has spent over 30 years in the financial services industry in Guernsey and internationally. From 1979 to 1997, he held positions in international banking and international private banking with the Lloyds Bank/Lloyds TSB Group in South America, the United States, the UK and Luxembourg. These included responsibility for Lloyds' international private banking operations in New York and in Luxembourg. From 1997 to 2011, he was jurisdictional Managing Director with responsibility for the Butterfield Group's operations in Guernsey, including banking, investment management, custody and fiduciary services. In June 2011, he was appointed to the position of Executive Vice President and Head of Group Trust for the Butterfield Group. He has also been a director of a number of other Guernsey banks and investment funds.

# CHAIRMAN'S STATEMENT

In last year's report I projected a somewhat gloomy outlook for the years to come with little or no growth in the European economies and a continued flow of newly designed regulation attempting to address and to prevent the past mistakes made in the financial world.

New rules emanating from the UK, USA and the European Union are putting a significant burden on the licensees and the Commission, even in those cases where these rules would not directly apply to the Bailiwick. In order to deal with this ever increasing burden, the Commission will need to improve its effectiveness and needs to develop into a leaner organisation, shifting the emphasis from administering to assessing risk and applying the regulations relevant to Guernsey and its reputation.

Commissioners and management started the implementation of the Independent Evaluation Review ("IER") in 2012 and you will find greater detail of these developments in the Director General's report. The main aim for the Commission remains to protect the reputation of Guernsey whilst accepting that, in order to generate profit, companies will need to have a certain, but controlled, level of risk.

The IER called for government action in clarifying a Financial Services Strategy for the Island and I am pleased that this process has now started with considerable input from government, licensees, the Commission and civil servants. It is my hope and expectation that we will have an agreed Financial Services Strategy for Guernsey in time for the 2014 Planning Round.

A second recommendation was seeking clarification of the governance of the Commission and its relations with the States, Ministers and the Fiscal and Economic Policy Group ("FEPG"). A first draft of proposals to be put for consultation has been issued in May of this year.

A third point to be addressed is the role of Commission in a quasi-legal position as and when it aims to enforce conduct and its stated regulation.

The requirements for the Commissioners to be independent and impartial when exercising their enforcement functions, particularly by imposing sanctions, currently restricts Commissioners from exercising proper governance over the enforcement processes for which they are responsible, which is undesirable when discharging Commissioners' obligations. I am pleased that Commerce and Employment is currently considering proposals to put before the States which will address the enforcement conundrum.

The Commission had made good progress with its internal reorganisation, including the launch of a centralised Anti-Money Laundering and Countering the Financing of Terrorism Division ("AML/CFT Division") and Authorisations Unit, which will assist in achieving a consistent level of review whilst meeting our efficiency targets.

The Commission has been investigating tools which will assist management with the delivery of risk-based regulation. This should result in greater consistency and should reduce the burden for those licensees who could be considered posing only comparatively minor risk.

The Commission strives to be a modern regulator requiring that transmission of data between the Commission and the licensees should take place by electronic means. It is essential that the Commission works closely with representatives of licensees as decisions taken will have inevitable 'knock on' effects on the IT infrastructure and capabilities of licensees. It is the intention that this project will be financed from the Commission's internal resources, with electronic personal questionnaires ("PQs") being delivered by the end of 2013.

The Commission was formed 25 years ago as one of the earliest unitary regulators. It is inevitable that many laws and statutes, whilst having served us well, are now showing their age. The Commission has embarked upon a review of Guernsey's financial services Laws, in conjunction with St James' Chambers, with the aim of consolidating and simplifying them. This should result in a reduction in volume, by cutting out overlaps. Again we will work closely with licensees and seek their input in the modernisation of the Bailiwick's regulatory framework.

In my first year as Chairman, I have made it my task to meet with as many industry leaders as was practicable and I will continue to do so in 2013. These meetings were invariably frank and useful. The subject of licensee fees continues to exercise us all. The Commission will in 2013 undertake a review of its various fees, in particular those charged for one-off product proposals. It seems reasonable that those who generate most of the work carry most of the burden. On existing economic and regulatory assumptions the Commission will not be seeking a fee increase of, in total, more than 2% each year over the next three years. There remains a high level of activity induced by outside demands and the need for the Commission to be more efficient and, where possible, transparent.

Last year I listed the principles that govern the Commission. This year I want to explain how the Commission and all who work in it interpret these on a daily basis.

In summary, we intend to exercise 'good and effective' regulation. By this we mean that we will work to ensure that the Commission delivers high-quality prudential, financial crime and conduct regulation within the Bailiwick of Guernsey. We will be mindful of the need to protect the Bailiwick's reputation and competitive position. In all that we do, we will have regard to the needs of the Bailiwick, its residents and of international regulatory expectations. We recognise the need to use finite resources efficiently and we will be risk-based in our supervisory, enforcement and policy creation activity. We will seek to form judgements as to the risks which the firms we regulate present to the Bailiwick and to mitigate risks which we reasonably regard as unacceptable whilst helping to facilitate innovation in the financial sector.

In the summer of 2012, Nik van Leuven, our Director General, indicated that he wished to retire from his role. This sparked a search for a successor who would be able to take the Commission and the Bailiwick forward in an increasingly demanding environment. Following a widespread and intensive search, the Commission appointed William Mason, who joined us in the second quarter of 2013. William joined us from the Central Bank of Ireland where he was Head of Risk, following a career in the UK Cabinet Office and the Financial Services Authority.

I greatly welcome William's decision to come and live on the Island with his family and give leadership and energy to Guernsey's financial services industry.

Nik has played a pivotal role in starting the IER, an important step in the professionalism of the Commission, and I thank him for that, wishing him a well-earned and happy retirement.

The Commission continues an active dialogue with the Policy Council and the Commerce and Employment Department. The Commission continues to meet periodically with the FEPG at both Commissioner and Executive level.

As I already expressed, the effort required from the Commission is substantial and I would like to thank the staff and the Directors of the Commission for their unrelenting endeavour and thank my fellow Commissioners, who have seen their workload increase substantially over the last couple of years. We also expect to appoint an additional Commissioner with a legal background in the second quarter. This brings the Commission close to its full strength and will allow us to deal effectively with our tasks over the next couple of years.

Cees Schrauwers, Chairman

# DIRECTOR GENERAL'S STATEMENT

Throughout 2012 the Commission continued the transformative process which I mentioned in last year's Annual Report and Financial Statements. It is still undergoing comprehensive structural, organisational and operational changes implementing the recommendations of the Independent Evaluation Review ("IER") conducted by Ernst & Young LLP in 2011. Much of the detail of this will be amongst the various sectoral contributions, but they have a common consequence. The ordinary business of the Commission has occasionally, but necessarily, yielded to the exigencies of these changes, yet in all this I have been heartened by the enthusiasm with which our staff, having recognised the need to progress, have embraced the substantive and incidental results. Also, the Commission is now far better equipped to address change management and deploy project methodology, to deal not only with the IER's outcomes but also with the future development of the Commission, including their adaptation to aspects of the Commission's supervisory functions, particularly significant enforcement cases. But it is reasonable to enquire: will the ends justify the means; or, put another way, will it all have been worth it? Prediction of costs savings as a result of improved methods and techniques is fraught with challenge.

The consequences of the global financial crisis continue to bear significantly upon Guernsey's financial services sector. Businesses are much more cost-conscious, and a number have either closed or taken steps to downsize. Those who retire are not being replaced, and redundancies have been announced by a number of the more significant operators. Conventional business flows are less rewarding, and new business is harder to win. Global competition is intense, and all this at a time when smaller international financial centres are coming under yet more scrutiny and criticism from their weightier neighbours or competitors.

The Commission faces many challenges. Some reflect the relentless march of regulation; others will arise as Guernsey's place in the financial services world moves to accommodate new business opportunities as conventional business lines wither or disappear. For much of this we will have to devise effective regulation and implement appropriate supervision of such business, particularly that conducted by and through the internet which is not infrequently targeted at individual investors of typically retail characteristics, and who are ordinarily excluded from opportunities available to those more fortunately placed. The Commission, in full cooperation with government and industry, will extend the reach of financial services education and information for the man in the street. The internet will eventually come to reach all the investing community hitherto without access, which poses threats because of its possibilities for misconduct, including misselling.

Guernsey businesses are actively developing new opportunities and markets – both service and product-based. And here lies a challenge for the Commission, whose regulatory regimes were devised with conventional business in mind, whereas the internet as a business tool has involved a number of propositions being put to the Commission for which the present regimes are unsuited. It is a fact of life that respectable and responsible financial services businesses want to be regulated. They also want to be in Guernsey because it is recognised as being responsive and accommodative, but without compromising on regulatory quality. Guernsey's government recognises the need for greater governmental involvement in business development, and is currently working with the Commission and industry to devise a financial services strategy. At a more practical level, the Commission relies upon government to address the drafting of legislation and regulation in those new areas for which no, or inappropriate, provision presently subsists. Regulators are invariably resented, and often misunderstood. If regulation suitable for new business propositions does not exist it is not government but the regulator who will get the blame for its absence or inadequacies. If Guernsey's reputation is to be maintained, sufficient resources must be made available to ensure that it is able to deal with new business, including particularly its regulation.

During the year, notable developments have included the establishment and immediately effective operation of the Anti-Money Laundering and Countering the Financing of Terrorism Division ("AML/CFT Division"); the implementation of the Authorisations Unit, and these besides continuing work on improving data management. These three projects usefully illustrate the Commission's new approach achieved by centralising functions. Presently, supervisory decisions consequent upon their work remain with the regulatory Divisions, but in time certain decisions will come to be taken centrally. Mention will be made elsewhere of particular aspects of these centralised functions. The AML/CFT Division provides a platform from which the Commission will better be able to develop – as it will be required to do – its role in relation to financial crime. This is not just the Commission arbitrarily extending its functions: international expectations and requirements, reflected in and by our international assessments, enjoin the Commission to address and resource the detection, prevention and reporting of financial crime. Criminals require the financial system and its businesses to transfer or disguise the proceeds of crime, besides their opportunities for fraud and criminality. This simple fact puts the Commission at the heart of AML/CFT measures, and financial crime in general. Maintenance of Guernsey's reputation is crucially dependent upon effective and efficient insular action and international co-operation.

Recently there has been a marked shift amongst the developed economies of attitudes towards tax evasion and avoidance, driven not only by governmental need to recoup lost or foregone revenues in times of economic malaise, but also a wider-spread perception of the inequities in tax burdens where the wealthy – individuals or corporate – use financial centres to reduce or shift tax burdens in a way which is denied the man or business in the street, or at least which is impracticable for them. The hardening perception *tout court* to the opportunities and facilities which financial centres are claimed to provide or facilitate makes jurisdictions such as Guernsey especially vulnerable to criticism, let alone countermeasure. I do not say whether this is fair or not; merely that it is a fact.

The Commission has not hitherto been much involved with fiscal issues unless they have carried a financial crime/money laundering component. The Commission is not a revenue authority, nor does it have a mandate to act in aid of government – whether in Guernsey or elsewhere – in direct or indirect assistance of revenue claims. The States have consistently recognised the need for cooperation and transparency, but the Commission does have a function to supervise financial services' business so as to protect Guernsey's reputation and will do so.

Perhaps the most challenging, and certainly the most demanding, internal project being undertaken by the Commission is the transformation programme known as Sentinel. This is about equipping the Commission to undertake high-quality and proportionate risk-based supervision. It will also provide the tools necessary to communicate electronically between us and our licensees. The various aspects of Sentinel include: implementing a fully functioning on-line personal questionnaires/personal declarations ("PQ/PD") system; developing an intranet; and – most excitingly – developing and implementing an IT system transporting the Commission to risk-based supervision, as is the developing prudential practice almost everywhere. Sentinel will not come cheap, but the Commission is determined that the benefits should not be overwhelmed by costs. Sentinel is being structured in such a way as to enable the Commission to pause, modify or terminate at appropriate stages over its lifetime, currently anticipated at four years.

Those benefits include: the proper positioning and resourcing of the Commission to cope with the inevitable expectations of our regulatory and supervisory techniques; the up-skilling of our staff; the directing of our efforts towards those businesses and activities which pose greater risk; and, concomitantly, more effective and efficient use of the Commission's resources.

I now briefly turn to enforcement. During 2012 the Commission has been actively engaged in investigating and pursuing some

# Director General's Statement *(continued)*

potentially significant enforcement cases, all of which have been extremely demanding in terms of staff resources. By its nature, enforcement is unpredictable as to occurrence, timing and consequence; the only assumption that can be made with confidence is that the Commission will inevitably be required to investigate breaches of the regulatory regimes for which it is responsible, with the attendant possibilities of sanctions and legal proceedings. What cannot be predetermined precisely is how any case will develop. The application of project methodology to more serious cases will undoubtedly assist in their effective and efficient disposal, but there is always an element of the unexpected. The Commission during 2013 will establish an Enforcement Division to assume the conduct of more serious cases to ensure their more effective and efficient handling, particularly to make them less vulnerable to legal challenge. For all the serious cases mentioned above, external lawyers were necessarily engaged. It is anticipated that the new Division will reduce our reliance on external lawyers.

For some while, the States and the Commission have recognised that the statutory framework for the governance of the Commission set out in the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended, needs to be reviewed and modified. This predates the financial crisis, but has been delayed on account of its consequences, including the reconsideration everywhere of regulatory precepts and practices. The IER made a number of recommendations in this area, and the Commerce and Employment Department has now issued a discussion paper. The Commission will participate vigorously in the discussions to secure the right outcomes. It is for the States to set the Commission's objectives, and it is for the Commission to deliver those objectives without interference. In this, the work in developing a financial services strategy as a collaborative effort is to be welcomed.

Here lurks another sensitive area. Advanced economies recognise that government should not undertake financial services regulation. The business of government is not about the practice of regulation, but it does include establishing the regulator's objectives and prescribing its functions. The operational independence of the regulator is of paramount consideration. Of course it may be hard for a community such as Guernsey's to accommodate that independence readily but it has to be done, particularly so in circumstances where regulation is so crucial in maintaining international perceptions besides qualitative actualities.

Threat and opportunity are elusive, and not necessarily contradictory, regulatory concepts. It is said that the great expansion of financial services regulation, driven particularly by the crises of the advanced economies and especially of the EU, provides Guernsey with opportunities. I doubt this is necessarily so, although there may be circumstances in which, in the result, Guernsey may benefit. But just as fiscal arbitrage is considered increasingly unacceptable, regulatory arbitrage will become ever more subject to the attentions of those governments and authorities whose own businesses and people will suffer from the exploitation of regulatory slackening elsewhere. From a regulatory perspective, the Commission cannot be seen as the means by which regulatory arbitrage is delivered. But adherence to international standards does not enjoin under-achievement. Complaints of 'gold-plating' are as unhelpful as they are pejorative. It is true that the Commission scored highly in its AML/CFT assessments by the International Monetary Fund against Financial Action Task Force standards, but for a financial services jurisdiction this must be right. Lower standards of regulation should not be encouraged. That way lies a race towards the bottom, to the eventual loss of the 'quality' brand which presently attaches to Guernsey's financial services sector.

This will be my last Statement before retirement. Throughout my tenure of office as Director General I have endeavoured to speak plainly about the proper ambitions for the Commission. What I have said has not always been well received or properly understood, but uncomfortable messages should not be diluted to please the listener. It is for others to judge how I have left the Commission, but it is certainly different, and better positioned both in attitudes and resources, to confront the challenges of the future. I have to thank the Commissioners for their advice, patience and support throughout. I welcome my successor, William Mason, into office confident that the Commission will be wisely, energetically and decisively led. But above all, I thank the staff of the Commission, whose forbearance, commitment and professionalism during the transformation to which I have referred have been exemplary. I am proud of all of them, and so should be the community.

Nik van Leuven QC, Director General

# BANKING DIVISION

## The Market

2012 was another difficult year for banks. The historically low interest rate environment continued as the recovery from economic recession, at least in Europe and North America, remained faltering. Banks' reactions to supervisors' requirements to rebuild capital bases were in many cases to contract balance sheets and this global deleveraging may have reinforced the weak economic recovery. Interbank lending remained at minimal levels. Ironically, the principal bright spot seemed to be a reduction of uncertainty in the Eurozone countries in 2012 and a more widespread belief that the Eurozone was not going to break up. By early 2013 strains re-emerged in the Eurozone as a tougher bailout methodology was proposed by the European Union ("EU") and International Monetary Fund ("IMF") for the bailout of Cyprus. A solution was finally agreed in late March 2013 to resolve and restructure the Cyprus banking sector but it required the imposition of capital controls in Cyprus to make it effective.

## International Developments

Global banks began the process of implementing the early stages of the Basel III proposals although, given the economic uncertainties, accessing new sources of capital proved very difficult. The most challenging question remains that of how to address the "too big to fail" issue and how to remove the notion that an implicit guarantee exists such that government and taxpayer-funded support would be available to prevent major banks from failing. Whilst most major banks operate internationally and are active in cross-border business bank resolution, proposals are invariably national in nature. This makes the issue one of the most fundamentally difficult to grapple with and so the most challenging work currently being undertaken by banking supervisors is on bank resolution and recovery regimes. In the UK the recommendations of the Independent Commission on Banking were adopted by the UK government and translated into a White Paper entitled "Sound banking: delivering reform". The UK proposals to "ring-fence" retail banks and isolate those "utility" elements from the riskier investment banking parts of UK clearing banks have been the basis for most recent thinking on the future shape of the banking industry. Along with Jersey and the Isle of Man we have been engaging with HM Treasury in order to endeavour to ensure that the Crown Dependencies participate in any restructuring of the UK retail banking industry as the UK clearing banks are fundamental to the functioning of the local economies in the Crown Dependencies.

Elsewhere the Basel Committee on Banking Supervision published its revised Core Principles against which, as a jurisdiction, we would be assessed for compliance with international regulatory standards. A new Corporate Governance core principle has been added but the main thrust of the revision has been to sharpen existing core principles to reflect experience in the 2008 banking crisis and to focus on their implementation and relevance to financial stability.

## Supervision

Our supervision of licensed banks evolved to meet the needs of the post-crisis world. We continued to use our principal supervisory tools of Internal Capital Adequacy Assessment Process ("ICAAP") and Supervisory Review and Evaluation Process ("SREP") reviews of subsidiary banks but re-instated our on-site credit reviews which were put on hold during the banking crisis period. These informed us about the state of credit quality and credit risk appetite at several active lending banks. Branch prudential meetings restarted in 2011, and were continued with a particular emphasis on UK clearing bank branches with a view to being better informed about the activities of those banks most likely to be affected by the proposals for UK banking reform. Certain other banks were subject to enhanced monitoring, in particular those with a Eurozone connection or vulnerability.

Participation in Colleges of Supervisors continued to be an essential element in our supervisory programme. The Division attended five Colleges in 2012 in respect of banks from the UK, Bermuda, Cyprus, the Netherlands and Switzerland. These help us to understand better the strategy and capital and liquidity strength of parent banks together with any business vulnerabilities. Whilst not facilitating such in-depth analysis as in Colleges, nevertheless attendance at bilateral meetings with home supervisors gives us better insights into the strengths and weaknesses of parents and head offices of our licensed banks. In 2012 meetings were organised with the UK, Jersey, the Isle of Man and Bermuda.

## Sector Developments (Local)

The combined effects of the loss of attractiveness of Swiss fiduciary deposits because of the ultra-low interest rate environment and deleveraging by banks facing capital pressures put the aggregate headline total deposits figures on a clear downward trend in 2012. The decline in total assets figures has been less steep, largely reflecting the continuing preference of some banks to fund assets with non-deposit liabilities.

In response to market developments banks have adopted a range of more complex solutions to hold liquid assets as a substitute for their previous liquidity management arrangements, employing straightforward third-party bank placements. Some of these solutions involve the management of a narrow band of liquid assets and others a wider spread of assets, some with different risk characteristics. What this means is that, while there are fewer licensed banks in the post-crisis world, those remaining require a more intense level of engagement as regards liquidity management and capital planning because in order to function effectively many have had to adopt a less simple and more nimble business model.

Not surprisingly, the protracted recovery from the economic recession has taken its toll on marginal banks and three banks surrendered their licences during the course of 2012. Bank of New York Mellon (CI) Limited and HSBC Bank International Limited – Guernsey Branch surrendered their licence following strategic reviews at group level. Laiki Bank (Guernsey) Limited – a very small subsidiary of Cyprus Popular Bank Public Company Limited – surrendered its licence to allow its parent to concentrate on the challenges facing its principal markets of Cyprus and Greece.

## Enforcement

One condition was put on a licensed bank in 2012 in respect of the implementation of a remediation plan imposed as a result of a breach of the AML/CFT Handbook.

One requirement was issued under Section 25 of the Banking Law to provide information about the activities of a prospective non-regulated financial services business.

The Division also placed on its website four warnings about non-bank entities in relation to misleading advertising about bank-like products and the misleading or inappropriate use of bank names.

## Industry Liaison

The Commission held a finance industry-wide seminar at St James Concert and Assembly Hall on the morning of 23 November 2012. The keynote speaker for the event was Lord Digby Jones. Specialist presentations for each sector were held in the afternoon. Banking Division's presentation was in two parts followed by a panel for questions and answers. The first part was a review of banking sector supervision in 2012 by Director Philip Marr, with a forward-looking section at the end entitled "What's New in Regulation". The second part was an update by Assistant Director Andrea Sarchet-Luff on the Division's Review of the Large Exposure Policy, including our thoughts on the likely shape of the forthcoming consultation paper. The text of the presentations is available on the Commission's website.

The Division had several meetings with the Association of Guernsey Banks ("AGB"), including a meeting to explain our understanding of the issues flowing from UK proposals on banking reform and how they might impact the Crown Dependencies. The Division has collected statistics from AGB members to collate with similar data from Jersey and the Isle of Man to support its position in discussions with HM Treasury. The Division is also facilitating the collection of statistics on dormant accounts.

## Review of Key Objectives for 2012

The Division met its key objectives for 2012 with one exception. We achieved our core banking supervision goals, engaged with other supervisors through bilateral meetings and colleges of supervisors and reinstated our structured reviews of credit books through on-site visits. Specifically we completed our revision of the Code of Conduct on Advertising and introduced a standard licence condition for Guernsey-incorporated banks, requiring them not to repatriate capital or pay dividends without the Commission's prior consent. Generally we continued our engagement with industry and government and worked with our counterparts in Jersey and the Isle of Man to monitor developments on the proposals for UK banking reform.

We were unable to complete our Review of Large Exposures Policy and to reissue guidance in 2012 because resources were required to be diverted to Commission-wide centralisation projects.

## Key Objectives for 2013

- Undertake appropriate supervisory visits and associated work.
- Continue to maintain and enhance relationships with other regulatory authorities.
- Undertake self-assessment against Revised Basel Core Principles.
- Work with HM Treasury to prepare for UK banking reform.
- Consult on Large Exposure Principles and issue final guidance.

# FIDUCIARY DIVISION

## The Market

The most notable change that occurred to the market was the challenges faced by those licensees administering Qualifying Recognised Overseas Pension Schemes ("QROPS"). At the very end of 2011 the UK government published additional tax requirements that jurisdictions needed to meet in order for them to be able to continue to accept new transfers into QROPS after 6 April 2012. The States of Guernsey enacted urgent legislation to ensure Guernsey continued to qualify as a jurisdiction that could provide QROPS. Guernsey's move was met equally swiftly by further changes enacted by the Treasury, the effect of which was to prevent new transfers into Guernsey-domiciled QROPS, although existing business was unaffected.

Away from the pensions sector, fiduciary licensees have continued to seek new business from the emerging markets. Statistical data from the 2012 annual return supports a slow steady growth in these markets. Over the last couple of years, representative offices have been opened by Guernsey licensees in many locations, including Shanghai, Hong Kong, Singapore, Delhi, Dubai and the US.

The Division also has responsibility for the non-regulated financial services businesses which it reviews in accordance with the "lighter-touch" regime that that Law requires. A key responsibility remains to ensure the reputation of the Bailiwick is maintained as a financial centre, and this led the Commission for the first time to issue a formal policy. The Commission, after consultation with the States of Guernsey, has decided that applications to run businesses providing "high interest, short-term unsecured lending to retail customers outside the Bailiwick" will ordinarily be refused.

## International Developments

Moves by national governments around the world to focus on and limit fiscal loss have led to the development of legislation. In the US this is in the form of the Foreign Account Tax Compliance Act ("FATCA") and it follows other models such as earlier French legislation. Compliance with the requirements of FATCA is not for the Commission to over-see: that sits with the relevant tax authorities. The effect of FATCA, however, cannot be ignored. It is a complex piece of legislation that places not insignificant administrative requirements on service providers. It is also an important development in international fiscal compliance. Many jurisdictions, including the United Kingdom, have entered into inter-governmental agreements with the US and it is anticipated that Guernsey will follow in due course. It is also likely the FATCA model will be followed by other countries in time.

Closer to home, the United Kingdom has re-visited its rules concerning stamp duty land tax, introducing a number of measures that make it unattractive to own property via companies, indeed encouraging a move towards personal ownership of realty. The United Kingdom is also introducing a general anti-avoidance rule to look more closely at schemes to determine whether or not there is a commercial justification to their structuring. This is a provision which has existed within Guernsey tax legislation for many years. It will be interesting to note how both the development of the FATCA-type legislation is picked up by other jurisdictions and the long-term effect of the move towards the general anti-avoidance rule within the United Kingdom.

In September 2012 Guernsey reinitiated the Quatre Isles Group which comprises the fiduciary regulators from Guernsey, Jersey, Isle of Man and Gibraltar. A very useful meeting was undertaken over two days and terms of reference were agreed upon, to include the exchange of information on developments in legislation; regulatory strategy and policy; supervisory techniques, and steps being undertaken to maximise efficient and effective supervision.

The Director of Fiduciary Services also attended the meeting of the Group of International Finance Centre Supervisors ("GIFCS"). This body represents those international finance centres within the wider Basel Group on Banking Supervision and is to date the international body taking the closest interest in the fiduciary sector.

## Supervision

The Commission has undertaken a significant degree of change during 2012 with the introduction of both the Anti-Money Laundering/Countering the Financing of Terrorism Division ("AML/CFT Division") and the Authorisations Unit. The changes have reflected a change of emphasis on supervision by the Fiduciary Services Division ("the Division"). The AML/CFT Division is now responsible for undertaking on-site visits to address and consider issues of AML and CFT compliance. The Division is moving towards more prudential regulation of the sector.

The Division operates in three teams. Two are operational teams, each headed by an Assistant Director and comprising three analysts/senior analysts. Each operational team has responsibility for a constituency of licensees, although no individual analyst has responsibility for any particular licensee. This new approach will develop over time a clear understanding by the team of the constituency. Each contains an equal spread of large, small and medium-sized trust companies, where non-regulated financial services businesses are administered by a licensee; they are aligned to the relevant team.

The third team, comprising an Assistant Director and an analyst, have responsibility for considering and analysing the macro prudential issues which arise from the fiduciary sector. It is this team, for example, that going forwards will maintain the statistical base and be involved with the undertaking of more thematic-based reviews. The Division will start to undertake thematic reviews during 2013, the first most likely to be on data security.

## Sector Developments

2012 saw the passing of the Guernsey Foundations Law. A foundation is a new product and in a sense a hybrid between a company and a trust. A foundation provides a product with which a civilian lawyer will be more readily comfortable than a trust. It is hoped that foundations will be of particular interest to the emerging markets who are looking to obtain appropriate wealth management services.

With the introduction of foundations, the Commission needed to consider the best way to approach the risk/reward balance. It was acknowledged that there are licensees who have for a number of years administered non-Guernsey foundations. It was determined that training should be accessible to the industry and licensees were encouraged to undertake it. The Commission is grateful to the involvement of the Society of Trust and Estate Practioners ("STEP") in developing and providing courses to the fiduciary sector. In addition the Commission held a conference on the legal and regulatory aspects of foundations generally, but specifically those now available under the Guernsey Foundations Law 2012. From this approach it is hoped that Guernsey will be able to benefit from the introduction of this new product.

In addition, 2012 also saw Guernsey as the first jurisdiction in the world to introduce the concept of the registration of image rights. This allows individuals to register their personality and underlying image rights and acquire intellectual property rights over both. This requires the involvement of a fiduciary licensee in the registration process.

During the year the Division has consulted on amendments to the Retirement Annuity Trust Scheme Rules 2010, and also on the introduction of a Code for Foundation Service Providers along the lines of those which already exist for corporate and trust service providers.

## Enforcement

During the year the Division continued to undertake a proactive approach towards Enforcement. This approach saw a number of issues resolved swiftly, with the result that, rather than having to impose conditions, licensees only received letters formally recording the issues that, but for their action, would have led to enforcement action. The issues that arose were across a broad range of matters but in particular underline the need for staff training at all levels on AML/CFT matters.

In addition the Division issued six notices seeking information from licensees either in support of international co-operation with over-seas authorities or where there were suspected breaches of regulatory requirements.

## Industry Liaison

Meetings have taken place during the year between the senior management of the Division and the Guernsey Association of Trustees and the Guernsey Association of Pension Providers. The Director of the Division has also continued to chair the Fiduciary Services Education Forum in association with the GTA University Centre. In addition, and in light of the many changes occurring to the markets, the fiduciary sector service senior management in the Division consider it important to attend relevant conferences in order to understand the issues arising in real time. In the last year management have attended conferences in Guernsey, Jersey, the UK and Switzerland.

## Review of Key Objectives for 2012

- Produce a Code for Foundation Service Providers.

  The Code went out to consultation on 18 December 2012.

- Ensure the sector has access to appropriate training on foundations.

  The Division worked closely both with the Fiduciary Services Education Forum and separately with the Guernsey branch of STEP to ensure courses were produced and made available. Separately the Commission ran its own conference "Firm Foundations" at the start of 2013.

- Review the application process, especially those for exemptions.

  The application process was considered, although not finalised, and a policy on applications for discretionary exemptions is in discussion with the Commercial Bar Association.

- Monitor and respond as necessary to developments in the legislative framework for QROPS.

  This objective was overtaken by the steps taken by HM Treasury in March and April 2013 (see above).

- Improve the statistical base for supervision.

  The Annual Return form was expanded and the results of the increased data received analysed. A statistical presentation was made during the Industry Presentations in November 2012.

- Re-engage with other regulators of fiduciary business, especially those in Jersey, the Isle of Man and Gibraltar.

  The Quatre Isles Group met in September 2012 at the instigation of Guernsey, and the Director attended the autumn meeting of the Group of International Finance Centre Supervisors ("GIFCS").

- Continue and develop engagement with industry.

  Meetings have continued to be held with industry and other relevant stakeholders.

## Key Objectives for 2013

- Undertake appropriate supervisory visits and associated work.
- Continue to maintain and enhance relationships with other regulatory authorities.
- Issue guidance to the fiduciary sector on annual returns.
- Undertake a thematic review of data security within the fiduciary sector and report on findings.
- Lead the work stream of the Group of International Finance Centre Supervisors to review the statement of best practice for trust and company service providers.
- Enhance the fiduciary sector's statistical base.

INSURANCE DIVISION

## The Market

In 2012 the global insurance industry weathered the challenges of the previous year well. General insurers and re-insurers rebuilt the capital loss resulting from exceptional catastrophic losses. Declining interest rates and a recovery in equity markets benefitted year-end valuations. The US captive market began to be bolstered by demand created by US federal health care legislation. At the same time, the global insurance market remains generally soft, with yields low and, although mitigated by developing country markets, growth limited in the developed country life sector.

The Guernsey insurance market is somewhat specialised and the main active sector is for captives. 2012 aggregate figures are unavailable at present but in 2011 gross assets and net worth remained broadly flat. Gross premiums rose by £0.57 billion to £4.62 billion, albeit largely due to one firm.

As in previous years, in 2012 the local Guernsey market remained relatively stable in terms of licences. In 2012, there were eight licensed domestic insurers dealing with local requirements compared to 11 in 2011, 40 licensed insurance intermediaries dealing with local and specialised requirements compared to 39 in 2011, and 19 authorised managers serving the captive market in both 2011 and 2012.

In contrast the number of international licences grew significantly to 737 in 2012 from 687 in 2011. The reason for this was idiosyncratic and relates to the NewBuy Scheme sponsored by the English government and the Home Builders Federation, designed to encourage the public to take out mortgages. This Scheme includes an element whereby building companies form captives in Guernsey to insure themselves against limited losses ultimately due to mortgagor default. In 2012 the Scheme alone led to the formation of two Protected Cell Companies ("PCC") and 53 PCC cells. It is as yet too early to determine take-up by the public and whether, for example, the Scheme will materially increase gross premiums in Guernsey.

Due not least to the NewBuy Scheme, the long-term trend around fewer companies and more PCC cells continued. In 2012 there were 242 companies, down from 255 in 2011; and 329 PCC cells, up from 267 in 2011.

In 2012 47 international insurer licences were surrendered, down from 60 in 2011, and 97 granted, up from 72 in 2011. These numbers show a significant turnover in the sector in response to business demands; and much of the work of the Division is to respond to this annual turnover volume.

## International Developments

The focus of the Division's global regulatory activity was to concentrate resources on the emerging guidance around captives to be issued in due course by the International Association of Insurance Supervisors ("IAIS"). Other than this, the Division participated in 2012 in the working group meeting of the Offshore Group of Insurance Supervisors and one overseas supervisory college. On behalf of Commissioners, the Division also undertook work on transitional equivalence in relation to Solvency II, by which Guernsey would have two regimes, one compliant with Solvency II and the other not. In the event the government chose not to pursue this option.

## Supervision

The Division continued in 2012 to vet carefully all new licence applications, including preliminary meetings with prospective licensees. Formal applications in principle were processed generally within one month.

In 2012, the Division completed 15 on-site visits compared to 23 in 2011. The reason for the fall was the need to devote divisional resources to the centralisation process, especially the Authorisation project, which was sponsored by the Division. Eight of the on-site visits focused on sales practices amongst life insurance intermediaries. Several shortcomings were uncovered and these were set out in generic terms in a letter to the life intermediary industry as a whole. There will be a second series of such visits in the latter part of 2013.

In 2012, the Division successfully piloted supervisory prudential meetings with several types of licensee with the aim that this approach in 2013 should replace the more restricted business plan-orientated annual meetings with insurance intermediaries and managers only. Particular attention was paid to those firms considered to pose the greater risk to the Commission's objectives.

In 2012 the Division conducted more detailed reviews on the actuarial reviews of key life companies than had hitherto been undertaken.

Due to increased efficiency and to the centralisation process, the establishment of the Division fell from 18 to 15 at end-2012.

## Sector Developments

During 2012 the Division issued several discussion papers to the local insurance industry. These papers put forward preliminary ideas as to how the Bailiwick might best implement the new Insurance Core Principles ("ICPs") set out by IAIS. This work will lay the foundation for formal consultation in 2013. It was also decided that in early 2013 a solvency exercise would be run with the industry to test run possible new solvency standards. As this exercise will include stress tests, the Division decided to forgo the 2012 annual stress test exercise.

In May 2012, the Commission delivered to the government its formal advice as to whether the Bailiwick should adopt the UK's policy set out in the UK Financial Services Authority's Retail Distribution Review ("RDR"). This published paper set out the pros and cons in the Commission's eyes and ended by arguing for a wait-and-see approach. The government launched formal consultation on RDR late in 2012, with the aim of concluding a policy position in 2013. Commission work on the RDR was undertaken by the Insurance and Investment Business Divisions.

The Division contributed to projected updates to the AML/CFT Handbook, arguing that general insurance should be excluded.

Over the course of 2012 the Division upgraded its website insurance statistics by sector. This included publishing, for example, a breakdown by business line of gross premium and insurance intermediary commissions.

## Enforcement

In relation to enforcement, the Division considered 43 breaches of regulatory requirements in 2012, of which six resulted in sanction action. However only one of these was high-level where a private fine was applied.

## Industry Liaison

The Division has frequent meetings with the local insurance trade bodies, including this year several on the regulatory changes noted above.

## Review of Key Objectives for 2012

- To focus on more proactive supervision – The Division has piloted short prudential meetings across a wide range of licensees, focused on-site visits on the intermediary sales process, and undertaken analysis of actuarial reviews on the larger life companies.
- To define the Commission's response to new international regulation – The Division has contributed to the Commission's response to RDR and has issued several discussion papers on the new ICPs.
- To play a full and active part in the continuing transformation of the Commission – The Division sponsored the Authorisation project.
- To improve the statistical base for supervision – The amount of data has been increased significantly in line with other jurisdictions.

## Key 2013 Objectives

- Undertake appropriate supervisory visits and associated work.
- Continue to maintain and enhance relationships with other regulatory authorities.
- Consult on implementation of the new International Association of Insurance Supervisors' Insurance Core Principles.
- Plan implementation of the Guernsey Financial Advice Standards.
- Undertake a thematic study of sales practices amongst insurance intermediaries.

# INVESTMENT BUSINESS DIVISION

## The Market

Guernsey's investment business sector continued to be affected by global economic conditions during 2012. Major stock markets again saw significant volatility during the course of the year which impacted listed investment valuations, albeit there were examples of gains as well as losses. Market confidence remained generally low. These factors had an impact on the levels of new business considered by the Commission. Fifty new licences to conduct controlled investment business were issued during the year (2011: 64) whilst in the investment fund sector 13 open-ended and 70 closed-ended collective investment schemes were either authorised or registered (2011: 19 and 75 respectively). A total of 217 new classes of existing open-ended collective investment schemes were approved (2011: 125) and finally, 29 approvals for the provision of specific services to non-Guernsey schemes were issued (2011: 44).

The various sectors within the overall investment fund community once again experienced varying fortunes in terms of valuations. In the open-ended sector the net asset value of Guernsey-regulated funds fell over the course of the year from £55.3 billion to £50.3 billion, a decrease of just over 9%. Net redemptions from funds were almost £3 billion, the other impacts arising from market movements, including foreign exchange fluctuations. It was a different story in the closed-ended sector where the net asset value of Guernsey-regulated funds increased from £119.1 billion at 1 January to a little under £131 billion at 31 December 2012, an increase of approximately 10%. This apparently inconsistent performance is probably not unexpected when you consider that the valuation of a significant number of assets within closed-ended structures is not necessarily directly correlated to stock market performance, especially in the private equity arena and vehicles investing in physical assets such as real property.

Overall, the net asset value of Guernsey-regulated investment funds rose by some £6.9 billion to end the year at £181.3 billion, an increase of 3.9%. The value of non-Guernsey open-ended collective investment schemes serviced from Guernsey also increased, by £8.5 billion to finish the year at £95.5 billion, an increase of 9.7%. The values of assets in the non-fund sector, covering asset managers and stockbrokers as at 31 December 2012, were £92.8 billion, an increase of £5.5 billion over the year.

## International Developments

The Investment Business Division ("the Division") continued to focus a large amount of attention on European Union ("EU") developments during 2012. The Alternative Investment Fund Managers Directive ("AIFMD") remained of significant interest, not just to the Commission but also the States of Guernsey and the local investment fund sector, and this will continue into 2013 and beyond.

The Commission indicated during 2012 that it was considering the implementation of two regulatory regimes for investment funds established and regulated in Guernsey. Whilst a number of fund promoters have a direct interest in the AIFMD, due to the structure of their funds, including EU participants or the funds being marketed into the EU, there are other promoters who have no such interest as their Guernsey-regulated products are not marketed into the EU or their managers are not EU-based. Adopting a single regulatory regime that solely focuses on the European issues risks adversely impacting this non-EU-directed business. Guernsey Finance issued a news release in November 2012 confirming this proposition, i.e. dual regulatory regimes. In effect, the issue will become a commercial decision for promoters: does the fund need to fall within the scope of AIFMD requirements or can it remain outside?

Notwithstanding the delays encountered relating to the publication of the EU regulations relating to the AIFMD following discussions between the Commission, the States of Guernsey and the Guernsey Investment Fund Association ("GIFA"), it was agreed that a working group would be established to begin work on drafting the necessary rules. The work of the group continued into 2013 as the relevant requirements were considered and the first set of proposed rules relating to the marketing of Guernsey funds into the EU was issued for public consultation in March 2013.

The Commission also liaised with the European Securities and Markets Authority ("ESMA") in respect of the Commission's application to sign up to the relevant co-operation agreements that will be a requirement for Third Countries seeking to conduct business with the EU within the scope of the AIFMD. Discussions with ESMA continued into 2013 and at the time of this report the Commission remains optimistic of a positive conclusion.

The Commission continues to monitor developments in respect of other European directives that may have an impact on the Bailiwick as a Third Country.

Senior staff of the Division participated in various meetings with, and conferences of, regulatory authorities and organisations during 2012 in order to meet with regulatory counterparts and better understand initiatives and developments that impact, or might impact, the Commission's scope and nature of regulation. International meetings attended included the Annual Meeting of the International Organisation of Securities Commissions ("IOSCO"), the European Regional Committee of IOSCO, the Enlarged Contact Group of Collective Investment Schemes Supervisors, the United States Securities and Exchange Commission's International Supervisory and Enforcement Programme and an IOSCO regulatory training course.

## Supervision

The Division's main regulatory activities continued to be undertaken by functional teams, being (1) desk-based monitoring, covering routine and ad-hoc submissions from regulated firms and collective investment schemes including notifications, pricing errors, rule breaches and complaints; (2) on-site visits, undertaking visits to licensees to review their compliance with regulatory obligations as well as desk top reviews of information provided by licensees in response to Commission requests for information; and (3) applications for new business, including new licences together with collective investment schemes' authorisations and registrations.

As would be expected, the desk-based monitoring function saw considerable activity over the course of 2012 as licensees and collective investment schemes continued to react to the wider global economic conditions. Desk-based monitoring is one of the primary methods by which the Investment Business Division can become aware of potential or actual concerns relating to regulated firms and/or products and the function is not simply limited to the processing and administration of regulatory submissions.

During the year a total of 15 visits to licensees were conducted, including one undertaken jointly with other divisions. The visits undertaken by the Investment Business Division covered not only the directly licensed firms but 59 administered licensees, 136 regulated collective investment schemes and 61 non-Guernsey schemes. Matters identified during these visits are reported to the licensee's senior management and will be considered for possible enforcement action (see below).

The Division, together with the Commission's Insurance Division, kept under review the developments regarding the United Kingdom Financial Services Authority Retail Distribution Review ("RDR"), which is a key part of its consumer protection strategy. Its aim is to improve clarity for people looking to invest, raise the professional standards of advisers, and reduce the conflicts of interest which are found in commission-based remuneration for adviser services. The Commission's recommendations relating to RDR were submitted to the political authorities for their consideration during 2012. The States of Guernsey Commerce and Employment Department undertook a public consultation in late 2012 in respect of RDR and following the conclusion of that process introduced the Guernsey Financial Advice Standards, for which the Commission will develop the necessary regulatory framework.

A workstream that had commenced prior to 2012 related to the review and amendment to the existing rules covering Class B open-ended collective investment schemes. Due to the work being undertaken in relation to the implementation of rules relating to the AIFMD, as mentioned above, work on the Class B Rules was suspended so that relevant investment funds would only be subject to one set of changes rather than two.

## Sector Developments

Guernsey's investment business sector continued to be affected by global economic conditions during 2012 and the ongoing uncertainty resulting from the AIFMD and the impact this directive would have on existing and new fund business. Licensees had to work hard in order to attract new business.

The Commission received a request from GIFA during the second half of 2012 to re-examine the approvals process in respect of the servicing of non-Guernsey-domiciled open-ended collective investment schemes from within the Bailiwick. Following a public consultation process it was confirmed that two approaches could be adopted by licensees when applying for approval to manage or administer these non-Guernsey schemes. The "traditional" approach requires the Commission to undertake a more detailed review of the proposed scheme, including due diligence on the relevant parties involved. The alternative approach, which is based upon the regimes already existing for Qualifying Investor Funds and Registered Funds, requires certification warranties being provided by the applying licensee. That approach requires less involvement from the Commission and approvals will be issued within two business days subject to receipt of all required documentation and warranties. The revisions to the application process came into effect on 2 January 2013 and demonstrated the Commission's ability to work with industry in order to amend existing processes, providing benefits for both.

## Enforcement

The most common form of action taken by the Division where circumstances were identified that were considered to require some form of sanction continued to be the imposition of conditions on the licensee involved. The imposition of conditions is subject to the normal safeguards provided for in the Protection of Investors Law and licensees are fully entitled to contest and appeal to the Courts in respect of any proposal to impose a licence condition. At the start of 2012, six licensees had conditions imposed on their individual licences with their agreement. During the course of the year four new sets of agreed conditions were imposed on licensees whilst one set was removed. Therefore as at 31 December 2012 nine licensees had conditions imposed on their licences.

In terms of the new conditions imposed during 2012 two of the cases related to the licensees concerned not meeting the due diligence requirements expected of firms submitting applications for Qualifying Investor Funds or Registered Funds, both of which require licensees to provide warranties to the Commission confirming that they have undertaken certain minimum due diligence on the relevant parties to the subject fund. This allows the Commission to undertake to process the application within a limited time frame. The imposed conditions have resulted in the licensees concerned having to submit additional information to the Commission with the application so that the Commission can assess the level and nature of the due diligence undertaken. The time allowed for the Commission's consideration is increased to allow a more detailed review of this material than would normally be the case under the "fast track" regimes. To date, licensees who have experienced this condition have amended their processes and procedures such that no licensee has yet been totally excluded from the regime. One licensee was required to conduct remedial action in terms of having to conduct detailed file reviews to address any deficiencies as a result of identified conduct of business rules breaches. The final conditions imposed related to a new licensee such that they could not undertake additional business, beyond that taken on at licensing, until such time as the Commission had assessed that they were appropriately resourced and managed to service additional business.

## Industry Liaison

In addition to routine bilateral meetings between the Division and licensees, regular meetings were held between members of the Division's senior management team and the senior personnel representing the two investment sector trade bodies, being GIFA and the Guernsey Investment Managers and Stockbrokers Association ("GIMSA"). These meetings provided good opportunities to communicate and discuss current and future initiatives and issues arising from the Commission's activities In addition, the Division undertook briefings to industry as part of the Commission's Annual Industry Presentations in November 2012.

## Review of Key Objectives for 2012

| *2012 Objectives* | *Result achieved* |
|---|---|
| Implement revised Class B Rules during the first half of 2012, having undertaken a public consultation process and provided detailed feedback as part of that process. | Consultation undertaken but workstream suspended in light of work undertaken relating to AIFMD which would also impact subject investment funds. Re-commence in 2013. |
| Conduct self assessments against the updated IOSCO Principles of Securities Regulation and consider the action required, including the extent and nature of any changes to legislation or underlying rules and regulations. | Self-assessment undertaken and necessary legislative changes factored into the consolidation/review of regulatory legislation workstream. |
| Continue to engage with European authorities, including ESMA, the UK Financial Services Authority (and successor body) and other European national regulatory authorities in respect of the Alternative Investment Fund Managers to consider the nature of any changes required in Guernsey's regulatory framework, including the access of Guernsey investment funds for marketing to EU-resident investors. | Various discussions and meetings occurred during the course of 2012 in respect of AIFMD and its impact on Guernsey as a Third Country. The Commission has made an application in respect of the co-operation arrangements required with ESMA and will continue the various dialogues in preparation for 22 July 2013, being the date that the Directive takes effect in Member States. |
| Continue to prioritise on-site visits undertaken by the Division using a risk-based approach and increasing the focus on risk-based supervision more generally. | Due to pressures on the division, on-site visits were undertaken using a risk-based approach. Senior divisional staff participated in the Commission-wide workstream relating to risk-based supervision. |

## Key Objectives for 2013

- Undertake appropriate supervisory visits and associated work.
- Continue to maintain and enhance relationships with other regulatory authorities, particularly the European Securities and Markets Authority and the UK Financial Conduct Authority.
- Introduce an appropriate regulatory regime for investment fund managers and associated investment funds to take account of AIFMD implementation.

# POLICY AND INTERNATIONAL AFFAIRS

## General

The Policy and International Affairs team has responsibility for coordinating many of the local and international policy issues facing the Commission, including changes to legislation. The team also has responsibility for the Commission's policies on the Anti-Money Laundering/Countering the Financing of Terrorism ("AML/CFT") framework, including the Handbooks for Financial Services Businesses and Prescribed Businesses on Countering Financial Crime and Terrorist Financing ("the Handbooks"). Together with the Director General, it is the Commission's main link with the Policy Council and the Attorney General's Office on policy matters. It is also the main link with certain international bodies, including the International Monetary Fund ("IMF"). In addition, the team coordinates a number of cross-divisional matters such as legislation.

## Cooperation and Coordination

During 2012 the committees and other groups which bring together the AML/CFT authorities in the Bailiwick were restructured. A new Financial Crime Strategic Steering Group was established to coordinate the activities of the other committees and groups engaged in work in relation to sanctions, corruption, money laundering and terrorist financing. It comprises representatives of law enforcement, the Law Officers' Chambers and the Commission. The Director General, the Director of Policy and International Affairs and Legal Counsel represent the Commission on the steering group. The group met once in 2012.

The AML/CFT Advisory Panel ("the Panel") met twice in 2012. The committee is a forum which enables coordinated advice to be provided to the Strategic Steering Group from the Attorney General's Chambers, the Commission, the Guernsey Border Agency (including the Financial Intelligence Service ("FIS")), Police, Income Tax, the Guernsey Company Registry and the Alderney Gambling Control Commission ("AGCC"). The Director of Policy and International Affairs sits on the Panel.

The Financial Crime Working Party (which includes the Commission's Deputy Director of Intelligence Services) reports to the Panel. Its objectives are primarily to discuss the implications for policy and practice of particular cases of interest and to provide practical assistance to interested parties. The group met twice in 2012.

The Sanctions Committee reports to the External Relations Group of the Policy Council and the Financial Crime Strategic Steering Group. The committee, chaired by the Director of Policy and International Affairs, and on which the Deputy Director of Intelligence Services sits as a member, met three times in 2012.

The Anti-Bribery and Corruption Panel reports to the AML/CFT Advisory Panel. The Director of Policy and International Affairs represents the Commission on the Panel, which met twice in 2012.

## AML/CFT Developments and Initiatives

During April 2012 the Director of Policy and International Affairs and Simon Gaudion, the Senior Investigation Officer of the FIS, led events which provided feedback on AML/CFT matters to the finance sector. These were followed in July 2012 by the issue of a report by the Policy and International Affairs team, which provided feedback on the Commission's AML/CFT on-site inspections.

The Policy and International Affairs team was substantially involved with the development and organisation of the Puppet Masters anti-corruption conference sponsored by the Anti-Bribery and Corruption Panel, which was held in May 2012.

A wide range of international and domestic speakers made presentations at the conference. The domestic speakers included representatives of the Attorney General's Chambers, the Guernsey Border Agency and the Commission. The international speakers included representatives of the World Bank and other experts who covered subjects such as bribery, corruption, politically exposed persons ("PEPs"), sanctions, international standards, criminal and civil law issues, and the practical effects of all of these on firms and individuals. The conference considered these issues so that delegates could put them in both a business and a Guernsey context.

In July 2012 the Commission consulted with industry on proposed modifications to the AML/CFT regulations and Handbooks. The final amendments, issued in March 2013, included a more sophisticated approach for firms in risk profiling their customers; the removal of general insurance from the AML regulations and rules; and a new chapter providing guidance for firms in relation to bribery and corruption.

During 2012 the Commission continued to issue further Instructions in respect of business from sensitive sources. These Instructions required financial services businesses and prescribed businesses to undertake enhanced customer due diligence measures and to pay special attention to business or transactions from countries or territories specified in the Instructions.

## International Work

The Policy and International Affairs team monitors developments by the Financial Action Task Force ("FATF"). It also attends the plenaries held each year. During the year the FATF issued revised Recommendations. The Director and Deputy Director participated in the working groups which took forward this work.

During 2012 the Director was Chair of the International Association of Insurance Supervisors ("IAIS") Supervisory Cooperation Subcommittee and the Multilateral Memorandum of Understanding Signatories Working Group. These groups met several times in 2012, normally by teleconference. During the year the IAIS working group reviewing adherence by IAIS members with the Insurance Core Principles on cooperation and information exchange, which was chaired by the Director, issued its report. The Director also chaired the expert team which commenced work in 2012 on reviewing adherence by IAIS members with the Insurance Core Principles on the objectives, powers and responsibilities of the supervisor and the supervisor's independence, accountability and transparency.

## IMF Surveys

The Commission provides statistics from Guernsey financial institutions to the International Monetary Fund ("IMF") for its Coordinated Portfolio Investment Survey ("CPIS") on an annual basis. Each year, institutions are asked to provide cross-border statistics in respect of Guernsey banks, open and closed-end collective investment funds, insurers, insurance intermediaries/brokers and special-purpose vehicles. The statistics for 2011 were obtained in respect of 103 institutions, representing 1,114 entities.

The total value of assets reported for Guernsey financial institutions as at 31 December 2011 was US$214.3 billion, a decrease of US$11.4 billion over the assets reported in the 2010 survey. By the end of 2011 the total assets held by investment funds were, at US$164.5 billion, a decrease of US$7.6 billion over the assets reported in 2010.

During 2012 the Commission participated for the seventh time in the IMF's information dissemination and monitoring framework initiative.

## Review of Key Objectives for 2012

During 2012 the Commission undertook significant work on drafting a consultation paper on the consolidation and revision of the laws it administers. The paper, which was issued in May 2013, proposed the consolidation of the Protection of Investors (Bailiwick of Guernsey) Law, 1987; the Banking Supervision (Bailiwick of Guernsey) Law, 1994; the Regulation of Fiduciaries, Administration Businesses and Company Directors, etc (Bailiwick of Guernsey) Law, 2000; the Insurance Business (Bailiwick of Guernsey) Law, 2002; the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002; and the Registration of Non-Regulated Financial Services Businesses (Bailiwick of Guernsey) Law, 2008. These laws were developed separately over a period of 20 years and reflect the needs and wants at the time of their preparation. Consolidation will enable the differences between the laws to be addressed. The consultation paper also proposed revisions to some areas of the current legal framework, which reflect the Commission's experience and will allow the Bailiwick to meet aspects of the revised international standards of the FATF, the Basel Committee on Banking Supervision, the IAIS and the International Organization of Securities Commissions requiring primary legislation.

The Policy and International Affairs team also continued work on refining the Commission's approach to risk. The revised international standards of the Basel Committee on Banking Supervision, the IAIS and the International Organization of Securities Commissions will require enhanced approaches to risk both at the level of the licensee and at the level of macro prudential supervision. The aims include, so far as it is possible, the creation of a Commission-wide approach to risk profiling licensees. Consideration of the IT systems applied by other supervisory authorities has allowed the Commission to calibrate its thinking with that of other authorities and also to consider the efficiencies offered by Commission-wide workflow management tools. This project will be facilitated by the development of Sentinel. The finalisation of the risk management and workflow management aspects of Sentinel in 2013 will enable the practical aspects of the enhanced approach to risk to be commenced.

## Key Objectives for 2013

- Take forward towards implementation the consolidation and revision of regulatory laws.
- Lead and finalise licensee impact and risk frameworks.
- Take forward work on alignment of the Crown Dependencies' anti-money laundering/countering the financing of terrorism frameworks.

# FINANCE AND OPERATIONS DIVISION (INCLUDING DATA MANAGEMENT)

## General

The Division is responsible for the provision of key support services to the Commission, covering financial and management information, communication and information systems, human resources, facilities management and general administration.

## Financial Information

The financial statements are shown on pages 43 to 47.

The overall deficit for the year 2012 is £550,746, compared to a surplus in 2011 of £1,643,645. This result combines a slight decrease in fee revenue with more marked increases in direct costs and, largely as a result of legal and professional expenses, common costs. Revenue and costs by sector are set out in table 7 on page 71.

Salary and related costs for the year were £8,767,951, compared to £7,917,626 in 2011. An analysis of these figures is provided in table 8 on page 71, and analyses of staff by salary band and movements in staff numbers are shown in tables 9 and 10 on pages 71 and 72.

The restructuring of the organisation to optimise operational efficiencies against a backdrop of expanding regulatory and supervisory challenges has necessitated some increase in staff resources. The Commission continues to prepare itself by adopting a model that will ultimately allow a higher proportion of staff to focus on these areas rather than on administrative tasks.

The result for 2011 benefitted from a net gain of £540,000 on the transfer of certain sub-contracted staff on 31 December 2011 to the employment of the GTA University Centre. Pension costs increased £105,000 during 2012.

The increase in common costs in 2012 reflects, in part, the expenses associated with the Independent Evaluation Review ("IER"), which is described elsewhere in this Report. The recommendations of the Review were in the course of implementation throughout 2012, with costs incurred of £730,000. Costs associated with investigative and enforcement activity increased in 2012 to £542,000 from £308,000. Overall, expenses for the year ended 31 December 2012 were 21% higher than in 2011, comprising in the main the exceptional, non-recurring costs referred to above.

The Commission faces a further period of cost in 2013 as the recommendations of the Review are brought to a conclusion, though this will largely comprise capital investment in the Sentinel programme, which is described elsewhere in this Report.

A breakdown of Commissioners' fees is shown in table 12 on page 72 the increase in late 2011 reflecting a review of the Commissioner roles and responsibilities.

The deficit in the pension scheme at December 2012 reported under Financial Reporting Standard 17 ("FRS17") is £6,774,291, a decrease of £802,888 compared to 2011, reflecting an inflation assumption that has decreased by 0.1% and an actual investment return for the year that was higher than expected. As this valuation is a point-in-time calculation, it can be expected to vary from year to year, without prejudicing the scheme's long-term ability to provide the required benefits. The scheme's actuary carried out a full actuarial valuation of the scheme as at 31 December 2010, for funding calculation purposes, which showed a funding surplus of £1,145,000. We also requested the actuary to prepare an estimated funding valuation as at 31 December 2012 which shows a shortfall of £56,000, a figure considerably lower than that disclosed by the FRS17 valuation of £6,774,291.

FRS17 includes the following requirements:

Pension scheme assets are to be measured using market values.

Pension scheme liabilities are to be discounted at an AA corporate bond rate.

The pension scheme surplus (to the extent it can be recovered) or deficit is recognised in full on the balance sheet in the accounts of the sponsoring employer.

There are extensive disclosures required under FRS17 which are intended to be an aid in comparing pension costs and liabilities between companies. FRS17 is prepared for accounting purposes whereas an actuarial valuation is carried out to compare the value of the scheme's assets with a funding target which calculates the value of the benefits that will be paid from the scheme in the future, using information about the scheme at the valuation date.

The basis of preparing FRS17 is very prescriptive and, whilst many of the assumptions used are the same as or very similar to those used in the actuarial valuation, there is a major variance in the key assumption of discount rate which makes a substantial difference in the calculation of liabilities and the resultant net funding position of the scheme.

## Financial Information *(continued)*

### *Defined benefit pension scheme*

The defined benefit pension scheme is part of the States of Guernsey Superannuation Fund (the "Fund"). The decision was made in 2007 that the Commission could no longer accept the on-going uncertainties associated with all defined benefit schemes which arise from the increasing levels of life expectancy and the varying investment performance of the funds. It therefore adopted a new defined contribution scheme for staff joining from 1 January 2008 onwards. Those staff who were already members of the defined benefit scheme at that date continue to be eligible for membership of that scheme, although the terms of the scheme are currently under review by a working party established by the States of Guernsey, but under the present arrangements the need remains for proper resourcing. The States of Guernsey has confirmed that in the final resort the claims of the Commission's pensioners and employees would be met from the whole Fund and any shortfall in the Fund would then be met by the States of Guernsey from general revenue.

### *Retained reserves*

The Commission maintains a policy comprising a target for retained reserves equivalent to a minimum of six months' expenditure. The Commission's aim is to be able to absorb unexpected or exceptional costs without putting its solvency at risk. The results for 2012 mean that the Commission's reserves of £1,374,245 are equivalent to little more than a month's expenditure.

### *Fees*

When setting fees for 2013, the Commission recognised that the saving of £440,000 through withdrawal of support of the GTA University Centre ("GTA") would be insufficient to negate the need for a rate rise due to other factors, principally the costs of developing the Sentinel programme, enforcement costs and pension costs. Fee rates were generally increased by 2% across all licence fee categories to meet these costs and to rebuild the Commission's reserves.

### *GTA University Centre*

The Commission discontinued its financial support of the GTA on 31 December 2012, having contributed £440,000 in the year, the same level as in 2011. This was the final year of the subsidy as the Commission believes that the provision of funding for an external training institution is no longer a core function of a financial services regulator, particularly as its funding of the GTA cannot be isolated for finance sector training.

### *Data Management Unit*

During the last quarter of 2012 work began on the creation of a Data Management Unit as recommended in the 2011 IER. This Unit is being set up in the second quarter of 2013 and will provide a central resource for the standardised control, management and distribution of defined regulatory data.

The Unit is planned to comprise six members upon establishment.

## Fee Legislation

The fees regulations for the banking, fiduciary, insurance, investment and the non-regulated financial service business sectors were revised with effect from 1 January 2013 in respect of fiduciary fees.

A list of the current regulations prescribing fees payable to the Commission is included below:

- The Financial Services Commission (Fees) Regulations, 2012.
- The Protected Cell Companies and Incorporated Cell Companies (Fees for Insurers) Regulations, 2012.
- The Criminal Justice (Proceeds of Crime) (Legal Professionals, Accountants and Estate Agents) (Bailiwick of Guernsey) (Amendment) (No. 3) Regulations, 2012.
- The Registration of Non-Regulated Financial Services Businesses (Bailiwick of Guernsey) (Fees) Regulations, 2012.
- The Amalgamation and Migration of Companies (Fees Payable to the Guernsey Financial Services Commission) Regulations, 2012.

Copies of the fees regulations and a summary of the fees payable are available on the Commission's website at www.gfsc.gg.

## Communications and Information Systems

Information systems remain critical to the efficiency of the Commission's operation and during 2012 further enhancements were made to our central regulatory database and its integration with other Commission systems continued, including:

- upgrade of the underlying software platform to its latest version.
- enhancements required for the establishment of the new centralised units for Authorisations and Anti-Money Laundering/Countering the Financing of Terrorism ("AML/CFT").

## Human Resources

The Commission continues to support the staff in continuing professional development and training. Internal training continues to be an important component of skill enhancement within the Commission.

2012 saw Neville Johnson appointed as Chief Operating Officer in the second quarter and Tim Loveridge joining the Commission as Chief Transformation Officer in the third quarter. Neville Roberts, Director of Finance and Operations, retired in April 2012 and Sylvia Sirett, Deputy Director of the Policy and International Affairs Division, retired in September 2012.

## Commissioners

Cees Schrauwers was re-elected as Chairman with effect from February 2013 for a further term of one year. Peter Harwood retired from his role as Chairman at the end of January 2012. David Mallett also retired at the end of January 2012. Susie Farnon was re-elected as an ordinary Commissioner with effect from February 2013. Richard Hobbs was elected an ordinary Commissioner in January 2012 and Bob Moore was elected an ordinary Commissioner in February 2012.

## Facilities Management

The Commission maintained its business continuity recovery site at a dedicated area at a service provider's premises in Pitronnerie Road. This continues to provide the Commission with a long-term business recovery solution.

## Review of Key Objectives for 2012

- To prepare licensee data for the commencement of the first phase of electronic document submission, allowing licensees to submit a range of documents and notifications, thus providing benefits to both regulated entities and the Commission. Partially achieved, with more revision work required on the Commission's licensee database.
- To continue the implementation of the Commission's human resources strategy to encourage staff development; to encourage movement between divisions; and to facilitate short-term secondments to industry and medium-term secondments to international organisations. Achieved with the exception of medium-term secondments, which are being facilitated in 2013.
- To participate in the implementation of Commissioner-approved recommendations arising out of the Review. Achieved.

## Key Objectives for 2013

- Develop, implement and monitor performance standards by reference to key performance indicators and implement a transparent service level standards regime.
- Deliver the human resources strategy to increase staff engagement and optimise the deployment of human resources.
- Provide the efficient, accurate and timely handling of data, including responsibility for receiving, recording and distributing incoming post and statistical returns; handling fee invoicing, annual returns, notifications and enhancements to statistical returns.
- Develop management information reports in light of operational experience.

# AML/CFT DIVISION

This Division was set up in late 2012 to provide a central source of expertise and resource to meet the Commission's delivery objectives regarding AML/CFT. The Division may extend its scope in future, but for the present it is concerned with the planning, execution and reporting of the results of on-site visits to licensees and registered businesses to assess their compliance with AML/CFT obligations. The Division is also the dedicated resource for guidance and information on AML/CFT for both internal and external enquiries.

## On-site visits programme

The Division conducted a total of six visits during 2012 and plans to conduct 65 visits in 2013.

## Staffing

The Division was comprised of six members of staff at inception, which consisted of an Assistant Director, three Senior Analysts and two Analysts, enabling three inspection teams of two to conduct on-site visits.

The Division is in close liaison with the Commission's Policy and International Affairs team and is reviewing its policies and procedures in anticipation of forthcoming changes to the Commission's AML/CFT Handbook and in considering the proposed Methodology for Assessing Technical Compliance with the Financial Action Task Force Recommendations and the Effectiveness of AML/CFT Systems.

The Division is also in close constant liaison with the Regulatory Divisions of the Commission to keep apprised of any sector-specific developments that would impact upon the Division fulfilling its responsibilities in an informed, consistent and professional manner.

## Industry Liaison

The Commission apprised the industry of the imminent commencement of the AML/CFT Division in its presentations to industry in November 2012 and explained the expected benefits to the Bailiwick of establishing such a facility.

The Commission will provide the industry with an evaluation and its conclusions on the effectiveness of the Division as a dedicated AML/CFT centralised function during the autumn 2013 Industry Presentations. It will also be an opportunity for the Division to provide statistical data and generic feedback on the findings and trends of the visits that the Division has conducted.

## Review of Key Objectives for 2012

- To establish a centralised AML/CFT Division to conduct on-site inspection visits to licensees and registrants. Achieved.
- To provide support, guidance and assistance to industry through responses to enquiries on AML/CFT-related matters and policy in a consistent and pragmatic manner within the legislatory confines. Achieved.
- To review processes and procedures and to propose and implement changes to optimise operational efficiency and consistency. Achieved.

## Key Objective for 2013

- Undertake appropriate supervisory visits and associated work.

# AUTHORISATIONS UNIT

This Unit was set up in late 2012 to provide for the central processing of various authorisations, notifications, applications and surrenders. The Unit commenced operations with the processing of Personal Questionnaire and Personal Declaration forms. During 2013 the Unit will take on the initial processing of all applications, and all the processing of simple applications. The Unit will also take on certain simple processes which are consistent across the regulatory divisions.

## Staffing

The Unit initially comprised five members. This increased in 2013 to seven as additional functions were taken on.

## Industry Liaison

The Chief Operating Officer represents the Unit at meetings with industry representative bodies. The Unit communicates with wider industry mainly through the Commission's website.

## Review of Key Objectives for 2012

- To establish the Unit. Achieved.
- To create a consistent process for dealing with Personal Questionnaires and Personal Declarations which increases transparency and efficiency. Partially achieved as efficiency gains were not realised in the first weeks of operation. Efficiency has improved during 2013 as the Unit has become familiar with new procedures and workflows.
- To develop systems and management information to ensure optimum use of resources within the Unit. Partially achieved as the initial range of management reporting has been expanded and will continue to be developed as more operational experience is acquired.

## Key Objectives for 2013

- Propose and implement operational improvements.
- Adhere to service level standards.
- Enhance the Unit to undertake the majority of authorisation processing.

# INDEPENDENT AUDITOR'S REPORT

# Independent auditor's report to the Guernsey Financial Services Commission

We have audited the financial statements of the Guernsey Financial Services Commission ("the Commission") for the year ended 31 December 2012 which comprise the Income and Expenditure Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet, the Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards.

This report is made solely to the Commission, in accordance with our Terms of Engagement as detailed in our letter dated 13 February 2013. Our audit work has been undertaken so that we might state to the Commission, those matters we are required to state in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Commission, for our audit work, for this report, or for the opinions we have formed.

### *Statement of the Commission's responsibilities*

The Commission is required by the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended to prepare financial statements for each financial year which give a true and fair view, in accordance with applicable Guernsey law and United Kingdom Accounting Standards. In preparing these financial statements, the Commission is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Commission will continue to operate.

The Commission is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Commission and to enable it to ensure that the financial statements have been prepared in accordance the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended. It is also responsible for safeguarding the assets of the Commission and hence for taking reasonable steps for the prevention and detection of fraud, error and other irregularities.

### *Respective responsibilities of the Commission and auditor*

As explained more fully above, the Commission is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's ("APB's") Ethical Standards for Auditors.

### *Scope of the audit of the financial statements*

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Commission's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Commission; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### *Opinion on financial statements*

In our opinion the financial statements:

- give a true and fair view of the state of the Commission's affairs as at 31 December 2012 and of its deficit for the year then ended;
- are in accordance with United Kingdom Accounting Standards; and
- have been properly prepared in accordance with the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended.

BDO Limited
Chartered Accountants
Guernsey
20 May 2013

FINANCIAL STATEMENTS

# INCOME AND EXPENDITURE ACCOUNT

For the year ended 31 December 2012

| | Note | 2012 £ | 2011 £ |
|---|---|---|---|
| **Income** | 2 | | |
| Fees receivable | 1(b) | 12,532,222 | 12,596,240 |
| Interest receivable and similar income | 1(c) | 159,456 | 122,162 |
| | | 12,691,678 | 12,718,402 |
| **Expenses** | | | |
| Salaries, pension costs, staff recruitment and training | | 8,767,951 | 7,917,626 |
| GTA University Centre net gain on pension transfer | 7(l) | – | (540,568) |
| Commissioners' fees | | 237,891 | 132,250 |
| Legal and professional fees | | 1,519,846 | 971,282 |
| Premises and equipment, including depreciation | 1(e), 1(g), 4, 10 | 1,333,318 | 1,411,098 |
| Other operating expenses | | 729,769 | 689,077 |
| Other finance costs | 1(h), 7(b) | 204,899 | 42,756 |
| Auditor's remuneration | | 8,750 | 11,236 |
| | | 12,802,424 | 10,634,757 |
| Commission's contribution to expenses of GTA University Centre | 9 | 440,000 | 440,000 |
| | | 13,242,424 | 11,074,757 |
| **(Deficit)/surplus for the year** | | £(550,746) | £1,643,645 |

There is no difference between the deficit for the financial year as stated above and its historical cost equivalent.

*The notes on pages 48 to 55 form an integral part of these financial statements.*

# STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 December 2012

| | Note | 2012 £ | 2011 £ |
|---|---|---|---|
| (Deficit)/surplus for the year | | (550,746) | 1,643,645 |
| Actuarial gain/(loss) | 7(e), (k) | 1,274,589 | (3,436,142) |
| **Total recognised gain/(loss) for the year** | | £723,843 | £(1,792,497) |

*The notes on pages 48 to 55 form an integral part of these financial statements.*

# BALANCE SHEET

As at 31 December 2012

| | Note | 2012 £ | 2011 £ |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 4 | 2,438,323 | 2,522,976 |
| **Current assets** | | | |
| Debtors | 5 | 547,259 | 499,928 |
| Short-term investments | 1(f), 14 | 6,730,106 | 5,847,996 |
| Deposits with States Treasury | 14 | 21,519 | 20,761 |
| Cash at bank and in hand | 14 | 201,124 | 1,743,673 |
| | | 7,500,008 | 8,112,358 |
| Creditors – amounts falling due within one year | 6a | (1,718,945) | (2,368,753) |
| **Net current assets** | | 5,781,063 | 5,743,605 |
| Creditors – amounts falling due after one year | 6b | (70,850) | (39,000) |
| **Net assets before post-retirement liability** | | 8,148,536 | 8,227,581 |
| Post-retirement liability | 7(a), (k) | (6,774,291) | (7,577,179) |
| **Net assets** | | £1,374,245 | £650,402 |
| **Reserves** | 8 | £1,374,245 | £650,402 |

The financial statements on pages 43 to 55 were approved by the Commissioners and signed on their behalf on 20 May 2013 by:

Cees Schrauwers
*Chairman*

Susie Farnon
*Vice-Chairman*

JN van Leuven
*Director General*

*The notes on pages 48 to 55 form an integral part of these financial statements.*

# CASH FLOW STATEMENT

For the year ended 31 December 2012

| | Note | 2012 £ | 2011 £ |
|---|---|---|---|
| **Reconciliation of (deficit)/surplus of income less expenditure for the year to net cash inflow from operating activities** | | | |
| (Deficit)/surplus of income less expenditure | | (550,746) | 1,643,645 |
| Other finance costs | 7(b) | 204,899 | 42,756 |
| Current pension service cost | 7(c) | 798,833 | 838,586 |
| Loss on curtailment | 7(c) | – | 25,641 |
| Gain on settlements | 7(l) | – | (586,209) |
| Contributions made to pension schemes | 7(d) | (532,031) | (724,000) |
| Depreciation on tangible fixed assets | 4 | 404,825 | 412,872 |
| Interest receivable | | (159,456) | (122,162) |
| Increase in debtors | | (47,331) | (89,455) |
| (Decrease)/increase in creditors | | (617,958) | 1,142,274 |
| **Net cash (outflow)/inflow from operating activities** | | £(498,965) | £2,583,948 |
| **Return on investments and capital expenditure** | | | |
| Returns on investments and servicing of finance – interest | | 159,456 | 122,162 |
| Capital expenditure | 4 | (320,172) | (304,318) |
| Management of liquid resources | 1(f), 14 | (882,110) | (1,285,856) |
| **(Decrease)/increase in cash in the year** | | £(1,541,791) | £1,115,936 |
| **Reconciliation of net cash flow to movements in net funds** | | | |
| (Decrease)/increase in cash in the year | 14 | (1,541,791) | 1,115,936 |
| Net funds at 1 January | 14 | 7,612,430 | 5,210,638 |
| Cash outflow from increase in liquid resources | 14 | 882,110 | 1,285,856 |
| **Net funds at 31 December** | 14 | £6,952,749 | £7,612,430 |

*The notes on pages 48 to 55 form an integral part of these financial statements.*

# NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2012

## 1. Accounting policies

### (a) Convention

These financial statements have been prepared in accordance with the historical cost convention and under applicable accounting standards in the United Kingdom. The principal accounting policies which the Commissioners have adopted within that convention are set out below. They have been applied consistently in dealing with items which are considered material to the financial statements of the Commission.

### (b) Fees receivable

Fees receivable are accounted for on an accruals basis.

### (c) Interest

Bank and States Treasury deposit interest is accounted for on an accruals basis. Interest income received on a portfolio of certificates of deposit, is also included, and accounted for on an accruals basis.

### (d) Investigation and litigation

Costs arising from investigation and litigation are accounted for as expenditure is incurred, whether or not it had been billed at the balance sheet date. Such costs recovered from third parties are accounted for in the year in which they are received. No provision is made for expenditure or recoveries which may arise in future years.

### (e) Tangible fixed assets and depreciation

Depreciation on tangible fixed assets is calculated to write down their cost to their estimated residual values over the period of their estimated useful economic lives at the following annual rates:

| | |
|---|---|
| Leasehold improvements | over the shorter of the term of the lease and the estimated useful economic life of the assets |
| Office equipment and fittings | 25% straight-line |
| Furniture | 10% straight-line |
| Computer equipment: | |
| Hardware | 33⅓% straight-line |
| Software | over the shorter of 10 years and the estimated useful economic life of the assets |

### (f) Short-term investments

Short-term investments, represented by a portfolio of certificates of deposit and managed by an investment manager, are actively traded and thus included as current assets irrespective of the maturity date of individual certificates.

### (g) Leases

Rental payments made in relation to office accommodation are treated as operating leases and are charged to the income and expenditure account on a straight-line basis over the lease term.

### (h) Pensions

Employees of the Commission who generally joined before 1 January 2008 are eligible to be members of the States of Guernsey Superannuation Fund ("the Fund") which is a defined benefit pension scheme funded by contributions from both the member and the employer.

A separate Actuarial Account comprising the assets and liabilities of the Fund attributable to the Commission's members ("the scheme") was established with effect from 1 January 2004. Regular valuations are prepared by independent professionally qualified actuaries.

In accordance with Financial Reporting Standard 17 - Retirement Benefits ("FRS17"), the regular service costs of providing retirement benefits to employees during the year, together with any past service costs, are charged to the income and expenditure account in the year.

A debit is included within other finance costs, representing the interest cost on the scheme's liabilities, less the expected return on the scheme's assets, for the year. A credit is included within other finance income where the expected return on the scheme's assets exceeds the interest cost.

The difference between the market value of assets and the present value of accrued pension liabilities is shown as an asset or liability in the balance sheet.

Differences between the actual and expected returns on assets during the year are recognised in the statement of total recognised gains and losses in the year together with differences arising from changes in assumptions and experience gains and losses arising on the scheme liabilities.

## 1. Accounting policies (continued)

### (h) Pensions (continued)

Employees of the Commission joining since 1 January 2008 are generally eligible to be members of the Island Trust Pension Plan ("the DC Plan") which is a defined contribution pension scheme funded by contributions from both the member and the employer. Employer contributions are charged to the income and expenditure account in the year in which they become payable to the DC Plan.

## 2. Income

Income is derived wholly from continuing activities.

## 3. Taxation

The Commission is exempt from the provisions of the Income Tax (Guernsey) Law, 1975 as amended.

## 4. Tangible assets

| | Leasehold improvements | Office equipment, furniture and fittings | Computer hardware | Computer software | Total |
|---|---|---|---|---|---|
| | £ | £ | £ | £ | £ |
| **Cost** | | | | | |
| At 1 January 2012 | 1,272,523 | 404,602 | 498,936 | 1,575,588 | 3,751,649 |
| Additions | – | 34,109 | 101,516 | 184,547 | 320,172 |
| Disposals | – | – | – | – | – |
| **At 31 December 2012** | 1,272,523 | 438,711 | 600,452 | 1,760,135 | 4,071,821 |
| **Depreciation** | | | | | |
| At 1 January 2012 | 70,874 | 125,904 | 411,777 | 620,118 | 1,228,673 |
| Charge for the year | 55,620 | 55,504 | 63,809 | 229,892 | 404,825 |
| On disposals | – | – | – | – | – |
| **At 31 December 2012** | 126,494 | 181,408 | 475,586 | 850,010 | 1,633,498 |
| Net book value at 31 December 2011 | £1,201,649 | £278,698 | £87,159 | £955,470 | £2,522,976 |
| **Net book value at 31 December 2012** | £1,146,029 | £257,303 | £124,866 | £910,125 | £2,438,323 |

## 5. Debtors

| | 2012 | 2011 |
|---|---|---|
| | £ | £ |
| Other debtors | 140.125 | 49,985 |
| Prepayments | 407,134 | 369,241 |
| Amount due from GTA University Centre | – | 80,702 |
| | £547,259 | £499,928 |

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 6a. Creditors – amounts falling due within one year

| | 2012 £ | 2011 £ |
|---|---|---|
| Expense creditors and accruals | 846,378 | 1,220,176 |
| Fees received in advance | 872,567 | 1,148,577 |
| | £1,718,945 | £2,368,753 |

## 6b. Creditors – amounts falling due after one year

| | 2012 £ | 2011 £ |
|---|---|---|
| Expense accruals | 70,850 | 39,000 |
| | £70,850 | £39,000 |

## 7. Superannuation

(i) FRS17 Disclosure for the Guernsey Financial Services Commission Actuarial Account of the States of Guernsey Superannuation Fund

### Employee benefit obligations

This is a defined benefit pension scheme funded by contributions from both the member and the employer which provides retirement benefits based on final pensionable salary. The employer contributions are determined on the basis of independent actuarial advice and are calculated to meet the cost of benefit accrual over the next year of pensionable service.

A separate Actuarial Account comprising the assets and liabilities of the Fund attributable to the Commission's members was established with effect from 1 January 2004 within the Fund following an instruction from the former States Advisory and Finance Committee. The Actuarial Account is used solely for the purpose of determining the contributions payable to the Fund by the Commission and to avoid the possibility of inappropriate subsidisation of one employer by another.

A full actuarial valuation of the scheme was carried out at 31 December 2010 by the scheme's actuary, which resulted in a funding surplus of £1,145,000. An interim actuarial valuation at 31 December 2012 resulted in a funding deficit of £56,000. The scheme's actuary has also completed valuations annually as at 31 December since 2005, for the purposes of FRS17.

The valuation used for FRS17 disclosures has been based on a full assessment of the liabilities of the Fund. The present values of the defined benefit obligation, the related current service cost and any past service costs (if applicable) were measured using the projected unit method.

(a) The amounts recognised in the balance sheet are as follows:

| | 2012 £ | 2011 £ |
|---|---|---|
| Fair value of scheme assets | 15,277,000 | 13,455,961 |
| Present value of funded obligations | (22,051,291) | (21,033,140) |
| **Net pension liability** | £(6,774,291) | £(7,577,179) |

The asset and liability values on the FRS17 basis reflect market conditions at the Commission's year-end date and, as point-in-time calculations, can be expected to vary greatly from year to year, without prejudicing the scheme's long-term ability to provide the required benefits.

## 7. Superannuation (continued)

(b) The amounts recognised in the income and expenditure account are as follows:

| | 2012 £ | 2011 £ |
|---|---|---|
| Interest on obligation | 982,298 | 1,040,352 |
| Expected return on scheme assets | (777,399) | (997,596) |
| Other finance costs | 204,899 | 42,756 |
| Current service cost | 798,833 | 838,586 |
| Loss on curtailment | – | 25,641 |
| Gain on settlement | – | (586,209) |
| Expense recognised in income and expenditure account | £1,003,732 | £320,774 |
| Actual return on scheme assets | £1,303,183 | £(584,759) |

(c) Changes in the present value of the defined benefit obligation are as follows:

| | 2012 £ | 2011 £ |
|---|---|---|
| Opening defined benefit obligation | (21,033,140) | (19,356,128) |
| Current service cost | (798,833) | (838,586) |
| Interest on obligation | (982,298) | (1,040,352) |
| Contributions by members | (255,208) | (289,855) |
| Actuarial gains/(losses) on obligations | 748,805 | (1,853,787) |
| Loss on curtailments | – | (25,641) |
| Gain on settlements | – | 586,209 |
| Net benefits paid including pensions, lump sums, refunds of member contributions and transfer values – general | 269,383 | 109,961 |
| – GTA University Centre | – | 1,675,039 |
| **Closing defined benefit obligation** | (22,051,291) | (£21,033,140) |

(d) Changes in the fair value of scheme assets are as follows:

| | 2012 £ | 2011 £ |
|---|---|---|
| Opening fair value of scheme assets | 13,455,961 | 14,811,865 |
| Expected return on scheme assets | 777,399 | 997,596 |
| Actuarial gains/(losses) on scheme assets | 525,784 | (1,582,355) |
| Contributions by employer | 532,031 | 724,000 |
| Contributions by members | 255,208 | 289,855 |
| Net benefits paid including pensions, lump sums, refunds of member contributions and transfer values | (269,383) | (1,785,000) |
| **Closing fair value of scheme assets** | £15,277,000 | £13,455,961 |

## 7. Superannuation (continued)

### (e) Analysis of amount recognised in statement of total recognised gains and losses ("STRGL")

| | | 2012 | 2011 |
|---|---|---|---|
| | | £ | £ |
| Opening amount of losses recognised in STRGL | | (7,712,308) | (4,276,166) |
| Actuarial gains/(losses) on obligations for the year | 7(c) | 748,805 | (1,853,787) |
| Actuarial gains/(losses) on scheme assets for the year | 7(d) | 525,784 | (1,582,355) |
| Total actuarial gains/(losses) for the year | | 1,274,589 | (3,436,142) |
| **Cumulative amount of losses recognised in STRGL** | | (6,437,719) | (£7,712,308) |

(f) The employer expects to contribute £477,579 to the scheme in the year ended 31 December 2013. Following the actuarial valuation of the scheme as at 31 December 2010, the actuary calculated that the Commission's contribution rate payable to the scheme, to reflect the future service cost, be decreased to 15.6% from 17.8% (the rate recommended by the actuary after the previous actuarial valuation on 31 December 2007). The contribution rate was decreased to 15.6% with effect from 1 January 2012. However, the current service cost, calculated in accordance with FRS17 and representing the cost to the Commission of the benefits accrued to active members of the scheme during the financial year ended 31 December 2012, has been reflected in the Commission's income and expenditure account.

### (g) The major categories of fund assets as a percentage of the total Fund assets are as follows:

| | 2012 | 2011 |
|---|---|---|
| | % | % |
| Equities | 69 | 64 |
| Gilts | 5 | 5 |
| Corporate bonds | 15 | 13 |
| Property | 7 | 10 |
| Other assets | 4 | 8 |

This allocation is at the discretion of the States.

### (h) Long-term principal actuarial assumptions at the balance sheet date (expressed as weighted averages where applicable):

| | 2012 | 2011 |
|---|---|---|
| | % | % |
| Discount rate as at 31 December | 4.7 | 4.7 |
| Expected return on fund assets at 31 December | 5.8 | 5.7 |
| Rate of increase in pensionable salaries | 4.0 | 4.1 |
| Rate of increase in deferred pensions | 3.2 | 3.3 |
| Rate of increase in pensions in payment | 3.2 | 3.3 |

The FRS17 standard refers to a discount rate determined as the current rate of return on high-quality corporate bonds (normally taken to be rated as AA) of equivalent currency and term to the Actuarial Account's liabilities.

## 7. Superannuation (continued)

### (i) Mortality assumptions

The mortality assumptions are based on standard mortality tables which allow for future mortality improvements. The assumptions are that members aged 60 will live on average until age 89 if they are male and until 90 if female. For members currently aged 45, the assumptions are that if they attain age 60 they will live on average until age 90 if they are male and until 92 if female.

### (j) Description of the basis used to determine return on fund assets

The States adopts a building block approach in determining the expected rate of return on the Fund's assets. The States retains full responsibility for the management of the Fund's assets. Historic markets are studied and assets with high volatility are assumed to generate higher returns consistent with widely accepted capital market principles.

Each different asset class is given a different expected rate of return. The overall rate of return is then derived by aggregating the expected return for each asset class over the actual asset allocation for the fund at the disclosure year end.

### (k) Amounts for the current and previous periods are as follows:

| | 2012 | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|---|
| | £ | £ | £ | £ | £ |
| Defined benefit obligation | 22,051,291 | 21,033,140 | 19,356,128 | 16,837,302 | 11,987,385 |
| Fair value of scheme assets | 15,277,000 | 13,455,961 | 14,811,865 | 12,344,058 | 8,424,935 |
| Deficit in the scheme | (6,774,291) | (7,577,179) | (4,544,263) | (4,493,244) | (3,562,450) |
| Actuarial gains/(losses) on scheme assets | 525,784 | (1,582,355) | 793,060 | 940,303 | (2,660,642) |
| Actuarial gains/(losses) on defined benefit obligation | 748,805 | (1,853,787) | (564,879) | (2,793,117) | 1,086,777 |
| Actuarial gains/(losses) recognised in STRGL | £1,274,589 | (£3,436,142) | £228,181 | £(1,852,814) | £(1,573,865) |

The States has confirmed that in the final resort the claims of the Commission's pensioners and employees would be met from the whole Fund and any shortfall in the scheme would then be met by the States from General Revenue.

(l) As a result of the transfer of certain staff, and their pension liabilities, on 31 December 2011, to the employment of the GTA University Centre, a net gain of £540,568 was credited to the income and expenditure account in 2011. This included a payment to the States of Guernsey Superannuation Fund to facilitate a transfer of GTA University Centre pension obligations, on a fully funded basis, partially offset by a contribution by the GTA University Centre. The composition was as follows.

| | 2012 | 2011 |
|---|---|---|
| | £ | £ |
| Gain on settlement | – | (586,209) |
| Loss on curtailment | – | 25,641 |
| Payment to the States of Guernsey | – | 50,000 |
| Contribution by the GTA University Centre | – | (30,000) |
| **GTA University Centre net gain on pension transfer** | – | £(540,568) |

### (ii) FRS17 Disclosure for the Island Trust Pension Plan ("the DC Plan")

The net cost of employer contributions to the DC Plan for the year ended 31 December 2012 was £271,539 (2011: £195,338). Contributions of £2,266 were outstanding as at 31 December 2012 (2011: £12,785). No contributions were prepaid as at 31 December 2012 or 2011. Employer contributions are calculated at 12% of pensionable salary and mandatory employee contributions are at a rate of 5% of pensionable salary.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 8. Reconciliation of movements in reserves

| | | 2012 | 2011 |
|---|---|---|---|
| | | £ | £ |
| Reserves brought forward | | 650,402 | 2,442,899 |
| (Deficit)/surplus of income less expenditure for the year | | (550,746) | 1,643,645 |
| Actuarial gain/(loss) on post-retirement liability | 7(e) | 1,274,589 | (3,436,142) |
| **Reserves carried forward** | | £1,374,245 | £650,402 |

Reserves are stated after deducting the accumulated pension liability of £6,774,291 (2011: £7,577,179) which equates to the post-retirement liability under FRS17 (see note 7).

## 9. GTA University Centre

The GTA University Centre ("GTA") arranges training for the finance industry and for other industry sectors. The company's staff, excluding those joining since 2007, were employed by the Commission and permanently seconded to the company up to 31 December 2011. The Commission provided a grant of £440,000 in 2012 (2011: £440,000) to the company in order to meet approximately 50% of its budgeted net operating expenditure, with £450,000 in 2012 (2011: £470,000) being provided by the States via the Commerce and Employment Department. 2012 was the final year of the grant provided by the Commission.

## 10. Lease commitments

The Commission leased office accommodation at Glategny Court during the year. Cessation of the underlease for Le Marchant House occurred on 10 December 2011. The lease for Glategny Court expires on 16 September 2034 and the rental payable in 2012 under the terms of the lease amounts to £646,338 (2011: £679,820).

Commitments to make payments during the next year in respect of an operating lease are as follows:

### Land and buildings

| | 2012 | 2011 |
|---|---|---|
| | £ | £ |
| Leases which expire more than 5 years after balance sheet date | £646,338 | £646,338 |

## 11. Investigation and litigation costs

As a consequence of fulfilling its regulatory responsibilities, from time to time the Commission undertakes investigations and is a party to legal actions, the costs of which may be significant. No provision has been made in the financial statements for any future costs in respect of current investigations or legal actions because the nature, complexity and duration of such actions remain uncertain.

In a few cases, some or all of the Commission's investigation and legal costs may be recoverable, although not necessarily in the same financial year as the expenditure is incurred. In such cases the recovery is recognised when received.

## 12. Related-party transactions

Peter Harwood was appointed as a Commissioner in August 2004, his term of office expiring on 31 January 2012. He was a partner of Ozannes, now Mourant Ozannes, until 31 December 2009. During the year the Commission engaged Mourant Ozannes to provide certain legal and professional services. These were contracted on an arm's-length basis and are not considered to be significant in the context of the business of the parties.

## 13. Controlling party

In the opinion of the Commissioners there is no controlling party of the Commission, as defined by Financial Reporting Standard No. 8 – Related Party Disclosures, as no party has the ability to direct the financial and operating policies of the Commission with a view to gaining economic benefits from their direction.

## 14. Analysis of changes in net funds

| | At 1 January 2012 | Cash flow | At 31 December 2012 |
|---|---|---|---|
| | £ | £ | £ |
| Deposits with States Treasury | 20,761 | 758 | 21,519 |
| Cash at bank and in hand | 1,743,673 | (1,542,549) | 201,124 |
| **Total cash balance** | 1,764,434 | (1,541,791) | 222,643 |
| Certificates of deposit | 5,847,996 | 882,110 | 6,730,106 |
| **Total funds** | £7,612,430 | £(659,681) | £6,952,749 |

The certificates of deposit are managed as liquid investments and have maturity dates typically between three months and one year after the balance sheet date.

In 2011, the total cash balance was reported as £7,612,430, but has now been restated by presenting separately the short-term investments – certificates of deposit of £5,847,996.

# STATISTICAL DATA - UNAUDITED DATA

## Banking Division

Table 1. **Licences, assets and deposits at the year end**

| End | Banks licensed | Assets £mns | Annual % change in assets | Deposits £mns | Annual % change in deposits |
|---|---|---|---|---|---|
| 1992 | 76 | | | 27,442 | 68.9 |
| 1993 | 75 | | | 37,482 | 36.6 |
| 1994 | 73 | | | 42,191 | 12.6 |
| 1995 | 73 | | | 46,855 | 11.1 |
| 1996 | 72 | | | 43,324 | -7.5 |
| 1997 | 78 | 54,205 | | 49,357 | 13.9 |
| 1998 | 78 | 57,248 | 5.6 | 52,922 | 7.2 |
| 1999 | 79 | 61,620 | 7.6 | 57,059 | 7.8 |
| 2000 | 77 | 72,563 | 17.8 | 68,474 | 20.0 |
| 2001 | 72 | 81,148 | 11.8 | 77,211 | 12.8 |
| 2002 | 67 | 74,760 | -7.9 | 71,943 | -6.8 |
| 2003 | 61 | 72,850 | -2.6 | 69,703 | -3.1 |
| 2004 | 54 | 74,948 | 2.9 | 70,426 | 1.0 |
| 2005 | 50 | 87,482 | 16.7 | 80,728 | 14.6 |
| 2006 | 50 | 100,584 | 15.0 | 92,349 | 14.4 |
| 2007 | 47 | 131,900 | 31.1 | 119,170 | 29.0 |
| 2008 | 48 | 179,117 | 35.8 | 157,009 | 31.8 |
| 2009 | 44 | 135,812 | -24.2 | 117,415 | -25.2 |
| 2010 | 38 | 134,128 | -1.2 | 111,030 | -5.4 |
| 2011 | 35 | 133,586 | -0.4 | 107,545 | -3.1 |
| 2012 | 32 | 114,048 | -14.6 | 86,683 | -19.4 |

Table 2. **Assets and liabilities of licensed banks at the year end**

| | 2005 Total £mns | 2006 Total £mns | 2007 Total £mns | 2008 Total £mns | 2009 Total £mns | 2010 Total £mns | 2011 Total £mns | 2012 Total £mns |
|---|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | | |
| Tier 1 capital* | 1,385 | 1,491 | 1,570 | 1,981 | 2,093 | 2,288 | 2,182 | 1,970 |
| Tier 2 capital** | 21 | 28 | 27 | 52 | 49 | 52 | 28 | 140 |
| Deposits by | | | | | | | | |
| British Isles banks and financial corporations | 11,845 | 16,681 | 20,306 | 20,866 | 23,130 | 25,087 | 23,336 | 19,911 |
| Other banks | 35,265 | 42,757 | 59,582 | 87,490 | 53,827 | 44,966 | 45,199 | 31,258 |
| British Isles public sector | 36 | 48 | 43 | 49 | 39 | 30 | 29 | 36 |
| Companies, persons, other | 32,191 | 31,977 | 38,138 | 45,898 | 37,706 | 38,250 | 36,102 | 32,907 |
| Other liabilities | 6,739 | 7,579 | 12,234 | 22,782 | 18,968 | 23,455 | 26,710 | 27,826 |
| **Total liabilities** | **87,482** | **100,561** | **131,900** | **179,117** | **135,812** | **134,128** | **133,586** | **114,048** |
| Assets | | | | | | | | |
| Loans, advances and market loans with: | | | | | | | | |
| Banks and financial institutions | 59,731 | 71,177 | 86,738 | 111,222 | 78,925 | 79,424 | 79,530 | 70,881 |
| British Isles public sector | 10 | 10 | 10 | 13 | 28 | 25 | 29 | 27 |
| Companies, persons, other | 6,067 | 5,931 | 17,647 | 27,111 | 23,673 | 25,656 | 27,278 | 24,952 |
| Government securities | 6,965 | 5,127 | 3,694 | 3,179 | 2,092 | 2,964 | 1,858 | 1,740 |
| Company shares/securities | 10,337 | 7,085 | 9,894 | 8,580 | 8,913 | 10,709 | 11,645 | 11,933 |
| CDs*** and all other assets | 4,372 | 11,254 | 13,917 | 29,012 | 22,181 | 15,350 | 13,245 | 4,515 |
| **Total assets** | **87,482** | **100,584** | **131,900** | **179,117** | **135,812** | **134,128** | **133,586** | **114,048** |

*Paid-up share capital and disclosed reserves
**Undisclosed reserves, revaluation reserves, general provisions, debt/equity instruments and subordinated debts
***CDs plus FRNS and commercial paper

Figure 1. **Assets at the year end**

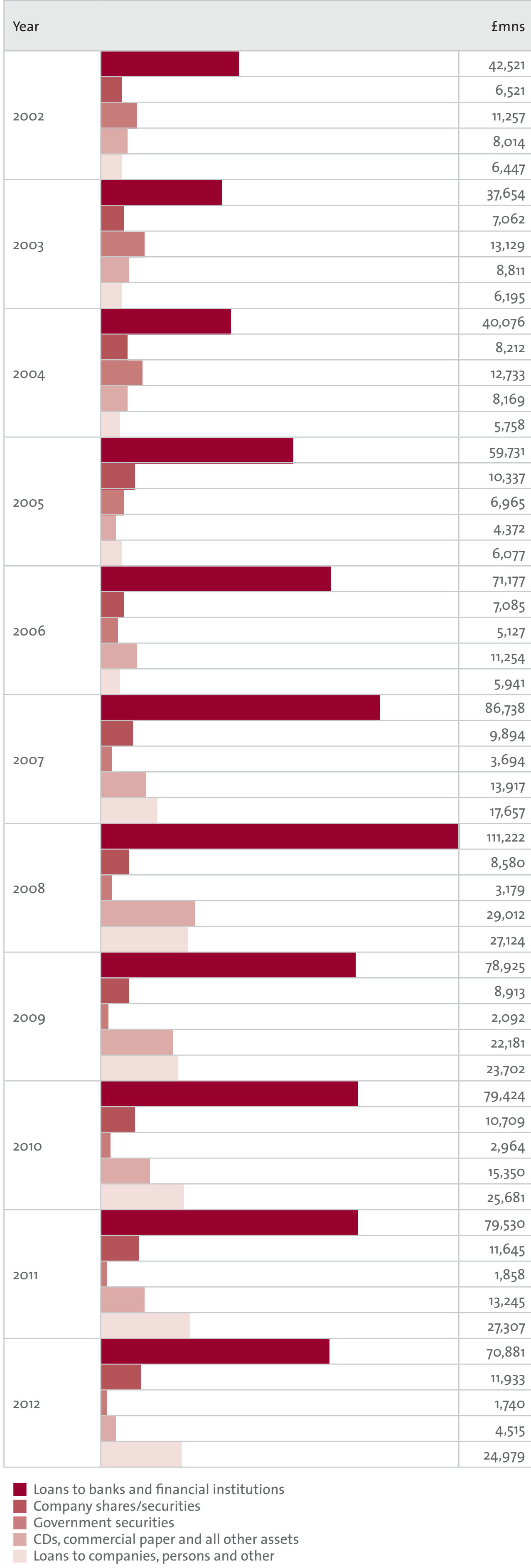



Figure 2. **Analysis of deposits with Guernsey banks by currency at end December 2011**

| Country | % |
|---|---|
| United States Dollar | 51.6 |
| United Kingdom Sterling | 27.2 |
| Euro | 12.9 |
| Swiss Franc | 2.9 |
| Australian Dollar | 1.7 |
| Canadian Dollar | 1.1 |
| Japanese Yen | 0.3 |
| Hong Kong Dollar | 0.2 |
| Other | 2.1 |

Figure 3. **Selected loans and advances since 2008**

| Month | £mns |
|---|---|
| Mar 08 | 2,891 |
| | 2,166 |
| | 2,281 |
| Jun 08 | 3,167 |
| | 2,291 |
| | 2,445 |
| Sep 08 | 2,813 |
| | 2,922 |
| | 2,556 |
| Dec 08 | 3,340 |
| | 3,756 |
| | 2,605 |
| Mar 09 | 2,544 |
| | 3,264 |
| | 2,634 |
| Jun 09 | 2,163 |
| | 2,879 |
| | 2,649 |
| Sep 09 | 2,136 |
| | 2,854 |
| | 2,694 |
| Dec 09 | 2,166 |
| | 2,541 |
| | 2,730 |
| Mar 10 | 2,386 |
| | 2,283 |
| | 2,816 |
| Jun 10 | 2,302 |
| | 2,319 |
| | 2,837 |
| Sep 10 | 2,288 |
| | 2,279 |
| | 3,386 |
| Dec 10 | 2,261 |
| | 2,420 |
| | 3,468 |
| Mar 11 | 2,091 |
| | 2,333 |
| | 3,543 |
| Jun 11 | 2,239 |
| | 2,196 |
| | 3,658 |
| Sep 11 | 2,320 |
| | 2,268 |
| | 3,815 |
| Dec 11 | 2,366 |
| | 2,263 |
| | 3,784 |
| Mar 12 | 2,331 |
| | 2,099 |
| | 3,809 |
| Jun 12 | 2,587 |
| | 2,306 |
| | 3,831 |
| Sep 12 | 2,313 |
| | 2,248 |
| | 3,894 |
| Dec 12 | 2,670 |
| | 2,342 |
| | 3,945 |

Corporate loans
Retail and private client loans
Residential mortgages

Figure 4. **Disposition of bank assets at December 2012**

| Location of bank assets | % |
|---|---|
| United Kingdom | 43 |
| United States | 17 |
| Other European Union | 9 |
| Switzerland | 9 |
| Guernsey | 8 |
| Jersey | 5 |
| Caribbean | 5 |
| Other | 4 |

Figure 5. **Source of bank deposits at December 2012**

| Location of bank deposit | % |
|---|---|
| Switzerland | 34 |
| Guernsey | 34 |
| United States | 9 |
| Jersey | 7 |
| United Kingdom | 5 |
| Caribbean | 3 |
| Ireland | 2 |
| Other European Union | 2 |
| Other | 4 |

Figure 6. **Total Tier 1 capital at the year end**

| Year | £mns |
|---|---|
| 1999 | 1,357 |
| 2000 | 1,715 |
| 2001 | 1,841 |
| 2002 | 1,686 |
| 2003 | 1,585 |
| 2004 | 1,479 |
| 2005 | 1,385 |
| 2006 | 1,491 |
| 2007 | 1,570 |
| 2008 | 1,981 |
| 2009 | 2,093 |
| 2010 | 2,288 |
| 2011 | 2,182 |
| 2012 | 1,970 |

Figure 7. **Country of origin of Guernsey-licensed banks – subsidiaries at end 2012**

| Country | Number of banks |
|---|---|
| United Kingdom | 4 |
| France | 2 |
| Switzerland | 2 |
| Belgium | 1 |
| Bermuda | 1 |
| Canada | 1 |
| Cyprus | 1 |
| Netherlands | 1 |
| South Africa | 1 |
| United States | 1 |

Figure 8. **Country of origin of Guernsey-licensed banks – branches at end 2012**

| Country | Number of banks |
|---|---|
| United Kingdom | 7 |
| Switzerland | 4 |
| France | 3 |
| Germany | 1 |
| Bahrain | 1 |
| Australia | 1 |

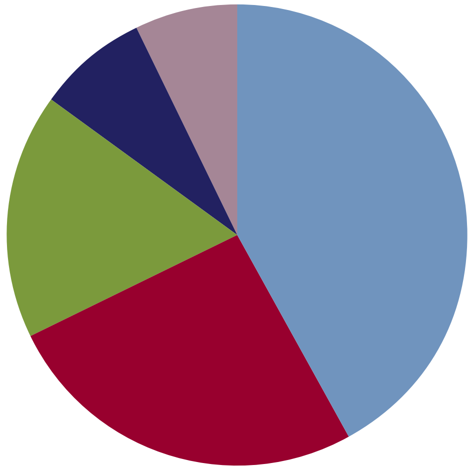
# Fiduciary Division

Figure 9. **Number of licensees in each turnover band based on fiduciary turnover for accounting periods falling in the year ended 30 June 2012***

| Turnover band | |
|---|---|
| <£249,999.99 | 35 |
| | 35 |
| | 36 |
| £250,000 to £999,999.99 | 24 |
| | 27 |
| | 28 |
| £1,000,000 to £1,999,999.99 | 19 |
| | 20 |
| | 18 |
| £2,000,000 to £3,999,999.99 | 24 |
| | 26 |
| | 25 |
| £4,000,000 or over | 25 |
| | 27 |
| | 32 |

*Based on licensees that have submitted audited financial statements. Financial statements may not have fallen due for recently licensed companies.

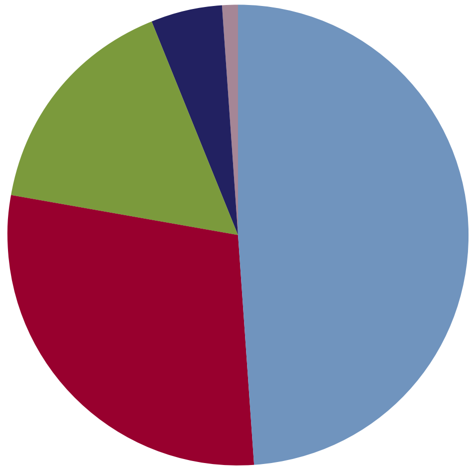
Figure 10. **Ownership of licensees at 30 June 2012***



| | |
|---|---|
| Privately owned - local | 63 |
| International financial group | 39 |
| Lawyers and accountants | 26 |
| Dual licence | 12 |
| Privately owned - overseas | 11 |

*Based on 151 persons holding a full fiduciary licence as at 30 June 2012.

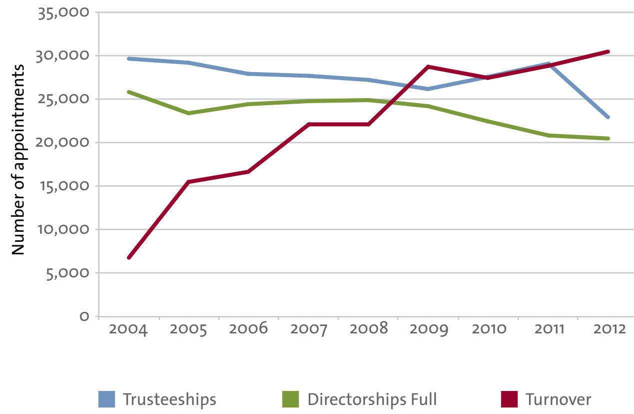
Figure 11. **Number of licensees* per total number of staff carrying out regulated fiduciary activities**



| | |
|---|---|
| Fewer than 10 staff | 74 licensees |
| 11-25 staff | 44 licensees |
| 26-50 staff | 24 licensees |
| 51-75 staff | 7 licensees |
| 76-100 staff | 2 licensees |

*Based on 151 persons holding a full fiduciary licence as at 30 June 2012.

Figure 12. **Director and trustee appointments for full fiduciaries at the year end**



# Insurance Division

Figure 13. **Gross assets**


Figure 14. **Net worth**

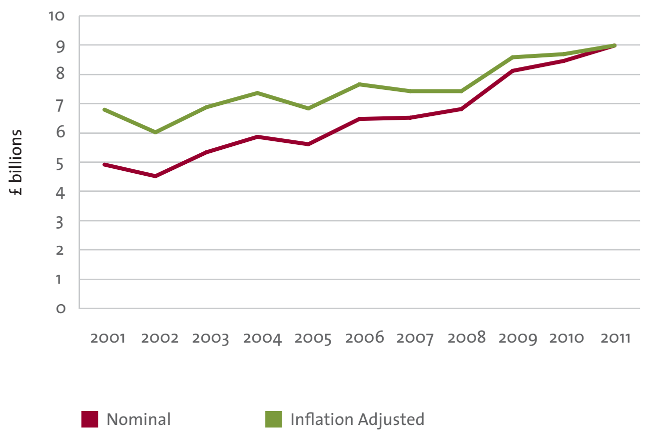



Figure 15. **Gross premiums**

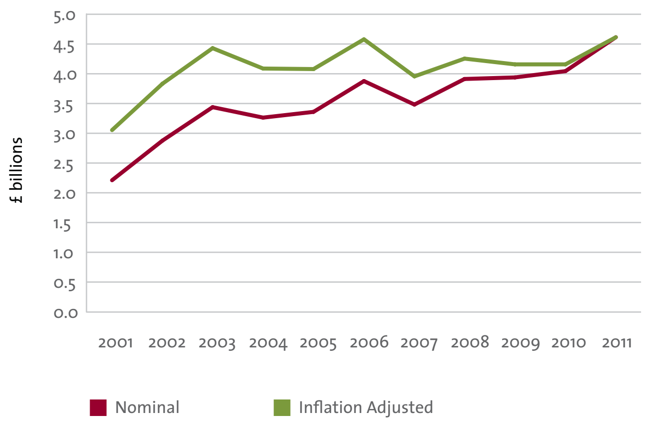



Figure 16. **December 2012: Last 12 months total number of licences issued by type of licence**

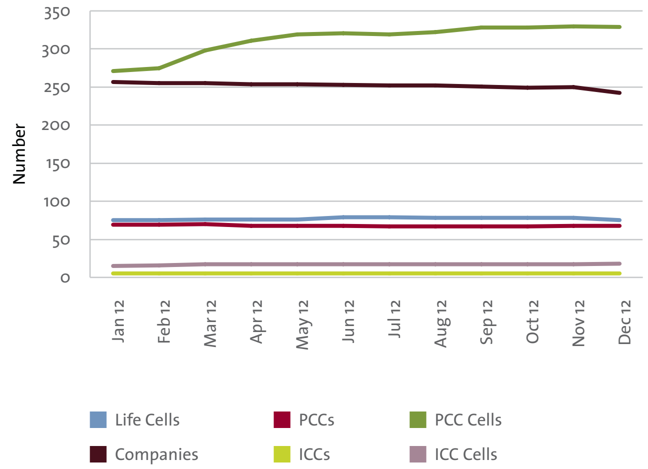



Figure 17. **December 2012: 12-month rolling summary of licences surrendered**

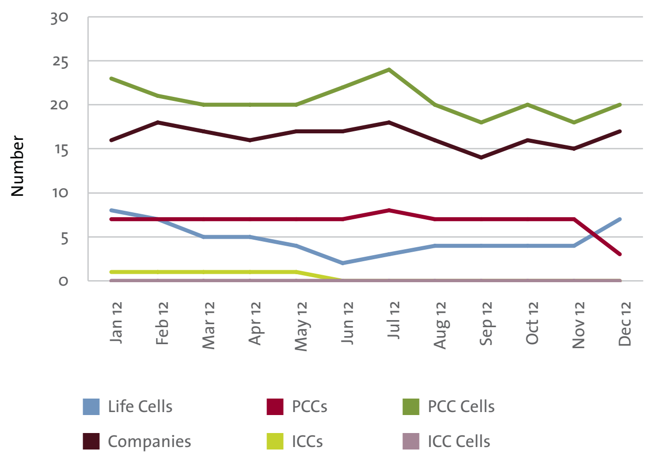
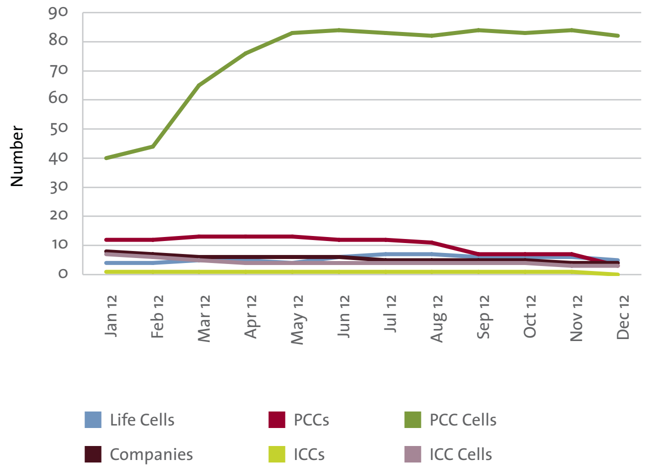



Figure 18. **December 2012: 12-month rolling summary of licences issued**



# Investment Division

Table 3. **New collective investment funds during the year**

| | 2011 | 2012 |
|---|---|---|
| Open-ended funds – authorised/registered | 19 | 13 |
| Open-ended funds – new classes approved | 125 | 217 |
| Closed-ended funds – authorised/registered | 75 | 70 |

Table 4. **Open-ended funds at the year end**

| | 2011 | 2012 | % change |
|---|---|---|---|
| Number of funds | 244 | 222 | -9.0% |
| Number of investment pools | 1,545 | 1,486 | -3.8% |
| Value of assets (£bns) | 55.35 | 50.32 | -9.1% |
| Net new investment over year (£mns) | 5.19 | -3.00 | -157.6% |
| Number of registered holders ('000s) | 53.31 | 51.61 | -3.2% |
| Stock exchange-listed | 144 | 109 | -24.3% |

Guernsey authorised open-ended funds are funds in which shares/units are offered for sale throughout their life and which investors are entitled to redeem on demand subject to any applicable notice period.

Figure 19. **Open-ended schemes – geographic breakdown of investments at year end 2012**

| Country | % |
|---|---|
| United Kingdom | 22 |
| Guernsey | 20 |
| Cayman Islands | 12 |
| USA | 11 |
| Other | 7 |
| Ireland | 4 |
| Luxembourg | 4 |
| Bermuda | 2 |
| France | 2 |
| Japan | 2 |
| Russia | 2 |
| Switzerland | 2 |
| Australia | 1 |
| British Virgin Islands | 1 |
| Canada | 1 |
| China | 1 |
| Denmark | 1 |
| Hong Kong | 1 |
| Jersey | 1 |
| Poland | 1 |
| Thailand | 1 |
| Turkey | 1 |

Figure 20. **Open-ended schemes – analysis by investment style at year end 2012**

| Investment Style | |
|---|---|
| Equity / Securities | 84 |
| Fund of Hedge Fund | 61 |
| Debt | 34 |
| Other | 31 |
| Real Property | 25 |
| Derivatives | 22 |
| Hedge Fund | 21 |
| Money Market / Cash | 18 |
| Emerging Markets | 12 |
| Managed Currency | 9 |
| Balanced | 8 |
| Private Equity | 4 |
| Venture Capital | 1 |

Figure 21. **Nationality of sponsors/joint sponsors of Guernsey open-ended funds at year end 2012**

| Country | |
|---|---|
| United Kingdom | 75 |
| Guernsey | 71 |
| Switzerland | 32 |
| South Africa | 8 |
| United States of America | 8 |
| British Virgin Islands | 6 |
| Cayman Islands | 5 |
| France | 5 |
| Australia | 4 |
| Luxembourg | 4 |
| New Zealand | 4 |
| Bahamas | 3 |
| Canada | 2 |
| Kuwait | 2 |
| Belgium | 1 |
| Hong Kong | 1 |
| Japan | 1 |
| Jersey | 1 |
| The State of Abu Dhabi | 1 |
| Turkey | 1 |

Note: Some funds may have more than one sponsor

Figure 22. **Nationality of sponsors/joint sponsors of Guernsey closed-ended funds at year end 2012**

| Country | |
|---|---|
| United Kingdom | 318 |
| Guernsey | 86 |
| Switzerland | 71 |
| United States of America | 40 |
| Germany | 18 |
| Netherlands | 15 |
| Norway | 13 |
| France | 12 |
| Finland | 10 |
| Cayman Islands | 7 |
| South Africa | 6 |
| Sweden | 6 |
| Turkey | 5 |
| British Virgin Islands | 3 |
| Greece | 3 |
| Japan | 3 |
| Spain | 3 |
| Canada | 2 |
| Czech Republic | 2 |
| Hungary | 2 |
| Israel | 2 |
| Italy | 2 |
| Luxembourg | 2 |
| Portugal | 2 |
| Republic of Ireland | 2 |
| Australia | 1 |
| Bahamas | 1 |
| Belgium | 1 |
| Curaçao | 1 |
| Dubai | 1 |
| Estonia | 1 |
| Hong Kong | 1 |
| Iceland | 1 |
| Isle of Man | 1 |
| Jersey | 1 |
| Kuwait | 1 |
| Lebanon | 1 |
| Russia | 1 |
| Singapore | 1 |
| United Arab Emirates | 1 |

Note: Some funds may have more than one sponsor

Table 5. **Closed-ended funds at the year end**

| | 2011 | 2012 | % change |
|---|---|---|---|
| Number of funds | 610 | 618 | 1.3% |
| Value of assets (£bns) | 119.11 | 130.98 | 9.9% |
| Number of registered holders ('000s) | 68.57 | 70.78 | 3.2% |
| Stock exchange-listed | 217 | 207 | -4.6% |

Guernsey-approved closed-ended funds normally have a fixed capital issued once and for all and investors have no absolute entitlement to redeem their shares/units.

Figure 23. **Closed-ended schemes – geographic breakdown of investments at year end 2012**

| Country | % |
|---|---|
| United Kingdom | 19 |
| USA | 14 |
| Guernsey | 10 |
| Cayman Islands | 8 |
| Luxembourg | 8 |
| Germany | 5 |
| Other | 5 |
| Netherlands | 3 |
| France | 2 |
| Norway | 2 |
| Russia | 2 |
| Sweden | 2 |
| Switzerland | 2 |
| Australia | 1 |
| Brazil | 1 |
| British Virgin Islands | 1 |
| Canada | 1 |
| China | 1 |
| Cyprus | 1 |
| Denmark | 1 |
| Egypt | 1 |
| Finland | 1 |
| Hungary | 1 |
| Ireland | 1 |
| Italy | 1 |
| Japan | 1 |
| Jersey | 1 |
| Mauritius | 1 |
| Poland | 1 |
| Spain | 1 |
| Turkey | 1 |

Figure 24. **Closed-ended schemes – analysis by Investment style at year end 2012**

| Investment | |
|---|---|
| Private Equity | 313 |
| Real Property | 125 |
| Equity / Securities | 68 |
| Other | 54 |
| Debt | 51 |
| Venture Capital | 33 |
| Infrastructure | 24 |
| Derivatives | 15 |
| Fund of Hedge Fund | 15 |
| Emerging Markets | 9 |
| Hedge Fund | 8 |
| Money Market / Cash | 2 |
| Balanced | 1 |

Figure 25. **Total funds authorised and registered at the year end**

| Year | Number of funds |
|---|---|
| 2005 | 584 |
| 2006 | 724 |
| 2007 | 851 |
| 2008 | 919 |
| 2009 | 884 |
| 2010 | 861 |
| 2011 | 854 |
| 2012 | 840 |

Figure 26. **Total Guernsey funds under management at the year end**

| Year | Number of funds |
|---|---|
| 2005 | 79,334 |
| 2006 | 105,139 |
| 2007 | 145,616 |
| 2008 | 155,046 |
| 2009 | 136,079 |
| 2010 | 167,453 |
| 2011 | 174,473 |
| 2012 | 181,310 |

Table 6. **Non-Guernsey schemes at year end**

| | 2011 | 2012 | % change |
|---|---|---|---|
| Number of funds | 308 | 274 | -11.0% |
| Value of assets (£mns) | 87.08 | 95.49 | 9.7% |
| Stock exchange-listed | 35 | 26 | -25.7% |

These open-ended schemes incorporated/established in other jurisdictions are not Guernsey-authorised/approved. However, Guernsey institutions licensed under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 provide management/administration or custody services to such schemes with specific approval from the Commission.

Figure 27. **Number of institutions licensed under the Protection of Investors Law at year end**

| Year | Number of institutions |
|---|---|
| 2005 | 486 |
| 2006 | 554 |
| 2007 | 636 |
| 2008 | 680 |
| 2009 | 661 |
| 2010 | 652 |
| 2011 | 654 |
| 2012 | 644 |

# Enforcement Statistics

## Introduction

The Commission introduced its Enforcement Policy, describing the manner in which it would approach the use of its enforcement powers and sanctions, in cases of regulatory non-compliance. In 2012, a number of regulatory matters were resolved through agreement with the subject concerned, while in a smaller number of cases the following regulatory sanctions were imposed, either with the agreement of the subject or decided upon by the Commission.

| | |
|---|---|
| Warnings | 68 |
| Conditions imposed on licence, authorisation, registration or consent | 9 |
| Requirement to provide information, documents or produce a report concerning identified areas of regulatory concern | 49 |
| Discretionary financial penalties | 1 |

# Finance and Operations Division

Table 7. Income and expenses by sector

| | Banking | | Fiduciary | | Insurance | | Investment business | | Non-regulated financial services businesses and prescribed businesses | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| Number of regulated and registered entities | 32 | 35 | 185 | 183 | 804 | 756 | 1,758 | 1,816 | 162 | 153 | 2,941 | 2.943 |
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Fee income | 1,714 | 1,880 | 2,397 | 2,347 | 3,041 | 2,838 | 5,216 | 5,368 | 164 | 163 | 12,532 | 12,596 |
| Direct costs | (1,358) | (1,286) | (1,570) | (1,431) | (1,952) | (1,857) | (3,773) | (2,693) | (177) | (140) | (8,830) | (7,407) |
| | | | | | | | | | | | | |
| Interest income | 24 | 18 | 29 | 22 | 37 | 28 | 70 | 54 | 0 | 0 | 160 | 122 |
| Common costs | (596) | (480) | (758) | (575) | (925) | (766) | (1,591) | (1,322) | (103) | (84) | (3,973) | (3,227) |
| Surplus/(deficit) | (216) | 132 | 98 | 363 | 201 | 243 | (78) | 1,407 | (116) | (61) | (111) | 2,084 |
| Contribution to costs of GTA University Centre | | | | | | | | | | | (440) | (440) |
| (Deficit)/surplus, net of GTA contribution | | | | | | | | | | | (551) | 1,644 |

Table 8. Salaries and related costs

| | 2012 | 2011 |
|---|---|---|
| | £'000 | £'000 |
| Salaries | 6,584 | 5,944 |
| Consultants/ secondees | 170 | 118 |
| Pension costs | 1,110 | 1,005 |
| Social insurance, permanent health and medical insurance | 637 | 567 |
| Recruitment and training | 267 | 283 |
| **Total** | **8,768** | **7,917** |

Table 9. Number of staff by salary band

| Annual salary | 2012 | 2011 |
|---|---|---|
| £0- £39,999 p.a. | 36 | 30 |
| £40,000 - £79,999 p.a. | 52 | 53 |
| £80,000 - £119,999 p.a. | 10 | 10 |
| £120,000 p.a. and above | 9 | 9 |
| Total number of staff | **107** | **102** |
| Full time equivalent | **102.7** | **97.0** |
| Comprising: | | |
| Full time staff | 89 | 85 |
| Part time staff | 18 | 17 |
| | **107** | **102** |
| Vacancies at year end | 2 | 10 |

Table 10. **Movement in number of staff**

| | 2012 |
|---|---|
| Employed at start of year | 102 |
| Recruited into new positions | 5 |
| Positions removed | (3) |
| Existing vacancies filled | 3 |
| Employed at end of year | **107** |

Table 11. **Legal and professional fees**

| | 2012 | 2011 |
|---|---|---|
| | £'000 | £'000 |
| Legal fees - enforcement | 542 | 308 |
| Legal fees - advisory | 56 | 50 |
| Professional fees - advisory | 45 | 56 |
| Professional fees - other | 123 | 90 |
| Consultancy fees – Independent Evaluation Review and implementation of recommendations | 563 | 434 |
| Consultancy fees – Sentinel programme | 168 | 0 |
| Internal audit | 23 | 34 |
| | **1,520** | **972** |

Table 12. **Commissioners' fees (increase effective October 2011)**

| | | 2012 | 2011 |
|---|---|---|---|
| | | £ | £ |
| Fees paid to Commissioners were as follows: | | | |
| Peter Harwood | Retired as Chairman 31 January 2012 | 2,917 | 25,000 |
| Cees Schrauwers | Appointed Chairman 2 February 2012 | 59,000 | 26,000 |
| Susie Farnon | Appointed Vice-Chairman 1 February 2012 | 38,000 | 17,500 |
| David Mallett | Retired as Vice-Chairman 31 January 2012 | 6,500 | 24,000 |
| Alex Rodger | | 25,000 | 17,500 |
| Lord Flight | | 30,000 | 24,000 |
| Richard Hobbs | Appointed 1 January 2012 | 42,500 | - |
| Robert Moore | Appointed 2 February 2012 | 22,756 | - |
| Paul Meader | Appointed 2 February 2012, resigned 24 February 2012 | 1,923 | - |

N.B. The Policy Council, in anticipation of the increasing input required from Commissioners, wrote to the Chairman of the Commission in January 2012 varying the fee arrangement for Commissioners. The arrangement allowed for *per diem* remuneration of £1,000 for Commissioners for work above the normal time commitment expected from them. The Commissioners waived their rights under this arrangement from 1 July 2012. The Commission expects the amounts for 2013 to be below those of 2012 as a result of completion of the Independent Evaluation Review project. The amount for 2012 also reflects an element of backpay.

# Functions, structure and corporate governance and other control systems of the Commission

## Functions of the Commission

The Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended (the Commission Law) established the Commission with both general and statutory functions. The general functions include the taking of "such steps as the Commission considers necessary or expedient for the effective supervision of finance business in the Bailiwick". The statutory functions include those prescribed under or arising pursuant to the following regulatory laws:

- the Banking Supervision (Bailiwick of Guernsey) Law, 1994 as amended;
- the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended;
- the Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law, 2000 as amended;
- the Insurance Business (Bailiwick of Guernsey) Law, 2002 as amended;
- the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002 as amended.

## Relationship with the States

The States Policy Council is responsible for international financial matters and for establishing the policy framework for financial regulation, including the government's relationship with, and reporting lines for, the Commission. The Commission Law states that the Commission shall issue its audited financial statements and the two reports, referred to later in this appendix, annually to the Policy Council. The Policy Council is also responsible for the administration of the Control of Borrowing Ordinances. Individual officials of the Commission act for the Policy Council in matters requiring consent under the Ordinances.

## The Commissioners

The activities of the Commission's executive are overseen by the members of the Commission (Commissioners). The Commission Law provides that the Commission shall consist of a minimum of five members and a maximum of seven members elected by the States from persons nominated by the Policy Council and appearing to it to be persons having knowledge, qualifications or experience appropriate to the development and supervision of finance business in the Bailiwick. The Chairman is appointed for a period of one year from amongst the Commissioners and is elected by the States following nomination by the Policy Council. The Vice-Chairman is appointed for a period of one year by the Commissioners. Each member is appointed as a Commissioner for a period not exceeding three years. A member whose term of office has come to an end is eligible for re-election. The Chairman and Vice-Chairman are also eligible for re-election to their positions. A member of the Commission must retire on reaching the age of 72 years.

The Commission currently has six Commissioners: Cees Schrauwers, Susie Farnon, Howard Flight, Alex Rodger, Richard Hobbs and Bob Moore. A brief résumé for each Commissioner is provided on pages 4 and 5 of this report. All of the Commissioners are non-executive – three reside in Guernsey, with the remainder living in the UK.

There were 10 meetings of the Commissioners in 2012. The attendance of the individual Commissioners at these meetings was as follows: Peter Harwood 1, David Mallett 1, Susie Farnon 10, Howard Flight 9, Alex Rodger 10, Cees Schrauwers 10, Richard Hobbs 9, Bob Moore 9. Prior to each meeting, Commissioners are provided with a full information pack to support the meeting's agenda.

An induction programme is in place for new Commissioners. The Commissioners periodically consider their roles, responsibilities and accountabilities.

The Commission Law also makes provision for the appointment of such officers and servants as are necessary for carrying out the Commission's functions and for the most senior officer to have the title of Director General.

## Delegation of functions to executive staff

The Commissioners have delegated certain of their statutory functions to the executive staff of the Commission. These statutory functions are exercised by the executives both jointly and severally. All statutory functions of the Commission may be delegated to the executives except:

- the power of the Commissioners to delegate functions;
- the Commissioners' duty to make an annual report on the Commission's activities during the previous year to the Policy Council;
- any statutory functions which:
  - (i) require the Commissioners to consider representations concerning a decision which they propose to take; or
  - (ii) empower the Commission to cancel, revoke, suspend or withdraw a licence, consent, registration, permission or authorisation (except where the cancellation, revocation, suspension or withdrawal is done with the consent of the person who is, or who is acting on behalf of, the holder of the licence, consent, registration, permission or authorisation); or
  - (iii) empower the Commission to petition for the winding-up of a body corporate.

## Annual report and financial statements

The Commission must, as soon as possible in each year, make a report to the Policy Council on its activities during the preceding year. The Chief Minister shall, as soon as possible, submit that report for consideration by the States.

The Commission Law also provides that the Commission shall:

(a) keep proper accounts and proper records in relation to those accounts; and

(b) prepare in respect of each year a statement of accounts giving a true and fair view of the state of affairs of the Commission;

and that the accounts of the Commission shall be:

(a) audited by auditors appointed by the States; and

(b) laid before the States.

The Commission includes a copy of its audited financial statements in the annual report to the Policy Council, referred to above.

## Report on internal control and corporate governance

Under the Commission Law, the Commission must also review in each year, by the appointment of appropriately qualified and independent professional persons or otherwise:

(a) the adequacy and application of the Commission's systems of internal control;

(b) the selection and application of the Commission's accounting policies and accounting procedures;

(c) the effective, efficient and economical management of the Commission's assets and resources; and

(d) the Commission's 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 in connection with the conclusions of each review and provide the Policy Council with a separate annual report on the matters covered by it.

The Commissioners are responsible for overseeing the Commission's corporate governance regime and for monitoring the effectiveness of management's systems of internal control. These systems are subject to regular review by management and address the risks to which the Commission is exposed. The Commission has an ongoing process for identifying, evaluating and managing operational risks (including regulatory and financial risks). In this connection, the Commission takes account of the guidance contained in the UK Code on Corporate Governance.

In accordance with the Commission Law, the Commissioners have reviewed the Commission's approach to risk management policies and processes. The annual report required by the law on internal control and corporate governance has been provided by the Commission to the Policy Council.

## Audit and Risk Committee

The Commission's Audit and Risk Committee, which comprises Alex Rodger and Richard Hobbs (who was appointed in January 2012) and is chaired by Susie Farnon, covers oversight of the management of risk – it reviews corporate governance and the systems of internal control and makes reports routinely to meetings of the Commissioners as a whole. Meetings are usually attended by the Director General, the Chief Operations Officer, the Chief Transformation Officer and the Commission Secretary (who is the committee's secretary). The committee met 5 times in 2012. The attendance of the individual members at these meetings was as follows: Susie Farnon 5, Alex Rodger 5, Richard Hobbs 3.

## Review systems

Rather than appoint its own internal auditor to monitor the Commission's non-regulatory internal audit standards, the Commission has retained specialist external consultants to ensure that the Commission is up to date with current expectations. The corporate governance standards of the Commission have been reviewed by the Audit and Risk Committee and by the Commission's officers. The Commission is satisfied that it meets expectations in connection with internal audit and corporate governance. The International Monetary Fund ("IMF") undertook an evaluation of the Bailiwick with international regulatory and supervisory standard in 2010 under its Financial Stability Assessment Program. The Commission and the other authorities in Guernsey were found by the IMF to have a high level of compliance with these standards.