



GUERNSEY
FINANCIAL
SERVICES
COMMISSION

ANNUAL REPORT & FINANCIAL STATEMENTS 2006

ANNUAL REPORT & FINANCIAL STATEMENTS

For the year ended 31 December 2006

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”.



**GUERNSEY
FINANCIAL
SERVICES
COMMISSION**

GUERNSEY FINANCIAL SERVICES COMMISSION

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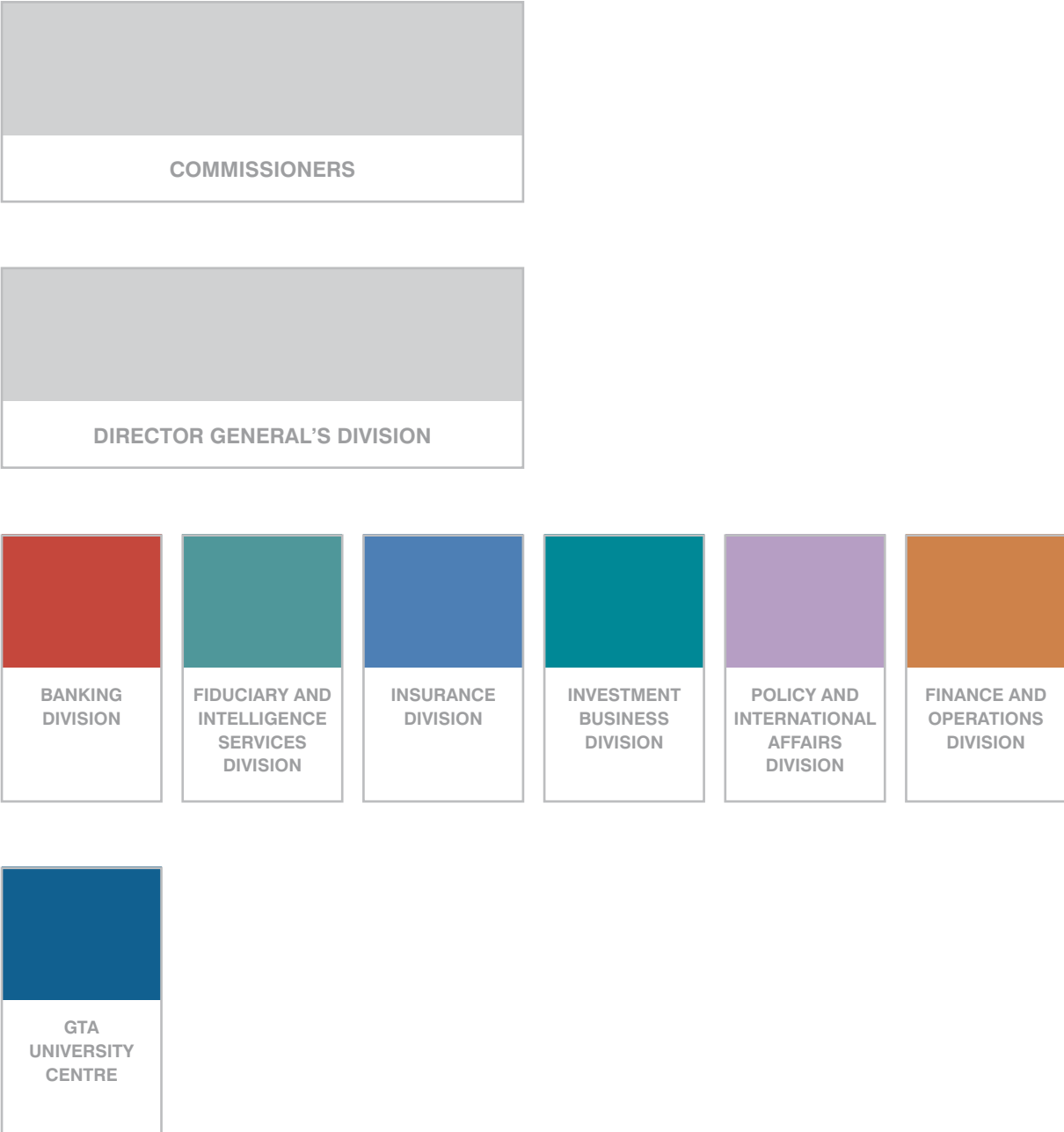
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COMMISSION STRUCTURE



The Guernsey Financial Services Commission is the regulatory body for the finance sector in the Bailiwick of Guernsey.

The Commission's primary objective is to regulate and supervise financial services in Guernsey, with integrity and efficiency, and in so doing help to uphold the international reputation of Guernsey as a finance centre.



PETER HARWOOD LL.B Chairman of the Commission

Peter Harwood was appointed as a Commissioner in 2004. He was admitted as a solicitor of the Supreme Court of England and Wales in 1972 and worked with Coward Chance and Hill Samuel Bank in London, before returning to Guernsey in 1981. He was admitted as an advocate of the Royal Court of Guernsey in 1982 and has been a partner of Ozannes since 1983. He has served as Chairman of the Guernsey Bar Council. He served as Chairman and non-executive director of TSB Bank Channel Islands Limited and as a non-executive director of TSB Group plc. He serves as a director of a number of captive insurance companies and collective investment fund companies.



DAVID MALLET BA, FCA Vice-Chairman of the Commission

David Mallett was appointed as a Commissioner in 2003. He has over 30 years' experience in banking and banking supervision. He joined the Bank of England's Banking Supervision Division in 1975 and was closely involved in the rescue and orderly rundown of a number of failed banks, the development of regulatory practice and a number of national and international accounting and auditing standards. From 1988 to 2000 he was successively Group Head of Audit and Group Head of Finance at Standard Chartered Bank. He has been a member of the Council of the Institute of Chartered Accountants in England and Wales and is co-author of *Banking: A Regulatory Accounting and Auditing Guide*. In 2006 he completed 17 years as a member of the Financial Reporting Review Panel.



MEL CARVILL FCA, CF, ACII, FSI

Mel Carvill has served as a Commissioner for eight years. He is Deputy General Manager, Head of Strategy, Finance and Risk Management, at Assicurazioni Generali SpA and is a director of financial services companies operating in North America, Europe and Asia. He has served as President of the Guernsey Society of Chartered and Certified Accountants, the Insurance Institute of Guernsey and the Guernsey Association of Pension Funds.



SUSIE FARNON FCA

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.



HOWARD FLIGHT MA (CANTAB), MBA, FRSA

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 to the Treasury, Shadow Paymaster General and Shadow Chief Secretary to the Treasury. He led the Conservative opposition during the committee stages of the Financial Services and Markets Act and the Finance Acts between 2000 and 2004. Howard Flight was also co-founder and Managing Director of Guinness Flight Global Asset Management, formed in 1986, and upon its acquisition by Investec in 1998 he became joint Chairman of Investec Asset Management. His career started as an investment adviser at Rothschilds in 1971 and in the second half of the 1970s he worked for the Hong Kong Bank's Merchant Bank in both Hong Kong and India. He pioneered the Managed Currency Fund and the Umbrella Fund structures and in 1988 Sedgwick & Jackson published his book *All You Need to Know About Exchange Rates*. He is currently a director of Panmure Gordon plc, Investec Asset Management Limited and a number of other companies and investment funds.



ROSEMARY RADCLIFFE CBE, MA, MPhil, FIMC

Rosemary Radcliffe was appointed as a Commissioner in February 2006. She is an economist and business consultant. She was for many years PricewaterhouseCoopers' Chief Economist, retiring from PricewaterhouseCoopers in 2001. She continues to undertake high-level project work in the field of economics and policy analysis and has served on a number of United Kingdom government advisory and review bodies, including the Review of Company Law. From 2001 to 2004 she was the first independent Complaints Commissioner for the United Kingdom Financial Services Authority. She is currently a member of the Advisory Panel for the Queen's Award for Industry. Rosemary Radcliffe is a non-executive director of Northern Rock plc and of Newcastle International Airport. She was awarded the CBE in 2001 for services to business competitiveness.



PETER NEVILLE MA (OXON), FCA Director General

Peter Neville read law at Oxford University and is a Fellow of the Institute of Chartered Accountants in England and Wales. Following a period working in the field of insolvency, he spent 12 years as a banker and merchant banker in the United Kingdom and the Far East. He joined the Investment Management Regulatory Organisation in 1987, holding a number of senior positions over a period of seven years. In 1994 he established the investment services regulatory regime for Malta and provided advice on financial services regulation to the government. In 1997 he joined the Regulatory Division of Lloyd's of London as general manager responsible for authorisation, individual registration and conduct of business permissions. He took up the position of Director General of the Commission in April 2001. He is a member of the Executive Committee of the International Association of Insurance Supervisors and the Financial Stability Forum Offshore Financial Centres Review Group.



DIANE COLTON FCII, CHARTERED INSURANCE PRACTITIONER Director of Insurance

Diane Colton started her career with Guardian Royal Exchange and joined the Commission in 1995. She was appointed Deputy Director of Insurance in 2001 and promoted to Director of Insurance in January 2007. She has undertaken work on behalf of the Financial Stability Institute and has worked as a member of the Financial Action Task Force Working Group on Insurance Typologies (which was set up to conduct an analysis into the money-laundering vulnerabilities in the insurance sector). She has also been involved with the Insurance Fraud Subcommittee of the International Association of Insurance Supervisors ("IAIS") in drafting various papers. Most recently she has become the Chair of the Captive Guidance Paper Drafting Group for the IAIS, which is working to publish guidance for captive insurance supervisors.



PHILIP MARR MSC (ECON), CFE Director of Banking

Philip Marr graduated in Economics at the University of Hull in 1968 and joined the Bank of England after a postgraduate degree. He was Economic Adviser to the government of Bermuda from 1974 to 1977 and entered Banking Supervision on his return to the Bank. He was appointed Adviser to the Bahrain Monetary Agency from 1982 to 1984. He was manager of several groups of banks in Supervision at the Bank of England. After a secondment to Hambros Bank in 1988–1989 he was Manager, On-Site Review Teams. He was appointed Senior Manager, Enforcement in 1995 and joined the Commission in June 1997.



PETER MOFFATT MA (OXON) Director of Investment Business

Peter Moffatt joined the Overseas Department of the Bank of England in 1968. International work involved liaison with European Community institutions and the Bank for International Settlements. He was a supervisor during the 1970s and later became Secretary of the City Capital Markets Committee. Leaving the Bank in 1987, he became a compliance officer in investment banking with PaineWebber and JP Morgan and then in investment management with John Govett and Framlington. He has served on legal and regulatory committees of the Association of Investment Trust Companies, the Association of Unit Trusts and Investment Funds and the Financial Services Authority. He joined the Commission in June 2000.



NEVILLE ROBERTS FCA Director of Finance and Operations

Neville Roberts is a Fellow of the Institute of Chartered Accountants. He served articles with Thomson McLintock where, following qualification, he worked in the field of receivership. In 1976 he moved to Ford Motor Co. before transferring to Schroder Life and Unit Trusts as Group Financial Accountant. He came to Guernsey as Director of Finance and Operations for the Schroder international group of companies. For 12 years prior to joining the Commission, he was Head of Finance and Operations for NRG Distribution. In August 2003 he was appointed as the Commission's first Head of Finance and Operations and in February 2007 became Director of Finance and Operations.



STEPHEN TREVOR LL.B, CFE Director of Fiduciary and Intelligence Services

Stephen Trevor read law at Exeter University before qualifying as a solicitor of the Supreme Court of England and Wales in 1991. He practised with Trump & Partners (subsequently TLT Solicitors) in Bristol in commercial litigation, acting for financial institutions in negligence claims against lawyers and other professionals and for insolvency practitioners in contentious insolvency matters. In 1997 he joined the Solicitors Indemnity Fund to settle and defend claims against solicitors' firms. In 1999 he joined the Commission as Assistant to the Director of Fiduciary Services and Enforcement. He was appointed Assistant Director in March 2001, Deputy Director in March 2002 and Director of Fiduciary and Intelligence Services in August 2004. He has served as a member of Guernsey's Trust Law Review and Company Law Reform Committees and is a Certified Fraud Examiner.



RICHARD WALKER BA, CFE Director of Policy and International Affairs

After a period in stockbroking, Richard Walker joined the Commission's Investment Business Division in 1990. In 1997 he was appointed as Assistant to the Director General. The Policy and International Affairs Division evolved from this work and he was appointed Director in March 2006. His role has included involvement in committees on regulation, anti-money laundering and combating the financing of terrorism ("AML/CFT"), and company and trust law. He has undertaken work on behalf of the International Monetary Fund and the Financial Stability Institute on AML/CFT and countering fraud. He also works with the International Association of Insurance Supervisors and the Offshore Group of Banking Supervisors, and is a member of the Financial Action Task Force Money Laundering and Financing Terrorism Trends Working Group.

The statistics in this report illustrate the buoyancy of the financial services sector in Guernsey and demonstrate, in particular, the strong flow of new business into the Island.

During the course of this past year, the Commission has continued to achieve a regulatory regime that is both effective and as non-intrusive as possible.

During his recent visit to the Island, it is gratifying to know that The Lord Mayor of London, Alderman John Stuttard, complimented the Commission on its regulatory approach. The real test for the Commission and for the Island, however, will be the forthcoming assessment by the International Monetary Fund during 2008. Guernsey needs to demonstrate effective regulation, in order to satisfy the international standards by which the Island's international reputation will be judged.

In response to fund industry representation, the States of Guernsey Commerce and Employment Department and the Commission, together, have announced a number of fundamental changes to the process for authorisation of Guernsey investment funds. Those changes have been welcomed by the Guernsey fund industry, which has accepted that it will assume greater responsibility for the pre-vetting of applications for investment funds against a process of self-certification. In allowing the fund industry to assume that responsibility, it is important that the Commission has appropriate enforcement powers to enable it to respond to any failure in the exercise of such responsibility. At present, the only enforcement powers available to the Commission across all its divisions is the "nuclear" option of cancellation, imposition of conditions upon or suspension of a licence. The Commission intends to request the States of Guernsey to consider granting to the Commission a wider range of enforcement powers. Such changes would enable the Commission to continue its switch of emphasis away from pure regulation to more effective levels of supervision.

Evidence of the benefits to be gained from the Commission's effective approach to regulation and supervision was apparent during 2006 when, thanks to the Memorandum of Understanding ("MoU") that had been entered into with the Dutch regulatory authorities, Guernsey incorporated companies were accepted as qualifying for listing on Euronext. Guernsey is one of

only three jurisdictions outside the European Union that benefited from such recognition.

In order to obtain the maximum benefit for Guernsey from the existence of the international regulatory standard-setting bodies, it is necessary for the Commission to enter into global MoUs, which are recognised by each jurisdiction participating in that organisation. One such organisation is the International Organization of Securities Commissions ("IOSCO"). A number of those jurisdictions which compete with Guernsey in the investment sector have already signed-up to the IOSCO Multilateral MoU. Unfortunately, the Commission is not yet able to sign-up to that Multilateral MoU unless it has powers to obtain information (for example, in connection with market manipulation investigations) from persons who may not be regulated or licensed by the Commission. For that reason, the Commission will be asking the States of Guernsey to consider an amendment to the Protection of Investors Law to widen the Commission's ability to obtain information subject to appropriate safeguards and an appeal process. Guernsey's inability to sign-up to the IOSCO Multilateral MoU would place significant sections of the Guernsey finance industry at a disadvantage against their competitors from other jurisdictions.

Once again, I am very grateful for the support I have enjoyed from my fellow Commissioners. The statistics included within Appendix 1 of this report indicate the number of formal meetings of the Commission that were held during 2006. What those statistics do not take account of, however, are the number of non-formal meetings that Commissioners have also attended; in particular ad hoc meetings of Decisions Committees where Commissioners are asked to participate. The decisions procedure that has been adopted by the Commission requires that, where the executive of the Commission is minded to refuse a licence application or impose conditions, the applicant should be given the opportunity to address the Commissioners. This process can be time-consuming, and I am grateful for those Commissioners who have volunteered to participate in that decision process. Even where an application for a licence is refused or where the applicant objects to the conditions that are imposed upon a licence, the applicant has the right to appeal to the Guernsey Financial Services Commission Tribunal. That Tribunal has heretofore operated on a non-statutory basis. The

Commission is, however, anxious to place the Tribunal on a statutory basis and has prepared a consultation document for industry comment, with a view to asking the States of Guernsey to enact legislation that is appropriate to that effect.

During the course of each year, the Commission receives a number of complaints from members of the public or clients of Guernsey regulated entities. Whilst the executive of the Commission will offer assistance to ensure that such complaints are considered at the appropriate level of authority within the relevant organisation, it is not the role of the Commission to act as an Ombudsman, nor is it the function of the Commission to usurp the role of the Courts in determining disputes between clients and their service providers.

Finally, as will be apparent from the business statistics included in this report, 2006 was a very busy year for the Commission, and the Commissioners are extremely grateful, once again, to Peter Neville and the staff of the Commission for the very effective way in which they have undertaken their duties over the past year.

Over the past twelve months, three new Directors have been appointed, all from within the existing staff of the Commission. It is particularly gratifying to know that the Commission has sufficient strength and depth of experience within its own team to be able to satisfy such appointments internally.

Peter Harwood
Chairman

The shape of Guernsey's financial services industry continues to change. During 2006 the total funds under management and administration by the investment sector in Guernsey increased by 30% to £130.2 billion. The number of banks in Guernsey remained unchanged at 50 following a number of mergers, acquisitions and cost-saving rationalisations. However, total deposits rose by 14% during the year to £92.3 billion. The insurance and fiduciary sectors did not see such dramatic shifts but continued to attract good flows of new business.

Guernsey's commitment to innovation continues to play a major role. The Qualifying Investor Fund regime and the listing route created by the recognition by the Dutch authorities of certain categories of closed-end funds have both resulted in significant increases in funds under management and administration. The recommendations made by the working party which considered the future of the investment business sector in Guernsey have been accepted and – to the extent possible before changes are made to the laws – have already been implemented. The resultant new closed-end registered fund vehicle is already generating considerable interest.

INTERNATIONAL

Maintaining Guernsey's international reputation is one of the Commission's main objectives. The Commission seeks to ensure that Guernsey remains a safe and stable environment in which the industry can continue to grow. There are some signs that the more strident and ill-informed criticisms targeted at all offshore finance centres are increasingly being challenged. I have spent a considerable amount of time over the past few years in my role as a member of the Executive Committee of the International Association of Insurance Supervisors ("IAIS"), and in International Monetary Fund ("IMF") and Financial Stability Forum groups, arguing that all finance centres should be assessed on the basis of the same standards and that offshore centres should not be subjected to different requirements. What matters is whether a jurisdiction meets international standards and cooperates effectively, not whether it is onshore or offshore. Although an increasing number of jurisdictions are supporting this view, the pressure on offshore centres to prove they are whiter than white is likely to continue for some time yet. In any event,

the Commission's vigilance in relation to Guernsey's international standing will continue, not least because Guernsey's reputation is one of the main factors in attracting business to the Island.

Indications of the changing attitude of international organisations are apparent in their growing recognition that international financial centres such as Guernsey are an integral part of the global financial system. It is also starting to be recognised that many transactions and products that involve offshore centres originate from and are managed in onshore centres and that problems associated with those transactions and products frequently originate from there too. In the light of this, programmes targeted at offshore centres are looking increasingly anachronistic. Equally, the assessments carried out by international bodies should increasingly resemble those carried out in onshore jurisdictions, by including more testing of the ability of the system within the jurisdiction to withstand economic shocks, particularly where there is substantial cross-border business.

More details of my international work is included in the Policy and International Affairs Divisional report.

ENFORCEMENT ACTION

In 2006 there was increased enforcement activity by the Commission as a number of problem cases progressed to their conclusions. In the fiduciary sector, a former employee of a regulated firm was prohibited from carrying out any function in relation to controlled investment business, deposit-taking business or regulated fiduciary activities.

In the insurance sector, we have uncovered a number of problems, particularly in the intermediary area. The problems principally concerned poor corporate governance, insufficient oversight of the business and inadequate internal and compliance procedures. We are reviewing the insurance laws with a view to clarifying and strengthening them in order to help us address the problems we have been uncovering.

Certain of the proposed changes to laws and regulations are intended to streamline the Commission's supervisory and enforcement processes and make them more effective. This will become increasingly important as the

Commission's efforts are focused on monitoring firms for compliance with a more principles-based and less prescriptive approach.

IMF ASSESSMENT

Preparations for the IMF assessment in 2008 are gathering pace. Each division has outlined in the following reports the work it is currently doing in this respect. The Commission has been liaising closely with industry, the Law Officers and the government to ensure that the programme of work is both understood and supported by all those involved. Although many of the legal and regulatory changes result from developments in international standards, a good number of them – for example, those arising from the recent review of the investment business sector – are being made in order to facilitate the healthy growth of the finance industry in Guernsey.

GTA UNIVERSITY CENTRE

The Commission has always been proud of our relationship with the Guernsey Training Agency ("GTA"), because of the role we played in setting it up, because of our continuing involvement in its financing and governance, and because we employ the staff seconded to it. It was therefore particularly pleasing when the GTA was accredited by Bournemouth University as a university centre and renamed the GTA University Centre in July 2006. This is a tremendous achievement and our warmest congratulations are sent to Professor Richard Conder and his team for all their hard work. The GTA continues to play a vital economic role by providing training for all sectors of the Guernsey economy.

FINANCIAL POSITION

The Commission achieved a substantial financial surplus in 2006, partly as a result of tight cost-control, but also because of the strong flows of new business, particularly in the funds sector. The Commission's reserves have also risen to a satisfactory level as a result of a change in our accounting and billing policies in respect of insurance fees. A prudent but not over-cautious assessment of the prospects in 2007 has enabled us to restrict the increase in fees for

many of the firms we regulate to a rate below inflation in many cases and indeed to avoid any increase at all for other firms. One notable exception to this is in relation to insurance intermediaries, a sector in which a considerable amount of remedial and enforcement action has been necessary. Here, fees have been increased.

Commission staff are members of the States of Guernsey public servants pension scheme. The terms of this scheme are currently subject to a review in which the Commission is taking part. We are giving very careful consideration to the rising costs of meeting the liabilities for existing scheme members, and also to the risks relating to the adding of new scheme members. This work is due to be completed in 2007.

COMMISSION STAFF

At the end of 2006, Alan Fleming, our Director of Insurance, retired. Alan was very active in relation to the Commission's liaison with industry and contributed substantially to the IAIS work on captive insurance, which has stood Guernsey and our local insurance firms in good stead. We wish him a long and enjoyable retirement. I am very pleased to report that Diane Colton has joined the senior management team as the new Director of Insurance. We wish her every success in this challenging position.

I am also very pleased to report two promotions within the senior management team itself. During 2006 Richard Walker was promoted to the position of Director of Policy and International Affairs, and at the beginning of 2007 Neville Roberts was made Director of Finance and Operations. Congratulations to them both.

As always, I am very pleased to record my thanks to the staff of the Commission for their hard work and dedication. It is hoped that we will soon be able to identify new premises which will house the whole Commission, in order to alleviate the problems we are experiencing as a result of overcrowded working conditions and being based in two locations.

Peter Neville
Director General



SECTOR TRENDS

The year 2006 was one of solid progress. Deposit levels recorded at the end of the year, once again, were the highest levels attained. At £92.3 billion, deposits were 14% above the level of £80.7 billion at the end of 2005 (table 1). Driving this increase was a strong increase in deposits from banks, which were up 22%. Within that category, Swiss fiduciary deposits grew by 13%, a more modest pace than in previous years.

The US dollar component of deposits fell back slightly to 37% and the proportion of sterling slipped back to 32%, but the proportion of euro advanced to 25% (figure 1).

Against the wider measure of total liabilities and total assets, the end-year position was more impressive as the sector passed the £100 billion mark for the first time, reaching £100.6 billion at end December 2006 (table 2). That achievement was underpinned by the strong growth in institutional deposits and continued demand for structured products. At the end of the year there were 19 large banks with total assets and liabilities of £1 billion or more, compared with 18 large banks at the end of 2005.

The combined loan book was very slightly down, cash-backed facilities and corporate business made progress and mortgage lending advanced strongly; only lending to persons showed a fall (figure 2). As in previous years, the bulk of assets were placements with banks, usually the head office or banks elsewhere in the group. There were slightly higher holdings of primary liquidity in the form of certificates of deposit and government securities (figure 3).

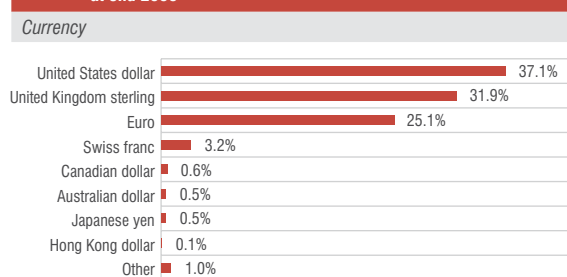
<i>End</i>	<i>Banks licensed</i>	<i>Deposits £mns</i>	<i>Annual change in deposits</i>
1997	78	49,357	+13.9%
1998	78	52,922	+7.2%
1999	79	57,059	+7.8%
2000	77	68,474	+20.0%
2001	72	77,211	+12.8%
2002	67	71,943	-6.8%
2003	61	69,703	-3.1%
2004	54	70,426	+1.0%
2005	50	80,728	+14.6%
2006	50	92,349	+14.4%

As in previous years, the largest proportion (38%) of assets were placed in the United Kingdom, followed by locations elsewhere in the European Union. In 2006 there were higher direct placements with the Caribbean centres rather than indirect placements via group treasury centres located in the City of London (figure 4). The sources of bank deposits were little changed from previous years with deposits, from Switzerland slightly lower, but offset by an increase in deposits from other European Union countries (figure 5).

After the solid recovery in profits in 2005, it was clearly going to be a challenge to improve on the position in 2006, and so it proved. Unfortunately, profits on investments held were down and, together with a marginal decline in net interest income, the overall earnings picture was subdued. Despite this, there was a positive performance from a majority of banks as more banks reported higher profits than reported lower profits.

Tier 1 capital recovered in 2006 by a net £105 million after it had declined the previous year, which had reflected the surrender of several banks' licences and migration of their capital outside the Bailiwick (figure 6). The increase in capital was mainly achieved by the retention of profits, with the aim of building a firmer foundation for further growth of business. There was a modest increase in Tier 2 capital by way of subordinated debt which was needed to underpin further growth in core business by a local bank. The weighted risk asset ratio remained healthy at 18.97%. Figure 7 shows the distribution of locally incorporated banks by risk asset ratio as at the end of the year.

Figure 1. Analysis of deposits with Guernsey banks by currency at end 2006



In comparison with recent years there were very few corporate actions in 2006. The number of licensed banks, at 50, was the same at the end of 2006 as it was at the end of 2005 (table 1). There was one change of name, as the Belgo-Dutch Financial Group changed the name of its local subsidiary from MeesPierson (CI) Limited to Fortis Bank (CI) Limited to reflect group branding better. There was one outright licence surrender as EFG Eurobank Ergasias (CI) Limited discontinued operations in the Bailiwick for economic reasons, as the flow of business initially emanating from Greek shipping sources tailed off and the entity ceased to be viable. Following a decision by the Cheshire Building Society to restructure its offshore funding arrangements, the business of its local subsidiary, Cheshire Guernsey Limited, was sold to the Icelandic bank, Landsbanki Islands hf. Following the change of ownership the bank will trade as Landsbanki Guernsey Limited, with the intention of attracting local and expatriate deposits in order to assist in the financing of the corporate business of the bank's London branch. One new banking licence was issued in 2006 to Clydesdale Bank plc – Guernsey Branch, and we hope this will be a valuable addition to the range of banks established here.

Figures 8 and 9 show the country of origin of the 27 bank subsidiaries and the 23 bank branches licensed at the end of 2006. A list of current licensees is available on the Commission's website at www.gfsc.gg.

SUPERVISION AND POLICY

No changes were made in banking policy applicable to licensed banks in 2006, although much preparatory work was undertaken by the Division on the groundwork for the new Basel II Capital Framework.

The Deputy Director attended three meetings of fellow supervisors from the Jersey Financial Services Commission and the Isle of Man Financial Supervision Commission with a view to achieving a broad consensus approach to Basel II for the three Crown Dependencies. The so-called Tri-party Group produced a paper in May for consultation about National Discretions, which would be allowed under the standardised approach to credit. This, amongst other things, addressed risk weightings of sovereign risk exposures and mortgage lending. After the consultation process a paper setting out the final decisions on National Discretions was published in August. In October a paper was issued on the mapping of external credit assessment institutions ("ECAIs") ratings to risk weights. One of the benefits to banks of adopting the standardised approach is that they will potentially be required to hold less capital in support of holdings of rated securities and loans. In October the Division published Basel II implementation plans setting out the likely timetable for implementation of the Basel II framework. In November the Tri-party Group updated the paper on mapping ECAI ratings and addressed the issue of unsolicited ratings by reputable credit agencies. In that month, the Director

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

	2002	2003	2004	2005	2006		2002	2003	2004	2005	2006
	total	total	total	total	total		total	total	total	total	total
	£mns	£mns	£mns	£mns	£mns		£mns	£mns	£mns	£mns	£mns
Liabilities						Assets					
Tier 1 capital*	1,686	1,585	1,479	1,385	1,491	Loans, advances and market loans with:					
Tier 2 capital**	23	21	23	28	51	Banks, etc.	42,521	37,654	40,077	59,731	71,177
						British Isles public sector	10	5	5	10	10
Deposits by:						Companies, persons, other	6,437	6,189	5,752	6,067	5,931
Banks etc.	13,040	13,811	15,063	16,433	21,480	UK CDs***	5,833	5,497	6,012	2,079	2,705
British Isles public sector	51	44	34	36	48	Government securities	11,257	13,129	12,733	6,965	5,127
Companies, persons, other	58,852	55,848	55,329	64,259	70,822	Company shares/securities	6,521	7,062	8,212	10,337	7,085
Other liabilities	1,108	1,541	3,020	5,341	6,692	Non-UK CDs*** and all other assets	2,181	3,314	2,157	2,293	8,549
Total liabilities	74,760	72,850	74,948	87,482	100,584	Total assets	74,760	72,850	74,948	87,482	100,584

* Paid-up share capital and disclosed reserves

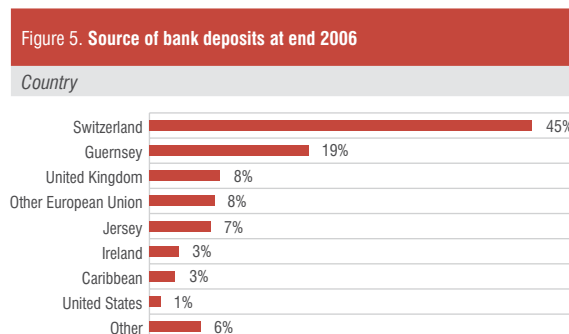
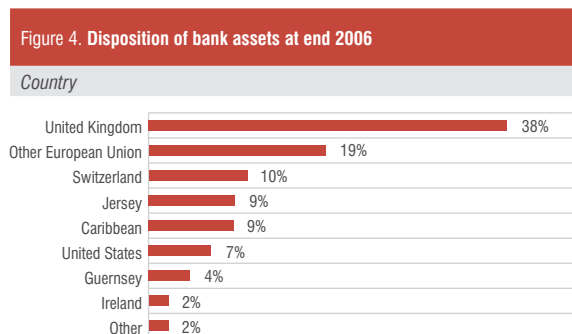
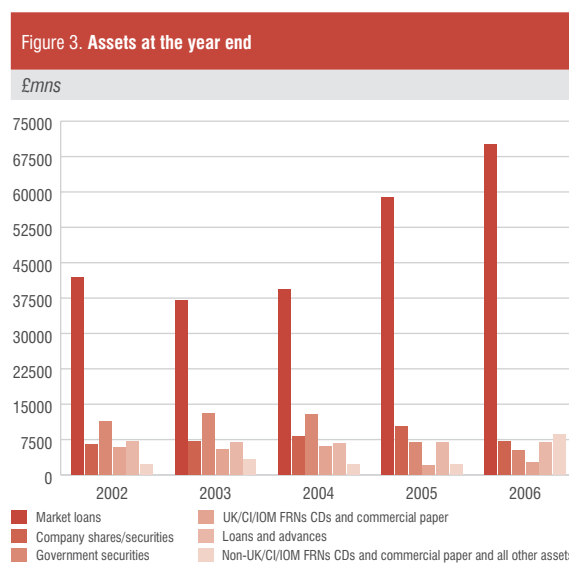
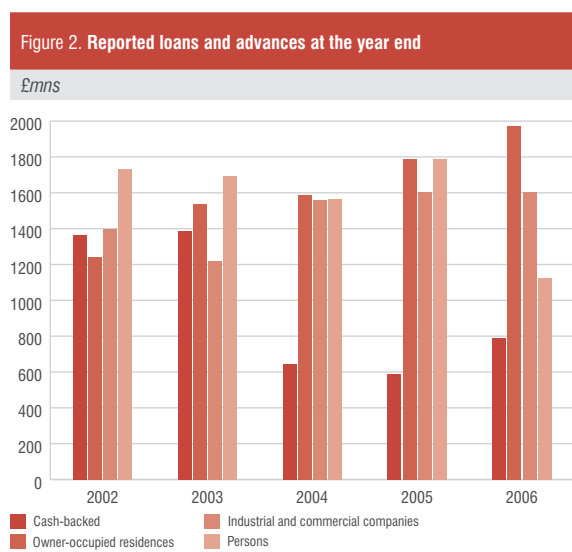
** Undisclosed reserves, revaluation reserves, general provisions, debt/equity instruments and subordinated debts

*** Certificates of deposit ("CDs") plus floating rate notes and commercial paper.

of Banking issued a briefing paper to banks on Pillar 2 risks and a suggested way forward for the supervisory review evaluation process. The intention of that paper was to alert bankers to the issues underlying Pillar 2 and to encourage them to start thinking about what “other” risks should be captured under Pillar 2, which were not already captured under Pillar 1. Amongst several risks, attention was drawn to concentration risk and reputation risk and there was discussion on the sort of issues that would be involved in the internal capital adequacy assessment process (“ICAAP”), which in due course will be a feature of the dialogue between banks and supervisors to agree capital requirements under the new capital framework. The work of the Tri-party Group is continuing in 2007 and initially will seek to achieve a consensus on reporting returns under Pillar 1 standardised approaches.

In preparation for the forthcoming assessment by the International Monetary Fund (“IMF”) of Guernsey

against international regulatory standards, an internal review was conducted of the proposed Revised Core Principles for Effective Banking Supervision issued by the Basel Committee as to whether the Division needed to make any significant changes to its practices in order to reflect those relatively few material changes to the Revised Core Principles which were confirmed in October 2006. The results of that review suggest we should amend the principles on large exposures issued under the Banking Supervision (Bailiwick of Guernsey) Law, 1994 to reflect the need to be consistent in our definitions with that of the standard setter. In terms of our practice we will have to adopt a more focused coverage of liquidity issues and introduce specific coverage of interest rate risk in our prudential meeting programme. We believe it will be sufficient to address the other material changes in the Core Principles by way of surveys: it would be timely to undertake another survey of banks’ business



continuity plans and a repeat survey to produce an up-to-date list of all subsidiaries, branches and sub-branches. Lastly, we will consider using a survey to produce comprehensive information on the extent of outsourcing by banks and the risks identified in those activities and how those risks are managed.

The Division undertook its annual trading book survey in the autumn to determine the extent to which banks were engaging in proprietary trading. The survey confirmed once again that there is very little own-account trading in the Bailiwick and that there was no material increase in such business compared with the previous year.

The programme of on-site credit review visits was continued and 11 such reviews were carried out during the year, slightly more than in 2005. These reviews are only targeted towards those banks where there are significant loan books and where loan books represent a material part of their overall assets. Once again, a feature of the programme this year was to continue to understand how those banks that are active in providing liquidity facilities for the growing funds of hedge funds sector in the Bailiwick make their credit decisions for that specialist business and to what extent those facilities are committed or uncommitted.

The Division also continued its cycle of on-site visits focusing on anti-money laundering (“AML”)/know your customer (“KYC”) standards and fraud prevention. Twenty banks were visited in 2006, somewhat up on the previous year. The principal issues raised during that programme were not that there were unidentified

risks but rather that the documentation of some of those risks was thin and incomplete. Banks were requested to strengthen their documentation of identified risks both at the client take-on stage and in the ongoing monitoring phase.

The programme of prudential supervisory meetings continued in the year and some 49 formal prudential meetings were held with banks’ management on their premises, compared with 49 last year. In addition there were 106 ad-hoc meetings held in Guernsey with banks to discuss various matters, notably strategy, changes in personnel, corporate restructuring, bank and Commission policy and prospective mergers and acquisitions and other corporate actions.

During the year senior members of the Division together with representatives from other Divisions contributed to discussions on the principles to be included in the proposed new *Handbook on Countering Financial Crime and the Financing of Terrorism*.

Once again the Division showed a commitment to training and staff attended a number of courses through 2006. The Division made use of the training opportunities provided by the Financial Stability Institute (“FSI”) in Basel, Switzerland. The FSI was established in 1999 to assist supervisors around the world in improving and strengthening their financial systems. Four staff attended seminars run by the FSI and the Division subscribes to and utilises its online training facility. Staff also attended seminars run by the British Bankers’ Association in London and a number of Guernsey-based courses and briefings on

Figure 6. Total Tier 1 capital at the year end

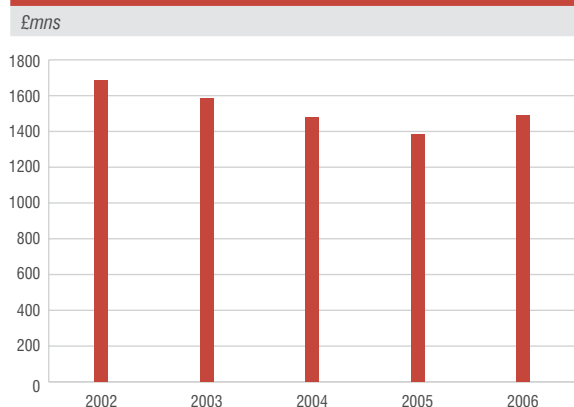
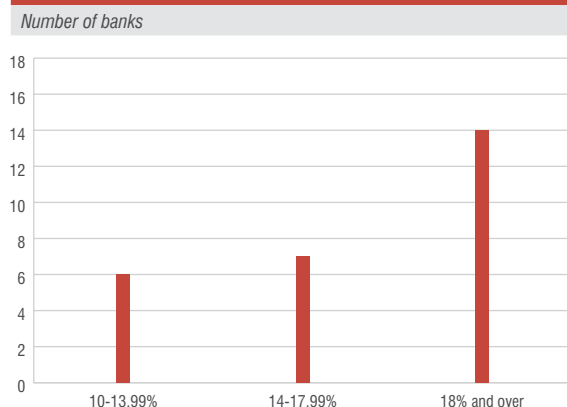


Figure 7. Distribution of locally incorporated banks by risk asset ratio at end 2006



a range of subjects, including AML, fraud prevention, human rights and sex discrimination law.

The Director was pleased to note that during the year one member of staff passed the International Diploma in Anti-money Laundering with merit and another passed a Graduate Diploma in Law with commendation. A further staff member successfully completed the penultimate year of her Law Degree.

INTERNATIONAL DEVELOPMENTS

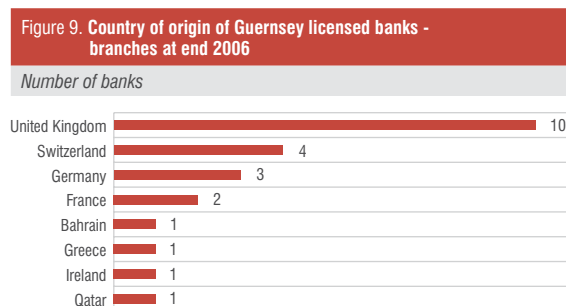
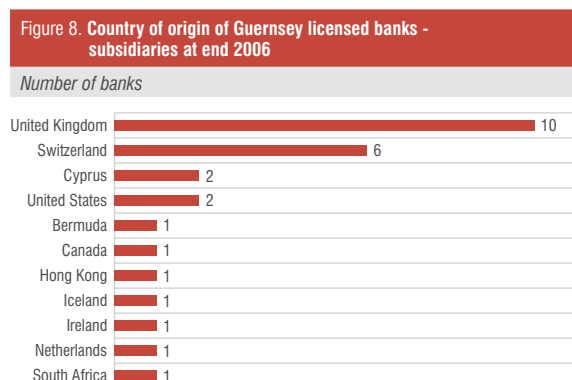
The Director and Deputy Director attended the Offshore Group of Banking Supervisors (“OGBS”) meeting in London in March. This was addressed by representatives of the Basel Committee on Banking Supervision, the IMF, the Financial Action Task Force (“FATF”) and the FSI. There was also discussion on technical issues in electronic banking and core principles. In October, the Director attended the meeting of the OGBS in Mexico ahead of the 14th meeting of the International Conference of Banking Supervisors (“ICBS”). The main themes of the ICBS meeting, which was also attended by the Director General, was the confirmation of the Basel Committee’s Revised Core Principles for Effective Banking Supervision and further discussion on home-host information sharing under Basel II. Other workshops included governance and accountability of financial supervisors, risk-based supervision, corporate governance of banks, stress-testing as a regulatory tool and cross-border cooperation in a problem bank situation.

Bilateral meetings were held with the Swiss Federal Banking Commission, who visited Guernsey in May; the UK Financial Services Authority, who were

visited in November; and with the Bermuda Monetary Authority with whom a meeting was held after the formal proceedings of the OGBS meeting in Mexico. In addition, a further three overseas supervisors visited Guernsey: the Canadian banking supervisor, the Office of the Superintendent of Financial Institutions visited the local subsidiary of one of its banks in September and performed an on-site review visit; and the Federal Reserve Bank of Chicago, together with the State of Illinois Superintendent of Banks, visited in November and also made an on-site visit to the subsidiary of one of its banks.

The Director participated in three meetings of the Working Group on Cross-border Banking. The principal object of the meeting in New York in July was to achieve a consensus on whether to produce a paper on the risk-based approach to the implementation of customer due diligence and AML guidance. It was agreed that the most productive use of the Group’s resources would be to produce a paper on the practical considerations of a risk-based approach to AML/KYC to be input to 2007 sessions of the FATF. It was not thought appropriate to reissue the Group’s paper on customer due diligence for banks published in 2001 since it was believed that, although slightly outdated, nevertheless the principles were still sound and still relevant five years later.

In September the Director attended the ninth Annual Fraud World Conference 2006 in London. Attendance at this annual event enables the Division to keep abreast of developing fraud issues and in this meeting there was relevant discussion of identity fraud and plastic card fraud.





SECTOR DEVELOPMENTS

At the year end there were 147 full and 58 personal fiduciary licensees (2005: 144 and 54 respectively). During the year full licences were issued for the first time to: Active Services (Guernsey) Limited, Aras Trust Company Limited, Bedell Trust Guernsey Limited, Cameron & Cameron Trust Company Limited, Gems Trustees Limited, International Administration (Guernsey) Limited and Mourant Guernsey Limited. These new licensees represent a diverse cross-section of activities, including small trust companies managed by another licensee and Jersey law firms establishing a presence in Guernsey.

SUPERVISION AND POLICY

The first cycle of visits to licensees (other than those only recently licensed) was completed in 2006. This is a major milestone which the Division's licensing team has worked very hard to achieve as the visits have been detailed and labour-intensive. However, they have also proved extremely worthwhile, in particular in developing both our knowledge of the activities of each fiduciary business and relationships with those businesses. We have had a very good level of cooperation and assistance during these visits and, in almost all cases, a mature discussion with the licensee of any issues arising.

Our view from the first cycle of visits is that, contrary to some concerns before the introduction of regulation in 2001, fiduciaries have a very good grasp of whose interests they are representing when administering trusts and companies. Levels of control exercised over those structures have significantly improved, although we still see some files on which further information and/or control should be obtained.

In tandem with completing these visits, we have been developing the format for the second cycle, due to start in January 2007. We presented our thinking and provisional plans to members of the Guernsey Association of Trustees and other licensees in June 2006 and intend to focus particularly on:

- Aspects of client take-on beyond the areas of know your client/verification of identity which we have already examined. This will include review of standard literature about fiduciaries'

services and of information provided to potential clients on how an administered trust or company will operate.

- The management of investments held by trusts and companies, for example when and how external investment advice is used and how performance is monitored.
- Corporate governance within the licensee, for example the content and format of board meetings and the exercise of the board's oversight generally.

In addition, we will be using the second cycle of visits to update ourselves on general developments within each licensee, and to re-visit any issues of concern identified during the first visit to the licensee.

In parallel with onsite visits, the licensing team has continued to have a heavy programme of meetings with licensees on all aspects of their businesses, and to deal with matters arising from formal notifications and review of financial statements and annual returns.

Senior members of the Division have been closely involved in the preparation of the new *Handbook on Countering Financial Crime and the Financing of Terrorism* and in discussions with other Divisions and sector representatives about the principles to be set out in the *Handbook*.

During the year, the Commission made the first prohibition order under the Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law, 2000 prohibiting an individual from future involvement in the sector. Under current legislation, the Commission is not able to publish details of such cases beyond the fact that an order has been made.

In preparation for the International Monetary Fund's assessment of Guernsey against international regulatory standards in 2008, the Division is working on a detailed self-assessment of its powers and regime against the Offshore Group of Banking Supervisors' Statement of Best Practice on Trust and Company Service Providers.

INTERNATIONAL DEVELOPMENTS

In July 2006 the Division hosted a meeting of fiduciary supervisors from the other Crown Dependencies and Gibraltar to discuss standards and trends across those jurisdictions. It is clear that we have many regulatory issues in common and it is, therefore, particularly important that we address them consistently where possible.

LEGISLATIVE DEVELOPMENTS

The Director has been closely involved in the work of groups established by the States of Guernsey Commerce and Employment Department to review the operations of the Companies Registry and other aspects of company law, and trusts law and related matters. These are important projects which will continue into 2007. In relation to the Companies Registry and law, very good progress has been made towards the establishment of a new Registry operating under new companies legislation.

In relation to trusts law, a States report was agreed by the States of Guernsey in December 2006 for legislation to be made in the short term to update the Trusts (Guernsey) Law, 1989. Changes of particular significance to professional trustees will include the introduction of purpose trusts for non-charitable purposes, and the repeal of section 70, which currently imposes concurrent liability on directors of corporate trustees for breaches of trust by the trustee. The working group will also prepare proposals for the Commerce and Employment Department to consider for the establishment of Foundations under Guernsey law. These are structures which discussions with sector representatives had identified as being useful for Guernsey fiduciaries to be able to offer.

COMPANIES

The intelligence team continued to review applications to register all Guernsey and Alderney registered companies. During the year a number of applications had consent withheld or were withdrawn following questions being raised by the team. Examples include applications relating to:

- a person promoting a dubious property investment scheme (which subsequently resulted in him being disqualified as a director in the United Kingdom);
- a United Kingdom-based motor warranty business where the owner was subsequently disqualified as a director in the United Kingdom;
- a cold-calling car sales business, already the subject of bad publicity in the United Kingdom;
- a Middle East defence consultant in circumstances where the risk of corruption had not been fully appreciated by the fiduciary; and
- an investment holding company for a person with a fraud conviction.

A number of other applications were not granted where the intended company was seeking either to conduct financial services outside the Bailiwick or to hold an overseas financial services business. Fiduciaries and their advisers should be aware of the policy, based on guidance given by the former States of Guernsey Advisory and Finance Committee, against the use of local companies in such circumstances. This recognises the risk to the Bailiwick's reputation in the event of problems with the financial services business conducted or owned by the local company, as the Commission would have no control over the finance business which may be unregulated in the jurisdiction where it operates.

INTELLIGENCE

Requests for assistance from overseas regulators led to the intelligence team serving notices under the Regulation of Fiduciaries, Administration Businesses, Company Directors, etc. (Bailiwick of Guernsey) Law, 2000, on two occasions. In one case this was to assist the Dutch regulator, De Nederlandsche Bank, and, in the other, the Australian Securities and Investment Commission. The second case related to a high-profile court action in Australia, which is continuing.

As a result of information received by the team, it provided information to the Japanese Financial Services Agency and issued a warning on the Commission's website about what appeared to be

a pyramid investment scheme falsely claiming to be registered in Sark.

The Assistant Director acts as Money Laundering Reporting Officer for the Commission. A number of reports were made following suspicions being raised when reviewing company applications or as a result of Commission staff coming across suspicious transactions or accounts when visiting licensees.

During the year the Commission's website was updated to reflect changes that had occurred regarding sanctions in force in the Bailiwick. Warnings were also issued in relation to the freezing of suspected terrorist assets and regarding dealings with Belarus.

Many of the above matters, and other areas, involved close liaison throughout the year with the Crown Officers, Guernsey Police, Customs and the Financial Intelligence Service as well as with regulatory bodies in the United Kingdom and elsewhere. The Assistant Director attended regular meetings in London of the Financial Crime Information Network, which exists to share intelligence relating to financial crime.



MARKET PERFORMANCE

International Insurance Market

By the end of 2006 the international market in Guernsey consisted of 312 insurance companies which were operating as either captives or commercial insurance companies together with 68 protected cell companies (“PCCs”) and, following the enactment of specific legislation in 2006, one incorporated cell company (“ICC”). Figure 10 shows the distribution by business sector of these companies. Within the PCCs there were 243 separate cells, which provide insurance in the same way as captive or commercial insurers to a wide variety of international companies and organisations.

During 2006, 51 new international insurance entities (made up of companies and PCC cells) were licensed in Guernsey. Just over 50% of these new insurers were established for UK companies (figure 11). Many of these are for well-known companies, such as the private hire and courier firm Addison Lee, and the property company Land Securities. The specialist construction group Morgan Sindall plc migrated its captive from Bermuda to Guernsey during the year. The parent companies of the remaining 49% of new insurers were based in countries around the world, including Iceland, Israel, Japan, Saudi Arabia and Switzerland. The large proportion of non-UK companies choosing Guernsey as the domicile for their captives demonstrates the continuing attractiveness of Guernsey as an international captive centre.

The size of the insurance market in Guernsey during 2006 has remained stable. This is partly due to the mature nature of the Guernsey market and the low level of major insured losses impacting on the world insurance markets during 2006. In addition, the number of new licences was offset by the large number of mergers and acquisitions. In 2006 insurance rates began to fall and, therefore, Guernsey, in common with captive insurance domiciles worldwide, saw a slow-down in growth.

The prospects for 2007 are encouraging because local insurance managers have indicated that they are optimistic that there will be further interesting business opportunities during the year. The Division is seeing continued innovation in the types of insurance vehicles seeking licensing in Guernsey. Examples of such innovation include cells and companies designed to enable the capital and insurance markets to interact; cells and companies designed to provide insurance for risks which are not able to be insured in the traditional market; and cells designed to provide more cost-efficient insurance protection for both captive and commercial risks.

The Domestic Insurance Market

In addition to the international insurance marketplace, Guernsey has an insurance market which exists to provide insurance services to the local community. At the end of 2006, this market consisted of 48 locally licensed insurance intermediaries and 24 insurers licensed to write Bailiwick of Guernsey-based risks for the local market.

Figure 10. Captives, PCCs and ICCs by business sector at end 2006

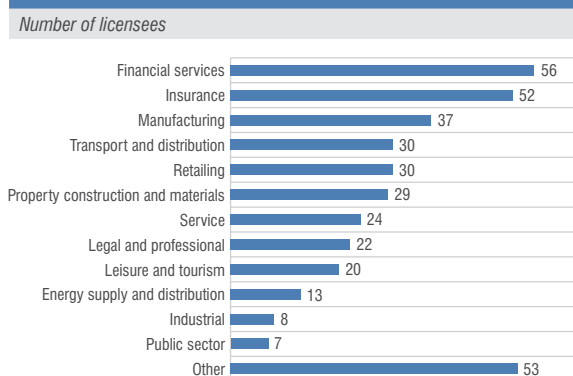
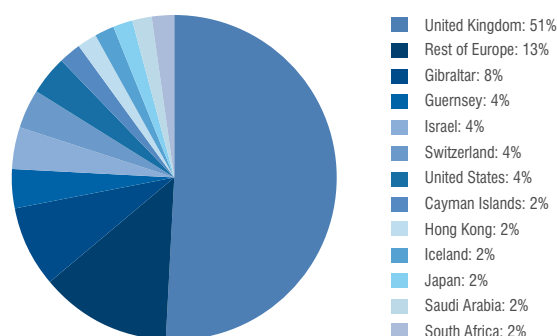


Figure 11. Shareholder location for new captives, PCCs, ICCs and cells licensed in 2006



There was a net increase of four insurance intermediaries. The number of domestic insurers remained at the same level as reported last year, although this is after a year in which there were four new entrants and four licence surrenders.

A full list of currently licensed insurance entities can be found on the Commission's website at www.gfsc.gg.

During 2006 the Commission took regulatory action against a small number of insurance intermediaries. The Commission is committed to ensuring that regulated entities comply with their obligations arising under applicable regulations and will not hesitate to use its regulatory enforcement powers where appropriate.

EDUCATION

The Division continues to support initiatives to improve standards within the sector. The Insurance Education Forum, which was set up by the Commission in conjunction with the Guernsey Training Agency, now the GTA University Centre, and whose members are from a cross-section of industry, met regularly during the course of the year. The stated purpose of the Forum is "to facilitate and exchange views on education and training needs of the insurance sector within the Bailiwick of Guernsey": several training issues have been identified and action taken to address them.

There was extensive cooperation between the Division and the representative bodies of the captive managers and intermediaries as well as actuaries, accountants and chartered secretaries. The Commission is continuing its drive to improve compliance standards by holding seminars and regular meetings with insurance intermediaries during 2007.

Mandatory minimum qualifications for authorised insurance representatives providing advice on long-term insurance products came into force in June 2006. These include a requirement to hold the Guernsey Insurance Certificate.

The Division actively encourages insurance managers and those working in the captive sector to complete the Certificate in Captive Management, which was launched in Guernsey in 2002. Although most applicants are Guernsey-based, more than 50 delegates from other parts of the world, have

applied to obtain this qualification. The Certificate in Captive Management and the Guernsey Insurance Certificate have been granted accreditation by the Chartered Insurance Institute ("CII") and count towards CII qualifications.

SUPERVISION AND POLICY

The Division continued to perform on-site visits in accordance with its three-year rolling programme. These visits are designed to enable the Division to enhance its understanding of licensees and their systems of control. In many cases, it has proved beneficial to perform a "themed" on-site visit, designed to address a specific issue, in order to gain a deeper insight into a particular aspect of the licensee's operations. During 2006, the Division visited 10 insurance intermediaries, 12 insurance managers, six international life companies and two domestic insurers. During each of the visits to the insurance managers several captive insurance companies were reviewed.

Members of the Division also had regular meetings with insurance managers and other licensees to discuss new applications, changes in business plans and other issues, such as capital requirements. Many of these meetings included owners or potential owners of captive insurance companies.

The Division adopts a risk-based approach to monitoring insurance companies, with a risk rating assigned to each company based on a set of standard criteria. This approach allows the Division to focus its resources on the areas of greatest risk and to identify where regulatory action may be required.

The Division continued to monitor developments concerning the Equitable Life Assurance Society ("Equitable Life"). Regular meetings were held with the United Kingdom Financial Services Authority and our lawyers to discuss issues and any developments that might have affected the interests of policyholders of Equitable Life's Guernsey branch. The recommendations of the Parliamentary Ombudsman, following the investigation into Equitable Life, are not now expected until mid-2007. In addition, Equitable Life is being considered by a special committee of the European Parliament.

As part of its preparations for the International Monetary Fund visit in 2008, the Division is currently involved in a comprehensive review of the Insurance Business (Bailiwick of Guernsey) Law, 2002 and the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002, together with the associated Regulations, Guidance Notes and Codes of Practice. In common with any new legislation, experience has highlighted refinements which should be made to the Laws. Several working groups were established under the chairmanship of leading members of the insurance industry to recommend changes to these laws and regulations. The Division has played an active part in these working groups and also chaired the steering group for each law.

Senior members of the Division provided input to discussions regarding the principles to be included in the new *Handbook on Countering Financial Crime and the Financing of Terrorism*.

The Division chairs the Forum for Insurance Development. This body provides an opportunity for representatives of the industry and the Commission to develop plans for the further development of Guernsey as an international insurance centre.

INTERNATIONAL DEVELOPMENTS

Guernsey has a high profile within the international and supervisory standard-setting bodies. The International Association of Insurance Supervisors ("IAIS") is the standard-setting body for the international insurance industry. The Offshore Group of Insurance Supervisors ("OGIS") represents jurisdictions concerned predominantly with cross-border captive insurance business.

It is important that the Commission monitors and influences international trends and developments. It therefore plays a very active role in the committee work of the IAIS. The Director General represents OGIS on the Executive Committee of the IAIS and members of the Division actively participate in IAIS subcommittees, including the Accounting, Implementation, Core Curriculum, and Reinsurance subcommittees. Work has included consultation with the IAIS membership on the draft text for a multilateral memorandum of understanding ("MMoU") for insurance supervision.

This MMoU, once finalised, will lay down a framework for cooperation and the exchange of information between insurance supervisors. The Director General represents the IAIS on the Financial Stability Forum Offshore Financial Centres Review Group. The Director General and the Director of Insurance attended the Triannual Working Party Meetings of the IAIS and represented the Commission and OGIS at the Technical and Executive Committee meetings of the IAIS.

The Deputy Director of Insurance and the Director of Policy and International Affairs are active members of the Insurance Fraud Subcommittee and sat on the drafting group for the guidance paper on insurer fraud. This paper was finalised at the IAIS meeting in Beijing in October. The Division's Actuary is also a member of the IAIS Solvency and Enhanced Disclosure subcommittees. The Solvency Subcommittee is currently developing a worldwide framework for insurance company solvency assessment, whilst the Enhanced Disclosure Subcommittee is developing standards for public disclosure of information on insurance company technical and investment performance.

The Commission liaises closely with members of OGIS and other jurisdictions, to ensure that these IAIS subcommittees are aware of the specific impact of the standards that are being developed on captives and other international insurance companies.

In some major jurisdictions there is still a lack of understanding at senior regulatory level of the role and benefits of captive insurance entities. The Commission led a working party to produce a Captive Issues Paper, which will help in the education and understanding in this field. In addition, the working party included representatives from the following jurisdictions: Bermuda, the British Virgin Islands, Cayman, Dubai, Gibraltar, the Isle of Man, Jersey and Mauritius, and received support and encouragement from several mainstream jurisdictions, including the United Kingdom, Canada, Singapore and Switzerland. The paper is a very useful source of reference for supervisors and covers the history of captive insurance, provides a general overview of the structures of various types of captive insurance entities, gives information about the management

of captive insurance companies and discusses regulatory issues relating to captives. The IAIS adopted the paper in October. Following the interest generated within the IAIS about the paper it was agreed that further work should be carried out to develop a guidance paper. The Director of Insurance is chairing the group which is currently drafting the guidance paper.

During the year the Director made presentations to a number of important captive-related conferences, including the Luxembourg Rendez-Vous in May and the Risk and Insurance Research Group in July. In September 2006, the Deputy Director visited Kazakhstan on behalf of the Financial Stability Institute, to provide training for insurance supervisors on the supervision of intermediaries.



MARKET SENTIMENT

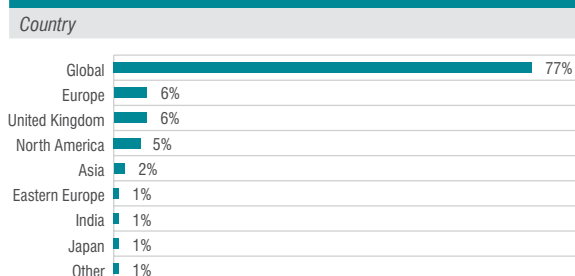
As we have seen over the last few years, continuing economic and political uncertainties have proved no obstacle to the continuing growth of the investment sector. Some volatility in markets has been seen following steps to tighten monetary conditions in certain countries; at the time of writing it is too soon to say whether this will have any long-term effect on the demand for investment funds.

Against that background of strong demand, once again Guernsey fund consents and licence approvals granted by the Division exceeded previous records. In the open-ended sector, a total of 48 new funds and 269 new classes of existing funds were authorised, compared with 40 funds and 155 new classes during the course of 2005 (table 3). We commented last year on the attractions of umbrella and protected cell structures as an efficient means for developing fund ranges, and the remarkable growth in the number of new cells authorised during 2006 reinforces that view. The total value of open-ended funds increased by 17% during the year from £48.2 billion to £56.7 billion. Table 4 and figures 12 to 14 provide an analysis of open-ended funds.

Table 3. New collective investment fund business at the year end

	2005	2006
Open-ended funds – authorised	40	48
Open-ended funds – new classes approved	155	269
Closed-end funds – approved	73	127

Figure 12. Open-ended funds: geographical distribution of investments at end 2006



In the closed-end sector, 127 new funds received consent, compared to 73 new funds in 2005 (table 3). New classes of closed-end funds were less of a feature in 2006, but the Qualifying Investor Fund (“QIF”) regime, initially launched in 2005, continued to show its attractions, with 14 open-ended funds, and 37 closed-end funds, being established in 2006, compared with 12 open-ended and 15 closed-end QIF funds established in the previous year. The total value of closed-end funds increased over the year by 56% from £31.1 billion to £48.5 billion. Table 5 and figures 15 and 16 provide an analysis of closed-end funds.

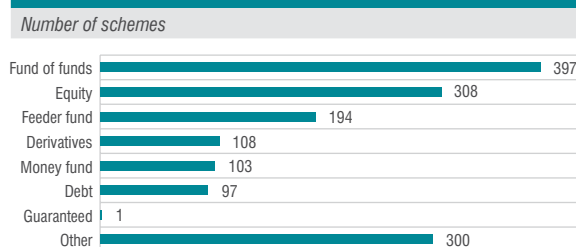
Consents for the administration in Guernsey of funds domiciled in other jurisdictions decreased, to 40 in 2006 compared with 46 in 2005; of those approvals, six were for QIFs against seven in 2005. The total value of non-Guernsey schemes under administration here increased by 21% from £20.7 billion to £25.1 billion (table 6). The trend over time in the number and total value of Guernsey open and closed-end funds and non-Guernsey open-ended funds administered here is shown in figures 17 and 18.

Table 4. Open-ended funds at the year end

	2005	2006	Change
Number of funds	233	270	+15.9%
Number of investment pools	1,103	1,508	+36.8%
Value of assets (£bns)	48.23	56.67	+17.5%
Net new investment over year (£mns)	10,557	8,017	-24.1%
Number of registered holders ('000s)	82.2	76.2	-7.3%
Stock exchange listed	72	87	+20.8%

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.

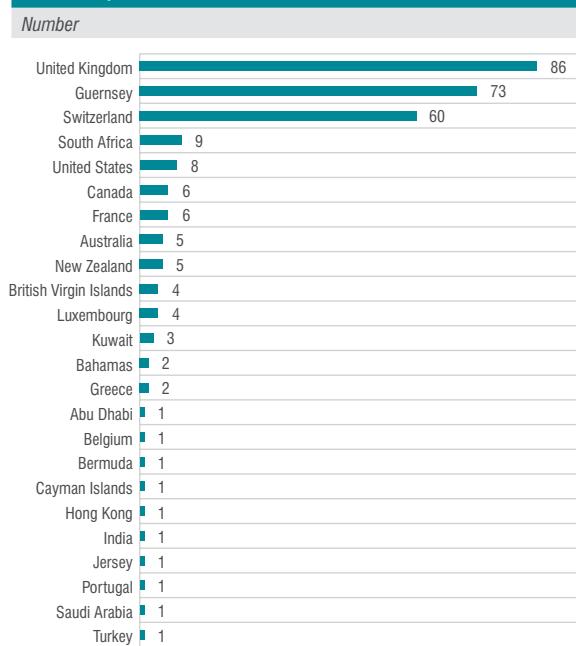
Figure 13. Open-ended funds: analysis by type of investment pool at end 2006



Demand for new investment business licences also increased. A total of 94 new licences were granted during the year, compared with 74 in 2005; new promoters seeking to establish investment vehicles in the Bailiwick increased from 21 in 2005 to 80 in 2006. The net number of institutions licensed under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (“POI Law”) increased to 554 during the year (figure 19). A list of institutions currently licensed under the POI Law can be found on the Commission’s website at www.gfsc.gg.

Towards the end of 2005, as a result of a change to their laws, the Dutch authorities requested a review of the arrangements under which they granted recognition to certain categories of open-ended fund. As a result of that review, the recognition was renewed and also extended to Guernsey-domiciled closed-end funds. A number of fund sponsors put that extended recognition to innovative use, particularly in the area of private equity funds; they were able to establish Guernsey-domiciled limited partnerships and then arrange for the partnership interests to be listed on the Euronext exchange in Amsterdam.

Figure 14. Nationality of sponsors/joint sponsors of Guernsey open-ended funds at end 2006



Note: Some funds may have more than one sponsor

SUPERVISION AND POLICY

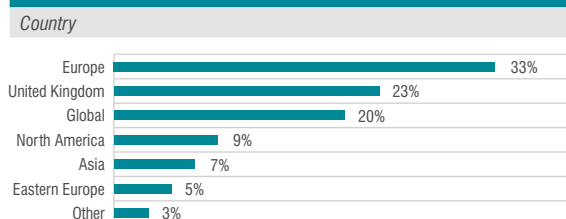
We referred last year to the committee set up under the Chairmanship of Advocate Harwood to report on the investment business sector in Guernsey. This committee, known as the Finance Industry and Policy Working Party, delivered its report to the Commission and to the States of Guernsey Commerce and Employment Department on 21 March 2006. Following a period of consultation, the Division is working with the fund sector to implement the core recommendations of the report, which were, in essence, to create a funds regime in which both open and closed-end funds were given equal treatment, by providing both a “regulated” and a “registered” category for each type of vehicle. In either case it would be a central requirement that the fund was administered by a Guernsey licensed administrator, subject to supervision and monitoring by the Commission. Much of the revised approach will require amendment of the POI Law, but certain policy changes – to establish the concept of the “registered” closed-end fund, and to abolish the requirement for a Principal Manager for open-ended funds – were implemented early in 2007.

Table 5. Closed-end funds at the year end

	2005	2006	Change
Number of funds	351	454	+29.3%
Value of assets (£bns)	31.10	48.47	+55.8%
Number of registered holders ('000s)	37.0	64.5	+74.3%
Stock exchange listed	112	161	+43.8%

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

Figure 15. Closed-end funds: geographical distribution of investments at end 2006



Following initial discussions with the UK Financial Services Authority (“FSA”) and HM Treasury, the Division initiated a project to revise the existing Guernsey Class A open-ended fund rules to bring them into line with more liberal developments in the United Kingdom and the European Union. A revised set of rules has been drafted and is currently being reviewed by an industry group. The next step will involve submission to the United Kingdom FSA for confirmation that the new rules provide equivalent protections to those accorded by United Kingdom rules, followed by a request to HM Treasury for a new Statutory Instrument designating the rules so that

funds operating in accordance with them may be freely marketed in the United Kingdom.

During 2006, the team conducted 31 monitoring and inspection visits. Of those visits: 10 were to designated managers and four to designated custodians of open-ended funds; one to an administrator of non-Guernsey funds; four to closed-end fund administrators; four to brokers and intermediaries; and eight to asset and portfolio managers and advisers. Three visits were conducted in conjunction with the Insurance Division and two with the Fiduciary and Intelligence Services Division. Two were follow-up visits to firms where we

Figure 16. Nationality of sponsors/joint sponsors of Guernsey closed-end funds at end 2006



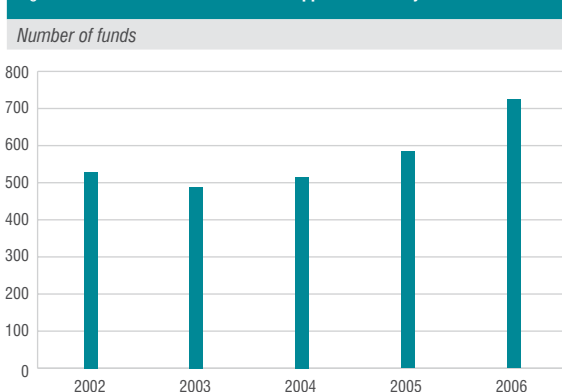
Note: Some funds may have more than one sponsor

Table 6. Non-Guernsey schemes at the year end

	2005	2006	Change
Number of funds	194	217	+11.9%
Value of assets (£bns)	20.71	25.09	+21.2%
Stock exchange listed	35	38	+8.6%

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 17. Total funds authorised and approved at the year end



had earlier identified deficiencies. No restrictions were imposed on licences during the year.

Fund Distribution Limited, the company set up to pay compensation to certain classes of investor in split capital investment trusts, made two distributions to qualifying claimants in 2006 and has effectively now disbursed the £145 million made available to it by contributing firms plus interest earned on those funds. In December 2006 the company took steps to commence closing itself down; the final liquidation process may take a few months. The Channel Islands Splits Adjudication Scheme continued to operate during the period. No new claims are now being accepted, although the Scheme continues to deal with a small number of remaining cases.

In operating the system of investment regulation in Guernsey, the Commission keeps in mind the 30 Principles of Securities Regulation enunciated by the International Organization of Securities Commissions (“IOSCO”), and the associated methodology for assessing compliance with those principles. Following the most recent International Monetary Fund assessment, published in 2003, the development of the IOSCO Multilateral Memorandum of Understanding, which provides a framework for cooperation between regulators, and recent developments in the assessment methodology, the Commission has further reviewed its conformity to the IOSCO 30 Principles. A significant programme of

legislative development is now envisaged to enhance the Commission’s power to obtain information, not solely from licensees, and, subject to suitable safeguards, to share that information with regulatory counterparts. The programme will also clarify the Commission’s right to conduct inspection visits on licensees, and will provide for a broader range of disciplinary action open to the Commission – possibly extending to public censure, administrative penalties and discretionary fines – in addition to the existing powers the Commission has to impose restrictive conditions on licences and, in extremis, to remove a licence completely. That legislative programme will run in parallel with the other legislative changes, outlined above, required to implement fully the recommendations of the Finance Industry and Policy Working Party.

Senior members of the Division provided input to discussions relating to the content of the proposed new *Handbook on Countering Financial Crime and the Financing of Terrorism*.

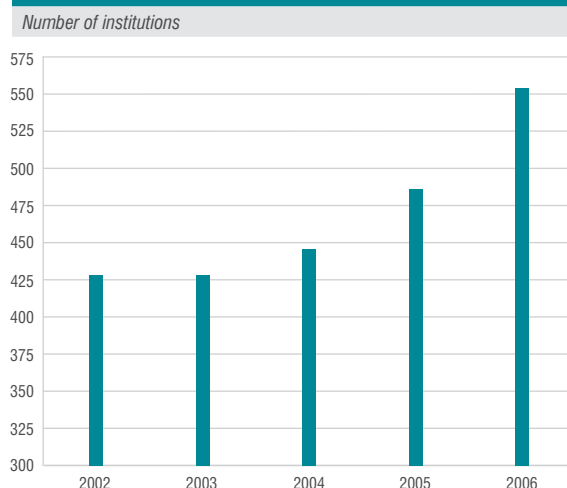
INTERNATIONAL DEVELOPMENTS

International contacts continue to be of central importance in the light of Guernsey’s international business base. During the year the Director General and the Director represented the Commission at the IOSCO Technical Committee policy seminar and the Deputy Director represented the Commission at the

Figure 18. Total funds under management at the year end



Figure 19. Number of institutions licensed under the Protection of Investors Law at the year end



IOSCO annual general meeting. The Deputy Director and one of the Assistant Directors also attended the annual meeting of the Enlarged Contact Group of Collective Investment Scheme Supervisors. The Director and an Assistant Director represented the Commission at the MARHedge European hedge fund summit, where the Director was a panellist for one session. The Director also attended the Annual Conference on Globalisation of Mutual Funds, where he gave a briefing on Guernsey developments, and the GAIM annual forum. In September the Division participated in panels during the first Guernsey Funds conference, held at the QEII Conference Centre in London. Senior staff have also attended seminars organised by the Toronto International Leadership Centre and the US Securities and Exchange Commission's Securities Market Oversight and Enforcement programme.



GENERAL

The Policy and International Affairs Division has responsibility for coordinating many of the local and international policy issues facing the Commission, including changes to legislation. The Division also has day-to-day responsibility for the Commission's anti-money laundering and countering the financing of terrorism ("AML/CFT") framework, including the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism. Together with the Director General, it is the Commission's main link with the Attorney General's Office, the States of Guernsey Policy Council and certain international bodies, including the International Monetary Fund ("IMF"). In addition, the Division coordinates a number of cross-divisional matters such as the preparation of the fees regulations and the production of this annual report, together with the annual report on internal control and corporate governance, referred to in Appendix 1.

COOPERATION

The Bailiwick Financial Crime Committee met twice in 2006. This committee is a forum for closer coordination at a strategic level between the Attorney General's Office, the Commission, Police, Customs and the Financial Intelligence Service ("FIS") in the prevention, detection, investigation and prosecution of economic crime and the countering of terrorist financing. The Director of Policy and International Affairs is secretary to the committee.

The Bailiwick Financial Crime Committee has established a Financial Crime Group. The group's objectives are to discuss the implications for policy and practice of particular cases of interest and to provide practical assistance to interested parties. The group met three times in 2006. The Terrorist Finance Team, which was established by the group to coordinate action and responsibilities relating to terrorism matters, also met three times in 2006.

In November representatives of the Commission took part in four industry-specific half-day seminars for the finance sector on preventing financial crime. The seminars were sponsored jointly by the Commission, the FIS and the Guernsey Police Commercial Fraud

and External Affairs Department. The aim was to provide the finance sector with commentary and case studies on recent and proposed developments locally, and to provide firms with information on common issues arising at on-site inspections by the Commission.

AML/CFT INITIATIVES

During the year, the Division continued to prepare revisions to the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Regulations, 2002 and the Guidance Notes on the Prevention of Money Laundering and Countering the Financing of Terrorism to reflect the most recent changes to the international standards issued by the Financial Action Task Force ("FATF"). The Director General, together with representatives of the Policy and International Affairs Division and the regulatory Divisions, met with the Joint Money Laundering Steering Group three times during the year to discuss the revisions. The Commission proposes to replace the existing Guidance Notes with a *Handbook on Countering Financial Crime and the Financing of Terrorism*, which will contain rules and guidance. The core elements of the Regulations and the *Handbook* will be a risk-based approach and the monitoring of business relationships so that financial services businesses will focus their attention on higher-risk business. The Commission intends to consult with the finance sector on the proposed new AML/CFT Regulations and the *Handbook* in the spring of 2007. The new Regulations and the *Handbook* are important aspects of the preparations for the IMF assessment in 2008.

The Division also devoted significant attention during the year to liaising with the Attorney General's Office and HM Treasury on Bailiwick legislation on wire transfers. In order to maintain Guernsey's position within the United Kingdom's payment and clearing system, Guernsey will enact legislation on wire transfers, which is equivalent to that in the European Union. The Commission consulted with the finance sector on the local legislation in February 2007. The aim is to bring the legislation on wire transfers into force at the same time as the new AML/CFT Regulations and the *Handbook*.

In 2006 the Commission undertook 107 on-site inspections of institutions' AML/CFT frameworks. While all of these on-site inspections which review AML/CFT are undertaken by the regulatory Divisions, the Senior Analyst within the Policy and International Affairs Division responsible for drafting AML/CFT guidance participated with the regulatory Divisions on six inspections. The main purpose of this is to ensure that the Division gains first-hand experience of the practical issues faced by financial services businesses in achieving compliance with the guidance notes.

INTERNATIONAL WORK

As indicated throughout this report, the Commission devotes significant resources to engaging with the international community.

The Director General sits on the Executive Committee of the International Association of Insurance Supervisors ("IAIS") and attended meetings of the IAIS in Basel in February, in Ottawa in May/June and in Beijing in October. Also in October, the Director General, together with the Director of Banking, attended the biennial International Conference of Banking Supervisors in Mexico. The Director General and the Director of Investment Business represented the Commission at the International Organization of Securities Commissions Technical Committee policy seminar in November. Later that month the Director General made a presentation on Guernsey's AML/CFT framework to representatives of the European Commission at a roundtable on Freedom, Justice and Security in Brussels. In December he attended

the fourth IMF Roundtable of Onshore and Offshore Supervisors and Standard Setters.

As the representative of the IAIS, in February, the Director General attended the meeting in Basel of the G7 Financial Stability Forum Offshore Financial Centres Review Group. This group seeks to ensure that offshore financial centres meet international standards.

In June the Director General, together with the Attorney General and the Director of Policy and International Affairs, met with the Commissione Nazionale per le Società e la Borsa in Rome and, with the Director of Investment Business, met with the Autorité des Marchés Financiers. In July the Director General, together with the Attorney General and the Chief Executive of the States of Guernsey, visited the United States and met with the IMF, the United States Treasury, the Department of Justice, the National Association of Insurance Commissioners, the Financial Crimes Enforcement Network, the World Bank and the Law Library.

In June the Director General made the keynote speech at a local conference dedicated to countering fraud. As usual, the Director General spoke at the Cambridge International Symposium on Economic Crime in September.

The Director General also met with the Directors General of the Jersey and the Isle of Man Commissions to discuss matters of common interest to the Crown Dependencies.

Table 7. IMF Coordinated Portfolio Investment Survey 2005
Cross-border securities* owned by institutions in the Bailiwick of Guernsey at end 2005

Sector	Equities US\$ mns	Short-term debt US\$ mns	Long-term debt US\$ mns	Total US\$ mns
Banks	6	5,120	25,376	30,502
Domestic insurers	2	–	34	36
Life insurers	2,455	103	1,401	3,959
Insurance managers and captives	639	2,732	2,716	6,087
Insurance intermediaries	–	–	–	–
Open and closed-end collective investment funds	69,666	3,682	22,425	95,773
Special purpose vehicles	–	13	189	202
States of Guernsey	42	343	278	663
Total	72,810	11,993	52,419	137,222

* The IMF Coordinated Portfolio Investment Survey includes information on cross-border holdings of equities, short-term debt and long-term debt. It does not include other assets, such as cash, derivatives, Islamic investments or property.

In 2007 the Director of Policy and International Affairs represented the Director General on two aspects of the IAIS's work. He participated in the drafting group for the IAIS Multilateral Memorandum of Understanding, which was agreed by the IAIS in February 2007. He, together with the Director of Insurance, participated in the drafting group for the IAIS guidance paper on countering fraud. He also participated in a workshop in Croatia as part of the European Commission's technical assistance programme in February and May and in an AML/CFT technical assistance mission for the IMF in Tunisia in September. In December the Director was a member of the joint Asia/Pacific Group and Offshore Group of Banking Supervisors AML/CFT assessment of Macau.

IMF SURVEY

The Commission provides statistics from Guernsey financial institutions to the IMF for its Coordinated Portfolio Investment Survey ("CPIS") on an annual basis.

Each year, institutions are asked to provide cross-border investment statistics in respect of Guernsey banks, open and closed-end collective investment funds, insurers, insurance intermediaries/brokers and special purpose vehicles. The statistics for 2005 were obtained from 119 institutions, representing 994 entities. Table 7 provides a summary of the results for 2005. The total value of assets reported for Guernsey financial institutions as at 31 December 2005 was

US\$137.2 billion, an increase of US\$3.4 billion over the assets reported in the 2004 survey. Figure 20 shows the results from Guernsey institutions over the last five years. The total value of assets reported has increased each year, although the increase was smaller between 2004 and 2005 than in previous years. There was a US\$23.6 billion (33%) increase in assets reported by investment administrators which partially reflects the increase in the sector but also takes into account the strengthening of the US dollar against the £ sterling during 2005. This increase in assets held by collective investment funds was offset by a decrease of US\$20.3 billion in the assets reported by banks. This decrease was predominantly due to the restructuring by one large institution of its investment portfolio which resulted in a move from investments in assets included in the survey to those not reportable (for example, market loans). Detailed results from the CPIS are available on the Commission's website at www.gfsc.gg.

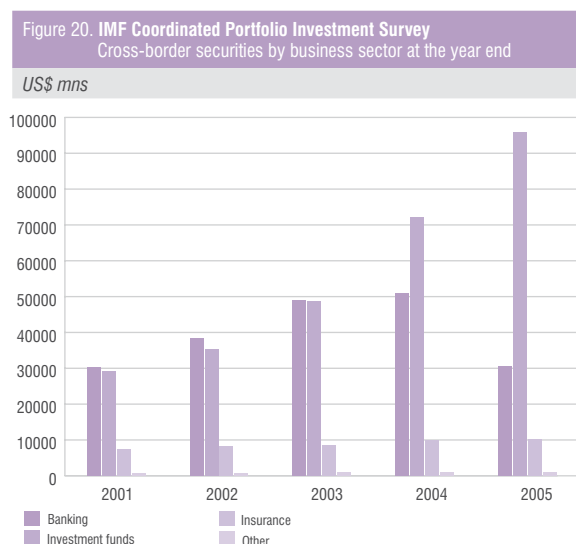
In April 2006 a Senior Analyst from the Banking Division represented the Commission at the IMF's annual workshop for small economies with international finance centres, which was hosted by the government of the Isle of Man.

IMF INFORMATION FRAMEWORK

During the year the Commission participated for the second time in the IMF's information dissemination and monitoring framework initiative (the "Information Framework"). The information provided will help improve transparency in the activities of finance centres around the world and aid the IMF and policy makers in the major countries in formulating a view as to the size, type and global impact of particular finance centres.

Participating jurisdictions provide the IMF with statistics relating to banks, insurers, collective investment funds and company and trust service providers, together with high-level data for the finance sector and the jurisdiction as a whole.

The IMF is now undertaking an evaluation of this initiative. The Commission along with regulatory bodies in other jurisdictions has provided feedback to the IMF regarding its data collection and dissemination



practices, together with comments regarding any difficulties encountered in collating the information requested.

OTHER DEVELOPMENTS

In February and September the Director General and the Director of Policy and International Affairs met with the Guernsey International Business Association (“GIBA”) Council in order to discuss the preparations for the next IMF assessment of Guernsey’s criminal justice and regulatory framework, including the new legislation and the AML/CFT *Handbook*. The Policy and International Affairs Division is coordinating the Commission’s preparations for the IMF assessment.

The Division, together with the Investment Business Division, prepared a consultation document which was issued in December 2006 on proposals for amendments to the Protection of Investors Law, the Financial Services Commission Law and the Insider Dealing Law. The recommendations took into account the proposals made by the Finance Industry and Policy Working Party referred to in the Investment Business section of this report and incorporate amendments to legislation in preparation for the IMF assessment. The main aims of the consultation paper were to enhance the development of the finance sector, to increase investor protection, to assist Guernsey’s finance sector to be fair, efficient and transparent and to reduce systemic risk.

During the year the Policy and International Affairs Division together with the regulatory Divisions continued the programme of work to consider the consistency and appropriateness of regulatory legislation, policies, procedures and controls across the Commission. In light of this work, the Commission intends to issue a consultation document in mid-2007 on revised appeals processes, enhanced enforcement powers and modifications to the minimum criteria for licensing in the regulatory laws.

During 2005 the Director General brought together representatives of the Citizens Advice Bureau, GIBA, the Guernsey Press, the Guernsey Training Agency (now the GTA University Centre) and the States Education Department to form the Guernsey Financial Literacy Advisory Group (“G-FLAG”). The group is a

catalyst for improving the ability of young people and adults in Guernsey to make informed judgements and to take effective decisions regarding the use and management of their money. The group is chaired by the Director General – the Director of Policy and International Affairs is its secretary. In September 2006 the Guernsey Institute of Directors and G-FLAG hosted a seminar for representatives from Guernsey’s education establishments and employers on “Bridging the Gap – A Discussion of School-Work Partnerships” with the aim of strengthening the links between schools – their teachers, their curricula and their students – and employers.



GENERAL

The Division is responsible for key support services to the Commission and is divided into four departments: finance, information and communication systems, human resources and facilities management.

FINANCE

The financial statements are shown on pages 48 to 60. At the end of 2006 the Commission changed its policy in relation to the collection of certain insurance fees, moving from collecting in arrears, based on licensees' accounting year-end dates, to collecting in advance for the calendar year. This change in policy more aptly reflects the time at which the Insurance Division provides its services to the industry. The Commission has therefore raised invoices for the previously unpaid period to December 2006. If the Commission had always adopted a policy of invoicing in advance, then all of this additional income would have been recognised in prior years' accounts. The additional income generated therefore needs to be accounted for as a prior-year adjustment in the 2006 financial statements (see note 9), and necessitates a restatement of the 2005 comparative figures in the financial statements.

The overall surplus for the year is £921,472, a significant increase compared to 2005. This is primarily as a result of increased fee income due to a substantial growth in business activity across some of the business sectors, notably in fund management. The total fee income for 2006 was £7,988,020, a 10.8% increase over 2005 (prior to restatement).

The Commission continued to incur significant legal and professional costs in respect of investigative and enforcement activity. These costs together with the impact of the Financial Reporting Standard 17 ("FRS 17") valuation of employer contributions, offset by robust cost control elsewhere, resulted in expenses for the year ended 31 December 2006 being £7,740,759, an increase of 7.5% compared to 2005.

The year 2006 is the second year of adoption by the Commission of FRS 17 on Retirement Benefits in its financial statements. The deficit in the scheme at the end of the year on the FRS 17 valuation basis is £1,197,992, which is similar to the deficit shown in the scheme for 2005.

The Commission's policy to retain reserves at a sum equivalent to a minimum of six months' expenditure remains in place. The aim is for the Commission to be able to absorb unexpected or exceptional costs without putting its solvency at risk. However, when setting fees for 2007, the Commission has once again borne in mind the commercial environment in which regulated firms operate and it is not anticipated that the surplus achieved for 2006 will be repeated in 2007. The majority of fees have either been held at the same level as in 2006 or have been increased at a rate well below the increase in the Guernsey retail price index for 2006. There are a number of external factors that could affect the Commission's expenditure in future. These include potential developments regarding the States of Guernsey pension scheme and the approach to be adopted towards the accounting treatment of the retirement benefits.

The Commission continues its close relationship with the GTA University Centre ("GTA"), previously the Guernsey Training Agency. It contributed 50% of the GTA's budgeted net operating expenditure in 2006 (£411,000) and has committed to provide funding at the same level of £411,000 in 2007.

Fee Legislation

Revised fee regulations came into effect on 1 January 2007. The following regulations apply to fees payable by the finance sector in Guernsey:

The Financial Services Commission (Fees) Regulations, 2006

The Protected Cell Companies and Incorporated Cell Companies (Fees for Insurers) Regulations, 2006

The Regulation of Fiduciaries (Fees) Regulations, 2006

The Amalgamation of Companies (Fees) Regulations, 2000

The Migration of Companies (Fees) (Amendment) Regulations, 1999

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

INFORMATION AND COMMUNICATION SYSTEMS

Information systems remain critical to the Commission's operation and enhancements have once again been made to its central regulatory database during the year. We have also reviewed the Commission's future requirements for information and communication systems and expect to implement further significant enhancements in 2007.

HUMAN RESOURCES

At the beginning of 2006, the Commission's permanent headcount was 86. A further analyst was recruited during 2006 to assist with the increased workload in the Investment Business Division. The Commission also appointed an existing contract employee to the permanent staff, bringing the permanent headcount to 88. The Commission also had two contract employees throughout the year, and the GTA had 13 staff seconded to it by the Commission. The GTA employs its Chief Executive directly.

In March 2006 Richard Walker was promoted to Director of Policy and International Affairs. Following the retirement of Alan Fleming as the Director of Insurance at the end of 2006, Diane Colton was promoted to Director in his place. The subsequent vacancy of Deputy Director of Insurance has been filled by the appointment of Michael Graham. At the beginning of 2007 Neville Roberts was made Director of Finance and Operations.

The Commission is keen to support its employees with their continuing professional education and we are pleased to announce that seven staff attained relevant professional qualifications in the year, with a further seven currently undertaking professional studies. The Commission remains committed to the development and training of staff, to maintain the quality of the Commission's work and to further each individual's career development.

Commissioners

In January 2007 the States of Guernsey re-elected Peter Harwood as Chairman of the Commission for a further one-year term commencing on 2 February 2007 and re-elected Susie Farnon as a Commissioner for a three-year period from the same date.

FACILITIES MANAGEMENT

The premises at La Plaiderie Chambers and Le Marchant House are at full capacity and it remains a long-term objective of the Commission to move to a more efficient, single location when circumstances allow.

The existing business continuity arrangements were revised again during the year and a second successful simulation exercise carried out at our dedicated business recovery facility.

We have audited the financial statements of the Guernsey Financial Services Commission for the year ended 31 December 2006 which comprise the income and expenditure account, the balance sheet, the statement of total recognised gains and losses, the cash flow statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

STATEMENT OF COMMISSIONERS' RESPONSIBILITIES

The Commissioners are required by the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended to prepare financial statements for each accounting period which give a true and fair view, in accordance with applicable Guernsey law and United Kingdom Accounting Standards, of the state of affairs of the Commission and of the income and expenditure of the Commission for the period. In preparing these financial statements, the Commissioners are 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 Commissioners confirm that they have complied with the above requirements in preparing the financial statements.

The Commissioners are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Commission and to enable them to ensure that the financial statements have been prepared in accordance with the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended and United Kingdom Accounting Standards. They are 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 COMMISSIONERS AND AUDITORS

The Commissioners are responsible for preparing the annual report. This includes responsibility for preparing the financial statements in accordance with applicable Guernsey law and United Kingdom Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for, and only for, the Commissioners as a body and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended. We also report to you if the Commissioners have not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

We read the other information as described in the contents section of this annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Commissioners

in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Commission's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

OPINION

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Accounting Standards, of the state of the Commission's affairs as at 31 December 2006 and of its income and expenditure, total recognised gains and losses and cash flows for the year then ended;
- the financial statements have been properly prepared in accordance with the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 as amended; and
- the information given in the Annual Report is consistent with the financial statements.

PricewaterhouseCoopers CI LLP
Chartered Accountants
Guernsey, Channel Islands
30 March 2007

The maintenance and integrity of the Commission's website are the responsibility of the Commissioners; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. Legislation in Guernsey governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

INCOME AND EXPENDITURE ACCOUNT

For the year ended 31 December 2006

	Note	2006 £	2005 as restated £
Income	2		
Fees receivable		7,988,020	7,241,704
Contributions from the States of Guernsey for services provided on behalf of government		300,000	300,000
Interest on deposits with States Treasury		214,678	162,249
Miscellaneous income, including bank interest		7,379	23,421
Other finance income	7(d)	152,154	103,781
		8,662,231	7,831,155
Expenses			
Salaries, pension costs, staff recruitment and training		5,586,517	5,045,024
Commissioners' fees		95,420	73,500
Legal and professional fees		399,073	445,675
Premises and equipment, including depreciation	4,11	768,194	810,257
Other operating expenses		470,555	416,118
Auditors' remuneration		10,000	10,000
		7,329,759	6,800,574
Commission's contribution to expenses of GTA University Centre	10	411,000	399,781
		7,740,759	7,200,355
Surplus of income over expenditure	2	£921,472	£630,800

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

The 2005 comparison figures have been restated following a change in accounting policy in respect of fee income (see note 9).

The notes on pages 52 to 60 form an integral part of these financial statements.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 December 2006

	Note	2006	2005 as restated
		£	£
Surplus for the year		921,472	630,800
Actuarial gain/(loss)	7(e)	478,994	(1,008,717)
Total recognised gain/(loss) for the year		1,400,466	(377,917)
Prior-year adjustment	9	1,628,038	(25,975)
Total recognised gains and losses since last annual report		£3,028,504	£(403,892)

The 2005 comparison figures have been restated following a change in accounting policy in respect of fee income (see note 9).

The notes on pages 52 to 60 form an integral part of these financial statements.

BALANCE SHEET

As at 31 December 2006

	Note	2006 £	2005 as restated £
Fixed assets			
Tangible assets	4	231,233	210,949
Current assets			
Debtors	5	1,823,423	1,853,268
Deposits with States Treasury		3,617,554	2,802,876
Cash at bank and in hand		242,487	214,529
		5,683,464	4,870,673
Creditors – amounts falling due within one year	6	(681,786)	(1,249,387)
Net current assets		5,001,678	3,621,286
Net assets before post-retirement liability		5,232,911	3,832,235
Post-retirement liability	7(b), (f)	(1,197,992)	(1,197,782)
Net assets		£4,034,919	£2,634,453
Reserves	8	£4,034,919	£2,634,453

The financial statements on pages 48 to 60 were approved by the Commissioners and signed on their behalf on 30 March 2007 by:

P A Harwood
Chairman

D J Mallett
Vice-Chairman

P J Neville
Director General

The 2005 comparison figures have been restated following a change in accounting policy in respect of fee income (see note 9).

The notes on pages 52 to 60 form an integral part of these financial statements.

CASH FLOW STATEMENT

For the year ended 31 December 2006

	Note	2006	2005
		£	as restated £
Reconciliation of surplus of income over expenditure to net cash inflow from operating activities			
Surplus of income over expenditure		921,472	630,800
Other finance income		(152,154)	(103,781)
Current and past pension service costs	7(c)	1,019,529	637,749
Contributions made to pension scheme	7(f)	(388,171)	(370,878)
Depreciation on tangible fixed assets	4	149,154	183,136
Interest receivable		(222,057)	(174,987)
Decrease/(increase) in debtors		29,845	(35,795)
Decrease in creditors		(567,601)	(15,123)
Net cash inflow from operating activities		£790,017	£751,121
Cash flow statement			
Net cash inflow from operating activities		790,017	751,121
Returns on investments and servicing of finance	16	222,057	174,987
Capital expenditure and financial investment	4, 16	(169,438)	(75,074)
Increase in cash in the year		£842,636	£851,034
Reconciliation of net cash flow to movements in net cash			
Increase in cash in the year		842,636	851,034
Net cash at 1 January	17	3,017,405	2,166,371
Net cash at 31 December	17	£3,860,041	£3,017,405

The notes on pages 52 to 60 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2006

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.

(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.

(d) Investigation and litigation

Costs arising from investigations and litigation are accounted for as expenditure is incurred, whether or not it had been billed at the balance sheet date. 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
Computer equipment	33 $\frac{1}{3}$ % straight-line

(f) Foreign currency translation

Monetary assets and liabilities denominated in currencies other than sterling have been translated into sterling at the rates of exchange ruling at the balance sheet date. Transactions during the year have been translated at the rates of exchange ruling at the date of the transaction.

(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 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.

Following the full adoption of Financial Reporting Standard 17 ("FRS 17"), 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 credit is included within other finance income, representing the expected return on the scheme's assets less the interest cost on the scheme's liabilities.

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.

2. INCOME AND SURPLUS OF INCOME OVER EXPENDITURE

Income and surplus of income over expenditure derive 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 and Fittings	Computer Equipment	Total
	£	£	£	£
Cost				
At 1 January 2006	83,713	697,972	643,366	1,425,051
Additions	24,416	39,540	105,482	169,438
At 31 December 2006	108,129	737,512	748,848	1,594,489
Depreciation				
At 1 January 2006	35,415	628,618	550,069	1,214,102
Charge for the year	9,641	60,364	79,149	149,154
At 31 December 2006	45,056	688,982	629,218	1,363,256
Net book value at 31 December 2005	£48,298	£69,354	£93,297	£210,949
Net book value at 31 December 2006	£63,073	£48,530	£119,630	£231,233

5. DEBTORS

	2006	2005
	£	as restated £
Fees receivable due but not paid (see note 9)	1,611,296	1,664,814
Other debtors	11,231	6,539
Amount due from GTA University Centre	48,323	38,977
Prepayments	152,573	142,938
	£1,823,423	£1,853,268

6. CREDITORS – amounts falling due within one year

	2006	2005
	£	£
Expense creditors and accruals	620,517	604,572
Fees received in advance	61,269	644,815
	£681,786	£1,249,387

7. SUPERANNUATION

FRS 17 Disclosure for the Guernsey Financial Services Commission Actuarial Account of the States of Guernsey Superannuation Fund

Employees of the Commission are eligible to be members of the States of Guernsey Superannuation Fund (“the Fund”). This is a defined benefit pension scheme funded by contributions from both the member and the employer. 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 (“the scheme”) 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 set of members by another.

A full actuarial valuation of the scheme was carried out at 31 December 2004 by the scheme’s actuary. The scheme’s actuary also completed valuations as at 31 December 2005 and 2006 for the purposes of FRS 17.

(a) The major assumptions used by the actuary in calculating the FRS 17 disclosures were:

	At 31 December 2006	At 31 December 2005	At 31 December 2004
Rate of increase in salaries	4.60%	4.40%	4.40%
Rate of increase in pensions in payment	3.10%	2.90%	3.00%
Discount rate	5.10%	4.70%	5.30%
Inflation assumption	3.10%	2.90%	2.90%

(b) The assets in the scheme and the expected rate of return were:

	Expected long-term rate of return			Value		
	2006	2005	2004	2006	2005	2004
				£	£	£
Equities	8.50%	8.00%	7.50%	6,796,550	5,657,011	4,281,057
Bonds	4.70%	4.30%	4.70%	1,560,970	1,390,025	1,141,787
Cash	5.00%	4.50%	4.75%	187,678	133,335	161,327
Total market value of assets				8,545,198	7,180,371	5,584,171
Present value of scheme liabilities				(9,743,190)	(8,378,153)	(5,610,146)
Net pension liability				£(1,197,992)	£(1,197,782)	£(25,975)

The asset and liability values on the FRS 17 basis reflect market conditions at the Commission's year-end date and 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

(c) Analysis of the amount included in salaries, pension costs, staff recruitment and training charged to income and expenditure account

	2006	2005
	£	£
Current service cost	880,878	637,749
Past service cost	138,651	–
Total operating charge	£1,019,529	£637,749

(d) Analysis of the amount credited to other finance income

	2006	2005
	£	£
Expected return on pension scheme assets	543,332	398,441
Interest on pension scheme liabilities	(391,178)	(294,660)
Net return	£152,154	£103,781

(e) Analysis of amount recognised in statement of total recognised gains and losses (“STRGL”)

	2006	2005
	£	£
Actual return less expected return on pension scheme assets	111,851	660,170
Experience (losses) and gains arising on the scheme liabilities	(117,666)	265,220
Changes in assumptions underlying the present value of the scheme liabilities	484,809	(1,934,107)
Actuarial gain/(loss) recognised in STRGL	£478,994	£(1,008,717)

(f) Movement in pension liability during the year

	2006	2005
	£	£
Deficit in scheme at beginning of the year	(1,197,782)	(25,975)
Movement in year:		
Current service costs	(880,878)	(637,749)
Contributions	388,171	370,878
Past service costs	(138,651)	–
Other finance income	152,154	103,781
Actuarial gain/(loss)	478,994	(1,008,717)
Deficit in scheme at end of the year	£(1,197,992)	£(1,197,782)

Following the actuarial valuation of the Fund as at 31 December 2004, the actuary recommended that the employer contribution rate be increased from 10.4% to 15.5% with effect from 1 January 2006. However, as the Fund is currently under review, the decision was taken not to increase the rate pending the outcome of that review. The employee contribution remains unchanged at 6%.

(g) History of experience gains and losses

	2006	2005	2004
Difference between the actual and expected return on scheme assets			
Amount	£111,851	£660,170	£65,610
Percentage of scheme assets	1%	9%	1%
Experience gains and losses on scheme liabilities			
Amount of (losses)/gains	£(117,666)	£265,220	£(307,859)
Percentage of the present value of the scheme liabilities	(1)%	3%	(5)%
Total amount recognised in statement of total recognised gains and losses			
Amount of gains/(losses)	£478,994	£(1,008,717)	£(479,827)
Percentage of the present value of the scheme liabilities	5%	(12)%	(9)%

It should be noted that the assets and liabilities have only been ring-fenced since 1 January 2004. Accordingly, it is not possible to produce all the information to meet the five years' data as required by FRS 17.

The claims of the Commission's pensioners and employees will be met from the Fund and in the final resort would be met by the States of Guernsey.

8. RECONCILIATION OF MOVEMENTS IN RESERVES

	Note	2006 £	2005 as restated £
Reserves brought forward as originally stated		1,006,415	1,442,607
Prior-year adjustments	9	1,628,038	1,569,763
Reserves brought forward as restated		2,634,453	3,012,370
Surplus of income over expenditure for the year		921,472	630,800
Actuarial gain/(loss) on post-retirement liability	7(e)	478,994	(1,008,717)
Reserves carried forward		£4,034,919	£2,634,453

Included in the reserves is a pension liability of £1,197,992 (2005 £1,197,782) which equates to the post-retirement liability under FRS 17 (see note 7).

9. PRIOR-YEAR ADJUSTMENT

The following prior-year adjustments have been made to opening reserves as shown in note 8:

During 2006 the Commission's Insurance Division moved from invoicing in arrears to invoicing in advance for regulatory services for the coming year. This has resulted in a change in accounting policy in the Insurance Division and led to there being additional income of £1,628,038, of which £32,300 related to 2005 and £1,595,738 related to 2004 and earlier years. All divisions now invoice licensed entities at the beginning of each year.

During 2005 the full adoption of FRS 17 resulted in a post-retirement liability adjustment of £25,975.

	2006 £	2005 £
Insurance fee income	1,628,038	1,595,738
Post-retirement liability	-	(25,975)
Reserves carried forward	£1,628,038	£1,569,763

10. GTA UNIVERSITY CENTRE

The GTA University Centre arranges training for the finance industry and for other industry sectors. The company's staff, excluding its Chief Executive, are employed by the Commission and permanently seconded to the company. The Commission provided a grant of £411,000 in 2006 (2005: £399,781) to the company in order to meet 50% of its budgeted net operating expenditure, the same amount being provided by the States of Guernsey via the Commerce and Employment Department.

11. FINANCIAL COMMITMENTS

The Commission leases office accommodation at La Plaiderie Chambers and Le Marchant House. The lease for La Plaiderie Chambers expires on 25 March 2020 and the lease for the car park expires on 21 November 2009 and the underlease for Le Marchant House on 10 December 2011. The rentals payable in 2006 under the terms of the leases amount to £303,700 (2005: £292,300).

Operating lease commitments

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

Land and buildings

	2006	2005
Leases which expire more than two years but less than five years after balance sheet date	£51,700	£–
Leases which expire more than five years after balance sheet date	£252,000	£292,300

12. INVESTIGATION AND LITIGATION COSTS

As a consequence of fulfilling its regulatory responsibilities the Commission undertakes investigations and is a party to legal actions from time to time, 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.

13. CONTINGENT LIABILITY

On 22 December 2004, the Commission became a member of Fund Distribution Ltd ("FDL"), a company limited by guarantee. FDL was formed to administer a fund established to pay compensation in respect of zero dividend preference shares issued by certain split-capital investment trusts. On 25 January 2007, FDL, having distributed some £143.5 million to claimants, was put into members voluntary solvent liquidation. As a part of that process the Commission has made a commitment to pay up to £10,000 to FDL in the event that its remaining assets are insufficient to meet its liabilities.

14. RELATED-PARTY TRANSACTIONS

The States appointed Peter Harwood, who is a partner of Ozannes, as a Commissioner in August 2004. During the year the Commission engaged 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.

15. 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.

16. NOTES TO THE CASH FLOW STATEMENT

	2006	2005
	£	£
Returns on investments and servicing of finance		
Interest received	£222,057	£174,987
Capital expenditure and financial investment		
Payments to acquire tangible fixed assets	£(169,438)	£(75,074)

17. ANALYSIS OF NET CASH

	At 1 January 2006	Cash flow	At 31 December 2006
	£	£	£
Deposits with States Treasury	2,802,876	814,678	3,617,554
Cash at bank and in hand	214,529	27,958	242,487
	£3,017,405	£842,636	£3,860,041



GENERAL

In July 2006 the Guernsey Training Agency (“GTA”) was awarded recognition by Bournemouth University as an accredited university centre and became known as the GTA University Centre. This is the first time such an award has been granted under the University’s new recognition criteria. It was a seminal moment in the development of the GTA, acknowledging as it does that the GTA is a high-quality provider of advanced training and higher education and has been subject to rigorous examination in terms of quality assurance, resources, processes, infrastructure and mission. This recognition places the GTA in a strong position in terms of scrutiny from regulators and other interested international observers. At the same time the recognition is not exclusive and does not constrain the GTA from working with other organisations or institutions.

Stephen Jones resigned as a trustee of the GTA during 2006. The directors and staff are most grateful to Stephen for his important contribution to the development and work of the GTA. Alan Bougourd has been appointed as a trustee in his place. The GTA is pleased to note the stability of the Board of Directors for the calendar year, which lends to the continuity of governance. The GTA continues to be funded jointly on an equal basis by the Commission and the States of Guernsey Commerce and Employment Department.

The long-term objective of the GTA is to engender a training and development culture within all organisations throughout the Bailiwick, and procure and facilitate high-quality training and development programmes in all business sectors. The culture is expected to generate a highly qualified, knowledge-based workforce, enabling all organisations to compete in a global marketplace and to broaden the Bailiwick’s skills base whilst adding value to all Bailiwick businesses. The GTA’s work covers all sectors of the Bailiwick’s economy – only those initiatives pertinent to the finance sector are outlined below. During 2006 the GTA has once again proved to be very successful in facilitating high-quality training and development initiatives for the Bailiwick workforce.

In February 2006 the GTA was re-recognised as an Investor in People (“IIP”). The report said: “The greatest strength of the Agency is the continued development of their culture in as much as they have now created a culture of ‘a family team’. Everyone works towards their shared objectives with the specific consideration of the need to work as a team and help each other. This is due to the involvement of all staff when the Business Plan is being prepared. All staff are invited to contribute ideas and suggestions for improving the services offered by the Agency. This is then developed as part of the regular Staff Meetings. Every member of staff is considered to be an important player in the team.”

The GTA held its second presentation and awards ceremony on 21 November. The Lieutenant Governor of Guernsey presented 70 successful postgraduate students of the GTA with certificates of completion. Over 300 guests attended, with representatives from the States of Guernsey, local businesses and family and friends of graduates celebrating the success of local students.

During 2006 the GTA continued to work with the on-island finance associations, professional institutes, the Guernsey International Business Association and the Commission to maintain the accuracy of the qualifications matrices for each of the four sectors of the finance industry. These matrices are published on the GTA’s website, www.gta.gg. In parallel, and in support of the furtherance of training and development in each of these sectors, the GTA continues to work with the on-island finance associations, the Commission and the professional institutions within education fora. These groups are important in providing strategic direction for the development of finance education and training within the Bailiwick.

The strategic relationship between the Guernsey College of Further Education and the GTA continues to be maintained through the Senior Management Forum. The members of the forum are the Principal and Vice-Principal of the Guernsey College of Further Education and the Chief Executive and the Deputy Chief Executive of the GTA. The forum meets monthly.

An extensive education and training programme took place throughout the year and the Nelson Place Study Centre continued to act as a focal point for education and training within St Peter Port. Staff at the GTA have worked closely with all the stakeholders in determining training priorities and meeting their requirements.

At the end of 2006 the GTA had 1,012 registered students who made 1,676 study visits to the centre. A total of 5,968 delegates attended the 400 training events that took place. Additionally 147 examinations were held, during which 636 candidates were examined on a range of award-bearing programmes (table 8).

AWARD-BEARING PROGRAMMES

Eleven students from the first cohort of the MBA degree which is run by Southampton University graduated in June. Eight students were awarded distinction, and three have been awarded merit passes. The GTA was extremely pleased with these outstanding results. A second cohort commenced in September 2005 with 10 students, who are due to graduate in 2008.

Five delegates completed the Postgraduate Certificate in Intellectual Property, offered through Bournemouth University. Three students achieved distinction and two were awarded merit passes.

Ten delegates commenced the new Masters programme in Human Resource Management, delivered by Bournemouth University, in September 2006.

The fifth cohort of the two-year MSc Corporate Governance/ Grad ICSA gained five "fasttrack" students in September 2005, making a total of 14 students commencing the second year of the

programme. Following the dissertation stage it is planned that the students will graduate early in 2007. A sixth cohort of the programme commenced in September 2006 with eight students.

The prestigious Institute of Directors Company Direction Programme commenced in October with 20 delegates; this is the seventh time the programme has been offered in Guernsey.

Central Law Training once again delivered the Foundation and Diploma Programmes in Offshore Trust Management on behalf of the Society of Trust and Estate Practitioners ("STEP"). Twenty-six students completed the Foundation Programme, with a further 29 students completing the Diploma Programme.

The International Compliance Association was established during 2002, offering diplomas for anti-money laundering and compliance. Sixteen students undertook the Diploma in Compliance.

Nine delegates successfully completed the Professional Certificate in Marketing and nine the Professional Diploma in Marketing. Both programmes are run by the Chartered Institute of Marketing and it is expected that both programmes will be run in 2007.

Five delegates have successfully completed the Certificate in Training Practice programme, leading to Associate Membership of the Chartered Institute of Personnel and Development.

During 2006 some 28 students undertook the Introductory Certificate in Team Leading, a three-day programme delivered by the staff from the Guernsey Business School. A further 19 students enrolled for the Introductory Certificate in First Line Management. This five-day programme is delivered by the Guernsey Business School and involves the completion of a 1,000-word work-based assignment.

Table 8. Training event/delegate numbers at the year end

Key Statistics	2002	2003	2004	2005	2006
Registered number of students	818	887	951	1,003	1,012
Recorded number of study sessions	1,971	2,341	2,731	2,572	1,676
Number of training events	295	322	321	386	400
Number of delegates attending	2,811	4,463	4,695	5,253	5,968
Number of examination days	69	92	113	114	71
Number of examinations	158	194	236	199	147
Number of examination candidates	686	793	874	757	636

Fifty delegates undertook Information Systems Examinations Board courses in Information Security, Security Management Principles and Service Management.

Fifty-one students have now successfully completed the Captive Insurance Certificate since the introduction of this qualification. This locally designed programme is awarded 20 points under the Chartered Insurance Qualifications framework. Twenty-two students successfully completed the locally examined Guernsey Insurance Certificate Qualification during 2006. This programme is awarded 16 points under the Chartered Insurance Qualifications framework.

SHORT COURSES AND CONFERENCES

During 2006 the GTA facilitated four conferences, one on behalf of STEP, the other three on Family Business, Risky Business and Information Technology ("IT"). The Family Business Conference held in June attracted a total of 55 delegates; the STEP Conference included nine seminars from a variety of local and UK speakers and attracted 80 delegates from the fiduciary sector. The Risky Business Conference was run in partnership with AO Hall and attracted 81 delegates. The IT Conference on Managing Information throughout the Organisation, held in September, attracted 56 delegates.

Over 40 lunchtime seminars and short courses for managers, covering subjects such as brain fitness at work, counselling skills and personal development, were held during 2006, with 414 delegates attending in total.

A seminar series on prevention of financial crime run by the Commission in conjunction with the Financial Intelligence Service and the Guernsey Police Commercial Fraud and External Affairs Department attracted 246 delegates.

A series of six law seminars run in conjunction with the Guernsey Bar in the lead-up to the Guernsey Bar exams was attended by 108 delegates.

A number of short courses pertaining to the finance sector, covering topics such as preparing trust accounts, an introduction to compliance, retirement annuity trust schemes and collateralised debt obligations, attracted 565 delegates.

INVESTORS IN PEOPLE

The GTA continues to promote the IIP Standard on-island and has completed a set of benchmarking reports for several organisations during 2006. Whilst operating purely in an advisory capacity, the organisations have found the exercise extremely helpful in positioning themselves against the IIP Standard and identifying what further work still needs to be done.

OTHER INITIATIVES

The Chief Executive and Deputy Chief Executive continued to meet with senior staff from the finance and commerce sectors to hear first-hand the training needs of organisations. The meetings continue to prove most informative and valuable.

A further two personal development programmes commenced during 2006 with 22 delegates. In conjunction with the Learning Company, two more Management Development Programmes were offered, attracting 21 delegates.

Working with the Law Officers of the Crown, the GTA is assisting with the administration of the Guernsey Bar examinations. The GTA is continuing to work with the Guernsey Bar in identifying events for continuous professional development purposes. During 2006 a series of "update" lectures were held on English criminal, tort and contract law.

The GTA, working in partnership with the human resources section of the States of Guernsey Policy Council, offered a series of seminars presented by Institute of Directors tutors aimed at senior managers. This was the first event under the private/public sector partnership initiative and is focused on leadership and development training. It was recognised that there is commonality between the different sectors, and managers are keen to work more closely so that they can learn from each other and improve their networking opportunities.

E-BUSINESS AND IT

The IT and e-Commerce Advisory Group met four times during 2006 to discuss a number of training and development needs within the sector. The group is

comprised of representatives from the Commission, the Data Protection Office, the Guernsey College of Further Education, and the finance, public and commercial sectors. The group has provided relevant and useful information on the types of courses to facilitate and the GTA is particularly pleased with the continuing growth in IT training that it has facilitated during 2006.

During the year 40 seminars and short-course programmes were held on topics such as voice over internet protocol, mail merge in a flash and on managing IT security, and were attended by 526 delegates.

The GTA continues to work closely with the British Computer Society (“BCS”) and is represented on the committee of the Guernsey sub-branch. The GTA jointly badged a number of BCS seminars during 2006.

APPENDIX 1

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 development and effective supervision of finance business in the Bailiwick”. The statutory functions include those under the following 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;

section 3 of the Road Traffic (Compulsory Third Party Insurance) (Guernsey) Laws, 1936 to 1989;

section 1 of the Surf-Riding Long Boards (Compulsory Third-Party Insurance) Law, 1969; and

section 1 of the Vessels and Speed Boats (Compulsory Third-Party Insurance, Mooring Charges and Removal of Boats) (Guernsey) Law, 1972.

RELATIONSHIP WITH THE STATES OF GUERNSEY

The States of Guernsey 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).

With effect from 1 January 2006, the Commission Law was amended to change the number of Commissioners. The Law provides that the Commission shall consist of a minimum of five members and a maximum of seven members elected by the States of Guernsey 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 number of appointed Commissioners was increased from five to six with effect from 2 February 2006. A brief résumé for each of the current members is provided on pages 6 and 7 of this report. All of the Commissioners are non-executive – three reside in the United Kingdom, with the remainder living in Guernsey.

There were 13 meetings of the Commissioners in 2006. The attendance of the individual Commissioners at these meetings was as follows: John Hallam (retired February 2006) – 1, Peter Harwood – 13, David Mallett – 12, Mel Carvill – 11, Susie Farnon (appointed February 2006) – 11, Howard Flight – 11, Rosemary Radcliffe (appointed February 2006) – 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,

**Functions, Structure and Corporate Governance
and other Control Systems of the Commission**

evaluating and managing operational risks (including regulatory and financial risks). In this connection, the Commission takes account of the guidance contained in the Combined 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 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. David Mallett was appointed as Chairman of the Committee following the retirement of Leslie Priestley in August 2005. In February 2006 Susie Farnon was appointed to the Committee. The Committee now comprises David Mallett (Chairman), Mel Carvill and Susie Farnon. Meetings are usually attended by the Director General, the Head of Finance and Operations and the Director of Policy and International Affairs (who is the committee's secretary). The Committee met twice in 2006, the attendance of the individual members at these meetings was as follows: David Mallett – 2, Mel Carvill – 2, Susie Farnon – 2.

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. A programme of assessment against international regulatory standards has also been put in place and is undertaken by the Commission's officers and reviewed by the Commissioners. An assessment of compliance with international regulatory standards

was carried out by the International Monetary Fund ("IMF") in 2002 – the Commission and the other authorities in Guernsey were found by the IMF to have a high level of compliance with these standards. The IMF is expected to undertake another assessment in 2008.

APPENDIX 2

Committees and Working Parties

The following advisory groups and committees have assisted the Commission with its work. Only current outside members are listed.

FORUM FOR INSURANCE DEVELOPMENT

Mark Colton	BWCI Group
John Copeland	Marsh Management Services Guernsey Ltd
Paul Cutter	Association of Guernsey Insurers
Tony Mancini	KPMG
Peter Niven	Financial Industry Policy Advisory Group
Paul Wakefield	Insurance Institute of Guernsey
Peter Walpole	Insurance Corporation of the Channel Islands Ltd
Adv. Jeremy Wessels	Ozannes
Dominic Wheatley	Willis Management (Guernsey) Ltd
Merise Wheatley	Guernsey Insurance Company Management Association
Nick Wild	JLT Risk Solutions (Guernsey) Ltd

GUERNSEY REINSURANCE MARKET PROJECT

Tony Mancini	KPMG
Peter Walpole	Insurance Corporation of the Channel Islands Ltd
Nick Wild	JLT Risk Solutions (Guernsey) Ltd

INSURANCE BUSINESS LAW STEERING GROUP

Stephen Ainsworth	BWCI Group
John Copeland	Marsh Management Services Guernsey Ltd
Paul Cutter	Nordben Life and Pensions
Chris Le Conte	Aon Insurance Managers (Guernsey) Ltd
Charles Scott	Alternative Risk Management Ltd
Andrew Weatherburn	Heritage Group Ltd
Dominic Wheatley	Willis Management (Guernsey) Ltd
Merise Wheatley	Heath Lambert Insurance Management

INSURANCE MANAGERS AND INSURANCE INTERMEDIARIES LAW STEERING GROUP

Richard Bowyer	Savills Private Finance
Richard Cotran	Norwich Union
Mark Latter	HSBC Insurance Management Guernsey Ltd
Andrew Lundie	Heritage Group Ltd
Sean Martin	2mi
Andrew Mills	Insurance Corporation of the Channel Islands Ltd
Barry Pitfield	Independent adviser
Peter Walpole	Insurance Corporation of the Channel Islands Ltd
Alan West	HSBC Insurance Management Guernsey Ltd

JOINT MONEY LAUNDERING STEERING GROUP

Antonia Bligh	Financial Intelligence Service
Alan Bougourd	Association of Guernsey Banks
Anna Burgess	Collins Stewart (C. I.) Limited
Ian Burns	Guernsey Association of Trustees
Stuart Butler	Association of Guernsey Insurance Brokers
Adv. Paul Christopher	Guernsey Bar
Mike De Haaff	Guernsey Investment Fund Association
Steve Hogg	Association of Guernsey Banks
Steve Le Page	Guernsey Society of Chartered and Certified Accountants
Gary Miller	HSBC Private Bank (Guernsey) Limited
Robert Moore	Guernsey International Business Association
Julian Parker	Guernsey Association of Compliance Officers
Robert Sinclair	Guernsey Association of Trustees
Linda Warner	Old Mutual International (Guernsey) Limited
Merise Wheatley	Guernsey Insurance Company Management Association

The Director General of the Commission and his colleagues take this opportunity of acknowledging the contribution made by the members of these groups and of thanking them for their support and assistance.

The purpose of this document is to provide guidance in respect of relevant issues relating to Qualifying Investor Funds, due diligence issues that need to be considered by Guernsey licensed service providers to such funds and the information required to be submitted to the Commission in support of an application.

Any questions in relation to this guidance, including those in respect of the Commission's regulatory approach to Qualifying Investor Funds and the responsibilities of Guernsey licensed service providers in their operation of such funds should be referred in the first instance to the Applications Team within the Investment Business Division of the Commission.

BACKGROUND

QUALIFYING INVESTOR FUNDS AND QUALIFIED INVESTORS

1. A Qualifying Investor Fund is either an open-ended collective investment scheme, authorised under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended or a closed-end investment fund for which consent has been granted under the Control of Borrowing (Bailiwick of Guernsey) Ordinances, 1959 as amended.
2. Only Qualified Investors (as defined below) would be permitted to invest in a Qualifying Investor Fund.
3. A Qualified Investor is deemed able:
 - (a) to evaluate the risks and strategy of investing in a Qualifying Investor Fund; and
 - (b) to bear the economic consequences of investment in the Qualifying Investor Fund including the possibility of any loss arising from the investment.
4. Qualified Investor means: a Professional Investor, an Experienced Investor, and/or a Knowledgeable Employee as defined below.
 - (a) A Professional Investor is:
 1. a Government, local authority, public authority or supra-national body (in the Bailiwick or elsewhere); or
 2. a person, partnership or other unincorporated association or body corporate, (whether incorporated, listed or regulated in an OECD country or otherwise) whose ordinary business or professional activity includes or it is reasonable to expect that it includes, acquiring, underwriting, managing, holding or disposing of investments whether as principal or agent, or the giving of advice on investments; or
 3. an affiliate of the Qualifying Investor Fund or an associate of an affiliate of the Qualifying Investor Fund. (The terms "affiliate" and "associate of an affiliate" are intended to refer to financial services businesses or financial services professionals associated, directly or indirectly, with the operation of the fund in question).
 4. an individual investor who makes an initial investment of not less than US\$100,000 or equivalent in the fund in question. Provided the initial test has been met, subsequent investments by the same investor may be of lower amounts.
 - (b) An Experienced Investor is:

a person, partnership, or other unincorporated association or body corporate which has in any period of 12 months (whether on his own behalf or in the course of his employment by another person) so frequently entered into transactions of a particular type in connection with:

 1. open-ended collective investment schemes and/or
 2. general securities and derivatives as defined in Schedule 1 of the Protection of Investors Law. (In summary, that definition includes equities, bonds, participations in closed-end investment vehicles, warrants, options, futures, contracts for differences and rights on any of those investments)

being transactions of substantial size entered into with, or through the agency of, reputable persons who carry on investment business, that he can reasonably be expected to understand the nature of, and the risks involved in, transactions of that description; or who provides a certificate from an appropriately qualified investment advisor confirming that the investor has obtained independent advice.

(c) A Knowledgeable Employee is:

1. a person who is (or has been within a period of three years up-to the date of application for investment in the Qualifying Investor Fund) an employee, director, general partner, consultant or shareholder of, or to, an affiliate appointed by the Qualifying Investor Fund to advise, manage or administer the investment activities of the Qualifying Investor Fund, who is acquiring an investment in the Qualifying Investor Fund as part of his remuneration or an incentive arrangement or by way of co-investment, either directly or indirectly through a personal investment vehicle, such as a trust, for or substantially for, that person; or
 2. any employee, director, partner or consultant to or of any person referred to at 4(a)2 above or anyone who has fulfilled such a role in respect of any person referred to at 4(a)2 above within a period of three years up-to the date of application for investment in the Qualifying Investor Fund. The term "employee" would only cover persons who are, or have been, employed in a relevant role and would not extend to clerical, secretarial or administrative roles.
5. Funds, which are approved as Qualifying Investor Funds, must have in place measures to ensure that they are only available to investors who fall within the above definitions. The Commission would expect any warranties provided by potential investors to confirm what type of

Qualified Investor they consider themselves to be, that is, whether they are a Professional Investor, an Experienced Investor, and/or a Knowledgeable Employee.

Commission staff will assess licensees' systems and controls in this respect as part of their post-facto monitoring of licensees.

6. The Commission does not wish to prescribe the exact requirements relating to the contents of warranties to be obtained from potential investors into Qualifying Investor Funds or the form of disclaimers that will be disclosed within the scheme particulars, offering document (or equivalent) of such a fund. However, the Commission does consider that, as a minimum, the following issues should be referred to in any such warranty or disclaimer relating to a Qualifying Investor Fund:
 - (a) An acknowledgement that the fund has been established in Guernsey as a Qualifying Investor Fund and is suitable only for those investors who satisfy the definition of a Qualified Investor as published by the Guernsey Financial Services Commission as being either a Professional Investor or an Experienced Investor or a Knowledgeable Employee.
 - (b) A representation that the potential investor satisfies the definition of a Qualified Investor and that they will not acquire an interest in the fund for the benefit of any person who is not a Qualified Investor.
 - (c) An acknowledgement that the potential investor has read and understood the fund's scheme particulars, offering document or equivalent including the risk warnings disclosed.
 - (d) An acknowledgement that investing in the subject fund may involve special risks that could lead to a loss of all or a substantial portion of any investment that the potential investor makes in the fund.

GUIDANCE

THE STRUCTURE OF THE FUND

The Fund

1. A Qualifying Investor Fund is either an open-ended collective investment scheme, authorised under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended or a closed-end investment fund for which consent has been granted under the Control of Borrowing (Bailiwick of Guernsey) Ordinances, 1959 as amended.
2. A Qualifying Investor Fund that is an open-ended collective investment scheme must comply with the requirements of the appropriate rules, that is the Collective Investment Schemes (Class A) Rules 2002, the Collective Investment Schemes (Class B) Rules 1990 or the Collective Investment Schemes (Qualifying Professional Investor Funds) (Class Q) Rules 1998.
3. Requests for modifications of the relevant rules must be made in writing to the Investment Business Division of the Commission in accordance with the relevant provisions of the appropriate rules. Such requests should be made at least three working days in advance of the submission of the formal application for the authorisation/consent of the fund.

The Promoter and/or Investment Manager

4. The promoter and/or investment manager should be an institution regulated and in good standing, or, if conducting activities which do not require regulation, otherwise in good standing.
5. Good standing would imply that the institution itself, its directors, controllers and senior managers had not during the past 5 years been the subject of material disciplinary action by a regulator or professional body, or subject to any conviction for fraud, dishonesty or related offences of a financial nature.
6. The Guernsey licensed service provider associated with the application for authorisation under the Protection of Investors Law or consent under the Control of Borrowing Ordinances

must certify to the Commission that they have performed sufficient due diligence to be satisfied that the promoter and/or investment manager are fit and proper. In that regard, such service providers should take account of the issues referred to at 11(a), (b) and (c) below and should document their findings and conclusions accordingly.

7. For the avoidance of doubt, applications on behalf of newly formed promoters and/or investment managers will be considered. The Guernsey licensed service provider who is seeking the fund's authorisation or consent will need to consider the track record and experience of the controllers, directors and management of such entities taking into account their previous employment history. Such previous employment history should demonstrate that the individuals possess relevant experience in relation to managing or advising on investors' funds using similar investment strategies to those that will be adopted by the Qualifying Investor Fund. The licensed service provider's consideration of these matters and conclusions arising should be documented.
8. Where applicants are aware of issues in relation to a promoter and/or investment manager (which term should be taken to include their controllers, directors and management) and associated parties, but are uncertain of their materiality or possible impact on the subject application, they should consult Commission staff prior to submitting the formal application at the time they become aware of the issue.
9. Commission staff will assess licensees' application due diligence as part of their post-facto monitoring of licensees. If the Commission were to find that warranties provided were defective, or misleading, the Commission would take action against the licensee and in appropriate cases would exclude that licensee from future participation in the self-certification programme.
10. The Commission expects each licensee to ensure that its due diligence in respect of the promoter and/or investment manager and associated parties is updated on a regular basis.

The Commission will not prescribe the means by which this requirement is to be achieved but as set out in 6 above licensees should take account of the issues at 11(a), (b) and (c) below and should document their findings and conclusions. Where licensees become aware of issues in relation to a promoter and/or investment manager (which term should be taken to include their controllers, directors and management) and associated parties, but are uncertain of their materiality or possible impact on the subject Qualifying Investor Fund, they should consult Commission staff, prior to the submission of a formal application to the Commission, at the time they become aware of the issue.

11. Promoters and/or investment managers (including their directors, controllers and senior managers) must be fit and proper. This can be defined as being a requirement for integrity (or honesty), competence and solvency. Guernsey licensed service providers should ensure that the following issues are covered as part of their due diligence procedures in respect of new client relationships and that their findings and conclusions are documented.

(a) Integrity

Promoters and/or investment managers (which term should be taken to include their controllers, directors and management) should be of a high reputation and standing. Poor reputation would be considered to be a negative factor.

The promoter and/or investment manager must carry on their business with prudence, professional skill and honesty.

In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established, the integrity of the controllers, directors and management should be assessed in the light of previous employment and experience. It would be expected that the Guernsey licensed service provider would make direct contact with relevant individuals' previous employers as part of the necessary due diligence enquiries.

Promoters and/or investment managers would be expected to deal openly and honestly with the Commission and any other regulatory authority to whose regulation they are subject (either on a consolidated basis or directly).

(b) Solvency

Promoters and/or investment managers should be solvent. A firm regulated in another jurisdiction should also comply with the solvency, capital adequacy or financial resources requirement (as appropriate) laid down by the relevant regulatory body to which it is accountable. Past performance in this respect should also be considered to ensure that relevant requirements have been consistently met in the past.

A promoter and/or investment manager that is not regulated would be expected to maintain a surplus of shareholders' funds as disclosed in its audited financial statements. Past performance in this respect should also be considered to ensure that relevant requirements have been consistently met in the past.

Promoters and/or investment managers would be expected to maintain adequate net liquid assets such that they are able to settle their debts when they fall due.

In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established (that is, not being able to produce audited annual financial statements for a period of at least 24 months), it will be necessary for the Guernsey licensed service provider to consider financial projections relating to the proposal under consideration. It will also be necessary to consider whether the controllers, directors and management of such promoters and/or investment managers have previously been responsible for considering the solvency of an entity (for example, if they held a director role or financial control function). Where individuals have been directors or held relevant positions

at entities that have gone into liquidation or suffered financial loss it will be necessary to consider the role undertaken by the relevant individual in such situations.

(c) Competence

The most obvious way to demonstrate competence is to have established a favourable track record, in a business similar to that to be conducted in the Bailiwick.

The promoter and/or investment manager should be able to demonstrate an acceptable complaints history. In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established, it will be necessary for Guernsey licensed service providers to consider whether the controllers, directors and management of such entities have been subject to significant complaints whilst employed by other firms.

Promoters and/or investment managers should have staff of adequate skills, knowledge and experience to undertake and fulfil their duties efficiently and effectively.

AUTHORISATION OF THE FUND

1. In order to consider authorising the fund (if it is open-ended) or granting the requisite consent (if it is closed-end) the Commission must receive a copy of the application form (Form QIF (2007)), which must be signed by the proposed designated manager/administrator of the fund. The form contains the following requirements:

- (a) Warranties to the Commission from the proposed designated manager/administrator that they have performed sufficient due diligence to be satisfied that:
- (i) the promoter and associated parties are fit and proper;
 - (ii) effective procedures are in place to ensure restriction of the fund in question to only Qualified Investors, as defined; and

- (iii) the economic rationale for the proposed fund and any attendant risks are clearly disclosed.

The Commission attaches great importance to these warranties. It expects applicants to be able to demonstrate that they have documentary evidence to support the warranties given, and to be able to produce that evidence immediately should the Commission request it. Applicants who cannot substantiate their applications may, as noted in paragraph 9 of this guidance, find themselves excluded from participation in the Qualifying Investor Fund self-certification programme.

- (b) Submission of fully completed, signed Form APA/APB/APQ/APC (as appropriate) together with Forms PQ in respect of controllers, directors and senior managers of the promoter and fund (as appropriate);
- (c) Payment of the application fee required under the relevant fees regulations;
- (d) Submission of certified complete final copies of the following documents:
 - (i) scheme particulars, prospectus, offering document or equivalent;
 - (ii) the application form, subscription agreement or equivalent;
 - (iii) constitutive documents, that is the memorandum and articles of association, trust deed or limited partnership agreement, as applicable;
 - (iv) all material agreements entered into by the fund.
- (e) For Class A and Class B open-ended schemes, a lawyer's certificate. For Class Q open-ended schemes, a manager's certificate.
- (f) The licensing under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended of persons intending to carry on a restricted activity within the Bailiwick

- of Guernsey in connection with the fund. Reference should also be made to 3 below.
2. The Commission will issue the necessary authorisation under the Protection of Investors Law or consent under the Control of Borrowing Ordinances within three working days of receipt/resolution of all of the above issues.
 3. Should the promoter of a Qualifying Investor Fund require the establishment of a Guernsey incorporated management company it will be necessary for such company to be licensed under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended before the relevant authorisation or consent can be issued in respect of the fund. The application process relating to the issue of a licence under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended will normally take longer than the three working days referred to at 2 above.
- (c) confirmation that no other licensee carries on or intends to carry on any of the restricted activities described in rule 2.01 in connection with the non-Guernsey scheme;
 - (d) details of any regulatory approval given by, or applied for from, the authorities in the country or territory in which the non-Guernsey scheme is, or is to be, incorporated or established;
 - (e) the notification fee as prescribed from time to time by Regulations made under Section 22 of the Law; and
 - (f) such other information as the Commission may require.
3. The Commission will issue the necessary approval under the Non-Guernsey Schemes Rules within three working days of receipt of the information and documentation set out under 2(a) to (f) above, together with a certificate covering the issues referred to under 1(a) of "Authorisation of the Fund" above.

NON-Guernsey Schemes

1. The Licensees (Conduct of Business and Notification) (Non-Guernsey Schemes) Rules 1994 ("the Non-Guernsey Schemes Rules") require Guernsey licensees wishing to undertake the restricted activities of management, administration or custody to provide prior written notice to the Commission of such proposal. The Commission's formal approval under the Non-Guernsey Schemes Rules is required before the licensee can act.
2. Section 2.02 of the Non-Guernsey Schemes Rules requires the following information to be submitted in support of a relevant application:
 - (a) the prospectus, or latest draft prospectus, of the non-Guernsey scheme;
 - (b) a copy of the agreement, or latest draft agreement relating to the proposed management, administration or custody services to be provided by the licensee to the non-Guernsey scheme;

The purpose of this document is to provide guidance in respect of relevant issues relating to Registered Closed-end Investment Funds, due diligence issues that need to be considered by Guernsey licensed service providers to such funds and the information required to be submitted to the Commission in support of an application.

Any questions in relation to this guidance, including those in respect of the Commission's regulatory approach to Registered Closed-end Investment Funds and the responsibilities of Guernsey licensed service providers in their operation of such funds should be referred in the first instance to the Applications Team within the Investment Business Division of the Commission.

BACKGROUND

REGISTERED CLOSED-END INVESTMENT FUNDS

A Working Party chaired by Advocate Peter Harwood was appointed in 2005 to consider investment sector legislation and regulation and to report to the Guernsey Financial Services Commission and to the Commerce and Employment Department of the States of Guernsey. In its report published in June 2006 the Working Party proposed the introduction of the concept of Registered Investment Funds, being either open-ended or closed-end investment funds that would not be regulated by the Guernsey Financial Services Commission.

The proposals made it clear that regulated categories of funds would be funds that are capable of being offered by the issuer directly to the public in Guernsey whereas Registered Funds may not be offered directly by the issuer to the public within Guernsey, but may be listed.

All Registered Funds would have to comply with the minimum prospectus disclosure requirements required by a new proposed generic "prospectus" law applicable to all Guernsey domiciled entities, whether they be investment funds or trading or commercial entities. The introduction of a new generic "prospectus" law will be the subject of detailed consultation and the legislative process. Until such legislation is implemented it is proposed

to utilise the existing disclosure requirements set out in the Commission's application Form APC, which is currently submitted by closed-end investment funds seeking consent under the Control of Borrowing Ordinance.

All Registered Funds would have to appoint a local licensed administrator. Each Registered Fund through its appointed administrator would be required to make an initial filing with the Commission and submit notifications to the Commission in respect of changes to the Fund, together with annual financial statements and quarterly statistical information. The administrator would be required to certify that it has undertaken due diligence on the promoter of the Registered Fund. The Commission would need to establish clear guidelines to establish minimum criteria for the due diligence to be undertaken by the administrator. This document meets that requirement.

There should be a standard rubric to be incorporated on any Prospectus, Information Memorandum, Offering Circular or similar document issued by a Registered Fund and also in the annual report and accounts of a Registered Fund to the effect that the Fund is a Registered Fund and that the Commission has relied upon specific warranties provided by the Guernsey licensed service provider when issuing the relevant consent under the Control of Borrowing Ordinance. Evidence that such rubric has been incorporated in the relevant documentation would need to be submitted to the Commission. Reference should be made to the relevant requirements set out in this document, together with the associated form to be submitted in connection with an application under the Control of Borrowing Ordinance in respect of a Registered Closed-end Investment Fund.

GUIDANCE

THE STRUCTURE OF THE FUND

1. A Registered Closed-end Investment Fund for which consent has been granted under the Control of Borrowing (Bailiwick of Guernsey) Ordinance, 1959 as amended can be a limited company (including a protected cell company or incorporated cell company), a limited partnership or a unit trust.

THE PROMOTER AND/OR INVESTMENT MANAGER

2. The promoter and/or investment manager should be an institution regulated and in good standing, or, if conducting activities which do not require regulation, otherwise in good standing.
3. Good standing would imply that the institution itself, its directors, controllers and senior managers had not during the past 5 years been the subject of material disciplinary action by a regulator or professional body, or subject to any conviction for fraud, dishonesty or related offences of a financial nature.
4. The Guernsey licensed service provider associated with the application for consent under the Control of Borrowing Ordinance must certify to the Commission that they have performed sufficient due diligence to be satisfied that the promoter and/or investment manager are fit and proper. In that regard, such service providers should take account of the issues referred to at 9(a), (b) and (c) below and should document their findings and conclusions accordingly.
5. For the avoidance of doubt, applications on behalf of newly formed promoters and/or investment managers will be considered. The Guernsey licensed service provider who is seeking the fund's consent will need to consider the track record and experience of the controllers, directors and management of such entities taking into account their previous employment history. Such previous employment history should demonstrate that the individuals possess relevant experience in relation to managing or advising on investors' funds using similar investment strategies to those that will be adopted by the Registered Closed-end Investment Fund. The licensed service provider's consideration of these matters and conclusions arising should be documented.
6. Where applicants are aware of issues in relation to a promoter and/or investment manager (which term should be taken to include their controllers, directors and management) and associated parties, but are uncertain of their materiality or possible impact on the subject application, they should consult Commission staff prior to submitting the formal application at the time they become aware of the issue.
7. Commission staff will assess licensees' application due diligence as part of their post-facto monitoring of licensees. If the Commission were to find that warranties provided were defective, or misleading, the Commission will consider taking action against the licensee and in appropriate cases would exclude that licensee from future participation in the self-certification programme.
8. The Commission expects each licensee to ensure that its due diligence in respect of the promoter and/or investment manager and associated parties is updated on a regular basis. The Commission will not prescribe the means by which this requirement is to be achieved but as set out in 4 above licensees should take account of the issues at 9(a), (b) and (c) below and should document their findings and conclusions. Where licensees become aware of issues in relation to a promoter and/or investment manager (which term should be taken to include their controllers, directors and senior management) and associated parties, but are uncertain of their materiality or possible impact on the subject Registered Closed-end Investment Fund, they should consult Commission staff, prior to the submission of a formal application to the Commission, at the time they become aware of the issue.
9. Promoters and/or investment managers (including their directors, controllers and senior managers) must be fit and proper. This can be defined as being a requirement for integrity (or honesty), competence and solvency. Guernsey licensed service providers should ensure that the following issues are covered as part of their due diligence procedures in respect of new client relationships and that their findings and conclusions are documented.
 - (a) Integrity

Promoters and/or investment managers (which term should be taken to include their controllers, directors and senior

management) should be of a high reputation and standing. Poor reputation would be considered to be a negative factor.

The promoter and/or investment manager must carry on their business with prudence, professional skill and honesty.

In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established, the integrity of the controllers, directors and senior management should be assessed in the light of previous employment and experience. It would be expected that the Guernsey licensed service provider would make direct contact with relevant individuals' previous employers as part of the necessary due diligence enquiries.

Promoters and/or investment managers would be expected to deal openly and honestly with the Commission and any other regulatory authority to whose regulation they are subject (either on a consolidated basis or directly).

(b) Solvency

Promoters and/or investment managers should be solvent. A firm regulated in another jurisdiction should also comply with the solvency, capital adequacy or financial resources requirement (as appropriate) laid down by the relevant regulatory body to which it is accountable. Past performance in this respect should also be considered to ensure that relevant requirements have been consistently met in the past.

A promoter and/or investment manager that is not regulated would be expected to maintain a surplus of shareholders' funds as disclosed in its audited financial statements. Past performance in this respect should also be considered to ensure that relevant requirements have been consistently met in the past.

Promoters and/or investment managers would be expected to maintain adequate net

liquid assets such that they are able to settle their debts when they fall due.

In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established (that is, not being able to produce audited annual financial statements for a period of at least 24 months), it will be necessary for the Guernsey licensed service provider to consider financial projections relating to the proposal under consideration. It will also be necessary to consider whether the controllers, directors and management of such promoters and/or investment managers have previously been responsible for considering the solvency of an entity (for example, if they held a director role or financial control function). Where individuals have been directors or held relevant positions at entities that have gone into liquidation or suffered financial loss it will be necessary to consider the role undertaken by the relevant individual in such situations.

(c) Competence

The most obvious way to demonstrate competence is to have established a favourable track record, in a business similar to that to be conducted in the Bailiwick.

The promoter and/or investment manager should be able to demonstrate an acceptable complaints history. In the case of promoters and/or investment managers with a limited history, due to the fact that they are newly or recently established, it will be necessary for Guernsey licensed service providers to consider whether the controllers, directors and management of such entities have been subject to significant complaints whilst employed by other firms.

Promoters and/or investment managers should have staff of adequate skills, knowledge and experience to undertake and fulfil their duties efficiently and effectively.

CONSENT UNDER THE CONTROL OF BORROWING ORDINANCE

1. In order to consider granting the requisite consent to the Registered Closed-end Investment Fund the Commission must receive a copy of the application form (Form REG), which must be signed by the proposed administrator of the fund. The form contains the following requirements:

- (a) Warranties to the Commission from the proposed administrator that they have performed sufficient due diligence to be satisfied that:
 - (i) the promoter and associated parties are fit and proper;
 - (ii) effective procedures are in place to ensure that the fund is not offered directly by the issuer to the public within the Bailiwick of Guernsey. For the purposes of this framework the public means any person not regulated under any of Guernsey's financial services regulatory laws; and
 - (iii) the status of the Registered Closed-end Investment Fund is specifically referred to in the prospectus, offering document or equivalent such that neither the Commission nor the States of Guernsey Policy Council have reviewed the prospectus, offering document or equivalent and that neither the Commission nor the States of Guernsey Policy Council takes any responsibility for the financial soundness of the fund or for the correctness of any of the statements made or opinions expressed with regard to it.

The Commission attaches great importance to these warranties. It expects applicants to be able to demonstrate that they have documentary evidence to support the warranties given, and to be able to produce that evidence immediately should the Commission request it. Applicants who cannot substantiate their

applications may, as noted in paragraph 7 of this guidance, find themselves excluded from participation in the Registered Closed-end Investment Fund self-certification programme.

- (b) Submission of fully completed, signed Forms GFA and APC together with Forms PQ in respect of controllers, directors and senior managers of the promoter and fund (as appropriate);
 - (c) Payment of the application fee required under the relevant fees regulations;
 - (d) Submission of certified complete final copies of the following documents:-
 - (i) prospectus, offering document or equivalent;
 - (ii) the application form, subscription agreement or equivalent;
 - (iii) constitutive documents, that is the memorandum and articles of association, trust deed or limited partnership agreement, as applicable;
 - (iv) all material agreements entered into by the fund.
 - (e) The licensing under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended of persons intending to carry on a restricted activity within the Bailiwick of Guernsey in connection with the fund. Reference should also be made to 3 below.
2. The Commission will issue the necessary consent under the Control of Borrowing Ordinance within three working days of receipt/resolution of all of the above issues. Following receipt of the formal application made by the licensed service provider in respect of the proposed Registered Closed-end Investment Fund the Commission will conduct limited enquiries into the parties to be associated with the fund and will consider the fund's investment objectives. Any concerns arising from these enquiries and consideration will be raised with the Guernsey licensed service provider and may, in extreme cases, delay issue of the relevant

consent. Where licensees have questions about any aspect of the proposed fund and its operation or become aware of issues in relation to a promoter and/or investment manager (which term should be taken to include their controllers, directors and management) and associated parties, but are uncertain of their materiality or possible impact on the subject Registered Closed-end Investment Fund, they should consult Commission staff, prior to the submission of a formal application to the Commission, at the time they become aware of the issue. This will assist Commission staff in expediting the formal application. The Commission's limited enquiries and consideration referred to above should not be considered to be a substitute for the licensee's responsibilities referred to in this document.

3. Should the promoter of a Registered Closed-end Investment Fund require the establishment of a Guernsey entity that will undertake controlled investment business in connection with the fund then it will be necessary for such company to be licensed under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended before the relevant authorisation or consent can be issued in respect of the fund. The application process relating to the issue of a licence under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended will normally take longer than the three working days referred to at 2 above.

