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Guernsey: Financial Sector Assessment Program Update—Detailed Assessment of Observance on Insurance Core Principles

This Detailed Assessment of Observation on Insurance Core Principles on Guernsey was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed in December, 2010. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Guernsey or the Executive Board of the IMF.

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FINANCIAL SECTOR ASSESSMENT PROGRAM UPDATE

GUERNSEY

INSURANCE CORE PRINCIPLES

DETAILED ASSESSMENT OF OBSERVANCE

DECEMBER 2010

INTERNATIONAL MONETARY FUND
MONETARY AND CAPITAL MARKETS DEPARTMENT

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ACRONYMS

AIRs	Authorized Insurance Representatives
AML/CFT Handbook	Handbook for Financial Services Businesses on Countering Financial Crime and Terrorist Financing
CED	Commerce and employment department
CGC	Licensed Insurers' Corporate Governance Code
CL	The Companies (Guernsey) Law
Commissioners	Members of the commission
Disclosure Law	Disclosure (Bailiwick of Guernsey) Law
EU	European Union
FSAP	Financial Sector Assessment Program
FSC Law	Financial Services Commission (Bailiwick of Guernsey) Law
GFSC	Guernsey Financial Services Commission
GIIA	Guernsey International Insurance Association
GSCCA	Guernsey Society of Chartered and Certified Accountants
IAIS	International Association of Insurance Supervisors
IOM	Isle of Man
ICCs	Incorporated Cell Companies
ICPs	Insurance Core Principles
IIG	Insurance Institute of Guernsey
IBL	Insurance Business (Bailiwick of Guernsey) Law, 2002
IMILL	Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002
Commissioners	Members of the Commission
MOUs	Memoranda of Understanding
MCR	Minimum capital requirement
MLRO	Money Laundering Reporting Officer
OFC	Offshore Financial Center
ORSA	Own Risk and Solvency Assessment
OSCA	Own Solvency Capital Assessment
PC	States of Jersey Policy Council
PCCs	Protected cell companies
PQ	Personal Questionnaires
UK	United Kingdom
US	United States

EXECUTIVE SUMMARY

Guernsey's status as the largest international insurance center in Europe hinges on its progressive infrastructure and operational flexibility. The insurance industry in Guernsey consists of two distinct sectors: domestic and international. The small domestic sector caters the insurance needs of Guernsey residents and has been consolidating. The international sector represents more than 90 percent of the market and is dominated by captive insurers, who represent 60 percent of the sector. Guernsey continues to attract U.K. reinsurers, with about 50 percent of international business originating from the United Kingdom (UK). The captive market is sensitive to tax changes. Given the maturity of the captive market, continued growth is expected to come from reinsurance and other specialized insurance lines.

The insurance industry is more exposed to external risks than local conditions. The domestic and international sectors have different risk profiles. Domestic insurers are exposed to weather risks in Guernsey. The captive and international life insurers are susceptible to external market developments, e.g., global economic downturn, industry-specific events affecting the parents of captives, or changes in legislative and political climates in the insurers' home markets. Although insurers generally adopt prudent investment strategies, their performances were affected by the global financial crisis.

Guernsey updates its regulatory regime continually and has implemented all the recommendations arising from the 2003 Offshore Financial Center (OFC) assessment. The Guernsey Financial Services Association (GFSC) adopts a risk-based and proportionate approach in supervising its large population of insurers, which promotes efficient allocation of regulatory resources. The GFSC gives licenses to captive insurers individually and adopts consistent prudential regulation for both captive and commercial insurers. On-going supervision of captives is exercised through insurance managers. The GFSC has adequate powers and well-documented policies, procedures, and customized checklists to ensure consistency in supervisory decisions. The introduction of the Own Solvency Capital Assessment (OSCA) by insurers has been well received by the industry. The regulatory frameworks for corporate governance, risk management, and Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) are comprehensive and robust.

While the updated regulatory framework has a high level of observance with the Insurance Core Principles (ICPs), there is scope for enhancements. Given the dominance of the international sector, the GFSC has a keen interest in establishing effective cooperation arrangements with relevant home/host supervisors in respect of recognized insurers without a physical presence, and to protect foreign policyholders of international life insurers. The GFSC should also consider expanding its range of enforcement powers and how best to implement the public disclosure standards established by the International Association of Insurance Supervisors (IAIS). The mission advised the GFSC to continually assess the practical implementation of OSCA, including establishing criteria on the use of internal models.

I. ASSESSMENT OF INSURANCE CORE PRINCIPLES

A. Introduction and Scope

1. **This assessment benchmarks Guernsey's regulatory regime against the ICPs issued by the IAIS in October 2003.** It also took into account relevant IAIS standards and guidance in addition to the ICPs. The assessment was conducted from March 1 to 10, 2010 under the Fund's Financial Sector Assessment Program (FSAP).[1]

2. **Guernsey's insurance regulatory regime was previously assessed in 2002, as part of the Fund's OFC Module 2 assessment, against the ICPs issued in October 2000.** The status of implementation of the previous recommendations is summarized in Appendix 1.

3. **The assessment covers all regulated entities licensed by the GFSC, including captive insurers and insurance intermediaries.** The regime applicable to captive insurers is benchmarked against the IAIS Guidance Paper on the Regulation and Supervision of Captive Insurers.

B. Information and Methodology Used for Assessment

4. **The level of observance for each ICP reflects the assessment of the essential criteria only.** Advanced criteria are not taken into account in assessing observance of the ICPs. On the basis of the assessment, each ICP is rated in terms of the level of observance as follows:

(i) Observed—when all the essential criteria are considered to be observed or when all the essential criteria are observed except for those that are considered not applicable.

(ii) Largely observed—when only minor shortcomings exist, which do not raise any concerns about the authority's ability to achieve full observance.

(iii) Partly observed—when, despite progress, the shortcomings are sufficient to raise doubts about the authority's ability to achieve observance.

(iv) Not observed—when no substantive progress toward observance has been achieved.

5. **The assessment is based solely on the laws, regulations, and other supervisory requirements and practices that are in place at the time of assessment.** Ongoing regulatory initiatives are noted by way of additional comments. The assessment took account of the GFSC's self-assessment and further information provided in response to a pre-mission questionnaire. The GFSC facilitated the assessment with the provision of full documentation of all relevant laws, regulations, and codes. The mission also received valuable inputs from

[1] This assessment was performed by Ms. Su Hoong Chang, Insurance Supervision Advisor, engaged by the IMF.

industry associations, insurers, insurance intermediaries, and professionals operating in Guernsey.

6. **The mission is grateful to the GFSC for its full cooperation and thoughtful logistical arrangements and coordination of various meetings with industry participants.** Discussions with and briefings by the GFSC officials during a series of technical meetings facilitated a meaningful assessment of Guernsey's regime.

C. Overview—Institutional and Macro Prudential Setting

Market structure and industry performance

7. **The insurance industry in Guernsey comprises two distinct segments: domestic and international.** At December 31, 2009 there were 699 insurance entities operating in Guernsey (Table 1). There were 21 domestic insurers and 678 international insurers; the latter segment included 323 cells in protected cell companies (PCC)[2] and incorporated cell companies (ICCs.)[3] The industry is also well served by 21 insurance managers and 40 insurance intermediaries. Total premiums written by Guernsey insurers in 2008 amounted to £3.3 billion and they held gross assets totaling £21.0 billion. The insurance sector employed approximately 840 staff in 2009.

8. **The domestic insurance segment caters to the insurance needs of residents and risks based in Guernsey.** Besides four locally incorporated insurers, a number of Guernsey branches of U.K. insurers are licensed to write "domestic business" i.e., insuring local residents and risks based in Guernsey including assets of trusts and companies managed on the island. Two of the locally incorporated insurers are friendly societies that offer short-term sickness benefits. The domestic market has been consolidating, mainly through mergers and acquisitions.

9. **There are about 30 active foreign recognized insurers conducting domestic businesses without a physical presence.** The GFSC has a policy of recognizing foreign insurers either by description (i.e., insurers licensed in the European Union (EU), Jersey, and Isle of Man (IOM)) or via notification. During the mission, the GFSC clarified its policy to reflect actual practice, i.e., there were only recognized insurers from the UK and IOM. Recognized insurers may carry on insurance business in Guernsey only through licensed insurance intermediaries. An insurer seeking recognition must submit a notification form providing details of its home supervisor and a description of the business it is authorized to undertake. The GFSC acknowledges receipt of the notifications and relies on the relevant

[2] A PCC is a single legal entity divided into an unlimited number of cells whose assets and liabilities are legally segregated from each other and from the general assets of the "core" cell.

[3] An ICC is a legal structure where each of the cells is a separate company in its own right with limited liabilities. It is unlike the PCC structure, where the cells are not separate companies.

home supervisors to supervise recognized insurers. Insurance intermediaries must declare the recognized insurers they deal with to the GFSC annually.

10. **Guernsey is the largest captive insurance centre in Europe.** Its international insurance sector comprises captives and commercial insurers writing an extensive range of businesses. General insurers offer for example, employers/public liability, business interruption, motor, property damage, catastrophe risks, and hull liability. The international life insurers service the life and health insurance needs of expatriates and high-net-worth individuals as part of their wealth management strategies, and provide insurance-based employee benefits. Three of the largest multinational employee benefit insurance networks are represented in Guernsey.

Table 1. Guernsey: Breakdown of Licensed Insurers

Type		Number
Domestic insurers		**21**
International insurers:		
Life insurer/reinsurer	21	
Life insurer/reinsurer cells	78	**99**
General insurer/reinsurer	44	
General insurer/reinsurer cells	67	**111**
Captive insurers	290	
Captive insurers cells	178	**468**
Total		**699**

11. **Captive insurers/cells account for approximately 60 percent of the market.**[4] The captives operating in Guernsey have a diverse range of operations in terms of scale, nature, and complexities. The majority of captives are owned by U.K. parents. Approximately 60 percent of captive insurers employ fronting arrangements[5] generally using EU insurers, mainly from the UK. Typically, a fronting insurer requires the captive to provide collateral, e.g., letters of credit that meet regulatory standards, to protect its legal and credit exposures. All but one captive insurer are managed by insurance managers.

[4] Captive insurance is defined by the IAIS as "an insurance or reinsurance entity created and owned, directly or indirectly, by one or more industrial, commercial, or financial entities, the purpose of which is to provide insurance or reinsurance cover for risks of the entity or entities to which it belongs, or for entities connected to those entities and only a small part if any of its risk exposure is related to providing insurance or reinsurance to other parties."

[5] In many jurisdictions, mandatory insurance, such as motor third party liability and workers compensation, can be underwritten only by an insurer licensed in that jurisdiction. To insure such risks with a related captive that is not located/licensed in that jurisdiction, a parent company will arrange with a licensed insurer to accept the risks with a back-to-back "reinsurance" to a related captive.

12. **Guernsey continues to attract U.K. reinsurers and insurance businesses from the UK.** As at end-December 2009, 210 (59 percent) of the 355 international insurers, and 36 percent of the 323 international reinsurer cells are owned by U.K. parents. Approximately 40 percent of the U.K. FTSE 100 companies and 95 of the global 1500 companies own captives in Guernsey. About 50 percent of the international business originated from the UK; the remaining business originates from a variety of jurisdictions.

13. **Guernsey's captive insurance market is mature and stable.** Guernsey pioneered the legislation for the PCCs and introduced the ICC legislation in 2006. While the effect of the intended legal segregation of the PCC has not been fully tested in any court, the GFSC and market practitioners believe that the PCC concept is legally robust. The legislation has now been in force for over 13 years and in that time—despite being widely used in a number of jurisdictions—it has not been subject to any legal challenge. The Guernsey authorities consider that the lack of any legal challenge indicates that the PCC concept has been accepted as robust. Future growth is expected in the areas of the PCC/ICC formations and reinsurance. While a "hard market" (i.e., high, commercial premium rates) may make captive formations more attractive, the captive market in Guernsey is mature and less market sensitive. The GFSC expects reinsurance to grow—following the licensing of Lloyd's syndicates in Guernsey—while recognizing that expansion in this sector has to be supported by adequate specialist staff.

14. **Guernsey's insurance industry is more exposed to external risks than local conditions, reflecting the dominance of the international sector.** Catastrophic weather conditions in Guernsey would only impact local insurers underwriting motor and property insurance. A sustained worldwide economic downturn could affect the captive and international life insurers, who are dependent on foreign interests. As life insurers offer mainly unit-linked products (policyholders typically bear the investment risks), market risks have minimal impact on their technical provisions and solvency requirements. However, industry participants highlighted that changes in Guernsey's tax regime that are likely to result from a current review of corporate taxation may have a significant impact on the captive sector.

15. **The GFSC is mindful of the implications of global market and regulatory developments for Guernsey as an international financial centre.** In particular, the EU Solvency II Directive may have an impact on some captive reinsurers, such as those who use EU fronting insurers. This is because reinsurance cessions to reinsurers subject to a solvency regime that is not Solvency II equivalent may not be fully admissible for the purpose of solvency requirements applied to the ceding insurers. The GFSC is committed to following international standards in enhancing its risk-based solvency regime. The GFSC is currently assessing its impact on the Guernsey insurance sector in the event that Guernsey decides to implement a risk-based solvency regime. An independent review of the implications of Guernsey seeking recognition of Solvency II equivalence has been commissioned by the

commerce and employment department (CED). The GFSC is fully involved in that review and is working with the CED on investigating the implications of Solvency II.

16. **While Guernsey's insurance industry has adopted prudent investment strategies, it has not been immune to the world financial crisis.** A number of insurers' parent companies were affected and a small number of captive insurers had exposures to Icelandic banks or Icelandic parents. Some captives placed reinsurance with a reinsurer group that was in distress, but the impact was determined to be immaterial. Several insurers, which wrote mortgage indemnity business, ceased business and returned capital to their parent companies. Life insurers did not suffer losses as the majority of their business is unit-linked, although profitability was reduced due to lower management fees derived from reduced policy values.

17. **The GFSC responded proactively to the global financial crisis.** The GFSC worked with the relevant insurance managers to resolve issues that arose from the crisis and assessed the financial condition of the parent companies of some captives. The relevant insurers affected by the crisis were closely monitored. The GFSC also required insurers who relied on loans to parent companies to meet solvency requirements to reapply for such loans to qualify as approved assets and GFSC imposed restrictions in some cases. As at March 3, 2010, insurers' loans to parents totaled £5.8 billion of which £5.2 billion was approved for solvency purposes, representing 33 percent of net assets.[6]

Institutional framework and arrangements

18. **The GFSC is the integrated regulator for the financial sector in Guernsey.** The GFSC was established under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 (FSC Law). The GFSC's main function is to take such steps as it considers necessary or expedient for maintaining confidence in the safety, soundness, and integrity of the financial services sectors in Guernsey. It is also responsible for countering financial crime and the financing of terrorism, pursuant to Guernsey's AML/CFT legislation. The GFSC does not have any mandate for the promotion and development of the financial services sector. The CED is responsible for the development of the industry while the responsibility for promotion sits with the Guernsey Ministry of Finance.

19. **The activities of the GFSC's executive are overseen by the members of the commission (Commissioners), who are elected by the States of Guernsey from persons nominated by the States of Guernsey Policy Council (PC).**[7] The chairman and vice-chairman are appointed for a period of one year, while each commissioner is appointed for a period not exceeding three years. The PC is responsible for international financial matters

[6] These figures are skewed by two large captive insurers. If the loans by these two captives are excluded, loans to parents amounting to £1.1 billion of which £392 million (or 2.2 percent of net assets) was approved for solvency purpose.

[7] All the commissioners are non-executive—three reside in Guernsey, with the remainder living in the UK.

and establishing the policy framework for financial regulation, including the government's relationship with, and reporting lines for, the GFSC.

20. **The Insurance Division of the GFSC is responsible for regulating and supervising insurers; insurance managers and intermediaries.** The insurance regulatory framework is governed under the Insurance Business (Bailiwick of Guernsey) Law, 2002 (IBL) and the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002 (IMIIL).

21. **The IBL provides the legal basis for regulating all categories of insurers and reinsurers, including captives.** It empowers the GFSC in supervising (a) licensing of insurers; (b) changes in control; (c) solvency and capital requirements; and (d) disclosure and regulatory requirements. It also sets out the legal authorities of the GFSC for a range of regulatory measures. Regulations and codes made under the IBL enhance the requirements under the IBL in areas such as licensing, annual returns, approved assets, and corporate governance. The GFSC licenses captives individually and exercises supervision of captives through their appointed insurance managers.[8] Where a captive is not managed by an insurance manager, the GFSC supervises the captive directly. Consistent prudential regulatory requirements apply to both commercial and captive insurers.

22. **The IMIIL covers insurance managers and intermediaries,[9] including licensing, changes in control, and disclosure of information.** The GFSC has issued regulations, codes, and rules pursuant to the IMIIL to detail supervisory expectations in licensing, annual returns, safeguarding client monies, and market conduct.

23. **Guernsey is considering the establishment of a Financial Services Ombudsman**. In August 2008, the GFSC issued a consultative paper revisiting the introduction of an ombudsman scheme, intended to cover all types of regulated financial services business.[10]

24. **The GFSC has taken a conscious decision not to establish a policyholder compensation scheme.** The policy position is that life policyholders are better-protected under the segregated trust fund that long-term insurers are required to maintain. Assets representing at least 90 percent of policyholder liabilities must be held in trust by a

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[8] s1 of IMIIL: An insurance manager is defined as a person who exercises, in relation to any insurer of which he is not an employee, managerial functions (including administration and underwriting) or such other functions as may be prescribed by the GFSC.

[9] s2 of IMIIL: an insurance intermediary is a person, other than an insurance representative, who by way of a business: (a) advises clients on their insurance requirements; and/or (b) arranges contracts of insurance between insurers and clients. An insurance representative is an individual who acts on behalf of—and under a contract of or employment with an agency—an insurer or insurance intermediary, for the purpose of arranging contracts of insurance for clients and giving advice to those clients.

[10] In 2002, the States of Guernsey Advisory and Finance Committee issued a consultation document, which set out proposals for a financial services ombudsman scheme for Guernsey.

Guernsey-based trustee licensed for fiduciary business by the GFSC. The trustee must report full details of the assets held by it to the GFSC at least quarterly and must also inform the GFSC if the insurer instructs a withdrawal of more than 5 percent of the market value of the assets held within one month. The trustee may hold the assets either directly or may appoint a custodian to hold the assets. Custodians do not have to be Guernsey-based. This trust fund requirement does not apply to general insurance, including mandatory insurances. The GFSC has obtained legal advice, which confirmed that the FSA Handbook treats policies issued by U.K. insurers to Guernsey policyholders as protected contracts of insurance, and hence they are protected by the U.K. Financial Services Compensation Scheme in respect of policies taken out with U.K. insurance companies, whether licensed (as branches) or recognized by the GFSC. The GFSC opines that policyholder compensation arrangements for domestic business of locally incorporated domestic insurers would be unworkable given the scale and structure of the market.

25. **The GFSC has established the decisions committee procedures to consider adverse decisions in relation to regulated entities proposed by the GFSC's executives.**[11] The decisions committee comprises at least three commissioners. Adverse decisions include license applications and conditions, suspension or revocation of licenses, objections to controllers or key officers, and imposing financial penalties. The decision committee may take an adverse decision if the need arises. The FSC Law was amended to empower the GFSC to impose financial penalties as from 2008.

26. **The GFSC introduced Own Solvency Capital Assessment (OSCA) in 2008 to take account of evolving international standards.** OSCA is applicable to all insurers, including captives. The objective is to ensure that the boards of insurers consider their own specific risk profile in determining the appropriate level of capital to be held. The GFSC has issued the Guidance Note on Licensed Insurers' Own Risk and Solvency Assessment detailing the risk factors that should be taken into account. The minimum solvency margin, calculated on a formulaic basis, acts as the lower solvency control level where a breach requires immediate rectification. The OSCA acts as the upper solvency control level and the GFSC may intervene, if it is breached, e.g., by impose licensing conditions to increase capital or reduce risks.

[11] The executive comprises at least three of the following: director general or directors of banking, fiduciary and intelligence services, insurance, investment business, and policy and international affairs.

Table 2. Guernsey: Summary of Compliance with the Insurance Core Principles

Insurance Core Principles	Grading	Comments
ICP 1 - Conditions for effective insurance supervision	O	Guernsey has well-established policy, legal, and institutional frameworks. The GFSC recognizes accounting, auditing and actuarial standards, and professional bodies from reputable jurisdictions and relies on these associations for the enforcement of professional standards and ethical codes. It is well served by a substantial pool of professionals operating locally or from abroad. Insurers have access to well functioning financial markets. It is important that auditors and actuaries have a clear understanding of the GFSC's expectations of their roles with respect to regulated entities so that they can act accordingly, thereby enabling the GFSC to place reasonable reliance on their work.
ICP 2 - Supervisory objectives	O	The GFSC's objectives and functions are clear and appropriate and it does not have any objective related to the promotion of the insurance industry. Recognized insurers permitted to write domestic risks without any physical presence in Guernsey (see ICP 6) may have implications to the GFSC's objective to protect domestic policyholders.
ICP 3 - Supervisory authority	O	The GFSC has adequate powers, legal protection, and resources. It is operationally and financially independent and accountable in the exercise of its functions and powers. While strict confidentiality applies to official information obtained in the course of duties, the GFSC may disclose confidential information under an appropriate range of specified circumstances.
ICP 4 - Supervisory process	O	The GFSC supervisory approach and processes are defined and transparent. Internal procedures are in place to ensure consistency in supervisory decisions. It has clear accountabilities to the States, and the public through various means. While the GFSC publishes selected industry information, there is scope for providing more comprehensive information to facilitate better understanding of the financial condition of the insurance industry, e.g., technical performance for domestic and international sectors.
ICP 5 - Supervisory cooperation and information sharing	O	GFSC regularly exchanges information with other supervisors and has signed eight MoUs with foreign supervisors covering the insurance sector. The GFSC has also applied to become a signatory to the IAIS Multilateral MoU.
ICP 6 - Licensing	O	The GFSC's licensing framework is clear and transparent and effectively implemented. It relies on the relevant home supervisor on prudential supervision of recognized insurers. During the mission, it has clarified

Insurance Core Principles	Grading	Comments
		publicly the criteria for recognition to reflect current practice, i.e., only from UK and IOM where domestic policyholders are protected under the compensation schemes of the respective jurisdictions.
ICP 7 - Suitability of Persons	O	The GFSC performs due diligence on any proposed owner, controller or director prior to licensing and in approving any subsequent changes in control or directors. Auditors and actuaries are assessed on their qualifications and experience and the GFSC is empowered to issue disqualification orders against auditors and actuaries.
ICP 8 - Changes in control and portfolio transfers	O	The GFSC assesses prospective owners and controllers in exactly the same way as for a new license application. Any person wishing to acquire 15 percent or more of an insurer requires the prior approval of the GFSC. Portfolio transfers must be approved by the GFSC or the Court, depending on the nature of the business to safeguard policyholders' interests.
ICP 9 - Corporate governance	O	The CGC applies to all insurers and incorporates the requirements of ICP 9. The boards of insurers are expected to apply the CGC in a manner appropriate to the nature, scale, and complexity of their business. Insurers must certify the level of adherence to the CGC on an annual basis and to explain where they consider elements of the CGC do not apply to them.
ICP 10 - Internal Controls	O	Regulatory requirements relating to internal controls are incorporated into CGC and are monitored during The GFSC's on-site visits. In practice, most captives rely on the internal procedures and controls of their appointed insurance managers.
ICP 11 - Market Analysis	O	The GFSC proactively monitors market developments both locally and globally, taking account of external events that affect relevant industry sectors of the parent companies of captive insurers.
ICP 12 - Reporting to supervisors	O	The GFSC has a well-developed and consistent process for reviewing annual returns and monitoring insurers' operations on an on-going basis.
ICP 13 - On-site inspection	O	The GFSC has clear and well-documented inspection policies and procedures and adopts a three-year rolling program for inspection. Under its risk-based supervision approach, insurers with high risk ratings are supervised more closely.
ICP 14 - Preventive and corrective measures	O	The GFSC is empowered to and does take a range of proportionate measures to address supervisory concerns.
ICP 15 - Enforcement or sanction	O	The GFSC has the legal powers to take enforcement actions or impose appropriate sanctions. There is a structured and transparent process in respect of

Insurance Core Principles	Grading	Comments
		adverse decisions against licensees and persons. However, its main tool is the imposition of licensing conditions and there is scope for a review to widen its enforcement powers.
ICP 16 - Winding-up or exit from the market	LO	The legal framework provides for orderly winding up and exits from the market, that takes into account the rights and interests of policyholders and beneficiaries. However, policyholders and beneficiaries are not given legal priority in the event of insolvency.
ICP 17 - Group-wide supervision	NA	The GFSC currently has no responsibilities as group/home supervisor of any insurance group. It is committed to establish an appropriate framework for group supervision when it acquires such responsibilities.
ICP 18 - Risk assessment and management	O	The GFSC has provided guidance to the industry on their risk assessment and risk management. Its risk-based approach to supervision addresses the risk profile of insurers and intermediaries systematically using a risk matrix. It is important for the risk matrix to be updated and enhanced as the GFSC gains experience and to take account of emerging risks.
ICP 19 - Insurance activity	O	The GFSC requires insurers to have in place strategic underwriting and pricing policies approved and reviewed regularly by the Board of directors. It checks that insurers manage their insurance risks effectively. The GFSC approves applications from captive insurers to have no reinsurance protection on a case-by-case basis.
ICP 20 - Liabilities	O	The CGC requires insurers to maintain adequate technical provisions and other liabilities. While there is no explicit legal provision on technical provisions, the GFSC may impose licensing conditions, where appropriate. In practice, insurers are expected to maintain adequate technical provisions under the CGC and the GFSC checks insurers' methodology in estimating technical provisions.
ICP 21 - Investments	O	The GFSC has established clear regulatory requirements relating to insurers' investment activities. Insurers are also required to conduct resilience testing as part of their OSCA.
ICP 22 - Derivatives and similar commitments	O	The GFSC's regulatory rules for derivative activities are well developed.
ICP 23 - Capital adequacy and solvency	O	The GFSC has taken a proactive approach in the introduction of OSCA and implementing a more risk-based solvency regime. It is advised to continually assess the practical implementation of OSCA, including establishing criteria on the use of internal models.
ICP24 - Intermediaries	O	GFSC has a comprehensive framework for regulation and on-going supervision of the market conduct of insurance managers and intermediaries.

Insurance Core Principles	Grading	Comments
ICP 25 - Consumer Protection	O	Regulatory measures to protect domestic policyholders are implemented via market conduct supervision of domestic insurers and intermediaries. However, GFSC has no jurisdiction over overseas intermediaries working with international life insurers, who have significant business volumes in a number of jurisdictions.
ICP 26 - Information, disclosure and transparency towards markets	PO	The IBL requires limited disclosures and only upon specific requests of policyholders and potential policyholders. The objective of ICP 26 is to facilitate market discipline through public disclosure to all stakeholders, including market analysts. GFSC has issued a consultation paper on public disclosure.
ICP 27 - Fraud	O	GFSC has set clear requirements and provided meaningful guidance to insurers, insurance managers and intermediaries to combat insurance fraud.
ICP 28 - Anti-money-laundering, combating the financing of terrorism	O	GFSC applies robust AML and CFT requirements to insurers and intermediaries for both life and general insurance products. It supervises compliance through on-site inspections. The AML/CFT handbook provides guidance to insurers and intermediaries in adopting a risk-based approach to AML/CFT.

Summary of Grading

Observed (O)	25
Largely observed (LO)	1
Partly observed (PO)	1
Not Applicable (NA)	1
Total	**28**

Recommended Action Plan and Authorities' Response to the Assessment

Table 3. Guernsey: Recommended Action Plan to Improve Observance of Insurance Core Principles

Insurance Core Principles	Recommended Action
ICP 1 - Conditions for effective insurance supervision	While it is not unreasonable for the GFSC to rely on oversight and professional bodies in other countries to establish and enforce professional standards, it is recommended that the GFSC consider providing clear guidance to accountants, auditors, and actuaries on their respective roles, including professional independence, with respect to regulated entities.
ICP 2 - Supervisory objectives	The GFSC is advised to have a clear articulation of its regulatory and supervisory scope as well as objectives in protecting domestic policyholders in respect of recognized insurers.
ICP 15 - Enforcement or sanctions	The GFSC should review its heavy reliance on licensing conditions to take enforcement actions and consider establishing a wider range of enforcement powers, e.g., appointment of judicial managers and receivers.
ICP 16 - Winding-up or exit from the market	To safeguard policyholders' interests, the GFSC should consider establishing (a) an explicit legal provision in legislation to ensure that policyholders and claimants are given high priority in the event of insolvency; and (b) regulatory policies on pledging or encumbrance of assets by insurers.
ICP 18 - Risk assessment and management	The GFSC is advised to refine the risk matrix to incorporate explicit factors that address insurers' corporate governance and risk management framework.
ICP 19 - Insurance activity	For transparency and consistency, the GFSC is advised to provide guidance on how it assesses the insurance risks of captive insurers seeking approval to have no reinsurance protection.
ICP 20 - Liabilities	The GFSC is advised to consider including an explicit legal provision in the IBL requiring insurers to maintain adequate technical provisions at all times.
ICP 25 - Consumer Protection	The GFSC is advised to consider effective regulatory cooperation with relevant regulatory authorities to enhance the protection of policyholders located outside of Guernsey.
ICP 26 - Information, disclosure and transparency towards markets	The GFSC should consider how best to implement the public disclosure standards established by the IAIS.[12]

[12] Technical Performance and Risks for Nonlife Insurers and Reinsurers, Technical Risks and Performance for Life Insurers and Investment Risks and Performance for Insurers and Reinsurers.

Authorities' response to the assessment

ICP 1	The GFSC will consider how best to address the IMF's recommendations.
ICP 2	Work is under way to provide improved transparency in relation to the protection of domestic policyholders in respect of recognised insurers.
ICP 15	The GFSC will consider how best to address the IMF's recommendations.
ICP 16	The GFSC will be working with the relevant parties to improve the legislation with respect to policyholders and claimants in the event of insolvency.
ICP 18	The GFSC's risk matrix is being reviewed to incorporate the additional risk factors.
ICP 19	The GFSC will consider how best to address the IMF's recommendations.
ICP 20	The position on technical provisions will be addressed when the insurance legislation is reviewed following the revision of the IAIS ICPs in October 2011.
ICP 25	The GFSC will consider how best to address the IMF's recommendations.
ICP 26	Disclosure rules, which have already been made, come into force in September 2010 and will be reviewed against the revised IAIS ICPs when they are issued in October 2011 to ensure they are both adequate and appropriate.

II. DETAILED PRINCIPLE-BY-PRINCIPLE ASSESSMENT METHODOLOGY

Conditions for Effective Insurance Supervision	
Principle 1.	Conditions for effective insurance supervision Insurance supervision relies upon: • a policy, institutional, and legal framework for financial sector supervision; • a well-developed and effective financial market infrastructure; and • efficient financial markets.
Description	The FSC Law[13] empowers the GFSC to exercise effective supervision of finance businesses in Guernsey and to take steps to maintain confidence in Guernsey's financial services sector as well as for the safety, soundness, and integrity of that sector. The IBL and IMIIL set out the legal framework for supervising the insurance industry. Guernsey's judiciary comprises the magistrate's court (limited jurisdiction), the royal court (unlimited criminal jurisdiction), and the court of appeal. The Court of Alderney in Alderney and the Court of the Seneschal in Sark have limited jurisdiction. More serious cases from these islands are tried in the Royal Court of Guernsey. The majority of the judges of the court of appeal are English Queen's Counsel. All judges are appointed by the English Crown. Appeals against the decisions of the court of appeal may be made to the Judicial Committee of the Privy Council in the UK. Reference may be made to the European Court of Justice on matters covered by Protocol 3 (which defines the relationship between Guernsey and the EU). Guernsey, being bound by the European Convention on Human Rights, is subject to the jurisdiction of the Court of Human Rights in Strasbourg. Judges are independent of the governments on the islands. The royal court civil rules provides that the court shall actively manage cases including encouraging and facilitating the use of appropriate alternative dispute resolution mechanisms.[14] The IBL and IMIIL require insurers to prepare annual accounts using recognized accounting standards. The GFSC has prescribed the International Financial Reporting Standards, U.K. GAAP, and U.S. GAAP as recognized accounting standards. The use of any other accounting standards would require the approval of the GFSC. Insurers and intermediaries must have their accounts audited and notify the GFSC of

[13] s2 of FSC Law.

[14] s38 of the Royal Court Civil Rules, 2007, which came into force in early 2008.

	appointments and changes of auditors. An auditor must notify the GFSC upon his resignation/removal, when an audit report is qualified, as well as on circumstances that should be brought to the attention of the GFSC.[15] Insurers carrying on long-term businesses must furnish actuarial reports in accordance with relevant professional standards. They must also notify the GFSC of appointments and changes of actuaries. Actuaries have whistle-blowing obligations to the GFSC. There are more than 650 qualified accountants operating in 35 practicing firms in Guernsey, including the "big four." The Guernsey Society of Chartered and Certified Accountants (GSCCA) is an industry association for accountants with no power to enforce professional standards or disciplinary powers. Actuaries in Guernsey may be members of the Channel Islands Actuarial Society, which is also a member body with no power to enforce professional standards or disciplinary powers. Auditors and actuaries of licensee are approved at the licensing stage and when there are any changes. Auditors and actuaries must be members of an appropriate professional body who set and enforce standards of professional conduct for their members,[16] e.g., the Institute of Chartered Accountants in England and Wales, Fellows of the Institute of Actuaries in England and Wales or the Faculty of Actuaries in Scotland or any other person approved by the GFSC.[17] The GFSC looks to professional bodies in the relevant jurisdictions for the enforcement of accounting, auditing, and actuarial standards. To date, there has not been any disciplinary action taken in Guernsey by the GFSC against any accountant, auditor or actuary for unsatisfactory professional conduct. While the IBL empowers the GFSC to disqualify auditors and actuaries, no such order has been issued. Economic, financial, and social statistics are published annually by the Policy and Research Unit of the States in a report entitled "Guernsey Facts and Figures." These statistics are available in book form and on the States website. Guernsey has no currency exchange control restrictions and shares the pound sterling currency with the UK, Jersey and the IOM. The insurance industry has access to the same asset range as U.K. insurers. Insurers may also tap international markets if investments denominated in euro, U.S. dollars or other currencies are required for matching purposes. A number of U.K. and international banks have branches in Guernsey. Guernsey has a large investment and securities infrastructure comprising management, administration, and custody of open and closed-ended

[15] S34, s35 & s36 of IBL and s21, s22 & s23 of the IMIIL.

[16] S260 of CL and schedule 5 of the IBL.

[17] s40 & s41 and schedule 5 of the IBL.

	collective investment funds, discretionary and nondiscretionary asset management, stock broking, and investment advice. Guernsey also hosts the Channel Islands Stock Exchange, which is recognized by a number of other major exchanges around the world. To deepen the pool of insurance expertise, the Guernsey government and the GFSC proactively support the skills upgrading and training initiatives taken by industry associations. The Insurance Institute of Guernsey, a local Institute of the Chartered Insurance Institute, currently has some 300 members. The Guernsey International Insurance Association offers training courses to insurance managers. The GFSC adopts a rolling program to update relevant insurance laws and regulations, as necessary, to take account of international standards and to reflect current best practices and industry conditions.
Assessment	Observed
Comments	Guernsey has well-established policy, legal, and institutional frameworks. The GFSC recognizes accounting, auditing, and actuarial standards, and professional bodies from reputable jurisdictions and relies on these associations for the enforcement of professional standards and ethical codes. It is well served by a substantial pool of professionals operating locally or from abroad. Insurers have access to well functioning financial markets. It is important that auditors and actuaries have a clear understanding of the GFSC's expectations of their roles with respect to regulated entities so that they can act accordingly, thereby enabling the GFSC to place reasonable reliance on their work. While it is not unreasonable for the GFSC to rely on oversight and professional bodies in other countries to establish and enforce professional standards, it is recommended that the GFSC consider providing clear guidance to accountants, auditors and actuaries on their respective roles, including professional independence, with respect to regulated entities.
The Supervisory System	
Principle 2.	Supervisory objectives The principal objectives of insurance supervision are clearly defined.
Description	The FSC Law sets out the general and statutory functions of the GFSC. 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." To achieve its statutory objectives, the GFSC is empowered to take any measures necessary or expedient for maintaining confidence in and the safety, soundness and

	integrity of the regulated financial sector. The IBL and IMIIL provide for the protection of the reputation of Guernsey as a financial centre as well as the protection of policyholders, potential policyholders and the public.[18] The GFSC's mission statement states that its "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." The GFSC does not have any mandate to promote or develop the financial services sector. The Commerce and Employment Department is responsible for the development of the sector, while the responsibility for promotion sits with Guernsey Ministry of Finance.
Assessment	Observed
Comments	The GFSC's objectives and functions are clear and appropriate and it does not have any official role in the promotion of the insurance industry. Recognized insurers permitted to write domestic risks without any physical presence in Guernsey (see ICP 6) may have implications to the GFSC's objective to protect domestic policyholders. The GFSC is advised to have a clear articulation of its regulatory and supervisory scope as well as objectives in protecting domestic policyholders in respect of recognized insurers.
Principle 3.	Supervisory authority The supervisory authority: • has adequate powers, legal protection and financial resources to exercise its functions and powers • is operationally independent and accountable in the exercise of its functions and powers • hires, trains, and maintains sufficient staff with high professional standards • treats confidential information appropriately.
Description	The GFSC has general powers to take any action conducive to the carrying out of its functions or to be incidental to their proper discharge.[19] The IBL and IMIIL empower the GFSC to make regulatory rules and issue codes providing guidance to facilitate licensees' compliance with duties, requirements, standards and best practices. While a contravention of rules

[18] See licensing criteria under s7 of IBL and s4 of IMIIL.

[19] s8 of FSC Law.

	or codes does not render a licensee open to any proceedings, the GFSC may take into account such contraventions when exercising its powers. The GFSC may also make a public statement or fine a licensee for contravening the IBL and IMIIL, including breaches of the rules.[20][21] The GFSC is obliged to comply with the legal framework set out in the IBL and IMIIL, e.g., the minimum criteria for licensing. The governance structure of the GFSC is clearly defined in the FSC Law and there are internal governance procedures to ensure integrity of operations. The Commissioners are responsible for overseeing the GFSC's governance and monitoring the effectiveness of internal controls. The GFSC has an ongoing process for identifying, evaluating, and managing operational risks (including regulatory and financial risks) and has established an Audit and Risk Committee. An internal audit of the Insurance Division's governance structure and procedures was carried out in 2008 by external auditors. The internal audit compared the ICPs with IBL, regulations and Insurance Division's procedure manual as well as analyzing the gaps identified in 2006. The GFSC established the Decisions Committee Procedures in February 2002 to consider adverse decisions proposed by the GFSC's executives[22] in relation to regulated entities and authorized/registered persons. Adverse decisions include those concerning license applications, imposition of licensing conditions, regulatory action, disqualification of auditors and actuaries or contentious issues. The Decision Committee, comprising at least three commissioners, may take an adverse decision or decide that no such decision is needed. The GFSC publishes annual reports of its activities and performance, which are audited by auditors appointed by the States. The director general and chairman give regular reports to the policy council of the States. The FSC Law prescribes clear procedures for the appointment and dismissal of Commissioners, including public disclosure of the reasons for the dismissal of the chairman. Commissioners who hold "company directorships of regulated organizations" or "political office of the States, Alderney or the Chief Pleas of Sark" must disclose the potential conflict-of-interests annually. The GFSC may appoint officers and servants as it considers necessary for carrying out its functions. The director general may only be dismissed on specified grounds and public notice must be given for the dismissal. The GFSC is operationally independent from government and industry. It is accountable to the States, which may issue general guidance or directions

[20] s38A to s38C & s78 of IBL; s18, s18AA, s18AB & s55 of IMIIL and s11C, s11D &s11I of FSC Law.

[21] s6 of the FSC Law.

[22] The executive comprises at least 3 of the following: Director General or Directors of Banking, Fiduciary and Intelligence Services, Insurance, Investment Business and Policy and International Affairs.

	to the GFSC. Such guidance or directions (a) may be given only in the public interest and cannot influence individual cases; (b) must not prejudice the operational independence of GFSC; and (c) must be published.[23] The GFSC consults with the industry as well as the political authorities in Sark and Alderney when considering changes to legislation. It is also required to consult the industry when considering rules and codes.[24] The GFSC has its own budget and levies fees from its licensees and annual fee regulations. The States may make a grant to the GFSC, e.g., to cover any budget shortfall.[25] The GFSC may publicize the fact that a condition has been imposed on a licensee by annotating the list of insurance licensees, which is available on its website. This has been done on a number of occasions. The GFSC also maintains a list of prohibition orders made against individuals which is available on its website. Information on problem or failed insurers may be disclosed in its annual report and website. The overall resources available to each division are considered in terms of both the divisional budget and that of the GFSC as a whole. Increases in headcount are considered by divisional management taking into account both the business case as well as the financial implications such as the impact on regulatory fees. Divisional proposals are considered by the director general, senior management, and commissioners. The insurance division has an agreed headcount of 19 and currently has 17 staff; 2 new staff joined on April 5, 2010. The staff of the insurance division specializes in the supervision of particular areas of insurance and all senior staff members are professionally qualified. Supervisory functions are not outsourced. GFSC may use inspectors to investigate matters related to licensees.[26] It also hires outside experts as necessary, such as accountants, lawyers, and actuaries. The GFSC commissioners and staff are not personally liable in any civil proceedings in respect of anything done in the discharge of its functions, unless done in bad faith. The GFSC will protect and indemnify current and former commissioners and staff against any costs, claims, liabilities and proceedings arising from the discharge of their functions. The GFSC participates in the States insurance policy to protect itself, commissioners, and staff against a civil liability claim.[27] The GFSC's Conflicts of Interest Code of Conduct applies to both commissioners and staff, who must complete annual declarations of

[23] s6 of the FSC Law.

[24] s38C & s78 of the IBL and s18AB & s55 of the IMIIL.

[25] s94 of the IBL, s71 of the IMIIL and s13 and s14 of the FSC Law.

[26] S9 of the FSC Law, s69 of the IBL and s46 of the IMIIL.

[27] Schedule 1, s9, s11 & s22 of the FSC Law, s93 of the IBL and s70 of IMIIL.

	compliance. The code requires disclosure of financial and nonfinancial conflicts including significant relationships, e.g., personal, family or professional relationship with any license holder/applicant, directorship of regulated entities or any other closely associated business with the GFSC, e.g., with professional firms or other companies providing services to the GFSC or "specific sector interests with which the individual is strongly connected." The annual declarations are reviewed by the appropriate divisional director. The GFSC in 2005 also established internal guidance for resolving potential conflicts of interests arising from the commissioners' relationships with regulated entities, which was published during the mission. The GFSC is obliged to safeguard confidential information acquired while carrying out its functions. The GFSC's Policy and Procedures on the Disclosure of Information in Respect of the Insurance Sector provides a definition of confidential information. Disclosure of confidential information is permitted only in specified circumstances, e.g., disclosure to another supervisor. Information received from an overseas authority may only be used for the purpose for which it was provided and can only be disclosed with the consent of that authority. The Court shall take into account any obligations of confidentiality of GFSC. (See also details provided under ICP5).[28] Commissioners and staff are required, on joining GFSC and annually thereafter, to sign a confidentiality declaration. The Data Protection Law provides that personal data should be protected against unauthorized or unlawful processing. It also provides that personal data shall not be transferred outside Guernsey unless the recipient country ensures an adequate level of protection. All EEA countries and specified other countries are regarded as having an adequate level of protection. External contractors are required to sign a Confidentiality Declaration for External Contractors which has the same provisions as the declaration for staff. Inspectors appointed by GFSC are required to sign a written agreement which includes the same confidentiality requirements.
Assessment	Observed
Comments	GFSC has adequate powers, legal protection and resources. It is operationally and financially independent and accountable in the exercise of its functions and powers. While strict confidentiality applies to official information obtained in the course of duties, GFSC may disclose confidential information under an appropriate range of specified circumstances.

[28] s21 of FSC Law, s79, s80, s81 &s81A of IBL and s56, s57, s58 & s58A of IMIIL.

Principle 4.	Supervisory process The supervisory authority conducts its functions in a transparent and accountable manner.
Description	The Insurance Division adopts a risk-based approach to monitoring insurers. Under its risk matrix, risk ratings (low, medium, and high) are assigned to each insurer based on a set of standard criteria. This approach allows GFSC to focus its resources on areas of greatest risk and to identify where regulatory action may be required. There are internal procedures documenting the levels of regulatory actions to ensure consistency. GFSC's supervisory approach has two aspects - prospective and retrospective. The prospective element consists of examining the business plan and being aware of any material changes to the plan prior to the event. The retrospective element consists of on-site visits as well as examination of annual returns and audited accounts. International insurers are supervised mainly through their insurance managers or general representatives. All licensees are subject to regular on-site visits to ensure that high standards of compliance and corporate governance are maintained. GFSC adopts a policy of selectivity, i.e., the fitness and propriety of proposed shareholders, directors, officers, insurance managers and/or general representatives is of paramount importance. All insurers (domestic and international) operating in or from within Guernsey and insurance intermediaries must be licensed and satisfy GFSC's licensing criteria including fit-and-proper tests. GFSC's approach to supervision and all relevant laws, regulations, rules, codes and guidance notes are published on its website. Before GFSC makes an adverse decision, it must notify the person concerned and provide an opportunity for representations from that person. GFSC may dispense with the requirement to give 28 days' notice of adverse decisions, if it considers necessary for the protection of the public, clients, policyholders or potential policyholders or the reputation of Guernsey as a finance centre. In dealing with urgent cases, the Decisions Committee may dispense with the representations procedure and make a decision by telephone, email, or other means not involving a physical meeting. Appeals against GFSC's decision may be made to the Royal Court.[29] GFSC consults with the local market participants when considering rules and codes. It consults the political authorities in Sark and Alderney on changes to legislation. The Insurance Division also holds regular seminars with the insurance industry. GFSC submits its annual report to the Policy Council of the States of

[29] s11H of FSC Law, s61, s62 & s63 of IBL and s43 & s41of IMIIL.

	Guernsey in April of each year and publishes its report in May of each year. Monthly statistics are provided on GFSC's website. Selected insurance market data are also published annually. Observations on the market are provided in GFSC's annual report. Press releases are issued as and when appropriate.
Assessment	Observed
Comments	GFSC supervisory approach and processes are defined and transparent. Internal procedures are in place to ensure consistency in supervisory decisions. It has clear accountabilities to the States, and the public through various means. While GFSC publishes selected industry information, there is scope for providing more comprehensive information to facilitate better understanding of the financial condition of the insurance industry, e.g., technical performance for domestic and international sectors.
Principle 5.	Supervisory cooperation and information sharing The supervisory authority cooperates and shares information with other relevant supervisors subject to confidentiality requirements.
Description	As at December 2009, GFSC had signed 19 *Memoranda of Understanding (MoUs)* with foreign supervisors/regulatory bodies. Eight of the MOUs cover the exchange of information relating to the insurance industry. It has also made an application for approval of the equivalence of professional secrecy standards as a prerequisite to signing an MoU with members of the Committee of European Insurance and Occupational Pensions Supervisors. The existence of an MoU is not a prerequisite for sharing information. GFSC's disclosure of information is not dependent on reciprocity. GFSC provides information to other supervisors when it thinks appropriate and when it establishes that it has a legal gateway for disclosure. In addition, GFSC will take into account the standards of data protection (e.g., supervisors in an EEA country or those who subscribe to the USA Safe Harbour agreement) and confidentiality of the third party recipient (e.g., whether GFSC has entered into an MoU with that country). GFSC is authorized to cooperate with, share information with and undertake investigations in support of a foreign supervisor. To this end, GFSC may disclose information for the purpose of enabling or assisting a foreign supervisor. Information shared with foreign supervisors should not be disseminated further without the written consent of GFSC and should only be used for supervisory purposes.[30] In deciding whether to provide assistance to a requesting authority, GFSC considers whether: (a) corresponding assistance would be given to GFSC; (b) the case concerns the breach of a law which has no close parallel in

[30] S21(6), s21A & 21B of FSC Law, s80(f) of IBL and s57(f) of IMIIL and GFSC's Policy and Procedures on the Disclosure of Information in Respect of the Insurance Sector.

	Guernsey or involves the assertion of a jurisdiction not recognized by Guernsey; (c) the case is serious and its importance to persons in Guernsey; (d) the assistance would lead to disproportionate injury, loss or damage to the persons subject to the exercise of the powers in question; and (e) it is appropriate in the public interest. GFSC may decide not to provide assistance unless the requesting authority contributes towards the cost of assistance. Where appropriate, GFSC also provides information to other supervisors in relation to entities in their jurisdiction. GFSC informs host supervisors of material changes in supervision that may have a significant bearing on foreign establishments in their jurisdiction. It may discuss any action to be taken with a host supervisor, if it will affect a foreign establishment in the host supervisor's jurisdiction. GFSC also discusses with the home supervisor any action that will affect the parent company. Information supplied by a foreign supervisor to GFSC cannot be further disclosed without the consent of that supervisor.[31] Such information can only be used by GFSC for the purpose for which it was provided by that authority. In practice, GFSC consults and seeks consent from other supervisors where it proposes to take action on the information provided by that supervisor.
Assessment	Observed
Comments	GFSC regularly exchanges information with other supervisors and has signed eight MoUs with foreign supervisors covering the insurance sector. GFSC has also applied to become a signatory to the IAIS Multilateral MoU.
The Supervised Entity	
Principle 6.	Licensing An insurer must be licensed before it can operate within a jurisdiction. The requirements for licensing are clear, objective, and public.
Description	All insurance entities (domestic and international) operating in or from within Guernsey must be licensed or recognized by GFSC, regardless of legal form or ownership structure. IBL only permits licensed insurers to carry on or to hold themselves out as carrying on insurance business in Guernsey. GFSC's internal procedures require consultation with home supervisors on cross border establishment, where applicable. An insurer, incorporated in the EU, Jersey or Isle of Man, and carrying on business in Guernsey by way of a branch, will be exempt from certain requirements of IBL, including capital and solvency requirements and separation of assets and liabilities attributable to long-term business[32]. A subsidiary will have to comply with all requirements of IBL. Within the EU,

[31] s81 of IBL and s58 of IMIIL.

[32] s38 of IBL exempts such insurers from s25 to s28, s30 to s32, s34 to s36 and s39 to s43.

	GFSC has signed MoUs only with Isle of Man, Gibraltar, Malta, and the United Kingdom and it does not have an MoU with Jersey. Only insurers licensed in respect of domestic business are allowed to write domestic business. Domestic business is defined as insurance business, excluding reinsurance business, insuring: (a) residents in Guernsey, (b) real property situated in Guernsey, personal property held or based in Guernsey or in transit to or from Guernsey.[33] Guernsey residents must purchase motor insurance from Authorised Motor insurers who have received specific authorisations. EU freedom of service does not apply to Guernsey as it is not a member of the EU. Nonetheless, GFSC recognizes insurers either by description (e.g., all *European Union (EU)*, Jersey and Isle of Man insurers) or by notification. GFSC relies on the relevant home supervisor to exercise prudential regulation of recognized insurers. The rationale for allowing recognized insurers is to provide a diversified range of insurance products to Guernsey residents. An insurer seeking recognition must submit a Notification Form providing details of its home supervisor and a description of business authorized. GFSC acknowledges receipt of the notifications and relies on the relevant home supervisors to supervise recognized insurers. An intermediary in Guernsey is permitted to place domestic business with recognized insurers. Insurance intermediaries must declare the recognized insurers they deal with to GFSC annually. The criteria for assessing notifications are not documented although GFSC indicated that the degree of policyholders' protection was a key consideration. While there is no published list of recognized insurers, GFSC informed that recognized insurers are from UK and IOM only. In addition, there are no formal criteria to assess the status of recognized insurers. Based on intermediaries' declarations, GFSC noted that there are about 30 active recognized insurers. The IBL specifies licensing criteria which must be fulfilled, including fit-and-proper criteria (see also ICP 7)[34] and regulations set out the information that an applicant must include with the application, e.g., details of ownership, business plan and financial projections, fronting arrangements, personnel and third party service providers, memorandum and articles of association, certificate of incorporation, details of the bank mandate signing powers, confirmation that share capital has been received and/or that letters of credit and subordinated loans are in place and available to the applicant. Where a foreign insurer applies for a license to operate in Guernsey, the relevant information is provided by the applicant or by supervisor-to-

[33] s1 to s5 and Schedule 5 of IBL.

[34] s7, s34, s40 and Schedule 7 of IBL.

	supervisor correspondence. When assessing applications, GFSC takes into account three main factors: (a) fitness and propriety of the persons involved; (b) business plan (insurance and reinsurance programme); and (c) management and control are resident in Guernsey. In the case of managed entities, GFSC requires the insurance manager to carry out appropriate due diligence checks on the applicant, in addition to its own due diligence checks. GFSC's website provides general information on its licensing approach. All licensed insurers are required to appoint a general representative,[35] either resident in Guernsey or a licensed insurance manager, to act on their behalf and to accept service of any document. The general representative is also the main point of contact between GFSC and an insurer. The IBL does not permit composite insurers or reinsurers. However, the IBL allows separate cells of PCCs and ICCs to write long-term and general business provided there is no reliance on common capital, i.e., they need to either be separately capitalized or a robust recourse agreement needs to be in place before cells can have access to core capital. GFSC ensures that there is no double gearing of capital resources within a PCC/ICC. A PCC shall not write both long-term and general business in the same cell. In addition, a PCC shall not: (a) create new cells or write new insurance business; or (b) write risks from non-associated parties without GFSC's consent.[36] GFSC aims to make a decision on all applications within one month from receipt of all relevant information. Unanimous approval of the Assessment Committee is required before a license is granted. GFSC may impose licensing conditions on insurers. Written reasons must be given where GFSC refuses to grant a license and the applicant must be given the opportunity to make representations. An insurer conducting long-term business shall maintain a segregated account and all receipts of long-term business shall be segregated in a separate insurance fund. Investment-linked policies shall be segregated from other insurance funds. Proper accounting records must be kept to identify the assets and liabilities of each insurance fund. The assets of the fund should not be withdrawn or transferred except to meet claims and expenses relating to the business of the insurance fund, except out of established surplus.[37] A long-term insurer's assets representing at least 90 percent of policyholder liabilities must be held in trust. It shall appoint a Guernsey-based trustee, approved by GFSC, to safeguard these assets. The trustee appointed must

35 A General Representative is defined by s29 of IBL as either a licensed insurance manager or an executive director of the licensed insurer.

36 s7(2)(h) & s11 of IBL and s7 of the Protected Cell Companies Ordinance.

37 s41 to s43 of IBL.

	report full details of the assets held by it to GFSC at least quarterly and must also inform GFSC if the applicant instructs a withdrawal of more than 5 percent of the market value of the assets held within one month. The trustee may hold the assets either directly or may appoint a custodian to hold the assets. Generally, custodians must be independent of the insurer or its manager. Custodians do not have to be Guernsey based.[38] GFSC monitors insurers' compliance with the relevant licensing criteria and requirements as part of its on-going supervision.
Assessment	Observed
Comments	GFSC's licensing framework is clear and transparent and effectively implemented. It relies on the relevant home supervisor on prudential supervision of recognized insurers. During the mission, it has clarified publicly the criteria for recognition to reflect current practice, i.e., only from UK and Isle of Man, where domestic policyholders are protected under the compensation schemes of the respective jurisdictions.
Principle 7.	Suitability of persons The significant owners, Board members, senior management, auditors and actuaries of an insurer are fit and proper to fulfil their roles. This requires that they possess the appropriate integrity, competency, experience, and qualifications.
Description	IBL requires that any director, controller (see ICP8), partner, manager or general representative of an insurer must be a fit-and-proper person, both at the licensing stage and for any subsequent changes. In support of any proposed appointment to such key positions, insurers must submit a *personal questionnaire (PQ.)*[39] Controllers and directors must keep GFSC informed of any changes to the information contained in their PQs and complete a new PQ every five years. Upon receiving a PQ, GFSC may serve a notice of objection or request for additional information within 60 days. The grounds for objection may include failure to meet fit-and-proper criteria or being prejudicial to the interest of the public or policyholders. GFSC may impose conditions on an insurer's license requiring the removal of any director, controller, manager, partner, employee or general representative.[40] In determining whether a person is fit-and-proper, GFSC will assess: (a) his probity, competence, experience and soundness of judgment of that position; (b) his diligence in fulfilling his responsibilities; (c) any impact on the interests of clients or (potential) policyholders or the reputation of Guernsey as a finance centre; (d) his educational and professional qualifications, (e) his knowledge and understanding of his obligations and;

[38] The Insurance Business (Licensing) Regulations, 2002.

[39] s11 of IBL.

[40] s12 of IBL.

	(f) his record of compliance with relevant laws and regulations, rules, codes, guidance, principles, and instructions. GFSC has access to the U.K. FSA Shared Intelligence System and checks with other authorities where appropriate. GFSC checks that auditors and actuaries have the relevant qualifications and appropriate experience. GFSC relies on the relevant professional bodies and makes its own checks, where necessary. Prior written notice must be provided to GFSC in the event of a change of auditor or actuary by a long-term insurer. GFSC may disqualify an auditor or actuary. To date, it has not issued any disqualification order.[41] GFSC may impose conditions on an insurer's license when it has concerns regarding its ownership. A notice of objection may be issued to either a prospective or an existing controller and contravention of such a notice is an offence. Following a notice of objection, GFSC may impose restrictions on the sale of shares and may apply to the courts for an order relating to the sale or transfer of such shares.[42] The *Licensed Insurers' Corporate Governance Code (CGC)* requires the Board of an insurer to establish high standards of business conduct and ethical behaviour for directors and senior management. In this regard, any actual or potential conflicts of interests must be declared to the Board as and when they arise. GFSC checks, both at licensing stage and when there are any changes, whether there are any potential conflicts of interest arising from any key functionaries simultaneously holding two positions in an insurer.
Assessment	Observed
Comments	GFSC performs due diligence on any proposed owner, controller or director prior to licensing and in approving any subsequent changes in control or directors. Auditors and actuaries are assessed on their qualifications and experience and GFSC is empowered to issue disqualification orders against auditors and actuaries.
Principle 8.	Changes in control and portfolio transfers The supervisory authority approves or rejects proposals to acquire significant ownership or any other interest in an insurer that results in that person, directly or indirectly, alone or with an associate, exercising control over the insurer. The supervisory authority approves the portfolio transfer or merger of insurance business.
Description	Insurers must notify and obtain prior written approval from GFSC before effecting any change of controller. Those seeking to become a controller must meet the same minimum criterion as for licensing (see ICP6). GFSC

[41] s11B of FSC Law and s84A & s84B of IBL.

[42] s12, s26, s27 & s28 of IBL.

	may object to a potential controller on the grounds that the interests of policyholders would be jeopardized. A controller is defined as a managing director, chief executive officer, parent company, shareholder controller, any person who has the power to appoint or remove a director or indirect controller (i.e., a person in accordance with whose directions or instructions any director, parent company or controller of the insurer is accustomed to act). All controllers must keep GFSC informed of any changes to the information contained in their PQs and to complete a new PQ every five years. Controller is not limited to Guernsey controllers.[43] Any person wishing to acquire 15 percent of voting power of an insurer should give prior notice to GFSC, and obtain GFSC's approval. Acquisition of significant shareholdings (i.e., 5 percent or more but less than 15 percent of the voting power) must be notified to GFSC.[44] Applications for proposed acquisitions or changes of control are considered on a case by case basis, including financial resources. As the majority of captive insurers outsource their management functions to insurance managers, nonfinancial resources are not a consideration. However, GFSC will consider nonfinancial resources of an insurer if it employs its own management staff. GFSC checks group structures at licensing stage by asking for an organogram and sufficient information to determine the ultimate controlling owners. The same information is requested when considering any changes of control. In addition, GFSC also considers whether the group structure hinders effective supervision.[45] Portfolio transfers must be approved by GFSC and assessed individually as well as in conjunction with an insurer's existing business plan. The transfer of all or part of long-term business of an insurer to another party is subject to the approval of the Royal Court. Policyholders and GFSC have a right to make representations to the Court on the application for transfer.[46] GFSC has internal requirements to assess applications to transfer business, including solvency and liquidity considerations. It also ensures that policyholders are protected. If necessary, GFSC can impose conditions on insurance licenses stipulating specific requirements.
Assessment	Observed
Comments	GFSC assess prospective owners and controllers in exactly the same way as for a new license application. Any person wishing to acquire 15 percent or more of an insurer requires the prior approval of GFSC. Portfolio transfers must be approved by GFSC or the Court, depending on the

[43] s11(6), s25 & Schedule 5 of IBL.

[44] s49, s49A and Schedule 5 of IBL.

[45] This practice is formalized in s6 of Schedule 7 of IBL w.e.f. 17 Feb 2010.

[46] s11(2A), s44 to s47 of IBL and s62, s79 & s93 of CL.

	nature of the business, to safeguard policyholders' interests.
Principle 9.	Corporate governance The corporate governance framework recognizes and protects rights of all interested parties. The supervisory authority requires compliance with all applicable corporate governance standards.
Description	The CGC applies to all insurers. The Board of an insurer has the discretion to implement the CGC in a way that is commensurate with the nature, scale and complexity of its business. Insurers are required to certify the level of adherence to CGC and to explain any departures from the code in their annual returns. In practice, insurers complete the CGC checklist which is available on GFSC's website. Insurers are expected to consider that the composition of the Board has an appropriate balance between executive directors and non-executive directors. There must be at least one independent director, except where GFSC waives this requirement.[47] Currently, GFSC encourages insurers to have an appropriate balance between local and nonlocal directors. The CGC outlines the responsibilities of the Board, e.g., to establish sub-committees with specific responsibilities, a remuneration policy for senior management and ensure compliance with relevant legislation. While insurers must appoint compliance officers, the responsibility for compliance remains with the Board. The Boards are required to conduct annual reviews of a number of key areas including insurers' strategic objectives and policies as well as risk management systems. For long-term insurers, the Board must ensure that their actuaries have direct access to the Board and to all relevant information. Where an insurer appoints an insurance manager, its Board must ensure that the duties, responsibilities and authorities of the insurance manager are clearly set out in a written management agreement. If a locally incorporated domestic insurer wishes to conduct business overseas, its Board must ensure that there are systems and controls in place to maintain a sound and verifiable system of reporting to its head office. Where prudential records are held outside Guernsey, an adequate summary of those records should be remitted periodically to the Board to demonstrate compliance with the relevant legislation. The Board is responsible for appointing and dismissing senior management, including executive directors. Senior management is responsible for overseeing the operations of an insurer and providing direction to it on a day-to-day basis, subject to the objectives and policies

[47] Defined as a person who is: a) not an associate of, or associated party in relation to the company; and b) not responsible for the management of the company's business; unless GFSC waived such requirement – Schedule 7 of IBL. Waivers may be given to insurers in run-off.

	set out by the Board and relevant legislation. Senior management is also responsible for providing the Board with recommendations for its review and approval on objectives, strategy, business plans and major policies as well as providing the Board with comprehensive, relevant, and timely information. Senior management may be employed by either an insurer or an insurance manager appointed by the insurer. The Board must establish an appropriate remuneration policy for senior management. Where appropriate, the remuneration policy should have regard to the performance of senior management as well as that of the insurer and should not include incentives that would encourage imprudent behavior. GFSC routinely checks compliance with the CGC during on-site visits. In the event of noncompliance with the CGC, GFSC would require remedial action or impose conditions on the insurer's license. GFSC has issued a draft code of corporate governance for the financial services sector, which is under consultation. There is a need to ensure consistency between the CGC and the proposed new code.
Assessment	Observed
Comments	The CGC applies to all insurers and incorporates the requirements of ICP 9. The Boards of insurers are expected to apply the CGC in a manner appropriate to the nature, scale and complexity of their business. Insurers must certify the level of adherence to the CGC on an annual basis and to explain where they consider elements of the CGC do not apply to them.
Principle 10.	Internal control The supervisory authority requires insurers to have in place internal controls that are adequate for the nature and scale of the business. The oversight and reporting systems allow the Board and management to monitor and control the operations.
Description	The CGC requires the Boards of insurers to establish effective internal controls to ensure that: (a) its business is conducted in a prudent manner in accordance with established strategies and policies; (b) transactions are only entered into with appropriate authority; (c) assets are safeguarded; (d) records provide complete, accurate and timely information; and (e) risks are assessed and managed effectively. This includes establishing an internal audit function of a nature and scope appropriate to their respective businesses. Insurers must be able to demonstrate to GFSC that adequate operational procedures are in place. In practice, most captives rely on the internal procedures and controls of their appointed insurance managers. This is often included in the management agreements between the insurer and insurance manager. The insurance manager shall advise the Board of any significant changes to its procedures and controls no later than the next Board meeting. Insurers are expected to establish appropriate divisions of responsibilities

	between the Board, senior management and third party service providers, clear delegation of authority, decision making procedures and segregation of duties. The Boards shall perform annual reviews of insurers' risk assessment and management systems to ensure that all significant risks are being adequately measured, monitored and controlled. (Please also see ICP 18). The internal control system should also be reviewed at least annually to ensure that it is operating effectively and that any deficiencies have been adequately addressed. Insurers' internal control systems shall include policies and procedures to: (a) address the findings of internal/external audits and actuarial reports; (b) ensure compliance with all legislation; (c) enable any breaches to be identified, reported and rectified promptly; (d) oversee the market conduct activities where an insurer deals directly with the public; (e) establish appropriate accounting procedures and controls; (f) establish clear accountability for all outsourced functions, which are subject to the normal standards of internal controls. All insurers are required to have an internal audit function of a nature and scope appropriate to the business. Where an insurer appoints an actuary, all actuarial reports should be made available to both senior management and the Board. GFSC assesses the internal controls of insurers during its on-site visits. In addition, insurers submit the management letter from their auditors as part of their annual returns.
Assessment	Observed
Comments	Regulatory requirements relating to internal controls are incorporated into CGC and are monitored during GFSC's on-site visits. In practice, most captives rely on the internal procedures and controls of their appointed insurance managers.
Ongoing Supervision	
Principle 11.	Market analysis Making use of all available sources, the supervisory authority monitors and analyses all factors that may have an impact on insurers and insurance markets. It draws the conclusions and takes action as appropriate.
Description	The insurance market in Guernsey is primarily a captive insurance market which is not susceptible to macro-economic conditions within Guernsey as the parent companies and risks underwritten are located outside of Guernsey. The captive insurance market is influenced by global market conditions and also by events which affect specific industries from time to time. In view of above, GFSC monitors events in the global insurance market and in the industries of the parent companies of captive insurers. Market conditions are continuously monitored through studying specialist press articles, internet news services and discussions with the local insurers and

	insurance managers. GFSC's market analysis aims to identify future trends, e.g., whether increasing premium levels in the commercial insurance market could lead to the formation of new captives or increased retentions for existing captives. Market analysis is also carried out in relation to specific market sectors, e.g., recent work on captives writing mortgage indemnity guarantee insurance. While its analysis reveals no major concerns, GFSC has been in discussions with the actuarial firm advising these captives to agree on a common set of assumptions for actuarial reports. Other examples include the potential impact of the EU Solvency II Directive, changes to U.K. Controlled Foreign Companies tax legislation, the impact on captives of increased levies to the London Fire Brigade. GFSC's market analysis takes account of both narrative and statistical information. Apart from public sources, confidential information from existing licensees, other jurisdictions and international bodies such as the IAIS is taken into account. GFSC publishes selected aggregated market statistics on its website, which are updated on a monthly basis. Quarterly analysis is provided to government and an annual report is published. In addition, Guernsey's promotional agency, Guernsey Finance, publishes statistical data. GFSC also monitors market-wide events to assess their implications for the financial stability of insurance markets. At the start of the 2008/9 crisis, GFSC wrote to all captive managers requesting information to enable an assessment of Guernsey's exposure and took appropriate action to address any concerns arising.
Assessment	Observed
Comments	GFSC proactively monitors market developments both locally and globally, taking account of external events that affect relevant industry sectors of the parent companies of captive insurers.
Principle 12.	Reporting to supervisors and off-site monitoring The supervisory authority receives necessary information to conduct effective off-site monitoring and to evaluate the condition of each insurer as well as the insurance market.
Description	All insurers must submit annual returns to GFSC within four months of their financial year end. The returns consist of financial information including audited accounts, updated business plans, margin of solvency calculations, claims information, asset information and an actuarial valuation report (for long-term business). In addition, where a captive undertaking general business employs the services of an actuary to assist in the estimation of IBNRs, GFSC requires that the actuarial valuations are submitted as part of the annual report. Insurers are required to have their accounts audited annually. The auditors' report must give an opinion on whether the accounts: (a) have been properly prepared; (b) give a true and fair view of the licensee's state of

	affairs; and (c) are in accordance with the IBL. The auditor must also report on any area where the annual return of the licensee is inconsistent with its accounts. The general representative of an insurer must also sign a declaration stating that the insurer has complied with the IBL during the financial period. GFSC reviews insurers' annual returns and has customised review checklists for different types of insurers and assigned risk ratings and may raise any issues with the insurer or insurance manager. GFSC has taken a policy decision not to require more frequent submission of returns, e.g., quarterly on the basis that the insurance market comprises largely captive insurers. Where there are supervisory concerns, GFSC may require insurers to provide further or more frequent reporting, e.g., quarterly management accounts. Occasionally, secondees from external audit firms may be used to assist the Insurance Division in reviewing low-risk-rated annual returns. They are required to comply with GFSC's confidentiality rules and are supervised by an Assistant Director or above. The FSC Law empowers GFSC to make regulations in respect of charging financial penalties for late submission of annual returns.[48] GFSC is currently drafting regulations in this respect. Any material changes to the business plan must be notified to the GFSC, prior to implementation. This enables the GFSC to consider the impact of these changes on the financial position of the insurers and comment if necessary. Insurers' business plans shall include: a) For general business— a spreadsheet showing unaudited financial projections for the next 12 months, a summary of proposed insurance program and reinsurance program, and any other material factors; and b) For long-term business— a summary, approved by the actuary, of the products offered and the markets in which the products are to be offered, an actuarial valuation report, unaudited financial projections for the next three years, and any other material factors. The GFSC has recently enhanced insurers' reporting requirements.[49] The revised annual returns include details of the method of calculating reserves, insurers' OSCA paving the way for the implementation of a risk-based solvency assessment, in line with international trends and the IAIS framework.
Assessment	Observed
Comments	The GFSC has a well-developed and consistent process for reviewing annual returns and monitoring insurers' operations on an on-going basis.

[48] s11I of FSC Law.

[49] Insurance Business (Annual Return) Regulations, 2008.

Principle 13.	On-site inspection The supervisory authority carries out on-site inspections to examine the business of an insurer and its compliance with legislation and supervisory requirements.
Description	The GFSC inspects insurance managers, insurance intermediaries and insurers not managed by an insurance manager on a three year rolling program. When visiting an insurance manager, a number of insurers are selected for review. The GFSC also makes ad hoc visits to licensees to address specific concerns.[50] The basis for selecting individual insurers includes their ratings as determined by the GFSC's internal risk matrix tool. The inspections focus on licensees' procedures, internal controls and anti-money laundering procedures and how these are applied in practice. In some cases, themed visits are performed to review particular areas of interest, such as underwriting procedures. The inspection process and procedures are clearly documented. GFSC may also meet auditors and actuaries to discuss the operations, regulation or licensing of licensees. Auditors and actuaries also have a duty to report matters that impinge on fitness and propriety of licensees and policyholders' interests to the GFSC. Insurers, insurance managers and intermediaries are required to furnish GFSC with a copy of the auditor's management letter or written confirmation that no auditor's management letter was issued. [51] GFSC discusses any major issues discovered during an inspection at the closing meeting and provides a formal report within four weeks of the inspection. The licensee is given a deadline to respond with their proposed measures. Any outstanding issues are followed up in correspondence or regular meetings. Where issues are not resolved within the timescales set, regulatory action is considered and taken, where necessary. GFSC has performed on-site visits at the premises of any party associated with the licensee, e.g., in respect of operations outsourced and may request documents from any person who may be in possession of them. It has visited licensees' operations in a few jurisdictions. GFSC may appoint inspectors in cases where a more formal and detailed investigation is required.[52] During 2009, GFSC visited 14 insurance intermediaries, 11 insurance managers, five international life companies, one general company, and two domestic insurers. In addition, GFSC held annual review meetings with 25 insurance intermediaries who were not subject to on-site inspection in 2009

[50] s67 of IBL and s44 of IMIIL.

[51] s36, s82, s83 & Schedule 2 of IBL and s23, s24, s59, s60 & Schedule 2 of IMIIL.

[52] S67(3), s68 &s69 of IBL and s44(3), s45 & s46 of IMIIL.

	and 22 regular coordination meetings with insurance managers.
Assessment	Observed
Comments	GFSC has clear and well-documented inspection policies and procedures and adopts a three-year rolling program for inspection. Under its risk-based supervision approach, insurers with high risk ratings are supervised more closely.
Principle 14.	Preventive and Corrective Measures The supervisory authority takes preventive and corrective measures that are timely, suitable and necessary to achieve the objectives of insurance supervision.
Description	GFSC is empowered to take preventive and corrective measures. Its primary regulatory measure is the imposition of licensing conditions, which may be done whenever deemed necessary and appropriate. Conditions are unlimited in scope and can include requirements such as to cease writing new business, to obtain prior written consent before moving any funds and to submit a recovery plan. Any breach of a licensing condition is a criminal offense and a ground for the revocation of the license.[53] GFSC regularly discusses issues with insurers and their managers to ensure that minor preventive and corrective measures are taken without resorting to formal measures. It holds regular seminars with the insurance industry to highlight any areas of concern arising from its off-site and on-site monitoring. GFSC also regularly holds individual meetings with insurance managers and intermediaries to discuss any areas of concern and to enable them to provide updates both on their businesses and on the business of the licensees for which they are responsible. GFSC's internal procedures set out a number of levels of possible regulatory action to ensure consistency and escalation of action. These levels comprise early warning, investigation, regulatory action and ultimately closure. Insurers' completion of their OSCA gives GFSC advance warning of any potential breach of solvency requirements. Urgent on-site visits may be carried out where necessary.
Assessment	Observed
Comments	GFSC is empowered to and does take a range of proportionate measures to address supervisory concerns.

[53] s10, s12 &s14 of IBL and s7 & s8 of IMIIL.

Principle 15.	Enforcement or sanctions The supervisory authority enforces corrective action and, where needed, imposes sanctions based on clear and objective criteria that are publicly disclosed.
Description	GFSC has a number of sanctions it can use against licensees and individuals, including fines, public statements and prohibition orders. It may also apply to the Royal Court for a directors' disqualification order under the *Companies (Guernsey) Law, 2008 (CL).* GFSC's power to impose licensing conditions enables it to take enforcement measures such as requiring the transfer of obligations of a failing insurer; requiring increased capital; restricting the payment of dividends, other asset transfers and purchase of an insurer's own shares. GFSC has restricted insurers' dividend payments on a number of occasions, in particular with regard to captive insurers whose parent companies are in financial difficulties. GFSC is also empowered to give formal directions to licensees whose licenses are revoked or surrendered. GFSC's direction may (a) require a licensee to take or refrain from certain action or to restrict the scope of its business; (b) prohibit or limit its carrying on insurance or other business; (c) prohibit the soliciting any new business; (d) prohibit any transaction(s); (e) require the removal of any director, controller, partner, manager, employee, general representative, auditor or actuary. Breach of a direction by a former licensee is an offence.[54] GFSC may restrict the sale of shares and payment of dividends under certain circumstances. The acquisition of a subsidiary would be regarded as a change to the licensee's business plan and is subject to approval by GFSC, taking into consideration whether the activities of a subsidiary would jeopardize the financial situation of the insurer[55]. GFSC also has the following sanctions powers: (a) prohibiting an individual from performing functions in the insurance industry or to serve as a director of any company; (b) applying to the Court for the appointment of a receiver only in respect of unlawful business; (c) applying to the Court for the appointment of an administrator under the CL.[56] However, GFSC does not have the power to initiate regulator-controlled rehabilitation process. GFSC ensures that sanctions are enforced. It may also apply to the Royal Court for an injunction restraining the breaching of its licensing conditions, directions or regulations.[57] GFSC can investigate persons suspected of acting as unlicensed insurers,

[54] s16 of IBL and s11 of IMIIL.

[55] s28 & s31 of IBL.

[56] s28A, s75, s76 of IBL and s375 & s427 of CL.

[57] s76 of IBL and s53 of IMIIL.

	insurance managers or insurance intermediaries. It may report such cases to the Attorney General's office for potential prosecution. GFSC may impose a license on an unlicensed insurer so that it can use its other powers under the IBL. GFSC may also apply to the Royal Court to wind up a company acting as an unlicensed insurer.[58] GFSC is empowered to impose discretionary financial penalties of up to £200,000 on licensees, former licensees and relevant officers for material breaches of the legislation or its criteria for licensing.[59] Any person who is guilty of an offence under the IBL will be liable to a fine not exceeding level 5 on the uniform scale and/or imprisonment for a term of between three months to two years. While FSC Law empowers GFSC to impose administrative financial penalties for late payment of fees or charges or late filing of returns, the enabling regulations have not been prescribed.[60] There are no dedicated enforcement staff in GFSC although it is in the process of recruiting a legal counsel. All cases requiring regulatory action are closely monitored and discussed at bi-weekly Division management meetings, as well as bi-weekly Division meetings. In addition, serious cases are discussed at bi-weekly Heads of Divisions meetings and monthly Commissioners' meetings. All adverse decisions against insurers are decided by the Decisions Committee, which ensures consistency. Pending a final decision, the Court may first suspend or modify the operation of GFSC's conditions. It is a criminal offence to provide information that is false, deceptive or misleading in a material particular to GFSC. It is also an offence to fail to provide GFSC with information that a person knows or should know is relevant to GFSC's functions and that the withholding of the information will mislead GFSC.[61] While licensees are entitled to a reasonable period of time to make representations against any adverse decisions by GFSC, GFSC may reduce or dispense with the notice period if it believes it is in the interests of policyholders, potential policyholders or the reputation of Guernsey.
Assessment	Observed
Comments	GFSC has the legal powers to take enforcement actions or impose appropriate sanctions. There is a structured and transparent process in respect of adverse decisions against licensees and persons. However, its main tool is the imposition of licensing conditions and there is scope for a review to widen its enforcement powers. GFSC should review its heavy reliance on licensing conditions to take

[58] s1, s10, s70 of IBL, s1, s47 of IMIIL and s410 of CL.

[59] s11D and s11I of FSC Law.

[60] s88 of IBL and s65 of IMIIL.

[61] s87 of IBL and s64 of IMIIL.

	enforcement actions and consider establishing a wider range of enforcement powers, e.g., appointment of judicial managers and receiver.
Principle 16.	Winding-up and exit from the market The legal and regulatory framework defines a range of options for the orderly exit of insurers from the marketplace. It defines insolvency and establishes the criteria and procedure for dealing with insolvency. In the event of winding-up proceedings, the legal framework gives priority to the protection of policyholders.
Description	The procedures for the winding up of a company, including insurers, are contained in CL. Both the CL and IBL set out the circumstances in which GFSC may be involved in the compulsory winding up of an insurer. In determining the point at which it is no longer permissible for an insurer to continue its business, CL provides only a general solvency test. The IBL provides a more specific solvency requirement (see ICP23). The compulsory winding up of companies is at the discretion of the Court, which will consider the rights and interests of policyholders.[62] Insurers who carry on long-term business shall not be wound up voluntarily and they are subject to additional requirements. They are also required to ring-fence assets attributable to their long-term insurance business in a segregated fund under a trust arrangement. (See ICP 6). The objective is to insulate such assets from the claims of other creditors. In the event of a winding up, the assets representing the segregated fund shall be available for meeting only the liabilities attributable to that business.[63] There is no segregation requirement for general insurance business. In the event of insolvency, i.e., where assets of a segregated fund are insufficient to meet all the liabilities of an insurer, the IBL is silent on whether policyholders and beneficiaries of the life fund would rank higher or *pari passu* with other unsecured creditors. Similarly, policyholders of general insurers, who are not protected under a segregated fund, are not given high legal ranking. The legal priority to policyholders is a key element of ICP 16 and stated at the principle level. In addition, GFSC does not have a published policy on whether insurers are allowed to pledge assets for credit facilities, e.g., letters of credit. As insurers are typically institutional investors, the need for credit facilities should be justified or approved. As secured creditors rank ahead of policyholders, there should be regulatory policies on pledging or encumbrances of assets to obtain credit facilities. Under the Insurance Business Approved Assets Regulations, any asset under lien is not an approved asset for solvency purposes unless it is securing an obligation under an insurance contract.

[62] s51 to s53 of IBL and s527 and Part XXIII of CL.

[63] s54 & s55 of IBL.

Assessment	Largely observed
Comments	The legal framework provides for orderly winding up and exits from the market, that takes into account the rights and interests of policyholders and beneficiaries. However, policyholders and beneficiaries are not given legal priority in the event of insolvency. To safeguard policyholders' interests, GFSC should consider establishing: a) an explicit legal provision in legislation to ensure that policyholders and claimants are given high priority in the event of insolvency; and b) regulatory policies on pledging or encumbrance of assets by insurers.
Principle 17.	Group-wide supervision The supervisory authority supervises its insurers on a solo and a group-wide basis.
Description	GFSC defines an insurance group as "a group structure which contains two or more insurers. The structure of international insurance groups may derive from an ultimate holding company which is not an insurer. Such a holding company can be an industrial or commercial company, another financial institution (for example a bank), or a company the majority of whose assets consist of shares in insurance companies (and/or other regulated financial institutions)." A financial conglomerate is "any group of companies under common control whose exclusive or predominant activities consist of providing significant services in at least two different financial sectors (e.g., banking, securities, insurance)." GFSC is not the home regulator for any fully-fledged insurance group or financial conglomerates. A number of Guernsey insurers are part of international groups and some have branches or subsidiaries in other jurisdictions. GFSC is a home/lead supervisor in respect of a PCC which also has operations in Gibraltar. It is the host supervisor for a number of insurers and has applied to join the supervisory colleges for two insurance groups. GFSC has power to obtain information relating to other entities in a group from a licensee. It cooperates with other supervisors to ensure effective and efficient group wide supervision. It does not require MoUs to be entered into before cooperation and information is provided as long as the jurisdiction's legislation permits the confidential exchange of information between supervisors. GFSC approves any changes in controller or management of insurers including those who are part of a group. GFSC may refuse to grant a license or withdraw an existing license if the group structure is seen to hinder effective supervision and the situation could not otherwise be resolved. Where functions are outsourced to other entities in the group, GFSC ensures that the outsourcing agreements give it the right to visit the outsourced functions. GFSC regularly carries out on-site visits to the outsourced function. There are no formal limits on intra-group transactions as related party assets are not admissible for solvency purposes unless specifically

	approved. In this regard, GFSC has been allowing captive insurers to use loans to parent companies to meet solvency requirements and in some cases, more than 90 percent of a captive insurer's assets could be held as parental loans. Arising from the 2008/9 financial crisis, it has imposed restrictions on such loans and required insurers to reapply for approvals. As at March 3, 2010, insurers' loans to parents totaled £5.8 billion of which £5.2 billion was approved for solvency purposes, representing 33 percent of net assets. Notably, the figures were skewed by two large captive insurers who held almost all their assets as loans to parents, posing concentration and contagion risks. GFSC has established some high level principles for group supervision, largely based on ICP 17. These principles could form the basis for developing a group supervision framework, tailored to its local market conditions when it acquires the responsibilities as a home supervisor.
Assessment	Not applicable
Comments	GFSC currently has no responsibilities as group/home supervisor of any insurance group. It is committed to establish an appropriate framework for group supervision when it acquires such responsibilities.
Prudential Requirements	
Principle 18.	Risk assessment and management The supervisory authority requires insurers to recognize the range of risks that they face and to assess and manage them effectively.
Description	The CGC requires insurers to specifically take account of underwriting, reserving and investment risk and provides guidance on a number of other risks. In particular, the Boards of insurers must establish risk assessment and management systems that: (a) are appropriate for the size, nature and complexity of their operations; (b) identify, measure, monitor and control effectively all significant risks on an on-going basis; (c) provides timely risk assessment and management information; and (d) are regularly reviewed by the Board. Insurers typically declare compliance with the risk management requirements as part of their annual returns using the Corporate Governance Checklist. Where appropriate, the Boards of insurers may establish sub-committees with specific responsibilities, including a risk management committee. The Guidance Note on Licensed Insurers' *Own Risk and Solvency Assessment (ORSA)* specifies the risks to be addressed in performing their *Own Solvency Capital Assessment (OSCA)*. GFSC has established a risk matrix for insurers that addresses a number of key risk areas: (a) structure/ownership risks; (b) business risks, e.g., third party business of captives, premium level and exposures; (c) transactional risks; and (d) changes in owners, directors and business plans. Staff members in the Insurance Division are expected to exercise sound judgment and the matrix allows manual override to take account of other risk factors not explicitly addressed by the matrix. Insurers are assigned risk

	ratings of low, medium, and high. A similar risk matrix has been customized for intermediaries. GFSC checks insurers' risk assessment and management systems during on-site inspections and through the analysis of their annual returns.
Assessment	Observed
Comments	GFSC has provided guidance to the industry on their risk assessment and risk management. Its risk-based approach to supervision addresses the risk profile of insurers and intermediaries systematically using a risk matrix. It is important for the risk matrix to be updated and enhanced as GFSC gains experience and to take account of emerging risks. GFSC is advised to refine the risk matrix to incorporate explicit factors that address insurers' corporate governance and risk management framework.
Principle 19.	Insurance activity Since insurance is a risk taking activity, the supervisory authority requires insurers to evaluate and manage the risks that they underwrite, in particular through reinsurance, and to have the tools to establish an adequate level of premiums.
Description	The CGC requires insurers to address underwriting risk through the establishment of an underwriting strategy, including policies on pricing and retention limits. As part of the annual returns, general insurers furnish a summary of their proposed insurance and reinsurance programs, including exposures accepted, names of reinsurers, security ratings and attachment points. Long-term insurers are required to provide a summary of the products to be offered and confirmation that the actuary has approved all such products. The Boards of insurers must also establish a reinsurance strategy, taking into account reinsurance credit risk and diversification. They should regularly monitor results of the reinsurance strategies, including recoverability of amounts due. Insurers are required to complete a declaration of reliance on reinsurers as part of their annual returns. The declaration requires disclosures of exposure to any reinsurer and its related companies in the same group exceeding 10 percent of an insurer's shareholder funds. Where the 10 percent threshold is exceeded, the insurer shall provide additional information to GFSC including the credit rating of the reinsurer, status of recovery and whether this is a related-party transaction. Some captive insurers do not have reinsurance protection. GFSC explained that some of them do not require reinsurance protection because their aggregate risks were fully covered by available capital. GFSC checks the application of these requirements by examining insurers' annual returns and during on-site visits. For insurers assessed as having higher risk, such as commercial insurers or reinsurers, further monitoring is undertaken, e.g., additional meetings or provision of additional information. Insurers submit their business plans with the annual returns. Any material

	changes to the risk retention or reinsurance strategy are regarded as a change of business plan and subject to prior notification to GFSC. Insurers' accounting treatment of risk transfer instruments is checked by the auditors. The auditors are required to confirm that the accounts are prepared in accordance with recognized accounting standards, which would include the proper accounting of risk transfer instruments.[64]
Assessment	Observed
Comments	GFSC requires insurers to have in place strategic underwriting and pricing policies approved and reviewed regularly by the Board of Directors. It checks that insurers manage their insurance risks effectively. GFSC approves applications from captive insurers to have no reinsurance protection on a case-by-case basis. For transparency and consistency, GFSC is advised to provide guidance on how it assesses the insurance risks of captive insurers seeking approval to have no reinsurance protection.
Principle 20.	Liabilities The supervisory authority requires insurers to comply with standards for establishing adequate technical provisions and other liabilities, and making allowance for reinsurance recoverables. The supervisory authority has both the authority and the ability to assess the adequacy of the technical provisions and to require that these provisions be increased, if necessary.
Description	Apart from the requirement to produce accounts in accordance with recognized accounting standards, GFSC has issued guidance on the factors to be included in an actuarial valuation of long-term companies. Insurers must provide a summary of the valuation methodology used and details of the valuation basis including per policy expenses, interest rate assumptions, unit growth rate, discount rate, inflation assumptions and mortality/morbidity rates. The actuary should also disclose whether any credit has been taken for negative reserves.[65] General insurers are required to provide a summary of the methodology used to calculate insurance reserves as part of their annual returns. This includes reserves for claims incurred but not reported or insufficiently reported and outstanding claim reserves. The summary of claims paid and outstanding should include, where relevant, a reconciliation of the movement in claims reserves over the financial period, by class of business. For PCCs, this information should be provided for the core, where applicable, and each active cell.[66]

[64] Schedule 3 of the IBL.

[65] Actuarial Valuation Guidance Notes.

[66] Guidance Note on the Submission of Annual Returns for International Insurers (NonLife).

	Credit is not given for reinsurance ceded to an associated party unless the reinsurer is a licensed insurer or with GFSC's consent.[67] Further guidance is also available in the ORSA Guidance Notes. Where actuarial advice has been obtained regarding the level of reserves, copies of the actuarial reports are provided to GFSC. Actuarial reports must be prepared in accordance with appropriate actuarial standards. The methodology used to establish technical provisions is assessed during on-site visits and in the case of long-term insurers, through a review of the actuarial valuation reports. If technical provisions are insufficient, GFSC may impose licensing conditions requiring insurers to rectify the shortfall. Actuarial reports are also reviewed for general insurance technical provisions where they have been used by the directors of the insurer to assist in determining the required level of IBNR. While GFSC may impose licensing conditions requiring insurers to rectify any shortfall in technical provisions, the IBL does not explicitly require insurers to maintain adequate technical provisions at all times. This is partly mitigated by the CGC requiring insurers to control reserving risk by: (a) establishing adequate technical provisions and other liabilities based on sound accounting and actuarial principles and evaluation by legal advisers and claims adjusters; (b) the establishment by the Board and senior management of appropriate reserving policies; and (c) stress testing the adequacy of capital resources on a regular basis for a range of adverse scenarios, where appropriate.
Assessment	Observed
Comments	The CGC requires insurers to maintain adequate technical provisions and other liabilities. While there is no explicit legal provision on technical provisions, GFSC may impose licensing conditions, where appropriate. In practice, insurers are expected to maintain adequate technical provisions under the CGC and GFSC checks insurers' methodology in estimating technical provisions. GFSC is advised to consider including an explicit legal provision in the IBL requiring insurers to maintain adequate technical provisions at all times.
Principle 21.	Investments The supervisory authority requires insurers to comply with standards on investment activities. These standards include requirements on investment policy, asset mix, valuation, diversification, asset-liability matching, and risk management.
Description	GFSC has specified the investments and limits or restrictions on the amounts of assets that can be taken into account for solvency purposes.[68]

[67] s1(6) of Schedule 2 of IBL.

[68] Insurance Business (Approved Assets) Regulations, 2008.

	Approved assets are categorized into four classes based on their liquidity and quality. Class 3 and Class 4 assets can only be counted as approved assets up to 10 percent of an insurer's total market value of gross assets per counterparty. Derivatives (other than those specified, see ICP 22), accounts receivable (other than premiums receivable that are less than three months overdue) from an associated party and encumbered assets do not qualify as approved assets. Insurers are required to provide details of investments held as part of their annual returns. Investments are to be valued in accordance with generally accepted accounting principles. GFSC has the power to approve specific investments and requires investments to be valued at market or fair value.[69] The CGC requires that insurers establish an investment strategy which is approved and reviewed annually by the Boards of insurers. The investment strategy should include a contingency plan. Insurers must establish investment monitoring procedures as well as monitor and manage the asset/liability matching position. Insurers should also conduct regular resilience testing for a range of market scenarios and changing investment and operating conditions to assess the appropriateness of asset allocation limits. While GFSC does not adopt a prescriptive approach for resilience testing, the assumptions should be realistic, but sufficiently adverse to show the impact of a significant market movement, e.g., equity prices move by 25 percent and a significant increase in the level of inflation from current levels. If the resilience testing demonstrates that there is a mismatch between assets and liabilities, an insurer should have regard to its capital position and consider establishing a specific mismatching reserve to ensure that it can still satisfy the minimum solvency requirements if market conditions change.[70] The CGC expects insurers to have risk assessment and management systems to address risks associated with investment activities, including market risk, credit risk, liquidity risk and custody risk, where these risks are significant. Investment monitoring procedures should also be appropriately segregated. The Boards of insurers are responsible for overseeing the custody and banking arrangements to safeguard the assets. They must ensure that key staffs involved in the investment activities have appropriate skills, experience and integrity. The ultimate responsibility remains with the Boards even if the investment activities and functions are delegated or outsourced. The actuarial valuation of long-term insurers must provide details of asset/liability matching and any resilience reserves required. This should

[69] Insurance Business (Asset and Liability Valuation) Regulations, 2008.

[70] Guidance Notes for Licensed Insurers on Resilience Testing.

	include the basis used for testing asset/liability matching under a range of scenarios and should specify the extent to which additional resilience reserves are required. Loans to related companies should always be conducted on an arms-length basis, attract a commercial rate of interest and are repayable on demand. Furthermore, insurers must ensure that such loans do not have significant impact on financial resources and risk profile. As part of its on-site visits, GFSC checks that insurers have in place adequate internal controls to ensure that assets are managed in accordance with the overall investment policy, as well as in compliance with legal, accounting, and regulatory requirements.
Assessment	Observed
Comments	GFSC has established clear regulatory requirements relating to insurers' investment activities. Insurers are also required to conduct resilience testing as part of their OSCA.
Principle 22.	Derivatives and similar commitments The supervisory authority requires insurers to comply with standards on the use of derivatives and similar commitments. These standards address restrictions in their use and disclosure requirements, as well as internal controls and monitoring of the related positions.
Description	Restrictions on the use of derivatives are applied through the approved asset regulations. This means that the approval of GFSC is required before derivatives can be used to satisfy solvency requirements. Derivatives are classified as Class 4 assets only if they meet specific stringent requirements. The admissibility of Class 4 asset is limited to 10 percent or less of the insurer's total gross assets per counterparty. Class 4 assets include: (a) exchange traded derivative contracts that are not leveraged or are used for index tracking strategy, as part of capital protected strategies, for efficient portfolio management, or to reduce investment risk; (b) forward foreign exchange transactions conducted with a recognized bank to hedge currency exposures; and (c) where a derivative contract changes the characteristics of underlying assets, those underlying assets. Where insurers wish to invest in derivatives, the CGC requires the Boards of Directors to establish an appropriate policy for their use, which is subject to annual review. The Boards should ensure that internal controls over derivatives and other complex investment instruments have been implemented and are adequate. The policy for the use of derivatives should include: (a) the purpose of using derivatives; (b) appropriately structured exposure limits; (c) restrictions on the use or amount of certain types of derivatives; and (d) the establishment of individual responsibility and a framework of accountability for derivatives transactions. The Boards should also ensure: (a) that the directors collectively have sufficient expertise and understanding of derivatives instruments; (b) suitably qualified and competent staff are responsible for conducting and

	monitoring derivatives activities; (c) controls are in place to verify that pricing of derivative instruments are appropriate; and (d) effective risk management so that risks arising can be analyzed and monitored individually and in the aggregate, and in an integrated manner with similar or correlated risks arising from nonderivative activities so that exposures can be considered on a consolidated basis. The use of derivatives by insurers is monitored by GFSC through the review of annual returns and on-site visits. Insurers' accounts must be prepared in accordance with recognized accounting standards and audited, with disclosure requirements for financial instruments and derivatives.
Assessment	Observed
Comments	GFSC's regulatory rules for derivative activities are well developed.
Principle 23.	Capital adequacy and solvency The supervisory authority requires insurers to comply with the prescribed solvency regime. This regime includes capital adequacy requirements and requires suitable forms of capital that enable the insurer to absorb significant unforeseen losses.
Description	All locally incorporated insurers must maintain paid-up capital of no less than the *minimum capital requirement (MCR*). Shareholders' funds must be at least 75 percent of MCR, taking account of currency fluctuations. Insurers who are not incorporated companies must maintain non-distributable funds of no less than the MCR.[71] General insurers must meet MCR in the form of minimum solvency margin requirement. The margin of solvency is the excess of the value of assets over the value of liabilities of an insurer. The minimum solvency margin for general insurers is the higher of: (a) the sum of 18 percent of the first £5 million of net premium income and 16 percent of the net premium income in excess of £5 million; or (b) 5 percent of loss reserves.[72] Long-term insurers are required to maintain solvency margin of not less than the greater of: (a) £250,000, or (b) 2½ percent of the segregated long-term insurance fund.[73] GFSC has prescribed valuation basis assets and liabilities under the Insurance Business (Asset and Liability Valuation) Regulations, 2008. Assets admissible for solvency purposes are spelt out under the Insurance Business (Approved Assets) Regulations, 2008. (Please also refer to ICP 19 to 22). GFSC may require insurers to maintain higher solvency, taking into consideration: (a) the nature and classes of business involved; (b) the spread of risk and the historic and industry based claims data; (c) the size,

[71] s32(1) & (2) of IBL.

[72] Loss reserves are the sum of reported outstanding losses and provision for losses incurred but not reported less reinsurance recoverables.

[73] Schedule 2 of IBL.

	complexity of business and business risks of the insurer; and (d) pertinent information relevant to evaluating the insurer's loss reserves. In practice, insurers are required to hold solvency capital equal to at least 150 percent of the MCR. The "risk gap" approach is adopted for simple captive insurers where account cannot be taken of diversification or pooling of risk. The risk gap is the difference between the maximum total claim amount in any one year and the expected premium income. The risk gap should be more than covered by available capital, i.e., paid-up capital, partly paid capital and retained earnings. In addition, captive insurers in Guernsey often use fronting insurers licensed in EU for certain classes of risk such as employers' or motor liability. Under such fronting arrangements, the captive insurer acts as a "reinsurer" and this means that the fronting insurer has to consider the admissibility of the "reinsurance" in its own solvency calculations.[74] GFSC is in active discussion with relevant insurance supervisors to establish the impact of Solvency II on the European captive insurance market. Consideration needs to be given in applying the Solvency II requirements to PCCs where individual cells have recourse to core capital for solvency purposes. GFSC has taken a proactive stance in introducing a risk based solvency regime through the introduction of OSCA in 2008, applicable to all insurers, including captives. The objective is to ensure that the Boards of insurers consider their own specific risk profile in determining the appropriate level of capital to be held in excess of the MCR. GFSC has issued the Guidance Note on Licensed Insurers' Own Risk and Solvency Assessment detailing the risk factors that should be taken into account. The CGC also requires insurers to undertake stress testing on the adequacy of their capital resources on a regular basis for a range of adverse scenarios, where appropriate. On the suitable forms of capital, GFSC's Guidance Note states that "insurers may wish to consider the nature of the capital resources needed to cover the OSCA." Whilst technical provisions and the minimum solvency margin must be covered by approved assets, additional capital resources can sometimes take the form of the unpaid element of partly paid share capital, letters of credit or loans to a parent or group company. In addition, certain liabilities, such as subordinated loans, could be treated as capital for this purpose. Intangible or illiquid assets, such as goodwill or property, are generally not acceptable for solvency purposes. Inflation of capital through multiple gearing is not permitted since an investment in an insurance

[74] Under Solvency II, EU insurers ceding reinsurance to an insurer outside the EU will not be able to take credit for the ceded reinsurance unless the reinsurer is subject to a regulatory and supervisory regime considered equivalent to Solvency II. Criteria for assessing equivalence are expected to be established by Committee of European Insurance and Occupational Pensions Supervisors by July 2010. Source: A leader in Regulation, Guernsey Finance.

	subsidiary would not be considered as an approved asset. During the mission, GFSC published its policy on suitable forms of capital, in line with the IAIS Guidance paper on the structure of capital resources for solvency purposes. In response to the 2008/9 financial crisis, GFSC reviewed all insurers where a parental loan had been approved as approved asset for solvency purposes. It has a policy for all such approvals to carry an expiry date or some other trigger for review of the loan approval. When considering approval for a parental loan, GFSC takes into consideration the financial position of the insurer and its parent, as well as the market conditions of the industry in which the parent operates. The minimum solvency margin, calculated on a formulaic basis, acts as the lower solvency control level where a breach requires immediate rectification or other measures, such as closure to new business. The OSCA acts as the upper solvency control level and GFSC may intervene if it is breached. An insurer's OSCA needs to be agreed by GFSC and additional capital requirements will be imposed, if required. Insurers may calculate their OSCAs using internal models to test solvency over a range of different economic and market conditions. The use of internal models is expected to be limited to certain large long-term insurers and reinsurers although it may also be an option for larger captive insurers. At this juncture, GFSC has consciously taken a non-prescriptive approach but plans to refine the framework, informed by the experience gained from implementing OSCA. The CGC requires insurers to establish an internal control system to monitor the adequacy of their resources to ensure compliance with the MCR and solvency requirements at all times. Any breaches are required to be reported to GFSC within seven days. Branches with head offices in EU, Jersey and Isle of Man, and carrying on business are exempted from capital and solvency requirements. GFSC informed that some UK insurers operate in Guernsey through branches, all of which were licensed historically (more than 10 years ago) because they had a physical presence in Guernsey. These insurers no longer have a physical presence and are providing products on a services basis only. GFSC opines that business written through these operations is caught within the FSA protected insurance contract framework. GFSC is currently working with these inactive branches on the withdrawal of their licenses. However, branches of non-U.K. life companies are required to localise assets and meet solvency requirements in their own right. This is monitored through a requirement for separate branch accounts.[75] GFSC conducts regular comparisons of its solvency regime with other jurisdictions. It monitors EU Solvency II developments and Guernsey is an

[75] Code of Practice for Branch Operations.

	active member of the IAIS Solvency Subcommittee.
Assessment	Observed
Comments	GFSC has taken a proactive approach in the introduction of OSCA and implementing a more risk-based solvency regime. It is advised to continually assess the practical implementation of OSCA, including establishing criteria on the use of internal models.
Markets and consumers	
Principle 24.	Intermediaries The supervisory authority sets requirements, directly or through the supervision of insurers, for the conduct of intermediaries.
Description	Any person carrying on business as an insurance manager or insurance intermediary must be licensed by GFSC and meet the minimum criteria for licensing. Intermediaries are required to conduct their business with prudence, integrity and appropriate professional skill. Directors of intermediaries and Authorized Insurance Representatives (AIRs) must also be fit and proper, including relevant educational and professional qualifications. Any unlicensed intermediary will be reported to the Attorney General's office for possible prosecution. GFSC may also apply to the Court to obtain an injunction against an unlicensed intermediary.[76] GFSC introduced mandatory minimum qualifications for AIRs providing advice on long-term insurance products in June 2006. These minimum qualifications include the requirement to hold the Guernsey Insurance Certificate. Since its introduction, nearly 150 AIRs have achieved this qualification. GFSC has issued the Code of Conduct for AIRs. Under the code, AIRs can give advice on only those matters in which they are competent. An AIR advising on long-term insurance should ensure that he has sufficient knowledge of relevant legislation and if he is unable to advise a client, he should refer the clients to a person who can give appropriate advice. GFSC has a similar range of powers that can be used against intermediaries as those used against insurers. These include conditions of license, revoking licenses, prohibition orders against individuals, discretionary financial penalties and public statements. An insurance intermediary shall open and maintain a separate bank account for client money, and ensure that this account is clearly separate and distinguishable from its own bank accounts. Client money shall be paid into the client bank account no later than the next business day after receipt. Where it is not so paid in, it must be paid into the account as soon as possible and the reason for the failure must be recorded on the client file. Where the money is not paid in within 3 business days of being

[76] s1, s2 and Schedule 4 of IMIIL.

	received, the relevant client must be informed. The intermediary must also carry out regular reconciliations of the amounts held in its client account against the amounts which should be held for clients. GFSC checks compliance with the client monies requirements during on-site visits.[77] Insurers must ensure that all AIRs used by them provide prospective clients with information as to whom they represent and what type of products they are able to sell and/or advise on. GFSC also requires insurance intermediaries to disclose to their customers any interest in excess of 10 percent in any insurer. It is an offence for an intermediary to induce another person to enter into any contract of insurance by making any statement, promise or forecast which is false, deceptive or misleading in a material particular or by dishonest concealment of material facts.[78]
Assessment	Observed
Comments	GFSC has a comprehensive framework for regulating and on-going supervision of the market conduct of insurance managers and intermediaries.
Principle 25.	Consumer protection The supervisory authority sets minimum requirements for insurers and intermediaries in dealing with consumers in its jurisdiction, including foreign insurers selling products on a cross-border basis. The requirements include provision of timely, complete and relevant information to consumers both before a contract is entered into through to the point at which all obligations under a contract have been satisfied.
Description	The Licensed Insurers' Code of Conduct and the Code of Conduct for AIRs require insurers and intermediaries, respectively, to conduct business "with utmost good faith and high standards of integrity, exercising due skill, care and diligence with dealing with clients." Licensees must also "have in place a fair dealing policy to avoid any conflicts of interest." The Code of Conduct for AIRs does not apply to AIRs used by international insurers outside of Guernsey as they are supervised by the supervisor that authorized their operations. The Principles of Conduct of Finance Business requires that where conflicts of interest arise, financial institutions "should ensure fair treatment to all its customers by disclosure, internal rules of confidentiality, declining to act or otherwise." Besides providing customers with "any information needed to enable him to make a balanced and informed decision," they are expected to seek from customers any relevant information about their circumstances.

[77] The Insurance Managers and Insurance Intermediaries (Client Monies) Regulations, 2008.

[78] s87(3) of IBL and s64(3) of IMIIL.

	An AIR should obtain and record all relevant information relating to the personal and financial circumstances of clients necessary to give suitable advice (long-term business). He is required to explain the principal terms of any insurance contract recommended by him. He should not advise a client to convert, lapse, cancel or surrender any long-term insurance contract unless he can demonstrate the action to be in the best interests of the policyholder. If such action is advised then the advice should be fully documented in a written advice, a copy of which should be sent to the client. The Conduct of Business Rules and the Licensed Insurers' Code of Conduct require insurers to have in place procedures for dealing with customer complaints. The complaints procedure should provide for: (a) complaints to be first reported to the compliance officer; (b) escalation to a member of the Board if a satisfactory response is not issued within 30 days; (c) if not resolved within 30 days after stage (b), the insurer should inform the complainant of his rights and procedures to pursue the complaint, further; (d) notification to GFSC if a satisfactory response is not issued within 90 days of complaint; and (e) appropriate information is to be provided to the customers to enable them to contact the relevant parties. AIRs shall not use or disclose any information acquired from clients except for negotiating a contract of insurance or in handling a claim for a client, unless the written consent of the client has been obtained. They may, however, disclose client information if required in the public interest or compelled by law. GFSC issues warning notices to consumers to avoid transactions with unsupervised entities on its website from time to time. The public is also warned on the risks of arranging insurance directly, either through the internet, with insurers or via insurance intermediaries that are not licensed by GFSC. GFSC checks compliance with the codes, rule and principles relating to market conduct during on-site visits. GFSC is actively engaged with the GTA University Centre by providing resources and support for insurance training and the Guernsey Insurance Certificate examination programme. The GTA University Centre procures, facilitates and promotes high quality training to all sectors of the Guernsey community. Guernsey is currently considering the establishment of a Financial Services Ombudsman.
Assessment	Observed
Comments	Regulatory measures to protect domestic policyholders are implemented via market conduct supervision of domestic insurers and intermediaries. However, GFSC has no jurisdiction over overseas intermediaries working with international life insurers, who have significant business volumes in a number of jurisdictions.

	GFSC is advised to consider effective regulatory cooperation with relevant regulatory authorities to enhance the protection of policyholders located outside of Guernsey.
Principle 26.	Information, disclosure & transparency towards the market The supervisory authority requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks to which they are exposed.
Description	Domestic insurers are required to make available to policyholders and potential policyholders, upon request, their annual audited accounts. The accounts may be an abridged form which must be approved by GFSC. All insurers writing long-term business are required to make available their annual actuarial report, on request, to policyholders.[79] GFSC has issued a consultation paper on public disclosure. Under the proposed Public Disclosure Rules, all insurers will be required to publicly disclose, on an annual basis, both quantitative and qualitative information on their financial position and performance. The requirement does not apply to captive insurers that do not insure unrelated party risks.[80] Insurers in Guernsey have raised concerns in complying with the disclosure requirements.
Assessment	Partly Observed
Comments	The IBL requires limited disclosures and only upon specific requests of policyholders and potential policyholders. The objective of ICP 26 is to facilitate market discipline through public disclosure to all stakeholders, including market analysts. GFSC has issued a consultation paper on public disclosure. GFSC should consider how best to implement the public disclosure standards established by the IAIS. [81]
Principle 27.	Fraud The supervisory authority requires that insurers and intermediaries take the necessary measures to prevent, detect and remedy insurance fraud.
Description	Insurers are required to establish effective procedures and controls to deter, detect, record and report fraud. Insurance managers and intermediaries must have adequate systems of control, which includes controls for deterring fraud.[82] The Guidance on Preventing, Detecting and Remedying Insurance Fraud,

[79] s39 & s41 of IBL.

[80] s38B of IBL.

[81] Technical Performance and Risks for Nonlife Insurers and Reinsurers, Technical Risks and Performance for Life Insurers and Investment Risks and Performance for Insurers and Reinsurers.

[82] CGC and Schedule 4 of IMIIL.

	2008 provides clear guidance to insurers, intermediaries and managers on meeting these requirements. It also covers the need for adequate training and the need to exchange information on an industry-wide basis. Insurance managers are expected to be alert to potential fraud risks by assessing identity and financial strength of parental companies, identity of insureds, location of parent, third party involvement and ownership structure. There may be higher fraud risks in some captive structures, e.g., producer-owned reinsurance captives. The Insurance Division assesses insurers' and intermediaries' measures to prevent fraud during on-site visits. The Director of Insurance is the chair of the IAIS Insurance Fraud Working Group; the Division may also tap into the anti-fraud experience of the Policy and International Affairs Division. Insurer fraud and claims fraud are addressed in the Fraud Law which came into force on 1 October 2009 and the Theft Law. A successful prosecution for claims fraud has been made under the Theft Law. All financial services businesses must have appropriate procedures for hiring staff to ensure high standards of employee probity and competence.[83] GFSC Chairs the IAIS Insurance Fraud Working Group. It can cooperate with other supervisory authorities and is able to exchange information under the IBL and IMIIL. The FSC Law also empowers GFSC to cooperate with any person or body for the purposes of the investigation, prevention or detection of crime. GFSC has cooperated with other supervisory authorities in the investigation of crimes.
Assessment	Observed
Comments	GFSC has set clear requirements and provided meaningful guidance to insurers, insurance managers and intermediaries to combat insurance fraud.
Anti-money laundering, combating the financing of terrorism	
Principle 28.	Anti-money laundering, combating the financing of terrorism (AML/CFT) The supervisory authority requires insurers and intermediaries, at a minimum those insurers and intermediaries offering life insurance products or other investment related insurance, to take effective measures to deter, detect and report money laundering and the financing of terrorism consistent with the Recommendations of the Financial Action Task Force on Money Laundering (FATF).
Description	Guernsey's AML/CFT legislation and supervisory practice are based on the requirements of the FATF Recommendations and Special Recommendations. The AML/CFT regime applies to all financial services

[83] CJ (POC)(FSB) Regs s13(1) – Employee Screening and Training.

	businesses in Guernsey, and to both life and general insurance products. It covers Guernsey-based branches and offices of companies incorporated outside Guernsey conducting financial services business in Guernsey. Guernsey satisfied the European Commission that its AML/CFT framework was equivalent to the second EU money laundering directive. The United Kingdom also issued a statement on equivalence in May 2008, which advised that it considers Guernsey and the other Crown Dependencies to have AML/CFT standards equivalent to the EU (i.e., the third EU money laundering directive). *The Handbook for Financial Services Businesses on Countering Financial Crime and Terrorist Financing (AML/CFT Handbook)* sets out rules and guidance to assist insurers in complying with the AML/CFT legislation. The *AML/CFT Handbook* permits an insurer to adopt a risk-based approach to AML/CFT appropriate to its particular circumstances. An insurer should give consideration to additional measures that may be necessary to prevent its exploitation and that of its services/products and delivery channels by persons seeking to carry out money laundering or terrorist financing. International life insurers conducting business through financial advisers in other jurisdictions are required to establish appropriate policies, procedures and customer due diligence to address AML/CFT risks. The assessors were informed that all documentation on customer due diligence are maintained locally. The IBL, the IMIIL and the Proceeds of Crime Law empower GFSC to monitor compliance with AML/CFT requirements, including the ability to request information and carry out on-site visits. Directors, controllers, partners, managers and general representatives of insurers must be fit-and-proper persons. GFSC performs due diligence checks on these persons. All individuals holding such positions must submit a PQ, to be updated whenever there is a material change, and a new PQ must be completed every five years. GFSC has the legal authority to object to potential beneficial owners or managers. (Refer to ICP 7). All insurers must: (a) establish policies, procedures and controls to prevent and detect money laundering and terrorist financing; (b) the Boards of insurers are responsible for regular reviews of compliance with AML/CFT requirements; and (c) ensure that a review of its compliance is discussed and recorded at Board meetings. All insurers must have a Money Laundering Reporting Officer (MLRO) (this may be the MLRO of the Insurance Manager). A change in the MLRO requires prior notification to GFSC based on a completed PQ. The IBL, the IMIIL and the FSC Law enable GFSC to exchange information with the law enforcement authorities and with other supervisory authorities, including foreign authorities, for AML/CFT purposes. (Refer to ICP 5). GFSC devotes resources to AML/CFT supervisory activities through the training of staff and on-site visits. Compliance with AML/CFT requirements

	is monitored through on-site inspections, including “themed” visits that have included specific AML/CFT compliance analysis. The Insurance Division has sufficient staff to devote to AML/CFT issues and the fees set annually provide sufficient financial resources for AML/CFT activities. AML/CFT specialists within the Policy and International Affairs Division provide technical expertise to the Insurance Division. A separate LEG/IMF mission in May 2010 is conducting a full assessment of Guernsey’s observance with the FATF AML/CFT standards.
Assessment	Observed
Comments	GFSC applies robust AML and CFT requirements to insurers and intermediaries for both life and general insurance products. It supervises compliance through on-site inspections. The AML/CFT handbook provides guidance to insurers and intermediaries in adopting a risk-based approach to AML/CFT.

Appendix 1. Status of Implementation of 2003 Recommendations

Reference Principle	Recommended Action	Action Taken
CP 1 Organization of an Insurance Supervisor	In order to strengthen the operational independence of GFSC, the mission recommends that GFSC Law be amended to remove the power of the Advisory and Finance Committee to provide guidance and direction to GFSC. The GFSC Law should establish safety, soundness, and integrity of the financial system as the objectives of GFSC, and eliminate "development" as one of the GFSC functions. Further, there should be no provisions in the Law that could potentially compromise the above-stated objectives. This would provide a clear legal framework that would avoid potential conflicts in the functions of GFSC. The attainment and sustainability of these objectives will enhance the reputation and contribute to the development of the financial system in Guernsey. The number of staff has to be increased.	The FSC law has been amended to implement the recommendation. The Insurance Division appears to have adequate staff resources. It may also engage external experts as necessary such as accountants, lawyers and actuaries.
CP 8 Capital Adequacy and Solvency	Increase the legally required solvency minimum.	GFSC has introduced Own Solvency and Capital Assessment requiring Boards of insurers to consider their own specific risk profile in determining the appropriate level of capital to be held in excess of the minimum capital requirement.
CP 14 Sanctions	Complete the range of sanctions by the power of the supervisor to impose penalties (administrative fines).	The FSC law has been amended to implement the recommendation.