Guernsey Financial Services Commission

9th Conference – 4th April 2019

Beyond Brexit

William Mason, Director General

When we were picking topics for our regulatory seminar, after a gap of 18 months, I looked at the dates, took the Prime Minister at her word, and thought it would be a really good time to pull together some reflections on Brexit, given that the process would have "finished" a few days previously. I now realise that that perspective was more than a little naïve but I'm delighted to welcome the panel we have assembled for this afternoon's discussion. Mr Rees Mogg and Deputy St Pier have not always held identical perspectives on Brexit as they have respectively sought to uphold and advance the interests of the Brexit voting majority in the UK and the interests of the Bailiwick through what has been and is an opaque and tortuous process. I am delighted to welcome them and am looking forward to their sharing some views with us on the subject, given the stage we have now reached. Given that they are far better placed to talk about Brexit than me, I thought I would not talk about Brexit itself but rather try to focus on what lies beyond in terms of the challenges we face, challenges which it has perhaps been difficult to focus on wholeheartedly whilst having to observe all the nuances of Brexit so closely.

Slide: The global concerns of the World Economic Forum

I will start by mentioning a few of the risks highlighted by the World Economic Forum in its 2019 report prepared for its famously un-populist summit at Davos where some members of the internationalist elite gather each year. As the Gilet Jaune across the water will testify, this elite can often appear to some to be tone deaf to the concerns of ordinary hard working people and their desire to preserve community, shared values, belonging and a sense of place - all qualities The Bailiwick has in such vast quantities that it is often difficult for us to appreciate quite how under pressure these things are in other jurisdictions. This populist critique of Davos should not lead us to believe that all the concerns the World Economic Forum expresses are misguided. Its global risk report is thought provoking and highlights:-

a) The change in the human condition in the developed world, perhaps for the worse. There has been the c. 50% increase in depression and anxiety disorders over the last quarter of a century with some seeing linkages between this and the use of digital technology. These anxieties may of course be linked to the fact that between c. 30% of people in the US, UK and a vast c. 60% in France expect to lead a worse life than their parents or the growing and unprecedented share of people living alone – up from 5% in pre-industrial communities to c. 30% in many developed nations with it hitting a high of 60% in Stockholm. Another contributory factor may be a fall in the number of close friends adults have say they have and an unsurprising increase in loneliness.

b) The impact of global warming in terms of the threat to the Antarctic ice sheet and the impact that would have on various coastal communities, not least of which ourselves. This, allied with the melting of the Hindu Kush glaciers and the impact of that on many populous Asian countries is perhaps especially concerning given that the last four years have been the hottest on record – the wonderful summer we had here last year has its downsides;

c) The increase in biological threats. The report highlights the impact of the increase in swift air travel to all quarters of the globe which, unfortunately, ensures that an infectious disease outbreak can move from the most remote African village to cities around the world in less than 36 hours giving precious little time for disease fighting agencies to react, especially given the paucity of resources devoted to developing vaccines for the top 11 infectious diseases and the declining effectiveness of antibiotics. A related biological threat which is concerning is the ease with which new pathogens can now be developed in micro-labs with the assistance of machine learning to help hostile actors engineer the most virulent possible disease strains which would pass easily from human to human killing millions deliberately rather than by accident; and

d) Somewhat less alarming but still concerning is the state of often antiquated "developed world" infrastructure and the commitment to public and private infrastructure funding in Africa falling to its lowest level for five years in the most recently available data.

Some of you will wonder why I've given you that list of something other than unbounded joy at the start of a regulatory talk. The more cynical of you will doubtless conclude that it's because it is the regulator's job to say depressing things to industry even if he can't find anything very bad to say about it at the moment. Well, I'm certainly not going to admit to that.

Slide: Offering Bailiwick Solutions

Rather I've highlighted these issues because I thought it was important to put some context around Brexit and because I believe that we should not be shy about thinking about how The Bailiwick's properly regulated IFC, as a significant gatherer and distributor of international capital, can help play a role in financing wealth enhancing private sector led solutions to some of these problems, problems which I do not believe are likely to be effectively addressed solely by governments alone without significant collateral damage to the prosperity enhancing international financial system - of which we form an important node.

We should be comfortable that others see us as part of the solution to such global problems too. Why else would so many developing parts of the world have paid us the most sincere flattery of imitation. If Hong Kong, Singapore, the Channel Islands and Bermuda are long established small state international financial centres, it is noteworthy how, in recent years, other countries have attempted to establish autonomous legal jurisdictions to mimic the benefits which we and the English Common Law offer for developmental finance. In the UAE there are now two competing centres, the DFSA and Abu Dhabi Global Markets whilst Qatar has its International Finance Centre with Kazakhstan setting up the AIFC in the last year to bring the benefits of an English speaking well regulated common law IFC to the steppes of Central Asia and wider to the Eurasian Economic Union. In summary, I think we should be comfortable, irrespective of whether London decides to rebrand itself as, "Singapore on Thames" that in a world facing many global issues, international financial centres are anything but passé but rather increasingly seen by many as part of the solution to global developmental challenges.

This is not to pretend that we can solve or even contribute meaningfully to the solution of all the many problems highlighted by the WEF (and I've only touched on a view of those which it discusses) but rather that in areas such as infrastructure finance, catastrophe reinsurance and the private equity management that will be required to finance the smaller problem solving companies that will develop many of the solutions to the current challenges facing humanity, we offer a valuable resource to help solve wider societal challenges.

We don't, of course, do that by sitting on our laurels. Over the past year, the Commission has been pleased to see We Are Guernsey developing its market facing strategy for presenting the Bailiwick's merits to external actors. Since we last assembled we have been happy to contribute to the Bailiwick with the development of a number of new and refined regulatory products:-

a) the revised PIF rules which appear to have encouraged considerably more use of this flexible fund vehicle;

b) the Guernsey Green Fund – designed to build upon the Bailiwick's strengths as the green isle with a long track record of successful infrastructure fund administration whilst offering investors reassurance that their money will be used for environmentally friendly purposes – solving global problems;

c) the Green insurance discussion paper. It's too early today for Jeremy Quick or I to give you an update on our intentions as we are still digesting the consultation feedback on our proposals to facilitate increased investment by life insurers in green and other productive long term assets without being discouraged by an unduly penal capital regime. What I will note is the very encouraging remarks in a similar vein on insurance capital made by the Vice Chairman of the US Federal Reserve since we published our discussion paper – perhaps evidence that our thinking is only a little ahead of the rather significant US pack on how to reform insurance capital regulation to enable life insurers to maximise their ability to invest in productive assets for future generations. We will continue to work with our counterparts in the UN's Sustainable Insurance Forum to make sure that insurance regulations take into account the need to meet climate risks.

d) the new Anti-Money Laundering handbook which whilst not the most spine tingling read for non-money launders, is easy to understand. It also enables the proper use of electronic due diligence methods which can potentially cut out swathes of paper pushing in connection with customer due diligence, enabling employees valuable time to be spent on more productive tasks. We are hoping that, in due course, the States commitment to the Lending, Credit and Finance Policy Letter which we developed, may enable the regulation of electronic due diligence providers thus filling another part of the Bailiwick's electronic due diligence proposition in terms of providing some official sector assurance to the public that electronic due diligence providers are proper rather than information thieves.

e) another aspect of the LCF Policy Letter is that it should provide for a framework for regulating FinTech businesses which will not easily fit into an established regulatory category – potentially helpful given our status as a founder and co-ordinating committee member of the Global Financial Innovation Network which looks to pilot innovative FinTech on a global basis across jurisdictional boundaries.

Slide: Today we offer further product innovation – the Insurance Fund Hybrid

Today I'm pleased to announce that we are, from now on, happy to receive applications from mixed purpose Protected Cell Companies containing both investment and insurance cells, things which previously had to be done through separate companies. This provides for the creation of an ILS Fund Hybrid. We think that this new regulatory product, well aligned with We Are Guernsey's strategy of looking for growth adjacent to current areas of expertise, will add value to the Bailiwick and to global finance by providing an appropriately high quality insurance and investment product in a jurisdiction of substance. I'd like to thank Christopher Andersen for the time he's put into helping us think about how this regulated company structure could work. We have seen considerable growth in the ILS space in the past three years and we believe that our willingness to make use of the Bailiwick's existing laws to accept applications for this product has the potential to simplify ILS administration, in effect making possible a new form of insurance company within which investor demand for exposure to specific risk types can be matched with policyholder demand for specific types of insurance, all within the one overarching Protected Cell Company. The Authorisations and Innovation Division would be happy to discuss the technicalities of the application process further with fund managers, insurance managers and lawyers who may wish to establish such a PCC or ICC company.

Slide: Where we need to be careful

If that was the positive section of my talk, what is worrying the Commission nearer to home ? I won't go into huge detail but, at a high level:-

a) Cyber-attacks remain and are likely to continue to remain a major threat to both our collective reputation and our operational effectiveness. We have been delighted at the degree of co-operation with which we have been met when undertaking our ground breaking cyber thematic over the last few months and we hope that the lessons we extract from it will be useful to all of you. Whilst we can never offer any regulatory safe harbours, I will volunteer the sentiment that we don't want to take enforcement action against anyone for lax cyber security. It is something where, with the help of the National Cyber Security Centre, we think we are all in it together (if that phraseology isn't just a bit too George Osborne) and we need to pull together against the multiple threats, sharing information sensibly to preserve our common infrastructure and reputation.

b) Financial crime – here the evidence we gather through our visits is that the vast majority of firms are taking beneficial ownership requirements seriously and working well to make sure that their clients' wealth comes from reputable sources. There are, as with conduct, small pockets of poor practise which we are working to eliminate but the picture is generally reassuring. Unlike other jurisdictions we have not been infected by ICOs, otherwise known by some as Initial Crime Offerings and the Commission is thankful for that - we welcome good quality FinTech based on value delivered to the customer or investor rather than *"smash, grab it and run" technologies.*

c) Then there are prudential risks which strike us as elevated. Since 2008 debt levels have risen and with Italy officially entering recession early this year, with many Euro-area banks not generously capitalised and China suffering something of a property boom induced hang-over, one must be conscious of increased risks which may manifest themselves through emerging markets if the US Dollar strengthens appreciably. Then there are continuing trade tensions and a possible general tightening of liquidity after a decade of ultra-loose money. If any of you thought a downturn and its impact on your business was a discussion you could defer until next year, we'd strongly recommend having it at a board meeting soon.

d) Lastly I will turn to conduct – here, whilst the majority of the Bailiwick's firms are behaving well, we still uncover small pockets of lamentable practise. As the WEF study shows, levels of mental ill health and living alone without many friends are rising globally. Such people can be all too easy to exploit and some, unfortunately, are bound to be exploited but we see it is as our job to make sure that such people are not exploited by the Bailiwick's firms. Most firms are going a decent job with regard to their clients or investors fiduciary interests but some seem to regard the idea of loyalty to such ideals, rather than to transferring cash into their wallet as fast as possible, as something of a stupid joke. My message to you is that we are catching them and that as and when we catch them, we will seek to inhibit their ability to do business in the Bailiwick. In doing so, we will be safeguarding the island's good reputation on which you all trade.

There are other detailed points to be made and I know my fellow directors are raring to make them in their own unique styles on a sector or subject specific basis once we have finished discussing Brexit.

Slide: Supervision – Backing the Bailiwick Beyond Brexit

I will conclude on a positive note, observing that there is much for us to be positive about beyond Brexit in terms of the new products, services and business which the Bailiwick is able to do to make a meaningful difference to global issues, provided of course that we can keep the regulatory environment in the right place to provide appropriate protection without inhibiting high quality businesses.

Thank you for listening so politely this afternoon when I'm merely, on this occasion, the warm up act for Mr Rees Mogg, the noted financial services entrepreneur and successful emerging markets fund manager who has become a noteworthy participant in the public life of the United Kingdom since taking the once very margin seat of North East Somerset in 2010. As the London Palladium event showed last month, Londoners are willing to pay premium prices (some £35 a head) to hear him speak. For our part we are delighted he's agreed to join our long list of distinguished speakers. For those of you who attend regularly, you may find him less philosophically challenging than the Bishop of Dover and less technically demanding than Dr Sarapota the Executive Director of the Bank of England was when she spoke to us about developments in insurance capital. That said, please have your Latin primers at the ready … [Jacob]