Guernsey Financial Services Commission

Industry Seminar – 16 November 2016

Conduct Unit Presentation

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Slide: The Interaction of Business Culture with Regulation in the Past Decade

Good afternoon ladies and gentlemen. First of all I would like to thank you for joining me in the final slot of this year's presentations. I hope you will find it a helpful and interesting insight into the work of the Conduct Unit over the last year.

The theme of this year's presentation is The Interaction of Business Culture with Regulation in the Past Decade. As was mentioned yesterday, in spite of regulation, financial scandals still adversely affect the public at large. Sadly, we are not immune to this in Guernsey and as you are all aware, there are certain advisers of former licensees who no longer have the authority, or ability, to give financial advice or even work in the financial services industry. Some further examples of poor conduct and poor corporate culture were given as case studies yesterday and this morning, together with ideas to help establish and maintain effective corporate governance and a sound culture to help protect the reputation of the firm and the Bailiwick from financial scandal.

The last ten years has seen an increasing shift towards conduct supervision led in the UK by the Financial Services Authority being replaced with the Prudential Regulatory Authority and the Financial Conduct Authority. Here in Guernsey, the thematic review on the sale of long term insurance business in 2012 together with the request from the Commerce and Employment Department to implement the Guernsey Financial Advice Standards "GFAS", gave added impetus for the Commission to create the Conduct Unit in 2013. The Conduct Unit's initial priorities were to implement GFAS and to carry out further thematic work on sales practices to establish whether industry had implemented appropriate measures to address the issues identified by the Commission from its earlier thematic.

Our remit also includes looking at all financial services consumer matters to help ensure that a Commission-wide approach is developed whilst being mindful of our goal of risk-based supervision.

Slide: The Conduct Unit

In our session today I will briefly revisit GFAS and what we have been doing over the last year, following the introduction of the new rules and codes, in relation to advice given to retail clients which apply to investment licensees and their advisers, insurance intermediaries and their

Authorised Insurance Representatives - regardless of whether advice is given on long term or general insurance business - and insurance managers and any Authorised Insurance Representatives they may have.

I will then move on to talk about our supervisory and policy work in relation to insurance intermediaries and tell you a little more about some of our supervisory and policy work for other licensees and, of equal importance, our educational and consumer initiatives. Finally I will summarise our plans for 2017 and beyond.

There will then be an opportunity for you to ask questions of Jeremy and myself at the end of my presentation.

Slide: Update on the Implementation of the Guernsey Financial Advice Standards

As part of my presentations in each of the last three years, I have explained the background to the implementation GFAS and the development of the new sets of rules and codes of conduct at some length. You will be pleased to hear that this year I will be limiting GFAS to an update only.

As you will be aware, the new requirements implementing GFAS came into effect on 1 January 2015. However certain of these only became relevant at the end of that year – namely the requirement for licensees to de-authorise any Financial Adviser, who was an existing adviser at 31 December 2014, and who had not attained an acceptable level 4 qualification by the end of 2015. Any such financial adviser was then no longer able to give advice to retail clients on behalf of their employing licensee. They were, and still are, able to advise professional clients and eligible counterparties. One word of warning here, is that should a professional client no longer fulfil the initial conditions that made it eligible to be classified as such, or opt to be treated as a retail client, only a suitably qualified, competent and authorised Financial Adviser would be able to advise that client.

The other requirement that came into effect at the end of 2015 was for licensees to obtain a Guernsey Statement of Professional Standing from each of their Financial Advisers.

Slide: Guernsey Statement of Professional Standing

Statements to reflect professional good standing were to be obtained by 31 March 2016 for all existing advisers as at 31 December 2014, failing which, the Financial Adviser was required to be de-authorised by the licensee and, would no longer be able to provide advice to retail clients, until such time as their Statement of Professional Standing had been received.

We are very grateful to the UK accredited professional bodies for working with us to produce these statements; they also see it as a means of encouraging professionalism in the industry. We understand that some of them have already started to receive renewal applications and I would encourage you, to remind your Financial Advisers, of the annual requirement for them to provide you with a Guernsey Statement of Professional Standing, within three months of the expiry of the valid statement that is already held. Please note that if a new statement is not provided within this deadline, the Financial Adviser should be de-authorised until such time as the new statement is received.

From information that we have received, it appears that at the end of last year, a couple of firms and their employees got slightly carried away by applying for a Guernsey Statement of Professional Standing in situations where the employee does not give advice to retail clients and is not authorised as a Financial Adviser, or has been authorised in error. Can I ask that you only request and receive a Guernsey Statement of Professional Standing from authorised Financial Advisers and, if you have an employee with an existing statement, who does not actually give advice to retail clients, that this is not renewed.

Slide: Competence of new Financial Advisers

The conduct of business rules require Financial Advisers who give advice to retail clients to be assessed as competent by the licensee prior to their appointment to this role. In this regard, we would not expect a new employee to be authorised as a Financial Adviser on the first day of their employment at a new firm, unless there is a sufficiently documented assessment as to why this is reasonable. We have seen, and queried, a small number of notifications of such an appointment. Although an adviser may be experienced and competent having worked as a Financial Adviser at another licensee, amongst other considerations, we would expect the new licensee to have considered and assessed competence to advise on differing products, as well as being competent in the procedures operated by the firm and how these may impact on the advice process. The guidance note on Training and Competency Schemes contains further information on the Commissions expectations.

https://www.gfsc.gg/sites/default/files/Guidance%20Note%20on%20Training%20and%20Competency%20Schemes.pdf

I would also like to take this opportunity to draw to your attention the notification requirement within the conduct of business rules, to notify the Commission within 14 days of the authorisation or de-authorisation of a Financial Adviser, preferably through the online portal by uploading the completed notification form, available from our website, as an attachment to Form 200 or alternatively by sending the completed form by email to conduct@gfsc.gg.

Over the coming months, we will be streamlining this notification requirement with its own form for submission through the online portal and will advise relevant licensees when this form is available.

Slide: Numbers of Licensees as at 1 January 2016

Prior to the implementation of GFAS, concerns had been expressed about the potential impact it would have on those who were currently able to give financial advice and either did not want to achieve the qualification requirements or failed to do so. Now that the qualification deadline has passed, we have been able to assess the accuracy of the forecast.

There has been no change in the number of firms licensed to give advice to retail clients on controlled investments since the implementation of the new rules and codes. There are still 42 such firms out of 567 investment licensees licensed for the activity of advising as at 1 January 2015 and closer to 600 now. 15 of these licensees are also licensed to give advice on long term insurance business. So from that perspective there has been little impact.

Slide: Numbers of Financial Advisers as at 1 January 2015 and 2016

The same cannot be said for a comparison of the number of Financial Advisers working for those licensees. The information we received from licensees as at 1 January 2015 indicated that there were 159 Financial Advisers who were authorised to give advice to retail clients on controlled investments, with a further 49 who gave advice on long term insurance products as well, a total of 208 Financial Advisers.

Enquiries at that time led us to believe that 10 Financial Advisers – just under 5% of the total population - indicated that they would not be pursuing an acceptable level 4 qualification and as a consequence would cease to give advice to retail clients in 2016 and of those 10, 8 were employed by the 15 firms with both types of licence.

In order to clarify the impact of GFAS we asked relevant licensees to confirm their Financial Advisers at 1 January 2016. We were quite surprised by the results as the total population had fallen from 208 to 159 – an overall drop of 49. This decrease required investigation to determine whether it could give rise to a lack of choice for consumers, or challenges for the firms, their advisers or those who were no longer Financial Advisers.

Looking first at the firms with both licences, the number of Financial Advisers fell from 49 to 36, a drop of 13 compared with the 8 that had been indicated at the start of the year. In other words, at 1 January 2016 there were 36 people authorised to give advice on long term insurance products and controlled investments.

For the firms with an investment licence only who told us that they advise retail clients, the number of Financial Advisers fell from 159 to 123, a drop of 36. Indications had suggested that only 2 of these Financial Advisers were not looking to attain a level 4 qualification. Further clarification with industry identified that 20 Financial Advisers had not pursued or failed to attain a relevant qualification. Also, that in anticipation of the new requirements, at the onset, certain individuals had been authorised as Financial Advisers although they did not actually advise retails clients. These advisers were subsequently de-authorised, reflecting much of the fall in numbers. Furthermore, people left and joined the industry – in similar numbers.

Although hindsight indicates that, based on the information provided, the forecast for those who would not meet the qualification requirement was on the low side, please remember that failure to qualify, or choosing not to progress a level 4 qualification, does not prevent an individual from re-sitting or sitting the necessary exams, being assessed as competent and consequently authorised or re-authorised by their employer, or a new employer, as a Financial Adviser.

Now that GFAS has been fully implemented, we will continue to liaise with industry, the accredited professional bodies and other relevant stakeholders to ensure that the rules and codes are effective and appropriate, with due consideration of any steps being taken in other relevant jurisdictions.

Slide: Insurance Intermediary supervisory and policy work

Turning to our supervision of licensed insurance intermediaries, primarily through a combination of a reactive and thematic approach, our thematic focus in the last quarter of 2015 was on the sale of general insurance add-on policies. You may recall that prior to this going ahead, the Commission wrote to all Bailiwick-licensed general insurance intermediaries and asked them to read two certain thematic reports, published by the FCA, which itemised poor practice around add-on policies by UK general insurance intermediaries and a failing to serve the interest of their clients.

The Commission's letter drew attention to our consideration of the FCA's reports and our own Code of Conduct for Authorised Insurance Representatives and the Principles of Conduct of Finance Business and, asked all intermediaries, to review their policies and procedures, to ensure general insurance add-ons are sold in a manner which is compliant with the code and, if not, to instigate a remedial action programme.

We issued our thematic report early this year and I will include a link to it in the copy of today's presentation when it is published. If you haven't already read this report I would encourage you to do so.

https://www.gfsc.gg/sites/default/files/20151210%20-%20Guernsey%20Financial%20Services%20Commission%20V15%20-%20For%20Publication.pdf

Although the thematic review did not find evidence of serious detriment to customers, it did find evidence of poor practice, on the part of licensees and their Authorised Insurance Representatives, in respect of the sale of add-on policies, with these deficiencies often applying to sale of the core policies to which the add-ons are attached.

The thematic report reinforced the Commission's expectations that licensees will take steps to ensure that they are complying with the principle to have "fair dealing" with their customers and, to consider outcomes for customers as a fundamental element of the operation of their business and the way in which they plan the future of their business. The Commission clarified that it does not consider that offering add-ons on an opt-out basis represents "fair dealing", and its expectation that all general insurance intermediaries should take the necessary steps to phase out the sale of add-on policies on an opt out basis, or as part of a breakable bundle.

That said, our thematic work identified that it was necessary for us to consider the appropriateness of the Code of Conduct for Authorised Insurance Representatives and, where necessary, make revisions to the code, making it suitable for the way in which business is transacted in practice, including online, whilst maintaining good and reasonable standards.

Our thematic work also concluded that no revisions to the Insurance Intermediaries (Conduct of Business) Rules 2014 were necessary. However, we found that some licensees did not have in place the necessary arrangements required in respect of training and competence and, that licensees are not correctly identifying and recording complaints. Our thematic report reminded all licensees (not only those subject to the thematic visits) that they should take appropriate steps to ensure they are fully complying with the rules, and where there are deficiencies, to rectify these shortcomings.

We are currently considering our thematic focus for 2017 and beyond. In this we will be focusing on conduct; both for long term and general insurance intermediaries. I would welcome your suggestion of areas in which we should concentrate our efforts and which will result in an enhanced treatment of consumers. If you have any thoughts on this, please do get in touch.

Following on from the add-ons thematic, we have carried out a thorough review of the Code of Conduct for Authorised Insurance Representatives. This has been done in conjunction with industry - through two workshops and an update session in which trickier areas were discussed - and with the assistance of an external consultant who is an expert in this area.

We have tied the revised code more closely to the Principles of Conduct of Finance Business through reflecting our expectations of how the principles should apply to the Authorised Insurance Representative as an individual. The revision has been written using language that should be easily understood by a new employee and will serve as a minimum standard to be expected in the eyes of the Commission.

We would hope that licensees will find the revision helpful for both them and their Authorised Insurance Representatives, especially as we have added guidance notes within the code where we think this would be useful. We have also expanded the introduction and interpretation sections to provide a background for the Authorised Insurance Representative explaining how they and the code fit into the regulatory framework. Naturally this has the effect of making the revised code slightly longer than it was.

We should shortly be releasing a consultation paper for the revision and I will look forward to receiving your responses in due course. I would hope that, by having worked together on the revision, the revised code will be practical and pragmatic, working for you and your Authorised Insurance Representatives, as well as the Commission.

Talking about Authorised Insurance Representatives, an area where the Commission has reduced its mandatory requirements, following discussion with industry and the GTA University Centre, is through the withdrawal, earlier in the year, of the requirement for all Authorised Insurance Representatives who advise on long term insurance business to attain the Guernsey Insurance Certificate. Although this Guernsey-specific syllabus was helpful for new employees, the cost of refreshing the syllabus and its associated question bank was disproportionate to demand, with much of the syllabus being covered in other training locally available.

However, please remember that there is a continuing qualification requirement, at level 3, for those Authorised Insurance Representatives, who are not Financial Advisers, and who provide advice on long term pure protection insurance products, with the Board being responsible for employee training and an appropriate training and competency scheme.

Slide: Other supervisory work

Turning to our other supervisory work, we have carried out on-site visits and risk assessments at bank, insurance and insurance intermediary licensees in accordance with our risk-based framework. In this regard, during the year the Conduct Unit has become responsible for the supervision of a small number of medium high and medium low impact bank and insurance licensees where there is a local consumer nexus. We also continue to supervise low impact insurance licensees, through reactive supervision, as necessary. This has the advantage of increasing our exposure and expertise on the fair treatment of local customers by banks, insurers and insurance intermediaries.

The Conduct Unit continues to assist and support other areas within the Commission on conduct issues - including guidance and accompanying other supervisory teams on onsite visits - as conduct risk is one of the risks that is always assessed in a licensee's Full Risk Assessment. You may have heard, in the presentation on the work of the Rick Unit this morning, that risk mitigation programmes - one of the Commission's tools for addressing risks assessed as exceeding the Commission's risk appetite in that area - for conduct risk accounted for almost one-fifth of all such programmes in the last year. Consequently, when a significant conduct risk is identified on a licensee's Full Risk Assessment, a Conduct Unit representative will be asked to be part of the Risk Governance Panel that quality assures the work of the supervisory team.

Another way in which we assist our supervisory colleagues is through the Conduct Unit's regular contact with the Channel Islands Financial Ombudsman. The law establishing the Ombudsman sets out details of restricted information and when it is permitted to disclose such information. It requires the Commission and the Ombudsman to take such steps as are considered appropriate to co-operate with the other in the exercise of its functions. The Commission and the Ombudsman have entered into a Memorandum of Understanding which sets out the basis of the working relationship between the two bodies. For example, the Ombudsman informs us if particular licensees appear to generate a concerning number of complaints as this may indicate poor licensee conduct. The Conduct Unit acts as the conduit for the flow of this information and, as the Ombudsman builds up a greater bank of cases relating to Guernsey licensees, this will better inform the Commission's reactive supervisory work.

Slide: Working with others

Over the past year the Conduct Unit has continued to be, or become, involved in a number of policy initiatives, with the interest of consumers at heart. I shall touch briefly on these to give you an idea of some of the topics we have been progressing with others at the Commission and from elsewhere.

We have been working with colleagues in the Fiduciary and Innovations Supervisory and Policy Division on what is termed the Lending, Credit and Finance Project. This project is considering consumer credit legislation and the regulation of innovative financial services businesses. As it stands, many of these businesses are required to be registered with the Commission under the non–regulated financial services businesses law. Unfortunately, that law does not enable the Commission to adequately address the risks presented by some of the business models of firms either in, or looking to enter, this space. My colleagues in Fiduciary spoke in depth on the project this morning and, if you missed that presentation, I would suggest you have a look at it when this becomes available on our website. However at this time, I would like to thank all of you who responded to the recent Discussion Paper on the subject; your comments are greatly appreciated.

A new focus this year is in regard to the regulation of pensions; this is currently being explored by the Commission with the input of a working group comprising representatives from stakeholders across the public and private sectors, in particular members of both the Guernsey Association of Pension Providers and the Guernsey Association of Trustees. A discussion paper was issued towards the end of last month and is available on our website. The closing date for responses to this paper is Monday 12 December and, as this is a subject that I imagine will be relevant to all present, either in a licensee or personal capacity, I would encourage you to respond with your views on the proposals.
https://www.gfsc.gg/news/article/regulatory-framework-provision-pensions-products

We have continued to build our relationships with Guernsey Citizens Advice and Trading Standards to increase our understanding of the issues arising from financial services business that cause referral to them. An area of common concern is that of financial exclusion, including the problems being faced in the rehabilitation of prisoners through being unable to open bank accounts. As I have mentioned in the past, this isn't an area where the Commission can produce a solution itself but we are aware of the problem and working with others to take this forward.

We continue to consider and learn from developments, good and poor practice in other jurisdictions and have met with other regulators to discuss common concerns, at both a licensee and sector level.

Slide: Educational initiatives

I like to describe the role of the Conduct Unit as narrowing the gap between the provider of financial products and services and the consumer who acquires them. We are working with industry to ensure that consumers are treated fairly and that they are sold products and services from firms they can trust. We are also trying to improve the information that is readily available to consumers, either directly or through those that have a face to face relationship with them. This in turn should lead to consumers having increased knowledge, a better understanding and being more able to make an informed decision. Financial literacy and capability is key.

In July we held our annual intermediary seminar on the UK's Insurance Act 2015. In selecting this topic, we recognised that significant changes would be faced by the local insurance industry with the act's coming into force in August. We were therefore delighted that our two guest speakers had already delivered masterclasses on the act to UK insurance broking firms and published material on this subject.

Although the seminar principally addressed the implications for local insurance intermediaries and their clients, it also considered the implications for insurers. Whilst the majority of attendees were from Bailiwick insurance intermediary firms, some domestic insurers and insurance managers also attended the event. Again, we were delighted to have a full house for an extremely interactive day.

A key learning point from the seminar was the impact that this UK act will have locally as the majority of commercial insurance policies for local policyholders are written under UK law. Also, in time, UK precedents will be generated based on the Act and are likely to be considered by the courts locally, hence an understanding of these developments is timely for local licensees.

I would like to thank all who attended and especially those who provided comment – both helpful suggestions and constructive criticism. Although at the event, a few suggestions were made for future seminars, I would be grateful for other suggestions on topics we could cover next year, including whether you would prefer more frequent shorter seminars, for example, an introductory session on the revision of the Code of Conduct for Authorised Insurance Representatives for those individuals who will be subject to it.

On the day, I floated the idea of a seminar on vulnerable customers, including an experiential session, and received rather a mixed response, notably through this question not being answered on some feedback forms. We subsequently became aware and circulated seminar attendees to notify of a training session on vulnerability being held by the GTA University Centre. I understand that a number of firms took the opportunity to attend this session, or arrange firm-specific training. I would be interested in receiving comment on learning outcomes from anyone who attended the GTA training or has arranged their own.

As you can imagine the scope for a rogue Financial Adviser to exploit vulnerable customers can lead to significant detriment and we have seen examples of this in the past. We would expect licensees to consider whether their firm has sufficient measures in place to identify customers that could be considered vulnerable and have safeguards in this respect. Please bear in mind that vulnerability does not just effect the elderly – you don't need to be old to be vulnerable. As has been mentioned a couple of times already, please don't let your firm become the next case study.

We have continued to enhance and expand the consumer pages of our website and I am delighted that our new website is accessible for those using tablets and mobile phones. We are always looking for useful non-branded information to add to our website consumer pages and aim to keep the content up to date and relevant. I would welcome your assistance in this, through identifying subjects that, from a consumer's perspective, are relevant for inclusion. If you can think of a topic that we should address, please let me know.

In addition to consumer information, the Commission also publishes news items for licensees if it becomes aware of threats that could have an impact on them – such as cyber-attacks, phishing emails or email hacking – and would encourage licensees to share the occurrence of any such incidents with the Police and/or the Commission, as appropriate, so that the message can be disseminated to industry as a whole. Please do not be reticent in coming forward with the expectation that the Commission will hold this against you. We need to have a full appreciation and insight into the risks being faced by the finance sector as whole. By keeping quiet, much greater harm could arise. The more we can protect businesses in the Bailiwick, the more we protect and enhance Guernsey's reputation as a finance sector.

I would also like to share a new initiative with you. You may not be aware that the Industry Presentation this year has departed from the norm by including a session on the Finance Sector in Guernsey for sixth form students and their equivalents at the College of Further Education. This was held yesterday morning and was organised by the Conduct Unit with the assistance of GIBA as well as industry representatives from Barclays, Brooks MacDonald, Ravenscroft, PWC and Collas Crill. GIBA and Guernsey Finance also permitted us to use their videos whilst attendees were gathering. Speakers were those that have recently embarked on careers either with the Commission or in industry with the aim of maximising the benefit for the students. I would like to thank all who were involved and would hope that we can work closer with industry, the schools and the colleges to improve knowledge of the financial services sector.

Slide: Plans for 2017 and beyond

Finally, I will touch on the Conduct Unit's plans for 2017 and beyond. In view of the variety of subjects I have covered today, in order to be cohesive, I incorporated much of our future plans into the relevant topic.

In summary though, the Commission's supervisory framework assesses the risk of poor conduct and consumer outcomes and enables the Conduct Unit and other supervisors to focus on the areas where risk is unacceptable. These may also be demonstrated by poor corporate governance and poor culture. The Conduct Unit will continue to assess and address these areas with licensees through thematic and other supervisory work, engaging with industry to encourage appropriate ethics and culture.

In order to narrow the gap I referred to earlier, I am very keen that the Conduct Unit continues to further financial literacy initiatives with industry, other stakeholders, consumers and the community at large. However, being restrained by time and resource, we have to focus our effort in areas where we can have the greatest effect, working with others where we can.

As I have mentioned on previous occasions, we will listen to what you have to say. We will work with you to enhance the regulatory framework underpinning your business, to facilitate you being able to meet consumer expectations that the financial services and products they receive, from you, meet their needs and, that these financial services and products have been provided by financial advisers and firms they can trust. We are grateful to you and I look forward to your continued support in the future.

Thank you for listening.