Guernsey Financial Services Commission

Industry Seminar – 23 November 2017

Fiduciary Supervision Policy and Innovations Division Presentation

Gillian Browning, Director

Good morning everyone and welcome.

During the next 40 minutes Eamonn and I, on behalf of the Fiduciary Supervision Policy and Innovation Division, will seek to build on the Commission's 2017 Industry Presentation themes – Brexit, Innovation and International Standards.

The first of our Industry Presentation themes is Brexit.

Slide: Fiduciary Economic Landscape

Brexit, arguably, is the biggest single historical event to occur during our lifetime – and we have interpreted this theme in the context of the landscape within which we are all operating.

The detail of Brexit implementation remains unclear and contested, however we know that our local industry can be nimble in times of change and is well placed to capitalise on opportunities. Taking a step back, and looking at the economic landscape in which we operate more generally, we recognise and highlight a number of other notable events. In no particular order these include:

- The ever present headline grabbing media pressure and scrutiny of tax neutral jurisdictions;
- An emergence from a sustained period of low interest rates;
- The rebalancing of the Chinese economy;
- The impact of Climate Change;
- The continued tide of international reporting and associated reporting acronyms, whether that be LEI, FATCA, CRS, BEPS or beneficial ownership; plus
- The Increased sophistication of cyber crime and data breaches

We are part of the global economy and are not immune from the impact shocks from the economic landscape in which we operate. Our challenge is to mitigate where we can the risks that arise from this landscape and seek out opportunities where we can.

In keeping with the theme of a global economic landscape, we would like to take a moment to remember those who have been affected by extreme weather conditions in the last few months and in particular our industry colleagues and friends so desperately impacted by the effects of

Hurricane Irma.

Slide: Fiduciary Economic Landscape
Offshore centres can aid recovery in the Carribean

Whilst it will take a significant period of time for these Caribbean Islands to recover, we would like to bring a letter, which was published in the Financial Times in September to your attention. The letter, by John Aspden who is the Chairman of GIFCS, (and also one of our local Commissioners), succinctly highlights the role the finance industry plays in the affected Islands, their importance in supporting the recovery from the hurricane and in sustaining local communities.

Slide: Fiduciary Staff Employed

Turning to the role the fiduciary finance industry plays in our local community, the following slides are generated from analysis of the Annual Returns submitted as at 30 June 2017 together with your aggregated financial statements.

This slide shows the continued positive trend of the number of staff employed in the fiduciary sector with the total number up from 3526 in 2016 to 3703 in 2017 - an increase of just over 5% on the year.

Virtually 12% of the total local workforce (11.95% 3703/30977 SOG Mar 17) are employed by the fiduciary industry – this is a material figure and demonstrates the substance of work being undertaken in the Bailiwick.

Consider also the income tax contribution from our fiduciary sector, this substantially builds our local community, for example in paying for our Island's schools, roads and social infrastructure. Staffing and resourcing remains a key indicator for the sector and a topic which is discussed at all of our onsite visits. We are conscious of the significant compliance costs associated with running a regulated business in 2017 – and recognise that more staff doesn't necessarily equate to more income – however when we look at the recent enforcement referrals a key theme is that some of those firms have not always invested sufficiently in staff – instead they may have had higher than normal dividends.

Slide: Fiduciary Turnover and Appointments

This slide provides a sense check on key metrics for the sector.

As in previous years the number of trustee and director appointments continues to decline – which from our discussions with licensees is part of a proactive strategy to target fewer, yet more complex structures.

Turnover is taken from licensees financial statements, with reporting year end dates varying between firms. As compared to 31 October 2016 turnover is largely flat. Our comment, as in previous years, would be that the fiduciary sector remains stable in Guernsey – but not in a growth phase.

This is further supported by the number of fiduciary licensees.

We currently have 40 Personal Fiduciary Licensees (compared to 35 last year) and 147 Full Fiduciary Licensees (compared to 154 last year). Comparison of the number of licensees needs to be considered in context – there continues to be a trend towards continued consolidation but this does not automatically equate to less business being undertaken here – as is demonstrated by the value of assets under trusteeship rising again over the past 12 months.

Slide: Fiduciary Asset Distribution

This slide reflects data from the Fiduciary Annual return as at 30 June 2017. It is therefore a reflection of what you report to the Commission.

What assets are you holding for your clients? Broadly our data illustrates a picture of stability – with a minor movement away from Liquid and Near Liquid Assets reflected in a similar increase into Other Diverse Assets. The level of Real Estate Assets (reported as 9% in 2017, compared to 10% in 2016) appears light, but potentially this is due to asset valuation methods, or the property being held via a company.

Slide: Fiduciary Location of New Business

The figures above, again from the data you submit to us, show that 40.2% of new business comes from the UK (compared with 32% in 2016), 17.1% from Guernsey and Jersey and 13.1% from Europe.

To add a caveat to this data - this year it reflects each country from which 5% or more NEW business derives – based on the residence of the settlor of a trust, founder of a foundation or beneficial owner of a company – this is subtly changed from previous years returns (which requested data on 7 locations identified by the Commission).

And now for something a bit different.

Slide: Regulatory Self Assurance

Please take out your mobile phone, go to the internet browser and type in www.slido.com
I can reassure you that this exercise is entirely anonymous.

Type in the log in code #gfsc2017

Slide: What do you think the Impact of Brexit will be on your business? [Positive/negative/ neutral]

You have around 10 seconds to answer and then the question will be locked.

As you may be aware Thematic reviews are a key part of our supervisory approach – they help us understand trends and themes in industry and assess broadly the impact of a particular subject on local businesses.

Each year during our Industry Presentation we share with you possible thematic topics for the year ahead. We will come back to this later in presentation, but to act as a teaser we would like to know:

Slide: Which thematic topic would make you sweat in 2018?
Eamonn has been taking notes and will touch on this later in our presentation.

The thematic topics are chosen because they reflect key areas of regulatory concern or focus. We are keen for you to consider which broad risk areas concern you, for your business the most. Put another way at this time which regulatory risk has the greatest potential of keeping you awake at night?

Slide: Which Risk area causes you, in your business, most concern? [financial crime, governance, operational, conduct, strategy/business model and insurance risks]

William touched on the subject of regulatory self-assurance yesterday. In essence we intend to encourage self-assurance exercises, such as this one, as a complement to our formal supervision. By providing self-assurance help sheets or questionnaires as a routine part of our education session we hope to support those of you who already reflect on what we share, and more explicitly prompt others who may have a tendency to listen but not take the further step of considering what it may mean for your business.

Finally, looking towards the future, and potential innovation:

Slide: What impact do you think Blockchain will have for your business in the next 5 years [significant – none option]

Thank you for taking part.
Please could you now turn your phones off or put on silent.

Slide: Fiduciary and GFSC RMP Actions

We have been asked about the common risk areas in Industry, and this is something William touched on yesterday. One way of monitoring common risk areas is to analyse the Risk

Mitigation Programmes – RMPs – set by the Commission over the previous year.

This graph reflects the same risk categories contained within Slido questions and breaks them down into the total number of RMPs over the past year (1st October 2016 and 30th September 2017) – both overall across all financial services businesses and specifically for Fiduciary Licensees.

Put another way, Slido asked which risk area caused you, in your business most concern – compare your answer to this slide - the RMP actions we have issued over the past year. Which accords with you – where is different?

You will note:

The highest number of RMPs for the Fiduciary Sector remains in respect of Financial Crime Risk, the total number of created RMP actions was 108 (which was 46 for Fids vs. 62 for the other sectors).

For Governance Risk, the total number of RMPs was 85 (with Fids at 17 vs. 68 for the other sectors).

To give some colour to this - Weak Governance – is a perennial regulatory concern, and often the root cause of our enforcement referral cases. If you didn't catch Callum McVean's Enforcement presentation yesterday we recommend you to do so once it is available on our website. Specifically over the past year we have seen a continued trend of somewhat overly Dominant Individuals within a firm, and a failure of other Board Directors to provide an adequate check, balance and challenge.

Linked to poor Governance is poor Conflict of Interest management and control. We recognise that conflicts often occur – what is important is that they are adequately identified and managed. It is simply not OK, for example, for client investments to be used to further the Fiduciary Business's Shareholder's own commercial interests without being adequately disclosed.

For Operational Risk, the total number of RMPs was 77 (of which Fids = 28 vs. Rest = 49).

The continued trend for Mergers and Acquisitions brings with it both opportunities and risks. Our reflection is that some firms try to run before they can walk. A change of control brings with it real operational challenges for any firm and this should not be underestimated. The timescales associated with M+A activity need to be realistic and efforts to "short cut" the process, in our experience, can lead to further pain and significant remediation costs down the line.

[For Conduct Risk, the total number was 43 (Fids = 18 vs. Rest = 25).

For Strategy/Business Model Risk, the total number was 36 (of which Fids = 11 vs. Rest = 25).

For Insurance Risk, the total number was 3 and all of which were for fiduciary firms.]

To be clear RMPs – Risk Mitigation Programmes – are what they say on the tin – mitigation plans. They are what we, or a licensee, has identified a risk, and set in train a programme to reduce that risk.

Another way of interpreting common risk areas is to analyse the Triages logged by the Division. Overall, there were 408 triages recorded for the Fiduciary sector last year – on average this would be nearly 3 per firm.

Triages are typically matters connected to a firm which we might immediately be concerned with or may act as a flag to us for the future.

Slide: Fiduciary Regulatory Risks

This word picture highlights some of the most common triages from our experience over the past year. It includes:

FRR - Financial Resources Requirement – firms potentially failing to hold sufficient capital to ensure an orderly wind down of its business should it be necessary. To be clear we are not a zero failure regulator – we expect that some firms will fail or exit the market – and as a regulator we are focused on ensuring sufficient financial resources are held to enable this to be done in an orderly fashion;

Professional Indemnity Insurance – some firms not checking the detail of their policies and discovering, potentially too late, gaps in their cover. Or on occasion we also see an over reliance on a Group policy, with some firms not fully understanding the extent and limits and excess of the particular local cover;

Data Breach and Cyber Security – covered elsewhere in the presentation and on a regular basis in the media, particularly at the moment, both locally and internationally.

As a reminder we expect Directors to be able to continually demonstrate how they have assessed the cyber risks to their business and the ways that risk is monitored and controlled. You can consider specifically whether you should risk rate your data – for example review all the data you hold, attribute a value to the different types of data, and implement controls relative to the risk or sensitivity of the data.

We anticipate the hacks will continue, and it is more a matter of when rather than if. Therefore we recommend you spend time planning and preparing for a data breach and agree contingency plans in advance – these plans as ever should be regularly monitored and tested;

And as a reminder – if you are subject to a data breach you should notify us in a timely fashion.

Finally, we are conscious of the increased weight of International Reporting Requirements. We commend you, as Directors and leaders of Guernsey Industry, to continue to ensure sufficient resources are devoted to record keeping, including your recently introduced responsibilities to the Beneficial Ownership Register.

To conclude this slide. These are some of our current key risk observations – all of which need resources dedicated to managing them. But before we leave the topic can I leave you with 2 questions for you to ponder –

Firstly - How does this accord with your own assessment of your business risks right now?

And secondly - What controls have you put in place to reduce these risk areas in your business?

Now, I am handing over to Eamonn Finnerty.