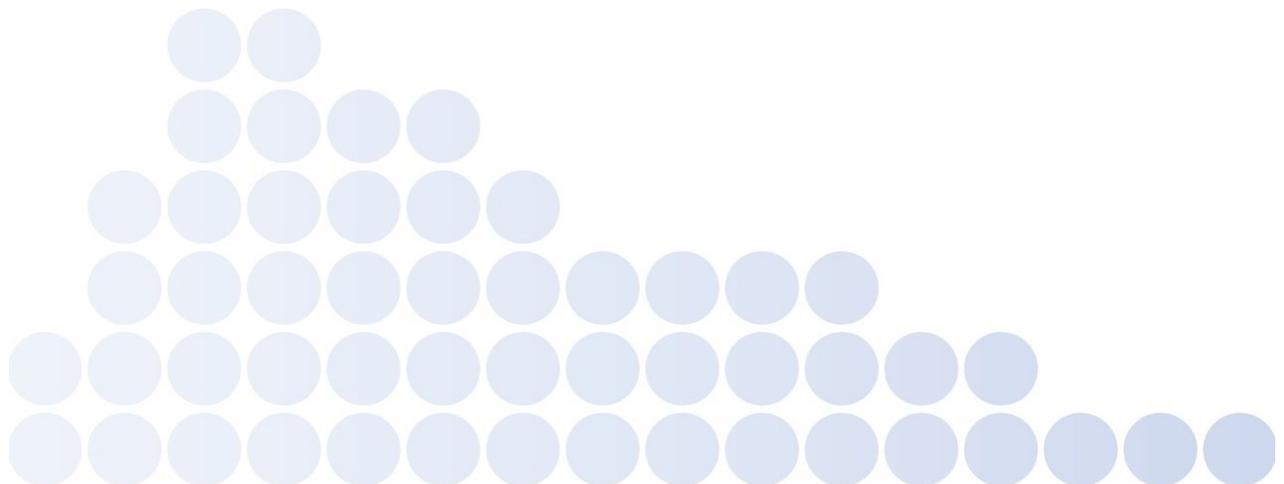




The Gibraltar Financial Services Commission

Supervisory Approach

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Introduction

In October 2014 we published our Strategic Plan and the steps we would be taking in order to deliver on such objectives.

We committed to deliver a more outcomes focused approach to supervision, supported by risk-based and transparent policies and processes; to take a proportionate approach to supervision, that allows us to focus on the bigger issues and higher risks across the financial services industry, specific sectors or within individual firms, and to be proactive in acting or intervening where appropriate earlier and decisively.

This document sets out our Risk Based Approach to Supervision that supports the delivery of our Strategic Objectives.

Our Approach

Key Principles

The driving principles that underpin our Risk Based Approach to Supervision are:

1. The level and type of supervision will be appropriate to the impact and likelihood of a firm failing, the reputation of the jurisdiction being negatively impacted or consumers experiencing significant detriment.
2. The level and type of supervision a firm receives will be reviewed by a panel of senior GFSC staff, as a minimum, every 12 months or at such time when a new or emerging material risk is identified, or the nature and scale of the firm's business changes.
3. A proportionate and tailored supervisory engagement plan will be developed for each licensee.

Assessing risks to our objectives

We use a variety of information and data sources to inform our Risk Based Approach to Supervision including information from returns completed by firms, complaints data, market intelligence, economic analysis, and outputs and insight from discussions with a wide range of stakeholders, including consumers and other regulators.

Individual firms are initially measured against criteria reflective of their industry to determine their potential impact on the stability of the financial system and on consumers should they fail. This initial assessment is based on the size of the licensee. Changes to how the firm measures against the different criteria will be tracked on an ongoing basis using the returns submitted by firms.

Firms are then assessed against a set of risk categories. The size of the firm will determine the minimum level of assessment.

To determine the overall risk score assigned to a risk category the following will be considered:

- The consequence should the risk materialise (Impact), and;
- The probability of the risk occurring, including a consideration of the frequency with which this may arise (Likelihood).

When assessing the impact and likelihood of a risk materialising, consideration will be given to the adequacy and effectiveness of the controls the firm has in place to manage the risk.

For licensees that are part of a wider group, or if there is a licensed individual linked to an entity or group, the assessments will be carried out simultaneously to identify any common or linked risks.

Areas of focus

When assessing risk in firms, the type of firm will drive the areas that we will focus on. The areas of focus have been set out below.

Governance and Controls – An assessment is made of the adequacy of the oversight and control mechanisms in place to help ensure a firm is soundly and prudently managed. The assessment will focus on the processes, structures, information flows and decision making processes enabling the board and senior management of the firm to satisfy themselves that authority is exercised in line with delegated levels to protect all stakeholders.

The GFSC seeks comfort that the individuals who manage a business are fit and proper. Attention is paid to a firm's board composition to ensure it is well-balanced in terms of skills and experience relevant to the activity of the company. Consideration is also given to the ability of individuals to be able to act independently.

Risk Culture and Controls - The embedding of an effective and proportionate risk and control culture remains a significant focus. We expect firms to have processes and systems that allow them to identify, measure, monitor and manage all types of risk in an appropriate and timely manner. We will seek evidence that a firm's culture promotes good risk management and ethical behaviours.

Business Model Analysis - The GFSC assesses the viability and sustainability of a firm's business plan. Business and strategic risks are assessed to determine the viability of the firm's current business model on the basis of its ability to generate acceptable returns and the sustainability of the firm's strategy over a forward-looking period. For groups and linked licensees the analysis looks at the holistic position to take account of the risk of contagion.

Prudential Risk - This analysis focuses on the financial standing of the firm to ensure that it has appropriate financial resources (adequate capital and sufficient liquidity). Consideration is given to how firms manage risks that can impact on their financial resources . This includes credit, legal, market and operational risks.

Conduct of Business – This focuses on a firm’s interaction with its customers. Ultimately we will seek assurance that firms conduct themselves in a manner that places consumer interests and market integrity at the heart of their operations.

Financial Crime Systems and Controls - Risks can arise from action not being taken to prevent money laundering, terrorist financing, fraud, tax evasion, corruption or bribery. Firms that fail to place adequate emphasis on implementing necessary systems and controls are more vulnerable and therefore put at risk the reputation of Gibraltar.

As part of our supervisory process we will consider the firm’s inherent risk exposure to financial crime and ensure that appropriate and proportionate safeguards are implemented.

Supervisory Engagement with Licensees

The outcome of the assessment will determine the type of engagement that the GFSC will have with the licensee. A supervisory engagement plan will be agreed every 12 months by GFSC senior management.

All licensees will receive a baseline level of desk based supervision via the review of supervisory returns and audited financial statements. Further targeted engagement might be scheduled in order to address any risks identified which the GFSC deems unacceptable. The type and frequency of the engagement (the engagement will always be directly with the licensee), will be driven by the risk but can include meetings with the board or any other staff member, a focused on-site visit or simply a request for further information.

By adopting a more targeted supervisory engagement plan which leverages on the knowledge, experience and skills of our supervisors, we will be able to make better use of our resources and offer more support to the firms that pose a higher risk.

Risk Events

A Risk Event is an unplanned occurrence which, through the lack of or failure of a control, has resulted in or could have resulted in a financial or non-financial impact. A Risk Event may also be considered an accident or near miss, or a newly identified material risk which has crystallised.

When a Risk Event is identified and reported promptly, remedial action can be agreed in a timely manner. We expect licensees to be forthcoming and transparent and report any Risk Events to us as soon as they become aware of them.

Our response to a Risk Event will depend on the nature and materiality of the event. Where necessary, our supervisory engagement plan will be revised to manage the risk in a timely manner.

Thematic Reviews

When we identify common risks across various firms or even across various industries we will carry out thematic reviews. This will allow us to carry out peer to peer analysis, identify common issues, provide for better route cause analysis and identify good and bad market practices.

We will publish the results of our thematic work and will provide industry wide feedback setting out our expectations and recommendations in order to raise industry standards. Individual feedback to licensees may also be provided where necessary.

In much the same way as our approach to assessing risks at individual firm level, our thematic reviews will be carried out in a pragmatic and proportionate manner with a clear focus on the most material risks.

What can firms expect from us?

As part of the Risk Based Approach to Supervision, licensees can expect the GFSC to be:

- Clear and transparent in our communications.
- Focused on the most material risks to our objectives with targeted engagement to help mitigate any risks deemed unacceptable.
- Professional in providing expert support and pragmatic in our approach to supervision.

What do we expect from you?

In order to be able to effectively deliver our commitments as part of the Risk Based Approach to Supervision, we expect all licensees to:

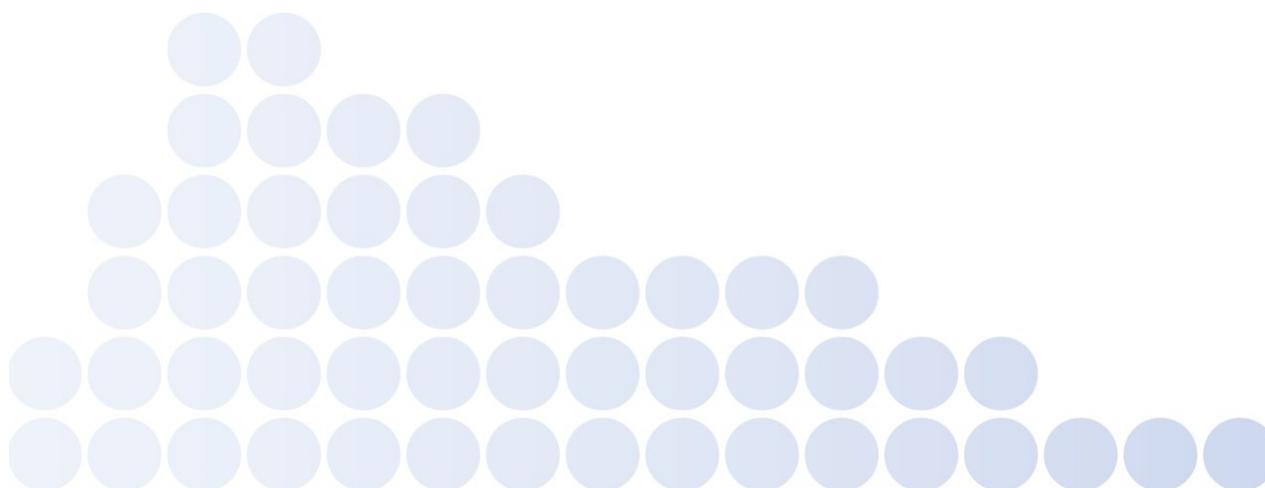
- Provide us with accurate information in a timely manner. We rely on the information you provide in order to make our assessment.
- Be able to demonstrate what you say you are doing. For example, from time to time we will want you to evidence that risks are being mitigated, controls are in place, the board has appropriate oversight of the business, etc.
- Be forthcoming with your information and keep us updated on any changes and developments to your business, and any new opportunities being pursued including how any associated risks are being managed.
- Run your business in a diligent and ethical manner giving consideration to the impact you might have on your customers and the reputation of Gibraltar.

Key Messages

Our Risk Based Approach to Supervision ensures that resources are focused on managing the most material areas of risk in a consistent manner. The approach will ensure that firms which pose the biggest risk to the financial stability of the jurisdiction, its reputation, or to consumers, receive an appropriate level of regulatory support, guidance and supervision.

Underpinning this are three key messages:

- The approach is designed to identify the most material risks to **our** objectives.
- It recognises that different sectors and firms that we regulate pose different risks and our approach can therefore be tailored to each individual licensee with greater reliance on judgement.
- The approach is designed to be proportionate and pragmatic and this will be evident in our targeted supervisory engagement with licensees.



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Gibraltar Financial Services Commission
PO Box 940
Suite 3, Ground Floor
Atlantic Suites
Europort Avenue
Gibraltar
www.fsc.gi
info@fsc.gi

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