

Guernsey legal and regulatory update

An overview of Guernsey legislative and regulatory developments
April to 30 June 2019 inclusive

1 Substance requirements – joint guidance notes

There have been further developments in the sphere of economic substance, firstly with the publication of the much anticipated guidance notes which were issued by the Director of Revenue Service jointly with the tax authorities of Jersey and Isle of Man on 26 April 2019 (the **JGNs**).

The JGNs add to the existing guidance contained in the Key Aspects Document (**KAD**) issued in November 2018 and, while they are at a high level (as they are designed to apply across all three Crown Dependencies of Guernsey, Jersey and Isle of Man (the **CDs**)), provide further detail on the scope and application of the economic substance legislation (the **Substance Regulations**), including further detail on a number of elements of the 'directed and managed' test; clarification in determining how a 'relevant activity' needs to be undertaken by relevant companies; outsourcing; and employees.

In preparing the JGNs, there has been particular attention on fund management activities, being one of the areas that the EU's Code of Conduct Group on Business Taxation and the OECD have focused on, from a policy perspective, in framing economic substance requirements.

While funds (corporate or other structures) regulated by the Guernsey Financial Services Commission (the **Commission**) under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (the **POI Law**) will continue to be out of scope, Guernsey tax resident corporate managers to funds (including corporate general partners to fund partnerships) will be in scope of the Substance Regulations, irrespective of whether the fund is regulated and whether the fund is established in Guernsey or elsewhere.

In practice, it is anticipated that the additional operational requirements of the Substance Regulations will sit naturally with the regulatory regimes and governance procedures that Guernsey managers are already subject to. For more information on the application and impact of the Substance Regulations on Guernsey tax resident fund management companies specifically, refer to our legal update, [Further clarity on economic substances issues for Channel Islands Fund Managers](#).

Service providers to funds such as administrators, custodians and advisors are also out of scope, although advisory services, where provided in Guernsey to a connected entity non-resident in the Island, may fall within the relevant activity of 'distribution and service centre activities'.

The JGNs as currently released are stated to be subject to further review and development over time, and this approach should provide helpful flexibility to allow companies to adapt to the Substance Regulations.

We have a webpage dedicated to economic substance ([here](#)) which, as well as providing a high level overview, houses all of our economic substance related legal publications, including those for BVI, Cayman Islands and Jersey. From a Guernsey perspective, we have most recently published a legal update, [More detailed guidance issued on Economic Substance for Channel Island Companies](#), giving an overview of the JGNs. We have also updated our original legal guide on [Guernsey's economic substance requirements](#) to reflect the latest detail provided by the JGNs.

2 Substance requirements – proposed amendments

The other development this quarter is the proposal to further amend the Substance Regulations next month. The headline changes are:

- **Exempt companies:** companies that have tax exempt status under the Income Tax (Exempt Bodies) (Guernsey) Ordinance, 1989 but which are not regulated funds under the POI Law will be brought within scope of the economic substance requirements, eg fund subsidiary companies and other non-fund tax exempt companies.
- **IP assets:** clarification that the core income generating activities (**CIGA**) for companies with income from IP assets should be linked to the nature of the IP asset, eg the CIGA for patents are based on the research and development activities; the CIGA for non-trade intangible assets such as brand, trademark and customer data are based on the marketing, branding and distribution activities.
- **Pure equity holding companies:** non-Guernsey and non-Alderney companies which are pure equity holding companies but tax resident in Guernsey will be required to comply with the companies law of their respective jurisdiction of incorporation.

Companies which are in scope should start making preparations now or early in their next accounting period commencing on or after 1 January 2019 to ensure that they can satisfy the economic substance requirements during that, and subsequent, accounting periods.

3 Beneficial Ownership Register

Guernsey, Jersey and Isle of Man have jointly announced commitments, in line with developing European Union (EU) standards, in relation to public registers of beneficial ownership of companies ([here](#)).

Transparency in the beneficial ownership of companies has, for some time, been an evolving area internationally, as exemplified in the EU with the passing of the Fifth Anti-Money Laundering Directive (the **EU Directive**) in 2018. Recognising this evolution, the CDs have chosen to announce the following commitments:

- working collaboratively with the EU in 2021 on the interconnection of their existing registers of beneficial ownership of companies with those in the EU for access by law enforcement authorities and financial intelligence units;
- following this interconnection and, in any event, before the end of 2022, permitting access to such registers for certain financial services and other businesses to enable them to undertake due diligence on companies with which they wish to do business; and
- bringing forward legislative proposals to establish public access to beneficial ownership data of companies in line with the principles of the EU Directive, within 12 months of the publication of the EU's planned review of the EU Directive (publication of that review being due in January 2022).

These commitments are the CDs' response to the developing international environment in relation to transparency and reflect their own approach in this area. Immediate changes to the laws of the CDs are not envisaged. Instead these commitments adopt a stepped approach over the next three to four years enabling Guernsey to review global developments in respect of public registers, particularly in respect of registers of beneficial ownership of legal entities. According to the States of Guernsey's Action Plan 2019 ([here](#)), Guernsey's approach is 'timed both to enable us to consider the EU's Implementation Review report and to keep pace with global developments'.

4 Beneficial ownership – Commission's thematic review

The Commission has issued a report ([here](#)) following its thematic review of beneficial ownership which was undertaken during the latter part of 2018. The aim of the review was to assess the actions taken by the fiduciary sector to implement the requirements of the beneficial ownership legislation (which came into force in 2017). The review encompassed all 190 Guernsey and Alderney fiduciary licensees (full and personal), gathering information on 12,033 legal persons and examining beneficial ownership records of almost 400 legal persons.

The Commission's objectives were:

- to assess how effective Guernsey and Alderney licensees have been in understanding and identifying the beneficial owners of legal persons for whom they act as resident agent and for whom they must submit the correct information to the Guernsey and Alderney Registries; and

- to analyse the effectiveness of the systems and controls implemented by licensees to meet their ongoing obligations under the beneficial ownership legislation.

The results of the review are positive, reflecting a strong framework in the Bailiwick for Anti-Money Laundering and Combating the Financing of Terrorism (**AML/CFT**). These findings, which will be of interest to firms in other sectors of the finance industry who are under identical obligations within the AML/CFT regulations to identify and verify beneficial owners of their customers, follow on from the endorsement of the effectiveness of Guernsey's AML/CFT framework by MONEYVAL in its report of the evaluation of Guernsey (January 2016) and by the OECD Global Forum (2018).

5 AML/CFT Handbook

The latest version of the Handbook on Countering Financial Crime and Terrorist Financing (the **Handbook**) is effective 13 June 2019 following approval of a further round of amendments, the most notable being to:

- introduce a start date of 31 March 2019 for domestic politically exposed persons (**PEPs**), so that the provisions for identifying a domestic PEP and considering the implication of them having held political office as part of a relationship risk assessment do not apply if the individual concerned ceased to hold a prominent public function in the Bailiwick before 31 March 2019;
- revise the definition of Money Laundering Compliance Officer (**MLCO**) to clarify that the role of the MLCO is to 'monitor' a specified business's compliance with its policies, procedures and controls; and
- revise the definition of the role of Money Laundering Reporting Officer to include 'make' as well as 'receive' disclosures of suspicious activities or transactions (which aligns with the terminology used in the legislation).

The current version of the Handbook applicable to **all** financial services businesses **and** prescribed businesses (noting that the Handbook for Financial Services Businesses (2007) and the Handbook for Prescribed Businesses (2008) have both been repealed) is available on the Commission's website ([here](#)).

6 Commission's annual report 2018

The Commission has published its 2018 annual report ([here](#)) which includes a new section setting out the Commission's three year business plan to the end of 2021. One of its plans over the next three years is to invest in data-driven technology, involving consideration and implementation of enhanced information systems designed to allow it to better and more effectively regulate firms.

Looking back at 2018, it appears to have been a buoyant year for Guernsey in terms of new financial services business, with a particular uplift in the investment sector in the latter part of the year. While the majority of the business coming to the island was repeat business, there was a good flow of new business, including some business relocating from other jurisdictions. It is thought that product innovations such as Insurance Linked Securities, Private Investment Funds (particularly after the refinements made in March 2018) and the Guernsey Green Fund have all contributed favourably.

Looking forward to this year and next, the new regulatory laws, which are an upgrade to the current legislation to meet the standards of the Basel Committee, the International Association of Insurance Supervisors and the International Organisation of Securities Commissions, are expected to go before the States during Autumn 2019 followed by Privy Council by the end of the year.

A similar timeline applies in respect of the new lending, credit and finance law which is expected to provide enhanced consumer protection for vulnerable borrowers, an ability to provide assurance about the standing of electronic due diligence providers to the financial services sector and a regulatory regime well-adjusted to the needs of innovative FinTech businesses which do not always fit well into the existing framework of the regulatory laws.

7 Quarter 1 (2019) Regulatory Statistics

The net asset value of total funds under management and administration has decreased for the quarter ended 31 March 2019 by 0.5 per cent: Guernsey domiciled open-ended funds having remained unchanged, the closed-ended sector having decreased by 1.2 per cent and non-Guernsey schemes having increased by 1.4 per cent.

The full statistics and related analysis are available [here](#).

8 The Commission's enforcement powers

The Guernsey Court of Appeal has struck down the Royal Court's decision in *Y v Chairman of the Guernsey Financial Services Commission and HM Procureur* that prohibitions imposed by the Commission which were time-limited, and disapplication of the exemption to allow six directorships (the **Exemption**) went beyond its scope of legal powers.

The case concerned the Commission's decision to impose a four year prohibition order and a four year disapplication of the Exemption (in addition to a financial penalty) under the regulatory laws. It was argued that there is no statutory framework permitting the Commission to make anything other than a prohibition order of unlimited duration and that, as such, both orders (which were time-limited) were made without jurisdiction - an argument which has never before been deployed in Guernsey.

While the Royal Court acknowledged that the intention of the relevant legislation at the drafting stage appears to have been to 'suspend or bar' persons who were not found to be fit and proper, it found that there was no express reference to prohibition orders being made for a specified time in the enacted legislation, ie the original intention at the policy stage had not been carried across in the drafting of the legislation. On that basis, the Royal Court remitted the case back to the Commission to reconsider the prohibition orders and whether it would be appropriate to give any indication as to when an application to revoke the prohibition orders could be made.

The Commission appealed, and was successful. The Court of Appeal confirmed that the Commission had in fact correctly interpreted the scope of its legal powers and, as such the Commission may continue to adapt prohibition orders and disapplication of the six directorships exemption to the individual circumstances of each case, making orders that are reasonable and proportionate in all the circumstances.

To read more, click [here](#).

9 Listings - TISE announce new service delivery framework

The International Stock Exchange (**TISE**) has introduced a new service delivery framework for listing applications bringing it into line with its main competitors. Under this new framework, TISE aims to release its initial comments letter on initial applications within three business days of submission (subject to receipt of the initial application documents in accordance with the Listing Rules and payment of the application fee) and respond within two business days for each subsequent review (including submission of the final application).

10 Commission Industry presentations

Videos, slides and speeches from the Commission's industry presentations on 4 April 2019 are available on its website ([here](#)). Topics covered include BREXIT, current themes arising from supervision, authorisations and innovation and consumer protection.

11 Data Protection

It is twelve months since the introduction of Guernsey's equivalent of the EU's General Data Protection Regulations (**GDPR**), 25 May 2019 marking the first anniversary of the Data Protection (Bailiwick of Guernsey) Law, 2017 (the **DP Law**) and also the end of the transitional relief, ie the grace period permitted for certain aspects of the DP Law which did not come immediately into force.

Entities registered on the list of the Office of Data Protection (**ODPA**) should be aware of the following recent changes to the registration process from 13 May 2019:

- the ODPAs will be collecting less information as part of the registration process. Registered entities are now responsible for maintaining their own publicly-available record of all information previously set out in their data protection registration. It is the registered entity's responsibility to ensure its privacy statement is kept up-to-date and that it includes all requisite information;
- the public search function of the ODPAs register has been removed and it is now only possible to renew or amend a registered entity's registration; and
- a change in terminology, ie use of the term 'registration' instead of 'notification'.

The European Commission (**EC**) has begun the process of reassessing the Bailiwick's 'adequacy' as a non-EU country in relation to how well it meets the standards of data protection laid out in the GDPR. The

ODPA has submitted a report to the States of Guernsey which formed part of the detailed adequacy report compiled and submitted to the EC in May.

Other news, the ODPa has confirmed that 40 personal data breaches were reported in the two months to 22 April 2019, with almost all occurring due to human error, indicating that human error poses the greatest risk to organisations' safe handling of personal data. Whilst the majority of breaches were of a low-level with no further action required, the ODPa has an ongoing caseload and a number will be subject to further investigation.

12 Channel Islands Financial Ombudsman

The Channel Islands Financial Ombudsman (CIFO) has succeeded in defending its first legal challenge since inception. The dispute concerned a complaint made against a Jersey-based mortgage broker which had arranged a mortgage loan for the complainants from a private lender. CIFO directed that the mortgage broker compensate the complainants for losses totalling £60,000 on the basis that the mortgage loan it had arranged from a private lender was unsuitable, ie it was much more costly than what should have been available from a conventional mortgage lender. CIFO also applied a rate of 8 per cent per annum to certain aspects of the compensation award to compensate for deprivation of funds to date.

The mortgage broker challenged CIFO's decision on the basis of illegality (ie its mortgage brokerage business did not fall within CIFO's jurisdiction as it was not a 'relevant ancillary business') and irrationality (ie CIFO failed to take into account relevant considerations and took into account a number of irrelevant considerations). The Court rejected both grounds.

This is the first judicial review of a determination made by CIFO under Jersey's equivalent legislation. Points of general interest concern the 8 per cent per annum interest rate applied by CIFO, which was upheld; the Court's remarks concerning procedure before CIFO, which is intended, as it was in this case, to be informal; and the anonymity which was granted in favour of the underlying complainants.

13 Recent enforcement cases

This quarter has seen the Commission impose prohibition orders and/or financial penalties on local licensees and individuals. To read more, click [here](#).

The first concerns the imposition of financial penalties on a local POI licensee (the **POI Licensee**), a principal manager of a protected cell fund and investment manager of the two cells of a PCC fund. It also acted as investment manager to approximately 1,300 alternative investment funds (**AIFs**) based in the UK and provided investment advisory services to a small number of trust clients. A financial penalty and prohibition order was also made against its director, managing director and controller (each role fulfilled by the same individual).

The Commission's investigation focussed on the POI Licensee's record keeping, compliance with reporting obligations, provision of investment advice to a Guernsey trust company and its provision of investment management services to collective investment schemes, including the PCC fund, its two cells and the AIFs. The Commission also considered the individual's role as managing director and the only constant director during the period 2013 to date, in relation to issues identified within the POI Licensee and whether he ensured that its board met its regulatory requirements.

The other, more recent, enforcement case concerns a local fiduciary licensee (the **Fid Licensee**) found to have serious failings in respect of its own, and its directors', compliance with applicable AML/CFT legislation.

In view of the Fid Licensee's failure to ensure compliance with the Criminal Justice (Proceeds of Crime) (Financial Services Businesses) (Bailiwick of Guernsey) Regulations, 2007, the Handbook, the Corporate Service Providers Code of Practice, Instruction 6 of 2009 and the minimum criteria for licensing set out in Schedule 1 of the Fiduciaries Law, the Commission imposed a financial penalty on each of the Fid Licensee and its individual directors.

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