

FINANCIAL SERVICES COMMISSION

Media Luncheon

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An Overview of Recent Regulatory Initiatives at the Financial Services Commission

INTRODUCTION

Good day, ladies and gentlemen. First of all, let me join the Chairman in thanking you for the interest you have shown by your presence here today. It is, hopefully, the first of many such events geared specifically towards providing us with an opportunity to inform you about some of the work being done by the Financial Services Commission (“FSC”) in protecting the customers of regulated financial entities.

THE FSC IS A GROWING BUT STABLE INSTITUTION

My first message to you today is that the FSC, while still a relatively young organization, is increasingly well-equipped to pursue its mandate. We have progressively grown the staff complement which now stands at 113 compared with 58 at the end of its first financial year (2002 March 31). The FSC has very quickly become a self-financed entity where over 95 percent of inflows are obtained from fees levied on regulated entities. The balance has mainly been sourced from donor grants for regulatory projects. The fee structure is based on

the principle of cost recovery, which is that fees charged to regulated sectors should normally reflect the costs of regulating each sector. The fee schedule is periodically reviewed to ensure that this principle is observed. A statement of the fee policy is provided on the FSC's website.

The fee policy has been highly successful in ensuring adequate funding for the FSC's operations. However, it will have been noted that in the 2005/06 and 2006/07 financial years, the FSC recorded losses that were financed out of reserves. As I believe is now well known, this was a predictable and, indeed, predicted result of the FSC incurring the developmental costs for the pensions regulatory regime (in FY 2005/06, for example, it amounted to \$77 million). Obviously, the FSC could not apply the cost recovery principle to the industry before it was authorised to do so by Parliament in accordance with the law.

Apart from one-time application fees, regulatory fees for the pensions industry are not paid by pension funds. Licensed investment managers and administrators will represent the principal focus of the FSC's regulatory attention since they represent the main location of the activities that are regulated in the new regime. It is they who make profits by providing their services to the industry and it is they who pay the regulatory fees in the form of an annual licensing fee. During the fourth quarter of the financial year that just ended, the FSC completed its review of all properly completed applications for licensing of investment managers and administrators. This process included establishing the fit and proper status of 389 individuals who are directors, managers or significant shareholders of the applicant companies. Twenty-one investment manager applications and 21 administrator applications were approved by the FSC, accounting between them for \$119 billion or 87 percent of total pension fund assets. Licensing fees paid during the same financial year by the new

licensees amounted to \$119 million, thus establishing full cost recovery for the pensions industry.

RECENT REGULATORY INITIATIVES

Selected Comparative Data on FSC-Regulated Sectors

It would be useful to understand how the sectors that the FSC regulates fit into the overall financial system in order to appreciate the importance of the FSC's regulatory activities. In terms of the size of balance sheets, at the end of 2006 the insurance and securities sectors together held \$523 billion in assets compared with \$629 billion for banks, building societies and credit unions combined (see Table 1). Taken together, the insurance and securities sectors (which include the investment managers for pension funds) account for a sizeable share of the invested financial wealth of the country.

Insurance Regulation

During the past year, insurance regulation has continued to focus on improving the solvency ratios of regulated entities through a strengthening of prudential standards and improved monitoring of corporate governance. In particular, capital standards for both life and general insurance companies were increased and the FSC began the introduction of a new capital regime for general insurers which is intended to better align capital provisions with insurance risks. The implementation of the new framework, referred to as the Minimum Capital Test ("MCT"), is expected to be completed in the current financial year. One of its important features is the improved provisioning that will be required for catastrophe risks.

At the end of 2006, the capital base of general insurers had increased by 44

percent compared to the level two years earlier with the ratio of capital to total assets improving by 9.5 percentage points (see Table 2). Life insurers, for their part, registered a 39 percent increase in their capital levels over the two years, with the capital ratio remaining broadly unchanged at just over 24 percent.

The FSC has also focused on improving the quality of the general insurance companies' reinsurance programmes as well as the capacity of the regulator to monitor and assess them. During the last financial year, reinsurance reviews were done for all general insurance companies and recommendations made for the strengthening of the reinsurance programmes of some companies. This is an ongoing activity. The mitigation of all risks, in particular, catastrophe risks, require strong capital together with appropriate reinsurance programmes. The FSC considers that these are extremely important considerations in promoting a healthy insurance sector, especially in an economy that is exposed to weather-related shocks.

Securities Regulation

Securities regulation has continued to focus on monitoring the solvency and market conduct of licensed entities through a programme of routine and special examinations and stock market surveillance. Findings from these examinations sometimes identify areas of potential risk exposure and when these deficiencies are identified the licensee is required to put in place effective corrective measures. Whilst it would not be possible to display here a wide range of indicators, the growth in the capital base of securities dealers is indicative of the improving financial health of this sector. At the end of 2006 the capital base had increased by 62.7 percent compared to the level two years earlier with the ratio of capital to total assets improving by 1.9 percentage points (see Table 3).

Amongst the FSC's other priorities has been a recently completed project to review and strengthen the framework for issuer registration and prospectus disclosure. Draft regulatory provisions have been prepared and circulated for industry comment. Public workshops have been held to facilitate wide public involvement in the process and the documents are available on the FSC's website. One feature of the new prospectus regulations which I am sure will be of interest to you is the proposal to establish a category of "accredited investor" covering sophisticated or wealthy investors to whom investment products can be sold which do not meet the more stringent issuer registration requirements. Under the accredited investor concept, investment products can be more flexibly tailored to meet the needs of a more select clientele with the capacity to obtain their own highly skilled professional advice and with sufficient surplus wealth to be able to sustain the loss of their investment. This concept was initially introduced to the local market by the FSC in November 2004 in a consultation paper entitled *The Concept of "Qualified Investor" and its Importance to Jamaica's Capital Markets* which also can be found on the FSC's website.

Another activity of interest in the area of securities regulation has been the FSC's programme of investigation and enforcement. It is well known that the FSC has been seeking to enforce the requirements of the Securities Act in relation to entities that are perceived to be conducting securities business without a license or issuing unregistered securities to the public. The FSC maintains a vigorous interest in detecting and investigating these operations as they arise. I take this opportunity to reiterate that the FSC's interest in the activities of unregulated schemes arises from its statutory obligation to ensure that the law designed for the protection of investors is observed. In accordance with the Securities Act, entities that conduct or that propose to conduct securities business or offer investment advice to the public are required to be licensed and issuers of

securities are obliged to apply to have their securities registered by the FSC before they are issued. The licensing and registration process gives the FSC the authority to monitor promoters of investment schemes to see that they meet their statutory obligation to make full disclosures to investors so that they can make informed decisions before investing. There are fundamental principles of fairness and equity that are at stake here.

Pensions Regulation

Supervision of the pensions sector begins with a first step, which is the licensing of administrators and investment managers. The second step is the registration of pension plans and trustees. The steps began in the third quarter of 2006/07 and are projected to be completed over a period of three years. Recent news stories have suggested that there may be a concern in some quarters about the pace of the FSC's licensing and registration effort. The following statistics (as at 2007 May 15) may be helpful in shedding more light on the debate:

- 520 applications for registration have been submitted by superannuation funds and retirement schemes. Only 45 (9%) were properly completed (that is, contained all the information required to be provided by law), mainly because most superannuation funds have not yet submitted constitutive documents (Trust Deeds and Plan Rules) updated to bring them into compliance with the Act and Regulations. The FSC's review of the 45 plans is progressing in a timely fashion having regard to the technical nature and fundamental importance of this aspect of our work. The other plans have been allowed sufficient time to upgrade their constitutive documents in an orderly fashion and the FSC expects to receive most of them within the next few months. We will continue to work closely with trustees and their professional advisors to bring their constitutive documents into compliance.

- 1,628 applications for registration of trustees have been received. Only 749 (46%) were properly completed applications. To date, fit and proper assessments have been completed for 316 trustees, representing 42% of properly completed applications. The FSC expects to have completed its review of all properly completed applications within the first year (ie, by 2007 September 30).
- As indicated earlier, all properly completed applications for investment managers and administrators' licenses have been approved. These entities represent 87% by value of pensions industry assets. Table 4 provides details on the approval status.

CONCLUSION

In conclusion, the information that I have shared with you today suggests that there has been significant progress in strengthening the regulatory framework for the insurance, securities and pensions industries. To be sure, more needs to be done and the FSC will continue to direct its efforts to improving the safety and integrity of the industries that it regulates. In closing, though, I would like to say some words to investors in particular. Notwithstanding the value to investors of the efforts of a vigilant regulator, it will always remain true that by far the best way for investors to protect the monies they put into financial instruments is to do research and ask questions. In order to facilitate this, it is incumbent on promoters of investments to disclose meaningful financial and other pertinent information to the public. Only through the steady flow of timely, comprehensive and accurate information can people make sound financial decisions. Investors can contact the FSC regarding any investments or market participant to ascertain their registration or licensing status. It is never wise, and always dangerous, to make any investment without being armed with

at least this minimum knowledge. To investors, we say, “think and check before you invest.”

Thank you.

Brian Wynter
Executive Director
Financial Services Commission

Table 1: Total Assets by Type of Financial Institutions, 2004- 2006

| Types of Financial Institution | 2004 | | 2005 | | 2006 | |
|--|-----------------------------------|------------------------------|-----------------------------------|------------------------------|-----------------------------------|------------------------------|
| | Balance Sheet Assets (\$ Million) | % of Financial System Assets | Balance Sheet Assets (\$ Million) | % of Financial System Assets | Balance Sheet Assets (\$ Million) | % of Financial System Assets |
| FSC -Regulated Institutions: | | | | | | |
| Life Insurance | 67,873.4 | 7.4 | 78,335.9 | 7.9 | 94,718.6 | 8.2 |
| General Insurance | 40,359.7 | 4.4 | 33,558.1 | 3.4 | 35,168.2 | 3.1 |
| Securities | 300,071.0 | 32.7 | 342,672.0 | 34.4 | 393,210.0 | 34.1 |
| Sub-Total | 408,304.0 | 44.4 | 454,566.0 | 45.6 | 523,096.9 | 45.4 |
| Deposit-Taking Institutions: ¹ | 510,305.96 | 55.6 | 542,797.85 | 54.4 | 629,256.09 | 54.6 |
| TOTAL | 918,610.0 | 100.0 | 997,363.8 | 100.0 | 1,152,352.9 | 100.0 |

Notes:

Deposit-taking Institutions include commercial banks, FIA licensees, building societies, and credit unions

Source: compiled by the FSC

Table 2: Capital Base of the Insurance Industry, 2004- 2006
(\$ Million)

| Indicators | General | | | Life | | |
|------------------------------|---------|---------|---------|----------|----------|----------|
| | 2004 | 2005 | 2006 | 2004 | 2005 | 2006 |
| Capital & Surplus | 6,120.5 | 7,279.7 | 8,818.7 | 16,600.9 | 19,740.2 | 23,102.0 |
| As % of Total Assets | 15.2 | 21.7 | 24.7 | 24.5 | 25.2 | 24.4 |

Source: Compiled by the FSC

Table 3: Capital Base of Securities Firms, 2004-06

| Indicators | (\$ Million) | | |
|-----------------------------|--------------|-----------|-----------|
| | 2004 | 2005 | 2006 |
| Capital | 23, 647.6 | 32, 591.5 | 38, 473.6 |
| As % of Total Assets | 7.9 | 9.5 | 9.8 |

Source: Compiled by the FSC

**Table 4: Applications for Licenses under the Pensions
(Superannuation Funds & Retirement Schemes) Act, 2006/07**

| Status of Application | Administrator | Investment Manager | Total |
|------------------------------|----------------------|---------------------------|--------------|
| Approved | 21 | 21 | 42 |
| Refused | 0 | 1 | 1 |
| Under-Review | 6 | 4 | 10 |
| Total | 27 | 26 | 53 |

Source: Financial Services Commission