



**Association of Bermuda Compliance Officers Conference 2009**  
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Good morning ladies and gentlemen. I'd like to thank the ABCO Executive for inviting me to share some remarks with you today; the Authority appreciates having the opportunity to be part of this important conference. The BMA is very supportive of ABCO. You are our ally in ensuring high standards of compliance are maintained in Bermuda's financial markets and in protecting this jurisdiction's reputation. Indeed, we know that when we're busy, then ABCO members are also busy.

And it has been remarkably busy since the last time you hosted this event. The Authority has had a very full agenda over that period, due to the activities of international standard-setters, the global financial crisis, and the regulatory response to the global financial crisis. We've been very transparent about our regulatory plans through publishing our Business Plan and conducting our consultation process, and we've established a pretty good track record of doing what we say.

We are just starting to put together our 2010 Business Plan and there will be many points of continuity in our programmes and initiatives moving forward. I'll explain the main regulatory priorities in that Plan, but then I also want to take this opportunity to set out for the first time a comprehensive statement of the BMA's approach to enforcement activity.

Regarding our regulatory priorities, the three highlights for 2010 will be: working towards achieving regulatory equivalence for Bermuda's insurance framework; managing the tail of the global financial crisis and its aftermath; and AML. My colleague Tom Galloway, Senior Counsel at the Authority, who heads up our AML Unit, will speak about AML later. I will also briefly cover AML in the context of enforcement.

So, I'll start with regulatory equivalence. Achieving regulatory equivalence has been a significant focus in the Authority's work plan over the past two years. Regulatory equivalence refers to the process by which regulators assess the frameworks and standards set by other jurisdictions. If a jurisdiction's framework is deemed to be broadly equivalent, access for companies to that market improves and duplicative regulation is eliminated. We're focused on achieving regulatory equivalence with the US and UK/Europe, given the importance of those markets to Bermuda. However, when we refer to equivalence, we don't mean an exact replication of standards from overseas being imposed in Bermuda, but rather adapting and applying those standards intelligently for this market after consulting with the stakeholders who will be most impacted. Our philosophy is that broad equivalence for frameworks should be the goal; anything else would frankly be impractical on a global scale. We remain sensitive to the fact that regulation should be appropriate for the scope and nature of the business being conducted in a market. We intend to continue our extensive consultation with the market in Bermuda regarding our work on framework changes designed to bring us closer towards achieving regulatory equivalence.

We're particularly focused on achieving equivalence for our insurance regulations, specifically in relation to the Solvency II Directive, a risk-based capital adequacy regime that will be applied to insurance companies based in Europe. Our Solvency II work is a major undertaking and is a useful example of the many elements and complexities involved in working towards regulatory equivalence. The Directive will seek to standardise and enhance the effectiveness of insurer solvency regulations and requirements across the EU. Due to the significant amount of insurance and reinsurance business conducted between Bermuda and Europe Solvency II is obviously important to

Bermuda. Earlier this year we published a roadmap document which gave details of our progress so far in relation to the Directive. We're making enhancements to our solvency regime for insurers that will result in changes in three core areas: capital adequacy; governance and risk management; and disclosure or transparency. Some highlights of the significant amount of work completed across these areas to date include:

- Establishing the Bermuda Solvency Capital Requirement, an enhanced solvency regime that will be applied to our Class 4 (re)insurers. Our BSCR work is focused on three critically important areas: determining eligible capital requirements; setting the amount of capital to be applied to companies using either the BSCR or companies' internal models; and ensuring firms demonstrate the link between their capital model, risk governance and decision-making (a process known as the Own Risk and Solvency Assessment or ORSA). The ORSA process helps regulators better understand the risk profile of companies.
  
- We have introduced a framework for permitting the use of internal capital models to determine regulatory capital for Class 4 insurers, including the standards and application process for accepting these models. This took place after an extensive survey of modelling practices within the Class 4 sector. Such models will be subject to a set of strict pre-approval criteria, which are currently under development.
  
- We've also conducted significant work on establishing a group wide supervision framework, including establishing a supervisory colleges programme for some of Bermuda's largest (re)insurers, as well as a Discussion Paper on our proposals for implementing group wide supervision. Group-wide supervision will be a very important consideration in the equivalency assessment of third country regulations for Solvency II. The Authority's intends to set standards for group supervision that are appropriately aligned with those being established by Solvency II and the International Association of Insurance Supervisors, the global standard-setting body for the insurance sector. We're currently reviewing the

- In terms of disclosure, the Class 4 sector is now required to produce GAAP financial statements which the Authority is publishing; similar requirements will be applied to Class 3B companies for 2010. In June the Authority published a Consultation Paper that outlines proposals for further enhancements to its transparency and disclosure regime for Class 4 and 3B insurers. We recognise that the international debate on this issue is on going; therefore we're taking a very measured approach to making changes to our disclosure regime. Our intention is to allow for sufficient time to consult with the market, while also ensuring the BMA's proposals keep pace with international developments.

This is just a summary highlighting some of the work that the Authority is conducting towards the goal of regulatory equivalence. I should also point out that these changes apply to the framework for large commercial insurers; the regime for captives will remain largely unchanged. Much has been achieved, and Bermuda is in the lead pack of jurisdictions making tangible progress in preparing for equivalence. However, there is still a lot of work to do, and we remain confident that we are on track to succeed in our efforts to reach our goal.

I'd like to move on now to the global financial crisis. Bermuda has weathered the financial storm well. There was some limited impact among the insurance sector, and the Authority conducted work with relevant parties here and overseas to restructure and stabilise financial guarantee firms. In terms of the banking sector, the Authority successfully implemented bank stress tests and precautionary capital buffers that have added another layer of protection against the impact of any further potential economic turmoil in the markets.

However, the Authority still remains vigilant to problems that could emerge in the aftermath of the crisis. The next phase in the fall-out from the crisis will be coping with the post-mortem of its effects and a resulting new phase of regulation internationally, which will inform our proposals for changes in Bermuda. For example, we anticipate major changes to banking legislation over the next few years; in the meantime, as an initial step, for 2010 we will be upgrading our liquidity standards. We also see the distinct possibility of changes to hedge fund regulation at the international level; there is currently discussion regarding new IOSCO standards and a draft EU directive that will likely impact offshore centres. Clearly, we need to be prepared and to show we can make our own contribution to what is right and practical in terms of standards for the hedge fund sector. With this in mind we are currently working with our regulatory counterparts in Cayman and BVI to discuss changes in hedge fund standards. We recognise the need to be nimble and to be ready for these and other changes, as the pace and direction of change in the international regulatory arena is constantly evolving.

Evolution is also the theme with respect to enforcement matters at the Authority. Our powers and approach to enforcement are indeed evolving, so it makes sense to pause and set out our thoughts in this area for the benefit of ABCO members, as you will be in the front line once changes are made.

Enforcement was previously conducted discreetly with impacted firms, in terms of private use of our powers. However, recently we have taken some public actions – for example, working with the Police to address unauthorised regulatory activity by a prominent businessman, and acting to wind up an investment firm that posed risks to consumers. Our powers have also changed – we have new AML powers of fining. We have published a statement of practice explaining our approach, but perhaps it may be useful to give a further explanation, as we have been thinking about our approach to enforcement.

First, a word about the scope of our responsibilities: in addition to our supervisory responsibilities, the Authority is responsible for, among other matters, ensuring that any company conducting financial business in or from Bermuda is properly licensed to do so.

When we become aware of entities that appear to conduct such activities without a license they are put on our Warning List, which is published on our website. The Authority has various powers to investigate and take action where unlicensed financial services business is being conducted, and in relation to any regulatory breaches. However, if there are issues of a criminal nature connected to institutions, they are a matter for the Police, with whom we continue to have a close working relationship. We will, as warranted, notify the Police of any suspicion of criminal activity we may discover in the course of our regulatory duties, and we've done so in the past in the form of submitting suspicious activity reports, as required by law. However, investigating and gathering evidence for a criminal prosecution remains primarily a matter for the Police, with the cooperation and assistance of the Authority. So the BMA has clearly defined enforcement responsibilities which match our clearly defined regulatory responsibilities: we are not the Police, Serious Fraud Office, FBI and Mission Impossible team rolled into one – nor do we want to be.

Second, some comments on our risk-based approach. We are a risk-based financial regulator and that applies equally to our approach to enforcement. We have increased our resources devoted to AML and enforcement matters in the past year under the leadership of Tom Galloway. But we still have limited resources and therefore need to prioritise our efforts. That means we will NOT investigate each and every suspicious case that comes across our desk, but will prioritise based on a number of factors. The questions we could consider in these circumstances are: What is the impact of the problem in terms of investor protection or Bermuda's reputation? What is the probability that a problem has actually occurred? Is the firm willing to work with us to rectify the situation? Are other regulatory authorities pursuing the matter? What is the previous compliance track record of the firm in question? Taking this approach allows us to allocate our resources effectively and to pursue actions appropriately, as required.

Third, what about our overall philosophy to enforcement action? It is NOT our intention to be an enforcement-led regulatory agency. Our instinct is that where we see a breach we will seek to work with the firm involved to give them an opportunity to remedy the

problem. However, there are a number of caveats to this. If the firm specifically, or industry as a whole, has been given sufficient notice of a concern but has failed to address it, then we WILL move to take enforcement action. If we see a severe and serious supervisory failing we will take enforcement action as well. And if we are aware of actual criminal activity, such as actual money laundering, as well as regulatory breaches, we will be minded to take enforcement action.

We believe that enforcement action provides a valuable tool to supplement our existing powers. Effective enforcement action can provide a deterrent to other firms, dissuading further regulatory breaches and providing an incentive for firms to raise their game. It also ensures that the regulatory regime is seen as credible and protects Bermuda's reputation as a place for quality business.

We have already consulted with the insurance market on proposals to expand our enforcement powers to include fining for breaches of the Insurance Act, in addition to AML and investment matters at present. We are also publishing proposed guidance on our fitness and propriety standards, to provide greater clarity about when we might refuse the appointment or indeed direct the removal of a director or shareholder controller of a regulated firm. We are also starting work to look at the adequacy of our enforcement powers for the banking, trust and investment areas, and with respect to breaches of the regulatory perimeter for unauthorised activity. Finally, we will shortly be publishing proposals concerning the publicity of enforcement action.

These steps are part of an overall plan to upgrade the enforcement framework in Bermuda incrementally, so that it is more consistent with international standards. This is not a process that will or should be rushed. We will take each step deliberately in close consultation with the market. It is most likely that our first enforcement actions will relate to AML issues, and Tom will give you more details on that later. But let me say that based on our AML-themed visits and regular on-sites we are already seeing some patterns of unacceptable practice where improvements are required: for example, KYC documentation has been good in many cases, but for some firms our file reviews have

shown significant gaps. Across the board we have seen some tardiness in updating procedures to reflect the new legislative framework. We have also routinely seen weakness in training practices on AML. And we have seen uneven practices in monitoring client activity to see whether SARs are required. The Authority would like to ask for your assistance, as the officers at the forefront of your organisations' compliance efforts, to make improvements in these areas. We are putting you on notice that persistent weaknesses in these areas into next year will make firms liable for enforcement action.

Finally, let me say a brief word about our approach to consumers and retail financial services. Bermuda is a predominantly wholesale financial market and our supervisory approach is calibrated accordingly. That has not and will not change. However, there is also a significant local retail market for financial services and recent events have shown the vulnerability of customers using those services. The retail sector will be an area of increased focus for the Authority in the coming year. We will not be getting involved in the transactional or commercial disputes between retail customers and financial firms – it's not our responsibility to handle complaints. However, we will be encouraging better standards of business conduct through improved codes of conduct in a number of areas. Stay tuned for more details. We will also be monitoring compliance with existing codes more closely as part of our supervisory activity. And we will be coming forward with measures next year to improve financial literacy within the local community through consumer education activities.

I hope my remarks have provided you an informative preview of the Authority's key priorities for next year, including some early plans related to retail consumers. Hopefully I have also given you a more complete picture of our approach to enforcement. The Authority has a full and challenging regulatory agenda, which reflects the ever-changing expectations being placed on regulators worldwide, as well as our commitment to ensure that Bermuda remains appropriately aligned with international regulatory standards. None of us, whether we are the regulators or among the regulated, can ignore the scrutiny that will come from on going reforms in financial regulation globally. As compliance professionals in the market here with your own growing set of responsibilities, the pace

and volume of regulatory changes in Bermuda may also seem challenging from your perspective. We appreciate your cooperation as our framework enhancements continue, and encourage you to provide us with feedback when we seek market consultation on changes that are relevant to your business; use the opportunity to participate in developments as they occur. We also ask that, once those changes are in place, you use your pivotal roles to ensure that, collectively, Bermuda maintains its long-standing track record of high regulatory compliance within the market. In that way we can all ensure that Bermuda's framework remains effective and practical, while also being mindful of our international standing as a credible, well-regulated jurisdiction.

Thank you.