1st Edition, April 2017

Financial Services Authority Newsletter

Mission: To jointly create a conducive environment for the growth and development of the financial services industry of Seychelles, in alignment with the national economic development strategy and in strict compliance with local and international regulatory norms and best practices.

CEO's Foreword

Welcome to the first edition of the Financial Services Authority Newsletter for 2017.

In the last edition of the newsletter for 2016, it was my pleasure to report the enactment and coming into force of the International Business Companies Act, 2016, the product of the hard work and collaboration of all stakeholders, including the industry. Since its enactment, the FSA has been working hard to implement the new Act. We thank the industry for its understanding through this transition and reinforce our commitment towards supporting our stakeholders to adhere to this new legislative framework.

2017 brings along new and exciting challenges. With the everchanging economic environment, we continue to strive for excellence. As customary, FSA is working in close collaboration with other government stakeholders and the industry to ensure compliance to these international best practices, as it is of utmost importance to protect our reputation as a jurisdiction. This year, the focus of the FSA is centered on compliance to the OECD's Base Erosion and Profit Shifting (BEPS) project. Seychelles is currently in the process of reviewing its different tax regimes in accordance with BEPS standards in order to identify whether any of these may be potentially harmful.

With a clear focus on our goals, the Financial Services Authority recognises that its structure and processes are significant to its long-term success. In this regard, it was crucial for the FSA to undergo a structural change as per recommendations from the IMF. In this regard, the licensing and supervision of products will be undertaken by one section. This will apply to capital markets and collective investment schemes and fiduciary services. In addition, the Human Resources and Administration Section has been separated into two separate sections. We are confident that the restructuring and its implementation will improve our daily work flow.

Finally, I would like to take this occasion to commemorate Labour Day by recognizing the hard work and dedication of the staff of the Financial Services Authority. I would also like to extend my sincere appreciation to all employees within the financial services industry and recognize their contribution to this sector. We can all be proud of all we have accomplished collectively. Have an enjoyable holiday.

Ms. Jennifer Morel

Chief Executive Officer

Results of the Financial Stability Committee meeting

Over the past decade, safeguarding financial stability has become an increasingly dominant objective in economic policy making of Seychelles. Hence, on March 21, 2016 a new legislation established a Financial Stability Committee (FSC) at the Central Bank. The Committee is charged with a primary purpose of identifying, monitoring and taking action to remove or reduce systemic risks with a view of crucially protecting and enhancing the resilience of the Seychelles financial system. In its role, the FSC provides immense support to the economic policy of the Government.

The four members of the Committee including the Governor of the Central Bank, Chief Executive Officer of the Financial Services Authority (FSA), Principal Secretary in the Ministry of Finance, Trade and the Economic Planning, and the director of the Financial Intelligence Unit (FIU) met on February 10, 2017 for the first session for the year 2017.

Pertinent issues which were discussed included the risk assessment analysis and development which were carried out over the course of the third quarter of 2016. The committee evaluated the monthly data to be collected for the rest of the year and its possible impact upon the financial stability of the country.

Stemming from subsequent meetings, the Committee recapped the probable risks which had been graded according to the likelihood and potential implications on the domestic economy. The ranking was undertaken from a qualitative perspective and the risks which were considered included one-off events as well as ever-persistent potential risks, which included but is not limited to political events on both domestic and international level, the performance of the tourism sector, continued impending impact of BREXIT, and the likely global interest rate developments.

Great attention by the members was placed on exploring potential mitigating actions and other risks which do not appear in the quantitative financial sector and macroeconomic data were highlighted. The risks identified were of both singular and topical nature and in addition, the persistent threats present to the financial stability of Seychelles. Included in the matrix of risks were cyber-crime and terrorist threats as well as legislative arbitrage. The Committee further considered risks arising from external developments such as the potential legislative and policy changes impacting global financial forums following the inauguration of President Trump. The ongoing negotiations following the United Kingdom's decision to leave the European Union were discussed at length and emphasis was placed on its looming trade implications for Seychelles as 33% of the country's tuna exports are aimed at the United Kingdom market. Therefore, it was decided that the trade negotiations between the United Kingdom and Seychelles are undertaken at the earliest.

The FSC went on to discuss the issues of global de-risking. The Governor of the Central Bank assured the members of the Bank's ongoing efforts through the establishment of another high-level committee within the Central Bank, tasked to assess the developments with regards to global de-risking and correspondent banking relationships. The high-level Committee focused on de-risking, had met prior to the FSC meeting and agreed to implement a set of recommendations as approved by the Cabinet which included to ensure the Anti Money Laundering and Combating of Financing of Terrorism regulatory frameworks are consistent with

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international standards, engage with foreign regulators and correspondent banks by addressing their concerns, launch a PR campaign to show the actions undertaken are in line with international best practices and finally to review the offshore sector model. Despite the formation and efforts of the high-level Committee, the FSC continues in its vital role of monitoring and assessing the risks facing the jurisdiction as a result of global derisking.

The FSC also discussed the changes to the Financial Intelligence Unit and the urgent need for adequate training of all law enforcement officers involved with preventing "white collar" crimes.

Another area of concern which was raised by the Committee was the unapproved national budget by the National Assembly. This poses a threat to the country's financial stability. Delays in the start dates of various Government projects have cost the Government greatly. Whilst the Principal Secretary for Finance and Trade, Mr. Patrick Payet reassured that other Government projects should cover these losses, he further advised that the Members of the National Assembly have agreed to give the budget priority so that it can be approved.

In conclusion, the members presented quantitative analysis covering various metrics relating to the broader economy and indicators of the financial sector performance during the course of the third quarter, including credit-to-Gross Domestic Product, loans-to-deposit ratios, inflation, and foreign exchange market developments. Furthermore, monthly results were presented up to and including December. Relatively stable trends in these regards were noted over the course of the third quarter of the year.

It was established that the overall financial system of Seychelles appears stable. However, the members were reminded to take into account the threat of evolving risks. In all, the FSC will continue to monitor market developments and where possible take necessary action to mitigate risk exposures. A major challenge is to develop a deeper understanding of how the dimensions of the financial stability interact with each other and the economy. Undoubtedly, this is a heavy agenda which will be navigated by the Committee members.

Correspondent Banking

The Financial Action Task Force defines Correspondent Banking as the provision of banking services by one bank (the "correspondent bank") to another bank (the "respondent bank"). Large international banks typically act as correspondents for thousands of other banks around the world. Respondent banks may be provided with a wide range of services, including cash management (e.g. interest-bearing accounts in a variety of currencies), international wire transfers, cheque clearing, payable-through accounts and foreign exchange services. The correspondent bank offers an ongoing service to the respondent bank. In Seychelles, correspondent banks are primarily used by domestic banks to service transactions that either originate or are completed in foreign countries. That is, they act as a domestic bank's agent abroad.

The withdrawal of correspondent banking relationship is often referred to as de-risking. Per the Discussion Note issued by the IMF on the withdrawal of correspondent banking relationships, this term is often applied indiscriminately and can refer to the banks avoiding the business or reputational risks altogether on a wholesale basis, without a case by case assessment of the risk associated with the individual customers or the country. It can also be the result of an analysis indicating that the business relationship is no longer profitable. In addition, de-risking has been used more broadly to refer to any form of withdrawal of financial services. The indiscriminate application of this term is often misleading.

The Discussion Note consolidates surveys conducted across Africa, the Caribbean, Central Asia and Europe and notes a prevalence of withdrawal of correspondent banking relationships, particularly in smaller jurisdictions and emerging markets. Over the past few months, the issue of correspondent banks choosing not to do business with the Seychelles has been addressed in the media. It has been stated that this is due to the banks de-risking as Seychelles is viewed as a high risk jurisdiction. Research has shown that the drivers leading to the withdrawal of correspondent banking relationships are multiple and interrelated.

These individual banks may decide to "de-risk" based on a number of considerations. Generally, such decisions reflect banks' cost-benefit analysis, shaped by the re-evaluation of business models in the new macroeconomic environment and changes in the regulatory and enforcement landscape, notably with respect to more rigorous prudential requirements, economic and trade sanctions, anti-money laundering and combating the financing of terrorism (AML/CFT) and tax transparency. These factors influences banks' risk and reputational cost perceptions. Further pressures to withdraw may arise where regulatory expectations are unclear, risks cannot be mitigated, or there are legal impediments to cross-border information sharing. These factors operate concurrently, although their relative significance varies case-by-case. Global banks have confirmed their stance of increased caution in maintaining correspondent banking relationships but have also maintained that while the number of banks offering these services have decreased, the volume and value of transactions have increased. Globally, most cases of "de-risking" involve US Banks given the key role played by the US Dollar in the international financial system. The number of Correspondent Banks in the euro area has decreased steadily since 2002 in view of a highly concentrated correspondent banking market. Furthermore, some global banks have decided to exit a number of countries as part of a risk re-evaluation in the context of increased compliance costs.

In Seychelles, only one bank offers services to the offshore sector. As such, the concerns of the intermediary banks are much more complex than the presence of the offshore sector. In fact, certain countries with no offshore financial sector have been affected while others such as Hong Kong with a thriving financial services sector remain relatively unaffected. The relative size of the Seychelles is an impediment as correspondent banks must consider economies of scale in offering their services, in view that correspondent banking has a low profit margin but high costs of compliance. Nevertheless, the risk to financial stability calls for an enhanced understanding of the situation as well as coordinated efforts from all stakeholders.

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Risk Based Supervision training for the Domestic Insurance Companies and the Seychelles Pension Fund

The role of a supervisory authority undertaking prudent supervision is to promote the maintenance of efficient, fair, safe and stable pension and insurance markets for the benefit and protection of policyholders and pensioners. An effective supervisory authority, such as the Financial Services Authority (FSA), is able to require an insurer or pension fund to take timely preventive and corrective measures should the entity fail to operate in a manner that is consistent with sound business practices or regulatory requirements. Traditionally, authorities have performed this role by way of compliance based supervision. Under this style of supervision, licensees must comply with a set of rules generally written into the law or subordinate legislation. In recent years, supervision has been evolving and moving from a style that is compliance based to one that is risk based. This progression has also been a feature of the activities of not just insurance supervision but increasingly pension and banking supervision.

Since mid-2016, the Insurance and Pension Section of the FSA, along with the help of consultants, Mrs. Holly Bakke, Mrs. Martha Kelly and Mr. Edward Sia have been working tirelessly to implement such risk based supervision framework to the insurance and pension market. As part of the implementation, the FSA organized a training held at the STC Conference Room on Tuesday 28th March, 2017, conducted by Mrs. Bakke, for the Domestic Insurance Companies and the Seychelles Pension Fund (SPF).

The training allowed the insurers and the SPF to understand the concept of risk based supervision, obliging both regulators and the companies to "focus on what matters" by assessing the degree of risk in the company's business operations and determining how to reduce the risk as required. Much emphasis was placed on the fact that with risk based supervision, the entities will be monitored, and both for compliance with the rules and for how they approach risk management.

A crucial feature of the training was that each company and their representatives had the opportunity to sit with their assigned business analyst from the FSA. The interaction allowed for brainstorming sessions to be conducted between the regulator and licensee with the aim of challenging how the licensees think about insurance and pension regulation in the Seychelles as well as regionally. The lengthy discussion involved analyzing the areas of the fi-nancial Sector in developing markets such as Seychelles and comparing it to that of more developed markets.

The training was designed to deepen the insurers understanding of why the FSA decided on the regulatory change from compliance based supervision to risk based supervision. The need for a new framework arose from the global desire for consistency thus keeping the Seychelles insurance regulation in line with international best practice, mainly the International Association Insurance Supervision (IAIS). There are increasing numbers of multi jurisdiction players which if left unsupervised poses a risk of financial meltdown in the country. The shift paves the way for more risk-based approaches to capital and solvency measurements and focus on risk management and corporate governance of the entities. As part of their risk management strategy, the insurers will have to introduce or increase the use of stress and scenario testing as a risk mitigating factor amongst others.

Further discussion was carried out on the concerns that the companies had about risk based supervision. Mrs. Bakke compared the traditional compliance based regulation model with that of the risk based supervision regulation. Some advantages in favor of the risk based framework include constant reassessment of risk by company and regulator which will result in anticipating the possible risks the supervised entity will be facing when executing its business plan thus going beyond its current financial situation. Traditional compliance approaches focus on a limited number of risks that are the subject of the rules. These are normally credit, liquidity, market and insurance risk. In view that risk based supervision is forward looking, the starting point for FSA is to understand and monitor the business strategy of the insurer. Having to understand the SPF and insurer's business strategy properly obliges the Authority to consider other risks such as the risks inherent in the strategy. The risk based supervision goes beyond by taking into consideration risks that are both external and unique to the individual insurers.

Under the new supervisory approach, the companies will have to implement risk management policy outlining how the risks will be consequently managed. Such analysis will require the licensees to conduct their Own Risk and Solvency Assessment (ORSA). The ORSA would assist in linking the SPF and insurer's risk identification, measurement and prioritization of the processes with capital management and strategic planning. The ORSA of each compa-ny would therefore be unique, reflecting their business, strategy and approaches to the risk. In turn, the FSA would use the ORSA as a tool to understand the SPF and the insurer's process. At minimum, ORSA should discuss three major areas, namely the entity's Risk Management Framework, their Assess-ment of Risk Exposure and its Group Risk Capital and Prospective Solvency Assessment.

The importance of ORSA allows companies to explore and describe the relationship between tolerance limits, regulatory capital requirements and economic capital. Mrs. Bakke further explained the need for the companies to have liability management policy, describing relationship product development, pricing, investment management and how policy complies with regulatory requirements.

Mrs. Bakke established that in order to achieve its objective of continuous supervision and early corrective action, the risk based supervision process focuses on various aspects including continuous collection of financial and non-financial data from the companies with a view to enable the FSA to independently perform analysis of raw data through off-site surveillance. It was relayed to the participants that the business analysts will collect both qualita-tive and quantitative data including annual filings, quarterly reports, and standard ratios from the insurers and SPF. Accordingly, the accuracy, complete-ness and timeliness of the data will be critical in determining the ratings of the licensees.

On the other hand, onsite examination is focused on evaluating the risk and control environment within the companies and much emphasis is being placed to ensure good corporate governance, transparency and accuracy of information used by senior management for decision making. Findings following the onsite assessment put significant onus on the licensees, where improvements various aspects of their operations where needed. Certain aspects may be improved sequentially whereas others may be required to be improved concurrently.

In further discussions, the business analysts, insurers and SPF explored how they can all help prepare the market for risk based supervision. It was pointed out that whilst the move towards risk based supervision is a step in the right direction for the insurance and pension industry, challenges abound both for the FSA and the companies as the industry grapples with wide-ranging issues including quality of data, scalability of regulatory reporting processes, efficacy of risk management systems and cost of compliance. However, the effective implementation of inclusive and data centric risk based supervision is expected to be a long-drawn and continuous process with improvements in various facets being brought about gradually. Therefore, it was agreed that the process demands the continuous engagement of all parties involved which would result in financial stability, managing contagion risk in an increas-ingly inter-connected marketplace.

Seychelles' assessment on Base Erosion and Profit Shifting

The Base erosion and profit shifting (BEPS) project is headed by the OECD's Centre for Tax Policy and Administration and deals with the tax avoidance strategy used by multinational companies, wherein profits are shifted from jurisdictions that have high taxes to jurisdictions that have low or no taxes. The project aims to ensure that profits are taxed where economic activities generating the profits are performed and where value is created.

Furthermore, the BEPS project is said to be an "attempt by the world's major economies to try to rewrite the rules on corporate taxation to address the widespread perception that the corporations don't pay their fair share of taxes".

BEPS has altogether 15 standards (Actions) of which Seychelles will have to comply with the 4 minimum standards, as stated below:

- Action 5: counter harmful tax practices more effectively, taking into account transparency and substance
- Action 6: prevent treaty abuse
- Action 13: re-examine transfer pricing documentation
- Action 14: make dispute resolution mechanisms more effective

BEPS mission to equip governments with domestic and international instruments to address tax avoidance continues as further assessments will be conducted during the year for the following regimes:

1. IP regimes (CSL and IBC)
2. Banking and Insurance regimes
3. Mutual Fund and Hedge Fund and Securities
4. International Trade Zone framework (to distribution services)
5. ICSP and presumptive tax regime (miscellaneous regimes)

The Ministry of Finance, Trade and Econimic Planning has established a committee, comprising representatives of both Government and the Private Sector, to collaborate on the BEPS project.

Restructuring of the FSA

On February 27th, 2017, the Board of Directors of the FSA approved a scheme of service for each section within the FSA designed to provide for a welldefined career structure, so as to attract, motivate and facilitate retention of suitably qualified and skilled personnel within the FSA. It was also designed to establish standards for recruitment, awarding benefits upon completion of training and advancement within the career structure on the basis of quali-fications and knowledge of the job. With the implementation of the scheme of service, a restructuring of the FSA's sections was undertaken in order to enhance the effectiveness of the organisation.

Firstly, the Human Resources and Administration section was split into two distinct sections, namely the Human Resources section and the Administration section with the Human Resources section responsible for recruitment and selection; capability development and learning and development strategy; performance management and development system; career development and succession planning; reward management; health and safety and well-being and operational human resources and the Administration section responsible for procurement; records management; fixed asset management; quality management; logistics and transport; maintenance and technical management; and housekeeping.

Secondly, the Supervision section was restructured and renamed to Fiduciary Supervision Section and the Authorisations and Registry section was restructured and split into the Registry Section and the Capital Markets and Collective Investments Schemes Supervision section. The Fiduciary Section is now responsible for both the licensing and supervision of International Corporate, International Trustee and Foundation Service Providers whereas the Capital Markets and Collective Investment Schemes Supervision Section is responsible for the licensing and supervision of entities licensed under the Securities Act 2007 and the Mutual Fund and Hedge Fund Act, 2008. The previous Authorisations Section (Fiduciary) has been merged with the Fiduciary Supervision Section.

The current structure of the organisation is as follows: