

**GLOSSARY**

AML	Anti-money laundering
BCP	Basel Core Principles
BCCI	Bank of Credit and Commerce International
BO	Banking Ordinance 1992
CFT	Combating the financing of terrorism
CJO	Criminal Justice Ordinance
CP	Core principles
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FSC	Financial Services Commission
FSCO	Financial Services Commission Ordinance
GFIU	Gibraltar Financial Intelligence Unit
GSCCAB	Gibraltar Society of Chartered and Certified Accountancy Bodies
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
LEG	Legal Department
MOU	Memorandum of understanding
OECD	Organization for Economic Cooperation and Development

## I. BASEL CORE PRINCIPLES

### General

1. This assessment of the Basel Core Principles for Effective Banking Supervision (BCP) was carried in March 2006 by Peter Hayward (consultant, formerly Bank of England and International Monetary Fund (IMF)) and Jorge Mogrovejo, (consultant, Superintendency of Banks and Insurance, Peru) as part of a Module 2 assessment of the regulation and supervision of the Gibraltar financial sector at the request of the Gibraltar government. The Gibraltar Financial Services Commission (FSC) and its staff cooperated fully with the assessment and their assistance is gratefully acknowledged.

### Information and methodology used for assessment

2. The assessment was based on the law applicable to the supervision of banks by the FSC, principally the Financial Services Commission Ordinance (FSCO), 1992 and the Banking Ordinance, 1992 (BO) and on Administrative Notices, Guidance Notes, Newsletters, and other written material supplied by the Commissioner and his staff. The assessors also read the report of a previous BCP assessment carried out as part of the first Module 2 assessment in 2001 as well as the statutory review published in January 2005. This review assessed regulation and supervision in terms of compliance with European Union (EU) legislation and the extent to which FSC practices match those of the U.K. supervisory authorities as required by the FSCO. The FSC staff also prepared a self-assessment of compliance with the BCP. The assessors met the Chief Minister, the Director of the Finance Centre, bankers, and external auditors as well as many of the staff of the FSC.

3. The assessment of observance of each of the Core Principles (CP) follows a qualitative approach and is based on the Core Principles Methodology Document of October 1999. The assessment method consisted of examining the degree of observance of each of a principle's essential criteria and, where the assessors judged necessary, of the additional criteria, as well.

4. A principle will be considered **compliant** whenever all essential criteria are generally met without any significant deficiencies. There may be instances where a country can demonstrate that a principle is observed through different mechanisms. Conversely, due to the specific conditions in individual countries, the essential criteria may not always be sufficient to achieve the objective of the principle and, therefore, other measures (including any additional criteria) may also be deemed necessary by the assessor to judge that compliance is achieved. A principle will be considered **largely compliant** whenever only minor shortcomings are observed, which do not raise any concerns about the authority's ability and intent to achieve full compliance with the principle within a prescribed period of time. A principle will be considered **materially non-compliant** whenever, despite progress, the shortcomings are sufficient to raise doubts about the authority's ability to achieve compliance. A principle will be considered **non-compliant** whenever no substantive progress toward compliance has been achieved. A principle will be considered **not applicable** whenever, in the view of the assessor, the CP does not apply given the structural, legal, and institutional features of a country.

5. A separate Monetary and Financial Department (MFD)/Legal Department (LEG) team assessed Gibraltar's compliance with the Financial Action Task Force (FATF) Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT). Their assessment, based on the latest version of the methodology, amplifies the assessment of CP 15 which is based on the 1999 methodology of the Basel Committee.

### **Institutional and macroprudential setting, market structure and overview**

6. The banking sector consists of 18 banks with total assets of £6.7 billion (\$11.7 billion) as of end-2005. Most of the banks are subsidiaries or branches of banks from other European countries, dominated by the United Kingdom with eight subsidiaries/branches in Gibraltar. There is only one bank which is not foreign bank owned and this has shareholders in the investment business in a major European financial centre. No licensing distinction is made between banks conducting cross-border and local business. The majority of business in the small local market is done by two banking groups. A major portion of cross-border banking business is providing private banking services, mainly asset management, to Swiss based customers and to the expatriate community in Spain and Portugal. This includes the provision of residential mortgages to clients purchasing property in the region. Another important component of cross-border banking are services provided to nonresident trusts and companies which benefit from the exemption from Gibraltar's relatively high corporate tax rate of 35 percent.<sup>1</sup>

7. The principal risks are reputational risk, both for the Gibraltar authorities and for the banks, as the bulk of the assets managed are off the balance sheet with the investment risk carried by the client. Credit risk is largely limited to residential mortgage lending and is heightened by the recent rapid rise in prices both in Southern Spain and in Gibraltar itself. Banks claim they are protected in the former by low loan/value ratios (typically 60-70 percent) and by the fact that banks normally manage substantial asset portfolios for borrowers. The price risk may be more acute in the small domestic market where competition is more intense and has led to higher loan value ratios at least for recent lending. No bank has a recognized trading book in Gibraltar and most treasury functions are carried out at head office which also typically manages liquidity. Thus market risks and liquidity risk are low. Investment advice is normally also based on head office analysis or services provided by specialist investment firms.

8. Banks have a competitive advantage over banks in other small financial centers in being able to provide services throughout the EU using the so-called "passport" arrangements. Although Spanish and Portuguese banks could compete with Gibraltar banks for business of expatriate residents of those countries they appear not to do so. Most clients have accounts with local banks for money transmission and general banking services, but local banks do not as yet offer significant competition for asset management and other private banking services. This business is therefore profitable and expanding. More typical

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<sup>1</sup> Some banks also benefit from this exemption but in many cases this is offset by group tax arrangements in the home country.

business for tax exempt companies and trusts with non-resident owners and beneficiaries is normally introduced by local law firms and other service providers. While the tax exemption is due to be phased out in order to comply with EU state aid rules, the business could survive if the new unified rate of corporate tax was not more than 10-15 percent.<sup>2</sup>

9. The FSC is a unified regulatory and supervisory authority for financial services. The FSC supervises the activity of banks, insurance companies, investment firms, collective investment schemes, and trust and company service providers. The FSCO requires that, since Gibraltar is considered as a part of the United Kingdom and, therefore, a constituent of the EU under the U.K. accession treaty, Gibraltar must ensure both that supervision complies with EU Directives, and that regulation and supervision in areas subject to EU supervisory legislative requirements match the standard of regulation and supervision in the United Kingdom. The statutory review mentioned in paragraph 2 above was designed to verify that the FSC met these obligations.

10. Under the FSCO the Commissioner is appointed by the Governor subject to the approval of the U.K. Secretary of State for Foreign and Commonwealth Affairs. The other members of the Commission are appointed in the same way but after consultation with the Commissioner.

### **General preconditions for effective banking supervision**

11. The preconditions for effective supervision are in place. As a member of the EU since 1973, EU directives have been adopted and implemented in Gibraltar legislation. In addition all except one of the banks are branches or subsidiaries of major international banking groups subject to consolidated supervision by their home supervisory authority.

12. International Financial Reporting Standards (IFRS) were adopted for all EU listed companies effective January 2005. However some subsidiaries of listed companies still continue to use older accounting standards even though the consolidated accounts of the group to which they belong use IFRS. Limited liability companies are required to submit audited financial statements to the Registrar of Companies and are publicly available.

13. Company law, accounting, and auditing arrangements are generally based on EU requirements and U.K. law and practice. Gibraltar's financial system and indeed its economy are small and there is little scope for differing from the U.K. model. Law enforcement is generally good and banks do not have difficulty in enforcing security on the rare occasions when they need to. Credit culture is also reported as strong with the incidence of default, especially in the local market reported as being exceptionally low.

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<sup>2</sup> A more damaging threat, regarded locally as extremely unlikely to materialize, arises from a case before the European Court of Justice, which could result in requiring Gibraltar to replicate completely the U.K. tax system.

## Principle-by-principle assessment

Table 1. Detailed Assessment of Compliance of the Basel Core Principles

<b>Principle 1.</b>	<p><b>Objectives, Autonomy, Powers, and Resources</b>  An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks. Each such agency should possess operational independence and adequate resources. A suitable legal framework for banking supervision is also necessary, including provisions relating to the authorization of banking establishments and their ongoing supervision; powers to address compliance with laws, as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.</p>
<b>Principle 1(1)</b>	<p>An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks.</p>
Description	<p>The FSC is established by the Financial Services Commission Ordinance 1989 (FSCO). The FSC consists of the Commissioner, who is both Chairman and chief executive of the FSC's staff, and seven independent and part-time members. All members of the FSC are appointed by the Governor of Gibraltar with the approval of the U.K. Secretary of State for Foreign and Commonwealth Affairs, in the case of the independent members after consultation with the Commissioner. (FSCO Section 3) The Commissioner is responsible for the supervision of institutions licensed to provide any financial services and ensure that that such supervision complies with any obligation imposed by European Union law, and, where such obligations apply, meets standards matching those required by legislation and supervisory practices within the United Kingdom. (FSCO Section 8).</p> <p>The FSC's functions include providing the Commissioner with such resources as are needed to undertake his functions and to review the effectiveness of supervision and the operation of Gibraltar legislation relating to financial services.</p> <p>Separate laws provide for the licensing and supervision of various types of financial service and these include the Banking Ordinance 1992 (BO) which empowers the Commissioner to license and supervise banks. The Government of Gibraltar can also make regulations and these include regulations implementing EU bank accounting directives and setting the fees charged by the Commission. Other EU legislation is given effect by Administrative Notices (AN) issued under BO Section 16. Alternatively the Government may decide to implement important requirements, such as new capital adequacy rules, by regulation, leaving the FSC to add details by Guidance Notes.</p> <p>Existing AN set out the criteria by which the Commissioner supervises banks including basic prudential requirements. BO Sections 22 and 23 set out licensing requirements which are required to be met continuously by licensed banks. As the Commissioner is the sole authority for the supervision of financial institutions in Gibraltar he also licenses banks and their affiliated companies to provide other financial services under separate legislation, for example, banks are licensed to provide investment services under the Financial Services Ordinance. Where a bank faces closure or requires restructuring the commissioner has powers and responsibilities under BO Sections 64 to 66 to cancel a license and issue directions to the bank. He may apply to the Supreme Court for the institution of winding-up procedures (BO Section 78) which are governed by the Companies Ordinance. Where the Commissioner believes it is necessary that the legal framework be revised, for example to implement new EU legislation or international standards, he proposes such changes to the Government of Gibraltar.</p> <p>The FSC also has a statutory obligation (FSCO Section 8) to monitor such developments. The FSC has published its regulatory objectives and the principles with which it has regard in achieving good supervision. It has also, rarely for a supervisory authority, achieved ISO recognition under ISO 9001:2000 involving periodic audits assisting the agency in achieving its objectives in a consistent fashion.</p>

	The Commissioner publishes statistical information on the performance of the banking industry and locally incorporated banks are required to file their annual financial statements with the Registrar of Companies.
Assessment	Compliant
Comments	In practice the Government has proposed and the Assembly has passed legislation to ensure that the legal framework remains up to date. The Commissioner has proposed amendments to the FSCO which would set out in law its objectives and its responsibilities and functions. The FSC has also instituted improvements to its own governance and has published a line-by-line assessment of its own compliance with the U.K.'s Combined Code on Corporate Governance. While, as the Statutory Review noted in 2005, the FSC's own corporate governance is in several ways inconsistent with modern corporate governance practices (as the FSC has accepted in its detailed description of compliance with the U.K. Combined Code) the FSC believes that the present arrangement is the most effective way of safeguarding the practice of supervision from conflicts of interest, given that Gibraltar is such a small entity. The assessors have certainly found no evidence to suggest that the independence of the supervisory process has thus far been compromised.
<b>Principle 1(2)</b>	Each such agency should possess operational independence and adequate resources.
Description	<p>The agency is operationally independent of the Government of Gibraltar. This is achieved in part by virtue of the fact that the Government has no formal role in the appointment of the members of the FSC. Although the U.K. government must approve the appointment of Commissioners the FSC is also independent of the U.K. government as the relative legislation has been passed by the Gibraltar House of Assembly and the U.K. authorities have no supervisory authority over Gibraltar.</p> <p>The FSC's activities are financed in part by Government subvention, but reliance on this source is now quite minor. However, the FSC cannot influence its revenue as fees payable by supervised institutions are determined by Government. The FSC has been able to build up reserves which would enable it to continue its activities in the event of a crisis without external support.</p> <p>The government has continually indicated that it supports the FSC's functions and there appears to be no indication of any attempt by the Government to interfere with the agency's supervisory activities. Nor is there evidence of banks attempting to influence the agency's activities improperly. The FSC has attempted to offset any potential threat to its autonomy by being rigorous in its accounting for its activities. It publishes a large volume of material relating to the Commissioner's supervisory activities and the FSC has published a self-assessment of its compliance with the U.K. Combined Code of Corporate Governance. Over the years the FSC and its staff have built up credibility based on a history of integrity and experience with all the professional staff having a background in the finance sector and relevant professional qualification. The FSC devotes considerable resources to training and the acquisition of personal professional qualification of its staff. Its financial position has enabled the FSC to offer salaries and conditions of employment in line with the industry it supervises so turnover remains quite low. The FSC also has powers to hire expertise that is not available within its staff from outside sources.</p> <p>The FSC has devoted significant resources to setting up and maintaining IT systems of a quality that enables it to discharge its responsibilities effectively and to publicize its operations on its web site and elsewhere.</p> <p>There is no statutory fixed term of office for members of the FSC, including the Commissioner. However, in practice appointments are made for fixed terms and these are published in the Gibraltar Gazette. Nor are the grounds for removal specified in law, although FSCO Section 3 does contain grounds for dismissal, these are not exclusive. Nor is there any requirement that reasons be specified if a member of the Commission were to be dismissed.</p>
Assessment	Largely compliant
Comments	The FSC should have responsibility for its own finances which would be facilitated if it had

	<p>powers to fix the fees payable by authorized institutions to the FSC.</p> <p>While it would be consistent with modern corporate governance practice for a term of office, and reasons for dismissal, to be specified in law, the fact that the Government does not make the appointments of Commissioner or Commission member means that it is unlikely that dismissal would occur for political reasons. There is no evidence that such has been the case in the past.</p>
<b>Principle 1(3)</b>	A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision.
Description	The BO governs the authorization and supervision of banks. The Commissioner is empowered by BO Section 24 to issue licenses and by BO Section 65 to withdraw them. While the BO sets the basic framework detailed prudential requirements are contained in AN issued under BO Section 16. These are “admissible in evidence in any action commenced in exercise of the rights contained in Section 72 or otherwise in connection with the operation or application of this Ordinance.” The Commissioner may also issue Guidance Notes (GN) and Newsletters to aid interpretation of the requirements of the Ordinance. BO Sections 60 to 63 enables the Commissioner, or any person authorized by him to require any information from banks he needs to carry out his responsibilities under the BO.
Assessment	Compliant
Comments	
<b>Principle 1(4)</b>	A suitable legal framework for banking supervision is also necessary, including powers to address compliance with laws, as well as safety and soundness concerns.
Description	Banks are required by BO Section 25(2) to observe continuously the essential licensing criteria in BO Sections 22 and 23. If it “appears to” the Commissioner that the criteria are not being observed or if the bank is engaged in actions likely to damage the interests of depositors or the reputation of Gibraltar he may impose conditions on the license or revoke it. (BO Sections 29 to 31). He may also issue conditions under BO Section 62. BO Sections 62 and 63 give the Commissioner and those authorized by him the right to enter premises and inspect such records as may be necessary. Where remedial action is necessary the Commissioner may issue directions under BO Section 29, and in cases of urgency, impose conditions under BO Section 30. BO Section 65 gives the Commissioner powers to revoke a license where a bank had failed to meet the licensing criteria. These formal powers have never needed to be used but reference has been made to their existence.
Assessment	Compliant
Comments	There are proposals for an “approved persons” regime which would give the Commissioner powers to act directly against an individual as well as a bank as an institution. Such persons would also have rights of redress not currently available to them if the FSC acts against an institution as a corporate entity. The Commissioner has no powers to impose civil financial penalties on banks or individuals but the absence of such powers has not so far proved a constraint on his ability to ensure compliance with supervisory requirements.
<b>Principle 1(5)</b>	A suitable legal framework for banking supervision is also necessary, including legal protection for supervisors.
Description	FSCO Section 18 and BO Section 14 provide protection against civil liability for the Commissioner or any person authorized by him in the discharge or purported discharge of his functions under law unless it can be shown he acted in bad faith. There is no provision requiring indemnification against the costs of such a person defending himself against suit (see additional criterion 3), although in practice no such cases have arisen.
Assessment	Largely compliant
Comments	The FSC has proposed an addition to FSCO Section 18 which would require the FSC to indemnify any existing or former member of the FSC’s staff against such costs.
<b>Principle 1(6)</b>	Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Description	The Commissioner is the sole regulator and supervisor of financial entities so there is no need for powers to share information domestically. Under BO Section 82 (10) (i), the Commissioner may share information with another supervisor where the latter has a need for the information

	for supervisory purposes and where the Commissioner is satisfied that the information will continue to be subject to confidentiality requirements. The FSC has concluded memoranda of understanding (MOUs) with several foreign supervisory authorities and has shared information with other authorities with which it has no formal agreement. It has done so with a number of the authorities that have supervisory responsibility over banks or parents or affiliates of banks authorized in Gibraltar. Where a request for information is not covered by one of the “gateways” in the BO the Commissioner cannot accede to such a request. Detailed rules on the exchange of information in paragraph 30 of the EU Banking Consolidation Directive (BCD) are included in Schedule 3 to the BO.
Assessment	Compliant
Comments	A Court of Appeal case in 2003 criticized internal processes used regarding disclosure in a particular instance. However, the Court confirmed the FSC’s powers of cooperation. The internal processes have now been improved. In addition the FSC has proposed a new Financial Services (Information and Co-operation: Powers and Confidentiality) Ordinance which would consolidate and clarify existing powers in various ordinances.
<b>Principle 2.</b>	<b>Permissible Activities</b> The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined, and the use of the word “bank” in names should be controlled as far as possible.
Description	The terms “credit institution” is defined in BO Section 2 by reference to the definition in the BCD. BO Section 4 defines “deposit”. BO Section 5 defines a “deposit-taking business” and BO Section 7 restricts the business of taking deposits to licensed institutions. Schedule 1 lists the permissible activities of institutions authorized under the BO by reference to the activities listed in the BCD2. Activities other than those authorized under the BO require separate authorization under other laws. BO Section 74 also restricts the use of the term “bank” etc. to institutions authorized under the BO or EU institutions authorized as such by other EU member states. BO Section 7 prohibits others not authorized from using the term “bank.” The Gibraltar Savings Bank, an institution regulated by the Government of Gibraltar under a separate law, is specifically exempted.
Assessment	Compliant
Comments	
<b>Principle 3.</b>	<b>Licensing Criteria</b> The licensing authority must have the right to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the banking organization’s ownership structure, directors and senior management, its operating plan and internal controls, and its projected financial condition, including its capital base; where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.
Description	Part IV of the BO deals with the licensing of banks. BO Sections 22 and 23 contain the main criteria which an applicant must satisfy. These criteria must continue to be satisfied so long as the license is retained. (BO Section 25(2)) Failure to satisfy the Commissioner on any of the criteria is grounds for rejecting the application. BO Section 2A incorporates requirements that the legal and management structures are not such as to hinder effective supervision. BO Section 23 (3) (e) requires that all shareholders that control more than 10 percent of the voting shares are judged ‘fit and proper’ to exercise such control. The provisions of AN 8 implement the so-called ‘Post BCCI’ directive of the EU and empower the Commissioner to reject an application where “the existence of a close link between a credit institution and another undertaking or individual prevents the effective exercise of his or the Banking Supervisor’s supervisory functions in relation to the institution.”  Although the BO does not require it, the Commissioner satisfies himself as to the source of the proposed capital of the applicant. A newly licensed bank is required to have an initial capital of at least €5 million. Banks also have to maintain a minimum ratio of their capital to their risk assets. (See CP 6.)  Under BO Section 23 (3) (e) controllers, shareholders, directors, and managers are required to



	<p>be ‘fit and proper’ for their respective positions. BO Section 23 (5) requires the Commissioner to have regard to the relevant person’s competence, probity, diligence, and soundness of judgment, as well as the interests of depositors generally in concluding whether a person is “fit and proper” to exercise the relevant role. “Probity” is further defined with reference to criminal record as well as evidence of unsound business practices and judgment, incompetence, and malpractice. In addition, the FSC issued a newsletter in 2002 with further guidance on the FSC’s fit and proper tests.</p> <p>Applications are required to be accompanied by financial projections and business plans, as well as the proposed staffing and governance arrangements. Although not specifically mentioned in the licensing criteria, the FSC’s ongoing supervisory requirements (on which see below) require banks to have appropriate internal controls and operating policies and procedures. These are therefore also required of new applicants. Although no new banks have recently been licensed, there have been changes of control and applications from new shareholders and the licensing requirements have been enforced on these occasions. BO allows the Commissioner to require additional information at any stage if he feels that necessary to assess the application fully. A licence can be cancelled if it is found that information provided in connection with an application proves to be misleading or untrue. (BO Section 64(1)). It is the practice of the Commissioner to request letters of comfort from shareholders indicating that they would be prepared to provide additional capital support if necessary.</p> <p>In the case of foreign banks, EU banks have the right under EU legislation (BCD enacted in Gibraltar by the BO) to establish within Gibraltar without additional authorization by the FSC. But the law does require the home supervisory authority to notify the FSC where an EU bank wishes to establish in Gibraltar. In the case of a non-EU bank, BO Section 18(4) requires that the Commissioner should assure himself that the home supervisor is content and he is also required to ensure that the home supervisor exercise effective supervision over the applicant. BO Section 18 does not explicitly require the consent of home supervisor of subsidiaries of non-EU banks, but it is the practice of the Commissioner to do so. In addition to the “fit and proper” tests, BO Section 23 (3) (f) requires that at least two persons direct the business of a bank. Application of this “four eyes” requirement ensures that directors and managers are competent to direct and manage the applicant bank. All banks are subject to continuous supervision, but new entrants would be particularly closely monitored.</p>
Assessment	Compliant
Comments	The proposal for a more extensive “approved persons” regime would apply the “fit and proper” tests to a wider range of individuals. By allowing appeal by affected persons, the Commissioner’s judgment would be more readily defensible.
<b>Principle 4.</b>	<b>Ownership</b>
	Banking supervisors must have the authority to review and reject any proposals to transfer significant ownership or controlling interests in existing banks to other parties.
Description	BO Section 53 provides that no person may become a “controller” as defined in BO Section 2 unless he has notified the Commissioner and the Commissioner has indicated he has no objection. This requirement applies to any person seeking to control more than 10 percent of the voting power of a bank. Similar requirements apply to shareholders exceeding 20, 33, and 50 percent thresholds. BO Section 54 empowers the Commissioner to object to a potential shareholder controller and BO Section 56 empowers the Commissioner to object to an existing controller if he is regarded as no longer fit and proper to hold that position. If a person nevertheless becomes a shareholder controller despite the Commissioner’s objections, he may be deprived of his voting rights. The Commissioner may also seek a court order requiring sale of the shareholding. BO Section 36 (3) requires licensed institutions to notify the Commissioner at least once a year of the names of each controller as defined in BO Section 2 and also of any close links as defined in AN 8.
Assessment	Compliant
Comments	

<b>Principle 5.</b>	<b>Investment Criteria</b> Banking supervisors must have the authority to establish criteria for reviewing major acquisitions or investments by a bank and ensuring that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Description	BO Section 40 prevents a bank from owning financial interests in any business or businesses in excess of 15 percent of the bank's capital in aggregate. There is no requirement for approval for any acquisition within this limit. AN 8 also prevents a bank from forming close links with any company such as to prevent effective supervision of the bank. Investments have to be reported in the bank's quarterly prudential returns.
Assessment	Compliant
Comments	Although the Commissioner has no power to vet acquisitions of investments by banks the limit of 15 percent effectively reduces any risk that might arise from a bank investing in inappropriate businesses. There are also tight limits on non-banking business that banks can engage on in their own name.
<b>Principle 6.</b>	<b>Capital Adequacy</b> Banking supervisors must set minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. For internationally active banks, these requirements must not be less than those established in the Basel Capital Accord.
Description	Gibraltar has implemented the minimum capital adequacy requirements set out in EU law in BCD. These follow closely the standards published by the Basel Committee and apply to all banks. The definition of capital and the risk weights also follow the Basel Committee's standards. A minimum capital ratio of 8 percent is therefore required by law. The legal requirements are set out in AN 1 and AN 2. The Commissioner has powers to apply capital adequacy ratios on a consolidated basis although no Gibraltar incorporated banks have significant subsidiaries requiring consolidation. If a bank fails to maintain the required minimum ratio, the Commissioner may impose conditions under BO Section 29 or 30. In severe cases, he could revoke the license under BO Section 64. Banks are required to report their capital ratios quarterly. Although the statutory minimum is 8 percent, banks are in fact also set "target" and "trigger" ratios above that figure which vary from bank to bank depending upon the Commissioner's assessment of the relative risk profile of the bank. Banks are required to maintain capital above the trigger at all times and to aim to exceed the target. A breach of the trigger would be followed by regulatory action. Banks are also required to exceed a minimum capital of €5 million at all times
Assessment	Compliant
Comments	In practice Gibraltar banks have ratios often substantially in excess of those required by the Commissioner. It is rare for any regulatory action to be required in this area.
<b>Principle 7.</b>	<b>Credit Policies</b> An essential part of any supervisory system is the independent evaluation of a bank's policies, practices, and procedures related to the granting of loans and making of investments and the ongoing management of the loan and investment portfolios.
Description	The FSC has developed over the last five years a risk assessment process which begins with the preliminary determination of the risks faced by the bank. On the basis of this preliminary assessment a supervisory strategy is set out involving on-site assessment of the principal risks faced by a bank. One such risk area is the granting of credit and assessment of this area would include high level controls, the delegation of authority to take credit risk, including by the making of loans. The FSC requires policy documents, approved by the board, in respect of all major risk area including credit. Implementation of these policies is tested on-site to establish the extent to which they are observed. Such testing could include examination of individual exposures, the taking of security, the classification of exposures, and the making of any necessary provisions.  As nearly all the banks in Gibraltar are part of foreign-controlled banking groups, Gibraltar operations are also subject to credit policies of the head office or parent bank and these invariably include monitoring by the head office or parent credit department. In addition,

	<p>internal audit functions would review and test application of the bank's internal controls and procedures.</p> <p>In practice, lending by Gibraltar banks is mainly high quality and well secured, and losses have been low. The main types of lending are residential mortgages and lending in connection with security transactions. In both cases such lending is secured by adequate collateral in the form of a mortgage over the relevant property or by a charge over marketable securities.</p> <p>In addition to assessment by the FSC's own staff, the FSC can commission work by reporting accountants, usually but not necessarily the bank's external auditors. The Commissioner has the power to require production of all relevant documentation so that on-site assessment is not impeded.</p> <p>The Commissioner requires that banks have prudent credit policies establishing delegated authorities for taking credit risk and tests during on-site work that these policies are observed. As noted above, such policies are in most cases also subject to control by head office/parent review functions. Bank credit policies must also include adequate information systems so that management can monitor the extent of credit risk and any deterioration in quality. Although all Gibraltar banks are owned or controlled by foreign institutions and shareholders, it is a requirement that all credit decisions must be taken in Gibraltar even though credit policies may well be established by head office or parent.</p> <p>Banks must report quarterly large exposures, defined as exposures in excess of 10 percent of capital as well as the ten largest exposures.</p>
Assessment	Compliant
Comments	<p>As most of the banks' principal line of business for non-residents is wealth management, credit is not the major function and credit risk is generally modest. However, some of the banks are significantly exposed to the real estate market both in Southern Spain and Portugal as well as in Gibraltar itself. Prices in both markets have been rising significantly in recent years. While maximum acceptable loan to value ratios in Spain are reported to be low (60-70 percent), in Gibraltar loan to value ratios approaching 100 percent are not uncommon. The fact that losses have not been encountered in the past is no guarantee that losses may not be incurred in the future. However, the main lending banks are well capitalized and the exposures are small in relation to group capital.</p>
<p><b>Principle 8. Loan Evaluation and Loan-Loss Provisioning</b></p> <p>Banking supervisors must be satisfied that banks establish and adhere to adequate policies, practices, and procedures for evaluating the quality of assets and the adequacy of loan-loss provisions and reserves.</p>	
Description	<p>BO Section 23(3) (d) requires banks to make adequate provision for bad and doubtful debts.</p> <p>The FSC does not prescribe loan classification and provisioning rules but banks are required to have statements of policy approved by their boards. GN 4 sets out what the FSC expects such policies to contain. On-site assessment will periodically review application of these policies to ensure that they meet the requirements set out in GN 4 which are based on U.K. practices. In addition loan valuations are subject to external audit. External auditors will apply either IFRS or U.K. practice as set out in U.K. statements of standard accounting practice. These are based on the principle that loans should be valued on the basis of what can realistically be expected to be recovered. These practices also provide that provisioning policies should include all exposures, including off-balance sheet exposures. Where a bank's policies are found to be inadequate the Commissioner requires that the policies be improved. If necessary he has powers to impose directions on the bank, for example, limiting its ability to extend credit. As there is no standardized classification and provisioning scheme, there can be no standardized reporting. Nonetheless, the Commissioner and his staff review the banks' annual audited financial statements and assess implementation of policies during on-site assessment. As loan quality is rarely an issue in Gibraltar this may well be done relatively infrequently. GN 4 requires banks to have adequate policies for the valuation and taking of security although no</p>

	rules are prescribed. Standard accounting rules prescribe that collateral be valued at net realizable value. There is no requirement that loans in arrears by specified numbers of days be treated in specified ways, although provisioning policies are expected to cover the treatment of arrears and provisioning arrangements for loans in arrears.
Assessment	Compliant
Comments	As credit exposures by several banks are limited to low risk lending, quality is in most cases very high, and thus does not receive intensive supervisory treatment in accordance with the risk based supervisory principles adopted by the FSC. It is expected that the directives adopting Basel II will require more extensive reporting of loan quality. There is no mandatory classification of loans by reference to the number of days payments are in arrears. In this regard Gibraltar follows the practice in the United Kingdom and other EU countries. Classification and provisioning are determined solely by reference to estimated recoverability.
<b>Principle 9.</b>	<b>Large Exposure Limits</b> Banking supervisors must be satisfied that banks have management information systems that enable management to identify concentrations within the portfolio, and supervisors must set prudential limits to restrict bank exposures to single borrowers or groups of related borrowers.
Description	Annex 1 of AN 3 defines a large exposure as being one in excess of 10 percent of the bank's capital. Exposures to two or more borrowers that are "closely related," as defined in paragraph 13 of AN 3, Annex 1, are treated as a single exposure for this purpose. "Closely related" is defined as including any case where the financial soundness of one borrower may affect the soundness of the other or where the same factor may affect the financial soundness of both borrowers. The aggregate of all large exposures must not exceed 800 percent of capital and the amount of any exposure is limited to 25 percent of capital. There are some exemptions which replicate those in the EU directive and include exposures to other banks and exposures collateralized by cash or securities issued by Organization for Economic Cooperation and Development (OECD) governments. All large exposures must be reported quarterly to the FSC. The adequacy of management information systems in identifying large exposures is assessed during on-site supervision and banks must furnish to the FSC policies agreed by the board dealing with risk concentrations. AN 3 requires observance of the limits on a consolidated basis although in practice no Gibraltar incorporated bank has subsidiaries significant enough to warrant consolidation. Banks now report exposures to individual countries and also report a broad sectoral breakdown of credit exposure. This is discussed during the supervisory process. Although there is provision for the Commissioner to allow the limits to be waived this power has never been used.
Assessment	Compliant
Comments	
<b>Principle 10.</b>	<b>Connected Lending</b> In order to prevent abuses arising from connected lending, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.
Description	AN 3 Annex 1 paragraph 15 contains a comprehensive definition of a "connected" exposure. It includes affiliated companies, shareholders, directors, management, staff, and close family members of the above. It also includes those with other connections. BO Section 2 defines an "associate" in wide terms, and the Commissioner has indicated in GN 2 he would deem a connection to exist where he judges there to be a connection even though the connection is not covered in the formal definition. AN 3 paragraph 16 requires any lending to connected parties to be carried out at arm's length and not on terms more favorable than those available to other borrowers. GN 2 requires that banks have policies in respect of any lending to connected borrowers and compliance with these is tested during on-site supervision. There is no specific requirement that connected loans in excess of a specified threshold be approved by the bank's board. The Commissioner has powers (AN 3, paragraph 18) to deduct connected lending from a bank's capital where the loan is for capital purposes or he considers that the transaction was not done at arm's length. Loans to connected parties must be reported quarterly and in aggregate must not exceed 25 percent of the bank's capital.

Assessment	Compliant
Comments	The definition of a connected party is wide and the Commissioner has not experienced cases where he believed a connection to exist which does not fall within the definition. And there is provision allowing the Commissioner to deem a connection to exist where it does not fall within the definition. There is no specific requirement that potential beneficiaries of a loan or their associates be barred from participating in the loan approval process but bank policies are expected to cover this aspect.
<b>Principle 11.</b>	<b>Country Risk</b> Banking supervisors must be satisfied that banks have adequate policies and procedures for identifying, monitoring, and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining appropriate reserves against such risks.
Description	With effect from the last quarter of 2005 FSC established a Supplementary Quarterly Return that requires that banks to submit an assets and liabilities break down by countries, differentiating exposures to banks and nonbanks. Before that, Quarterly Returns only had a regional break down of loans.  GN 4 “Provisioning Policy Statements” (December 2001) includes country or transfer risk as an issue that should be considered. The FSC risk based supervision framework also explicitly draws attention to country and transfer risk.
Assessment	Compliant
Comments	The countries to which Gibraltar banks have relevant exposures are mainly countries with low transfer and country risk.
<b>Principle 12.</b>	<b>Market Risks</b> Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor, and adequately control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposure, if warranted.
Description	Banks in Gibraltar do not have active treasuries or offer sophisticated products (they do not have a trading book or if they do it is minimal). All banks, with one exception, are subsidiaries or branches of well known bank groups (with competent home country banking supervision). So whenever a client needs a service or product carrying substantial market risk, their head offices would provide for them.  The FSC risk based framework considers market risk as a risk element under the risk group environment. And the risk management element under the risk group control includes risk identification, measuring, monitoring and control. So FSC should be able to evaluate this risk if banks start dealing in more developed treasury products.  The risk-based framework also includes as a topic to be assessed by the FSC, the positions in foreign exchange and the limits set by the banks themselves.  AN 7 introduced into Gibraltar Law the requirements of the EEC Directive 93/6/EEC (amended by 98/31/EC and 98/33EC) on the minimum capital requirements for credit institutions and investment firms for the market and other risks associated with their trading activities.
Assessment	Compliant
Comments	
<b>Principle 13.</b>	<b>Other Risks</b> Banking supervisors must be satisfied that banks have in place a comprehensive risk management process (including appropriate board and senior management oversight) to identify, measure, monitor, and control all other material risks and, where appropriate, to hold capital against these risks.
Description	The FSC risk based framework considers risk management, quality management and corporate governance as elements to be assessed. In relation to liquidity risk, the Quarterly Returns have a table with a maturities schedule with

	<p>net positions in each time period being accumulated. FSC does not impose across the board liquidity ratio norms, but specific mismatch ratios for each bank are monitored on a case by case basis. In many cases there is little or no liquidity risk in Gibraltar as this is managed at head office. But if a bank holds persistent and excessive mismatches the FSC could, under BO Sections 29 and 30, impose a condition on the license (and limit specific kind of operations). As stated before, these powers have never needed to be used, as banks have not experienced liquidity problems in the past.</p> <p>Liquidity risk is reported to the FSC on a quarterly basis; however, liquidity is a kind of risk that can escalate rather quickly, which is why banks worldwide would normally set up liquidity information systems that produce daily reports. Many Gibraltar banks do not conduct retail business neither are they active in taking deposits or giving loans to local customers, but those that do, should have at least internal daily reporting on liquidity, and the FSC should verify that these processes are observed and that liquidity positions are periodically tested against scenarios based on varying assumptions. This means that FSC should have different approaches as what to expect from liquidity management.</p> <p>AN 7 deals with interest rate risk arising from positions in the trading book and how to allocate capital for this type of exposure. The FSC risk based framework description of market risk includes interest rate risk in the banking book.</p> <p>Operational Risk is also a risk element under the risk group environment. The detailed description comprises exposures arising from processes and systems, exposures arising from change, exposures arising from firm structure, exposures arising from management and employees, risk appetite, and risk mitigation.</p>
Assessment	Largely compliant
Comments	The FSC should ensure that banks with high potential liquidity risk meet agreed limits or provide information about liquidity positions on a daily basis and that this can be verified by the Commissioner.
<b>Principle 14.</b>	<p><b>Internal Control and Audit</b></p> <p>Banking supervisors must determine that banks have in place internal controls that are adequate for the nature and scale of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding its assets; and appropriate independent internal or external audit and compliance functions to test adherence to these controls, as well as applicable laws and regulations.</p>
Description	<p>All banks, but one, in Gibraltar are branches or subsidiaries of major banking organizations with recognized corporate governance and internal controls. In most cases internal auditors come from head office and the external audit firm is the same for the whole group. Similarly, back office functions are performed in head offices.</p> <p>The Companies Ordinance and common law clearly establish the responsibilities of directors. Section 23 (3) (h) of the BO requires a bank to maintain at all times adequate accounting records and adequate systems of control of the business and records. GN 6 deals with the internal audit function in banks and communications between the internal audit function, the external auditors, and the FSC.</p> <p>The FSC risk-based framework has internal audit and quality of management as risk elements to be considered in the pre-assessment and in the assessment conducted by the FSC after an on-site visit.</p> <p>The Risk Based Self Assessment Questionnaire includes questions about internal control systems, management and organization. Section 23 (3) (f) of the BO 1992 introduces the concept of the four eyes principle, requiring that the business will be effectively directed by no</p>

	<p>fewer than 2 individuals.</p> <p>An ordinance for an Approved Persons Regime that deals with the approval and removal of key individuals (i.e., directors and managers) has been prepared.</p> <p>FSC has in past years, for several banks, called on Reporting Accountants to conduct focused reports on High Level Controls.</p>
Assessment	Compliant
Comments	<p>Boards would normally include local members with executive functions but also non resident members from head office without connection with the business being taken in Gibraltar, which gives them a certain level of independence.</p> <p>Internal audit is normally based in head office or parent which would have an internal audit committee overseeing all the operations of the group including those in Gibraltar.</p>
<b>Principle 15.</b>	<b>Money Laundering</b>
	<p>Banking supervisors must determine that banks have adequate policies, practices, and procedures in place, including strict “know-your-customer” rules that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.</p>
Description	<p>Banks have to comply with the EEC Directive (91/308/EEC) and with the Anti-money laundering Guidance Notes (AMLGN) part II on the prevention of the use of the financial system for criminal purposes. The directive was transposed into Gibraltar Law by virtue of the Drug Trafficking Offences Ordinance and the Criminal Justice Ordinance (CJO).</p> <p>The FSC risk-based framework considers Anti-Money Laundering Controls as a risk element to be assessed off-site and on-site. FSC can also appoint reporting accountants to do a more focused exam.</p> <p>AMLGN part IV sets the requirements in relation to KYC and record retention, part VI deals with recognition and reporting of suspicious transactions.</p> <p>Banks have to appoint a Money Laundering Reporting Officer. The role of the Money Laundering Reporting Officer is described in AMLGN part VI</p> <p>Bank managements have to inform the FSC of any material failings that could pose a threat to depositors; this would include fraud or other misfeasance.</p> <p>Section 2(3) and 3(5) of the CJO exempts the person making a disclosure of suspicious transactions from any liability.</p> <p>The CJO and AMLGN require that institutions have training programs for their staff. FSC verifies the existence of these programs during its on-site visits as part of the risk assessment process and with the self assessment risk questionnaire.</p> <p>Section 20 of the CJO imposes an obligation upon the FSC to make disclosures to GFIU of suspicious transactions.</p>
Assessment	Compliant
Comments	Concurrently compliance with the FATF 40 plus 9 was assessed by a specialist team.
<b>Principle 16.</b>	<b>On-Site and Off-Site Supervision</b>
	<p>An effective banking supervisory system should consist of some form of both on-site and off-site supervision.</p>
Description	<p>During 2003 FSC launched a revised version of the new risk based supervision framework originally introduced in 2001 after the first IMF assessment. Each supervisory period has four phases: pre-assessment, assessment, formal feedback and risk mitigation. The grading methodology uses six evaluation factors known as “Risk Groups”: Financial Soundness and Capital, Environment, Business Plan, Controls, Organization and Management. Each risk group is graded (from 1 to 5); the grades are multiplied by fixed weights and by the impact score for the bank to obtain the final risk profile. The result of the assessment will determine the intensity of the supervisory program. The on-site visits are part of the assessment phase after the bank has completed a Self Assessment Questionnaire and the preliminary assessment has been done. A visit would normally consist of meetings with senior management and heads</p>

	<p>of significant units. Discussions would focus on controls, strategy, organization structure and risk management. Sample testing would be conducted if they are not adequately covered by internal audit.</p> <p>The FSC can also rely on reporting accountants (BO Section 60), which are normally the external auditors, to conduct on-site examinations (i.e., money laundering, credit risk, information technology, private banking, high level controls). A trilateral meeting is held between the bank management, the reporting accountants, and the FSC to discuss the findings. Off-site supervision is conducted based on analysis of the information collected in the quarterly reports, annual financial reports, management letters, internal audit reports etc. The off-site reports include trend analysis and peer group reviews.</p> <p>The FSC has attained ISO 9001:2000 certification for its quality management process. BO 1992 Section 60 enables the FSC to gain access to all types of records and information within a bank including reports submitted to the board by the internal and external auditors. BO 1992 Section 86A imposes confidentiality provisions on the information obtained under the ordinance but provides for suitable gateways for disclosure.</p>
Assessment	Compliant
Comments	
<b>Principle 17.</b>	<b>Bank Management Contact</b>
	Banking supervisors must have regular contact with bank management and a thorough understanding of the institution's operations.
Description	In addition to the visits under the risk-based assessment program, regular "prudential" visits are made to the banks, during which organization, management, strategic planning, budgets, financial performance and product and market developments are discussed. These meetings take place about every nine months with licensed institutions and once a year for EU branches. The FSC risk-based framework considers management quality and corporate governance as elements to be assessed.
Assessment	Compliant
Comments	
<b>Principle 18.</b>	<b>Off-Site Supervision</b>
	Banking supervisors must have a means of collecting, reviewing, and analyzing prudential reports and statistical returns from banks on a solo and consolidated basis.
Description	<p>The Banking (Accounts Directive) Regulation 1997 specifies the method of accounting on both a solo and consolidated basis. This regulation complies with EU directives on those matters.</p> <p>The Banking Supervisory Returns are submitted quarterly to the FSC within 14 days of the end of the period to which it relates. The Return is required to be signed by a Senior Manager and another authorized official of the bank. The FSC can commission a reporting accountants report on the control systems including the completion of reports or even impose conditions on the license, if a pattern of reporting errors is detected.</p> <p>The quarterly returns include information from the balance sheet, income statements, non performing loans, provisions and supervisory ratios.</p> <p>BO Section 59 (b) and AN 7 (the Post BCCI Directive: Close Links) enable FSC to seek information about related companies and subsidiaries.</p> <p>The FSC has an analytical system for processing the information contained in the quarterly returns, the data has the same reporting date and is in GBP enabling the cross referencing of data across the banking system.</p>
Assessment	Compliant
Comments	
<b>Principle 19.</b>	<b>Validation of Supervisory Information</b>



Banking supervisors must have a means of independent validation of supervisory information either through on-site examinations or use of external auditors.	
Description	<p>The FSC risk-based framework explicitly includes an on-site visit that is focused on those areas assessed as significant. FSC also has the possibility to require examination by reporting accountants. Normally reporting accountants would be the external auditors. The appointment of external auditors for the auditing of financial statements is subject to approval by the Commissioner.</p> <p>BO Section 60 deals with the “power to obtain information and require the production of documents.”</p> <p>The FSC discusses with the Gibraltar Society of Chartered and Certified Accountancy Bodies (GSCCAB) areas of common interests in particular those related to auditing and supervision of banks.</p>
Assessment	Compliant
Comments	
<b>Principle 20.</b>	<b>Consolidated Supervision</b>
An essential element of banking supervision is the ability of the supervisors to supervise the banking group on a consolidated basis.	
Description	<p>None of the banks licensed in Gibraltar have any overseas operations or subsidiaries, so that in no case is FSC the Home Supervisor of a banking group. FSC has legal authority to supervise banks on a consolidated basis, AN 4 is the implementation in Gibraltar of the Banking Consolidated Directive (2000/12/EC) and AN8 is the implementation of the so called Post-BCCI directive (95/26/EC).</p> <p>AN 4 section 24 states that when the licensee belongs to a group for which the Commissioner determines consolidation would be inappropriate (i.e., where the preponderance of the group business comprises industrial and insurance business) the Commissioner will require the parent institution and its other subsidiaries to supply him with any data or information which he considers relevant to the purpose of supervising the licensee.</p> <p>BO Section 59 extends the power of the FSC to subsidiaries, parents or other undertakings or persons falling under Article 56 of the Directive 2000/12/EC (i.e. a credit institution, a financial holding company, a financial institution, an ancillary banking services undertaking, etc.).</p>
Assessment	Compliant
Comments	
<b>Principle 21.</b>	<b>Accounting Standards</b>
Banking supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with consistent accounting policies and practices that enable the supervisor to obtain a true and fair view of the financial condition of the bank and the profitability of its business, and that the bank publishes on a regular basis financial statements that fairly reflect its condition.	
Description	<p>BO Section 23 (3) (g) and (h) impose as a criterion for licensing and as an on-going requirement that each bank maintains all proper accounts and records as well as adequate systems of controls over its business and records. Quarterly returns should be submitted to the FSC within 14 days of the end of the period to which it relates, but FSC has no capacity to apply penalties in case of late returns.</p> <p>EU-listed companies are now required to report using IFRS and this applies to most Gibraltar banks. However, in some case Gibraltar subsidiaries may still be using earlier U.K. accounting standards</p> <p>The Banking (Accounts Directive) Regulations 1997, section 13, require banks to publish audited financial statements.</p> <p>BO Sections 46, 46A and 47 establishes auditors’ immunity from civil liability, enabling the</p>

	<p>auditor to communicate freely with the FSC in relation to the affairs of a licensee without fear of breach of any professional obligation to which they may otherwise have been subject.</p> <p>The Banking (Accounts Directive) Regulations 1997 Schedule 1, Chapter 1, Part III covers the valuation rules to be applied for the financial statements of banks. These rules followed the EU directives on the publication of financial statements for credit institutions.</p> <p>BO Section 62 (2) gives power to the Commissioner to appoint and retain an auditor.</p> <p>The FSC regularly publishes an abstract of key banking statistics obtained from quarterly returns.</p>
Assessment	Compliant
Comments	
<b>Principle 22.</b>	<b>Remedial Measures</b>
	Banking supervisors must have at their disposal adequate supervisory measures to bring about timely corrective action when banks fail to meet prudential requirements (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the ability to revoke the banking license or recommend its revocation.
Description	<p>The Commissioner can take a range of remedial actions that goes from an oral request, a formal written request, an order to refrain from taking some course of action (BO Section 62 (1)), varying a license by imposing, amending or revoking any condition on the license (BO Sections 29 and 30) and finally cancel the license (BO Section 64).</p> <p>Even though a regime of penalties, including fines on banking officers, is usual in other jurisdictions, it must be admitted that the absence of such powers has not so far been a constraint on the FSC's ability to ensure compliance with supervisory requirements.</p>
Assessment	Compliant
Comments	The Government of Gibraltar has prepared a draft of an ordinance establishing an Approved Persons Regime that will deal with the approval and removal of key individuals (i.e., directors and managers), and give the Commissioner the power to apply sanctions to individuals.
<b>Principle 23.</b>	<b>Globally Consolidated Supervision</b>
	Banking supervisors must practice global consolidated supervision over their internationally active banking organizations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organizations worldwide, primarily at their foreign branches, joint ventures, and subsidiaries.
Description	None of the banks licensed in Gibraltar have any overseas operations or subsidiaries, so that in no case is FSC the Home Supervisor of a banking group. However, FSC does have the legal authority to supervise banks on a consolidated basis should the need arise.
Assessment	Compliant
Comments	
<b>Principle 24.</b>	<b>Host Country Supervision</b>
	A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved, primarily host country supervisory authorities.
Description	<p>So far FSC has not had the need to establish contact with any other supervisor as a home supervisor of a Gibraltar bank, but if the need were to arise, FSC is legally prepared to be a home supervisor, including the capacity to refuse applications for a license (and even cancel a license) where the existence of a close link between a credit institution and another undertaking or individual prevents the exercise of the supervisory functions.</p> <p>The FSC has the legal authority to supervise banks on a consolidated basis. AN 4 is the implementation in Gibraltar of the Banking Consolidated Directive (2000/12/EC) and AN8 is the implementation of the so called Post-BCCI directive (95/26/EC).</p>
Assessment	Compliant
Comments	

<b>Principle 25.</b>	<p><b>Supervision Over Foreign Banks' Establishments</b></p> <p>Banking supervisors must require the local operations of foreign banks to be conducted with the same high standards as are required of domestic institutions and must have powers to share information needed by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.</p>
Description	<p>BO Section 18 establishes that in the case of an application by an applicant which is a subsidiary of a holding company or which is controlled by a controller of a European institution, the Commissioner shall consult the relevant supervisory authority of the European institution before determining whether to grant or refuse an application.</p> <p>In the case of an applicant whose head office is in a country outside the European Economic Area (EEA), the Commissioner has to be satisfied as to the nature and scope of the supervision exercised by that authority. The relevant supervisory authority in that country has to inform the Commissioner that it is satisfied with respect to the prudent management and overall financial soundness of the applicant.</p> <p>The FSC as a host supervisor allows supervisory authorities of EEA states to exercise powers similar to those of the Commissioner in relation to the prudential supervision of Gibraltar banks that are part of a conglomerate being supervised by an EEA supervisor.</p>
Assessment	Compliant
Comments	In practice, the FSC has developed extensive contacts with home supervisory authorities responsible for banking groups operating in Gibraltar.

Table 2. Summary Compliance of the Basel Core Principles

Core Principle	C <sup>1/</sup>	LC <sup>2/</sup>	MNC <sup>3/</sup>	NC <sup>4/</sup>	NA <sup>5/</sup>
1. Objectives, Autonomy, Powers, and Resources					
1.1 Objectives	X				
1.2 Independence		X			
1.3 Legal framework	X				
1.4 Enforcement powers	X				
1.5 Legal protection		X			
1.6 Information sharing	X				
2. Permissible Activities	X				
3. Licensing Criteria	X				
4. Ownership	X				
5. Investment Criteria	X				
6. Capital Adequacy	X				
7. Credit Policies	X				
8. Loan Evaluation and Loan-Loss Provisioning	X				
9. Large Exposure Limits	X				
10. Connected Lending	X				
11. Country Risk	X				
12. Market Risks	X				
13. Other Risks		X			
14. Internal Control and Audit	X				
15. Money Laundering	X				
16. On-Site and Off-Site Supervision	X				
17. Bank Management Contact	X				
18. Off-Site Supervision	X				
19. Validation of Supervisory Information	X				
20. Consolidated Supervision	X				
21. Accounting Standards	X				
22. Remedial Measures	X				
23. Globally Consolidated Supervision	X				
24. Host Country Supervision	X				
25. Supervision Over Foreign Banks' Establishments	X				

<sup>1/</sup> C: Compliant.

<sup>2/</sup> LC: Largely compliant.

<sup>3/</sup> MNC: Materially non-compliant.

<sup>4/</sup> NC: Non-compliant.

<sup>5/</sup> NA: Not applicable.