

FINANCIAL STABILITY FORUM

Report of the Working Group on Offshore Centres

5 April 2000

FINANCIAL STABILITY FORUM

Preface

At its inaugural meeting on 14 April 1999, the Financial Stability Forum (FSF) established an ad hoc Working Group on Offshore Financial Centres. Mr. John Palmer, Superintendent of Financial Institutions, Canada, chaired the Group.

The Group's report was submitted to the Financial Stability Forum for discussion at its meeting in Singapore on 25-26 March 2000. The Financial Stability Forum welcomed the report and endorsed its recommendations.

As Chairman of the Forum, I have transmitted the report to the G-7 Ministers and Governors. I have also forwarded it to the G-20 Ministers and Governors, and to the heads of the IMF and the World Bank, with the request that the reports be forwarded through Executive Directors to Ministers and Governors in anticipation of the April meetings of the International Monetary and Financial Committee and the Development Committee.

The Forum urged national authorities, international financial institutions, and the international groupings and other agents referred to in this report to consider promptly the Group's recommendations and to take the necessary actions to implement them.

Andrew Crockett

Chairman

Report of the Working Group on Offshore Financial Centres

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I. Executive Summary

1. The FSF Working Group on Offshore Financial Centres (OFCs) was convened to consider the significance of OFCs in relation to financial stability in all its aspects. This report lays out the Group's findings, the key issues that have been identified with respect to OFCs, and its recommendations.
2. In conducting its work and developing its recommendations, the Group has drawn on OFC-related work undertaken by international financial institutions, standard-setting bodies and national authorities, the available analytic work on OFCs, and has considered recent episodes of financial crises and the role of OFCs. It has met with major internationally active financial institutions, industry associations, professional financial advisors, regulators and supervisors¹, and OFC representatives, both individually and as a group. In addition, the Group has conducted a formal survey on OFCs of supervisors from both onshore and offshore jurisdictions. A description of the survey and a summary of its results are provided in Annexes D, and E, respectively. The survey's recipients and OFC non-respondents are included in the main report (paragraph 29 and Table 1).
3. OFCs, to date, do not appear to have been a major causal factor in the creation of systemic financial problems. But OFCs have featured in some crises, and as national financial systems grow more interdependent, future problems in OFCs could have consequences for other financial centres. The significant growth in assets and liabilities of institutions based in OFCs and the inter-bank nature of the offshore market, together with suspected growth in the off-balance sheet activities of OFC-based institutions (about which inadequate data exist), increase the risk of contagion.
4. Problematic OFCs (i.e., OFCs that are unable or refuse to adhere to international supervisory standards, resulting in weak supervisory practices or little or no co-operation and transparency) allow financial market participants to engage in regulatory arbitrage and constitute weak links in the supervision of an increasingly integrated financial system. The "loopholes" presented by some OFCs hinder efforts to improve the global supervisory financial system through the implementation of international standards more broadly, frustrating collective efforts to reduce overall exposures to global financial instability, and creating a potential systemic threat to the financial system.
5. Not all OFCs are the same. Some are well supervised and prepared to share information with other centres, and co-operate with international initiatives to improve supervisory

¹ The term 'supervision' is generally understood to apply to government oversight of the banking and insurance industry, while the similar term for the securities industry is 'regulator'. However, for ease of reference, in this Report, the terms 'supervisor' and 'supervision' are understood to include 'regulator' and 'regulation'.

practices. But the Survey carried out by the Working Group indicated that there are serious concerns by onshore supervisors about the quality of supervision in, and degree of co-operation provided by, some OFCs.

6. Weakness in supervision and lack of co-operation by some OFCs together lead to two types of problems, which can be inter-related, in the oversight of the international financial system: ***prudential concerns***, relating to the scope for effective supervision of internationally active financial intermediaries; and ***market integrity concerns***, relating to the effectiveness of international enforcement efforts in respect of illicit activity and abusive market behaviour.
7. The Group has highlighted a number of key specific ***prudential and market integrity concerns in relation to OFCs, including:***
 - Cross-border co-operation on information exchange, timely access to information, and the ability to verify information with OFCs are all critical to conduct effective supervision, as well as to engender the international co-operation necessary to enhance financial stability and fight financial fraud.
 - The quality of the underlying supervision in an OFC is also of key importance. The impact of weak supervision can be amplified in cases where consolidated supervision is ineffectively exercised by the home supervisor of a financial institution with operations in an OFC.
 - The lack of due diligence with which financial institutions can be formed in many OFCs can facilitate inappropriate structures, or inappropriate ownership, that can impede effective supervision.
 - The lack of availability of timely information on beneficial ownership of corporate vehicles (companies, trusts, partnerships and other vehicles with limited liability) established in some OFCs can thwart efforts directed against illegal business activities.
 - The lack of comprehensive and timely data on OFCs' financial activity impedes effective monitoring and analysis of capital movements.

In the course of its work, the Group has also identified some ***general prudential issues*** affecting onshore and offshore jurisdictions alike. Among these are:

- International standards for insurance activities may not be sufficient, in particular concerning regulatory capital requirements.
 - There are no internationally accepted standards for reinsurance.
8. ***Enhanced acceptance and implementation of international standards by OFCs would address many of the concerns raised about some OFCs.*** International standards of regulation and supervision, disclosure and information sharing have been developed, which address issues of the kind associated with some OFCs from both a prudential and market integrity perspective.

9. The Group's recommendations can be summarised as follows:

Recommendation 1: *An assessment process for OFCs' adherence to international standards*

The Group recommends that an assessment process (as described in Box 6) for assessing OFCs' implementation of relevant international standards be put in place.

Recommendation 2: *Responsibility for an assessment process*

The Group recommends that the FSF request the IMF take responsibility for developing, organising and carrying out an assessment process for OFCs.

The Group considers that the FSF should facilitate the efforts of the IMF (with the World Bank as appropriate) as the IMF organises assessments of the implementation of standards by OFCs. This would include providing moral suasion to encourage OFCs to participate in the assessment process, calling on FSF members to make available appropriate resources to the IMF to help it carry out the assessment process and to OFCs to assist them in improving their supervisory systems, and encouraging major financial centres to promote a wider acceptance of international standards.

Recommendation 3: *Priority OFC jurisdictions for assessment*

The Group recommends that priority for assessment be placed on those OFCs where procedures for supervision and co-operation are in place but where there is substantial room for improvement (i.e., OFCs that would fall into Group II, see paragraph 30). Priority could also be given to those jurisdictions with the most significant financial activity.

Recommendation 4: *Standards for priority implementation and assessment by OFCs*

The Group recommends that the international standards relating to cross-border co-operation and information sharing, essential supervisory powers and practices, and customer identification and record keeping, be assigned priority in implementing and assessing OFCs' adherence to standards in the more immediate term. The specific standards identified by the Group are listed in Annex H (which should not be seen as exhaustive), although adherence to all relevant international standards should be the ultimate goal.

The Group considers that assessments should also take into account the capacity of supervisors and law enforcement authorities to obtain, on a timely basis, information about the beneficial ownership of corporate vehicles registered in their jurisdiction and the ability to share that information with foreign authorities.

Recommendation 5: *Incentives to enhance OFCs' adherence to international standards*

The Group recommends that a menu of incentives—market, disclosure-type, membership, provision of assistance, supervisory, and other incentives identified in Box 7—be considered for application by the appropriate bodies or groupings in relation to an OFC's adherence to the relevant international standards.

The Group also recommends that the FSF discuss the IMF's conclusions arising from the proposed assessment process, and foster efforts, including by supervisors of major financial centres, that would be most effective if undertaken collectively in the application of incentives to enhance OFCs' adherence to relevant international standards.

Recommendation 6: *Actions for onshore jurisdictions*

The Group encourages onshore jurisdictions to engage in more effective consolidated supervision in the banking and insurance sectors, recognising the important responsibilities of home country supervisors, so that the ability of offshore activities to escape oversight is reduced. Similarly, the Group encourages securities supervisors to enhance their oversight of securities firms to improve their understanding of relevant offshore activities.

Recommendation 7: *Insurance standards development*

The Group encourages the IAIS in its work to develop best practices for reinsurance and its supervision, as well as with respect to developing specific supervisory standards on solvency and consolidated supervision for all insurance activities.

Recommendation 8: *Assessment methodologies for standards*

The Group encourages those bodies that have not already done so to develop methodologies for assessing observance with their respective standards, or to complete their efforts, as soon as possible, in consultation with the IMF and World Bank and others.

Recommendation 9: *Corporate vehicles and beneficial ownership*

The Group recommends that appropriate international fora be asked to explore the issue of developing mechanisms to prevent the misuse of corporate vehicles. These mechanisms should assure that supervisors and law enforcement authorities are able to obtain, on a timely basis, information on beneficial ownership of corporate vehicles and the sharing of that information with foreign authorities.

Recommendation 10: *Data reporting by OFCs*

The Group strongly encourages OFCs with significant financial activities to report financial data to the BIS for its quarterly publication on International Banking Statistics with the requested breakdown (distinguishing between debt securities and other claims), and on a timely basis. The Group notes that such action could be considered as an indicator of an OFC's willingness to co-operate within the international financial system. As necessary, OFCs should seek the available technical assistance from national authorities and international financial institutions to improve their statistical practices and capacity.

Recommendation 11: *Co-ordination of OFC-related initiatives*

The Group recommends that the published version of this Report be formally transmitted by the FSF to the various international groups that are concerned with the activities of OFCs. In addition, the Group recommends the development of a mechanism to assist the international community in keeping abreast of progress on OFC-related initiatives.

10. To facilitate the review of progress in implementing these recommendations, the Group suggests that a brief report be prepared by the FSF Secretariat for the Fall 2001 meeting of the Forum.

II. Introduction and terms of reference

11. Financial institutions, investors, and commercial enterprises seek out the particular attractions offered by offshore financial centres (OFCs), resulting in significant capital flows into and out of entities established in OFCs. In addition, participants in illegal activities utilise certain OFCs. Consequently, OFCs have become the focus of considerable attention by financial market participants, and by supervisors, regulators, and law enforcement authorities. Concerns about OFCs have intensified in the context of initiatives undertaken by the international community to strengthen financial systems, in response to financial crises.
12. As a result, in April 1999 the FSF created a Working Group to consider the significance of OFCs in relation to global financial stability.² The OFC Working Group was asked:
 - *to consider the uses of OFCs and the possible role they have had or could play in posing threats to the stability of the financial system;*
 - *to evaluate the adherence of OFCs with internationally accepted standards and good practices; and*
 - *to make recommendations, including to enhance problematic OFCs' observance of international standards.*³
13. The Group has focused on the issue of financial stability in all its aspects. There was a general recognition that significant work has been, and continues to be, undertaken in other fora (e.g., the Financial Action Task Force (FATF) on Money Laundering), and that the Group should avoid duplication. Accordingly, the Group has aimed to build on existing initiatives, where appropriate, and is recommending new initiatives only where it is apparent that gaps exist.
14. The Group reported on its progress to the FSF in September 1999. The FSF broadly endorsed the framework adopted by the Group and its tentative areas for recommendations. This report lays out the Group's findings, the key issues that have arisen in relation to OFCs, and its recommendations for addressing these issues.

² The Group's terms of reference are provided in Annex A. The members of the Working Group are provided in Annex B.

³ Subsequent to its meeting in Paris in September 1999, the FSF also established a task force, chaired by Andrew Sheng, Chairman of the Hong Kong Securities and Futures Commission, to examine ways of fostering the implementation of international standards relevant to the strengthening of financial systems more broadly.

III. Previous or ongoing work relevant to the Group's mandate ⁴

15. OFC issues have been of concern for some time within the official sector. Considerable work has been undertaken by the *Basel Committee on Banking Supervision (BCBS)*, *International Association of Insurance Supervisors (IAIS)*, *International Organisation of Securities Commissions (IOSCO)*, *Financial Action Task Force (FATF)*, *United Nations (UN)*, *Organisation for Economic Co-ordination and Development (OECD)*, and *G-7 Finance Ministers*. Much of this work has focused on the development and assessment of standards or best practices in the areas of banking and insurance supervision, securities market regulation, corporate governance, money laundering, and information exchange, all of which has relevance for OFCs.⁵ In addition, the *United Kingdom* has reviewed the financial regulation of its Crown Dependencies⁶ (“Review of Financial Regulation in the Crown Dependencies” known as the Edwards Report) and the *United States* has addressed issues arising out of the Long-Term Capital Management episode (“Hedge Funds, Leverage, and the Lessons of Long-Term Capital Management”, Report of the President’s Working Group).
16. The Group took note of the ongoing FATF work on non-cooperative jurisdictions (“*FATF on Money Laundering: Report on Non-Cooperative Countries and Territories*”), and on the work being undertaken by the *OECD* on tax competition (“Harmful Tax Competition: An Emerging Global Issue”) as well as bribery and corruption (“Convention on Combating Bribery of Foreign Public Officials in International Business Transactions”).
17. The Group also drew on the available analytical work on OFCs (see Box 1).

⁴ A selected bibliography is provided in Annex C.

⁵ The term ‘supervision’ is generally understood to apply to government oversight of the banking and insurance industry, while the similar term for the securities industry is ‘regulator’. However, for ease of reference, in this Report, the terms ‘supervisor’ and ‘supervision’ are understood to include ‘regulator’ and ‘regulation’.

⁶ A joint review by the United Kingdom and Overseas Territories governments is currently being undertaken with respect to financial supervision in those Overseas Territories with significant OFCs (Anguilla, Bermuda, British Virgin Islands, Cayman Islands, Montserrat, and Turks and Caicos Islands). Under the framework set by the 1989 Ordinance (i.e., the need to match UK standards of supervision when implementing EU legislation), Gibraltar’s financial regulation was reviewed in 1997; its banking supervision was reviewed again in 1998; and a follow-up review of investment services is slated for 2000/01.

Box 1. Available Analytical Work on OFCs

The Group has considered the available analytical work on OFCs, which generally focuses on the causes of their growth and is based mainly on case studies of a wide range of OFCs. The main contributing factor identified for the historical growth of offshore banking and OFCs was the imposition of increased regulation (reserve requirements, interest rate ceilings, restrictions on the range of financial products, capital controls, financial disclosure requirements, high effective tax rates) in the financial sectors of industrial countries during the 1960s and 1970s.¹ OFCs that have been successful in attracting non-resident financial activity usually offer some clear advantage, such as lower tax rates or a less onerous regulatory burden, to those who participate in international capital markets. Financial centres that offer a high degree of secrecy to users of their services and that do not co-operate with law enforcement officials making legitimate requests for information play a key role in criminal activity in OFCs.²

A recent IMF staff study on offshore banking indicates that OFC banks' cross-border assets and liabilities grew by over 6 percent annually during 1992-1997 to around US\$5 trillion. More than 70 percent of OFC banks' cross-border assets and almost 60 percent of cross-border liabilities were vis-à-vis other banks, at the end of 1997.³ The study highlights the inter-bank nature of the offshore market and the risk that, in the event of financial distress, contagion is likely.

To a large extent, however, the available analytical work has concentrated on the banking sector and relatively little attention has been paid to other areas of the financial sector. Complicating the ability to undertake more in-depth study of OFCs is the absence of good data with which to examine the activities of financial institutions in OFCs. While the BIS publishes stock data covering the consolidated international claims of reporting banks on individual countries, there are no comprehensive data on financial flows. Further, the magnitude of derivative activity is unknown.

¹ For example, the growth of London as the largest offshore banking centre has been linked directly to regulations imposed on the U.S. banking sector: capital controls implemented through the Interest Equalisation Tax of 1964, the Foreign Credit and Exchange Act of 1965, cash reserve requirements on deposits imposed in 1977 and a ceiling on time deposits in 1979. By establishing foreign branches to which these regulations did not apply, U.S. banks were able to operate in more cost-attractive environments.

² See *Financial Havens, Banking Secrecy and Money Laundering*, UN Office for Drug Control and Crime Prevention, May 1998.

³ See Luca Errico and Alberto Musalem, *Offshore Banking: An Analysis of Macro-and Micro Prudential Issues*, IMF Working Paper (WP/99/5), January 1999. The figures include offshore banking activities in Bahamas, Bahrain, Cayman Islands, Hong Kong SAR, Japan, Luxembourg, Singapore, United Kingdom, and the United States.

IV. The Group's approach

18. An OFC is not easily defined. Any jurisdiction can be considered “offshore” to the extent that it is perceived as having a more favourable economic regime than another, e.g., low corporate tax rates, light regulation, special facilities for company incorporation, or highly protective secrecy laws. While OFCs are commonly perceived to be small island states, a number of advanced countries have succeeded in attracting very large concentrations of non-resident business by offering economic incentives either throughout their jurisdiction or in special economic zones.
19. The term “offshore” carries with it in some quarters a perception of dubious or nefarious activities. There are, however, highly reputable OFCs that actively aspire to and apply internationally accepted practices, and there are some legitimate uses of OFCs. OFCs are not homogeneous and there is a wide variety of practices found in them. Hence, there is a strong aversion by some jurisdictions to being listed as an offshore centre given the risk of “guilt by association”. Also, it is recognised that there may be jurisdictions not formally thought of as OFCs that are more problematic in terms of global financial stability than some OFCs. In this light, coming up with a precise definition and listing of offshore centres was not considered the most fruitful use of the Group's efforts. Instead the Group focused on the characteristics of OFCs (see Box 2) and considered the uses of OFCs.

Box 2. Characteristics of Offshore Financial Centres

Offshore financial centres (OFCs) are not easily defined, but they can be characterised as jurisdictions that attract a high level of non-resident activity. Traditionally, the term has implied some or all of the following (but not all OFCs operate this way):

- Low or no taxes on business or investment income;
- No withholding taxes;
- Light and flexible incorporation and licensing regimes;
- Light and flexible supervisory regimes;
- Flexible use of trusts and other special corporate vehicles;
- No need for financial institutions and/or corporate structures to have a physical presence;
- An inappropriately high level of client confidentiality based on impenetrable secrecy laws; and
- Unavailability of similar incentives to residents.

Since OFCs generally target non-resident clients, the volume of non-resident business substantially exceeds the volume of domestic business. For most OFCs, the funds that are on the books of the OFC are invested in the major international money-centre markets.

20. ***OFCs are used by*** ⁷:

- International companies, to maximise profits in low tax regimes.
- International companies, to issue securitised products through special purpose vehicles.
- Individuals and companies, to protect assets from potential claimants.
- Investors (individuals, investment funds, trusts etc.), to minimise income and withholding taxes and to avoid disclosing investment positions.
- Financial institutions with affiliates in OFCs, to minimise income and withholding tax and to avoid regulatory requirements in the “onshore” jurisdictions in which they operate.
- Financial institutions, to assist customers in minimising income and withholding tax.
- Insurance companies, to accumulate reserves in low tax jurisdictions and to conduct business in responsive regulatory environments.
- Criminals and others, to launder proceeds from crime through banking systems without appropriate checks on the sources of such funds and to use local secrecy legislation as a means of protection against enquiries from law enforcement and supervisory authorities (including foreign authorities), and/or to commit financial fraud.

Some of these activities also happen in other jurisdictions and the fact that they take place does not necessarily mean that the OFC authorities approve of such practices (i.e., money laundering, financial fraud).

21. ***Uses of OFCs cover a wide range of activities with some more benign than others*** (See Box 3).

⁷ Although taxation figures prominently in the list below, the Group has not addressed taxation issues as they are currently under discussion by the OECD.

Box 3. Examples of Uses of Offshore Financial Centres (OFCs)

Offshore Banking Licences: A multinational corporation sets up an offshore bank to handle its foreign exchange operations or to facilitate financing of an international joint venture. An onshore bank establishes a wholly owned subsidiary in an OFC to provide offshore fund administration services (e.g., fully integrated global custody, fund accounting, fund administration, and transfer agent services). The owner of a regulated onshore bank establishes a sister, “parallel” bank in an OFC. The attractions of the OFC may include no capital tax, no withholding tax on dividends or interest, no tax on transfers, no corporation tax, no capital gains tax, no exchange controls, light supervision, less stringent reporting requirements, and less stringent trading restrictions.

Offshore Corporations or International Business Corporations (IBCs): IBCs are limited liability vehicles registered in an OFC. They may be used to own and operate businesses, issue shares or bonds, or raise capital in other ways. IBCs may be set up with one director only. In some cases, residents of the OFC host country may act as nominee directors to conceal the identity of the true company directors. In some OFCs, bearer share certificates may be used. In other OFCs, registered share certificates are used, but no public registry of shareholders is maintained. In many OFCs, the costs of setting up IBCs are minimal and they are generally exempt from all taxes. IBCs are a popular vehicle for managing investment funds.

Insurance companies: A commercial corporation establishes a captive insurance company in an OFC to manage risk and minimise taxes. An onshore insurance company establishes a subsidiary in an OFC to reinsure certain risks underwritten by the parent and reduce overall reserve and capital requirements. An onshore reinsurance company incorporates a subsidiary in an OFC to reinsure catastrophic risks. The attractions of an OFC in these circumstances include favourable income/withholding/capital tax regime and low or weakly enforced actuarial reserve requirements and capital standards.

Special Purpose Vehicles: One of the most rapidly growing uses of OFCs is the use of special purpose vehicles (SPVs) to engage in financial activities in a more favourable tax environment. An onshore corporation establishes an IBC in an OFC to engage in a specific activity. The issuance of asset-backed securities is the most frequently cited activity of SPVs. The onshore corporation may assign a set of assets to the offshore SPV (e.g., a portfolio of mortgages, loans, credit card receivables). The SPV then offers a variety of securities to investors based on the underlying assets. The SPV, and hence the onshore parent, benefit from the favourable tax treatment in the OFC. Financial institutions also make use of SPVs to take advantage of less restrictive regulations on their activities. Banks, in particular, use them to raise Tier I capital in the lower tax environments of OFCs. SPVs are also set up by non-bank financial institutions to take advantage of more liberal netting rules than faced in home countries, reducing their capital requirements.

Asset Management and Protection: Wealthy individuals and enterprises in countries with weak economies and fragile banking systems may want to keep assets overseas to protect them against the collapse of their domestic currencies and domestic banks, and outside the reach of existing or potential exchange controls. If these individuals also seek confidentiality, then an account in an OFC is often the vehicle of choice. In some cases, fear of wholesale seizures of legitimately acquired assets is also a motive for going to an OFC. In this case, confidentiality is very important. Also, many individuals facing unlimited liability in their home jurisdictions seek to restructure ownership of their assets through offshore trusts to protect those assets from onshore lawsuits. Some OFCs have legislation in place that protects those who transfer property to a personal trust from forced inheritance provisions in their home countries.

Tax Planning: Wealthy individuals make use of favourable tax environments in, and tax treaties with, OFCs, often involving offshore companies, trusts, and foundations. There is also a range of schemes that, while legally defensible, rely on complexity and ambiguity, often involving types of trusts not available in the client's country of residence. Multinational companies route activities through low tax OFCs to minimise their total tax bill through transfer pricing, i.e., goods may be made onshore but invoices are issued offshore by an IBC owned by the multinational, moving onshore profits to low tax regimes.

Tax Evasion There are individuals and enterprises who rely on banking secrecy and opaque corporate structures to avoid declaring assets and income to the relevant tax authorities.

Money Laundering: Individuals and enterprises moving money gained from illegal transactions or fraudulent market activities seek maximum secrecy to avoid criminal and supervisory investigation.

22. To improve further its understanding of OFCs and the key issues that arise across the spectrum of the financial sector, as well as to formulate recommendations for implementation, members of the Group met with major internationally active financial institutions, industry associations, professional financial advisors, supervisors, and representatives of OFCs, to gain their impressions.^{8 9} In addition, the Group invited a wide range of OFC representatives for a full day session in November 1999 to brief them on the work of the FSF generally, on the preliminary findings of the Group and its tentative areas for recommendations, and to solicit their feedback and suggestions.¹⁰
23. The Group also conducted a formal survey on OFCs of supervisors from both onshore and offshore jurisdictions in the areas of banking, insurance and securities. The aim of the survey was to gather preliminary information, based on supervisors' impressions, about various OFCs' adherence to international standards of financial supervision and co-operation, which could be used as the basis for identifying priority jurisdictions for a subsequent more formal program of assessment. A description of the survey, including the questionnaires that were sent to onshore and offshore supervisors, is provided in Annex D.
24. In addition, the Group commissioned a study on the reinsurance industry and OFCs. This work was based on background analytical research on the industry as well as interviews with representatives from most major reinsurance companies, insurance supervisors in jurisdictions with significant insurance activity, and insurance rating agencies.

V. Summary of Group's findings

25. Based on information gathered, as well as the Group's discussions, the Group's findings can be summarised as follows:
26. ***Problems with OFCs, which arise principally from inadequate supervision in OFCs, can hinder supervision in "onshore" centres, posing a potential threat to the global financial system. Problems include:***
 - Inadequate due diligence in incorporation and licensing of new financial institutions and shell companies (IBCs and SPVs) owned by affiliates of financial institutions.

⁸ The discussions were conducted on the basis of confidentiality, resulting in frank and candid expressions of views. Interviews were conducted with senior executives of over 30 financial institutions (banks, insurance companies, broker-dealers, investment fund managers), industry associations, accounting firms, and law firms from 11 countries. In addition, discussions were held with 18 supervisors from 8 economies.

⁹ The Chairmen of the Offshore Groups of Banking Supervisors and of Insurance Supervisors as well as the head of an OFC's financial services commission attended part of the Group's second meeting. In addition, members of the Group's Secretariat met with representatives of the Bahamas, Barbados, Bermuda, and the Cayman Islands.

¹⁰ The Group invited 29 jurisdictions to participate in a full day session of its meeting in Singapore in November 1999, which 13 representatives attended. The Chairman of the Offshore Group of Insurance Supervisors attended as a representative of the members of that group.

- Inadequate disclosure rules.
- Inadequate knowledge of activities of financial institutions based in OFCs, including identity of depositors and counterparties, and “onshore” lending activities.
- Lack of resources to conduct effective supervision of branches or subsidiaries of foreign financial institutions by local supervisors.
- Absence of political will to improve the quality of supervision.
- Lack of co-operation with “onshore” supervisors.
- Excessive secrecy laws, which impede sharing of information.

As a result,

- Home country regulatory requirements can be thwarted, and effective supervision frustrated.
 - The ability to rely on OFC supervisors by home supervisors is often limited, or not possible.
 - Investigation by securities regulators of securities violations can be impeded.
 - Tracing by law enforcement authorities of proceeds of financial crime can be frustrated.
27. ***Implementation of standards varies considerably across OFCs, with some making serious efforts to adhere to internationally accepted standards, while others make little or no effort, or actively use supervisory laxity as a means of promoting their attractiveness to investors and customers.*** Some representatives of OFCs pointed out that while some OFCs wish to improve their adherence, a shortage of skilled resources, especially in smaller jurisdictions can be an obstacle. Other supervisors noted that, in some OFCs, an absence of political will has impeded efforts to improve adherence to international standards.
 28. The results of the survey on OFCs conducted by the Group broadly confirmed these initial impressions. Some OFCs are highly regarded. However, many respondents from onshore jurisdictions expressed serious concerns about the quality of supervision in, and degree of co-operation provided by, a number of OFCs. Further, the responses by offshore supervisors revealed a number of OFCs in which a relatively—and probably excessively—small number of professional staff is responsible for the oversight of a large number of financial service providers (see Annex E for a summary description of the survey results).
 29. A summary list of the jurisdictions surveyed is provided in Table 1 (below). A good response¹¹ to the survey was received from supervisors of major financial centres with 27 out of the 30 jurisdictions surveyed responding (i.e., 90 percent). The response from

¹¹ In most jurisdictions, more than one entity from that jurisdiction was identified and requested to complete the questionnaire. Some survey recipients did not respond as supervision was not in their purview. If at least one recipient of the questionnaire from a jurisdiction responded to the survey, then that jurisdiction was included as having responded.

financial centres with significant offshore activities was more moderate with 25 out of the 37 jurisdictions surveyed responding (i.e., 68 percent). The cover letter accompanying the survey indicated that the names of those OFCs that participated in the survey as well as those that did not would be published.¹² No responses were received from any supervisor in the following jurisdictions with significant offshore activities as of 15 March 2000: Antigua, Cook Islands, Costa Rica, Lebanon, Marshall Islands, Nauru, Nevis, Niue, St. Kitts, St. Vincent, Seychelles, and Turks and Caicos Islands.¹³

**Table 1. Survey on Offshore Centres of Supervisors and Regulators:
Recipients**

Major Financial Centres (30 jurisdictions)		
Argentina	India	Norway
Australia	Ireland 1/	Portugal
Belgium	Israel	Singapore 1/
Brazil	Italy	South Africa
Canada	Japan	Spain
Chile	Korea	Switzerland 1/
Denmark	Luxembourg 1/	Sweden
France	Malaysia 1/	Thailand
Germany	Mexico	United Kingdom
Hong Kong 1/	Netherlands	United States
Financial Centres with Significant Offshore Activities (37 Jurisdictions)		
Andorra	Cyprus	Netherlands Antilles
Anguilla	Gibraltar	Nevis 2/
Antigua 2/	Guernsey	Niue 2/
Aruba	Isle of Man	Panama
Bahamas	Jersey	St Kitts 2/
Bahrain	Lebanon 2/	Saint Lucia
Barbados	Liechtenstein	St Vincent 2/
Belize	Macau	Samoa
Bermuda	Malta	Seychelles 2/
British Virgin Islands	Marshall Islands 2/	Turks & Caicos Islands 2/
Cayman Islands	Mauritius	Vanuatu
Cook Islands 2/	Monaco	
Costa Rica 2/	Nauru 2/	

1/ Supervisors in these jurisdictions received questionnaires for onshore and offshore supervisors.

2/ No response was received to the questionnaire from any of the recipients of the survey in the indicated jurisdiction. However, in the case of Antigua, St. Kitts and Nevis, and St. Vincent, which are members of a currency board, a response was received from the monetary authority responsible for the domestic banking system, but not the supervision of offshore activities, in these jurisdictions.

¹² In addition to the initial survey request, a reminder notice was also faxed at the end of January 2000 to those that had not responded. Further, the secretariat of the Group has attempted to follow-up individually by phone with contacts in all jurisdictions that had not responded.

¹³ In the case of Antigua, St. Kitts and Nevis, and St. Vincent, which are members of a currency board, a response was received from the monetary authority responsible for the domestic banking system, but not the supervision of offshore activities, in these jurisdictions.

30. ***The quality of supervision and the degree of co-operation by a jurisdiction is a basis for suggested grouping of OFCs.*** The first group (Group I) would be jurisdictions generally viewed as co-operative, with a high quality of supervision, which largely adhere to international standards. The second group (Group II) would be jurisdictions generally seen as having procedures for supervision and co-operation in place, but where actual performance falls below international standards, and there is substantial room for improvement. The third group (Group III) would be jurisdictions generally seen as having a low quality of supervision, and/or being non-co-operative with onshore supervisors, and with little or no attempt being made to adhere to international standards.
31. ***The review of recent episodes of financial instability indicate that, in some cases, the failure or the inability of home prudential supervisors to conduct effective consolidated supervision of their banks doing business offshore impacted their domestic banking system.***¹⁴ In Thailand during the early and mid 1990s, the build up in use of Bangkok International Banking Facilities (BIBFs) to finance foreign currency lending domestically (“out-in lending”), which was largely unhedged, increased the banking system’s vulnerability to foreign exchange and maturity risks. In the banking crises in Venezuela (1994) and Argentina (1995), the failure of parent banks to oversee effectively the activities of offshore establishments exacerbated the weakness of the domestic financial sector in the wake of external shocks.
32. In the case of Long Term Capital Management (LTCM), incorporation of the hedge fund in an OFC appears to have been motivated by tax considerations rather than an attempt to avoid regulatory requirements, given that hedge funds are not subject to prudential regulation in the United States or elsewhere.¹⁵
33. ***Examination of the reinsurance industry in OFCs as well as elsewhere yielded little evidence to suggest a significant threat to systemic financial stability.*** While one or more large reinsurance company failures could have a significant, adverse impact on the primary insurance sector, due to the extended time in which insurance claims are typically paid out, it is unlikely to lead to the kind of liquidity crisis that can follow from an equivalent large bank failure. Further, the capital and reserves of the industry appear large relative to all but extremely low probability, extremely high damage, natural catastrophies. Nevertheless, there are some features of the reinsurance industry that raise potential prudential-type problems. The market has become increasingly concentrated, and there has been a significant increase in the number of firms domiciled in OFCs.

¹⁴ See “Offshore Banking: An Analysis of Macro-and Micro Prudential Issues”, Luca Errico and Alberto Musalem, IMF Working Paper (WP/99/55), January 1999.

¹⁵ See “Hedge Funds, Leverage and the Lessons of Long-Term Capital Management”, Report of the President’s Working Group on Financial Markets, United States, April 1999.

34. ***There is a need to co-ordinate OFC-related initiatives.*** Concern was expressed—and not just by OFC representatives—about the proliferation of initiatives on OFCs and their sometimes overlapping subject matters.

VI. Key issues identified for financial stability

35. Based on the Group's review of the available literature and previous work, its interviews with financial intermediaries, information provided by onshore supervisors, and the findings articulated above, the Group has identified the following key issues for global financial stability going forward.
36. ***OFCs, to date, do not appear to have been a major causal factor in the creation of systemic financial problems. But OFCs have featured in some crises and as national financial systems grow more interdependent, future problems in OFCs could have consequences for other financial centres.*** The significant growth in assets and liabilities of institutions based in OFCs and the inter-bank nature of the offshore market, together with suspected growth in the off-balance sheet activities of OFC-based institutions (about which inadequate data exist), increase the risk of contagion.
37. Problematic OFCs (i.e., OFCs that are unable or refuse to adhere to international supervisory standards, resulting in weak supervisory practices or little or no co-operation and transparency) allow financial market participants to engage in regulatory arbitrage and constitute weak links in the supervision of an increasingly integrated financial system. The “loopholes” presented by some OFCs hinder efforts to improve the global supervisory financial system through the implementation of standards more broadly, frustrating collective efforts to reduce overall exposures to global financial instability, and creating a potential systemic threat to the financial system.
38. The activities of OFCs are of concern where they attract significant volumes of financial activity, while failing to abide by international standards of supervision and information disclosure. This concern is amplified where the failure relates to an inability or unwillingness to meet international standards of co-operation in cross-border information exchange and enforcement. Problematic OFCs also add complexity and opaqueness to corporate structures and financial transactions, increasing the overall level of risk.
39. Weaknesses in supervision and international co-operation together lead to two types of problems, which can be inter-related, in the oversight of the international financial system. They raise ***prudential concerns*** relating to the supervision of internationally active financial intermediaries, with implications for stability in international financial markets. And they raise ***market integrity*** concerns, relating to the effectiveness of international enforcement efforts in respect of illicit activity and abusive market behaviour (See Box 4).

Box 4. Prudential and Market Integrity Concerns

The Group has highlighted two types of problems related to some OFCs:

Prudential Concerns

Prudential issues concern the supervision of internationally active financial intermediaries. Weak supervision, lack of co-operation and poor transparency in OFCs can impair the detection of excessive risk exposures and inadequate risk-management systems. When large international financial players¹ or a large number of international financial intermediaries² are active in problematic OFCs, these risks may assume systemic proportions. This is of particular concern where OFCs compete to attract a concentration of institutions in specific financial industries to locate in their jurisdictions by offering lax supervisory treatments.

Market Integrity Concerns

Market integrity concerns arise chiefly from the favourable secrecy, trust and asset protection regimes found in certain OFCs, compounded by the lack of transparency and the difficulties that home law enforcement agencies and regulators face in securing their co-operation. These features potentially allow such OFCs to attract money of criminal origin, tax fraud, tax evasion, and other illicit financial activities, and thwart the application of international financial and economic sanctions. Weaknesses in supervision and international co-operation can also impair detection and enforcement actions with regard to market-abusive activities, especially in securities markets. There can be a higher risk of unauthorised or illegal financial activities in onshore jurisdictions if those activities are performed via entities registered in problematic OFCs.

In general, these problems of market integrity may not pose immediate risks to international financial stability. However, in hampering international market surveillance and law enforcement, they ultimately erode the integrity of international financial markets and represent a potential systemic threat to global financial systems.

¹ For example, Bank of Credit and Commerce International (BCCI) failed in June 1991 with significant disruption to many national financial markets around the world. BCCI had a complex structure with sister companies in London and the Cayman Islands under a non-banking holding company incorporated in Luxembourg. Subsequently, the Basel Committee and European Union decided that it was important in the future to give supervisors powers to prohibit corporate structures that are deliberately designed to impede effective consolidated supervision of international banking groups. Supervisors were advised to ensure that “mind and management” of the group reside in its principal place of incorporation.

² The over-concentration of any significant financial industry in a jurisdiction with lax supervision increases the likelihood of systemic risk to the international financial system.

40. The key issues that relate to both ***prudential*** and ***market integrity concerns*** are:
- ***Cross-border co-operation on information exchange, timely access to information, and the ability to verify information are all critical to conduct effective supervision, as well as to engender the international co-operation necessary to enhance financial stability and fight financial fraud.*** The Group does not suggest that these are issues for all OFCs, and notes that similar problems arise with some onshore jurisdictions. Like many onshore jurisdictions, some OFCs are willing to provide necessary information on the basis that the information will be treated confidentially and used only for supervisory and law enforcement purposes. However, some OFCs make overly narrow interpretations of use and confidentiality provisions, thereby impeding effective cross-border co-operation.
 - ***The quality of the underlying supervision of an OFC is of key importance.*** If a jurisdiction has a weak supervisory regime or allocates insufficient resources to implement it, its ability to co-operate effectively will be compromised, whatever its willingness. ***Weak supervision undermines effective consolidated supervision by the home supervisor of institutions with operations in an OFC. This weakness is***

amplified in cases where consolidated supervision is exercised by the home supervisor, but is not applied effectively.

- ***As recent events have demonstrated, the international financial system is increasingly interdependent. Deliberately (and blatantly) lax supervisory practices in one part of the system are a potential source of weakness to the entire system. It would be short sighted, therefore, not to address such practices.*** The many jurisdictions, including some OFCs, that are actively and effectively applying accepted international standards are at risk of losing business to the lax jurisdictions. More generally, the strengthening of the financial system through the adoption of international standards may be impeded if there are sources of leakage from the “standards net”.
- ***The lack of due diligence with which financial institutions can be formed in many OFCs can facilitate inappropriate structures, or inappropriate ownership, that can impede effective supervision.*** For example, the establishment of parallel banking structures can render consolidated supervision of the banking group ineffective. Some supervisors do not have the ability to require changes in corporate structures or to otherwise ensure that the banks are adequately supervised to address this issue.
- ***The lack of availability of timely information on beneficial ownership of corporate vehicles (companies, trusts, partnerships and other vehicles with limited liability) established in some OFCs can thwart efforts against illegal business activities.*** There are some international standards concerning the disclosure of information about corporate vehicles (e.g., the FATF Recommendations require financial institutions to know the identity of their customers, including corporate customers, before opening accounts). However, there is no international standard or standard-setting body for corporate formation. As a result, practice varies widely across jurisdictions, both onshore and offshore, on arrangements whereby authorities can obtain information about the beneficial ownership of corporate vehicles registered in their jurisdiction and the powers to share that information with foreign authorities. In addition, ‘flight clauses’ which are a permitted feature of trusts in certain jurisdictions, when coupled with excessive secrecy, undercut the efficacy of international supervisory and law enforcement co-operation.
- ***There is a need for co-ordination across the various initiatives related to OFCs.*** Problems of overlap and duplication across initiatives should be avoided to ensure timely and effective results, and to maximise the use of onshore and offshore resources.

41. The key issues that relate to *prudential concerns* are:

- ***The lack of comprehensive and up-to-date data on OFCs' financial activity impedes effective monitoring and analysis of capital movements.*** The available banking stock data indicate roughly US\$1.4 trillion in deposits by reporting banks vis-à-vis OFCs at end June 1999.¹⁶ Even for banking activity, however, this is likely an underestimate as the available data are incomplete, lack timeliness and do not include off-balance sheet activities, which are believed to be substantial.¹⁷ Discussions with financial market participants suggest that the magnitude of flows through OFCs is significant and increasing. Considerable efforts have been undertaken in recent years by national authorities and international financial agencies to improve statistics on debt and capital flows. Most onshore jurisdictions with significant financial activities provide, on a voluntary basis, relevant and timely data to the BIS for its Locational Statistics. Not all OFCs with significant financial activities report to the BIS, and many that do report with long delays and without the requested breakdown of their claims between debt securities and other claims.

There are also some *general prudential issues* affecting onshore and offshore jurisdictions alike. Among these are:

- ***International standards for insurance activities may not be sufficient.*** While not unique to OFCs, concern was expressed that the regulatory capital requirements for insurance may not be adequate in some jurisdictions. Moreover, there is no internationally accepted regulatory capital standard for insurance companies equivalent to the Basel Capital Accord for deposit taking institutions.¹⁸
- ***There are no internationally accepted standards for reinsurance.***¹⁹ ²⁰ Nor is there agreement on the way in which reinsurers should be supervised. A number of major reinsurance companies based in OFCs and in industrialised countries are either not supervised or are only lightly supervised against widely varying local standards.
- ***While not unique to OFCs, wind-up or work out situations can be complicated when multiple jurisdictions are involved.*** The Group took note of, and encourages,

¹⁶ See Bank for International Settlements (BIS) Quarterly International Banking Statistics, November 1999. In addition to the quarterly locational data, the consolidated international claims of BIS reporting banks on a set of OFCs are currently published on a semi-annual and annual basis by the BIS.

¹⁷ The FSF Working Group on Capital Flows has also identified this issue in their work.

¹⁸ The IAIS has established a Solvency Subcommittee to address this issue. An issues paper, which will serve as the foundation for the Subcommittee's future work on developing specific supervisory standards on solvency, was presented at the IAIS Annual Conference in December 1999. Work has begun on one of the building blocks—defining what constitutes capital.

¹⁹ The IAIS has established a Reinsurance Subcommittee: to develop and recommend an IAIS standard of best practices for evaluating the reinsurance cover of primary insurers and the security of their reinsurers; to discuss and possibly develop IAIS principles for areas in which the insurance supervisor should have authority and control over reinsurance companies; and to produce a database of reinsurers.

²⁰ The Offshore Group of Insurance Supervisors has developed guidelines on reinsurance for its members.

the work being undertaken in various international fora on the development of sound practices in the area of insolvency.²¹

42. The prudential and market integrity issues highlighted above have been of concern to the supervisory community for some time in respect to both onshore and offshore centres. This has led in some cases to the development of standards of best practices in a number of areas by relevant standard-setting bodies, in particular with respect to cross-border co-operation and information sharing. Many of the market participants and supervisors interviewed and surveyed, as well as some OFC representatives, stressed the importance of adoption by OFCs of international standards and best practices in reducing the prudential and market integrity concerns raised by certain OFCs.
43. *The Group considers that the enhanced acceptance and implementation of international standards of supervision, disclosure and information sharing could minimise problems created by some OFCs and address many of the key issues as described above.*

VII. International standards and assessing adherence

44. Under its terms of reference, the Group was tasked with reviewing progress made by OFCs in implementing international standards and making recommendations, including some directed at improving OFCs' adherence to standards. In addressing these tasks, the Group took note of the significant progress in developing standards in recent years by key standard-setting bodies (See Box 5). However, only limited progress has been made in assessing adherence to internationally accepted standards.²²
45. The FATF has made the most headway on assessing adherence to its 40 Recommendations to combat money laundering through a process of both self-assessment and mutual evaluation.²³ Early progress is also being made with respect to evaluating adherence to the Basel Core Principles, initially through a self-assessment exercise and now under the auspices of the IMF and World Bank. The IAIS and IOSCO have used self-assessment techniques for assessing observance with their standards. Overall, the Group regards progress as limited, both in terms of coverage and impact.

²¹ For example, the United Nations Commission of International Trade Law (UNCITRAL) has developed a *Model Law on Cross-Border Insolvency*. The World Bank is developing with other multilateral and professional organisations an initiative to develop guidelines for sound insolvency law in developing countries. Drawing on the advice of a wide range of insolvency experts as well as other international organisations, the IMF has published a report on *Orderly and Effective Insolvency Procedures*.

²² See Annex F for a more detailed account of the progress in developing and assessing observance of a selection of relevant standards.

²³ The first cycle of FATF mutual evaluations (MEs) of FATF members began in 1992 and aimed essentially at determining whether legislation on money laundering was in place. The second round has gone more deeply into the problem of "effective" implementation of the FATF 40 Recommendations. The country reports that serve as the basis for the MEs are strictly confidential and are not circulated outside the FATF membership, but a summary is provided in the FATF Annual Report, which is publicly available.

The Group also considers that self-assessments by themselves are unlikely to be fully effective. Self-assessments without external verification can suffer from a lack of rigour, or credibility, or both. Even when based on well-defined standards, it can be difficult to verify the accuracy of self-assessment.

46. In part, the lack of progress in assessing standards reflects the difficulty of the task and the time it takes to carry out assessments. Most standards are in the form of fairly general principles and require significant expertise, both with respect to the standard itself as well as an economy's actual practices, to make adequate assessments of adherence. In this regard, assessments are facilitated when there are well-defined criteria (methodologies) as assessment tools.

Box 5. International Standards

Over the last several years, the international community has emphasised the development and promulgation of internationally accepted standards or codes of good practice to address issues of enhanced transparency, effective co-operation, and adequate supervision, which can contribute to a strengthening of the financial system. Allowing market participants to compare information on potential counterparties, both public and private, against agreed benchmarks should lead to better-informed lending and investment decisions.

Adherence to well-defined standards can also improve the quality of economic management in the countries that adopt them, as well as enhance transparency and good governance. More generally, increased globalisation and complexity of financial markets have heightened the need for all jurisdictions to implement standards to ensure effective oversight and integrity of the global financial system.

Progress has been achieved in developing standards by standard-setting bodies. While not limited to, progress has been made in the following areas:

- The IMF has developed the Special Data Dissemination Standard, a Code of Good Practices on Fiscal Transparency and a Code of Good Practices on Transparency in Monetary and Financial Policies. For fiscal policy transparency, a manual for assessing compliance has been developed, and a supporting paper, setting out good practices with respect to transparent monetary and financial policies, is under preparation.
- The Basel Committee on Banking Supervision (BCBS) has developed the *Basel Core Principles for Effective Banking Supervision* and, working with other international organisations and a broad range of supervisors, criteria for assessing adherence to the Core Principles (“methodology”) have been issued. The IMF and the World Bank have begun assessing jurisdictions’ adherence to the Basel Core Principles. The BCBS has also developed recommendations, with the Offshore Group of Bank Supervisors (OGBS), on the *Supervision of Cross-border Banking*. A survey of adherence with the recommendations covering most jurisdictions has been conducted as well as a survey of BCBS members on specific issues encountered in members’ cross-border supervision efforts. The BCBS has reconvened the Cross-border Banking Working Party (which includes participants from the OGBS) to consider whether further initiatives are required.
- The International Organisation of Securities Commissions (IOSCO) has developed a set of *Objectives and Principles of Securities Regulation*. The Assessment Methodology has been prepared in co-operation with the World Bank, the IMF and the regional development banks. Self-assessments of IOSCO members under the Assessment Methodology are expected to be completed shortly. In addition, IOSCO has passed a *Resolution on Principles for Record Keeping, Collection of Information, Enforcement Powers and Mutual Co-operation* to improve the enforcement of securities and futures laws. Self-assessments of IOSCO members’ ability to share information with one another have been completed.
- The International Association of Insurance Supervisors (IAIS) has developed a set of *Insurance Supervisory Principles* as well as the *Insurance Concordat*. Development of a methodology for assessing adherence is underway.
- The Joint Forum has developed *Principles for Supervisory Information Sharing* with respect to supervisory information exchange particularly in the context of cross-sector financial institutions residing in financial conglomerates.
- The OECD has developed *Principles for Corporate Governance*. Jointly with the World Bank, work is underway to advance the Principles via the Global Forum and regional roundtables. The OECD has also developed the legally binding *Convention on Combating Bribery of Foreign Officials in International Business Transactions* as well as non-binding recommendations to fight corruption. It is now considering more specific recommendations to prevent the use of an OFC in bribery and corrupt transactions. The OECD has established 19 recommendations to counter harmful tax practices, including the spread of tax havens, and is engaged in a dialogue to gain global acceptance of these recommendations.
- The Financial Action Task Force (FATF) has developed the FATF 40 Recommendations aimed at combating money laundering. A process of mutual evaluation against the Recommendations is well established. In addition, an ad hoc group is addressing the issue of non co-operative jurisdictions. Criteria for defining and a process for identifying such jurisdictions, and countermeasures to protect economies against money laundering have been agreed. Identification of jurisdictions that meet these criteria has begun, with a view to listing non-co-operative jurisdictions and persuading them to change their detrimental rules and practices.

In addition, the G-7 has agreed on *Ten Key Principles on Information Sharing and Disclosure* and *Ten Key Principles for the Improvement of International Co-operation Regarding Financial Crime and Regulatory*

Abuse.

47. As noted in Section VI, enhancing acceptance and implementation of international standards by OFCs would address many of the prudential and market integrity concerns raised by some OFCs. To be in a position to review systematically OFCs' adherence to international standards, an assessment framework is needed. To develop such a framework, the Group has focused on addressing the following questions:
- who should be responsible for the assessment process;
 - how should an assessment process be organised and what are its resource considerations;
 - what jurisdictions should be assessed as a priority;
 - whether the results of assessments should be disclosed;
 - what are the standards against which jurisdictions would be assessed; and
 - what consequences could emanate from a satisfactory (or unsatisfactory) assessment and who would apply them.
48. In the Group's view, the *key elements of an assessment framework* would include the following.
49. **Responsibility for an assessment process.** The Group considers that an appropriate body or group needs to take responsibility to develop and organise an effective assessment process, to monitor progress, and to produce tangible results within a reasonable timeframe. Its responsibilities would also entail ensuring that independent assessments—as part of the process—are conducted against appropriate standards, and being accountable for the overall integrity and effectiveness of the process.
50. The desired characteristics of the appropriate body that would have responsibility for the assessment process can be summarised as follows:
- **Authority:** A body that is sufficiently well regarded that its management and judgements will carry weight, particularly by those considering actions against non-adherent jurisdictions.
 - **Expertise:** Although it will not necessarily have all the resources in-house to carry out assessments, it will need to be able to identify and tap the necessary resources from appropriate bodies for assessments to be done.
 - **Acceptability:** It will need to be capable of engendering the co-operation and support of both onshore and offshore centres.
 - **Speed:** It will need to be capable of getting an assessment process underway relatively quickly.
51. Against these criteria, the Group has considered the merits of a range of options for who could take responsibility for an assessment of OFCs, including the offshore groups, the standard setters themselves, the IMF/World Bank, the FSF, and a new and independent body, as well as variations across this spectrum.

52. The Group considers that the IMF is well placed to organise and supervise, in collaboration with the World Bank and by accessing expertise of standard-setting bodies as appropriate, a process of assessing OFCs' adherence to international standards. The IMF is gaining relevant experience with the World Bank through the *Financial Sector Assessment Program (FSAP)*, which provides input for the IMF's surveillance function (through its *Financial Sector Stability Assessments (FSSAs)*). Also, it is already dealing with jurisdictions on the disclosure of the results of assessments through the IMF's *Reports on the Observance of Standards and Codes (ROSCs)*. These initiatives accord with the IMF's Article IV process, which has international support as the appropriate centre for surveillance of implementation of standards, and organising assessments of standards, as part of the IMF's general remit to strengthen the international financial system.
53. The Group recognises that there are several operational and possibly complex aspects that the IMF would need to consider and address in taking up this responsibility. In particular, several OFCs are not IMF members. However, the Group notes that there are precedents for the IMF to engage with non-members, or "non-sovereign" entities.²⁴ The assessment process envisaged by the Group is voluntary, while designed so as to encourage OFCs to co-operate. In this context, the Group considers that it would be possible for the IMF to carry out such assessments, provided the necessary political will exists to do so.
54. Briefly, the Group envisages that the IMF would develop the assessment process, organise and manage the assessments, including assembling the assessment teams with the appropriate expertise, and the reporting of the assessment conclusions. It would liaise with other bodies working on relevant issues, so as to avoid duplication and effectively use relevant information in the assessment process. It would help OFCs upgrade supervisory systems drawing from other bodies as appropriate and carry out follow-up assessments to monitor progress in implementation. As experience is gained, improvements would be undertaken to the assessment process.
55. The Group envisages that the FSF would have an important role with respect to an assessment process in recommending that a process be put in place and in encouraging the IMF to develop and operate it. The FSF would facilitate the efforts of the IMF (with the World Bank as appropriate) as the IMF organises assessments of the implementation of standards by providing moral suasion to encourage OFCs to participate in the assessment process, by calling on its members to make available appropriate resources to the IMF to help it carry out an assessment process and to OFCs to assist them in improving their supervisory systems, and by encouraging major financial centres to promote a wider acceptance of international standards. In addition, the FSF would

²⁴ IMF Article IV consultation discussions are held with for example Hong Kong SAR and the Netherlands Antilles; technical assistance is, and has been, provided by the IMF to some non-members (e.g., Cayman Islands).

discuss the IMF's conclusions, and foster effective dialogue among its members about the application of incentives and other consequences based on the assessment process (see paragraph 68).

56. ***Assessment process and resources.*** The Group considers that a successful standards implementation program for OFCs will have most, and probably all, of the following inter-related components:
- A public commitment by the OFC to implement the relevant standards.
 - A plan for meeting the commitment, with clearly defined and measurable intermediate targets.
 - Public disclosure of the implementation plan, and of progress against plan targets.
 - An independent (or outside) assessment against standards, to assist identification of areas where implementation could be enhanced, to help identify technical assistance needs, and to help assess progress at key stages during the implementation period.
 - Public disclosure of the results of the independent assessment.
 - Provision of external technical support, as needed, at appropriate stages during the implementation process.
57. Self-assessment would be a feature within the program, which could facilitate co-operation by offshore centres, minimise the call on external resources, and help ensure that some actions can begin swiftly. However, the traditional weaknesses of self-assessments will need to be addressed (see paragraph 45). Outside assessment as an integral part of the process should help to encourage diligence and candidness in the preparation of self-assessments.²⁵ The involvement of outside expertise that can provide impartial advice and judgement in helping jurisdictions to prepare self-assessments could also foster more credible self-assessments.
58. Drawing on the elements above, a staged program is elaborated in Box 6 for achieving confirmed observance with international standards. It starts with an easily measured event—a declaration of intent. It ends with an outside opinion that the jurisdiction is in adherence. By addressing the task in stages, it recognises that implementation and assessment can be a time-consuming, resource-intensive activity. It also minimises the need for significant outside resources at the beginning, while ensuring that some actions can take place immediately. Moreover, it recognises that for some international standards, some jurisdictions will require time to put in place revised legislation and procedural changes needed to achieve full adherence.
59. Some jurisdictions may opt to move immediately to the outside assessment stage, and should be encouraged to do so.²⁶ The ultimate goal is full observance of all international

²⁵ It could be expected that self-assessments would be undertaken with more frankness and be considered more reliable, if it was known that such an assessment would be subject to outside scrutiny.

²⁶ In addition, some jurisdictions have already undergone, or are undergoing a form of outside assessment, such as the UK Crown Dependencies and Overseas Territories.

standards pertinent to the activities in the relevant jurisdictions. However, for some OFCs, the initial plan would be to adhere to a set of international standards for priority implementation and assessment articulated in paragraphs 66 and 67 with a subsequent plan to adhere to all pertinent international standards.

60. Disclosure of findings is a key feature of an assessment program. The purposes of disclosure are to demonstrate progress in standards implementation, to foster peer pressure, to improve market functioning, and to help form the basis on which incentives (both positive and negative) could be applied by supervisory authorities and market participants. The program outlined by the Group includes a strong presumption that the results of both assisted self-assessments and independent assessments would be disclosed. To help foster such disclosure, the latter should include a “right of reply” by the jurisdiction assessed.

Box 6. An Assessment Program for OFCs

The assessment program envisaged by the Group would have the following stages:

Stage 1. Announcement by a jurisdiction that it is committed to:

- Implementing the pertinent international standards;
- Following the staged assessment process as set out below, including disclosure aspects; and
- Completing the second step (assisted self-assessment) by a certain date.

Stage 2. Undertaking the assisted self-assessment

- The assistance could entail a single expert provided by relevant international financial institutions or international supervisory organisations. Appropriate steps would have to be taken to ensure that whatever the source of assistance, the advice received and judgement applied was reasonably objective and consistent.

Stage 3. Addressing the shortfalls identified by the assisted self-assessment

- This would entail disclosure of the results by the OFC of the assisted self-assessment, together with a plan (including a resource plan and timetable) to address the identified shortcomings. Assistance in meeting this plan could be provided by a number of sources, including from those bodies that provided assistance at the self-assessment stage.

Stage 4. Undergoing an outside assessment

- This would require outside reviewers competent in the international standards against which the jurisdiction is being assessed. The assessment team could include a representative from another OFC. At the completion of the assessment, there would be disclosure of the results of the assessment, together with a plan to address shortcomings.

Stage 5. Monitoring of progress in addressing shortcomings

- This might entail at least a partial recycling through some of the stages above, until such times as the outside assessor is able to report full adherence in all material respects with the relevant standards. Review of adherence would be needed over time, the frequency of which would need to be assessed on a case-by-case basis.

61. ***Assessment expertise and resource considerations.*** The Group recognises that outside assessments can by their nature be resource-intensive activities and sufficient resources will need to be made available to facilitate timely progress in putting in place and generating results from an assessment program. The Group also notes that there are factors that could help in organising the assessments and help mitigate an inordinate demand on assessment resources.
- The Group considers that there is a finite supply of assessors with the necessary expertise on OFCs and availability. It would be this pool that would be drawn from to undertake individual outside assessments of OFCs. This should enhance the comparability and help ensure high quality assessments. To avoid any possibility of conflict, individuals involved in assisted self-assessments by a particular OFCs should not have a leadership role in independent assessments of that OFC.
 - Assessment teams would be comprised of experts in the areas of banking supervision, securities regulation, insurance supervision, law enforcement authorities, as relevant to the business transacted in the OFC (e.g., an expert in insurance supervision may not be needed, if insurance is not a main feature of an OFC's activities). In some cases, an expert may have expertise in more than one of the above areas. An expert from another OFC could also be included.
 - Relative to other more comprehensive programs of financial sector assessments, the expertise required from an assessor relates more to the nature of activities in OFCs rather than specific expertise on a specific OFC (although some experts may in fact have both).²⁷
 - Outside assessors would also not have to start from a zero base of knowledge, as information, including assisted self-assessments, and previous assessments by other groups are available that could be drawn upon by the outside assessors.²⁸ Further, assessments would be facilitated by drawing on the available methodologies that have been developed by standard-setting and international supervisory bodies. This information and the available assessment tools should enable a more rapid pace for undertaking an assessment program of OFCs than would otherwise be the case.
62. Having the necessary and appropriate resources will be critical to the success of the assessment process. Many details of the process would need to be worked out before estimating the resource costs entailed. To give some order of magnitude of what could be involved, Annex G provides a preliminary approximation of the possible resource implications for one variation of an assessment process outlined in this report.
63. The Group also recognises that an assessment process would benefit from offshore groupings and from some individual OFCs representatives more generally having some

²⁷ That is, to assess OFC X's adherence to international standards, an expert with expertise in OFC activities is needed, not necessarily an expert on the economic structure of OFC X.

²⁸ For example, self assessments prepared by the BCBS, IAIS, IOSCO, FATF and its sister regional bodies, independent reports such as the Edwards Report on the Crown dependencies, etc. Information on member jurisdictions' adherence to the FATF Recommendations is available in the FATF Annual Report, and the FATF has recently put in place a process for identifying non-co-operative jurisdictions with respect to money laundering.

role to play in assisted self-assessments and outside assessments to tap their knowledge and expertise, and to improve the chances of greater acceptance to undertake such an assessment process. In the Group's view, however, it would not be appropriate for such representatives to lead outside assessment teams, owing to inherent conflict of interest considerations.

64. The Group recognises that the timing of the assessments of OFCs' adherence to relevant international standards will be crucial, including the application of an effective and efficient system of incentives (see paragraph 68). While sufficient time will be needed to undertake objective and thorough assessments, they need to be delivered within a reasonable timeframe across OFCs so that the application of incentives would not result in inequalities and distortions. Similarly, OFCs that repeatedly refuse to commit to the assessment process or repeatedly refuse to fulfil the obligations of the commitments made under the process (for example by not remedying the non-adherence identified by the process), would need to be considered as non-adherent by those that would be responsible for applying incentives.
65. ***Jurisdictions that should be assessed.*** The Group considers that priority should be placed on assessing those OFCs where procedures for supervision and co-operation are in place, but where there is substantial room for improvement in actual practices (i.e., OFCs that would fall into Group II). Priority could also be given to those jurisdictions with the most significant financial activity.
66. ***Priorities in implementation and assessment of standards.*** In the view of the Group, jurisdictions that encourage international financial institutions to operate in their jurisdictions must ensure that they supervise their activities according to international standards as a minimum, and that they have the necessary resources to do so. While recognising that full implementation of all relevant international standards is the ultimate goal, the Group has identified those standards that address the most urgent concerns relating to some OFCs, and deserve implementation and assessment priority in those cases where it is not practical to move towards full implementation in a single stage. These international standards fall into three broad categories:
 - Cross-border co-operation, information sharing, and confidentiality;
 - Essential supervisory powers and practices; and
 - Customer identification and record-keeping.
67. The specific standards identified by the Group are listed in Annex H (which should not be considered as exhaustive). The Group considers that assessments should also take into account the capacity of supervisors and law enforcement authorities to obtain, on a timely basis, information about the beneficial ownership of corporate vehicles registered in their jurisdiction and to share that information with foreign authorities.

68. ***Incentives to enhance OFCs' adherence to international standards.*** The Group has agreed that to enhance OFCs' adherence to international standards, adequate incentives are needed to support a level playing field and reduce the opportunity for regulatory arbitrage. A key aim of an incentive system would be to attract the Group II OFCs (i.e., OFCs where procedures for supervision and co-operation are generally in place, but where there is substantial room for improvement in actual practices) into Group I (i.e., OFCs generally viewed as co-operative with a high quality of supervision) and put increased pressure on those OFCs that choose to remain in Group III (i.e., OFCs that are seen to have a low quality of supervisory oversight, and/or as being non-co-operative with onshore supervisors). Further, the Group has agreed that a system of incentives should encourage OFCs to volunteer for assessments of their implementation of relevant standards.
69. The Group considers that a system of incentives should have the following features:
- Application of both positive and negative incentives for adherence and non-adherence, respectively—a “carrots and sticks” approach.²⁹
 - Strength of incentives would be on a graduated scale, that is, jurisdictions would be asked to indicate their political willingness to implement international standards and be given time in which to achieve progress, but an increasing scale of negative incentives would be applied in cases of continued non-adherence.
 - Application of incentives would be a matter for individual jurisdictions, but they would be most effective if undertaken collectively by the major financial centres.
 - Incentives would address the areas of non-adherence in the OFC.
 - In applying incentives to non-adherent jurisdictions, it could be expected that supervisors, as relevant, would first notify the jurisdiction of their intent to apply an incentive and provide an opportunity for the jurisdiction in question to take remedial action.
70. The Group considers that the ***menu of possible incentives*** in Box 7 should be considered by the appropriate bodies and groupings as an array of means for enhancing OFCs' adherence to international standards. Possible incentives include both market and official incentives. Official incentives are discussed separately in Box 7, however, market incentives are also important. Market incentives operate when market participants factor information about an economy or institution into their risk evaluations and reflect this in their investment decisions, in differentiated credit ratings, or in borrowing spreads, for that economy or for institutions in that economy. Market participants use a range of quantitative and qualitative economic and financial indicators in their risk evaluations. Disclosure of information is critical to the effectiveness of market incentives. An assessment of an OFC's adherence to relevant international

²⁹ Hereinafter, the term incentive refers to both positive and negative incentives (which are sometimes referred to as sanctions).

standards can be an important factor in market participants' risk evaluations if the results are publicly available.

71. Some ***legislative or regulatory changes*** in major financial centres may be necessary to apply the incentives suggested.³⁰ The Group recognises that some of these types of incentives, particularly those related to supervisory practices, would have implications for the competitive position of onshore financial institutions if there were different responses from different onshore jurisdictions. This underlines the importance of maximising collective action by major onshore centres.
72. In this regard, the Group notes that the FSF's composition includes senior representatives from supervisory agencies, finance ministries and central banks from most major financial centres. This, in combination with the FSF's mandate to promote international financial stability through enhanced information exchange and international co-operation in financial market supervision and surveillance, points in the Group's view to the FSF as a well-placed forum for discussion on problematic OFCs in a collective and effective fashion by major financial centres, which can bring actions to bear on OFCs as appropriate.

³⁰ For example, some onshore jurisdictions would need legislation for supervisors to refuse to allow institutions regulated in their jurisdiction to either open new operations or close existing ones in designated OFCs (incentives D (vi) and D (vii)). Similarly, legislative changes would be needed if new obligations on reporting (incentives D (ii) and (iii)) were to be binding on financial institutions (as opposed to just being advisories).

**Box 7. A Menu of Possible Incentives
To Enhance OFCs' Adherence to International Standards**

A. Disclosure-type incentives

- (i) Publication of OFCs' progress in implementing their action plan to adhere to the relevant international standards could be prepared on the basis of the assessment process.
- (ii) Problems with an OFC could be highlighted by an individual onshore jurisdiction or multilateral grouping through publishing an advisory (a form of "name and shame"). This could serve as a warning letter to financial institutions to be careful in conducting business in the identified problematic OFC.¹

B. Membership-type incentives

- (i) Membership in international groupings (e.g., IOSCO, IAIS, committees of bank supervisors etc) could be conditioned on some level of adherence to its own standards, and failure to meet a group's standards could be a condition for removal from, or demotion of status within, the group.²

C. Provision of assistance

- (i) Technical assistance (including training and secondments) could be provided—by bilateral donors, national supervisors, standard-setting bodies, the IMF, multilateral development banks (including the World Bank), other international institutions, such as UN agencies, the Financial Stability Institute, and other training providers—to OFCs to help them implement relevant international standards.
- (ii) Financial assistance, including access to IMF and multilateral development bank financing, could be made conditional on progress towards implementation of relevant international standards. In the event of continued non-adherence, the provision of assistance could be constrained or withdrawn.³

Contd.....

¹ This incentive could also be considered to fall into the supervisory incentive category.

² For example, IOSCO currently requires applicants for membership to meet co-operation and enforcement standards. On this basis, IOSCO has deferred membership to certain applicants. In addition, membership in the Offshore Group of Bank Supervisors (OGBS) now requires adherence to a specific checklist, with respect to legislation, political commitment to standards, etc. Some applications have failed to meet the criteria and have been denied membership. However, to be truly effective, the criteria need to be applied equally rigorously to existing members, which can be contentious. Similarly, the Offshore Group of Insurance Supervisors (OGIS) requires acceptable regulatory legislation, its effective enforcement, and adequate resources as prerequisites for membership. OGIS also monitors continuous observance of their existing members with the membership criteria.

³ However, some OFCs may not qualify, or be expected to apply, for financial assistance given per capita income, etc.

**Box 7 (contd.). A Menu of Possible Incentives
To Enhance OFCs' Adherence to International Standards**

D. Supervisory incentives

- (i) **Market access.** Financial institutions' location in an OFC that adheres (does not adhere) to international standards could be considered as a positive (negative) factor by onshore jurisdictions to consider in making market access determinations. For example, supervisors in onshore jurisdictions could consider, as a positive factor, the fact that an OFC adheres to international standards when evaluating applications for licences from financial institutions in that OFC.
- (ii) **Increased "know-your-customer" obligations** could be applied for financial institutions doing business with individuals or legal entities established or registered in problematic OFCs.
- (iii) **Increased reporting requirements** could be applied for financial institutions doing business with individuals or legal entities established or registered in problematic OFCs.
- (iv) Home country supervisors could consider location in a problematic OFC as a factor in deciding to **increase examinations** of its financial institutions' operations in the OFC.
- (v) Home country supervisors could consider location in a problematic OFC as a factor in deciding to require **increased external audit requirements** of its financial institutions' operations in the OFC.
- (vi) Home country supervisors could **refuse to allow their financial institutions to open new operations** in OFC jurisdictions that do not comply with international standards.
- (vii) Home country supervisors could **require their financial institutions to close existing operations** in OFC jurisdictions that do not comply with international standards.
- (viii) **Capital requirements.** Supervisory bodies could be asked to design regulatory concessions (penalties) to reward (penalise) financial institutions operating in jurisdictions that adhere (do not adhere) to relevant standards, such as lower (higher) capital requirements.⁴

E. Other official incentives

- (i) In extreme cases of continued non-adherence to international standards, governments or supervisory authorities, as appropriate, could **restrict or even prohibit financial transactions** with counterparties located in problematic OFCs. Measures could include restrictions on home financial institutions from entering into correspondent banking relationships with counterparties located in problematic OFCs.⁵

⁴ The Basel Committee's Consultative Document on a New Capital Adequacy Framework requested comment on whether a claim on a bank should receive a risk weighting of less than 100 percent only if the bank supervisor in the country has implemented, or has endorsed and is in the process of implementing the Basel Core Principles for Effective Banking Supervision. The Consultative Document also proposed a parallel approach for claims on securities firms. These claims would only receive a risk weighting of less than 100 percent if that firm's supervisor has endorsed and is in the process of implementing IOSCO's Objectives and Principles of Securities Regulation. In addition, the Document proposed that claims on sovereigns would only be eligible for a risk weighting of less than 100 percent, if the sovereign had subscribed to the IMF's Special Data Dissemination Standard. These proposals have raised concerns in some quarters, and will be discussed further by the Basel Committee.

⁵ Such measures have been taken in the past but usually as part of formal and wider sanctions, and on a concerted basis. Many countries would need new legal powers in their own jurisdictions to take such measures because of an OFC's failing to adequately supervise its financial sector.

VIII. Areas for recommendations

73. The Group's recommendations can be summarised as follows:

Recommendation 1: *An assessment process for OFCs' adherence to international standards*

The Group recommends that an assessment process (as described in Box 6) for assessing OFCs' implementation of relevant international standards be put in place.

Recommendation 2: *Responsibility for an assessment process*

The Group recommends that the FSF request the IMF take responsibility for developing, organising and carrying out an assessment process for OFCs.

The Group considers that the FSF should facilitate the efforts of the IMF (with the World Bank as appropriate) as the IMF organises assessments of the implementation of standards by OFCs. This would include providing moral suasion to encourage OFCs to participate in the assessment process, calling on FSF members to make available appropriate resources to the IMF to help it carry out the assessment process and to OFCs to assist them in improving their supervisory systems, and encouraging major financial centres to promote a wider acceptance of international standards.

Recommendation 3: *Priority OFC jurisdictions for assessment*

The Group recommends that priority for assessment be placed on those OFCs where procedures for supervision and co-operation are in place but where there is substantial room for improvement (i.e., OFCs that would fall into Group II). Priority could also be given to those jurisdictions with the most significant financial activity.

Recommendation 4: *Standards for priority implementation and assessment by OFCs*

The Group recommends that the international standards relating to cross-border co-operation and information sharing, essential supervisory powers and practices, and customer identification and record keeping, be assigned priority in implementing and assessing OFCs' adherence to standards in the more immediate term. The specific standards identified by the Group are listed in Annex H (which should not be seen as exhaustive), although adherence to all relevant international standards should be the ultimate goal.

The Group considers that assessments should also take into account the capacity of supervisors and law enforcement authorities to obtain, on a timely basis, information about the beneficial ownership of corporate vehicles

registered in their jurisdiction and the ability to share that information with foreign authorities.

Recommendation 5: *Incentives to enhance OFCs' adherence to international standards*

The Group recommends that a menu of incentives—market, disclosure-type, membership, provision of assistance, supervisory, and other incentives identified in Box 7—be considered for application by the appropriate bodies or groupings in relation to an OFC's adherence to the relevant international standards.

The Group also recommends that the FSF discuss the IMF's conclusions arising from the proposed assessment process, and foster efforts, including by supervisors of major financial centres, that would be most effective if undertaken collectively in the application of incentives to enhance OFCs' adherence to relevant international standards.

Recommendation 6: *Actions for onshore jurisdictions*

The Group encourages onshore jurisdictions to engage in more effective consolidated supervision in the banking and insurance sectors, recognising the important responsibilities of home country supervisors, so that the ability of offshore activities to escape oversight is reduced. Similarly, the Group encourages securities supervisors to enhance their oversight of securities firms to improve their understanding of relevant offshore activities.

Recommendation 7: *Insurance standards development*

The Group encourages the IAIS in its work to develop best practices for reinsurance and its supervision, as well as with respect to developing specific supervisory standards on solvency and consolidated supervision for all insurance activities.

Recommendation 8: *Assessment methodologies for standards*

The Group encourages those bodies that have not already done so to develop methodologies for assessing observance with their respective standards, or to complete their efforts, as soon as possible, in consultation with the IMF and World Bank and others.

Recommendation 9: *Corporate vehicles and beneficial ownership*

The Group recommends that appropriate international fora be asked to explore the issue of developing mechanisms to prevent the misuse of corporate vehicles. These mechanisms should assure that supervisors and law enforcement authorities are able to obtain, on a timely basis, information on beneficial

ownership of corporate vehicles and the sharing of that information with foreign authorities.

Recommendation 10: *Data reporting by OFCs*

The Group strongly encourages OFCs with significant financial activities to report financial data to the BIS for its quarterly publication on International Banking Statistics with the requested breakdown (distinguishing between debt securities and other claims), and on a timely basis. The Group notes that such action could be considered as an indicator of an OFC's willingness to co-operate within the international financial system. As necessary, OFCs should seek the available technical assistance from national authorities and international financial institutions to improve their statistical practices and capacity.

Recommendation 11: *Co-ordination of OFC-related initiatives*

The Group recommends that the published version of this Report be formally transmitted by the FSF to the various international groups that are concerned with the activities of OFCs. In addition, the Group recommends the development of a mechanism to assist the international community in keeping abreast of progress on OFC-related initiatives.

74. To facilitate the review of progress in implementing of these recommendations, the Group suggests a brief report be prepared by the FSF Secretariat for the Fall 2001 meeting of the Forum.

FSF Working Group on Offshore Financial Centres (OFCs)**Terms of Reference**

Drawing on the work and experience of national authorities, the regulatory and supervisory groupings, and the Financial Action Task Force, the working group on offshore centres should:

1. Take stock of the use made by participants in international financial markets of OFCs and consider the impact of such use on financial stability.
2. Review progress made by OFCs in enforcing international prudential and disclosure standards, and in complying with international agreements on the exchange of supervisory information or information relevant to combating financial fraud and money laundering.
3. Taking account of the analysis under (1) and (2) above, identify, and evaluate the threats to financial stability or credibility of regulatory efforts that arise from continued non-compliance, non-enforcement, and non-co-operation by OFCs.
4. Evaluate the scope for improving compliance and co-operation through technical assistance to, and/or intensify regulatory contacts with, OFC authorities, and such others steps as may be appropriate, including supervisory reactions in the case of non-compliance and non-co-operation.

Members of the Working Group on OFCs**John Palmer** (Chairman)

Office of the Superintendent of Financial Institutions, Canada

Niramon Asavamane

Bank of Thailand, Thailand

Giovanni Carosio

Bank of Italy, Rome, Italy

Hervé Dallérac

IOSCO Representative

(Commission Des Opérations De Bourse, France)

Hans-Joachim Dohr

Federal Banking Supervisory Office, Germany

Thierry Francq

Ministry of Economy, Finance and Industry, France

Marco Franchetti

Swiss Federal Banking Commission, Switzerland

Charles Freeland

Basel Committee on Banking Supervision, Basel

Joseph Halligan

H.M. Treasury, United Kingdom

Knut Hohlfeld

International Association of Insurance Supervisors, Basel

Marisa Lago

US Securities and Exchange Commission, United States

Rinaldo Pecchioli

OECD, Paris, France

Tharman Shanmugaratnam

Monetary Authority of Singapore, Singapore

Sakura Shiga

Financial Supervisory Agency, Japan

Secretariat**Kate Langdon**, (Secretary)

Financial Stability Forum Secretariat, Basel

Tony Maxwell

Office of the Superintendent of Financial Institutions, Canada

Jerry Goldstein

Office of the Superintendent of Financial Institutions, Canada

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OFC Working Group Survey on Offshore Financial Centres

At its September 1999 meeting, the FSF supported a survey of onshore and offshore supervisors of regulated financial service providers to be undertaken by the Working Group. The term “financial service provider” includes deposit-taking institutions, insurance companies, and those engaged in the securities business.

The goal of this survey was to provide a preliminary identification of OFCs with respect to compliance with international standards of supervision established by the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors, and the International Organisation of Securities Commissions.

In November 1999, separate questionnaires were sent to supervisors responsible for those entities engaged in deposit taking, insurance services, and the securities business. Supervisors were asked to respond to each question for all financial centres with significant offshore activities with which they have familiarity. A copy of the two questionnaires is attached.

Questions for the Onshore Supervisors

The questions submitted to the onshore supervisors were designed to elicit their views on the quality of regulation and supervision in those OFCs about which they have some degree of familiarity, and the quality of co-operation they have experienced in their dealings with OFC supervisors.

Questions for the Offshore Supervisors

The questions submitted to OFC supervisors were designed primarily to provide information on how these offshore jurisdictions interact with the home supervisors of financial service providers operating in, or from, their offshore jurisdictions. The actual entity operating in an OFC may be a branch, a subsidiary, or an affiliate of a financial service provider incorporated in an onshore jurisdiction.

Who received the questionnaire?

Because there is no single, widely accepted list of OFCs, a variety of sources was used to develop the list of recipients. These sources include: the membership list of the Offshore Group of Banking Supervisors, the membership list of the Offshore Group of Insurance Supervisors, jurisdictions that have been included in a variety of publications, such as OFC studies by UN staff, studies by IMF staff, academic periodicals and monographs, and business periodicals. In addition, respondents were asked to indicate if there was a jurisdiction that, in their view, belongs in the list, but is not there.

The cover letter stated that the names of those OFCs that participated in the survey, as well as those that did not, will be published. The cover letter also stated that, because these questions are only a preliminary step in a longer process, the responses could be based on impressions from experience and not on formal evaluations.

BY FAX

November 24, 1999

Supervisors in Major Financial Centres
Supervisors in Financial Centres with Significant Offshore Activities

Dear Supervisor:

Survey of Major Financial Centres and Financial Centres with Significant Offshore Activities

I am writing to you in my capacity as chairman of the Financial Stability Forum (FSF) Working Group on Offshore Financial Centres (OFCs). In February 1999, the G-7 Finance Ministers and Central Bank Governors set up the *Financial Stability Forum* to promote international financial stability through enhanced information exchange and international co-operation in financial market supervision and surveillance. For your information, I have attached a brief description of the membership and ongoing work of the FSF.

As described more fully below, I request your assistance in participating in a survey of major financial centres (onshore centres) and financial centres with significant offshore activities (OFCs) focussing on issues related to regulation of financial activities and co-operation with foreign regulators.

The Financial Stability Forum and the Survey of OFCs

In April 1999 the FSF convened the Working Group on Offshore Financial Centres to consider the significance of OFCs in relation to financial stability in all its aspects.

At its September 1999 meeting, the FSF approved a survey of onshore and offshore supervisors of regulated financial providers to be undertaken by the Working Group. The term "financial service provider" includes deposit-taking institutions, insurance companies, and those engaged in the securities business.

The goal of this survey is to provide a preliminary identification of OFCs with respect to compliance with international standards of supervision established by the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors, and the International Organization of Securities Commissions.

Separate questionnaires are being sent to supervisors responsible for those engaged in deposit taking, insurance, and the securities business. To facilitate completion and analysis of the results of the survey, the same questions have been submitted to all supervisors. Please respond to each question for all financial centres with significant offshore activities with which you have familiarity. If, in your view, a specific question is not applicable to your responsibilities please indicate, explaining briefly the reason.

Questions for the Onshore Supervisors

The questions submitted to the onshore supervisors are designed to elicit their views on the quality of regulation and supervision in those OFCs about which they have some degree of familiarity, and the quality of co-operation they have experienced in their dealings with OFC supervisors.

The individual responses to these questions will be kept strictly confidential. Answers of all the respondents will be aggregated, and, in those cases where aggregation will not in any way compromise this confidentiality, summary results may be published.

Questions for the Offshore Supervisors

The questions submitted to OFC supervisors are designed primarily to provide factual information on how these offshore jurisdictions interact with the home supervisors of financial service providers operating in, or from, their offshore jurisdictions. The actual entity operating in an OFC may be a branch, a subsidiary, or an affiliate of a financial service provider incorporated in an onshore jurisdiction.

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Individual responses to the last question submitted to OFC supervisors, that asking about OFC supervisors' concerns about particular home supervisors, will be kept strictly confidential. Again, where aggregation of the responses to this question will not compromise this confidentiality, results may be published.

Who will receive the questionnaire?

Attached is a list of financial centres with significant offshore financial activities being asked to participate in the survey. Because there is no single, widely accepted list of OFCs, we have used a variety of sources to develop the list. These sources include: the membership list of the Offshore Group of Banking Supervisors, the membership list of the Offshore Group of Insurance Supervisors, jurisdictions that have been included in a variety of publications, such as OFC studies by UN staff, studies by IMF staff, academic periodicals and monographs, and business periodicals. If there is a jurisdiction that, in your view, belongs in the list, but is not there, please include this OFC in your responses.

When should the questionnaire be completed?

I am asking that you complete the questions for supervisors in major financial centres and in financial centres with significant offshore activities by 22 December 1999. Please respond to the questions for all OFCs with which you have some experience, including those in which financial service providers supervised by you have operations.

The names of those OFCs that participate in the survey, as well as those who do not, will be published.

Because these questions are only a preliminary step in a longer process, the responses can be based on impressions from your experience and not on formal evaluations. The results will accompany a report to the FSF on OFCs, and will likely be used to support a recommendation that a formal assessment of OFC compliance with international standards of supervision should be undertaken.

I recognise that your time is extremely valuable and your responsibilities numerous. The questionnaire is relatively short however, and the questions direct. I would appreciate your time in responding to the questions as fully as possible, providing examples wherever you think it would be helpful.

If you have any questions about a particular question, or about the survey in general, please contact Dr. Jerry Goldstein, Director of Research at the Office of the Superintendent of Financial Institutions in Canada (telephone: 613-990-8911; fax: 613-993-6782; E-mail: ggoldst@osfi-bsif.gc.ca).

Thank-you very much for your help.

John Palmer
Chairman of the FSF Working Group on Offshore Financial Centres
Superintendent of Financial Institutions, Canada

Attachments

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Questions for Supervisors in Major Financial Centres

1. Are you the home supervisor of any financial service provider (defined as deposit-taking institution, insurance company, or company in the securities business) that has branches, subsidiaries or affiliates in an OFC? On what basis do you decide whether you need information about these OFC operations in order to regulate or supervise the financial service provider on a consolidated/comprehensive basis?
2.
 - (a) From which OFCs is information important to your regulation or consolidated/comprehensive supervision of financial service providers?
 - (b) Are there specific OFCs for which information has been important in non-routine regulatory investigations that you have undertaken, including investigations into potential breaches of rules, regulations, and laws? Which OFCs?
3.
 - (a) As a host country, are you aware of entities incorporated in OFCs or affiliated with companies incorporated in OFCs that are operating as unregulated financial service providers in your jurisdiction?
 - (b) Would any of these entities be regulated as banks or other deposit-taking institutions, insurance companies, or as businesses in the securities industry if they were incorporated in your jurisdiction?
 - (c) If so, with which OFCs are they linked?
 - (d) Do you know if the entity incorporated in the OFC undertakes financial activities in the OFC or is it simply a "mailbox"?
4.
 - (a) Do you have restrictions, rules, requirements, or incentives that affect the ability of financial service providers, for which you are the home supervisor, to establish or operate outside your country?
 - (b) Are there specific OFCs in which the operations of financial service providers for which you are the home supervisor are
 - (i) forbidden, or
 - (ii) restricted in some way?
 - (c) Which OFCs? Please explain why.
 - (d) Do OFCs permit your financial service providers to undertake activities abroad that you do not permit your financial service providers to do at home? Please explain.
5.
 - (a) Are there specific OFCs about whose system of regulation/supervision you have developed some degree of familiarity?
 - (b) Could you please rate each of these OFCs with respect to your view of its overall quality of regulation/supervision on a scale of 1 (very poor) to 5 (excellent)?
 - (c) Are there specific OFCs you do not feel that you can rate, but about whose system of regulation/supervision you have concerns? Which OFCs? Please explain why, briefly.
6.
 - (a) Have any OFCs denied a request that you have made
 - (i) for routine information to assist with the supervision of a financial service provider for which you are the home supervisor? or
 - (ii) for formal assistance with a non-routine regulatory investigation (including an investigation into potential breaches of rules, regulations, and laws)?
 - (b) Which OFC(s)? On what basis was a denial made?
7.
 - (a) Have you had difficulty obtaining information or co-operation in connection with investigations, including investigations of financial misconduct or money laundering, from a regulatory, judicial or civil law enforcement authority? In which jurisdictions?
 - (b) Have you had difficulty obtaining information or co-operation in connection with investigations, including investigations of financial misconduct or money laundering, from a criminal law enforcement authority? In which jurisdictions?
 - (c) Have the difficulties referred to in (a) and (b) arisen as a result of issues related to the

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transmission of information from a criminal law enforcement authority to a regulatory, judicial or civil law enforcement authority?

8. (a) Have you, or your jurisdiction, established a formal or informal procedure (through an MOU or otherwise) for the exchange of information with an OFC to facilitate the supervision of financial service providers for which you are the home supervisor? If so, with which OFCs?
- (b) Have you, or your jurisdiction, established an formal or informal procedure (through an MOU or otherwise) for the exchange of information to facilitate non-routine regulatory investigations, including investigations into potential breaches of rules, regulations, and laws? If so, with which OFCs?
- (c) Are you satisfied with the established procedure(s)?
- (d) Are there any specific shortfalls? If so, please explain.
9. (a) Have you requested and received permission to undertake local on-site examinations of OFC entities of financial service providers for which you are the home supervisor? If so, with which OFCs? If you have not received permission, which OFCs have said no?
- (b) For those who said no, have you negotiated alternative arrangements (e.g. the use of external accountants) which satisfy your requirements? If so, with which OFCs?
10. (a) Overall, based on your experience, could you please rate each OFC, identified above, with respect to its degree of co-operation in exchange of information on a scale of 1 (very poor) to 5 (excellent)? Please explain briefly the reasons for the rating.
- (b) Are there specific OFCs that you do not feel you can rate, but about whose level of co-operation you have concerns? Which OFCs? Please explain why briefly.

Questions for Supervisors in Financial Centres with Significant Offshore Activities

(These questions are based on principles developed by the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors, and the International Organization of Securities Commissions.)

Please answer the following questions based on your existing legislative, regulatory, and supervisory regime. If changes are underway or proposed, please indicate briefly the nature of the changes and the timetable. If you are the supervisor for more than one industry, please answer for each separately.

1. (a) Do you, or does another government agency, license entities engaged in
 - (i) banking (and deposit-taking),
 - (ii) insurance, and
 - (iii) the securities business?How many entities are there in each of these classifications? Can you provide an estimate of the magnitude of the business?
- (b) Are the activities of entities that are licensed to engage in
 - (i) banking,
 - (ii) insurance, and
 - (iii) the securities business clearly defined?
- (c) Do you supervise the activities of entities licensed to engage in
 - (i) banking,
 - (ii) insurance, and
 - (iii) the securities business?How many entities do you supervise in each of these classifications?
2. In your review of a request by a foreign financial service provider to establish a local entity, is prior consideration given to:
 - (a) the track record of the applicant?
 - (b) obtaining prior consent (or a statement of “no objection”) from the home supervisor?
 - (c) quality of home supervision?

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3. Do you, as the host supervisor, check for compliance with prudential regulations and other legal requirements through:
 - (a) off-site work (review and analysis of the financial condition of individual financial service providers using prudential reports, statistical returns and other appropriate information)? If yes, please provide an indication of how many of your staff are involved.
 - (b) on-site work (conducted either by own staff or through the work of external auditors)? If yes, please provide an indication of how many of your staff are involved?
 - (c) how many of your staff in total are involved in financial regulation and supervision?
4. Do you, as the host supervisor, have the legal right of full access to all financial service provider records, including third party records, for the furtherance of supervisory work?
Do you also have similar access to the board, senior management and staff, when required?
5. Do you, as the host supervisor, allow the authority of the home supervisor to supervise activities of locally incorporated entities of financial service providers for which the home supervisor has the overall responsibility for supervision?
6. Are local entities of foreign financial service providers subject to prudential, inspection, and regulatory reporting requirements that are similar to those required of your domestic financial service providers?
7. Can you, as the host supervisor, share with home country supervisors information about the local operations of foreign financial service providers as long as confidentiality is protected?
8.
 - (a) Do you have the ability to co-operate and share information (including the provision of confidential information) with foreign regulatory, judicial, and civil law enforcement authorities?
 - (b) Do you, or does your jurisdiction, have the ability to co-operate and share information (including the provision of confidential information) with foreign criminal law authorities?
9.
 - (a) Do you have in place defined measures to combat money laundering? If yes, does this include:
 - (i) “know your customer” principles adopted by financial institutions?
 - (ii) record-keeping for at least five years?
 - (iv) mandatory suspicious transaction reporting?
 - (b) Have you, or your jurisdiction, been reviewed as part of a mutual evaluation by the FATF or a FATF-style regional body?
10. Are home country supervisors given on-site access, by you, to local offices of entities for which the home supervisor has the responsibility for supervision? Please explain.
11. Do you, as the host country supervisor, advise home country supervisors on a timely basis of any material remedial action you plan to take regarding the operations of a local entity of a foreign service provider?
12. Do you, as a host supervisor, have concerns with a particular home supervisor? If so, which one(s)? Please explain separating regulatory/supervisory issues from law enforcement issues.

Summary of Results of Survey on OFCs

1. All onshore jurisdictions with extensive dealings with OFCs, as well as most OFCs with a significant volume of offshore financial activity, responded to the questions. In addition, most respondents appeared to be candid in their responses to the questions. As stated by the Chairman of the Working Group in the cover letter to OFC supervisors, the names of those OFCs that participated in the survey, as well as those who did not, would be published (see paragraph 29 and Table 1 in the main report).
2. Some OFCs are highly regarded. However, many respondents from onshore jurisdictions expressed serious concerns about the quality of supervision in, and the degree of co-operation offered by some offshore jurisdictions. Further, the responses to the questions by the offshore supervisors revealed a number of jurisdictions in which a relatively small number of professional staff at the supervisory agency is responsible for the surveillance of a relatively large number of financial service providers. In addition, in a number of cases, on-site inspection of financial service providers is either not exercised at all, or is not done in a timely fashion.
3. The results of our survey strongly suggest that an assessment process be developed to obtain more detailed information on OFCs' implementation of international standards. The assessments would aim at evaluating the quality of supervision and degree of co-operation and OFCs could conveniently be classified into three groups.
 - The **first group** would be jurisdictions generally viewed as co-operative jurisdictions with a high quality of supervision, which largely adhere to international standards.
 - The **second group** of OFCs would be jurisdictions generally seen as having procedures for supervision and co-operation in place, but where actual performance falls below international standards, and there is substantial room for improvement.
 - A **third group** of OFCs would be jurisdictions generally seen as having a low quality of supervision, and/or being non-co-operative with onshore supervisors, and with little or no attempt being made to adhere to international standards.
4. Within the second and third groups there may not be uniformity of law and practice. For example, some OFCs may be in the third group because they have deliberately chosen to be poorly supervised and not to co-operate with onshore supervisors in order to attract dubious business. Other OFCs may be in the third group because they do not have the expertise to supervise their offshore financial sector properly.
5. The precise reasons for placing an OFC in a particular category would be important in determining responses to address the shortcoming identified in the assessments. The assessment will also need to distinguish between the quality of supervision in the different financial sectors within the same jurisdiction.

International Standards: Progress in Developing and Assessing Observance of Standards^{31 32}

Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Transparency of Monetary and Financial Policies	IMF	Code of Good Practices on Transparency in Monetary and Financial Policies	Code approved by IMF Executive Board (July 1999) and endorsed by the IMF Interim Committee (September 1999).	Document on examples of good practice being developed in consultation with national authorities, other international organisations and groupings.
Banking Supervision	Basel Committee on Banking Supervision (BCBS)	Basel Core Principles (1997)	Initial self-assessments completed by 124 jurisdictions (October 1998).	Jurisdictions shortly to be invited to re-assess their observance with the Core Principles based on the Methodology.
			Set of harmonised and detailed criteria for assessing the Core Principles (the Methodology) issued in October 1999.	BCBS workshop scheduled for May 2000 to review Core Principles Methodology in light of ongoing field-testing.

³¹ A Compendium of Standards relevant to the stability of the financial system is available on the FSF web site (www.fsforum.org).

³² The quality of underlying accounting and auditing practices are also important.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Banking Supervision contd.			Independent assessment of jurisdictions' implementation of Core Principles using the Methodology are being conducted by mixed teams from the IMF, World Bank and regional supervisory groups.	
		The Supervision of Cross-border Banking (October 1996)	BCBS Working Group on Cross-Border Banking has reviewed results of 1998 survey on implementation of the 1996 recommendations. In addition, a survey of BCBS members was undertaken on specific issues encountered in members' cross-border supervision efforts.	BCBS reconvened the Cross-border Working Party (made up of BCBS and OGBS representatives) to consider whether further initiatives are required.
	Offshore Group of Bank Supervisors (OGBS)		Members of the OGBS have been actively involved with the Basel Committee, including in the development and assessment of progress in implementing the Recommendations from the BCBS' 1996 paper on supervision of Cross-border Banking. The OGBS has developed an on-site assessment checklist. New applicants to the OGBS are required to adhere to the checklist as a condition of membership in the OGBS. Their adherence is independently assessed.	

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Securities Market Regulation	International Organisation of Securities Commissions (IOSCO)	Objectives and Principles of Securities Regulation (September 1998)	IOSCO members have already conducted self-evaluations regarding co-operation. IOSCO members are currently completing self-assessments concerning their adherence with the Principles overall and, on a more highly detailed level, self-assessments regarding their adherence with two key sections of the principles: the ‘role of the regulator’ and ‘issuers of securities’. The self –assessment methodologies have been developed with IFI input. The IMF, World Bank and other IFIs are using the Principles in assessment programs	IOSCO members, with IFI input, are currently developing highly detailed methodologies for conducting self-assessments of adherence with the remainder of the Principles (dealing with secondary markets, market intermediaries and collective investment schemes). Continue working with IFIs to use the Principles in their programs for assessing countries’ financial systems.
		Resolution on Principles for Record Keeping, Collection of Information, Enforcement Powers and Mutual Co-operation To Improve The Enforcement of Securities and Futures Law (1997)	Key aspects of this resolution have been further developed in the Objectives and Principles of Securities Regulation (1998).	

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Insurance Supervision	International Association of Insurance Supervisors (IAIS)	Insurance Supervisory Principles (1997)	Self-assessments of the Principles conducted by IAIS members in 1998. Additional detailed standards have been developed for licensing; on-site inspection; derivatives; and asset management.	Work on detailed standards to continue (e.g. solvency requirements and assessments, reinsurance, electronic commerce).
			Taskforce on IAIS Supervisory Principles Methodology established in 1999.	Methodology will form the basis for a renewed comprehensive assessment of observance of IAIS principles and standards, for self-assessment as well as by third parties, e.g. IMF.
		Insurance Concordat (1997, revised in 1999)	Principles applicable to Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations.	

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Insurance Supervision contd.	Offshore Group of Insurance Supervisors (OGIS)	<i>Recommendations:</i> personal lines business <i>Principles:</i> fit and proper evaluation <i>Guidelines:</i> quality of assets and capital adequacy; standards for reinsurance security; technical reserves for property and casualty insurers; and implementation of “fit and proper” statement of principles	Membership in OGIS requires acceptable legislation that permits exchange of information with other regulators for prudential regulation, effective enforcement, and adequate resources, as well as a clear commitment to implement the FATF Recommendations. All OGIS members are IAIS members and completed IAIS self-assessments questionnaire, indicating substantially compliant. Self-assessments undertaken annually (every 3 years in more detail) with respect to compliance with OGIS membership criteria. Under OGIS’ evaluation process, one member (Anguilla) was demoted in 1997 to observer status due to delays in amending insurance legislation. Another member has been demoted because of difficulties encountered in the exchange of information.	More detailed evaluation procedure and additional guidelines (on-site inspection; loans to related parties; regulation of insurance on the internet; prevention of money laundering in insurance companies; cease and desist orders and winding up of insurers) are being prepared. Initiative to establish membership of OGIS as the standard setter for non-members is being launched.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Corporate Governance	Organisation for Economic Co-operation and Development (OECD), World Bank	OECD Principles of Corporate Governance (May 1999)	Co-operation framework established between OECD and World Bank for the promotion of a sustained, global policy dialogue. It is structured around a Global Forum and several regional Round Tables.	The Round Tables for Asia and Russia were launched in 1999 and their second round of meetings will be held in the first half of 2000. They bring together policy makers, regulators and private sector leaders. A Latin American Round Table will be launched in April 2000, while Round Tables for Africa and Eurasia are envisaged for the second half of the year. Using the OECD Principles as a starting point, the Round Tables will produce white papers on corporate governance reforms in the regions.
Taxation	OECD, Forum on Harmful Tax Practices	OECD Guidelines for Dealing with Harmful Preferential Tax Regimes (1998).	<i>Harmful Tax Competition: An Emerging Global Issue</i> adopted by OECD Ministers in 1998. Forum on harmful tax practices established. The Forum is charged with providing OECD Ministers a report identifying certain jurisdictions as tax havens and also establishing a framework for long-term dialogue with co-operative jurisdictions. The Forum is currently examining 47 jurisdictions that may be classified as tax havens.	Report on tax havens expected by Spring 2000. A high-level meeting with more than 30 non-member economies is scheduled for June 2000.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Taxation contd.	OECD, Committee on Fiscal Affairs		The OECD Committee on Fiscal Affairs has undertaken a project to identify best and worst practices in the design, implementation and administration of tax policies impacting on the operation of open financial markets. It includes an examination of both onshore and offshore tax regimes.	Results to be discussed in Spring 2000.
Money Laundering	Financial Action Task Force (FATF); FATF-style regional bodies (e.g. Caribbean Financial Action Task Force(CFATF)) and the Council of Europe Select Committee of experts on the evaluation of anti-money laundering measures (PC-R-EV)	FATF 40 Recommendations	Monitor compliance with FATF 40 Recommendations; members undergo regular self-assessment exercises and periodic mutual evaluations. Each FATF member has undergone two rounds of mutual evaluations. The CFATF and Council of Europe PC-R-EV should have completed their first round of mutual evaluations by end-2000.	A third round of mutual evaluations of FATF members will start at the beginning of 2001.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Money Laundering contd.		<i>FATF Report on Non-co-operative Countries and Territories</i> (14 February 2000).	FATF ad hoc group discussing in more depth the steps to be taken regarding non co-operative jurisdictions, both inside and outside the FATF membership. Clear criteria for defining non-co-operative countries or territories have been adopted. The ad hoc group also agreed on the <i>process</i> for identifying those countries or territories as well as on <i>counter-measures</i> to protect economies against money laundering.	FATF has begun to identify the jurisdictions, which meet these criteria, with a view to listing non-co-operative jurisdictions (June 2000) and persuading them to change their detrimental rules and practices.
	United Nations Office for Drug Control and Crime Prevention (UNODCCP)		The UN Offshore Initiative has been established to achieve a consensus on best practices to increase industry transparency and the quality of anti-money laundering measures in all OFCs.	The UN Offshore Forum (UNOF) is being developed. An informal advisory group has met twice. The program would aim at the enhancement of transparency and the adoption of international standards of best practice through training, technical assistance and mentoring. A plenary session with a wide range of OFC participants is scheduled to take place at the end of March 2000.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Information Sharing and Disclosure	Group of 7	Information Sharing: Ten Key Principles (G-7, May 1998).	Agreed by G-7 Finance Ministers with the aim of seeing them adopted as a global standard. They have subsequently been specifically endorsed by the Asia-Europe Finance Ministers (Frankfurt, January 1999), the international bodies of supervisory authorities, and by the Joint Forum on Financial Conglomerates (February 1999).	G-7 Finance Ministers have committed themselves to ensuring that their own countries incorporate these Principles and to disseminate them widely.
	Group of 7	Ten Key Principles for the Improvement of International Co-operation Regarding Financial Crime and Regulatory Abuse (G-7, 1999)	These principles were established after a review by G-7 countries of their laws and practices concerning information exchange between financial regulators and law enforcement agencies. They are intended to serve as a guideline not only for G-7 countries, but by all countries.	The Principles have been sent to international organisations such as the Basel Committee, FATF, IAIS, IMF, Interpol, IOSCO, OECD, and the World Bank for distribution among their members to encourage broader acceptance. Progress in implementing the Key Principles is expected to be reviewed in 2 to 3 years time.

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Area	Agency (s) responsible	Standards, Principles, Good Practices	Status	Next Steps
Information sharing and Disclosure contd.	Joint Forum	Principles for Supervisory Information Sharing (February 1999)	The Principles aim at providing supervisors involved in the oversight of regulated financial institutions residing in financial conglomerates guiding principles with respect to supervisory information sharing, to build on and enhance existing information sharing arrangements, particularly cross-sectorally. A framework methodology has been developed to examine the structure and operations of financial conglomerates and better identify the possible opaque structures that could impair effective supervision.	The Joint Forum has tentatively proposed to review implementation on an ongoing basis and work towards developing best practices to give effect to these principles.
Bribery and Corruption	OECD	Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (1999) OECD Anti-Bribery Recommendations	OECD Working Group on Bribery has identified certain practices associated with offshore centres that facilitate bribery and corruption transactions and/or act as obstacles to successful anti-corruption investigations and prosecutions (e.g. lack of adequate regulation, inadequate company law requirements and the use of bank secrecy to decline mutual legal assistance).	The Working Group is considering recommendations to prevent the use of OFCs in “grand” bribery and corruption transactions by improving standards of transparency in three main areas: financial rules and regulations, company law, and mutual legal assistance.

Estimate of Assessment Resource Requirements

A very preliminary estimate of resource requirements has been made, based on the assumptions set out below. They should be considered as illustrative only.

Key Assumptions

1. In the first three years of the program, 25 OFCs will undertake both an assisted self-assessment (stage 2) and an outside assessment (stage 4). In addition, another 10 will undertake a stage 2 assessment only. The assumed three-year pattern of assessments is: stage 1 @ 10/10/15; stage 4 @ 5/10/10.
2. A stage 2 (assisted self-assessments) will require the following resources:
 - 80% will require one outside expert;
 - 20% will require two experts;
 - Each expert will be required to work, on average, for 4 weeks;
 - 60% of experts will be paid; 40% will be seconded from other agencies, with their salary costs absorbed by their home agency.
3. A stage 4 (outside assessment) will require the following:
 - 50% will require two outside experts;
 - 30% will require three experts;
 - 20% will require four experts;
 - Each expert will be required to work, on average, for 5 weeks;
 - 80% of experts will be paid; 20% will be seconded from other agencies, with their salary costs absorbed by their home agency.
4. Salary and other costs will be as follows:
 - Paid experts will receive on average \$5,000 per week
 - Living expenses incurred by all experts will average \$2500 per week;
 - Travel expenses for all experts will average \$4000 per assignment;
 - Administration costs will be \$500,000 per year.

Estimated Resource Requirements

Based on the above assumptions;

- A stage 2 (assisted self-assessment) will incur salary, travel and living expenses, on average, of about \$31,000 per assessment.
- The equivalent average cost for a stage 4 (outside assessment) will be \$117,000.
- The estimated total annual costs, including administration, are \$1.4 million in year 1; \$2.0 million in year 2; \$2.2 million in year 3.
- The number of experts required will be 26 in year 1; 39 in year 2; 45 in year 3.

Enhancing OFCs Adherence to International Standards: Standards for Priority Implementation and Assessment

1. The G-7 Finance Ministers, the Financial Action Task Force, the Basel Committee on Banking Supervision, the International Organisation of Securities Commissions, the International Association of Insurance Supervisors, the Joint Forum on Financial Conglomerates and the Offshore Group of Banking Supervisors have developed standards that address issues relevant to the supervision of internationally active financial institutions generally.
2. Jurisdictions that encourage international financial institutions to operate in their jurisdictions are obliged to ensure that they supervise their activities according to international standards, and that they have the necessary resources to do so. While recognising that full implementation of all relevant international standards is the goal, the Group has identified those international standards that address the most urgent concerns relating to OFCs, and deserve implementation priority in those cases where it is not practical to move towards full implementation in a single stage. These standards (hereinafter “priority standards”) fall into three broad categories³³:
 - Cross-border co-operation, information sharing, and confidentiality;
 - Essential supervisory powers and practices; and
 - Customer identification and record-keeping.

Cross-border co-operation, information sharing and confidentiality

3. Financial supervisors and regulators (hereinafter “supervisor”) are tasked with ensuring that the domestic and international operations of the institutions for which they have responsibility are adequately supervised, wherever they are located. To do so, supervisors need to exchange information with and obtain other forms of co-operation from their fellow supervisors, provided that such information will be treated with appropriate confidentiality.

Essential Supervisory Powers and Practices

4. A supervisor’s powers to co-operate and share information across its borders must be complemented by certain basic supervisory powers and practices, without which co-operation and information sharing will be of limited value. Supervisors must have a strong voice in decisions on allowing financial institutions to operate in their jurisdiction. Failure to apply basic entry standards (e.g., fit and proper tests) on institutions and their key owners and managers can open up the system to future abuse. Supervisors must also have the ability to examine the books (wherever physically located) of the financial institutions for which they have supervisory responsibility, and to take appropriate actions when they have material supervisory concerns, including appropriate communications with other relevant supervisors.

³³ This listing should not be considered as exhaustive and assessors will need to take into consideration the specific circumstances of individual OFCs.

Customer Identification and Record-keeping

5. While international cooperation and adequate supervision are important aspects of the fight against money laundering, as well as illicit activities and abusive market behavior, they cannot be effective if financial institutions do not follow certain basic practices in terms of customer identification and record keeping.

Standards Sources

6. The priority standards are sourced from the following organisations and documents; the specific sources within a given document are indicated in italics, and are set out in full in the attached.

G-7 Finance Ministers

- Information Sharing: Ten Key Principles (May 1998)
Nos. 1, 2, 4, 5, 6, 9.
- Ten Key Principles for the Improvement of International Cooperation Regarding Financial Crimes and Regulatory Abuse - Working Group on Financial Crime (May 1999)
Nos. 3, 4, 5, 6, 7, 8, 9

Joint Forum on Financial Conglomerates (Joint Forum)

- Principles for Supervisory Information Sharing (February 1999)
Nos. 2, 3, 4

Basel Committee on Banking Supervision (BCBS) & Offshore Group of Banking Supervisors (OGBS)

- The Supervision of Cross-Border Banking (October 1996)
Nos. i, ii, iii, iv, x, xvi, xxiii, xxv

Basel Committee on Banking Supervision (BCBS)

- Core Principles for Effective Banking Supervision (September 1997)
Nos. 3, 18, 19, 20, 23, 24, 25

International Association of Insurance Supervisors (IAIS)

- Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations (Insurance Concordat) (December 1999)
Principle 3; Nos. 20, 21, 22, 23, 25

International Association of Securities Commissions (IOSCO)

- Resolution on Principles for Record Keeping, Collection of Information, Enforcement Powers and Mutual Co-operation to Improve the Enforcement of Securities and Futures Laws (November 1997)
Nos. A, B, C, D
- Objectives and Principles of Securities Regulation (September 1998)
Nos. 8, 9, 10, 11, 12, 13

Financial Action Task Force (FATF)

- Forty Recommendations on Money Laundering (1996)
Nos. 10, 11, 12, 32, 33, 34, 35, 36, 37

7. In addition to the above, assessments should also take into account the capacity of supervisors and law enforcement authorities to obtain, on a timely basis, information about the **beneficial ownership of corporate vehicles** registered in their jurisdiction and to share that information with foreign authorities.

Annex H attachment

The full text of the individual standards within each of the above documents that address matters of cross-border co-operation, information sharing, confidentiality, essential supervisory powers and practices, and customer identification and record-keeping are reproduced in full below, with the original reference numbers indicated. The use of bold, italics and underlining are generally as per the original documents. In some cases in the original texts the individual standards are supported by extensive supporting text, which is not reproduced here, but which should be read by anyone interested in gaining a fuller understanding of the rationale for the standard.

Information Sharing: Ten Key Principles (G-7)

1. **Authorisation to share and gather information:** Each Supervisor should have general statutory authority to share its own supervisory information with foreign supervisors, in response to requests, or when the supervisor itself believes it would be beneficial to do so. The decision about whether to exchange information should be taken by the Provider, who should not have to seek permission from anyone else. A Provider should also possess adequate powers (with appropriate safeguards) to gather supervisory information sought by a Requestor.

Lack of sufficient authority can impede information sharing. Without a power to gather information for other supervisors, a Provider may be limited to providing only information it already holds, or that it can obtain voluntarily, or from public files.

2. **Cross-sector information sharing:** Supervisors from different sectors of financial services should be able to share supervisory related information with each other both internationally (a securities supervisor in one jurisdiction and a banking supervisor in another) and domestically.
4. **Information about individuals:** Supervisors should have the authority to share objective information of supervisory interest about individuals such as owners, shareholders, directors, managers or employees of supervised firms.

Supervisors should be able to share objective information about individuals as they can about firms and other entities.

5. **Information sharing between exchanges:** Exchanges in one jurisdiction should be able to share supervisory information with exchanges in other jurisdictions, including information about the positions of their members.

Exchanges have a supervisory function in many jurisdictions. Where they do, they need to be able to share supervisory information to form a view on the potential impact of market events, on its members, and on the customers, counterparties, and financial instruments affected by it.

6. **Confidentiality:** A Provider should be expected to provide information to a Requestor that is able to maintain its confidentiality. The Requestor should be free to use such information for supervisory purposes across the range of its duties, subject to the minimum confidentiality standards set out in Appendix B.

While most Providers, quite properly, require a Requestor to maintain the confidentiality of information, as a condition of providing it, they should not seek to limit its use, by the Requestor, in carrying out its supervisory duties, including use in connection with (depending on legal arrangements in the country) administrative, civil or criminal cases where the Requestor, or another public authority, is a party to an action which arise from the exercise of those duties.

9. **Cases which further supervisory purposes:** In order to ensure the integrity of firms and markets, the Provider should permit the Requestor to pass on information for supervisory or law enforcement purposes to other supervisory and law enforcement agencies in its jurisdiction that are charged with enforcing relevant laws, in cases which further supervisory purposes.

The criminal, civil and administrative components of a jurisdiction's securities, banking and insurance laws are sometimes enforced by a number of agencies. Restrictions should not be so onerous that they can prevent the effective sharing of information. For example, exchange of information between supervisors, in cases which further supervisory purposes, should not be subject to the constraint that it cannot be passed to criminal authorities, though this should not be used to circumvent established channels of co-operation.

Appendix B

A Requestor should keep confidential non-public information that it receives from a Provider. This means that non-public information will not be disclosed, except in connection with supervisory purposes specified by the Requestor, or when asked for by the legislative body in the Requestor's jurisdiction – which may itself be subject to confidentiality rules – where that body could otherwise compel disclosure, or when required to produce documents or testimony by a court in a proceeding in which the Requestor or its government is a party. In any event, a Requestor will provide no less protection to non-public information received from a Provider than it affords its non-public domestic information. In cases involving requests by the legislative body or the courts the Provider should be notified of the onward disclosure, when possible. In all other cases—except in an emergency—the Requestor requires the permission of the Provider to disclosure information.

* * * *

Ten Key Principles for the Improvement of International Co-operation Regarding Financial Crimes and Regulatory Abuse (G-7)

While remaining consistent with fundamental national and international legal principles and essential national interests, countries should:

3. provide accessible and transparent channels for co-operation and exchange of information on financial crime and regulatory abuse at the international level, including effective and efficient gateways for the provision of information. Instruments such as Memoranda of Understanding and Mutual Legal Assistant Treaties can be very valuable in setting out the framework for co-operation but their absence [the absence of MoU or MLAT] should not preclude the exchange of information;
4. at the international level, either introduce or expand direct exchange of information between law enforcement authorities and financial regulators or ensure that the quality of national co-operation between law enforcement authorities and financial regulators permits a fast and efficient indirect exchange of information;

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5. ensure that law enforcement authorities and financial regulators are able to supply information at the international level spontaneously as well as in response to requests and actively encourage this where it would support further action against financial crime and regulatory abuse;
6. provide that their laws and systems enable foreign financial regulators and law enforcement authorities with whom information on financial crimes or regulatory abuse is shared to use the information for the full range of their responsibilities subject to any necessary limitations established at the outset;
7. provide that foreign financial regulators and law enforcement authorities with whom information on financial crimes or regulatory abuse is shared are permitted, with prior consent, to pass the information on for regulatory or law enforcement purposes to other such authorities in that jurisdiction. Proper account should be taken of established channels of co-operation, such as mutual legal assistance statutes and treaties, judicial co-operation, Memoranda of Understanding, or informal arrangements;
8. provide that their law enforcement authorities and financial regulators maintain the confidentiality of information received from a foreign authority within the framework of key principles 6 and 7, using the information only for the purposes stated in the original request, or as otherwise agreed, and observing any limitations imposed on its supply. Where an authority wishes to use the information for purposes other than those originally stated or as otherwise previously agreed, it will seek the prior consent of the foreign authority;
9. ensure that the arrangements for supplying information within regulatory and law enforcement co-operation framework are as fast, effective and transparent as possible. Where information cannot be shared, parties should as appropriate discuss the reasons with one another;

* * * *

Principles for Supervisory Information Sharing (Joint Forum)

2. Supervisors should be proactive in raising material issues and concerns with other supervisors. Supervisors should respond in a timely and satisfactory manner when such issues and concerns are raised with them.
3. Supervisors should communicate emerging issues and developments of a material and potentially adverse nature, including supervisory actions and potential supervisory actions, to the primary supervisor in a timely manner.
4. The primary supervisor should share with other relevant supervisors information affecting the regulated entity for which the latter have responsibility, including supervisory actions and potential supervisory actions, except in unusual circumstances when supervisory considerations dictate otherwise.

* * * *

The Supervision of Cross-Border Banking (BCBS & OGBS)

- i In order to exercise comprehensive consolidated supervision of the global activities of their banking organisations, home supervisors must be able to make an assessment of all significant aspects of their banks' operations that bear on safety and soundness, wherever those operations are conducted and using whatever evaluative techniques are central to their supervisory process.

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- ii Home supervisors need to be able to verify that quantitative information received from banking organizations in respect of subsidiaries and branches in other jurisdictions is accurate, and to reassure themselves that there are no supervisory gaps.
- iii While recognising that there are legitimate reasons for protecting customer privacy, the working group believes that secrecy laws should not impede the ability of supervisors to ensure safety and soundness in the international banking system.
- iv If the home supervisor needs information about non-deposit operations, host supervisors are encouraged to assist in providing the requisite information to home supervisors if this is not provided through other supervisory means. The working group believes it is essential that national legislation that in any way obstructs the passage of non-deposit supervisory information be amended.
- x Subject to appropriate protection for the identity of customers, home supervisors should be able, at their discretion, and following consultation with the host supervisor, to carry out on-site inspections in other jurisdictions for the purposes of carrying out effective comprehensive consolidated supervision. This ability should include, with the consent of the host supervisor and within the laws of the host country, the right to look at individual depositors' names and relevant deposit account information if the home supervisor suspects serious crime as defined in section (d). If a host supervisor has reason to believe that the visit is for non-supervisory purposes, it should have the right to prevent the visit taking place or to terminate the inspection.
- xvi In the case of information which is *specific to the local entity*, an early sharing of information may be important in enabling a potential problem to be resolved before it becomes serious. The home supervisor should therefore consult the host supervisor in such cases and the latter should report back on its findings. In particular, it is essential that the home supervisor inform the host supervisor immediately if the former has reason to suspect the integrity of the local operation, the quality of its management or the quality of internal controls being exercised by the parent bank.
- xxiii The supervisor that licenses a so-called shell branch has responsibility for ensuring that there is effective supervision of that shell branch. No banking operation should be permitted without a licence, and no shell office should be licensed without ascertaining that it will be subject to effective supervision. In the event that any host supervisor receives an application to license a new shell branch that will be managed in another jurisdiction, that supervisor should take steps to notify both the home supervisor and the appropriate host supervisor in the other jurisdiction in order to establish that there will be appropriate supervision of the branch before approving the application.
- xxv Where the home authority wishes to inspect on-site, they should be permitted to examine the books of the shell branch wherever they are kept. The working group believes that in no case should access to these books be protected by secrecy requirements in the country that licenses the shell branch.

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Core Principles for Effective Banking Supervision (BCBS)

Licensing and Structure

- 3. The licensing authority must have the authority 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 organisation'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 organisation is a foreign bank, the prior consent of its home country supervisor should be obtained.

Methods of Ongoing Banking Supervision

18. Banking supervisors must have a means of collecting, reviewing and analysing prudential reports and statistical returns from banks on a solo and consolidated basis.
19. Banking supervisors must have a means of independent validation of supervisory information either through on-site examinations or use of external auditors.
20. An essential element of banking supervision is the ability of the supervisors to supervise the banking group on a consolidated basis.

Cross-border banking

23. Banking supervisors must practise global consolidated supervision over their internationally-active banking organisations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organisations worldwide, primarily at their foreign branches, joint ventures and subsidiaries.
24. A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved, primarily host country supervisory authorities.
25. Banking supervisors must require the local operations of foreign banks to be conducted to 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.

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Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations (Insurance Concordat) (IAIS)

Principle 3

The creation of a cross-border insurance establishment should be subject to consultation between the host and home supervisors.

20. **Information Needs of Supervisors** – The principal requirement of the home supervisor is to ensure that its information needs from the parent insurer are fully met in a timely fashion. This will typically require a sound and verifiable system of reporting from any foreign establishment to the head office or parent insurer, and that practical solutions be found for dealing with particular information needs. To this end:

(2nd bullet) - If a host supervisor identifies, or has reason to suspect, problems of a material nature in a foreign establishment, it should take the initiative to inform the home supervisor, subject to its own judgement. The level of materiality will vary according to the nature of the problem. Home supervisors may wish to inform host supervisors as to the precise levels of materiality which would trigger their concern. However, the host supervisor is often in the best position to detect problems and therefore should be ready to act on its own initiative.

(3rd bullet) - Home supervisors may wish to seek an independent check on data reported by an individual foreign establishment. Where inspection by home supervisors is permitted, host supervisors should welcome such inspections. Where inspection by home supervisors is not at present possible (or where the home supervisor does not use the inspection process), the home

supervisor can consult the host supervisor with a view to the host supervisor checking or commenting on designated features of the insurer's activities. It is desirable that the results obtained should be available to both host and home supervisor.

21. Host supervisors should make the home supervisor aware of any material difficulties arising from the provision of insurance on a cross-border services basis.
22. **Information needs of host supervisors** - Host supervision of foreign establishments will be more effective if it is undertaken with an awareness of the extent to which the home supervisor of the immediate parent insurer monitors the foreign establishment and of any prudential constraints placed on the parent insurer or the group as a whole. To this end:
 - Home supervisors should inform host supervisors of changes in supervisory measures which have a significant bearing on the operations of their insurers' foreign establishments, subject to their own judgement. Home supervisors should respond positively to approaches from host supervisors for factual information covering, for example, the scope of the activities of a local establishment, its role within the insurance group and the application of internal controls and for information relevant for effective supervision by host supervisors.
 - Where a home supervisor has doubts about the standard of host supervision in a particular jurisdiction and, as a consequence, is envisaging action which will affect foreign establishments in the jurisdiction concerned, the home supervisor should consult the host supervisor in advance.
 - In the case of particular insurers, home supervisors should be ready to take host supervisors into their confidence as much as possible. Even in sensitive cases such as impending changes of ownership or when an insurer faces problems, liaison between home and host supervisors may be mutually advantageous, though decisions on both substance and timing on such sensitive issues can only be taken by case.
23. Home supervisors should respond positively to approaches from host supervisors seeking factual information on individual insurers known to be providing insurance on a cross-border services basis.
25. **Confidentiality constraints on the flow of information** - Jurisdictions whose confidentiality requirements continue to constrain or prevent the sharing of information for supervisory purposes with insurance supervisors in other jurisdictions, and the countries where information received from a foreign supervisor cannot be kept confidential, are urged to review their requirements in consideration of the following conditions:
 - Information received should only be used for purposes related the supervision of financial institutions.
 - Information sharing arrangements should allow for a two way flow of information, but strict reciprocity in respect of the format and detailed characteristics of the information should not be demanded.
 - The confidentiality of information transmitted should be legally protected, except in the event of criminal prosecution. All insurance supervisors should, of course, be subject to professional secrecy constraints in respect of information obtained in the course of their activities, including during the conduct of on-site inspections.
 - The recipient should undertake, where possible, to consult with the supervisor providing the information if he proposes to take action on the evidence of the information received.

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Resolution on Principles for Record Keeping, Collection of Information, Enforcement Powers and Mutual Co-operation to Improve the Enforcement of Securities and Futures Laws (IOSCO)

- A. **Record Keeping.** Contemporaneous records should be maintained sufficient to reconstruct all securities and futures transactions subject to regulation.
- B. **Collection of Information.** Competent authorities within each IOSCO member's jurisdiction should have the power to require information identifying persons who beneficially own or control any public companies or any other entities and business organisations with a direct or indirect interest in publicly held companies; and beneficially own or control bank accounts and brokerage accounts.
- C. **Enforcement of Securities and Futures Law and International Co-operation.** As provided in the *Resolution on Enforcement Powers* adopted by the Presidents' Committee on November 14, 1997, each member of IOSCO should strive to ensure that it or another authority in its jurisdiction has the necessary authority to obtain information, including statements and documents that may be relevant to investigating and prosecuting potential violations of laws and regulations relating to securities and futures transactions; and that such information can be shared directly with other IOSCO members or indirectly through authorities in their jurisdictions for use in investigations and prosecutions of securities and futures violations.
- D. **Removal of Impediments to Co-operation.** Each IOSCO member should assess the legislative framework in its own jurisdiction to determine whether it has the necessary authority to co-operate and share information with other IOSCO members and, to the extent necessary, should work with the appropriate domestic government authority to identify and remove any impediments to such co-operation.

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Objectives and Principles of Securities Regulation (IOSCO)

B. Principles for the Enforcement of Securities Regulation

- 8. The regulator should have comprehensive inspection, investigation and surveillance powers.
- 9. The regulator should have comprehensive enforcement powers.
- 10. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.

D. Principles for Co-operation in Regulation

- 11. The regulator should have authority to share both public and non-public information with domestic and foreign counterparts.
- 12. Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts.
- 13. The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.

FATF Forty Recommendations on Money Laundering

Customer Identification and Record-keeping Rules

10. Financial institutions should not keep anonymous accounts or accounts in obviously fictitious names: they should be required (by law, by regulations, by agreements between supervisory authorities and financial institutions or by self-regulatory agreements among financial institutions) to identify, on the basis of an official or other reliable identifying document, and record the identity of their clients, either occasional or usual, when establishing business relations or conducting transactions in particular opening of accounts or passbooks, entering into fiduciary transactions, renting of safe deposit boxes, performing large cash transactions).

In order to fulfil identification requirements concerning legal entities, financial institutions should, when necessary, take measures:

- (i) to verify the legal existence and structure of the customer by obtaining either from a public register or from the customer or both, proof of incorporation, including information concerning the customer's name, legal form, address, directors and provisions regulating the power to bind the entity.
 - (ii) to verify that any person purporting to act on behalf of the customer is so authorised and identify that person.
11. Financial institutions should take reasonable measures to obtain information about the true identity of the persons on whose behalf an account is opened or a transaction conducted if there are any doubts as to whether these clients or customers are acting on their own behalf, for example, in the case of domiciliary companies (i.e. institutions, corporations, foundations, trusts, etc. that do not conduct any commercial or manufacturing business or any other form of commercial operation in the country where their registered office is located).
12. Financial institutions should maintain, for at least five years, all necessary records on transactions, both domestic or international, to enable them to comply swiftly with information requests from the competent authorities. Such records must be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved if any) so as to provide, if necessary, evidence for prosecution of criminal behaviour.

Financial institutions should keep records on customer identification (e.g. copies or records of official identification documents like passports, identity cards, driving licenses or similar documents), account files and business correspondence for at least five years after the account is closed.

These documents should be available to domestic competent authorities in the context of relevant criminal prosecutions and investigations.

Administrative Co-operation

Exchanges of information relating to suspicious transactions

32. Each country should make efforts to improve a spontaneous or "upon request" international information exchange relating to suspicious transactions, persons and corporations involved in those transactions between competent authorities. Strict safeguards should be established to ensure that this exchange of information is consistent with national and international provisions on privacy and data protection.

Basis and means for co-operation in confiscation, mutual assistance and extradition

33. Countries should try to ensure, on a bilateral or multilateral basis, that different knowledge standards in national definitions - i.e. different standards concerning the intentional element of the infraction - do not affect the ability or willingness of countries to provide each other with mutual legal assistance.
34. International co-operation should be supported by a network of bilateral and multilateral agreements and arrangements based on generally shared legal concepts with the aim of providing practical measures to affect the widest possible range of mutual assistance.
35. Countries should be encouraged to ratify and implement relevant international conventions on money laundering such as the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime.

Focus of improved mutual assistance on money laundering issues

36. Co-operative investigations among countries' appropriate competent authorities should be encouraged. One valid and effective investigative technique in this respect is controlled delivery related to assets known or suspected to be the proceeds of crime. Countries are encouraged to support this technique, where possible.
37. There should be procedures for mutual assistance in criminal matters regarding the use of compulsory measures including the production of records by financial institutions and other persons, the search of persons and premises, seizure and obtaining of evidence for use in money laundering investigations and prosecutions and in related actions in foreign jurisdictions.