

**IMMEDIATE
ATTENTION**

SM/07/148

May 3, 2007

To: Members of the Executive Board

From: The Secretary

Subject: **Gibraltar—Assessment of Financial Sector Supervision and Regulation**

Attached for the **information** of Executive Directors is a paper on the assessment of financial sector supervision and regulation for Gibraltar. Management has consented to a request from the authorities of Gibraltar to publish the assessment and it will be posted on the Fund's external website after **May 10, 2007**.

Questions may be referred to Mr. Darbar, MCM (ext. 34252).

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

GIBRALTAR

ASSESSMENT OF FINANCIAL SECTOR SUPERVISION AND REGULATION

Prepared by the Monetary and Capital Markets Department
(In consultation with other Departments)

Approved by Jaime Caruana

May 2, 2007

This report is based primarily on work undertaken during a visit to Gibraltar during March 1–17, 2006.

The assessment team comprised Mr. R. Barry Johnston (Head), Mr. Salim M. Darbar, Ms. Tanya Smith, Ms. Mariela Moreno (all MCM), Mr. Joseph Myers, Mr. Andrews Gors, and Ms. Joy Smallwood (all LEG), Mr. Peter Hayward (consultant, for banking), Mr. Jorge Mogrovejo (consultant, Superintendency of Banks and Insurance, Peru, for banking), and Mr. William McCullough (consultant, for insurance). The assessment team received excellent cooperation from the authorities and market participants. The main findings of the assessment are:

- Gibraltar has a well-regulated financial sector and the authorities have taken a number of steps to implement recommendations of the last IMF assessment in 2001.
- The assessment found a high standard of compliance with the Basel Core Principles and the Insurance Core Principles.
- While Gibraltar has done a good job of improving its AML/CFT regime to keep abreast of evolving standards, it needs to take a number of steps to update its legal and regulatory regime to reflect the revised FATF 40+9 Recommendations.
- The reputation of Gibraltar as a financial center will depend on maintaining the independence of the Financial Services Commission (FSC).

The main authors of this report are R. Barry Johnston and Salim M. Darbar with contributions from the rest of the team.

The AFSSR is a summary report on implementation of the indicated financial sector regulatory standards. It has been developed to help jurisdictions identify and remedy weaknesses in financial sector supervision and regulation. The reviews do not directly assess risks such as those associated with asset quality, markets, or fraud that could affect the soundness of financial systems or individual institutions.

Contents	Page
Glossary	3
Executive Summary	4
I. Introduction	6
A. Political and Economic Background.....	6
II. Financial System Overview	7
A. Overview of the Legal and Institutional Framework	7
B. Financial Institutions and Market.....	9
C. Findings from Earlier Assessments and Authorities Response.....	10
III. Main Findings and Recommendations.....	11
A. Cross-Sector Issues	11
B. Sectoral Assessments	13
Financial Action Task Force Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism.....	25
Table	
1. Gibraltar: Financial System, 2001–06	16
Box	
1. Priority Recommendations.....	5
Appendix	
I. Reports on the Observance of Standards and Codes	17
Appendix Tables	
2. Recommended Action Plan to Improve Compliance of the Basel Core Principles.....	21
3. Recommended Action Plan to Improve Observance of IAIS Insurance Core.....	25
4. Ratings of Compliance with FATF Recommendations	31
5. Recommended Action Plan to Improve the AML/CFT System.....	37

GLOSSARY

AML	Anti-money Laundering
AMLGNs	Anti-Money Laundering Guidance Notes
APR	Approved Persons Regime
BCBS	Basel Committee on Banking Supervision
BCP	Basel Core Principles
CDD	Customer Due Diligence
CFT	Combating the Financing of Terrorism
CIS	Collective Investment Schemes
CJO	Criminal Justice Ordinance
DNFBP	Designated Nonfinancial Businesses and Professions
DTOO	Drug Trafficking Offence Ordinance
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
FSA	Financial Services Authority
FSC	Financial Services Commission
FSCO	Financial Services Commission Ordinance
GCID	Gibraltar Criminal Intelligence Division
GFIU	Gibraltar Financial Intelligence Unit
GO	Gambling Ordinance
GRA	Gibraltar Regulatory Authority
IAIS	International Association of Insurance Supervisors
ICP	IAIS Insurance Core Principles
ICSFT	International Convention for the Suppression of the Financing of Terrorism
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
IMF	International Monetary Fund
LEG	Legal Department, IMF
MCM	Monetary and Capital Markets Department, IMF
ML	Money Laundering
MLA	Mutual Legal Assistance
MMOU	Multilateral Memorandum of Understanding
MOU	Memorandum of Understanding
OFC	Offshore Financial Center
OGBS	Offshore Group of Banking Supervisors
PEP	Politically Exposed Person
PIN	Public Information Notice
ROSC	Report on Observance of Standards and Codes
STR	Suspicious Transaction Reporting
TCSP	Trust and Company Service Provider
TF	Terrorism Financing
UCITS	Undertakings for Collective Investment in Transferable Securities
UNSCR	UN Security Council Resolution
VAT	Value-added tax

EXECUTIVE SUMMARY

Gibraltar has a well-regulated financial sector. The Gibraltar authorities are concerned with protecting the reputation and integrity of Gibraltar as a financial center, and are cognizant of the importance of adopting and applying international regulatory standards and best supervisory practices. Gibraltar has a good reputation internationally for cooperation and information sharing.

The authorities have taken a number of steps to implement the recommendations of the last IMF assessment in 2001. In particular, the Financial Services Commission (FSC) has been assigned significant additional resources and has developed a well structured approach to the management of its resources that includes a risk-based approach to supervision.

The reputation of Gibraltar as a financial center will depend on maintaining the independence of the FSC. Steps taken to implement a governance structure of the FSC that would bring it into line with best international practice should be helpful in this regard.

The assessment found a high standard of compliance with the Basel Core Principles for banking supervision. Prudential requirements are based on EU requirements and U.K. prudential rules and practices as required by the Banking Ordinance. The risk-based supervision system introduced in 2001, and recently enhanced, is well-designed.

The assessment found that the insurance supervision was compliant with the majority of the Insurance Core Principles. On site inspections are being undertaken on a risk-based approach. The FSC has confirmed that attention is being given to increasing the number of supervisors to achieve a higher rate of on-site inspections in a growing sector.

The Gibraltar authorities have done a good job of improving their AML/CFT regime to keep abreast of evolving standards. Gibraltar authorities take a practical approach to implementing AML/CFT controls, and they have focused much of their resources and attention on providing effective international cooperation. Nevertheless, Gibraltar needs to take a number of steps to move its legal and regulatory regime forward to reflect the revised FATF 40 + 9 Recommendations:

- The criminal laws on money laundering should be consolidated, and proposed legislation on mutual legal assistance should be enacted.
- The FSC's Anti-Money Laundering Guidance Notes need to be updated to cover terrorist financing, and some of the key provisions currently in the guidance notes need to be reflected in law or regulation.
- Bureaux de change and money transmitters should be supervised for AML/CFT compliance, and the Government needs to conduct risk assessments of a number of designated non-financial businesses and professions and, as appropriate, extend AML/CFT supervision to them, as well.

Box 1 provides the priority recommendations.

Box 1. Priority Recommendations

Governance of the FSC

- The FSC should adopt a governance structure in line with best international practice. This would help it to continue to maintain its independence.
- The FSC should be granted the authority to set its own fees.

Banking

- Legislation should be amended to require the FSC to indemnify staff for costs that arise in defending themselves against legal action.

Insurance

- Legislation relating to the “Approved Persons Regime” should be introduced without delay.
- Attention should continue to be given to increasing the number of supervisors and to training of supervisors to achieve a higher rate of on-site inspections in a growing sector.

AML/CFT

- Criminal laws should be consolidated, and powers presently available only in drug-related money-laundering cases should be extended to money laundering cases involving the proceeds of other crimes.
- Proposed legislation on mutual legal assistance should be enacted.
- Prosecutors and police should pursue cases as they arise to create a deterrent against misfeasance by professional service providers.
- The FSC should update its AML Guidance Notes to reflect risks associated with terrorist financing.
- Bureaux de change and money transmitters should be supervised for compliance.
- The government should conduct risk assessments of designated non-financial businesses and professions not presently supervised and, as appropriate, extend authority for monitoring for compliance with AML/CFT requirements to them, as well.

I. INTRODUCTION

1. **This report provides an assessment of Gibraltar's compliance with respect to international standards in banking, insurance, and anti-money laundering and combating the financing of terrorism (AML/CFT), respectively:**

- The Basel Core Principles for Effective Banking Supervision (BCP);
- The International Association of Insurance Supervisors (IAIS), insurance core principles (ICP) and;
- The Financial Action Task Force (FATF) 40+9 Recommendations on AML/CFT.

2. **This assessment is a follow-up to the one undertaken in 2001 in the first phase of the offshore financial center (OFC) program¹ and has provided an opportunity to take into account the revision in standards.²** The assessment of the AML/CFT regime is based on the revised 2003 FATF 40+9 Recommendations and covers trust and company service providers and other designated nonfinancial business and professions. The ICP were also revised in 2003, and the insurance sector has been assessed using the updated standard and methodology.

3. **Though relatively small in absolute terms, Gibraltar's financial center is important to its economy, and Gibraltarians universally place a high priority on maintaining Gibraltar's reputation as a well regulated center.** Gibraltar has welcomed multiple external reviews of its system by the Offshore Group of Banking Supervisors (OGBS), the IMF, and the United Kingdom (U.K.).

A. Political and Economic Background

4. **Gibraltar is an overseas territory of the United Kingdom.** Gibraltar and the U.K. Government recently agreed to a new Gibraltar Constitution that provides for a modern relationship between Gibraltar and the United Kingdom. Gibraltar has been a constituent of the European Union (EU) since 1973 under the U.K. Treaty of Accession. However, it is excluded from the common external tariff, the common agricultural policy, and the requirement to levy value-added tax (VAT).

¹ In 2003 the IMF Executive Board agreed that the IMF should conduct periodic assessments (every 4–5 years) to monitor progress as well as ensure that good supervisory practice has been maintained. See PIN No. 03/138 at <http://www.imf.org> for a summary of the Executive Board discussion.

² The last IMF assessment addressed AML issues mainly via the BCP and ICP assessments. A mutual evaluation of the AML regime, based on the then-current FATF Recommendations, was conducted by the Offshore Group of Banking Supervisors (OGBS) in 2001, prior to the development of an agreed methodology.

5. **Gibraltar's economy is dominated by three sectors—tourism, ports and shipping, and financial services.** Over the past two decades the economy has transformed significantly from one based on the provision of services to the Ministry of Defense to one increasingly reliant on the provision of financial services. Recently, internet gambling firms have established operations in Gibraltar providing further employment opportunities. Gibraltar has a population of about 30,000 with per capita GDP of some £18,000 in 2002/03.

6. **Fiscal policy, and in particular tax policy, has helped to diversify the economy.** Since 1967 an exempt company regime has applied to corporate taxation. Exempt companies are those that are not owned by Gibraltarians and do not do business domestically, and are thus exempt from paying corporate taxes. Otherwise effective corporate tax rates range from 20 to 35 percent. There are no capital gains tax, wealth tax, inheritance tax, estate duty, VAT, or sales tax. Personal income tax contributes the bulk of fiscal revenue. The government plans to reform the tax regime to comply with the European Union's state aid rules.³ A new tax regime is expected to be in place by July 2007.⁴ The exempt tax regime is to be phased out by 2010 and starting July 2006 no new entities will be given an exempt status.

7. **Gibraltar's financial service sector has benefited from access to the EU market, through "passporting."**⁵ The number of entities seeking to passport out of Gibraltar has been increasing in recent years, particularly in the insurance sector. Gibraltar has also developed a skilled pool of labor and expertise in the financial services sector.

II. FINANCIAL SYSTEM OVERVIEW

A. Overview of the Legal and Institutional Framework

8. **The FSC is the unified regulatory and supervisory authority for financial services.** The FSC is responsible for supervision of banks and building societies, investment businesses, insurance companies, investment services, company management, professional trusteeship, insurance management, and insurance mediation. The FSC was established under the FSC Ordinance (FSCO) 1989.

³ Broadly, state aid rules aim to ensure that that government interventions do not distort competition and do not provide unfair advantage to select enterprises over their competitors (see http://ec.europa.eu/comm/competition/state_aid/overview/). In the case of Gibraltar the exempt company regime could be inconsistent with EU state aid rules.

⁴ In this context a package of reforms has been submitted to the EU for approval, and the EU's response is expected by end-2006. The main features of this tax package include: abolition of the current corporate tax regime and replacing it with: a profit tax on financial service providers; a payroll tax; a business property occupation tax; annual company registration fee; and profit tax on utility companies.

⁵ Under the EU's "passporting" provision, institutions (banks, insurance companies, and investment firms) incorporated in Gibraltar can provide cross-border financial services to clients in European Economic Area (EEA) states and vice-versa. Separate agreements on passporting banking, insurance, and investment services to the United Kingdom have been reached.

9. **The governance structure of the FSC is somewhat unique.** The Governor of Gibraltar with the approval of the U.K. Foreign and Commonwealth Secretary appoints an eight member Commission with the Commissioner as Chairman. While the Commission has broad supervisory and regulatory responsibilities, the key implementation authorities are vested in the Commissioner through separate legislation such as the Banking Ordinance (1992) and the Insurance Companies Ordinance (1987). The main statutory accountability of the FSC is an obligation to undergo periodic reviews, commissioned by the Governor of Gibraltar. In those areas to which EU law applies, these reviews monitor the extent to which Gibraltar legislation and supervision of licensed institutions: (i) comply with EU obligations; and (ii) establish and implement standards which match those required by legislation and supervisory practice governing the provision of financial services within the United Kingdom. The latest such statutory review was undertaken during 2004, and the report was published in 2005.⁶

10. **The main legal instruments governing the regulation and supervision of the financial system, in addition to the FSCO (1989), are:**

- The Banking Ordinance (1992) (and subsequent amendments) provides the Commissioner power to license and supervise banking and other categories of deposit-taking business in Gibraltar.
- The Insurance Companies Ordinance (1987) provides the powers to regulate and restrict the conduct of the business of insurance; for the licensing of insurers, the winding up of insurance companies and other related matters. Insurance intermediaries are licensed through the Financial Services Ordinance (1989). A Protected Cell Companies Ordinance was enacted in 2001 to provide for the incorporation and supervision of protected cell companies.
- The Financial Services Ordinance (1989 and 1998) and the Financial Services (Collective Investment Schemes) Ordinance 2005 provide for the licensing and supervision of investment business including the promotion, establishment and operation of collective investment schemes and the establishment and operation of investment exchanges and clearing houses. These Ordinances also provide for the licensing and supervision of company and trust service providers.

11. **The Gibraltar legal framework for money laundering is well developed.** It is divided into two fundamental statutes—the Drug Trafficking Offences Ordinance (1995) (DToo) and the Criminal Justice Ordinance (1995) (CJO). Terrorism financing is addressed by the Terrorism Ordinance (2005) and the Terrorist Order issued by the United Kingdom in 2001 and 2002. Gibraltar has a police-style financial intelligence unit (FIU) embedded in its joint police/customs, the Gibraltar Criminal Intelligence Division (GCID), that is a member

⁶ Review of the Supervisory Activities of the Gibraltar Financial Services Commission and the Financial Services Commissioner, January 2005 (see <http://www.fsc.gi/review/downloads.htm>).

of the Egmont Group. The FSC is responsible for AML/CFT supervision of the entities it supervises and in this context it has issued Anti-Money Laundering Guidance Notes (AMLGNs).

B. Financial Institutions and Market

12. **Gibraltar's financial sector consists primarily of branches or subsidiaries of international firms** (see Table 1 for an overview of the financial system). Given the limited size of the domestic market, most of the firms have established themselves in Gibraltar to provide services to nonresidents. While there is competition among these firms for nonresident clients most have identified a niche market or product (see below).

13. **All except one of the 18 banks are branches or subsidiaries of international banks.** Seven banks provide retail services to the very small domestic market, and for only two of these does this constitute a significant part of their business. The remainder focus almost exclusively on nonresident clients.

14. **The provision of investment services to nonresident clients is the most important function (in terms of value added) conducted by the banks in Gibraltar.** The banks provide various related services for wealth/asset management. The business may be directed to the banks through independent asset managers either located in Gibraltar or overseas, or through the parent offices, or acquired through Gibraltar based marketing efforts. Fiduciary deposits from parent banks are also a common feature of the banking industry in Gibraltar. The client base is made up mostly of European nationals who reside in this region for part of the year, and are interested in owning property in the region. Another important nonresident service provided by some of the banks, in addition to asset management functions, is mortgage lending for properties located in southern Spain and Portugal. For various tax reasons some banks book such activity out of their parent offices (e.g., in the United Kingdom). Nevertheless, the banks in Gibraltar provide all the administration services associated with such lending activity and it remains an important source of revenue for the Gibraltar banks.

15. **The insurance sector has been growing in recent years** (Table 1). A key reason for this is the ability of firms licensed in Gibraltar to passport their services to EU member states. As of March 2006, there were 50 insurance companies licensed in Gibraltar. Of these, seven had notified that they would be passporting their services by establishing a branch in other EEA states. Forty-two of the Gibraltar companies had notified that they would provide services to other EEA states and nine companies licensed in other EU states provide services in Gibraltar. Insurance managers who manage many of the companies licensed in Gibraltar also provide some brokering and accounting services. There are two locally incorporated firms that provide insurance services to Gibraltar residents. Gibraltar residents can however purchase insurance through branches or agencies of EEA companies.

16. **While most of the investment services are provided by banks there are a number of non-bank investment firms that also provide similar services** (Table 1). A majority of these provide portfolio management services either on a discretionary or non discretionary

basis, a few serve as securities brokers (investment dealers), and at least one provides spread betting services.⁷ There are also 48 collective investment schemes (CIS) registered of which only five are domiciled in Gibraltar and supervised directly by the FSC. Forty-three are recognized as UCITS or U.K. registered funds. Under the recent Financial Services (Experienced Investor Funds) Regulations (2005) six experienced investor funds have been established.⁸

17. **The number of company and trust service providers has been fairly stable in recent years** (Table 1). The sector is made up of large international firms and domestic firms with a mix of professional accountancy firms, legal firms, and pure company management firms. There are 14 bureaux de change and one money transmission agent outside the banking system.

18. **There has been significant growth in the online gaming industry in Gibraltar.** Fifteen licenses have been issued and employment in this sector has increased from 550 to about 1,350 people. These firms provide online gambling and sports betting services. Several of the firms are listed on the London Stock Exchange and two firms are very large global players. There is also one land-based casino located in Gibraltar. It has an annual turnover of about £ 6 million per year.

C. Findings from Earlier Assessments and Authorities Response

19. **The 2001 assessment covered the banking, insurance, and securities sectors, and trust and company service providers and found that supervision was generally effective.**⁹ The assessment of the AML regime was limited to related principles under the BCP and ICP standards. The report noted that Gibraltar meets most of the international standards and is making good progress with respect to those principles with which it is not yet fully compliant or observant. The banking assessment found that Gibraltar was compliant or largely compliant with all the principles of the standard. The insurance assessment found that Gibraltar was materially nonobservant with only one principle and was either observant or largely observant with the rest. Areas identified for improvement included supervisory resources, on-site inspections, legislative protection of FSC staff, monitoring banks' country risk, licensing procedures, and oversight of compliance with AML procedures.

⁷ Spread betting is more akin to gambling than investing. It allows the investor to speculate, for example, on the movement of stock price index. For instance a firm may quote a high and low position (spread) of the stock market index and the investor can bet if the index will end higher or lower.

⁸ Investment in such funds are limited to high net worth individuals or bodies (such as corporate, trustee of a trust, etc.) with a minimum net worth/assets of Euro 1 million or a participant who invests a minimum of Euro 100,000.

⁹ See "Gibraltar: Assessment of the Regulation and Supervision of Financial Services, October 2001" at <http://www.imf.org/External/NP/ofca/2001/eng/gbr/103101.pdf>.

20. **The mission found that the authorities have implemented most of the recommendations of the 2001 assessment.** The FSC has significantly increased the number of supervisory staff since 2001. On-site supervision has been addressed with the adoption of a risk-based supervisory approach. Implementation of some of the recommendations await the enactment of legislation. The revised FSC Ordinance would introduce protection of FSC staff from the cost of civil law suits and the draft Approved Persons Regime (APR) provides the power in certain instances to prevent select personnel from working in a licensed institution. With regard to imposing civil monetary penalties, the FSC is of the opinion that there are other measures that it can take which are equally or more effective, and the updated BCP assessment concurs with the authorities' views. In insurance, a review of corporate governance is ongoing. In securities, the FSC does not consider the industry large enough to justify introduction of self-regulatory organizations to augment its own efforts in regulating the securities industry.

21. **A 2005 Statutory Review of the FSC's obligations to match the supervisory standards of the United Kingdom in areas covered by the EU Directives was complementary of Gibraltar's supervisory standards.** The Review recommended changes in the organization and governance structure of the FSC, and noted the need to increase staff at the FSC, and to raise awareness and provide training to FSC staff on AML/CFT issues focusing on specific vulnerabilities related to services offered in Gibraltar. In the areas of governance the Review recommended the setting up of a traditional governance structure for the Commission: assignment of the regulatory powers and responsibilities to the Commission rather than the Commissioner; and appointment of a Chairman of the Commission separate from the Chief Executive who would be accountable to the Commission for its day-to-day operations.

III. MAIN FINDINGS AND RECOMMENDATIONS

A. Cross-Sector Issues

Legislative initiatives

22. **A number of legislative initiatives on the financial sector are at various stages of preparation**—a modernization of the FSCO, a draft money services business ordinance, an ordinance on an approved persons regime, and a bill to strengthen powers to obtain and exchange information. The authorities indicated that legislative reforms needed to safeguard the safety and soundness of the financial sector would be implemented promptly.

Governance of the FSC

23. **The current assignment of powers and responsibilities to the Commissioner and the FSC is rather unique and should be brought into line with international best practices.** The current arrangements in the FSC appear to have been implemented effectively

with a number of checks and balances.¹⁰ Nevertheless, it may be timely, concurrent with revisions to the constitution, to reform the FSC's governance structure to bring it into line with best international practice.¹¹

24. **The reputation of Gibraltar as a well regulated financial center will depend critically on maintaining the independence of the FSC in the exercise of its regulatory and supervisory functions.** Ensuring the independence of the regulator is a challenge, and can raise specific issues in small jurisdictions. Vesting the regulatory and supervisory powers in an independent and well constituted FSC Board rather than the Commissioner may be helpful in this regard. The Board members would need to be appointed in a transparent manner and, in view of Gibraltar's role as an international financial center, be made up of experienced representatives of high standing both from within Gibraltar and internationally. The FSC's accountability should also be clearly defined.

25. **The independence of the FSC would be further bolstered by providing it with the authority to set its own fees.** As concerns its budget, the FSC is partly dependent on Government subventions, and cannot fix fees payable to it which are the FSC's main source of income. Protection of the supervisory staff should be further strengthened by formalizing indemnification of any costs involved in staff defending litigation.

Cross-border Cooperation and Information Exchange

26. **Gibraltar authorities are to be commended for the resources they have devoted to international cooperation.** Information is shared through both formal and informal channels with foreign financial sector supervisors. Being a constituent of the EU facilitates cooperation and information sharing with EU member states. Gibraltar is also taking steps to further improve the mechanism for cooperation and information exchange (see below). The mission was also advised by several foreign supervisors that the FSC has cooperated and shared information in the past. In 2005, Gibraltar became a member of IOSCO and intends to sign IOSCO's Multilateral Memorandum of Understanding (MMOU) in 2007.

27. **As a constituent of the EU, Gibraltar is able to provide full cooperation at early stages of criminal investigations to EU member states.** Gibraltar has recently enacted legislation that extends the same privileges to non-EU member states, provided such states

¹⁰ The FSC has voluntarily published self-assessments against the IMF Code of Good Practices on Transparency in Monetary and Financial Policies (see <http://www.fsc.gi/imf/imftransparency.htm>) and Combined Code of Corporate Governance (see <http://www.fsc.gi/fsc/combinedcode.htm>).

¹¹ Since the assessment new legislation has been submitted to Parliament that will transfer the responsibility of appointing the Commissioner to the Gibraltar Government and make the Commission responsible for the powers currently vested in the Commissioner. In addition the new Act will also provide for the separation of the role of Chairman and Commissioner (who will become the Chief Executive Officer). The statutory reviews will continue under the new Act (but under the direction of the Gibraltar Government) which will require that they occur at least every four years. The Commission will also have direct fee raising and rule making powers (subject to ministerial consent).

agree to reciprocity. Further, recently published draft legislation would extend such privileges automatically to all states that have ratified the UN Transnational Organized Crime Convention. The draft legislation would also solve another limitation in Gibraltar's current law, namely that in non-drug related money laundering cases foreign states are not permitted to obtain restraint orders or register and enforce their confiscation orders in Gibraltar.

28. **Since being admitted to the Egmont Group in 2004, the Gibraltar FIU (GFIU) regularly shares information with other FIUs through the Egmont secure web system.** It has responded to all 40 requests it has received, and initiated ten requests. In several cases, the GFIU has been able to contribute to overseas investigations by taking the initiative to cooperate closely with other Egmont Group members.

29. **The FSC shares information with other pertinent international authorities subject to the relevant financial sector ordinances.** The Commissioner may share information with foreign supervisors when he/she is satisfied that the information will continue to be subject to confidentiality requirements. The FSC has concluded memoranda of understanding (MOUs) with several foreign supervisory authorities, and has also shared information with other authorities with which it has no formal agreements (in particular with those authorities that have supervisory responsibilities over banks or parents or affiliates of banks authorized in Gibraltar). The FSC has also put in place an internal process to ensure that information exchange takes place in a manner consistent with the laws. The FSC has also proposed a new Financial Services (Information and Cooperation: Powers and Confidentiality) Ordinance that would (i) consolidate all the powers related to cooperation and information exchange in the various ordinances; (ii) permit information exchange with other domestic agencies; and (iii) satisfy requirements to sign the IOSCO's MMOU.

B. Sectoral Assessments

30. **This section summarizes the findings in the assessments of standards and codes for banking, insurance and AML/CFT.** The Report on Observance of Standard and Codes (ROSCs) attached and detailed assessments provide more detailed information.

Banking

31. **The assessment found a high standard of compliance with the Basel Core Principles for bank supervision.** Prudential requirements are based on EU minimum requirements implemented via the Banking Ordinance 1992 and U.K. prudential rules as required by the FSC Ordinance. The effectiveness of the system for approving directors, managers, and key staff would be enhanced by the adoption of the proposed Approved Persons Regime.

32. **The risk-based supervision system introduced in 2001, and recently enhanced, is well-designed.** Risk is categorized and analyzed as per the following six groups: financial soundness and capital; environment; business plan; controls; organization; and management. A risk profile is obtained by calculating an impact score based on weighted risks for each of the above risk groups. The intensity of the supervisory program depends on the final risk

profile. The risk-based supervision recognizes the particular attributes of banking business in Gibraltar and the risks involved. Credit risk is low and usually well secured and there is little market and liquidity risk as these are managed by head offices. Credit concentrations are also low.

Insurance

33. **The assessment found that the insurance supervision was compliant with the majority of the Insurance Core Principles.** The insurance supervisory authority has established policy and objectives which are effectively considered in all aspects of supervision. The legislation clearly defining insurance regulation and supervision is in place and detailed guidance notes have been prepared to assist with practical application. The senior members of the insurance supervisory authority are experienced supervisors and have specific skills in insurance and financial reporting. The supervisors have adequate powers of intervention and enforcement which have been used when required. EU Directives are continually introduced and legislation is continually updated.

34. **The supervisory process for monitoring financial and other statutory reporting is of a high standard, and the authorities have been implementing on-site inspection of insurance companies and insurance managers following a risk based approach.** The FSC has confirmed that attention is being given to increasing the number of supervisors as well as to training of supervisors to achieve a higher rate of on-site inspections in a growing sector. While consumer protection is available to those policy holders in Gibraltar who are insured with U.K. companies and for U.K. policy holders insured with Gibraltar insurers, it is recommended that consideration be given to the introduction of legislation to provide protection to domestic insurance policy holders insured with Gibraltar insurers.

AML/CFT

35. **The Gibraltar authorities have done a good job of implementing improvements to Gibraltar's AML/CFT regime in banking (their largest sector) to keep in line with evolving standards in AML/CFT.** In other sectors of financial intermediation, the FSC is making considerable progress in enhancing the effectiveness of existing preventative measures. This is in common with many other jurisdictions where the regulation and supervision of the banking sector has been in existence for a longer period of time and where the focus of AML/CFT measures has been concentrated. Authorities take a practical approach to implementing AML/CFT controls, and they have focused much of their resources and attention on providing effective international cooperation.

36. **The principal AML risk to Gibraltar is lodged in its professional sector, which is exposed to the risk of being involved in the layering and integration of proceeds of crime.**¹² There is also some risk to Gibraltar at the placement stage, in connection with drug

¹² Money laundering is generally regarded as a dynamic, three-stage process involving "placement," "layering," and "integration." Placement refers to the introduction of illegal proceeds into the financial system (e.g., through

trafficking, migrant smuggling, and organized crime in southern Spain. Most money laundering cases involving Gibraltar arise out of investigations into international fraud schemes. Traditional organized crime and drug related cases, though important, comprise a minority of criminal investigations that touch Gibraltar's financial center. The professional sector of lawyers and accountants often introduces their clients to the financial sector institutions in Gibraltar.

37. Gibraltar needs to take a number of steps to move its legal and regulatory regime forward to reflect the revised FATF 40 plus 9 Recommendations. The criminal laws on money laundering should be consolidated, and powers presently available only in drug-related money laundering cases should be extended to money laundering cases involving the proceeds of other crimes. Prosecutors and police should pursue cases as they arise to create a deterrent against misfeasance by professional service providers. Proposed legislation on mutual legal assistance should be enacted. The Financial Service Commission's Anti-Money Laundering Guidance Notes need to be updated, inter alia, to reflect risks associated with terrorist financing, and some of the key provisions currently in the Guidance Notes need to be reflected in law or regulation. bureaux de change and money transmitters (non-bank) need to be supervised for AML/CFT compliance.¹³ Finally, the Government needs to conduct risk assessments of those designated non-financial businesses and professions that are not supervised by the FSC or GRA and, as appropriate, extend authority for monitoring for compliance with AML/CFT requirements to them, as well.

a bank deposit); layering refers to the process of separating the criminal proceeds from their source through layers of transactions designed to disguise the audit trail and to foil potential pursuit by law enforcement agencies; integration refers to the process of making the funds available for use in legitimate commerce or investment.

¹³ Since the assessment legislation to amend the Financial Services (Investment and Fiduciary Services) Act 1989 has been drafted that would make the FSC responsible for the licensing and supervision of bureaux de change and money transmission services.

Table 1. Gibraltar: Financial System, 2001–06

(as of end-March, unless otherwise specified)

	2001	2002	2003	2004	2005	2006
Banking						
Number	19	19	18	17	18	18
Branches	9	8	8	6	7	7
Subsidiaries	10	11	11	11	11	11
Total assets (end-December; in billions of £)	5.2	5.6	4.9	4.8	5.7	8.4
Assets under management (in billions of £)	5.9	5.5	5.2	5.2	5.2	6.5
Insurance						
Companies						
Number	17	22	31	39	46	50
Life	1	2	2	2	3	3
Non-life	6	10	16	24	30	33
Reinsurance	4	4	3	1	3	3
Captives	6	6	10	12	10	11
Total assets (in billions of £)	0.9	1.4	2.0	...
Intermediaries (number)	27	29	27	28	29	30
<i>Of which:</i> Life	20	20	20	20
Managers (number)	7	7	7	6	8	8
Investment						
Investment firms	24	26	23	22	25	26
Dealers	6	8	6	4	5	5
Managers	18	18	17	18	20	20
Principal dealer	0	0	0	0	0	1
Funds under management (in billions of £)	1.2	1.4	1.0	1.0	1.4	3.7
Collective Investment Schemes (CIS)						
CIS (recognized; UCITS/FSA)	44	44	44	42	42	43
CIS (authorized)	1	1	2	4	4	5
Total assets (in millions of £)	20.8	11.9	12.4	162.3	221.8	...
Experienced investor funds	n.a	n.a	n.a	n.a	n.a	6
Fund related activity						
CIS operator	1	3	2	3	2	1
CIS administrator	n.a	n.a	0	1	2	4
Trust and company service providers	83	78	78	80	82	82

Source: Gibraltar FSC

APPENDIX I. REPORTS ON THE OBSERVANCE OF STANDARDS AND CODES

Summary Assessment of Compliance with the Basel Core Principles for Effective Banking Supervision

General

38. This assessment of the Basel Core Principles for Effective Banking Supervision (BCP) was carried out in March 2006 as part of a Module 2 assessment of the regulation and supervision of the Gibraltar financial sector at the request of the Gibraltar government.¹⁴ The Gibraltar FSC and its staff cooperated fully with the assessment and their assistance is gratefully acknowledged.

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

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

41. A separate IMF team assessed Gibraltar's compliance with the FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT). Their assessment, based on the latest version of the methodology, amplifies the assessment of CP 15 which is based on the 1999 methodology of the Basel Committee.

Institutional and macroprudential setting, market structure—overview

42. The banking sector consists of 18 banks with total assets of £8.4 billion as of end-2006. Most of the banks are subsidiaries or branches of banks from other European countries, dominated by the United Kingdom with eight subsidiaries/branches in Gibraltar. There is only one bank which is not foreign-bank-owned and its shareholders are in the investment

¹⁴ The assessment was undertaken by Peter Hayward (consultant, formerly Bank of England and IMF) and Jorge Mogrovejo (consultant, Superintendency of Banks and Insurance, Peru).

business in a major European financial centre. No licensing distinction is made between banks conducting offshore and onshore business. The majority of business in the small local market is done by two banking groups. A major portion of offshore banking business is providing private banking services, mainly asset management to Swiss based customers and to the expatriate community in Spain and Portugal. This includes residential mortgages to clients purchasing property in the region. Another important component of offshore banking are services provided to nonresident trusts and companies which benefit from the exemption from Gibraltar's relatively high corporate tax rate of 35 percent.¹⁵

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

44. Gibraltar banks have a competitive advantage over banks in other small financial centers in being able to provide services throughout the EU using the so-called "passport" arrangements. Although Spanish and Portuguese banks could compete with Gibraltar banks for business of expatriates who reside in these countries they appear not to do so. Most expatriates in Spain and Portugal who are offshore clients of Gibraltar banks have accounts with local Spanish and Portuguese banks for money transmission and general banking services, but these local banks do not as yet offer significant competition for asset management and other private banking services. This business is therefore profitable and expanding for the Gibraltar banks. More typical offshore business for tax exempt companies and trusts with non-resident owners and beneficiaries is normally introduced by local law firms and other service providers. While the tax exemption is due to be phased out in order to comply with EU state aid rules, the business is believed to be able to survive if the new unified rate of corporate tax were not more than 10-15 percent.¹⁶

45. The FSC is a unified regulatory and supervisory authority for all financial services. The FSC supervises activity of banks, insurance companies, investment firms, collective

¹⁵ Some banks also benefit from this exemption but in many cases the benefit is offset by group tax arrangements in the home country.

¹⁶ A more damaging threat, regarded locally as extremely unlikely to materialize, arises from a case before the European Court of Justice, which could result in requiring Gibraltar to replicate completely the U.K. tax system.

investment schemes, and trust and company service providers. The FSCO requires that, since Gibraltar is considered as a part of the United Kingdom and, therefore, a constituent of the EU under the U.K. accession treaty, Gibraltar must ensure both that supervision complies with EU Directives, and that regulation and supervision in areas subject to EU supervisory legislative requirements match the standard of regulation and supervision in the United Kingdom. The statutory review mentioned above was designed to verify that the FSC met these obligations.

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

General preconditions for effective banking supervision

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

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

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

Main findings

50. The assessment revealed a high standard of compliance with the Basel Core Principles and the risk-based approach to supervision is well designed and implemented. The principle findings of the assessment are as follows:

- **Objectives, Autonomy, Powers, and Resources (CP 1).** The FSC supervises all financial institutions in Gibraltar and has established supervisory objectives and principle for good supervision and has publicized these. The FSC is effectively independent from political and commercial pressure in its operations, although it is partly dependent on Government subventions and cannot fix fees payable to it which are the FSC's main source of income. The legal framework is based on EU

requirements and is up to date. The FSC has sufficient powers and authority to ensure compliance with laws and ensure the safety and soundness of the financial system. Supervisors are protected from litigation although there is no formal indemnification of any costs involved in staff defending litigation. The FSC can and does share information with other supervisory authorities especially home supervisors of foreign banks in Gibraltar.

- **Licensing and Structure (CPs 2–5).** Only authorized banks may take deposits in Gibraltar and the licensing process is thorough. The effectiveness of the system for approving directors, managers, and key staff will be enhanced by the adoption of the proposed ‘approved persons’ regime. The FSC has sufficient powers to ensure that banks are owned only by reputable shareholders and nearly all the banks are in fact part of major international banking groups.
- **Prudential Regulations and Requirements (CPs 6–15).** Prudential requirements are based on EU minimum requirements and U.K. prudential rules as the FSC is required to ensure its standards match those of the United Kingdom. The risk-based supervision system introduced in 2001, but recently enhanced, is well designed. It recognizes the particular attributes of banking business in Gibraltar and the risks involved. Credit risk is low and usually well secured and there is little market and liquidity risk as these are taken in head offices. Credit concentrations are low.
- **Methods of Ongoing Supervision (CPs 16–20).** The FSC has been relying less on the use of reporting accountants and has supplemented its off-site supervision with a structured system of on-site work by FSC staff. The relatively infrequent nature of this work reflects the low risk business in the banking system. However, contact with bank management is frequent and ordered. The reporting system is comprehensive and is validated through reliance on internal and external audit as well as FSC staff visits. The FSC has powers to undertake consolidated supervision but has not needed to use them so far.
- **Information Requirement (CP 21).** Accounting standards are high and most banks belong to groups subject to IFRS standards. External auditors practice to International Standards for Auditing and belong to large international firms.
- **Formal Powers of Supervisors (CP 22).** Although the FSC has no powers to levy civil money penalties it has a wide range of other powers and has not experienced any difficulty in achieving compliance with supervisory requirements.
- **Cross-Border Banking (CPs 23–25).** The banks in Gibraltar have no offices in other jurisdictions. All the banks have foreign owners and the FSC has adequate powers to exchange information with home supervisory authorities. In some cases the FSC has signed formal MOUs but is not prevented from co-operating in other circumstances. A Court of Appeal case in 2003 criticized internal processes used regarding disclosure in a particular instance. However, the Court confirmed the FSC’s powers

of co-operation. The internal processes have now been improved. A proposed new co-operation ordinance should help by consolidating and simplifying existing powers.

Table 2. Recommended Action Plan to Improve Compliance of the Basel Core Principles

Reference Principle	Recommended Action
Objectives, autonomy, powers and resources (CP 1)	<p>The FSC's objectives and responsibilities should be enshrined in law by amendment to the FSCO.</p> <p>The level of fees payable to the FSC should be fixed by the FSC.</p> <p>The term of office of the Commissioner and members of the Commission should be established in the FSCO.</p> <p>The amendment proposed by the FSC to FSCO Section 18 requiring the FSC to indemnify staff for costs that arise in defending themselves against legal action should be introduced.</p>
Other risks (CP 13)	<p>The FSC should require banks that FSC assesses as having a high potential liquidity risk meet their liquidity mismatch ratio or provide information about liquidity positions on a daily basis and duly report whenever a breach occurs.</p>

Authorities' response

51. The FSC welcomes the IMF's assessment of its compliance against the BCP and thanks them for their skill and diligence in conducting the review. The assessment validates the hard work that the FSC has been conducting, particularly over the past years, in the area of banking supervision. The FSC is very proud with the team's assessment of the individual core principles but is particularly so in relation to the Risk Assessment Framework methodology designed and implemented by its staff and deployed across all of its supervisory functions.

Summary Assessment of Observance of the IAIS Insurance Core Principles

General

52. This assessment of the observance of the core principles of the International Association of Insurance Supervisors (IAIS) in Gibraltar was done as part of a Module 2 assessment in the context of the International Monetary Fund's (IMF) offshore financial center assessment program. The assessment was conducted during a mission to Gibraltar during March 6–17, 2006, and thus reflects the practices and circumstances at that time.¹⁷

53. The purpose of this assessment is to measure the application of the IAIS insurance core principles adopted in 2003 to the insurance industry in Gibraltar. It is also to ensure that

¹⁷ The assessment was conducted by William McCullough (consultant to the IMF).

the legislation in operation provides the supervisory authority with the powers of enforcement sufficient to regulate the industry to the IAIS standards. Information was provided by supervised insurance managers, brokers, agents and auditors in addition to that provided by the insurance supervision staff. Information was gathered from members of the insurance industry and auditors in the private sector. Considerable assistance was provided by the FSC which is the supervisory authority. There were no limiting factors in any of the discussions.

54. Guidance notes have been issued relating to the majority of the reporting functions to be carried out by licensed insurers and intermediaries. These were reviewed and sample files were tested for both the application process financial returns and of-site monitoring.

Institutional and macroprudential setting—overview

55. The insurance market in the domestic sector in Gibraltar is small and there are only two locally incorporated insurance companies together with one agent of a European Union (EU) member state operating in this sector. The majority of the licensed insurers are “open market insurers” operating in the United Kingdom with head office facilities provided by independent insurance managers. There are also a small number with an operational office facility. Foreign establishments operating in Gibraltar are all EU based and therefore covered by the EU directive on freedom of establishment. In the insurance supervision department there is an operational staff of four, including the head of insurance supervision, with many years of insurance experience, and the insurance manager who is an accountant and been with the FSC for a considerable time. The other two regulators have been recruited within the past two years and are undertaking a structured training program.

Main findings

56. The insurance industry has been growing during the past year and this shows no signs of slowing with new applications and inquiries up on last year at this time. There are presently 50 active insurers; an increase of over 100 percent since 2002. The domestic market is small with two local insurers although there are branches of EU companies. The majority of Gibraltar licensed companies provide insurance to other EU countries mainly the United Kingdom. Growth is attributed to the ability of Gibraltar based companies to “passport” into other EU countries under the EU single market legislation. There are eleven substantial single parent captive insurers also licensed.

57. All EU directives issued have been incorporated into law. Currently a proposed “Approved Persons Regime” intended to strengthen the corporate governance principle is awaiting consideration by the Gibraltar Legislative Assembly. A recent review was undertaken to compare the Gibraltar regulation and supervision with U.K. standards. The main recommendation was related to Capital adequacy and Solvency. Whilst the FSC is keeping this area under review, the Capital Adequacy requirement in Gibraltar already exceeds the minimum requirement of the EU directive on this issue.

58. Gibraltar benefits considerably as an offshore center by membership of the EU. The facility for insurance companies to establish in Gibraltar and operate in other EU member states is the main source of growth of insurers. The benefits include a more efficient application process, and accessibility of the supervisor and Commissioner for decision making. It is also considered that operating costs are also a factor. The infrastructure of the industry whilst small is effective. The effective use of sanctions and custodial management in recent years has been shown by the experienced management of the Commission.

59. The senior members of the insurance supervisory authority are experienced regulators and have specific skills in insurance and financial reporting. However with a fast growing regulatory portfolio attention must continue to be given to training and to increase the number of regulators. It is unlikely that the existing team will be able to complete the cycle of on-site inspections in the immediate future.

Organization of supervisor

60. The FSC has established policy and objectives which are effectively considered in all aspects of supervision. The legislation clearly defining insurance supervision objectives is in place and reporting processes are provided by the issue of guidelines for each reporting function and the initial application process. The supervisory authority is independent and has adequate powers of intervention and enforcement which have been used when required. The structure however is defined in relation to the supervision of insurance companies and intermediaries by the insurance supervisory authority, and intermediaries by the investment division. The senior members of the division are experienced and skilled but staff numbers will need to be increased. The supervisory authority conducts its functions in a transparent manner and publishes rules and procedures and annual report on its web site. The supervisors can share information with other supervisors having taken confidentiality into consideration.

Licensing and changes in control

61. The requirements for licensing are clearly set out in guidelines issued by the authority. Risk managements systems, reinsurance programs, internal controls, IT systems policies and underwriting and claims guidelines must be included in a business plan. Detailed checks on beneficial owners, senior managers and controllers are required and take place before approval is considered. The supervisors are totally committed to detail and scrutiny of applications and equally for changes in control. The supervisory authority ensures compliance with all criteria in ICP 6. To facilitate these controls the FSC is in the process of introducing an "Approved Persons Regime" this year. All changes in control of companies are treated in exactly the same way as that of a new application.

Corporate governance and internal controls

62. Whilst the insurance supervisory authority considers that the Guideline on Criteria for Sound and Prudent Management and newsletter issued in 1998 are sufficient for compliance with international standards, there is now draft legislation currently with the government covering an Approved Persons Regime which will incorporate Corporate Governance

principles into Law so establishing best practice in this area. In addition Corporate Governance was of particular focus in the initial on-site inspection program. The self assessment questionnaire and aide-mémoire provided are clear guidance to the supervisory requirements. The scope of on-site inspections programmed for the current year have been increased to be compliant with various ICP's, which depend on verification of practical application. Similar comments apply to internal controls. The supervisor requires detailed information regarding controls, systems and operational management relating to underwriting procedures claims management reinsurance and risk management at the time of application however the absence of verification increases the risk of non observance in practice.

Market conduct

63. The domestic market in Gibraltar is small in relative standards. General insurance is concentrated in motor and personal lines supervised by the insurance supervisory division of the FSC. Intermediaries, predominantly involved in life insurance and related business, are supervised by the investment division of the FSC as conduct of business requirements are covered by the wider rules governing investment business. The Association of Gibraltar Insurers and Managers represents the industry but as yet they have not yet produced a Code of Conduct.

Monitoring, inspections, and sanctions

64. The requirements for the submission of financial, statistical and other reporting statements are set out in the Insurance Company Ordinance and the Insurance Accounts and Statements Regulations. Guidelines and Valuation of Assets and Liabilities Regulations all apply. The returns are closely scrutinized by the Supervisors and action is taken when required. The reporting time for annual accounts is at present six months after year end and the U.K. reviewers recommended shortening this period. This is being considered by the FSC. Additional and more frequent reporting is required from newly licensed insurers during the first two years of operation. As a follow up to off-site monitoring supervisors are required to carry out an on site investigation. The FSC has recently commenced such inspections undertaken on a risk-based approach, but a complete review of insurance companies will take some time. Inspections of five insurance managers were carried out in 2005 and a further nine were undertaken in 2006. Detailed self Assessment questionnaires have been produced as have aide-mémoires to assist in the proposed on-site inspection. While the initial on-site inspections focused on Corporate Governance the program has now been extended to include a wide range of management risks. All of the criteria for preventative and corrective measures are covered by the Insurance Companies Ordinance. There have been instances where appropriate enforcement procedures have been taken.

Cross border cooperation and confidentiality

65. Sufficient gateways exist to permit the insurance supervisory authority to share information with other supervisors either informally or by agreement. Safeguards apply to ensure that confidentiality from the other supervisors must be agreed and in place.

Table 3. Recommended Action Plan to Improve Observance of IAIS Insurance Core Principles

Reference Principle	Recommended Action
Suitability of Persons (CP 7)	Legislation relating to the “Approved Persons Regime” should be introduced without delay.
Corporate Governance (CP 9)	Legislation relating to the “Approved Persons Regime” should be introduced without delay.
Internal Control (CP 10)	It is recommended that legal requirements should be strengthened in relation to internal controls and the annual submission of detailed business plans.
Market analysis (CP 11)	Recommended that complete market statistics and detailed analysis should be compiled by the FSC and attention should be paid in detail to market analysis and trends both in Gibraltar and EU states, particularly the United Kingdom
Reporting to supervisors and off-site monitoring (CP 12)	It is recommended that reporting time, for the submission of annual financial returns, should be reduced to four months.
Insurance activity (CP 19)	It is recommended that the cycle of on site inspections be completed as soon as possible to confirm application of approved underwriting procedures and operational risk control.
Liabilities (CP 20)	It is recommended that the cycle of on site inspections be completed as soon as possible to confirm practical application of declared policies on technical provisioning.
Anti-money laundering (CP 28)	It is recommended that the cycle of on site inspections be completed as soon as possible to confirm that approved AML/CFT procedures are applied in practice.

Authorities’ response

66. The FSC welcome the findings of the IMF assessment of our compliance with IAIS standards. We appreciate the skill and attention given in conducting the review and have already actioned the recommendations made, which we fully accept. Whilst we are naturally delighted that our high level of compliance with the standards has been recognized, we consider that such standards are always subject to further development and we therefore remain committed to applying new standards as and when they evolve.

Financial Action Task Force Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism

Introduction

67. This Report on the Observance of Standards and Codes for the *FATF 40 Recommendations 2003 for Anti-Money Laundering (AML) and the 9 Special*

Recommendations on Combating the Financing of Terrorism (CFT) was prepared by a team composed of IMF staff and using the AML/CFT Methodology 2004.¹⁸ The report provides a summary of the level of observance with the Financial Action Task Force (FATF) 40+9 recommendations and provides recommendations to strengthen observance.

Information and methodology used for the assessment

68. In preparing the detailed assessment, the assessment team reviewed the institutional framework; the relevant AML/CFT laws, regulations, guidelines and other requirements, and the regulatory and other systems in place to deter and detect money laundering (ML) and the financing of terrorism (FT)—through financial institutions and designated nonfinancial businesses and professions (DNFBPs); and examined the capacity, implementation, and effectiveness of these systems. The assessment is based on the information available at the time of the on-site visit from March 1 to 17, 2006 and immediately thereafter.

Main findings

General

69. **Gibraltar authorities have done good work to implement improvements to their AML/CFT regime to keep abreast of evolving standards in AML/CFT.** Though relatively small in absolute terms, Gibraltar's financial center is important to Gibraltar's overall economy, and Gibraltarians universally place a high priority on maintaining its reputation as a well regulated center. Gibraltar has welcomed multiple external reviews of its system by the Offshore Group of Banking Supervisors (OGBS), the IMF, and the United Kingdom. Gibraltar authorities take a practical approach to implementing AML/CFT controls, and they have focused much of their resources and attention on providing effective international cooperation.

70. **The principal AML risk to Gibraltar is lodged in its professional sector (lawyers, accountants and TCSPs), which is likely to be involved—wittingly or not—in the layering and integration of proceeds of crime.** There is also some risk to Gibraltar at the placement stage, in connection with drug trafficking, migrant smuggling, and organized crime in southern Spain. Most money laundering cases involving Gibraltar arise out of investigations into international fraud schemes. Traditional organized crime and drug related cases, though important, comprise a minority of criminal investigations that touch Gibraltar's financial center.

71. **Gibraltar needs to take a number of steps to move its legal and regulatory regime forward to reflect the revised FATF 40 plus 9 Recommendations.** The money laundering offense is split between two different statutes that provide authorities different powers depending on whether the predicate offense is related to drug trafficking or to another

¹⁸ The mission comprised Mr. Joseph Myers (team leader), Ms. Joy Smallwood, and Mr. Andrew Gors (all LEG), and Ms. Tanya Smith (MCM).

crime. Under current judicial practice, for a ML prosecution to proceed, the government must prove the connection between a specific drug trafficking offense or another serious crime and the ML offense itself. This hampers prosecutors' ability to bring charges for ML and creates an incentive to focus on the predicate offense alone. Mutual legal assistance is available but full cooperation is limited by the fact that legal assistance to countries outside the EU during the investigative stage prior to formal commencement of "proceedings" is available only in drug-related cases. The assessment report contains recommendations to address these deficiencies. In addition, the Financial Services Commission's Anti-Money Laundering Guidance Notes need to be updated, inter alia, to reflect risks associated with terrorist financing; some of the key provisions currently in the Guidance Notes need to be reflected in law or regulation; and bureaux de change and non-bank money transmitters need to be supervised for AML/CFT compliance.

Legal systems and related institutional measures

72. **The Gibraltar legal framework for money laundering is divided into two fundamental statutes—the Drug Trafficking Ordinance and the Criminal Justice Ordinance.** These statutes, along with a terrorism ordinance, articulate criminal prohibitions against money laundering from a wide range of offenses and against various types of support to terrorists. These statutes also require financial institutions and others to report suspicious transactions in line with the FATF Recommendations. After the decision by the House of Lords in Montilla (2005), which required proof that the predicate offense was either drug trafficking or another serious crime, and adverse local rulings in two significant cases in Gibraltar, however, the Attorney General has concluded that he cannot go forward with domestic money laundering prosecutions without clear and convincing proof of the underlying offense. Since most predicates occur abroad, the Attorney General has not been able to pursue effectively in Gibraltar cases that have been brought to his attention.

73. **Prosecutors' powers could be enhanced by consolidating the provisions of the CJO and the DTOO into a single statute that extends powers currently available to authorities only in drug-related money laundering cases.** The money laundering risk in Gibraltar is lodged principally in the professional sector (lawyers, accountants and TCSPs), and a number of Gibraltarian professionals have been implicated in foreign fraud prosecutions. With consolidated authorities, Gibraltar authorities would be better positioned to follow up on credible suspicions or intelligence and aggressively pursue cases of money laundering by professional advisors if and when they arise. A consolidation of the two offenses would be appropriate so that there is one offense, which then would have a series of indictable proceeds-generating predicate offenses. This would obviate the need for prosecutors to prove the predicate offense between criminal conduct and drugs. Given the two money laundering cases from Gibraltar that were overturned on appeal, it may also be advisable to arrange for a training session for the bench and bar on international developments in the criminal law of money laundering.

74. **Gibraltar has implemented the terrorism orders issued by the United Kingdom promptly after September 11, 2001.** This has included implementing targeted freeze action against two separate terrorist financing suspects. In addition, Gibraltar has enacted its own

domestic Terrorism Ordinance 2005, which gives authorities broad powers to prosecute suspected supporters of terrorism and to confiscate their assets.

75. **Like the Gibraltar criminal prohibition on money laundering, the domestic confiscation regime is split between drugs-related and nondrug-related schemes.** The authorities for drugs-related confiscation are very broad and include reversals of the burden of proof, the ability to enforce external confiscation orders, and the ability to seize cash suspected of being proceeds of drug trafficking. Conversely, in cases involving other criminal proceeds, the authorities have more limited powers. This split causes practical difficulties for the authorities. For example, when suspect cash is detected at the border, authorities are not able to detain it unless they can prove that it represents the proceeds of a specific offense. Similarly, after a conviction on a nondrug-related, proceeds generating crime, the government—not the defendant—bears the burden of proving that the defendant’s property is derived from illicit proceeds.

76. **Gibraltar has a small police-style FIU embedded in its joint police/customs Gibraltar Coordinating Centre for Criminal Intelligence and Drugs (GCID).** The FIU is a member of the Egmont Group and functions effectively within the Gibraltar system. The FIU would benefit, however, from a clearer public explanation of its authority and functions, especially with respect to potential STRs related to terrorism. The government should also consider, in light of the questionable legal basis for the practice of freezing accounts on the basis of “nonconsent” letters, whether to promulgate explicit freezing authority to the GFIU and/or GCID.

Preventive measures—financial institutions

77. **The authorities in Gibraltar have established a robust, risk-based regulatory and supervisory framework for financial institutions for AML.** Since the last assessment in 2001, there has been continued progress in the systems and controls implemented in the financial industry. The FSC has taken the lead in this area. It has issued the key document for AML compliance, namely the Anti-Money Laundering Guidance Notes. These Guidance Notes require customer due diligence, ongoing monitoring, designation of a Money Laundering Reporting Officer, and reporting of suspicious transactions. The Guidance Notes will be further strengthened when they are extended to better capture considerations related to the financing of terrorism. In addition to issuing the Guidance Notes, the FSC conducts on-site inspections and off-site analysis, it can compel production of any record to assist in its supervisory efforts, and it can impose sanctions in the case of noncompliance with the standards.

78. **The FSC is responsible for supervising banks and building societies, investment businesses, insurance companies, and controlled activities,** which include investment services, company management, professional trusteeship, insurance management and insurance intermediation. Outside of its supervisory scope and responsibilities is the Gibraltar Savings bank, the only state-bank, bureaux de change, and (nonbank) money transmitters. The Gibraltar Savings Bank is subject to reasonable oversight and regulation by the Treasury

and supported by the government's auditors, who review controls and systems, as well as the accounts.

79. **The current weaknesses in Gibraltar's supervisory and regulatory structure stem from the limited and ineffective oversight of bureaux de change and the complete lack of oversight of its single money transmission agent.** The bureaux de change are licensed by a government committee, the Bureaux de Change Committee, headed by the Financial and Development Secretary. The bureaux de change are subject to the Anti-Money Laundering Guidance Notes issued by the FSC. A single customs investigating officer provides the only oversight of bureaux de change. But he has no remit to check for compliance and very limited powers to sanction. The Bureaux de Change Committee can suspend or cancel a license, but it cannot impose conditions or directions that would ensure corrective action of identified deficiencies. These weaknesses were identified during an AML review conducted by the Offshore Group of Banking Supervision (OGBS) in 2001, and three bureaux de change were closed in connection with a money-laundering investigation in the United Kingdom in 1998, yet authorities still have not addressed the continued risk of money laundering through the bureaux de change. There is currently only one money transmitter in Gibraltar that is outside the banking industry. As a stand-alone entity, this business is not subject to licensing or registration and is not regulated or supervised.

80. **The government of Gibraltar recognizes the issues and risks associated with the bureaux de change and the money transmission agent.** A draft Money Services Business Ordinance has been developed, but not finalized. Bureaux de change and money transmitters would be captured under this new Ordinance and subject to oversight by a government committee. The current proposal is that the FSC commissioner would head this Committee and this seems reasonable, because the FSC has demonstrated that it has the skills, abilities, and resources to provide appropriate oversight of the rest of the financial system.

Preventive measures—designated nonfinancial businesses and professions and nonprofit organizations

81. **Gibraltar has been a pioneer in establishing a strong AML control environment for trust and company service providers, but this is not matched for other DNFBPs.** The TCSPs are licensed, regulated, and supervised by the FSC and are subject to regular inspections and significant regulatory requirements. The only other DNFBP that is subject to oversight is the internet based gambling industry, but that oversight regime is limited and in the process of transition to an entirely new system. The new system, which is being developed in response to the new Gambling Ordinance 2005, will comprise a commissioner to take significant decisions vis-à-vis the gambling sector, a regulatory team and an ombudsman. Currently, both TCSPs and the internet based gambling sector are subject to the Anti-Money Laundering Guidance Notes, but only the TCSP are actually supervised against them.

82. **The remainder of the DNFBPs, including lawyers, notaries, accountants, high value goods dealers, and real estate agents are subject to the Criminal Justice Ordinance and thus to STR requirements.** However, no further rules or regulations on

AML/CFT have been promulgated in Gibraltar for DNFBPs, although the Government of Gibraltar has issued non enforceable guidance for the high value goods dealers. In addition, there is no oversight by competent authorities of these industries to ensure that systems and controls are in place to combat money laundering and the financing of terrorism. Lawyers are required by local law to comply with English AML regulations, but there is no local monitoring of compliance with these requirements.

83. **Overall, the Charities Ordinance provides a solid framework for the supervision of charities by the Charities Board (the “Board”).** The requirements for registration of charities with the Board, after an appropriate application and disclosure of material information by the applicant, indicate that the Board is fulfilling its gatekeeper role with regard to the registration of charities. The blanket exception granted to religious charities under Section 6(4) of the Charities Ordinance should be reviewed. Adequate legal provisions are in place for ongoing supervision of, investigation of and intervention regarding charities to prevent abuse. In practice, all charities are required to file annual audited accounts with the Supreme Court registry and these accounts are reviewed by the Board. Should clandestine diversion of funds be discovered, adequate legal provisions exist for the Board to undertake immediate and effective actions to halt terrorist financing.

Legal persons and arrangements

84. **Gibraltar has been a pioneer in the supervision and regulation of professional trusteeship and company service providers.** Only persons licensed under the Financial Services Ordinance can form and manage companies in Gibraltar, and they are subject to the full panoply of preventive measures and oversight on the same terms as banks and other traditional financial service providers. The FSC has applied its risk-based supervisory system to the fiduciary services industry, and the industry appears generally to be compliant. The government should repeal legislation allowing share warrants to bearer, as it promised to do from years ago in negotiations with the OECD, and ensure that Companies House’s data base is searchable by all relevant fields.

National and international cooperation

85. **The United Kingdom has not extended the Vienna, Palermo, or International Convention on Financing of Terrorism to Gibraltar.** The Gibraltar government, however, has legislated a number of key provisions that mirror some of those in the conventions. The mission recommends that the United Kingdom move swiftly to extend the provisions of these important conventions to Gibraltar.

86. **Gibraltar authorities are to be commended for the resources they have devoted to international cooperation on money laundering and terrorist financing cases.** As a member of the EU, they are able to provide full cooperation at the investigative stage to other EU member states. Last year, they enacted legislation that extends the same privileges to non-EU member states, provided such states agree to reciprocity. Further, recently published draft legislation would extend such privileges automatically to all states that have ratified the UN Transnational Organized Crime Convention. The draft legislation would also solve

another limitation in Gibraltar's current law, namely that in nondrug-related money laundering cases where foreign states are not permitted to obtain restraint orders or register and enforce their confiscation orders in Gibraltar.

87. **Financial intelligence unit.** Since being admitted to the Egmont Group in 2004, the GFIU regularly shares information with other FIUs through the Egmont secure web system. It has responded to every request it has received, and initiated requests, as well. In several cases, the GFIU has been able to contribute to overseas investigations by taking the initiative to cooperate closely with other Egmont Group members.

88. **The FSC regularly shares information with other international competent authorities.** In the case of *the Queen (on the application of a Gibraltar company, X, Y, and Z and other respondents)* (2003), the FSC was challenged on legal authority to provide information to a foreign supervisor. The court found that, in order for the commissioner to share information with foreign counterparts, he must satisfy himself that the requesting body performs a function similar to his own, the disclosure is necessary to assist the requesting body, and it is in the interests of the public of Gibraltar that he should disclose it to the requesting body. The mission was advised by several foreign supervisors that the FSC has in fact shared information.

Ratings

89. The table below sets out the ratings of compliance for each of the FATF 40+9 Recommendations and the factors underlying the ratings. The rating of compliance vis-à-vis the FATF Recommendations should be made according to the four levels of compliance mentioned in the 2004 Methodology: (compliant (C), largely compliant (LC), partially compliant (PC), non-compliant (NC)), or could, in exceptional cases, be marked as not applicable (NA).

Table 4. Ratings of Compliance with FATF Recommendations

Forty Recommendations	Rating	Summary of factors underlying rating ¹⁹
Legal systems		
1. ML offence	PC	Migrant smuggling is not an indictable offense and so is not a predicate offence for money laundering; very few cases of money laundering have been charged in the eleven years since the offense was enacted; only 17 arrests in the last four years, no prosecutions, no convictions and only one case currently under investigation.
2. ML offence—mental element	C	This Recommendation is fully met.

¹⁹ These factors are only required to be set out when the rating is less than compliant.

and corporate liability		
3. Confiscation and provisional measures	LC	Authorities' power to seize suspect cash at the border is limited in non-drug related cases, and the post-conviction burden to show that proceeds were legitimate shifts only in drug-related cases, as well.
Preventive measures		
4. Secrecy laws consistent with the Recommendations	C	This Recommendation is fully met.
5. Customer due diligence	PC	Several criteria have not been appropriately addressed in law or regulation; they are instead part of the Guidance Notes.
6. Politically exposed persons	LC	Bureaux de change, the Gibraltar Savings Bank, and money transmitters (outside of banks) are weak as to implementation of requirements.
7. Correspondent banking	LC	Need to ensure that information has been gathered on respondents.
8. New technologies & non-face-to-face business	PC	Implementation of new language on non-face-to-face and new technologies for all institutions and lack of oversight for bureaux de change, the Gibraltar Savings Bank, and money transmitters on these issues.
9. Third parties and introducers	PC	Controls relative to reliance on intermediaries have not been established.
10. Record keeping	PC	Two criteria need to be addressed in law or regulation and policies and procedures of the bureaux de change and stand-alone money transmitter must be reviewed to ensure that the requirements are being followed.
11. Unusual transactions	LC	The current standards do not provide for review and retention of records on <i>all</i> cases involving large, unusual or complex transactions, but do cover those where there are concerns or suspicions.
12. DNFBP-R.5, 6, 8-11	PC	While there are numerous deficiencies in the requirements for DNFBPs on CDD, PEPs, etc, two key areas of risk (TCSP and internet based gambling) are subject to more robust standards through the AMLGNs.
13. Suspicious transaction reporting	LC	There is some confusion over who to report to and STRs on attempted transactions are not explicitly required.
14. Protection & no tipping-off	C	This Recommendation is fully met.
15. Internal controls, compliance & audit	LC	Need to extend consideration of TF issues to controls and training and need to ensure that all licensees have an internal audit program in place.
16. DNFBP-R.13-15 & 21	PC	Reporting requirements and tipping off provisions are appropriately in place, but significant attention is needed on requirements for audit and dealing with clients from outside of Gibraltar.

		In addition, the current lack of effective oversight of most DNFBPs other than the FSC supervised TCSP sector, creates an inability to assess the effectiveness of the provisions that are in place and lack of an appropriate range of sanctioning powers limits the ability to ensure corrective action.
17. Sanctions	LC	<p>Bureaux de Change and money transmitters are not subject to adequate sanctions.</p> <p>A range of supervisory sanctions apply for the TCSP and internet based gambling sector, but few for the land based casino or other DNFBP entities.</p>
18. Shell banks	C	This Recommendation is fully met.
19. Other forms of reporting	C	This Recommendation is fully met. Authorities considered and rejected threshold based reporting based on valid reasons.
20. Other NFBP & secure transaction techniques	C	This Recommendation is fully met.
21. Special attention for higher risk countries	LC	The efforts by the bureaux de change and the stand-alone money transmitter need to be reviewed. Extend to include TF.
22. Foreign branches & subsidiaries	C	This Recommendation is fully met.
23. Regulation, supervision and monitoring	PC	No supervision for the bureaux de change or the non-bank money remitter; no specific standards that prohibit criminals or their associates from holding key ownership or management positions in financial institutions.
24. DNFBP—regulation, supervision and monitoring	PC	<p>There is an effective monitoring arrangement for the high risk TCSP sector. Placing the new Gambling Ordinance into effect and resourcing of the GRA will afford the opportunity, mechanism and framework to effectively monitor the compliance of the gambling sector. However, until that occurs the level of effective monitoring for this sector is low.</p> <p>Whilst disciplinary action in some form exists for lawyers, it is not clear to how non compliance with specific AML/CFT obligations would be brought to the attention of the relevant authorities and what credence would be afforded.</p> <p>The assessment team is not aware of any process that has been undertaken to determine the appropriate level of monitoring for the remaining DNFBP sectors. No authority has been designated responsibility for such monitoring.</p>
25. Guidelines & Feedback	PC	<p>Existing guidance does not address the techniques or methods associated with terrorist financing; no feedback or guidance has been provided to bureaux de change, the stand-alone money transmitter.</p> <p>No feedback or guidance for bureaux de change and money transmitters; existing guidance must be fully extended to cover TF</p>

		<p>issues.</p> <p>Little guidance exists to assist businesses and professions on how to implement and comply with AML/CFT requirements for categories of the DNFBP sector outside of TCSPs, internet gambling and high value dealers, and no efforts to address TF outside of the FSC's AMLGNs, which only apply to the TCSPs and internet based gambling.</p> <p>Little general feedback to the DNFBPs, outside the FSC regulated TCSPs and car dealers, as the GFIU has had minimal contact with them</p>
Institutional and other measures		
26. The FIU	LC	<p>A clear public record of GFIU's functions and should be issued.</p> <p>The recently enacted Gambling Ordinance if implemented requires disclosures to be made to the Gambling Commissioner in the first place provide a copy to the GFIU. The GO currently allows for the Gambling Commissioner, not the GFIU to decide to disseminate copies of the disclosures it receives to law enforcement authorities.</p> <p>Legal requirements for STRs relating to financing of terrorism are confusing. The March 2006 amendment to the AMLGNs partly addresses this issue for the sector regulated by the FSC.</p> <p>The circumstance and extent to which the GFIU can and will obtain additional information from reporting businesses are not clear..</p>
27. Law enforcement authorities	C	<p>Dedicated, specialized law enforcement resources are responsible for ML and TF cases. Authorities work closely with foreign counterparts and have discretion to postpone or waive the arrest of suspects or seizures of funds. Law enforcement authorities have authority to use—and do use in ML and Financing of Terrorism cases—special investigative techniques. Authorities keep abreast of trends and techniques, and discuss developments with colleagues at home and abroad.</p>
28. Powers of competent authorities	C	<p>Through production orders and search warrants authorities may obtain relevant documents held by financial institutions and others. Witness statements may also be obtained.</p>
29. Supervisors	LC	<p>No oversight of bureaux de change or money transmitters.</p>
30. Resources, integrity and training	LC	<p>The Royal Gibraltar Police, Customs, and GFIU are adequately staffed by qualified, specialized professionals. Independence of police is ensured by their reporting to the governor. Customs is a major revenue source for the Government. As a police style body, the FIU is integrated into the police and customs framework, but they could benefit from formal clarification of their role.</p> <p>Compliant for FSC; inadequate resources for oversight of bureaux de change and money transmitters;</p>

31. National cooperation	LC	DNFBP oversight authorities (excluding FSC with respect to TCSPs) are not represented in the Enforcement Group.
32. Statistics	PC	<p>No statistics kept by the attorney general on prosecutions and convictions. The police have statistics on the number of money-laundering charges laid.</p> <p>Authorities can remember the big cases and construct tables from records, but they do not keep consolidated statistics readily available.</p> <p>The FSC has no information on the level of compliance in the financial sector with UN Security Council Resolutions.</p> <p>Statistics regarding disclosures are comprehensive, but they may understate the true level of suspect activity because to date limited education of the real estate, internet gaming and legal/accounting sectors or High Value Dealers has been undertaken.</p> <p>GFIU produces statistics on STR disclosures and the usefulness of disseminations to the police and customs.</p> <p>The authorities do maintain information about narcotics-related cash seizures and forfeitures, but this is only partially relevant to the recommendation overall.</p> <p>Compliant for FSC.</p> <p>Overall, agencies should keep more detailed statistics.</p> <p>The authorities maintain reliable records on mutual legal assistance and extradition requests (including requests related to freezing, seizing, and confiscation) that are made or received, relating to ML, the predicate offenses, other international money-laundering investigations and prosecutions. The assessment team had some difficulty, however, in getting consistent information promptly from the authorities in these areas.</p> <p>Gibraltar maintains records on its extradition requests, as well as on international arrest warrants, but did not have statistics readily available for the assessors.</p>
33. Legal persons–beneficial owners	LC	Share to warrants should be abolished and Companies House registry should be searchable by multiple fields.
34. Legal arrangements – beneficial owners	LC	Continued existence of asset protection trusts and flee clauses. Competent law enforcement authorities may not have access in a timely fashion to adequate, accurate and current information on beneficial ownership and control.
International Cooperation		
35. Conventions	PC	The Vienna Convention has not been extended to Gibraltar.

36. Mutual legal assistance (MLA)	LC	Gibraltar authorities' general willingness to provide full cooperation on mutual legal assistance is limited by the fact that legal assistance during the investigative stage prior to formal commencement of "proceedings" is available only in drug related cases with respect to countries outside the EU.
37. Dual criminality	C	<p>Except in limited circumstances involving extradition and the issuance of physical search warrants, dual criminality is generally not a bar to obtaining mutual legal assistance from Gibraltar. The authorities do not take an overly technical approach to the application of dual criminality requirements.</p> <p>Gibraltar does impose dual criminality requirements on extradition, but its authorities do not take an overly technical approach to the application of such requirements.</p>
38. MLA on confiscation and freezing	PC	Gibraltar authorities general willingness to provide comprehensive mutual legal assistance is limited by the following significant impediments in its legal framework: (1) except in drug-related cases, the law of Gibraltar provides no power to the authorities to secure restraint or charging orders to secure proceeds of crime during the pendency of proceedings, or to detain suspect cash detected at the border; and (2) although the authority to do so was provided in the CJO more than ten years ago, the governor has failed to promulgate an order listing countries whose non-drug related confiscation orders may be registered and enforced in Gibraltar.
39. Extradition	PC	Money-laundering is an extraditable offense, Gibraltar can extradite its own nationals for money laundering, Gibraltar has a proven record of cooperating with foreign governments on money-laundering cases, Gibraltar may extradite within the EU based on the EU arrest warrant. Nevertheless, in the only money-laundering extradition request on record, authorities were unable to respond positively due to evidentiary requirements imposed by English case law. Authorities also have not elaborated specific procedures for processing requests.
40. Other forms of co-operation	C	This Recommendation is fully met.
Nine Special Recommendations		
SR.I Implementation of UN instruments	PC	The ICSFT has not been extended to Gibraltar but Gibraltar has implemented UNSCRs 1267, 1373 and successor resolutions by UN Order 2001 and the Al-Qaida and Taliban (UN Measures) (Overseas Territories) Order 2002.
SR.II Criminalize terrorist financing	C	This Recommendation is fully met. While there have been no charges of terrorist financing, two accounts have been frozen on the suspicion as they are terrorist funds.
SR.III Freeze and confiscate terrorist Assets	LC	Despite very broad legal authorities that have been successfully applied by the law enforcement community in two cases, there is a disconnection in the financial community concerning their

			affirmative obligations under the UNSCR 1267 and EU regulations.
SR.IV	Suspicious transaction reporting	LC	Filing procedures under various overlapping laws should be clarified, and guidance on TF has not been included in the AMLGNs.
SR.V	International cooperation	LC	Terrorist financing is an extraditable offense, and nothing in the law of Gibraltar or the practices of its authorities would prevent full and effective cooperation in the extradition of a person alleged to be involved in terrorism or terrorist financing. Without specific experience, however, the FATF methodology does not allow for a fully compliant rating.
SR.VI	AML/CFT requirements for money/value transfer services	PC	Only one stand-alone money transmitter so risk is low, but lack of overall framework is a significant issue.
SR.VII	Wire transfer rules	LC	The application of these standards by the stand-alone money transmission agent is unknown given the lack of overall regulatory framework for these entities.
SR.VIII	Non-profit organizations	LC	Conduct a review to ensure that terrorist financing risks are fully addressed, particularly regarding exempt religious charities.
SR.IX	Cash border declaration and disclosure	NC	No declaration or disclosure system is in place. Partial measures for seizure and confiscation of currency suspected to be related to drug trafficking is ineffective with respect to proceeds of unknown origin.

Recommendations

90. The table below summarizes recommended actions in areas related to the FATF 40+9 Recommendations.

Table 5. Recommended Action Plan to Improve the AML/CFT System

FATF 40+9 Recommendations	Recommended Action (listed in order of priority)
1. General	No text required
2. Legal System and Related Institutional Measures	
Criminalization of Money Laundering (R.1, 2 & 32)	<ul style="list-style-type: none"> Consolidate the ML offences laid out in the DTOO and the CJO into one consolidated ordinance to avoid two-track approach to the ML offence, as indicated by the Chief Minister. Criminalize migrant smuggling as an indictable offence so that it may be considered a predicate offence for money laundering Consider criminalizing the export of cigarettes as an indictable offence (rather than a summary conviction only offence) in order that it becomes a predicate crime for money laundering

	<p>as part of the required category of offences for “illicit trafficking in stolen and other goods.”</p> <ul style="list-style-type: none"> • Consider charging domestic persons in the financial industry with money laundering when a mutual legal assistance request reveals complicity in money laundering by Gibraltar residents. • Hold seminars for the bench and bar on money laundering prosecutions. • Maintain statistics on the number of charges laid, the number of prosecutions brought and the number of convictions for money laundering offences.
Criminalization of Terrorist Financing (SR.II & R.32)	
Confiscation, freezing and seizing of proceeds of crime (R.3 & 32)	<ul style="list-style-type: none"> • Consolidate the asset forfeiture provisions of the CJO and DTOO, and in doing so take advantage of the best features of each. Thus, reversal of burden of proof provisions should be extended beyond drug-related confiscation to all crimes, and cash seized at the border should be allowed to be detained on a suspicion that it is proceeds of or intended to be used in any crime, not just drug trafficking. • Enact the proposed legislation extending to all states that are parties to the UNTOC the ability to enforce external confiscation orders. • Clarify the authority of the GFIU to issue “nonconsent” letters and provide guidelines for their use. • Maintain consolidated asset confiscation and forfeiture statistics.
Freezing of funds used for terrorist financing (SR.III & R.32)	<ul style="list-style-type: none"> • Procedures for delisting requests and the unfreezing of funds should be developed and published. • The FSC should issue guidance to the financial services community concerning affirmative obligations to freeze assets of persons listed by the UNSCR 1267 Committee and the EU. These affirmative obligations should include incorporating the information into their AML/CFT compliance programs, and reporting to authorities on any transactions that may be connected to terrorist financing.
The Financial Intelligence Unit and its functions (R.26, 30 & 32)	<ul style="list-style-type: none"> • Provide clearer public explanations of the roles and responsibilities of the GFIU vis-à-vis the GCID and the police particularly with respect to TF. • Clarify the implications, if any, on the GFIU of legal requirements that suspicious transactions related to terrorism be reported variously to the Governor and the police. • Amend Sections 33(2) and (3) of the GO to require holders of gambling licenses to report disclosures of suspected money laundering to the GFIU instead of the gambling commissioner. • Analyze possible relationships between observed trends in disclosures and other criminal intelligence. • Consider providing the FSC, the GRA and any other authority having AML/CFT oversight responsibility with numerical only

	<p>statistical data on the reporting performance of specific individual businesses. This would assist those authorities in their supervisory programs.</p> <ul style="list-style-type: none"> • GFIU should give priority to establishing contact with the sectors not regulated by the FSC to: provide clear education and guidance as to reporting obligations and procedures for making disclosures to the GFIU and to foster sharing of information on potential ML/TF risks in these sectors. • Document internal procedures for all GFIU functions. • Consider ways to clarify the circumstances and extent to which the GFIU can and will obtain access to further information from reporting businesses.
Law enforcement, prosecution and other competent authorities (R.27, 28, 30 & 32)	<ul style="list-style-type: none"> • Update production order and warrant statutes to make them more effective in nondrug related financial investigations. Specify types of documents that may be made available, include provisions protecting information retained on computers, and authority for police and customs to enter premises to execute production orders. Use Schedule 10 of the Companies Ordinance as a model. • Clarify and document the roles and responsibilities of the GFIU within the GCID vis-à-vis the private sector.
3. Preventive Measures–Financial Institutions	
Risk of money laundering or terrorist financing	
Customer due diligence, including enhanced or reduced measures (R.5– 8)	<ul style="list-style-type: none"> • Prohibit anonymous and fictitious accounts in law or regulation; • Address, in law or regulation, the need to undertake customer due diligence when: carrying out occasional transactions that are wire transfers; there is a suspicion of money laundering or terrorist financing; and the financial institution has doubts about the veracity or adequacy of previously obtained customer identification data; • Require through law or regulation that the financial institution determine the natural person who ultimately owns or controls the customer, when the customer is a legal person or arrangement; • Address, in law or regulation, the requirement for financial institutions to conduct ongoing due diligence on its business relationships; • Determine if institutions, having refused business because full “know your customer” information was not provided, have provided STR reports to the GFIU; • Ensure that bureaux de change, the Gibraltar Savings Bank, and money transmitters are subject to and implementing PEP requirements; • Review existing correspondent banking arrangements to ensure that the institution has gathered sufficient information

	<p>on the reputation and supervisory arrangements for the respondent;</p> <ul style="list-style-type: none"> • Ensure that bureaux de change, the Gibraltar Savings Bank, and money transmitters are looking at the risks associated with new technologies; • Ensure effective implementation of the new language in the AMLGNs requiring that institutions carefully consider the risks associated with new technologies; and • Generally review the AMLGNs for language and tone that may read as permissive or informational in places.
Third parties and introduced business (R.9)	<ul style="list-style-type: none"> • Require financial institutions relying on intermediaries to immediately obtain from that intermediary information on the identity of the customer, and beneficial owner of the account and the legal status of legal persons or arrangements. Beneficial ownership requirements should be included in law or regulation; • Require that financial institutions have access, without delay, to the identification or other relevant documentation housed with the intermediaries; • Require that institutions have processes to assess whether or not an institution within the EU may be accepted as an intermediary; • Determine to what extent the industry has been allowing intermediaries under the fourth scenario of the AMLGNs (paragraph 4-85) and ensure that all institutions are now obtaining the appropriate due diligence information; and • Ensure that the ultimate responsibility for customer identification and verification remains with the financial institution relying on the third party.
Financial institution secrecy or confidentiality (R.4)	<ul style="list-style-type: none"> •
Record keeping and wire transfer rules (R.10 & SR.VII)	<ul style="list-style-type: none"> • Address the confusion related to Section 17(2) of the CJO, ideally through repeal of the passage; • Address, in law or regulation, that business correspondence must also be retained (in addition to the requirements for identification and transaction records); • Address, in law or regulation, the requirement that institutions maintain their records in a way that they are able to provide information to the appropriate authorities on a timely basis when appropriately authorized to do so; and • Verify that bureaux de change and the stand-alone money transmitter are effectively implementing the record keeping requirements.
Monitoring of transactions and relationships (R.11 & 21)	<ul style="list-style-type: none"> • Ensure that bureaux de change and the stand-alone money transmitter are applying risk-based procedures for relationships and transactions coming from persons outside of Gibraltar, who may not be subject to equivalent AML/CFT requirements; and

	<ul style="list-style-type: none"> • Extend the discussion on equivalency to include considerations related to TF.
Suspicious transaction reports and other reporting (R.13, 14, 19, 25 & SR.IV)	<ul style="list-style-type: none"> • Clarify the reporting obligations for the suspicious transaction reports related to money laundering (GFIU vs. GCID vs. “customs and police”); • Clarify, through law or regulation, where reporting entities should file suspicious transaction reports related to TF in Gibraltar; and • Ensure that there are requirements in place to report suspicions on attempted transactions.
Cross Border Declaration or disclosure (SR IX)	<ul style="list-style-type: none"> • Amend laws to require disclosure of cross-border movements of currency and bearer negotiable instruments. Such a system could apply only above a certain threshold. • Amend laws to enable customs and police officers to detain currency and negotiable instruments that are falsely disclosed or that are suspected of being related to terrorist financing or money laundering; and • Amend laws to enable authorities to confiscate such seized currency and negotiable instruments under appropriate circumstances consistent with Special Recommendation IX.
Internal controls, compliance, audit and foreign branches (R.15 & 22)	<ul style="list-style-type: none"> • Extend AMLGNs to include TF in the areas of controls and training; • Ensure that financial institutions have an internal audit or other mechanism to check compliance with the AMLGNs in place, including bureaux de change and the stand-alone money transmitter; and • Extend the standards for hiring to insurance firms, bureaux de change, and money transmitters.
Shell banks (R.18)	<ul style="list-style-type: none"> •
The supervisory and oversight system—competent authorities and SROs Role, functions, duties and powers (including sanctions) (R.23, 30, 29, 17, 25 & 32)	<ul style="list-style-type: none"> • Address the lack of “effective, proportionate, and dissuasive” sanction regime for both bureaux de change and nonbank money transmitters in the area of AML/CFT; • Address the lack of effective oversight for bureaux de change; • Ensure that all financial institutions are subject to requirements that prohibit criminals or their associates from holding or being the beneficial owner of a significant or controlling interest or holding a management function in a financial institution; • Extend the AMLGNs to focus not only on ML, but also on TF; and • Ensure that authority responsible for bureaux de change and money transmitters (non-bank) is given appropriate regulatory powers and resources so that the authority can effectively conduct oversight, compel records, require remediation, and, where necessary, issue sanctions.
Money value transfer services (SR.VI)	<ul style="list-style-type: none"> • Close the gap in the financial services area by ensuring that all entities that provide money or value transfer services are licensed and supervised;

	<ul style="list-style-type: none"> • Require that principals keep lists of all agents of money and value transfer service providers; and • Develop a mechanism to ensure that money and value transfer service providers can be sanctioned.
4. Preventive Measures–Nonfinancial Businesses and Professions	<ul style="list-style-type: none"> •
Customer due diligence and record-keeping (R.12)	<ul style="list-style-type: none"> • Develop and apply strong requirements for customer due diligence for all categories of DNFBPs not subject to the requirements of the FSC issued AMLGNs²⁰ This should include provisions requiring ongoing monitoring; obtaining information on the purpose and intended nature of the business relationship; performing enhanced due diligence on higher risk customers or business relationships; and prohibiting the opening of an account or commencing business relationships when an entity cannot provide appropriate CDD information; • Address criteria 5.1, 5.2(c), 5.2(d), 5.2(e), 5.5.2(b), and 5.7 in law or regulation; • Ensure that DNFBPs are subject to adequate requirements for PEP clients or business relationships; • Address the risks associated with new technologies and nonface-to-face business; • Develop requirements for DNFBPs in the area of large, complex or unusual transactions to ensure that these are reviewed, with findings set in writing and kept for five years; • Address the lack of sanctioning ability for DNFBPs, other than TCSP, in the area of conducting appropriate customer due diligence. • Finalize the development and release of the regulations for the Conduct of Business (Fiduciary Services); • Finalize the new licensing agreement for the sole land based casino and include specific observance to the need to comply with the AMLGNs; and • Afford priority to the implementation of the new gambling Ordinance and resourcing of the GRA. The GRA should also give priority to releasing a Code of Conduct under its powers specifying the GRAs expectations for license holders to meet the legal AML/CFT obligations. Furthermore reference to, and adherence with, such a Code of Conduct should be mandatory in all licensing agreements for the gambling sector
Suspicious transaction reporting (R.16)	<ul style="list-style-type: none"> • Consider specifying time limits on consent and non consent letters to assist disclosing businesses to avoid inadvertent

²⁰ The TCSP category of the DNFBP sector is subject to the same AMLGN requirements as Financial Institutions. The recommendations on standards in Sections 2.2, 2.3, 2.5 and 2.6 therefore apply. Similarly, licenses for all internet casinos require compliance with the FSC issued AMLGNs. The sole land based casino is currently not subject to the higher requirements detailed in the AMLGNs.

	<p>tipping off to customers; and</p> <ul style="list-style-type: none"> Remove the current s 33(1)(2) requirement in the new gambling ordinance that requires gambling licensees to in the first place make disclosures of the alleged money laundering to the gambling commissioner as opposed to the GFIU. This is necessary to maintain continued integrity and confidence in the confidentiality of the disclosure system.
Regulation, supervision, monitoring, and sanctions (R.17, 24 & 25)	<ul style="list-style-type: none"> Extend, in law or regulation, the provisions for internal control systems to cover the financing of terrorism in addition to AML; Address the need for an audit function to test compliance with policies, procedures, and controls in DNFBP entities, not subject to the FSC issued AMLGNs; Require screening procedures in DNFBP entities not subject to the FSC issued AMLGNs, to ensure high standards when hiring employees; Extend the requirements related to dealing with clients in jurisdictions that do not or insufficiently apply the FATF Recommendations to all DNFBPs. Consider a more proportional level of regulatory sanction for the non gambling and non-TCSP categories of the DNFBP sector; Determine, implement and publicly declare the appropriate monitoring and sanctioning authority to be responsible for monitoring compliance with AML/CFT obligations by those categories of the DNFBP sector not subject to supervision by the FSC, the Financial & Development Secretary or future GRA. Make mandatory the requirement for the gambling Licensing Authority to include in any license agreement that compliance with the AMLGNs and any subsequent Codes of Conduct that may be issued by the gambling commissioner is a condition of license. Amend the Schedule 1, Section 4, of Gambling Ordinance 2005 to make mandatory requirements identified in subsection (a) through (k) and also that compliance with the AMLGNs and future codes of conduct issued by the GRA is an explicit condition of license; Implement Gambling Ordinance 2005 as a priority; Ensure that the GRA is allocated appropriate budget, staffing and other resources to properly meet the requirements established under the new gambling ordinance; Develop sector-specific guidelines on AML/CFT for DNFBP entities not covered by the AMLGNs and the High-Value Dealers Guidance Notes, which cover both AML and CFT; Ensure that the FIU provides guidance to all sectors

	<p>regarding reporting requirements and typologies;</p> <ul style="list-style-type: none"> Identify and designate an appropriate authority to monitor DNFBPs (other than TCSP and the gambling sector) in the area of AML/CFT. Given the size of the jurisdiction consideration to using the FSCs expertise may be appropriate; and Ensure that designated competent authorities (once designated) for DNFBPs are represented on the domestic Enforcement Committee.
Other designated nonfinancial businesses and professions (R.20)	<ul style="list-style-type: none">
5. Legal Persons and Arrangements & Nonprofit Organizations	<ul style="list-style-type: none">
Legal Persons–Access to beneficial ownership and control information (R.33)	<ul style="list-style-type: none"> Repeal legislation allowing share warrants to bearer; Ensure that Companies House’s data base is searchable by all relevant fields; Provide the FSC complete access to information on file at Companies House; and Allow police and customs to compel production of client information required to be maintained by licensees under customer identification requirements in domestic and international criminal investigations. Use schedule 10 of the Companies Ordinance as a model.
Legal Arrangements–Access to beneficial ownership and control information (R.34)	<ul style="list-style-type: none"> Abolish or limit asset protection trusts, or failing that require disclosure of the name and address of the settlor in addition to the other information required in the registration application; Amend trust legislation to restrict the use of “flee clauses;” and Consider requiring trusts that hold shares in corporations to disclose the trust settlor, beneficiaries, and/or trustees.
Nonprofit organizations (SR.VIII)	<ul style="list-style-type: none"> Review the current legislation and approval and monitoring process in light of the FATF documents that the assessors provided to the Board; and Review, in particular, the current policy of granting a blanket exemption from registration to religious charities.
6. National and International Cooperation	<ul style="list-style-type: none">
National cooperation and coordination (R.31 & 32)	<ul style="list-style-type: none">
The Conventions and UN Special Resolutions (R.35 & SR.I)	<ul style="list-style-type: none"> Request that the Vienna and ICSFT Conventions be extended to it at the earliest possible occasion.
Mutual Legal Assistance (R.36, 37, 38, SR.V & 32)	<ul style="list-style-type: none"> Gibraltar and U.K. authorities should move swiftly to conclude agreements to implement the MLA (International) Ordinance, in order to improve the ability of Gibraltar to provide mutual legal assistance to non-Schengen countries. Gibraltar should amend the CJO to enable local authorities to secure restraint and charging orders in connection with nondrug related criminal investigations being conducted

	<p>abroad.</p> <ul style="list-style-type: none"> • Customs and police should have the authority to seize and detain suspicious cash and bearer negotiable instruments whose provenance is unknown, on the same terms as that provided by the DTO for seizure of cash suspected to be related to drug trafficking. • The governor should issue an order, pursuant to the terms of the CJO, promulgating a list of countries whose authorities are entitled to register and enforce nondrug related confiscation orders in Gibraltar. • Gibraltar authorities should clarify the authority of the GFIU to issue “nonconsent” letters, and issue guidelines for their use; and • Gibraltar authorities should compile in one location more detailed statistics on mutual legal assistance requests and responses.
Extradition (R. 39, 37, SR.V & R.32)	<ul style="list-style-type: none"> • Consider elaborating procedures—including for example form response letters for requesters, checklists for dealing with HM Foreign Service, etc.—for responding to extradition requests in money laundering and terrorist financing cases.
Other Forms of Cooperation (R. 40, SR.V & R.32)	
7. Other Issues	
Other relevant AML/CFT measures or issues	

Authorities’ response

91. The Government welcomes the recognition given by the IMF to the efforts of the Gibraltar financial services industry and the regulator to ensuring that strong preventative and deterrent measures against the threats of money laundering and terrorist financing are effective. This has enabled both the industry and the Gibraltar FSC to apply an AML/CFT regime that addresses the real risks facing a small international financial services centre.

92. The Government has recognized that in order for these measures to continue to be effective, the regulatory requirements here, as elsewhere, always need to develop and has already embarked on a major revision to the framework and methodologies for systems of control operated by the industry. These changes when combined with the legislative amendments, to be implemented by the Government of Gibraltar to give effect to the 3rd Money Laundering Directive, will ensure that Gibraltar's AML/CFT regime for the regulated financial services sector will continue to be at the forefront of international best practice.