

INTERNATIONAL MONETARY FUND



Staff Country Reports

**Liechtenstein: Assessment of the Supervision and Regulation of the Financial Sector
Volume I—Review of Financial Sector Regulation and Supervision**

This review of financial sector regulation and supervision in **Liechtenstein** in the context of the offshore financial center assessment program contains technical advice and recommendations given by the staff team of the International Monetary Fund in response to the authorities of Liechtenstein's request for technical assistance. It is based on the information available at the time it was completed on **August 2003**. The staff's detailed assessment of the observance of standards and codes can be found in Volume II. The views expressed in these documents are those of the staff team and do not necessarily reflect the views of the government of **Liechtenstein** or the Executive Board of the IMF.

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**ASSESSMENT OF THE SUPERVISION AND REGULATION OF THE
FINANCIAL SECTOR**



**Volume I: Review of Financial Sector Regulation
and Supervision**

Principality of Liechtenstein

AUGUST 2003

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ACRONYMS

AML	anti-money laundering
BCP	Basel Core Principles for Effective Banking Supervision
CFT	combating the financing of terrorism
DDA	Due Diligence Act
DDU	Due Diligence Unit
DDEO	Due Diligence Executive Order
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FT	financing of terrorism
FSA	Financial Services Authority
FIU	financial intelligence unit
IAIS	International Association of Insurance Supervisors
IOSCO	International Organization of Securities Commissions
ISA	Insurance Supervisory Authority
MFD*	Monetary and Financial Systems Department
ML	money laundering
MOU	Memorandum of Understanding
SAR	suspicious activity report
UCITS	undertakings for collective investments for transferable securities (investment funds, mutual funds)

* The IMF's Monetary and Exchange Affairs Department (MAE) was renamed the Monetary and Financial Systems Department (MFD) as of May 1, 2003. The new name has been used throughout the report.

PREFACE

In July 2000, the Executive Board approved a program of assessments on the basis of a paper “Offshore Financial Centers—The Role of the IMF” published in June 2000.¹ In this context, the government of Liechtenstein invited the IMF to carry out an assessment of the country’s compliance with internationally-accepted standards for the regulatory and supervisory arrangements. The activities of Liechtenstein financial institutions include resident and nonresident alike, with no difference in the supervisory and regulatory arrangements for domestic and offshore activities. The assessment was carried out on the basis of the “Module 2” approach, which is described in the June 2000 policy paper—SM/00/136).

The mission consisted of Mr. Michael Moore and Ms. Jennifer Elliott (both Monetary and Financial Systems Department), and Ms. Moni SenGupta (Legal Department) of the International Monetary Fund; Mr. Michael Deasy (Central Bank of Ireland); Mr. Guillaume Leroy (private consultant from France); Mr. Ronald Ranochak (private consultant from the United States); and Mr. Alain Vedrenne-Lacombe (Bank of France). Ms. Bärbel Bernhardt (MAE) was the assistant to the mission. The team received excellent cooperation from the government and industry, and expresses its appreciation to the staff of the Due Diligence Unit (DDU), the Financial Intelligence Unit (FIU), Financial Services Authority (FSA), and the Insurance Supervisory Authority (ISA).

The mission team held extensive discussions with regulatory agencies active in the financial sector—DDU, FIU, FSA, and ISA—and conducted meetings with representatives of several banks; accounting firms; lawyers; trustees; representatives of the insurance industry; and law enforcement and judiciary bodies. The meeting participants were well prepared and the mission engaged in candid discussions regarding the regulatory and supervisory framework. The mission team observed very dedicated and professional staff in each of the agencies carrying out their tasks diligently.

¹ *IMF Board Reviews Issues Surrounding Work on Offshore Financial Centers*, (July 10, 2000, NB/00/62, <http://www.imf.org/external/np/sec/nb/2000/nb0062.htm>.)

Offshore Financial Centers—The Role of the IMF, (June 23, 2000—SM/00/136, <http://www.imf.org/external/np/mae/oshore/2000/eng/role.htm>.)

EXECUTIVE SUMMARY

This report contains the findings of an MAE mission that visited Vaduz from October 28 to November 8, 2002, as part of the Fund's initiative for offshore financial centers. The mission was conducted under Module 2 of the OFC initiative, as described in the Board paper "Offshore Financial Centers: the Role of the IMF" (SM/00/136 of June 23, 2000).

Under Module 2, the mission team carried out detailed assessments of Liechtenstein's implementation of four international supervisory and regulatory standards that considered (i) the Basel Core Principles (BCP) for effective banking supervision; (ii) International Association of Insurance Supervisors (IAIS) core principles for insurance supervision; (iii) the International Organization of Securities Commissions (IOSCO) Objectives and Principles of Securities Regulation; and (iv) Financial Action Task Force (FATF) 40+8 Recommendations for anti-money laundering and combating the financing of terrorism.² Main observations and recommendations are provided in Table 1 according to the four sets of standards.

The mission team considered the supervisory and regulatory activities of the FSA with respect to two of the detailed assessments. The first considered the level of compliance with the Basel Core Principles and the second considered the level of implementation of the IOSCO principles for regulation of securities activities. The observations from these two assessments are that there is a high level of dedication among FSA staff, and that financial sector supervision and regulation is underpinned by a good foundation of modern laws and regulations that derive from Liechtenstein's membership in the European Economic Area (EEA).

The mission team noted material weakness in the adequacy of resources for the FSA. Presently, resources are not sufficient to effectively use the work of the auditors and the regulatory reporting in order to carry out off-site supervision and monitoring. The FSA must be in a position to properly analyze the financial reports and audit results, which it currently does not, in order to communicate specific instructions to the auditors and regulated institutions. The weaknesses result directly from insufficient staff for the supervision and regulatory functions. Priority attention should be given to increasing the staffing level to better carry out the off-site monitoring requirement and to improve the FSA's ability to actively develop policy that fits with the needs of the Liechtenstein market. An increase in resources will require legislative action to add the positions and to have funding to pay salary, benefits, and provide for office space.

² The mission conducted the AML/CFT assessment based on the October 2002 final methodology that was endorsed by the Financial Action Task Force at their plenary meeting on October 11, 2002.

For the ISA, the issue of resources is less pronounced; however, it remains a concern.

The ISA oversees 12 life insurance firms, 4 non-life companies, and 5 reinsurance companies, all with growing cross-border activity. The supervision of the insurance activities, along with continuing responsibilities for the oversight of social security (pension funds, health and sickness insurance, and accident insurance), are placing heavy demands on the ISA's small staff. The mission team strongly supports the ISA's intention to develop increased capacity to conduct on-site inspections, with augmented prudential reporting requirements that begin in 2003. This planned activity will need to be appropriately supported with additional professionals for the ISA.

The mission team observes a high level of compliance with international standards for anti-money laundering and combating the financing of terrorism (AML/CFT); particularly, the standard issued by the Financial Action Task Force (FATF).

The heightened commitment to AML/CFT efforts reflects, in large part, the FATF's adverse listing of Liechtenstein as a "noncooperative" country in the fight against money laundering in June 2000. Following significant strengthening measures by the authorities and the industry, the FATF observed progress in addressing earlier identified deficiencies and, subsequently, removed Liechtenstein from its list of non-cooperative countries or territories in June 2001 and ceased further monitoring in June 2002.

Planning is underway to create an integrated financial supervisory authority that would bring together the current supervisory and regulatory functions of the FSA, the ISA, and the DDU.

The government's January 2002 study that reviewed the options for an integrated supervisory agency proposes that the agency be in place by 2004. The creation of the new agency is now planned for early 2005, with legislative changes to be completed in mid 2004. The mission team strongly supports the timely creation of an integrated regulatory agency, as its creation would provide an efficient vehicle to address some of the resource concerns raised in this assessment. The mission team recommends, in the preparation of implementing legislation, that the drafters be mindful that the new agency should be vested by law with a clear mandate, that there be operational independence (including sufficient funding resources) and flexibility to add staff, that the agency be granted the authority to license and withdraw licenses, levy penalties and other sanctions against regulated entities without approval from government, and that the new agency have the power to make legally binding rules.

This report (Volume I) contains the executive summary; an introduction and financial system overview, including a description of the supervisory and regulatory environment (Chapter I); and a summary discussion of the results of the detailed assessments (Chapter II). Volume II contains the detailed assessments of implementation of the four supervisory and regulatory standards.

Table 1. Recommendations and Follow-Up Plan

Observations	Recommendations
Financial Services Authority	
<p>General drawbacks to the structure and independence of the FSA.</p>	<p>The FSA’s mandate should be set out more clearly in the law—current provisions are sometimes vague and there is no clear constitution of the agency itself.</p> <p>The FSA could operate more independently and should be granted authority to license and withdraw licenses, levy penalties and other sanctions against regulated entities without approval from government.</p> <p>The FSA should have the ability to make legally binding rules.</p> <p>The FSA should introduce some transparency measures to its work—including a more detailed annual report and a website, which would assist the public in understanding its function and create a more accountable regulatory process.</p> <p>The FSA would benefit from efficiencies that would come through the medium-term effort to establish an integrated financial service regulator.</p>
Banking supervision	
<p>Insufficient staff resources and experience for effective and comprehensive analysis of audit reports and bank reporting and understanding of banks’ operations.</p>	<p>Recruit experienced staff, implement more training for staff.</p>
<p>Auditors rely on Swiss or other practices regarding credit and operational risk because of gaps in law</p>	<p>FSA should formalize a complete set of rules.</p>
<p>Remedial orders applied to banks are undefined</p>	<p>Create series of specific and gradual remedial measures.</p>
Insurance supervision	
<p>Insufficient resources to carry out adequate on-site reviews</p>	<p>Recruit experienced staff</p>
<p>Inadequate guidance on assets for unit-linked policies and asset-liability management</p>	<p>Adopt rules with respect to assets for unit-linked policies and asset-liability management.</p>
Capital markets regulation	
<p>Insufficient staff resources and experience for effective oversight of audits of investment funds</p>	<p>Recruit staff, expand training opportunities for staff and consider foreign counterparts as a source of training.</p>
<p>Asset managers with general trustee licenses operating without proper supervision</p>	<p>Create separate license for asset managers; FSA to have inspection power over asset managers, establish audit program for asset managers.</p>
Anti-money laundering	
<p>Financing of terrorism is not fully covered under existing legislation.</p>	<p>Complete the proposals to add a new provision for financing of terrorism that includes financing of planned terrorist acts and gathering or assembling of funds for a wide range of terrorist acts.</p>

Observations	Recommendations
The prohibition against tipping off after filing of SARs is limited to the ten-day automatic blocking after filing. Further, the automatic ten-day blocking of accounts and transactions upon filing of SARs is overly broad.	The prohibition against tipping off should not be limited in time and should be permanent. The automatic 10-day blocking should be replaced by discretionary authority of the FIU to block accounts and transactions from a period of 48 hour up to 10 days, when necessary after the filing of a SAR. There should be a specific administrative sanction for violations of the tipping-off prohibition.
The external audits for due diligence for banks are currently required to be conducted separately from the supervisory audits and by different auditors. This framework does not capitalize on depth of management and internal control information available in the supervisory audit, and may result in gaps of coverage.	The due diligence audit for banks should be conducted by the same auditor that conducts the supervisory audit. These audits should be conducted in a coordinated manner, if not concurrently. The statutory requirement for independence is sufficient to ensure that audits are conducted thoroughly and without undue influence.
No industry guidance exists for the insurance sector to identify activities vulnerable to money laundering.	Guidelines for monitoring of accounts should be amended to require special attention to single-premium life and buying and selling second-hand endowments.

I. INTRODUCTION AND FINANCIAL SYSTEM OVERVIEW

1. At the request of the authorities, an MAE-led mission visited Liechtenstein from October 28 to November 8, 2002. The mission assessed Liechtenstein’s observance of financial sector supervisory standards in the context of a Module 2 of the IMF’s initiative for offshore financial centers and the arrangements for anti-money laundering and combating the financing of terrorism (AML/CFT).

A. Background

2. Liechtenstein is a sovereign state with a population of 34,000 occupying a 160 square km area between Austria and Switzerland. It has a customs union and monetary union with Switzerland. Liechtenstein belongs to the European Free Trade Association (EFTA), the European Economic Area (EEA), and is a member of the United Nations.

3. *Government*—Liechtenstein is a constitutional monarchy with a democratically elected parliament; H.S.H., the reigning Prince Hans-Adam II of Liechtenstein, is currently the monarch and Head of State. The Cabinet is elected by the Diet and confirmed by the Prince. The Prince usually appoints the leader of the majority party in the Diet as the head of government and the deputy head of government is usually the leader of the largest minority party. The consent of both the Prince and Diet is needed to enact new legislation. The unicameral Diet has 25 seats and Members are elected by universal suffrage using proportional representation for a period of four years.

4. Liechtenstein law incorporates aspects of both Swiss and Austrian law with local characteristics. The court system consists of a district court (Landgericht), a court of appeals (Obergericht), and a supreme court (Oberste Gerichtshof). There is also a constitutional court with respective powers in the area of public law.

5. *Relationship with the European Union (EU)*—The relationship between Liechtenstein and the EU is based on the EEA Agreement. Liechtenstein has been a member of the EEA since May 1995. The EEA serves as a bridge between the European Free Trade Association and the European Union. Membership in the EEA permits Liechtenstein to participate in the single market, while not assuming the full responsibilities and rights of membership in the European Union.

B. Financial Institutions and Markets

Structure of the economy

6. In 1924, Liechtenstein entered into a customs and economic union with Switzerland and, since that time, has developed into a highly industrialized, free-enterprise economy. Liechtenstein's economic success has been facilitated by liberal economic legislation, an expandable and skilled work force (about 44.9 percent of the work force commutes daily from Austria or Switzerland), tax advantage for resident companies (20 percent maximum), and a strict legal duty of confidentiality for banks.

7. Economic activity today is largely based on the manufacturing and services sectors. Manufacturing accounts for about 45 percent of GDP and services 55 percent. More than 40 percent of exports currently go to EU countries with an additional 12 percent to Switzerland. The financial services sector employs about 2,000 people and accounts for some 30 percent of government revenues.

Financial services sector

8. Liechtenstein's financial services sector offers a wide range of services, including banking, trust, other fiduciary services, investment management, and insurance to a global market with a majority of the services provided to nonresidents.

9. The Liechtenstein banking sector is regulated under the Law on Banks and Finance Companies of 1992, as amended. At end-2001, the balance sheet assets for the 17 banks were CHF 34 billion (\$23 billion), with off-balance sheet items (including derivative contracts) of CHF 1.3 billion. Assets under management of banks reporting are CHF 106 billion. For the year ended December 2001, nine banks made profits; six broke even or made marginal profits or losses, and two, which were just recently established, made significant losses. In terms of balance sheet size, the three largest banks account for almost 90 percent of bank market share.

10. Two of the three largest banks are publicly quoted on the Swiss stock exchange; the third was once listed but is now privately held by the family of the Prince of Liechtenstein. Ten of the remaining banks are subsidiaries of foreign banks (5 from Austria, 3 from Switzerland, 1 from Germany, and 1 from France). The remaining four banks are owned by local interests. Four of the banks have operations in foreign countries, generally in the form of banks and investment and trust companies. These are mainly located elsewhere in Europe and in the Caribbean.

11. There were 16 licensed fund-management companies and 5 licensed investment companies managing a total of 81 authorized funds with CHF 5.2 billion in client funds under management in Liechtenstein as of June 2002. The FSA has responsibility for bank supervision as well as fund-management activities; however, its responsibilities with respect to trustees are limited to primarily the licensing of their activities.

12. Corporate bodies are formed under the Law on Persons and Companies 1926, as amended, known as the PGR Code. Trust enterprises are formed under the Law Concerning the Trust Enterprise 1928. Principal providers of these services are the 355 trustees and 87 attorneys licensed to operate in Liechtenstein. Many of the trustees and a few attorneys also carry on portfolio-management activity. A wide variety of legal entities may be formed. The most commonly used are Company Limited by Shares, Limited Liability Company, The Establishment (Anstalt), The Foundation (Stiftung), and the Trust Enterprise (Liechtenstein is the only civil law jurisdiction that has adopted largely Anglo-Saxon trust legislation).

13. As of July 2002, there were 21 insurance companies (12 life, 4 non-life, and 5 reinsurance companies) licensed and supervised by the Insurance Supervisory Authority, with a premium volume of CHF 500 million and assets totaling CHF 1.8 billion. Three Liechtenstein banks jointly hold a minor participation besides other shareholders in one insurance company. In addition, 34 Swiss and 1 EEA insurance providers operate in Liechtenstein with an agency, and more than 100 EEA and Swiss insurance providers have notified their intention to operate in Liechtenstein by the way of freedom to provide services; these companies are supervised by their home-country authorities (financial supervision; cf. Art. 13 of the First Non-Life Directive and Art. 15 of the First Life Directive). Foreign companies based in the EU or in Switzerland are—with respect to their activity in Liechtenstein—subject to the supervision of general Liechtenstein law through the ISA even if they depend on the authority of their home country for financial supervision. (cf. Art. 56 of the Insurance Supervision Law; Art. 10 of the Agreement between Liechtenstein and Switzerland concerning direct insurance; Art. 40 Para. 5 Third Life und Third Non-Life Directive).

C. Regulatory Framework, Oversight, and Market Integrity Arrangements

14. The government of Liechtenstein is the primary authority for licensing all banking, investment, and insurance activities. As an EEA member, Liechtenstein is obliged to transpose relevant EU legislation into national legislation. Accordingly, all banking, insurance, securities, and accounting legislation are based on the relevant EU Directives.

Because of its close monetary links with Switzerland, financial institutions—primarily banks—are also required to meet the accounting guidelines of the Swiss regulatory authority (Swiss Federal Banking Commission).

15. Supervision for banking and securities activities is based on a dualistic system where the FSA relies on external auditors to be directly responsible for on-site supervision of financial intermediaries.³ Supervision for insurance is more reliant on the direct supervision by the ISA, with reliance on auditors and actuaries for specific reporting on activities of insurance firms. The auditors are paid by the entities they audit. The regulatory agencies have some shared competencies and maintain close contacts and cooperation. Professional associations for banks, investment funds, insurance companies, trustees, lawyers, and auditors play an active role in promoting best professional practices. The bankers' association manages the deposit and investment insurance scheme. Finally, supervisory agencies can issue administrative orders to enforce legal and regulatory provisions; punishments for criminal infringements are pronounced by the courts; administrative sanctions are imposed by the government; and disciplinary penalties are imposed by the President of the Court of Appeals (Obergericht).

16. The FSA, formerly the Banking Supervisory Authority, dates from 1993 and was at that time charged with regulating and supervising the legal compliance of banks and financial companies. In 1996, these powers were extended to the regulation and supervision of investment companies; in 1999, they were extended further to the regulation and supervision of trustees, lawyers, accountants, and auditing companies. The FSA is an office responsible to the ministry of finance. Within the FSA, there are 11 staff members. The FSA's director, one consultant, and another administrative person carry out the oversight of the banking and finance company sector. Two lawyers and an administrative person carry out the oversight of investment funds. Oversight of the other service providers such as lawyers, trustees, and auditors is carried out by another professional. All FSA departments are assisted by the legal department, which is staffed by two lawyers.

³ The mission team recommends in the section of the report, "***Proposal to create an integrated financial supervisory authority***," that while it is still appropriate to rely on external auditors for supervision tasks, the FSA should also have capacity to carry out some on-site inspection tasks.

Table 2. Developments in the Financial Sector

Type of Institution	2000	2001	June 30, 2002
Banks	15	17	17
Number			
		(million CHF)	
Assets	36,522.4	34,340.6	33,156.7
Loans	12,036.4	11,619.9	11,260.9
Deposits	28,440.7	26,773.9	24,781.1
Tier 1 Capital	4,291.2	4,646.4	4,463.2
Net Income	546.1	440.0	174.5
Assets under management (million CHF) (three firms reporting)	113,669.6	105,842.4	n.a.
		(in percent)	
Return on assets (average)	1.5	1.3	1.1 Annualized
Investment Funds			
Number	44	72	81
Total assets (million CHF)	3,038.4	5,600.7	5,200.5
Mutual funds			
Insurance			
Number of life insurance firms	7	10	12
Premium income (million CHF)	302.5	426.6	n.a.
Number of non-life firms	3	4	4
Premium income (million CHF)	8	19.3	n.a.
Number of reinsurance firms	4	5	5
Trustees			
Number (natural persons / legal entities)	67 / 256	79 / 265	79 / 276
Memorandum items:			
Number of registered incorporated entities (approximate)			31,000
Number of foundations that are deposited (approximate)			51,000
of which have a commercial purpose (approximate)			2,900
Number of family purpose trusts (approximate)			1,500

17. The Banking Act also provides for the establishment of a banking commission. The purpose of the commission is to advise the government on banking supervisory matters, particularly on licensing issues. It is also charged with counseling the independent work of the FSA.

18. The Insurance Supervisory Authority has responsibility for the supervision of the insurance industry. Among the ISA's present duties are additional operational tasks to run the social security system, as well as its supervisory activities for occupational pension funds, social health insurance, and companies which run the compulsory accident insurance program (occupational and personal). The ISA, including the director has a staff of six professionals, and one clerical staff. The ISA staff conducts on-site inspections, but given the

small staff, these activities are limited. The ISA is authorized to require information directly from the institutions that it supervises. The ISA is part of the Office of the National Economy under the ministry of economy.

19. Responsibility for enforcing Liechtenstein's due diligence/anti-money laundering legislation, as well as coordination with international bodies resides with the Due Diligence Unit, which was established as a separate department responsible to the ministry of finance in October 2001. Previously, the FSA had responsibility for the DDU. The DDU includes a director, three lawyers, and one clerical staff. The Financial Intelligence Unit was also established in 2001. It is an administrative body with a director, four professionals, and an administrative staff.

20. The financial sector legislation has comprehensive provisions that set out minimum audit requirements and qualifications for auditors. Criteria for the licensing of auditors consider independence, professional organization and management, and financial soundness. The audit firms must certify that financial institutions comply with the law and the statutes, that the prerequisites for licensing are met permanently, and that the business is conducted on a sound basis. By law, auditors must have complete access to any documents they deem necessary to fulfill their duties. For regulated entities subject to the external audit requirement, appropriate measures must be enforced when legal provisions are not met, and the FSA and ISA must be informed of the outcome of the actions. However, any serious infringement must be immediately reported to the supervisory authorities. For regulated firms, the scope of audit reviews is defined through the regulatory outline of the auditor's reports as set out in laws and ordinances. For companies more generally, the FSA does not set any specific terms of the audit, but has the power to do so. As well the FSA can require auditors to answer specific questions or examine specific issues at any time.

Proposal to create an integrated financial supervisory authority

21. Under discussion is an effort to consolidate the agencies involved in financial sector supervision and regulation into a single integrated financial supervisory authority. Under the proposal, the current functions of the FSA, the ISA, and the DDU would be brought together into the integrated regulator. The efforts are proceeding according to a January 2002 report prepared by a project team. A formal steering group has now been formed to guide the process. The preparation of implementing legislation is underway, with the intent that a new law be in place in mid-2004, and that the integrated regulator be in place by early 2005.

22. The mission team concludes that a deepening of the supervisory and regulatory functions is needed and strongly supports the medium term-effort to establish an integrated financial service regulator. Important in this medium term-effort, is that immediate priority be given to adding staff sooner for the present needs of the FSA and ISA. The immediate staffing needs should not be delayed while awaiting the creation of the integrated agency.

23. The mission team recommends that with the preparation of implementing legislation that the drafters are mindful that the new agency should be vested by law with a clear mandate as the financial sector regulatory agency. Consequently, it is important to provide the integrated agency with proper operational independence (including sufficient funding resources) and flexibility to add staff. Among the powers that should be vested with the integrated agency are the authority to license and withdraw licenses, levy penalties and other sanctions against regulated entities without approval from government, and that the new agency have the power to make legally binding rules.

24. The mission team's view is that the proposed integration of the supervisory and regulatory functions would offer advantages over the current structure. A single agency could allow for more efficient administration of the supervisory functions through greater flexibility in the allocation of staffing resources. Moreover, an integrated agency would better allow for the development of common information systems and administrative support mechanisms.

25. In conjunction with the review of the proposal to create an integrated supervisory agency, the mission team further recommends that the integrated agency have capacity to carry out on-site inspections of regulated entities. While the dualistic approach of reliance on external auditors is still very much an accepted international practice for the conduct of onsite supervision, there is strong momentum developing towards supervisory agencies also having a capacity to carry out on-site inspections. This trend has developed greater momentum in today's environment where there is an increasing demand on auditors for services other than traditional accounting/auditing activities. A capacity within the integrated supervisor to at least conduct limited-scope inspections would provide a useful safeguard to the traditional reliance of external auditors. Particularly, the integrated regulator should have a case-by-case capacity to review on-site the adequacy and compliance with due diligence requirements, internal control policies, credit underwriting, operational risk, and market risk.

26. The proposal to integrate the supervision and regulation efforts will further enhance coordination and effectiveness between the prudential and due diligence requirements imposed on regulated financial intermediaries. In addition, the integration of functions would facilitate domestic information sharing and help to resolve current concerns relating to the exchange of information between the ISA and FSA, and the ISA and DDU as these agencies do not operate from within a common ministry. Moreover, the structure would provide a more efficient framework for conducting consolidated supervision with foreign regulators.

Key legislation affecting the financial services sector:

- The Persons and Companies Act 1926, as amended;
- Law Concerning the Trust Enterprise 1928, as amended;
- Act Concerning Banks and Savings Funds 1960;

- Act Relating to National and Local Taxation 1961, as amended;
- Law on Banks and Finance Companies 1992 (Banking Act (BA)), as amended;
- Act on Trustees 1992, as amended;
- Act on Lawyers 1992, as amended;
- Act on Auditors and Audit Companies 1992, as amended;
- Banking Ordinance on the Banking Act 1994 (Banking Ordinance);
- Law on the Supervision of Insurance Undertakings (Insurance Supervision Law) 1995
- Executive Order on the Law on Supervision of Insurance Undertakings 1996;
- Law on Investment Undertakings, 1996, as amended;
- Ordinance on the Law on Investment Undertakings 1996;
- Law on Professional Due Diligence in Financial Transactions (Due Diligence Act, DDA) 1996, as amended;
- Executive Order Concerning the Law on Professional Due Diligence (Due Diligence Executive Order, DDEO) 2000, as amended;
- Law on the Amendment of the Criminal Code 2000;
- Law on International Mutual Assistance in Criminal Matters (Legal Assistance Law)
- Law on the Amendment of the Code of Criminal Procedure 2000;
- Insurance Contract Act of 2001;
- Law on the Financial Intelligence Unit (FIU-Law) 2002.

Previous third-party reviews of regulatory arrangements

27. In September 1999, the Council of Europe's PC-R-EV⁴ conducted an examination of Liechtenstein's anti-money laundering program and reported a number of weaknesses of varying severity. Prior to the PC-R-EV examination, Liechtenstein had initiated a self-review

⁴ Liechtenstein is a member of the PC-R-EV, which is a FATF-Style Regional Body. Since the earlier assessments, the PC-R-EV has changed its name to Moneyval.

of its anti-money-laundering regime. Efforts were undertaken to address weaknesses to the legislative and enforcement mechanisms that were identified from the self-review.

28. In June 2000, Liechtenstein was identified by the FATF as a noncooperative country and territory (NCCT). The listing prompted the Liechtenstein authorities and private sector to strengthen the anti-money laundering regime. In June 2001, the FATF reviewed the progress made by Liechtenstein in implementing reforms. Though the FATF continues to express some concerns regarding implementation, the FATF delisted Liechtenstein in June 2001 on the basis of commitments for further affirmative action by the prime minister. In June 2002, the FATF decided to cease its monitoring, recognizing the improvements Liechtenstein had implemented.

29. In January 2001, the PC-R-EV follow-up to a self-assessment, noted substantial progress in adopting measures to prevent and combat money laundering; specifically, changes in legislation and the institutional framework. These changes included the (i) amendment of the Due Diligence Act and new Due Diligence Executive Order; (ii) creation of duties of due diligence/compliance department within the FSA and creation of the FIU; (iii) revision of the Law on International Mutual Assistance in Criminal Matters (Legal Assistance Law); (iv) increased staffing at the Princely Court and Public Prosecutor's office; and (v) creation of a special unit at the National Police Force to combat financial crime.

30. In May 2000, the Financial Stability Forum (FSF) released the results of a study provided by an FSF working group on offshore financial centers. The study, which is now out of date, was based on a 1999 survey of onshore supervisors in 27 countries. Based on the survey, the FSF working group placed 42 jurisdictions (countries and territories) among three groups. Liechtenstein along with 26 other countries and territories was placed in group three,⁵ the FSF viewed group three jurisdictions as having weak supervision and not adhering to international standards. Taking into account the improvements implemented since the 1999 FSF survey, the assessment team considers it unlikely that the result would be the same today.

⁵ Group one jurisdictions were viewed to be cooperative, with adequate legal and supervisory systems adhering to international standards. Group-two jurisdictions were viewed as having most components for supervision and cooperation in place, but fall short of meeting international standards.

II. OBSERVANCE OF FINANCIAL SYSTEM STANDARDS AND CODES: SUMMARY ASSESSMENTS

31. The mission assessed the level of observance with the supervisory and regulatory principles relative to: (i) the Basel Core Principles for effective banking supervision; (ii) the IAIS Core Principles for insurance supervision; and (iii) the IOSCO Objectives and Principles of Securities Regulation. In addition, the mission completed an assessment of Liechtenstein's compliance with the FATF Recommendations for Anti Money Laundering on the basis of the final version of the AML/CFT methodology document.

32. The mission reviewed and assessed (i) the legal and institutional framework for AML/CFT, including the adequacy of criminal justice measures, international cooperation, and laws for preventative measure for financial institutions; and (ii) the effectiveness of implementation of preventative measures in the banking, insurance, securities and trust, and company service providers sectors.

A. Summary of the Basel Core Principles Assessment

General

33. This section provides summary findings from the assessment of the Basel Core Principles.⁶ The Liechtenstein banking sector is regulated under the Law on Banks and Finance Companies of 1992, as amended, and the Ordinance on the Banking Act 1994, as amended. The detailed legislative framework is based on the implementation of EU banking legislation as is required of Liechtenstein as a member of the European Economic Area (EEA). Both the government and the Financial Services Authority (FSA)—the latter established under the 1992 Act—share responsibility for banking supervision. The government is responsible for the granting, withdrawal, and the revocation of licenses. The FSA is responsible for ongoing supervision; it employs a dualistic system whereby it relies on external auditors to carry out on-site supervision while carrying out off-site supervision itself.

34. The assessors held discussions with current and former representatives of the FSA, the bankers association, the auditors association, as well as with commercial banks and the banks' external auditors. The assessors received full cooperation from the FSA. Its meetings with the FSA and other counterparty agencies and officials were conducted in an open and forthright manner. Access to consolidated prudential data was somewhat limited due to the lack of resources within the off-site monitoring unit of the FSA. This limited access, however, could not be said to have created any material obstacles in making the assessment.

⁶ The assessment was carried out by Mr. Michael Deasy (Central Bank of Ireland) and Mr. Alain Vedrenne-Lacombe (Bank of France).

35. The assessment was carried out in accordance with the ‘Core Principles Methodology’ paper issued by the Basel Committee on Banking Supervision in October 1999.

Institutional and macroprudential setting, market structure—overview

36. Seventeen banks and two finance companies operate in Liechtenstein. Finance companies, which are also supervised by the FSA, are permitted to engage in general banking business with the exception of deposit taking; one is a subsidiary of a major bank and is currently being wound up, the other engages in lending.

37. At end-2001, total banking assets were CHF 34.3 billion and assets under management were CHF 106 billion. The market is highly concentrated, with the three major banks accounting for 90 percent of the total banking assets; and 14 other institutions have set up operation over the last 10 years. Regulations allow universal banking activities, but only the three largest banks conduct retail and corporate banking mainly with resident customers. The credit portfolio is relatively small, comprising largely mortgages and Lombard loans. The major business is in private banking and wealth management.

38. Two of the three largest banks are publicly quoted on the Swiss stock exchange; the third was once listed but is now privately held by the family of the Prince of Liechtenstein. Ten of the banks are subsidiaries of foreign banks (5 from Austria, 4 from Switzerland and 1 from France). The remaining four banks are owned by local interests. Four of the banks have operations abroad; generally, in the form of banks, and investment and trust companies, located mainly elsewhere in Europe and in the Caribbean. The total staff working in the banking sector is 1,760 people.

39. All banks are relatively highly capitalized, all have a capital adequacy ratio above 15 percent and 16 were in excess of 20 percent at end-2001.

40. The downturn in the financial markets has had an impact on the industry; nine banks made profits in 2001, six more or less broke even, and the two most recently established institutions recorded substantial losses.

General preconditions for effective banking supervision

41. The banking system operates in a small, but highly developed, economy. Its public infrastructure (legal, accounting, payments, transparency, and financial sector oversight practice) are based on up-to-date international law and practice. Liechtenstein is a member of the European Economic Area since 1995 and as such, is obliged to transpose EU legislation into national legislation. Accordingly, all its banking and accounting legislation is based on the relevant EU Directives. The Swiss Franc is the official currency and the Swiss National Bank acts as lender of last resort.

42. Banks operate within a well-defined prudential regulatory framework in accordance with EU and Basel standards. These standards incorporate detailed provisions on corporate

governance: banks must have a dual management structure, with a board of non-executive directors and a management board; the internal audit function is well developed, as is the external audit function. The standards also contain detailed fit-and-proper criteria relating to directors, senior managers, and heads of internal audit.

Main findings

43. The legislative framework for banking supervision is comprehensive. As indicated above, responsibility for supervision is shared between the government and the FSA. While this agreement appears to have worked well, it would seem more desirable that supervision should be exercised by a single regulatory body. There is a strong willingness within the FSA to carry out its supervisory mandate, but its ability is seriously hampered by a lack of qualified staff. The main medium-term challenge for banking supervision is to recruit experienced staff.

44. **Objectives, Autonomy, Powers, and Resources (CP1):** A sound legislative framework for banking supervision exists; however, the inadequate staffing resources reflect a material deficiency.

45. The current staff complement of the banking supervisory department is two persons and a part-time banking consultant. Of the two persons, one is also head of the FSA and the second is an administrative assistant. The situation is exacerbated by a lack of continuity due to recent staff turnover. The impact of inadequate resources is reflected in the FSA's weak ability to carry out effectively on-site and off-site supervision. The assessors recommend the immediate recruitment of two banking analysts.⁷

46. The FSA has the legal authority to share information with foreign supervisory agencies in line with EU requirements. This authority was affirmed in a ruling by Liechtenstein's supreme administrative court on May 7, 2003. (See discussion in the response from the authorities.) The court's decision clarifies the authority for information exchange; however, the process remains untested.

47. **Licensing and Structures (CPs 2–5):** Banking activity and licensing criteria for banks and financial companies are consistent with international practices. They encompass strong governance requirements and, notably, fit-and-proper tests are applied to directors, senior managers and heads of internal audits.

48. **Prudential Regulations and Requirements (CPs 6–15):** Banks operate within a well-defined prudential regulatory framework, in accordance with the EU and Basel standards. However, the FSA has not defined more specific guidelines for operational risk or for credit risk assessment but instead relies extensively on the external auditors, who conduct

⁷ Following the close of the mission, the authorities report the creation of two additional professional positions, one of the positions was filled in June 2003.

the on-site examinations. Moreover, the absence of such specific guidelines means that consistent and rigorous policies in these areas may not be applied across the industry.

49. The Banking Act and the Banking Ordinance have comprehensive provisions on corporate governance: banks must have a dual management structure, with a board of nonexecutive directors and a management board; the internal audit function is defined, as well as the external auditor function. All of them are subject to supervisory authorities' scrutiny in the form of fit and proper tests for banks' officials and licenses for audit firms. Based on the comprehensive DDA, AML policies and procedures are in place.

50. **Methods of Ongoing Supervision (CPs 16–20):** The supervisory authority's ability to carry out its functions is undermined by the lack of staff and expertise. Actual resources are limited to the head of the FSA, who took his position on October 1, and a consultant, who is largely involved in the transposition of EU Directives. Since the mission, two positions were created in the Banking Supervision Department, one of these two positions was filled in June 2003. Because of a lack of resources the Banking Supervision Department is unable to conduct timely off-site monitoring of banks, nor to analyze promptly and thoroughly external audit reports. The Department should aim at having a better understanding of banks' activities, risks, and financial situations. In addition, enforcement powers, in the form of "orders" issued by the FSA, need to be more detailed and specific.

51. **Accounting Standards (CP 21):** In accordance with EU banking and accounting Directives, which have been transposed into Liechtenstein law, all banks must maintain adequate records drawn up in accordance with consistent accounting standards. They must also meet accounting guidelines set by the Swiss regulatory authority. Banks are also subject to an annual audit by external auditors, who are required to give an opinion as to whether the accounts give a true and fair view of the financial condition of the banks. Banks are required to publish their annual accounts.

52. **Formal Powers of Supervisors (CP 22):** Formal powers range from the FSA's ability to remove any officer of a bank, the suspension of business by a bank, recommending to the government that it withdraw a license, etc. The court of justice can impose imprisonment and fines on banks and bank staff for various offences, including violating the obligations connected with a license, furnishing false information to the FSA, failure to keep proper books and records, etc. The government can impose fines for offences, including failure to produce annual accounts or communicate with the FSA.

53. **Cross-Border Banking (CPs 23–25):** Consolidated supervision can be carried out whether Liechtenstein is the home or the host country; although, the FSA has not established MOUs with any foreign regulators. Specific provisions should be included in the legislation for Liechtenstein banks proposing to establish abroad.

Table 3. Recommended Action Plan in Relation to the Basel Core Principles

Reference Principle	Recommended Action
Independence and resources (CP 1-2)	Recruit experienced staff and/or train new staff
Other risks (CP 13)	Determine applicable norms
On-site and off-site supervision (CP 16)	Add resources for effective and comprehensive analysis of audit reports and bank reporting.
Bank management contact (CP 17)	Add resources for effective and comprehensive understanding of banks' operations
Off-site supervision (CP 18)	Add resources for effective and comprehensive understanding and analysis of audit and bank reports.

Authorities' response

54. The authorities expressed their thanks to the assessors, describing the experience as an enriching one. They appreciated the recommendations and expressed a willingness to put the recommendations into effect. In the area of greatest concern to the assessors, i.e., lack of resources, the authorities have stated that the recruitment of two additional banking staff members has been assured by government decision of December 3, 2002. Accordingly, the FSA will recruit two highly qualified auditors/financial analysts. One of these vacancies was already filled in June 2003. Furthermore, the organization of the FSA has been streamlined and the responsibility of each staff member has been defined. The FSA is also introducing a short- and long- term (permanent) training and education program in 2003.

55. In its decision of May 7, 2003, the supreme administrative court confirmed that information can be shared with foreign regulators while the information provided is only used within the scope of supervisory duties as described in the request of the foreign authority. Within the foreign authority, access to the information provided has to be granted only to persons who are subject to official secrecy provisions. The information has to be kept strictly confidential and may be used only in accordance with the agreed supervisory purpose. Any further disclosure of the information whether to other national authorities or to other foreign authorities is not allowed. In the case that according to the foreign legislation the information provided by the FSA has to be forwarded to other authorities, the regular mutual assistance procedure has to be duly complied with. Information is shared by the FSA according to this decision of last resort.

56. The FSA would further like to point out that there is an annual report published every year. This report has always been available to the public and can even be requested electronically under info@afdl.li. Nevertheless, the FSA acknowledges that this annual report could be improved with respect to level of detail. The FSA will strive to provide more detailed annual reports in the future.

B. Summary of the IOSCO Core Principles Assessment

General

57. This section provides summary findings from the assessment of implementation of the IOSCO Objectives and Principles of Securities Regulation (the IOSCO Principles).⁸ The assessment relied on the Fund/Bank Guidance Note for Assessing Implementation of IOSCO Principles. The limited nature of permitted securities activity in Liechtenstein was an important factor in assessing the IOSCO Principles.

58. The assessment was based on a review of the relevant legislation, questionnaires prepared by the authorities prior to the mission, detailed discussions with the staffs of the FSA and the DDU, and presentations by and discussions with members of industry and industry associations.

Institutional and macroprudential setting and market structure

59. **Securities related activity in Liechtenstein is focused on asset management for high net worth clients.** The major established business is asset management—carried out by universal banks, licensed under the Banking Act, and trustees acting as asset managers, licensed under the Law on Trustees. The majority of clients are located outside of Liechtenstein (the largest number are in Switzerland, followed by other European jurisdictions). Brokerage services—including the sale of mutual funds and securities—are also available to small retail investors at two of the banks. There are no secondary markets or underwritings in Liechtenstein. To the extent that banks participate directly on secondary markets, they do so through their operations in Switzerland. There have been six prospectuses filed in the past two years, following introduction of the Law on Prospectuses, all from the same issuer.

60. **The investment fund industry is relatively small and new but growing.** There are currently 81 investment funds with client assets of CHF 5.2 billion (up from CHF 437 million in 1996, when investment funds were introduced in Liechtenstein). Investment undertakings, as they are known in Liechtenstein law, may operate collective investment schemes organized as trusts or as limited liability companies and may not directly distribute funds. Many collective investment schemes are eligible under the UCITS directive for sale in other European jurisdictions. Investment undertakings do not distribute funds directly to the public.

61. Regulation of securities activities is largely the responsibility of the FSA, but some important aspects of regulatory oversight are carried out directly by the Cabinet. The FSA has general oversight responsibility for banks and investment undertakings. The FSA is responsible for screening licensing applications, reviewing and approving prospectuses and

⁸ The assessment was conducted by Ms. Jennifer Elliott.

disclosure documents, and supervising the audit process, as well as to taking supervisory measures. Licenses are granted formally by the government (Cabinet) at the recommendation of the FSA; withdrawal of licenses and imposition of fines are also carried out by the government at the recommendation of the FSA. The public prosecutor is responsible for enforcement activity. The DDU is responsible for enforcement of compliance with anti-money laundering regulations, including for banks, investment undertakings, and trustees. The preconditions for effective securities regulation, including a sound legal, accounting, and tax framework are in place in Liechtenstein.

Main findings

62. **Regulator (Principles 1–5): The FSA’s mandate should be set out more clearly in the law—current provisions are sometimes vague and there is no clear constitution of the agency itself.** The FSA could operate more independently and should be granted authority to license and withdraw licenses, and levy penalties and other sanctions against regulated entities without approval from government. The FSA should have the ability to make legally binding rules. The FSA should introduce some transparency measures to its work—including a complete annual report available to the public and on a website. This would assist the public in understanding its function and create a more accountable regulatory process.

63. Weaknesses in the assessment of the securities regulatory system are mostly related to the low level of staffing and resources at the FSA—particularly for the supervision of banks, which engage in securities activities. While current staff is professional and extremely diligent, the FSA does not have sufficient resources to make credible use of the inspection system. The FSA must be in a position to communicate specific instructions to the auditors and to properly analyze inspection results, which it currently does not. An adequate review of prospectuses in the growing investment funds market also requires greater staff time. Staff time is currently taken up with licensing issues and the implementation of EU Directives, leaving little time for supervision. Immediate attention should be given to increased staffing in order to use the existing inspection system effectively and improve the FSA’s ability to actively develop policy.

64. **Self-regulatory organizations (Principles 6 and 7): The regulatory system in Liechtenstein incorporates the activities of industry associations.** These resources are a complement to the stretched resources of the FSA. The FSA must be vigilant in maintaining resources and experience sufficient to benefit from the association’s work in the policy-making process but not be dominated by it. One industry association—the Trustees Association acts as a self-regulatory body, since membership in the association and compliance with its code of conduct is mandatory. The FSA should have a formal role in the association’s formulation of rules for asset management activities.

65. **Inspections, Investigations and Enforcement (Principles 8–10):** The FSA has full inspection and investigations authority other than over trustees, but requires resources to effectively execute this authority. The public prosecutor, responsible for enforcement, has

sufficient authority over regulated entities. While the FSA has a licensing authority over trustees, it does not have inspection authority (although these entities are subject to a DDU audit). Under the dualistic system, regular inspections of most regulated entities are carried out by third-party auditors. These audits could be extended to trustees acting as asset managers. The FSA does not have sufficient resources to make credible use of the inspection system, however, and must be in a position to communicate specific instructions to the auditors and to properly analyze inspection results.

66. **Information Sharing and Cooperation (Principles 11–13):** Domestic information sharing is fully implemented. In the case of trustees, the FSA is further limited by its lack of ability to obtain information through inspections and lack of responsibility for ongoing oversight. The FSA is not a party to any information-sharing agreement with foreign counterparts. A recent court case clarifies the authority of the FSA to share supervisory information with foreign supervisory agencies. (See discussion in the response from the authorities.)

67. **Issuers (Principles 14–16):** Issuance of securities is a rare event in the Liechtenstein market; nevertheless, the Principality has implemented the EU Prospectus Directive. Under the Law on Disclosure on Major Participation in Companies those with 10 percent or greater of voting shares are required to disclose transactions. There are no other continuous disclosure requirements, corporate governance or take-over bid rules—however, an issuer must be listed on an exchange, which would have such rules in place. The six prospectuses that have been reviewed and approved during the past two years, all have been from the same issuer (mostly in the form of amendments). Accounting standards are a mixture of EU and Swiss accounting standards and, for banks, IAS standards. Auditors are held to EU standards also.

68. **Collective Investment Schemes (Principles 17–20):** The legislative framework governing collective investment funds (known as investment undertakings) is largely in place in Liechtenstein, which has implemented the EU UCITs directive. Investment undertakings are subject to detailed licensing requirements, are audited annually by third-party auditors with reports made to the FSA and must publish disclosure documents in accordance with detailed rules. There is a need for conflict of interest rules for collective investment schemes—these rules should, among other things, address related party transactions, borrowing and lending with affiliates, trading using a related-party brokerage, employee conduct, and disclosure of conflicts of interest to clients. Net asset valuation rules should be developed in more detail with a clearer definition of transferable security that imports an element of liquidity and detailed requirements for the valuation of illiquid securities.

69. **Market Intermediaries (Principles 21–24):** Market intermediaries in Liechtenstein are banks and trustees who may act as asset managers—trustees acting as asset managers are largely unsupervised, although they are subject to a licensing process, and are inspected by the DDU. Regulation of banks is discussed in detail under the Basel Core Principles assessment. The extent of the asset management business carried on by trustees is unknown and because they operate under a general license, there is no transparency to the public. The

authorities should consider licensing these entities separately from other trustees and must implement periodic audits in order to monitor compliance with existing requirements. The need for more detailed rules (some of which should apply to trustees also) should be addressed in a global fashion with rules governing account documentation, representations made to clients, disclosure to clients (both risk and conflicts of interest), rules regarding related party transactions, and employee conduct.

Recommended actions and authorities' response to the assessment

Table 4. Recommended Action Plan in Relation to the IOSCO Principles

Reference Principle	Recommended Action
Principles Concerning the Regulator (P 1–5)	<p>Increased staffing resources are urgently needed. Training of staff should be a priority, consider working with other jurisdictions.</p> <p>The FSA mandate should be clearer in law.</p> <p>The FSA should have authority to grant, refuse and withdraw licenses for banks, investment undertakings and asset managers.</p> <p>Criteria for selection and dismissal of the FSA head should be set out in a manner that is transparent and legally binding on the government.</p> <p>Greater transparency through a website should be introduced the FSA should have the authority to make legally binding rules.</p>
Principles for the Enforcement of Securities Regulation (P 8–10)	<p>FSA should have the ability to withdraw licenses and levy fines.</p> <p>FSA should have authority to inspect and supervise trustees</p>
Principles for Cooperation in Regulation (P 11–13)	<p>FSA should enter into information-sharing arrangements with key counterparts, specifically the Swiss.</p>
Principles for Collective Investment Schemes (P 17–20)	<p>FSA should develop more detailed net asset valuation rules.</p> <p>FSA should develop conflicts of interest rules for investment undertakings.</p> <p>FSA should consider more detailed rules for duties of custodians.</p> <p>FSA requires more resources/more experience for review of audits and prospectuses.</p>

Reference Principle	Recommended Action
Principles for Market Intermediaries (P 21–24)	<p>Asset managers organized as trustees should be subject to a separate licensing procedure, which sets terms of their ability to carry out asset management business and makes this transparent to the public.</p> <p>FSA should have authority to license, supervise, withdraw licenses from, and make rules regarding asset managers.</p> <p>Asset managers should be subject to an annual FSA audit.</p> <p>FSA should develop more detailed rules regarding sales and business conduct of market intermediaries.</p>

Authorities' response

70. The authorities were generally in agreement with the report. The FSA acknowledges the need for more resources, but pointed out that it has created two staff positions since the assessment was carried out (both in banking supervision). One of these vacancies was already filled in June 2003. The government of Liechtenstein acknowledges that there is a lack of resources and is fully committed to do its utmost to grant the essential staff resources to the supervisory authorities. The authorities expressed some concern that the issue of trustees acting as asset managers was unduly emphasized, since the activities of trustees are low risk and trustees are inspected by the DDU. The FSA was concerned that additional responsibility for trustee regulation would stretch existing resources. The FSA did not agree that the Trustees Association is unsupervised.

71. With respect to the recommendation that criteria for selection and dismissal of the FSA head should be set out transparently in legislation, it has to be pointed out that it is most likely that under the law concerning the planned integrated financial supervisory authority the composition and structure of this authority will be set out. As a result, the recommendation will be fulfilled with the implementation of the integrated financial supervisory authority.

72. In its decision of May 7, 2002, the supreme administrative court confirmed that information can be shared with foreign regulators while the information provided is only used within the scope of supervisory duties, as described in the request of the foreign authority. Within the foreign authority, access to the information provided has only to be granted to persons who are subject to official secrecy provisions. The information has to be kept strictly confidential and may only be used in accordance with the agreed supervisory purpose. Any further disclosure of the information whether to other national authorities or to other foreign authorities is not allowed. In the case that, according to the foreign legislation, the information provided by the FSA has to be forwarded to other authorities, the regular mutual assistance procedure has to be duly complied with. Information is shared by the FSA according to this decision of last resort.

73. The authorities also pointed out a number of proposed changes on their immediate schedule including revised collective investment scheme and market abuse legislation as a result of new EU directives.

C. Summary of the IAIS Insurance Core Principles Assessment

General

74. This section provides summary findings from the assessment of the IAIS Core Principles.⁹ The assessment was based on discussions held with the staff of the Insurance Supervisory Authority (ISA), representatives of the Insurance Association of Liechtenstein, and insurance firms. The assessment considered several documents, including the review of the below legislation and guidance for on-site inspections.

- Liechtenstein—Switzerland agreement on direct insurance of December 19, 1996;
- Note on on-site inspection of July 17, 2002, by the insurance supervisory authorities;
- Note on report by insurance auditors and companies of May 21, 2002 by the Insurance Supervisory Authority;
- EC directives on insurance: life insurance third directive 92/96 of November 10, 1992, nonlife insurance third directive 92/49 of June 8, 1992, insurance accounting directive N91/674 of December 19, 1991.

75. In addition, the assessment considered the review of (i) the ISA circular letter on the use of assets in unit linked policies (November 30, 2000); (ii) a specific on-site inspection report; (iii) financial and structure information on insurance companies; and (iv) the draft financial report file to be sent by the companies to the supervisor from 2003 on.

Institutional and macroprudential setting—overview

76. Liechtenstein insurance companies did not exist until 1995, as insurance services were previously provided by branches of Swiss companies. In 1995, Liechtenstein joined the EEA while Switzerland remained outside. Liechtenstein was able to gain from its EEA membership by creating its own insurance market, which, with the implementation of third generation EU directives, allowed Liechtenstein companies to operate throughout the EEA under the provisions of freedom of services.

⁹ The assessment was conducted by Mr. Guillaume Leroy, JWA-Actuaires France.

77. Supervision of insurance activity in Liechtenstein is based on the Insurance Supervision Law of 1995, which formed the cornerstone of the insurance regulatory system following Liechtenstein's membership in the EEA.¹⁰ With a legal framework in place, the authorities established an institutional framework for insurance regulation. New companies were licensed starting in 1996 and by end-2002, there were 12 life insurance companies, 4 nonlife companies, and 5 reinsurance companies.

78. There are 34 branches of Swiss companies that operate in Liechtenstein under the principle of freedom of establishment between Switzerland and Liechtenstein. In addition, more than 10 Swiss companies have notified the ISA of their intention to take up business in Liechtenstein also under the arrangement of freedom to provide services. A company based in the EEA has also set up an affiliated company in Liechtenstein.

79. The Liechtenstein market consists of two parts. The first part is the local market, which is dominated by the branches of Swiss insurance companies with a premium income of about 197 million euros at end-2001. The second part is the life and reinsurance markets, which have been incorporated in Liechtenstein and carry out activities in the European Union, Switzerland, and other non-EU countries. It amounted to as much as 319 million euros in 2001.

80. As a consequence of Liechtenstein's EEA membership and its arrangement with Switzerland, the ISA is charged with the protection of predominantly non-Liechtenstein residents, whereas the Swiss Supervisory Authority has responsibility for the protection of Liechtenstein policyholders.

81. The assets held by the Liechtenstein companies amount to CHF 1.1 billion in the field of direct insurance (nearly all of it is made of assets matching life technical reserves) and CHF 0.78 billion for the reinsurance business, basically assets matching captives technical reserves.

82. For the time being, little global market data is available. In the field of solvency, there is no aggregate data, which makes it difficult to have an accurate view of the market, all the more so because there is no annual report from the Insurance Supervisory Authority or the Insurance Association.

¹⁰ The Executive Order on the Law on Supervision of Insurance Undertakings, 1996, is also highly relevant, as it details the practical application of the 1995 Insurance Supervision Law.

General preconditions for effective insurance supervision

83. Since the establishment of the market in 1995, insurance has been supervised by the Insurance Supervisory Authority, which is a department of the Office of National Economy, one of the government administrations in Liechtenstein. The ISA relies upon the activity of six trained people to achieve its tasks. The Due Diligence Unit oversees anti-money laundering requirements in the insurance sector. The supervision of the insurance industry will significantly evolve in 2003; the ISA has the intention to carry out more frequent on-site inspections, once the licensing process of the Liechtenstein incorporated companies has been finished.

84. The legislative framework for insurance supervision in Liechtenstein has been created over the last five to eight years. The insurance legislation implements EU directives and, therefore, broadly the same as other European jurisdictions. The Liechtenstein legal framework is additionally influenced by the civil law and written law systems common to many other continental European countries.

85. Yet, there are some specific aspects of Liechtenstein law; for instance, the presence of trusts, that make it slightly different from the legal framework of other continental countries and that give it specific features. However, the strongest influence over its rule does stem from EU directives and neighboring countries, especially Switzerland.

Main findings

86. The insurance industry in Liechtenstein is relatively young and, to date, no significant problems have emerged. While some improvement to supervision is required, the risks in the market appear relatively small due to the low-risk profile of the products sold.

87. The main area of concern regards the staffing of the Insurance Supervisory Authority, which is stretched to carry out on-site supervision. The staffing is an area of near-term needs, particularly, in that a number of ISA staff also must deal with other important issues, especially in the field of social security. To date, on-site inspections have been infrequent, and not comprehensive, which is ill-suited for the insurance environment given the increasing size of companies and risk profiles. Moreover, the additional staff will be needed for the off-site monitoring function, particularly given the improved reporting requirements that will take effect in 2003.

88. The insurance regulation has enabled the development of Liechtenstein's insurance market over the past seven years. To date, there have been no significant problems, yet there are a number of areas where further developments of the regulation system are required for a mature market. In this regard, not all IAIS principles are observed and some strengthening is necessary. The Liechtenstein authorities are aware of this situation and have started implementing new rules and practices.

89. The mission observes that the authorities have introduced new legislation that will apply from 2003 on, including as follows:

- more comprehensive supervision of the cross-border activities of Liechtenstein companies out of the EEA: new article 27a of the insurance supervision law (see Principle 15);
- tighter links with supervisory authorities outside of the field of insurance: new article 61 of the insurance supervisory law (see Principle 16).

90. Recommendations are proposed to improve the present supervisory system and the level of compliance with the IAIS Core Principles. Principles 1 and 13 assessments express concern regarding the staffing of the Insurance Supervisory Authority, which is stretched to carry out on-site inspection on a regular and comprehensive basis. This will prove to be all the more useful as the processing of data and files sent by companies will become more comprehensive and complex (see Principle 12).

91. The regulatory framework should consider the assets authorized for unit-linked policies (especially considering the surrender value issue in Liechtenstein but also in the countries where Liechtenstein products are sold), and, to a larger extent, asset liability management. Inadequacies in asset liability or liquidity risk management on unit-linked products proved to be very significant issues in other countries (for instance Japan or Switzerland for guaranteed interest rates life liabilities, which were matched by inadequate assets in terms of liquidity, yield, safety,... over the last few years). Therefore, the list of assets to be held for unit linked policies should be considered from an insurance and not predominantly financial point of view. Specific regulation should be considered (see Principles 6 and 9). This has already been implemented in several EU countries. Therefore, the ISA might add new rules in this field (see Principles 6, 7, and 9).

92. Additionally, a more sophisticated system to deal with customer claims out of the general consumer protection system, within the companies or through the adequate channel (ombudsman) might be useful to make a satisfactory market conduct system (see principle 11).

93. As mentioned in Principles 10, 13, and 15, the soundness and effectiveness of the supervision is dependent on a satisfactory international cooperation, especially in the field of reinsurance and life insurance where the bulk of the business is made in foreign countries.

Table 5. Recommended Action Plan in Relation to IAIS Core Principles

Reference Principle	Recommended Action
Organization of an Insurance Supervisor (CP 1)	Increase the staff number to supervise insurance companies (CP 1).
Prudential Rules (CPs 6–10)	Adapt the ALM supervision (CP 6).
	Clarify the legal framework for unit linked products and capital redemption operations (CP 6-9).
Market Conduct (CP 11)	A new insurance protection act has been passed but it is not yet implemented. Processes for consumer protection will need to be developed.
Monitoring, Inspection, and Sanctions (CPs 12-14)	Develop systems for receiving reports sent to the ISA (CP 12) Increase in the number of staff devoted to the supervision of insurance companies (CP 1 and 13).
Cross-Border Operations, Supervisory Coordination and Cooperation, and Confidentiality (CPs 15–17)	More cooperation to supervise intermediaries (CP 15).

Authorities' response

94. The government of Liechtenstein acknowledges that there is a lack of resources and is fully committed to do its utmost to grant the essential staff resources to the supervisory authorities.

95. *Prudential rules, monitoring and inspection* The ISA has prepared a new set of reporting templates that companies are required to send to the ISA beginning in 2003. The reporting will enhance the information available to the ISA in the field of asset liability management and solvency analysis. In this context, new systems will be developed to receive and analyze the reported information. The ISA shall develop new rules in the field of the assets authorized for unit-linked products.

96. As mentioned above, the ISA intends for the year 2003 to perform systematically on-site inspections, depending, of course, on available staff.

97. *Cross-Border Operations, Cooperation*—With the transposition of the new EU Directive on Insurance Intermediation, there will be an effective supervision on insurance intermediaries. In this context, the cooperation with foreign authorities to supervise intermediaries will become more intensive.

D. Summary of AML/CFT Assessment

General

98. This section provides summary findings from the assessment of the FATF 40 Recommendations for anti-money laundering and 8 special recommendations for combating the financing of terrorism, and provides recommendations to strengthen observance.¹¹

99. The assessors reviewed the relevant AML/CFT laws and regulations, and supervisory and regulatory systems in place to deter money laundering and financing of terrorism among banking, insurance and securities, as well as for trust and company service providers, (comprised of 344 separately licensed trustees), which are macro-relevant and vulnerable to money laundering. The IAE reviewed the capacity and effectiveness of implementation of criminal law enforcement systems. The assessment is based on the information available at the time it was completed in March 2003.

Main findings

100. **Overall, the AML/CFT legal, institutional, and supervisory framework provides a sound basis for the prevention, detection, and prosecution of offenses of money laundering and the financing of terrorism.** The Liechtenstein authorities have devoted considerable effort to increase compliance with international standards for the FATF 40+8 Recommendations. Major legislative achievements have been the enactment and enhancement of the Law on Professional Due Diligence in Financial Transactions (DDA) and the Law Concerning the Financial Intelligence Unit (FIU Law). The supervisory structure for due diligence has been significantly enhanced by the establishment of the Due Diligence Unit (DDU), which is responsible for ensuring compliance with all due diligence requirements. A fully staffed and functioning, financial intelligence unit (FIU) has been established and been in operation since March 2001.

101. **The Liechtenstein authorities have devoted substantial attention and resources to improving the country's anti-money laundering legal and institutional framework, and effective supervision of due diligence requirements. The strengthening effort comes in response to the FATF's listing of Liechtenstein as a noncooperative country and territory in June 2000.** Both the authorities and financial sector began to improve the quality of anti-money laundering measures to achieve conformity with the FATF 40+8 Recommendations. Following significant strengthening measures, the FATF observed progress in addressing earlier identified deficiencies and, subsequently, removed Liechtenstein from its list of Non-Cooperative Countries or Territories in June 2001 and

¹¹ The assessment was conducted by Ms. P. Moni SenGupta (LEG), Mr. Ronald Ranochak (private consultant), and Boudewijn Verhelst (CTIF-CFI, Belgium), the independent anti-money laundering expert (IAE). Throughout this report, portions of the assessment attributable to the IAE are shown in *italics*.

ceased further monitoring in June 2002. Some implementation measures remain, particularly with respect to enhancing compliance among trustees and insurance concerning monitoring and reporting of suspicious activity.

102. Liechtenstein has been a signatory to the Palermo Convention since 2000, the Convention on Laundering, Search, Seizure and Confiscation (Strasbourg Convention) since 2000 and the International Convention for the Suppression of the Financing of Terrorism (Financing of Terrorism Convention) since 2001. Liechtenstein is not a signatory to the Vienna Convention, but the specific provisions relating to criminalization of money laundering are included in Liechtenstein legislation.

Criminal justice measures and international cooperation

Criminalization of ML and FT

103. **The criminal provisions for ML are sufficient to prosecute offenses discovered since enhancements to primary legislation were adopted amending the criminal provisions on money laundering to liberalize the intent requirement of the offense and to permit prosecution for self-laundering.** As a result, investigations and criminal prosecutions for money laundering are being pursued regularly and without undue evidentiary impediments. In addition to the ML offenses, the DDA provides for criminal penalties for certain willful failures to comply, and the public prosecutor has opened criminal investigations under the DDA criminal provisions. There are some limitations to prosecutions, however, because Liechtenstein law does not permit prosecution for both the predicate offense and money laundering, nor does the ML criminal offense apply to legal entities. Criminal sanctions in the DDU do apply to legal entities, which mitigates to some degree the loophole for legal entities. There is continuing concern that the limitation on offenses applicable to legal entities may not only limit penalties but may also have an inhibiting effect on both confiscation and in the provision of mutual legal assistance.

104. **FT appears to be adequately addressed through application of the offense of participation in criminal organizations, which covers financing of terrorist organizations to a limited extent. Nevertheless, there are pending proposals to enhance the criminal code to have a separate offense for the financing of terrorism.** Currently, the financing of terrorism is prosecuted under Art. 278a of the Penal Code (StGB), which applies to the financing of terrorist acts and criminal organizations, including known terrorist organizations. Further, the government has established a Counter-Terrorism Coordination Task Force, headed by the FIU, and including the DDU, national police, public prosecutor, legal assistance unit, judicial service, personal staff of the government (directly reporting to the prime minister), foreign ministry, and the press office.

Confiscation of proceeds of crime or property used to finance terrorism

105. Liechtenstein has a comprehensive framework for confiscation, freezing and seizing of assets, property, and funds associated with ML and FT. The legal provisions authorize forfeiture upon conviction, siphoning off amounts equal to unjust enrichment, and authorize

civil *in rem* forfeiture, even in the absence of a criminal conviction. Confiscation, freezing, and seizing may be executed on behalf of foreign countries through receipt of a mutual legal assistance request. Liechtenstein forfeiture and confiscation proceedings take into account the rights of bona fide third parties and provide such persons with an opportunity to be heard. The *in rem* procedure allows for confiscation of assets of legal entities, notwithstanding that the Liechtenstein penal provisions for ML do not allow for criminal penalties.

The FIU and processes for receiving, analyzing, and disseminating intelligence: functions and authority

106. A fully staffed and operational FIU has responsibility for the collection, analysis, and dissemination of financial intelligence, and is a key gateway in the information exchange concerning ML and FT with foreign counterpart FIUs. The FIU has the authority to require reporting parties to supplement SARs and has broad powers to obtain relevant information needed to combat money laundering and the financing of terrorism. The FIU may exchange information with counterpart FIUs without violation of banking or professional secrecy. Domestically, the FIU works in close collaboration with the DDU, public prosecutor, Princely Courts to ensure effective detection and prevention of ML and FT. In addition, the FIU has direct and close working relations with the FSA concerning matters that may affect prudential supervision. The FIU may obtain directly financial information from a financial institution that has filed a SAR as needed and has indirect access through the DDU for financial information from other financial institutions needed to analyze SARs. *The FIU would benefit from direct access to financial information in nonfiling financial institutions to enhance its analytical functions.*

Law enforcement and prosecution authorities, powers, and duties

107. **Law enforcement personnel and resources have increased substantially to combat money laundering and the financing of terrorism.** The national police, through a special unit called EWOK, is responsible for investigations of white-collar crime, including money laundering, predicate offenses, and organized crimes. The public prosecutor is primarily responsible for development and prosecution of ML offenses and criminal violation of the DDA and in execution of confiscation orders, both through the domestic criminal process, a separate proceeding for *in rem* confiscation and those that are received from mutual legal assistance requests. The Princely Courts have authority in conducting all the criminal processes, confiscation matters, as well as the execution of mutual legal assistance requests.

108. Investigative, prosecutorial and judicial resources have been substantially enhanced through recruitment and refocusing of these entities. Of great importance in the enhancement of these bodies have been amendments to the Criminal Code to liberalize the intent requirement of the offense of money laundering and the separate penal offenses for willful violations of the DDA that may apply to both natural persons and legal entities. The public prosecutors have focused on using the offenses of ML and FT in developing a number of ongoing matters within Liechtenstein and have opened cases for criminal violations of DDA.

Comprehensive statistics are maintained to aid authorities in assessing the effectiveness of the systems adopted and, as a result, the authorities have been able to tailor investigative, prosecutorial, and judicial practices accordingly.

International cooperation

109. **International Cooperation has been substantially enhanced since the enactment of the Law on International Mutual Assistance in Criminal Matters (MLA Law) and the addition of a number of personnel to handle a previous backlog of requests from foreign countries.** The main conduit for mutual legal assistance is the legal assistance Office of the Ministry of Justice. The MLA Law has truncated the procedures for delivery of mutual legal assistance requests for search, seizure, subpoenas for bank documents, interrogation of witnesses, and extradition. Extradition and transfer of prosecution are widely available. Although there are international agreements on a bilateral basis to permit assistance in some fiscal-related matters, there continues to be a strict interpretation of “fiscal offenses” that appears to limit the scope of assistance provided, including in fiscal fraud such as VAT carousels and in organized fiscal fraud schemes. *In light of Liechtenstein’s vulnerabilities and the risks for reading fiscal offenses as a basis for denying assistance too broadly, the exclusion of serious and organized fiscal fraud schemes, such as VAT-carousels, from mutual legal assistance because of the strict interpretation of the “fiscal offence” concept, should be reviewed.*

Preventive measures for financial institutions

110. **The Due Diligence Act (DDA) provides a comprehensive framework for customer due diligence, internal controls, procedures, monitoring of relationships, suspicious activity reporting, record keeping, and audit.** The DDA imposes strict minimum requirements for customer identification (know-your-customer), establishing beneficial owner, training, designation of compliance, and due diligence officers for all financial intermediaries. Specific provisions for information sharing by the DDU and cooperation among national authorities were enacted to override limitations in banking and professional secrecy with respect to disclosures of AML/CFT intelligence to the DDU, FIU, and foreign competent authorities. The DDA is supplemented by additional specific requirements in the Executive Order Concerning the Law on Professional Due Diligence (DDEO). The DDA contained a transitional provision requiring all financial institutions to update customer identification and beneficial ownership information for existing customers by year-end 2001. As of the date of the assessment, approximately 99 percent of accounts had updated information and the remainder has been blocked.

111. **The DDA applies to a broad range of financial intermediaries, which comprise the most significant financial services.** The provisions of the DDA apply equally to all financial intermediaries, including banks and finance companies, lawyers, trustees, investment undertakings, insurance companies engaged in direct life insurance business, bureaux de change, and the Liechtenstein Post, as well as on a blanket basis, other persons

who accept or keep in custody client assets. The scope of covered persons and entities of the DDA and DDEO is quite extensive and the obligations encompassed by the DDA and DDEO are specified in great detail.

112. **The DDU was created in October 2001, to administer compliance with the DDA and DDEO.** The DDU is fully staffed and resourced to carry out the responsibilities for ensuring compliance with the DDA, and to promote training and awareness in the financial sector of money laundering. The DDA vests complete supervisory authority for preventive measures of financial institutions and intermediaries with respect to money laundering with the DDU. The DDU provides detailed guidance on the necessary scope and depth of due diligence audits, which are quite substantial. However, guidelines should be enhanced; specifically, insurance entities to be alert to the implications of financial flows and transaction patterns of existing policy holders and should be extra vigilant to the particular risks from the practice of buying and selling second-hand endowment policies and single-premium life.

113. **The DDU closely monitors compliance with the DDA through the use of external auditors as well as direct on-site and off-site monitoring itself, as needed.** Although the dualistic system of supervision has been efficient, the authorities recognize that direct supervision is required and are stepping up efforts to conduct direct on-site monitoring. In 2001, the DDU conducted 11 on-site audits for trustees and, in 2002, participated in an extended examination. There is some concern that if a crisis arises and more direct supervision is required by the DDU, the staffing numbers would not support this need. Nevertheless, it is encouraging that the DDU staff continues to develop its expertise through active participation in on-site audits of the entities it supervises with regard to DDA and DDEO compliance.

114. **Financial intermediaries are required to monitor relationships and accounts on an ongoing basis and to monitor transactions for unusual or suspicious activity that indicates that there could be a connection to money laundering, predicate offense or organized crime.** Suspicious activity reports (SARs) must be filed with the FIU and banking secrecy does not pose an impediment to filing. There are both penal and administrative sanctions for failure to file SARs.

115. **The banking sector has apparently embraced the need for effective and thorough customer due diligence, and ongoing monitoring of relationships and transactions.** However, some sectors have not traditionally been subject to a compliance culture. The insurance and trustees sectors may require specialized attention in this regard. There is a need to educate trustees further to focus more on effective know-your-customer policies, and ongoing monitoring of accounts and transactions, rather than on formalistic application of the minimum due diligence requirements and papering the files. Awareness of the vulnerability to money laundering and financing of terrorism in trust companies, trustees, and insurance should be enhanced. The DDU reports that based on 2002 DDA audits that there is less clear evidence of compliance in the insurance sector than in the banking sector.

Overall, the quality of the external audits to date has been adequate and the general level of compliance within the financial sector meeting minimal standards, although with some notable weaknesses in the customer profiles that are available.

Summary assessment against the FATF Recommendations

116. Overall, the AML/CFT legal, institutional, and supervisory framework provides a sound basis for the prevention, detection, and prosecution of offenses of money laundering and the financing of terrorism, and largely fulfills the requirements of the FATF 40+8 Recommendations. Nevertheless, the business climate of Liechtenstein and its vulnerabilities require enhanced measures for effective combating of ML and FT. The efforts to achieve a fully effective system are progressing, but specific improvements warrant closer attention, as detailed below in the recommended action plan.

Table 6. Recommended Action Plan in Relation to the FATF Recommendations

Reference FATF Recommendation	Recommended Action
Forty Recommendations for AML	
General framework of the Recommendations (FATF 1–3)	<i>Fiscal offenses should be read more narrowly to ensure that mutual legal assistance requests that have nonfiscal aspects are not rejected on the basis of fiscal grounds.</i>
Scope of the criminal offense of money laundering (FATF 4–6)	Extend legal liability to legal entities.
Provisional measures and confiscation (FATF 7)	<i>Ensure that limitations on prosecutions of legal entities do not hinder effective confiscation in penal matters.</i>
General role of financial system in combating ML (FATF 8–9)	Implementation by trustees and trust companies requires additional supervisory attention.
Customer identification and record-keeping rules (FATF 10–13)	Implementation by the insurance sector, trustees and trust companies should be enhanced, and specific guidelines for insurance and trustees are needed.
Increased diligence of financial institutions (FATF 14–19)	Abolish the provision on automatic 10-day blocking of assets and accounts when filing SARs and replace with authority of the FIU to order blocking upon receipt of a SAR, and reduce the amount of time for blocking to a shorter time period, with extensions to 10 days. Amend the law to impose a permanent prohibition against tipping off. Provide for a specific administrative sanction for violations of the tipping-off prohibition. Due diligence audits and supervisory audits should be conducted by the same auditor or audit firm and should be conducted together, insofar as possible.
Implementation & role of regulatory and other administrative authorities (FATF 26–29)	Additional monitoring directly by the FSA is warranted regarding the fit-and-proper requirements and impeccable management of trustees and trust companies.

Reference FATF Recommendation	Recommended Action
Administrative Cooperation—Exchange of general information (FATF 30–31)	<i>Attention should be given to the potential limiting effect of Article 7 of the FIU Act on the exchange of financial intelligence with foreign counterparts.</i>
Administrative Cooperation—Exchange of information relating to suspicious transactions (FATF 32)	The FIU should have direct access to financial information from intermediaries needed to analyze SARs and conduct its functions.
Other forms of cooperation – Basis & means of cooperation in confiscation, mutual assistance, and extradition (FATF 33–35)	Ensure that additional multilateral and bilateral agreements needed to ensure coverage are pursued.
Other forms of cooperation—Focus of improved mutual assistance on money laundering issues (FATF 36–40)	<i>Review the position on refusing assistance on fiscal fraud matters, such as VAT carousel.</i>
Eight Special Recommendations on terrorist financing	
I. Ratification and implementation of UN Instruments	Ratification of the UN Convention on the Suppression of the Financing of Terrorism should be completed.
II. Criminalizing the financing of terrorism and associated money laundering	Complete criminalization of a separate offense for financing of terrorism.

Authorities' response

Criminalization of ML and FT

117. The government has approved a draft proposal to parliament to amend the Criminal Code, the Code of Criminal Procedure and the Due Diligence Act—the so-called Counter-Terrorism Package. The focus of this criminal law revision is the establishment of “Terrorist Offenses,” “Financing of Terrorism,” and “Terrorist Groups” as new penal provisions.

118. The criminal offense of “Terrorist Offenses” provides for the imposition of severe sentences for the specific commission of terrorist attacks. The offense of “Financing of Terrorism” punishes persons who gather or provide assets with the intention to fund a crime classified as a terrorist offense. The offense of “Terrorist Groups” criminalizes organized associations of more than two persons established over a prolonged period of time and aimed at the joint commission of terrorist offenses.

119. In accordance with the normal legislative process, the proposed legislative amendments have been circulated for consultation and discussed for the first time by the parliament in June 2003 on the basis of a draft law presented by the government.

120. In addition to the definition of new crimes, the modification and extension of existing definitions of crimes are recommended as follows:

- Taking terrorist associations into account with regard to the confiscation of proceeds of crime and forfeiture (Art. 20 and 20 b StGB);

- extension of domestic jurisdiction according to Art. 64 StGB to terrorist associations and terrorist financing;
- extension of the definition of money laundering (by expanding the list of predicate crimes and through the new Art. 278 d StGB).

121. Furthermore, in the area of substantive criminal law in Art. 320 StGB (“Support of a Party in a Foreign Armed Conflict”), the crime of “Arms Brokering” shall be included.

122. The proposed new penal provisions are intended to close the gaps in criminal legislation covering terrorism and the support of terrorism, and to fulfill the requirements of the UN convention on the financing of terrorism and the relevant UN Security Council resolution.

123. The Liechtenstein Penal Code is modeled on the Austrian Penal Code. The creation of criminal liability of legal entities is currently under discussion in Austria with respect to money laundering. Liechtenstein will observe the discussions and envisages to react accordingly.

Revision of Due Diligence Legislation

124. The due diligence legislation is currently under revision. The recommendations of the IMF team will be considered in this process, which is intended to be finished not later than by the end of 2004.

125. Particular attention will be given to the recommendations regarding increased diligence for financial institutions (FATF 14-19) and administrative cooperation—exchange of information relating to suspicious transaction (FATF 32).

126. Furthermore, the DDU will give additional attention to the implementation of due diligence by trustees, trust companies, and insurances. Therefore, specific provisions for trustees, trust companies, and insurances will be taken into consideration in the context of the planned revision of DDA and DDEO.