

Liechtenstein: Assessment of Financial Sector Supervision and Regulation

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LIECHTENSTEIN

ASSESSMENT OF FINANCIAL SECTOR SUPERVISION AND REGULATION

Prepared by Monetary and Capital Markets Department

Approved by Jaime Caruana

March 21, 2008

This report is based primarily on work undertaken during a visit to Liechtenstein in the period March 21 to April 4, 2007. The assessment team comprised Messrs. Michael Moore (head; MCM), Terence Donovan (team leader, LEG), Paul Ashin, Alain Vedrenne-Lacombe, and Ms. Gabriele Dunker (all LEG), and Mr. Michael Deasy (banking supervision expert), Ms. Tanis MacLaren (securities regulation expert), and Mr. Boudewijn Verhelst (AML/CFT expert). The key findings are as follows:

- The assessment team observed substantial progress in implementing the recommendations from the 2002 assessment following the creation of the independent Financial Markets Authority (FMA) (see Appendix I). A high level of compliance in the focused review of the Basel and IOSCO standards was noted, though some weakness was observed for insurance supervision. Onsite inspections of insurance companies were not conducted as planned and the preparation of industry guidance is delayed, both as a result of resource limitations.
- The authorities and industry continue to make progress to strengthen the anti-money laundering regime. This assessment of compliance with the revised Financial Action Task Force standard, however, identifies a number of further necessary steps to achieve better compliance. The AML/CFT legislation provides a broad framework for customer due diligence (CDD), though it falls short of the international standard on some substantive issues and a range of technical points that should be addressed as Liechtenstein implements the Third ML Directive (2005/60/EC). (See Table 1 of Appendix II for key recommendations.)
- Strategic planning will need to take account of ongoing and increasing resource requirements. The assessment team observed a generally effective capacity to conduct the current level of direct supervision (with the exception of insurance) and to carry out the indirect regulatory and AML/CFT due diligence audit activities. However, the authorities will need to undertake a review of resource requirements in light of future demands on the FMA more generally. Current resources may need to be supplemented to (i) undertake direct onsite inspections in other areas (e.g., AML/CFT due diligence); and (ii) as a result of new demands from the implementation of EU directives, particularly MiFID, Solvency II, and the Third Money Laundering Directive.

Appendix II provides the *Report on the Observance of Standards and Codes (ROSC)* for the FATF standard for Anti-Money Laundering and Combating the Financing of Terrorism.

Michael Moore is the main author of this AFSSR with contributions from the rest of the assessment team.

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

Contents	Page
Acronyms.....	<u>3</u>
Preface.....	<u>4</u>
Executive Summary	<u>5</u>
Priority Policy Recommendations	<u>6</u>
I. Introduction	<u>8</u>
II. Financial System Overview	<u>9</u>
A. Political and Economic Background.....	<u>9</u>
B. Financial Sector and Regulatory Arrangements.....	<u>9</u>
C. Prudential Regulation and Supervision	<u>13</u>
D. Results of the 2002 Assessment.....	<u>14</u>
III. Main Findings and Recommendations.....	<u>15</u>
A. Sectoral and AML/CFT Assessments	<u>15</u>
B. Cross-Sectoral Regulatory and Supervisory Issues.....	<u>19</u>
Tables	
1. Financial System Structure	<u>12</u>
Appendixes	
I. Status of Implementation of the 2002 Recommendations.....	<u>23</u>
II. Report on Observance of Standards and Codes (ROSC)—FATF Recommendations.....	<u>26</u>

ACRONYMS

AML	Anti-money laundering
BCP	Basel Core Principles for Effective Banking Supervision
CESR	Committee of European Securities Regulators
CFT	Combating the financing of terrorism
CDD	Customer Due Diligence
CRD	Capital Requirement Directive (implementation of Basel II)
DDA	Due Diligence Act
DDO	Due Diligence Ordinance
DNFBP	Designated nonfinancial businesses and professions
EC	European Communities
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FIU	Financial intelligence unit
FMA	Financial Markets Authority
FSA	Financial Services Authority
FT	Financing of terrorism
GBOERA	Office of Land and Public Registration
IAIS	International Association of Insurance Supervisors
IOSCO	International Organization of Securities Commissions
LEG	IMF Legal Department
MCM	IMF Monetary and Capital Markets Department
MiFID	Markets in Financial Instruments Directive
ML	Money laundering
MLA	Mutual Legal Assistance
MONEYVAL	Council of Europe Committee of Experts on the Evaluation of Anti-Money Laundering Measures
MOU	Memorandum of Understanding
MVT	Money or Value Transfer Services
NCCT	Non Cooperative Countries and Territories
NPO	Non Profit Organization
OFC	Offshore Financial Center
PEP	Politically Exposed Person
ROSC	Report on Observance of Standards and Codes
SAR	Suspicious activity report
TCSP	Trust and Company Service Provider
UCITS	Undertakings for collective investments in transferable securities (investment funds, mutual funds)
UNSCR	United Nations Security Council Resolution

PREFACE

This report presents the conclusions of the IMF assessment of observance of financial sector supervisory and regulatory standards in the context of the Module 2 offshore financial center (OFC) assessment, which visited Liechtenstein during March 21 to April 4, 2007. The mission reviewed developments in the supervisory and regulatory framework since the last Module 2 OFC assessment mission in 2002.

The mission team held extensive discussions with staff of the Financial Markets Authority (FMA), other representatives of government, and with members of industry and industry associations. Staff of the FMA and the other authorities were very generous in making themselves available for discussions, which were helpful, frank, and forthcoming. The assistance from industry representatives was also very helpful.

The assessment was based on a review of the relevant legislation, questionnaires prepared by the authorities, and publicly available information that was considered in advance of and during the mission. The relevant laws, ordinances, and most other documentation were made available to the mission team in English.

The mission team comprised Messrs. Michael Moore (head; MCM), Terence Donovan (team leader, LEG), Paul Ashin, Alain Vedrenne-Lacombe, and Ms. Gabriele Dunker (all LEG), and Messrs. Michael Deasy (banking supervision expert) and Boudewijn Verhelst (AML/CFT expert), and Ms. Tanis MacLaren (securities regulation expert).

The mission team would like to express its appreciation for the excellent cooperation of all parties consulted and the kind hospitality of the Liechtenstein authorities.

EXECUTIVE SUMMARY

The financial sector in Liechtenstein provides primarily wealth-management services, including banking, trust, other fiduciary services, investment management, and life insurance. The industry is expanding, including in the nonbanking areas, particularly investment undertakings and insurance. The success of the financial services industry reflects in part the not insignificant role of quality supervision and regulation.

The establishment of the Financial Market Authority (FMA) as the unified, independent regulator in January 2005 was a huge step for the financial services industry. This assessment has observed the substantial progress achieved in establishing a modern supervisory and regulatory regime. The FMA's ability to share information with domestic and foreign regulatory authorities works well in practice, and the capacity and willingness to cooperate has been demonstrated in the interactions by the FMA and other authorities with their foreign counterparts.

The FMA and other authorities have been very successful in implementing most of the recommendations provided in the earlier 2002 IMF assessment. The mission team found a high standard of compliance in its focused review of the Basel Core Principles and IOSCO Principles.¹ The IAIS Insurance Core Principles were not assessed; however, there appears to be a capacity constraint at the FMA for insurance supervision in light of the significant growth in the insurance sector. In this regard, and for all areas subject to FMA supervision, the authorities will need to consider the demands on the FMA to ensure that it is able to sustain quality supervision. This assessment recommends that there be an increased capacity by the FMA to conduct onsite inspections of regulated firms. The development of this increased capacity, along with the demands to implement the EU requirements will mean that resources will need to be kept under review to ensure sufficiency, and augmented as necessary.

The authorities and the industry continue to make significant efforts to strengthen the anti-money laundering regime, though there is still work ahead. There have been substantial improvements since 2002, particularly in ensuring that there is a high awareness by the financial services industry to prevent misuse of the financial system. The IMF's earlier assessment recognized the progress that had been made as measured against the earlier Financial Action Task Force (FATF) anti-money laundering standard. This assessment of compliance, which is against the now more rigorous FATF standard, identifies a number of further necessary steps to achieve a higher level of compliance (see item 5 of the Priority Policy Recommendations).

¹ Under current policies, partial assessments of financial sector standards (e.g., BCP and IOSCO) do not result in issuance of a formal Report of Observance of Standards and Codes.

PRIORITY POLICY RECOMMENDATIONS

1. Financial Markets Authority

- Follow through with the strategic plan to consider future resource requirements for on-site supervision and the future demands from implementation of EU Directives.
- A formal process should be agreed to ensure that a suitable alternative Board member can act in the event of an extended absence by any Board member.

2. Banking (Basel Core Principles)

- Review resources to ensure that they remain sufficient in light of the developing nature of banking supervision and increasing EU requirements, particularly the Capital Requirement Directive (CRD) and Markets in Financial Instruments Directive (MiFID).
- Amend guidance to external auditors to include specific requirements for the Capital Requirement Directive (i.e., Basel II).

3. Securities (IOSCO Principles)

- Priority should be given to the development of appropriate guidance for auditors in performing the regulatory audits of asset managers.
- Principles for Market Intermediaries:
 - Provide the names of authorized personnel on the website listing of authorized firms.
 - Introduce an affirmative obligation on the part of an asset manager to give prompt notice to the FMA, if it becomes undercapitalized.
 - Implement fully all parts of the Asset Management Act; in particular, the Code of Conduct should be finalized.
 - Ensure that compliance with the MiFID investor protection requirements is reviewed during the regulatory audit performed on both asset managers and banks.
- Pursue membership in the Committee of European Securities Regulators (CESR) in line with EEA status. This would be as a measure to strengthen international cooperation arrangements for cross-border securities activities.

4. Insurance (IAIS Core Principles)

- Undertake inspections of insurers in line with expectations for *direct* supervision.
- Review capacity for the insurance supervision function with a view to ensuring that resources are sufficient to conduct onsite inspections and implement EU directives.
- Review reporting requirements, with a view to increasing the frequency of prudential reporting requirements to permit interim offsite analysis of the condition of firms.
- Expand the coverage of regulatory audits to include the assessment of risk-management systems.