

# **METHODOLOGY FOR ASSESSING COMPLIANCE**

## **WITH THE GIFCS STANDARD ON THE REGULATION OF TCSPs**

### **Background to the Standard**

The Group of International Finance Centre Supervisors (GIFCS – see [www.gifcs.net](http://www.gifcs.net)) is a group of supervisors from smaller nations which amongst its purposes has a mission to promulgate and encourage effective compliance amongst its members with relevant international standards of supervision.

A number of GIFCS members are active in the trust and company service provider (TCSP) sector. This activity, which typically attracts a large number of international clients, can give rise to significant risks if not properly regulated. The risks arise from how legal vehicles are administered and used, the fact that such business relationships are often ‘introduced’ and therefore not established face-to-face, and how the FATF’s anti-money laundering and countering the financing of terrorism (AML/CFT) requirements are being applied. The latter includes the requirement to know who ultimately beneficially owns or lies behind all legal vehicles established, incorporated or administered on behalf of clients.

Recognising these risks, and the fact that there was no formal standard covering TCSP oversight for regulators to follow, the GIFCS published a formal standard on regulation of the sector in October 2014 (see <https://www.gifcs.net/images/GIFCSStandardonTCSPs.pdf>).

The Standard addresses all the wider prudential areas normally expected from a regime applying to a regulated activity, not just AML/CFT. These include licensing, corporate governance, controllership, prudential and conduct issues, as well as co-operation with other regulators.

All GIFCS member jurisdictions undertaking material TCSP activity have undertaken to achieve at least a largely compliant position with the TCSP Standard within three years (ie by end April 2019). Members have prepared their own internal action plans for meeting this goal. Members have also resolved that in order for implementation of the Standard, and observance of it by GIFCS members, to be effective and credible, a system of assessment of compliance needs to be put in place.

This document provides a methodology to be used in carrying out assessments. It will be further informed and expanded as experience with conducting assessments is accumulated.

### **Objectives of the Standard**

The Standard is based on the following objectives:

- clients of TCSPs should receive a degree of protection equivalent to that afforded to clients of other financial institutions, in terms of the licensing and supervision of persons undertaking such business.
- TCSPs should be subject to a similar regulatory regime as other financial institutions.
- to be effective, standards should be applied internationally.

Part 2 of the Standard lays out the five key overarching principles that apply to Regulators, the regulatory system and jurisdictions as a whole in relation to the regulation and supervision of TCSPs. These five principles speak to an integrated environment where a comprehensive legislative framework, risk based supervisory practices, cooperation arrangements and robust enforcement measures promote a sound regulatory/supervisory system for TCSPs to operate in. In addition to the

principles applying to the Regulator, Part 2 of the Standard lists general principles that jurisdictions should implement to create an effective regulatory environment for TCSPs and their Clients.

Part 3 of the Standard governs the oversight of the operations of licensed TCSPs by the Regulator. This Part is composed of ten standards divided into sub-standards on topics that include licensing, controllers and key persons, conduct and corporate governance, and financial crime and international standards. The standards and sub-standards constitute the minimum elements that should be present in a regulatory framework for TCSPs in order for such framework to meet the objectives of TCSP regulation set out above.

### **Initial assessments of compliance**

To date one formal assessment of compliance with the Standard has been undertaken, and all members have commenced a process of self-assessment. It is recognised that some jurisdictions do not undertake material TCSP activity and therefore currently do not envisage implementing such a regime; in other jurisdictions measures are still evolving.

A number of jurisdictions have put themselves forward for assessment. The assessment process is therefore already being well supported on a voluntary basis. However the objective is to cover all GIFCS members undertaking TCSP activity within an agreed timeframe, with the more active jurisdictions being assessed first.

The assessments will be undertaken by small peer groups of members acting as individual review committees. Initially the Chairman or Deputy Chairman of GIFCS will oversee each review committee to ensure consistency.

The scope of the assessment will include the relevant laws and all regulatory measures of the assessed jurisdiction but the assessors are not required to form an opinion on the product laws of that jurisdiction.

### **Preconditions for effective regulation of TCSPs**

As with any regulatory regime, for it to be effective there must be a robust and supporting framework in place to ensure that the regime can be effectively applied. Many of these preconditions are included in the Standard. However they in particular cover:

- An independent and authoritative regulator which is itself subject to credible corporate governance disciplines and is free to operate without fear of political interference
- A comprehensive framework of legislation
- A regulator with adequate powers, and a legal and enforceability framework which allows those powers to be effectively used
- Sufficient resources to carry out a risk-based approach of oversight for the TCSP sector
- An established relationship of dialogue with the licensed sector to be able to communicate to and work with the TCSP industry fostering a culture of compliance.

It is expected that jurisdictions should have in place an ongoing process of self-assessment against the GIFCS Standard, so that compliance can be monitored internally and that action to cover any shortfalls can become embedded as a continuous exercise.

### **Criteria for assessing compliance with the Standard**

The Standard sets down specific requirements and expectations for regulators to adopt and follow in the following areas.

- Licensing
- Corporate governance
- Controllers of TCSPs
- Individuals
- Control over vehicles
- Conduct
- Prudential
- Administration
- Financial crime and international sanctions
- Co-operation

Assessments will be undertaken using a two-stage process.

The first stage will involve the completion of a technical compliance questionnaire by the jurisdiction being assessed, as well as provision of information to demonstrate effectiveness of compliance. A template has been created to assist in this process. This will facilitate the collection of information for an initial, desk-based analysis by the Review Committee of compliance under the individual criteria. A conference call to clarify and discuss any matters arising from the responses will be held. Previous assessments by international bodies will also be consulted for background information.

The second stage will be an onsite visit by the Review Committee (or members thereof) for discussion of the questionnaire response, to clarify areas of doubt and to verify on the ground the information which has been provided.

The purpose of the assessment, also embracing discussion with the jurisdiction, will be to arrive at an objective understanding of compliance with the individual standards. As far as possible the assessment will cover both technical compliance and effective implementation. A matrix approach will assist this work. The findings for each paragraph of the Standard will be rated according to the following headings.

1. In place and being effectively applied through legislation and/or other enforceable arrangements
2. In place and largely being applied, but possibly lacking full enforceability
3. Effective measures planned with political support, with introduction and implementation in demonstrable progress
4. Requirements not planned, or not in progress as per 3 above.

A jurisdiction will be able to establish compliance by demonstrating an equivalent outcome where the letter of the Standard is not met ("comply or explain"). A regulatory measure will be considered enforceable if a sanction can be applied for non-compliance.

Guidance on measuring effectiveness in the context of the Standard was issued by GIFCS in August 2017 (<https://www.gifcs.net/images/TCSPseffectiveness.pdf>).

The Principles for Regulation will fall within scope of the assessment, but will not be rated. However any deficiencies will be mentioned in the report.

Based on the paragraph ratings, assessors will then use their judgement to rate each section of the Standard using the following headings:

- Compliant ("C" – no shortcomings)

Largely Compliant (“LC” – only minor shortcomings)

Partly Compliant (“PC” – moderate shortcomings)

Non-Compliant (“NC” – major shortcomings)

A rating of “Compliant” will only be achieved where there are no shortcomings identified within a section.

A draft assessment report will be prepared within three months from the onsite visit initially for discussion with the jurisdiction concerned. The report will include the section ratings but not each individual paragraph rating.

For each assessed requirement or set of requirements there will be:

- a) A finding, in terms of an assessing comment/explanation of understanding as set out above
- b) The jurisdiction’s response to the finding
- c) An action plan setting out what follow-up measures are planned, and the timetable for their introduction and implementation.

The focus throughout will be to arrive at a judgement, based on clear evidence, of how effectively are the requirements being applied.

Whilst post-assessment actions will be considered by the assessors and included in the report where appropriate, the cut-off point for the purposes of deciding on the ratings will be the date of the on-site visit.

An agreed final draft of the report will be completed within six months from the onsite visit. In the event of there being any matters where agreement of the jurisdiction and its assessors cannot be reached, the final draft will show any dissenting comments of the jurisdiction by separate annotation.

At this stage the final draft of the report will undergo a peer review by a small number of jurisdictions nominated by the Chairman.

The final draft with any comments from the assessed jurisdiction and the peer reviewers would subsequently be reviewed by the full Plenary which would have the opportunity to question both the assessed jurisdictions as well as the assessors. A final report would then be prepared.

With the agreement of the assessed jurisdiction it would be intended to publish a report of the assessment on the GIFCS website.

Actions arising from the assessment will be reviewed at plenary meetings to monitor progress.

## **The way forward**

This methodology and addendum are intended to set down a consistent basis for conducting evaluations of members’ regulatory regimes. The methodology will evolve in the light of ongoing experience, especially in the area of effectiveness of implementation of the Standard.

## **Group of International Finance Centre Supervisors**

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