“Increasing the burden or spreading the load”
Is it time to create an international regulatory standard setter for trust and company service providers?

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As the annual Offshore Investment company formation survey shows, the company service sector remains highly significant in many small international finance centres. Similarly the trust industry continues to thrive. However, unlike banking, insurance and investments there is not, as yet, a formal organisation representing those engaged in the supervision of trust and company service providers (TCSPs). An informal working group comprising some of them does exist and an adhoc sub group of the Offshore Group of Banking Supervisors was established to create a Best Practice paper for these activities.

Yet this area is regulated in many of these smaller centres. TCSPs have come under significant attention, by bodies such as the OECD and FATF (through their revised 40+9 principles). The EU’s Third Money laundering Directive which comes into force in December, makes the supervision of TCSP’s a requirement.

So why does this gap exist and why, when a number of regulators consider that the lack of such a formal international standard setting organisation may result in an inconsistent approach to regulation and supervision, is nothing apparently being done?

Historically the so called “onshore” centres have portrayed abuse of company and trust vehicles as an exclusively “offshore” problem. Through this device they have been able to pressurise the offshore centres to regulate and supervise, whilst avoiding the issue in their own jurisdictions. Thus bearer shares have been immobilised in a number of offshore locations but remain freely available in many onshore ones. Anti money laundering provisions expressly applied offshore have remained patchy onshore.

If the proponents of this divide are correct then there is no need for a global standard setter, such as the International Organisation of Securities Commissions (IOSCO) or International Association of Insurance Supervisors (IAIS). Any standards should be applied, selectively where the problem lies, with TCSP’s in uncontaminated areas being allowed to continue unmolested by regulatory bureaucracy. But are onshore and offshore so different?
In April 2006 the US Government Accountability Office produced a Report for the U.S. Senate “Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs”. Entitled, “Company Formations- Minimal Ownership Information Is Collected and Available” it stated:

“Most states do not require ownership information at the time a company is formed, and while most states require corporations and limited liability companies (LLC) to file annual or biennial reports, few states require ownership information on these reports.

With respect to the formation of LLCs, four states require some information on members, who are owners of the LLC. Some states require companies to list the names and addresses of directors, officers or managers on filings, but these persons may not own the company. Nearly all states screen company filings for statutorily required information, but none verify the identities of company officials.

Third-party agents may submit formation documents to the state on a company’s behalf, usually collecting only billing and statutorily required information for formations. These agents generally do not collect any information on owners of the companies they represent, and instances where agents told us they verified some information were rare.

Federal law enforcement officials are concerned that criminals are increasingly using U.S. shell companies to conceal their identity and illicit activities.”

This looks surprisingly similar to accusations occasionally levelled at “offshore” centres. Whilst many onshore commentators remain in a state of wilful denial, the evidence from the GAO and others provides ample evidence that the problem is a global.

So does a global issue require a unified response or is the current patchwork of standards fit for purpose?

In their paper the GAO concluded that;

“All requirement would need to uniformly apply to all states and/or agents, because if it were not, those wanting to set up shell companies for illicit activities would simply move to the jurisdiction that presented the fewest obstacles.”

Clearly if they are right about uniformity between states this is equally applicable to uniformity between countries. GAO have set out the issues relating to even simple gathering of ownership information and the competitive effects of a lack of level playing fields between centres. These include:

- Increased time, cost and workload for company registries and agents
- Derailment of business dealings
- Lost revenue
- Lost business for agents
- Changes could require jurisdictions to pass new legislation
• Tension with privacy rights

The prevention of this market distortion can only be achieved through the establishment of minimum global standards. If so, the next issue is whether an existing standard setter could be tasked to do undertake the role.

The FATF have established standards in so far as AML/CFT is concerned, but they are not a regulatory standard setter along the lines of IOSCO or IAIS. Nor is their membership open which raises questions of accountability and representation.

As stated previously, the Offshore Group of Banking Supervisors did establish an adhoc working group which, in 2002, produced a best practice paper on the supervision and regulation of TCSP’s. Regretfully, even though four G7 countries (France, Italy, Netherlands and United Kingdom) and three international organisations (FATF, IMF and OECD) were represented on the group, and significant efforts by OGBS, little progress was made to turn these into a global framework other..

Other standard setters have shown a resistance to become involved in this area. Indeed the national regulators who participate in these bodies are often not responsible for TCSPs. For instance in the UK, responsibility for supervision falls to the HM Revenue and Customs, not the FSA.

The OECD has investigated the issue but is not a standard setter in the regulatory sense.

If there is to be a set of reasonable but globally applied standards there has to be a forum from which to launch them. This would require the creation of a wholly new body, specifically focused on the regulation and supervision of TCSP’s. Being separate from existing bodies it would be able to attract its own membership amongst interested parties.

As a new body it would lack any offshore baggage (which groups such as OGBS could be considered as subject to) or having potential conflicts of interest (such as the OECD and its focus on tax rather than regulation per se) but could position itself as an independent international regulatory standard setter for this activity.

Whilst a significant element of its membership would come from offshore, it would not be an “offshore” standard setter. This would prove attractive to those seeking to level the playing fields. Recent moves in the USA show the need to be proactive in this area.

The proposed Levin-Coleman-Obama “Stop Tax Haven Abuse Act” in the USA and its initial list of 34 “offshore secrecy jurisdictions”, which includes some EU member states and four FATF members, demonstrates that the failure to establish and monitor common standards on a global basis will allow misunderstanding, unfair competition and bigotry to flourish.

Some of those who currently regulate may find the initial standards lower than they would wish, and, as a result may find pressure to reduce rather than increase their
standards. This is not ideal for them, but a global standard is clearly a worthwhile goal and a goal whose time has come.