CFL1

Administration of Offshore Centres

5 OCTOBER 2004

1. Time allowed	:	Three (3) hours
2. Total number of questions	:	Five (5) questions
3. Number of questions to be answered	:	All five (5) questions [20 marks each]

4. Begin each answer to a new question on a fresh page.
5. Answer **all** questions in **English**.

ANSWER ALL FIVE (5) QUESTIONS

1. (a) Define “offshore financial centre”. [2]

   (b) List **five** advantages an offshore financial centre offers for business operations and transactions. [10]

   (c) State **four** primary objectives of the Government in setting up Labuan as an International Offshore Financial Centre. [8]
   (Total:20 marks)

2. (a) State the tax rate for an offshore company carrying on offshore trading activities. [2]

   (b) What is “offshore banking business” as defined in the Offshore Banking Act 1990 and the Offshore Banking (Amendment) Act 2000? [8]

   (c) Define “offshore leasing”. [5]

   (d) Define the term “resident” under the Offshore Insurance Act 1990. [5]
   (Total:20 marks)

3. (a) State **five** licensing requirements for a Labuan offshore money broker. [10]

   (b) List **five** advantages of the Labuan International Financial Exchange. [10]
   (Total:20 marks)

4. (a) Describe **four** criteria required by Bank Negara Malaysia in approving foreign currency credit facilities (exceeding the equivalent of RM5million) to residents. [10]

   (b) Explain the following:

      (i) Transferable loan certificates [5]

      (ii) Floating rate notes [5]
   (Total:20 marks)

5. (a) Define “money laundering”. [2]

   (b) Identify and describe **three** stages of money laundering. [6]

   (c) Briefly explain “know your customer policy” in the context of banks complying with the safeguards against money laundering. [6]

   (d) State **six** examples of suspicious transactions under money laundering activities. [6]
   (Total:20 marks)

- END OF QUESTION PAPER -

OUTLINE ANSWERS

The comments given in the boxes below indicate the areas of weaknesses the examiners have identified and their advice to future candidates.

Questions 1

- Candidates were unable to state the advantages of the offshore financial centre.

1. (a) An offshore financial centre is defined as a geographical location where non residents conduct business due to the jurisdiction being free from the restrictions of domestic reserve requirements and monetary controls as well as offering low tax rates for businesses.

(b) Advantages of offshore centres.

(Choose any five of the following advantages:)

- Relatively lower tax rates than other countries.
- May impose no tax on income earned by foreign individuals.
- Strict laws of secrecy for banking and commercial transactions.
- No currency exchange controls for non-residents.
- Professional advisers.
- Less complex and less regulated jurisdictions that are flexible, self-reliant and self-sufficient.
- Efficient transportation facilities which facilitate internal and external travel.
- Good network of communications supported by technological development.

(c) The four primary objectives are to:

- complement the onshore financial system centred in Kuala Lumpur.
- strengthen the contribution of the financial sector towards the Gross National Product of Malaysia.
- enhance the attractiveness of Malaysia as an investment centre.
- promote the economic development of Labuan and its vicinity.

Question 2

- Candidates were unable to state the tax rate for an offshore company carrying on offshore trading activities.
- Candidates could not define most of the terms required in the question.

2. (a) 3% of net profits from audited accounts or a fixed sum of RM20,000 upon election by the offshore company.

(b) Offshore banking business is the business of:

- receiving deposits on current accounts, deposit accounts, savings accounts or any other accounts as may be specified by the Labuan Offshore Financial Services Authority (LOFSA) and providing credit facilities,
- offshore investment banking business,
- Islamic banking business, subject to such terms and conditions as LOFSA may specify,
- building credit business, credit token business, development finance business, leasing business or factoring business, and
- any such other business as LOFSA with the approval of the Minister, may specify in any currency other than Malaysian currency.

(c) Offshore leasing means the business of letting or sub-letting movable and non-movable properties on hire for the use of such property by the hirer or any other person where the lessor is the owner of the property or such other business as approved by the Minister of Finance.

(d) Resident means any person who is:

- a citizen of Malaysia who is residing in Malaysia;
- the holder of an entry permit under the Immigration Act 1959/63 who is lawfully residing in Malaysia; or
- a corporation established under the laws of Malaysia, other than the Offshore Companies Act 1990 (OCA), or established as a foreign company under the Companies Act 1965.

Question 3

- Candidates were unable to state the licensing requirements.
- Candidates could not state the advantages of the Labuan International Financial Exchange.

3. (a) Licensing requirements for a Labuan Offshore Money Broker.

(Give any five of the following requirements:)

- Must have minimum paid-up capital of RM300,000 (unimpaired by losses) or its equivalent in any foreign currency.
- The applicant must produce an undertaking letter from the head office/parent company to undertake any liability arising from the operations of its branch or subsidiary in Labuan.

- The applicant must obtain prior approval from the Labuan Offshore Financial Services Authority for the appointment of its controller or director or chief executive officer who must be fit and proper person.

- The applicant is to submit a business plan for the first three consecutive years of operations.

- The applicant is to submit, where applicable, audited annual accounts for the three years immediately preceding the application.

- The applicant must maintain a registered office in Labuan and all dealings must be done through that office.

(b) Advantages of the Labuan International Financial Exchange (LFX) are as follows:

- Simplicity in operations and minimal bureaucracy for efficiency and effectiveness.

- Labuan shares same time zone with other Asian financial centres such as Hong Kong, Kuala Lumpur, Seoul, Singapore, Taipeh and Tokyo.

- The rules of the LFX are flexible in order to cater to the listing of a multitude of financial instruments.
- Promotes the extensive usage of multimedia and internet facilities allowing accessibility through international network communication systems.

- No capital gains tax, no contract note duties, no exit levies and minimal corporate tax.

Question 4

- Candidates were unable to explain the transferable loan certificates and floating rate notes.

- Candidates should give answers based on the question's requirements.

4. (a) Criteria for approval are as follows:

- Productive purposes which generate foreign exchange earnings for Malaysia.

- Productive purposes which save outflow of foreign exchange from Malaysia through the production of import substitution goods.

- Large infrastructure projects. Priority given to telecommunications and high technologys projects such as biotechnology and medicine.

- Working capital should ideally be sourced locally in the form of Ringgit facilities.

(b) (i) Transferable Loan Certificates are funding instrument commonly used in international financing. It is a form of direct lending structured as a revolving credit or a term loan and can either be a bilateral (one-to-one) or syndicated facility (more than one lender).

(ii) Floating Rate Notes are generally long term (3–5 years) public offerings of debt securities which may be unsecured notes paying interest rates varying with yield from time to time on selected money market indicators and may be issued in any major currency for a minimum amount of USD100,000 per note.

Question 5

- No comments were provided for this question.

5. (a) Money laundering is an activity intended to change the identity of illegally obtained money into what appears to be a legitimate source.

(b) Three stages of money laundering:

1. Placement: The physical disposal of cash from illegal sources.

2. Layering: A series of complex financial transactions designed to disguise the audit trail so as to provide anonymity for the funds' source.

3. Integration: The final stage in which illegitimate funds becomes legitimate.

(c) It is a policy that requires staff of financial institutions to request for proper identification from customers at the time a relationship is established to prevent fictitious accounts from being opened.

Identification can be in the form of the customer's passport, driver's licence, identity card or even a proper introduction from an existing customer of the financial institution.

(d) Examples of suspicious transactions under money laundering activities.

(Give any six of the following examples:)

- Unusually large cash deposits by an individual or a company whose business is not reflective of large cash takings.

- Unexplained electronic fund transfers by customers without passing through an account.

- Substantial amount of funds from countries which are noted for production, processing and marketing of drugs or terrorist organisations.

- Request to borrow against assets of third parties where the origin of assets are not known or where the assets' value is inconsistent with the borrower's standing.

- Substantial increases in cash deposits of money to or from overseas locations with instructions to pay in cash.

- Customers seeking to exchange large quantities of low denomination notes for larger denominations.

- Customers refusing to furnish information.