

**CFL1**

# **Administration of Offshore Centres**

**4 APRIL 2006**

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 of establishing business operations in offshore centres. [10]  
(c) Describe **four** functions of the Labuan Offshore Financial Services Authority. [8]  
(Total:20 marks)
2. (a) State **five** business restrictions which are imposed on Labuan offshore companies. [10]  
(b) List **five** conditions a potential applicant must fulfil to obtain a Labuan International Offshore Financial Centre offshore banking licence. [10]  
(Total:20 marks)
3. (a) State **five** eligibility requirements to obtain an offshore fund management licence. [10]  
(b) List **five** advantages of listing and trading financial products in the Labuan International Financial Exchange. [10]  
(Total:20 marks)
4. (a) State **four** criteria required by Bank Negara Malaysia in approving foreign currency credit facilities (exceeding the equivalent of RM5million) to residents. [8]  
(b) Briefly describe the following types of financial products:  
(i) Floating rate notes [4]  
(ii) Transferable loan certificates [4]  
(iii) Standby letters of credit [4]  
(Total:20 marks)
5. (a) Define “money laundering”. [3]  
(b) Briefly describe “suspicious transactions” under money laundering activities. [7]  
(c) Define “tax avoidance”. [5]  
(d) What is “tax evasion”? [5]  
(Total:20 marks)

- END OF QUESTION PAPER -

## **OUTLINE ANSWERS**

### **Question 1 – 5**

- There are no examiner's comments for the following questions as the only candidate who registered for this subject passed the paper in the April 2006 examination sitting.

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 low tax rates for businesses.
- (b) Give any five of the following advantages of establishing business operations in offshore centres.
  - Low tax rates
  - Strict laws of secrecy
  - No currency exchange controls for non-residents in foreign currencies transactions
  - Lower costs of conducting business in the offshore centres
  - Availability of professional advisers
  - Efficient transport facilities to facilitate both internal and international travel
  - Good communications and network facilities in line with technology development
- (c) Give any four of the following functions of the Labuan Offshore Financial Services Authority
  - To administer, enforce, review and give effect to the provisions stated in the Labuan Offshore Acts and any other law relating to offshore financial services in Labuan.
  - To ensure offshore financial transactions are conducted according to the laws provided and in line with established norms of good and honourable conduct as well as to preserve and maintain the good repute of the Labuan International Offshore Financial Centre (IOFC).
  - To carry out research and commission studies on offshore financial services in Labuan.
  - To recommend the creation and improvement of any facility to enhance Labuan's attraction as an IOFC.
  - To foster high standards and promote offshore financial services in Labuan by co-operating and working with offshore financial institutions, professional and industry associations.
  - To advise the Minister of Finance generally on matters relating to offshore financial services in Labuan.
  - To license or register persons/companies carrying on offshore financial services in Labuan.
  - To regulate and supervise the conduct of offshore financial services in Labuan.

## Question 2

2. (a) Give any five of the following:

- Banking business unless permitted under the Offshore Banking Act 1990.
- Insurance or reinsurance business unless permitted under the Offshore Insurance Act 1990.
- Business with a resident of Malaysia except as permitted by the Labuan offshore legislation or the Labuan Offshore Financial Services Authority (LOFSA).
- Transacting in the Malaysian currency except for defraying administrative and statutory expenses as permitted under the Labuan offshore legislation.
- Shipping operations in Malaysia
- A resident investing in an offshore company may not use the offshore company to invest in a domestic company.

(b) Give any five of the following:

- The potential applicant must be an offshore company established or a foreign offshore company registered for the sole and exclusive purpose of carrying on offshore banking business/offshore investment banking business in the Federal Territory of Labuan or it is a Malaysian bank.
- Must be a well-established bank of international standing and meets capital requirements:
  - International bank – capital / shareholders' funds of USD1billion
  - Regional and domestic bank – capital / shareholders' funds of USD500million
- Setting up a subsidiary requires capital funds, unimpaired by losses, of at least RM10million or its equivalent in other currency  
Setting up a branch requires the head office to maintain capital funds of not less than the equivalent of at least RM10million.
- Furnish LOFSA with a letter of awareness from the home supervisory / regulator which effectively supervises the applicant.
- Furnish a guarantee or an undertaking or both to LOFSA as an assurance that the offshore bank will be able to meet all its liabilities arising from the business in Labuan.
- Has a good credit rating by established rating agencies e.g. Moody's Investors Services Incorporated, Standard and Poor's Corporation, IBCA Limited.

### Question 3

3. (a) Five eligibility requirements for an offshore fund management licence.
- The application may be made by a company incorporated or registered under the Offshore Companies Act 1990, while the registration may be made by a fund management company licensed or qualified in any recognised country or jurisdiction.
  - The applicant's paid-up capital shall be at least an amount equivalent to RM2million in any other currency.
  - The applicant's parent company or holding or related company must have a sound track record in fund management activities and must submit its annual reports and Memorandum and Articles of Associations and a 2-year business plan.
  - Every director and secretary of the applicant must be a "fit and proper" person allowed to own and operate the fund management company and approved by the Labuan Offshore Financial Services Authority.
  - There must be no adverse report on the company's directors and senior management from the relevant home authority.
- (b) Advantages of the Labuan International Financial Exchange (LFX):
- Operations are kept simple with minimal bureaucracy for efficiency and effectiveness.
  - Labuan shares almost the same time zone with other Asian financial centres such as Hong Kong, Singapore, Seoul, Taipei and Tokyo.
  - The LFX's rules are flexible in order to cater to the listing of a multitude of financial instruments.
  - The LFX promotes extensive usage of multimedia and internet facilities allowing accessibility through international network and communication systems.
  - No capital gains tax, no contract note duties, no exit levies and minimal corporate tax.

### Question 4

4. (a) Four criteria required by Bank Negara Malaysia:
- 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.
  - Working capital preferably should be sourced locally in the form of Ringgit facilities.

(b) Floating rate notes

Public Offerings of debt securities with tenors between 3-5 years. Can be unsecured notes paying interest at rates varying with the yield from time to time on selected money market indicators. Can be issued in any major currency and their yield is quoted as a discount margin against a benchmark rate such as the London Interbank Offered Rate. Usually issued in tranches of at least USD100,000 per note.

Transferable loan certificates

A funding instrument used in international financing. Represents a form of direct lending which can be structured as a revolving credit or a term loan in transferable form which allows the lender the right to transfer all or part of its commitment under a credit facility to another financial institution without the consent of the borrower. The borrower is not allowed to assign liability to another party without the lender's written consent.

Standby letters of credit

A financial instrument for Malaysian companies to source funding from Labuan offshore banks. It is used to guarantee financial payments to the domestic financial institutions in consideration of them providing Ringgit loans to borrowers. Standby letters of credit issued by Labuan offshore banks can be denominated in Ringgit Malaysia or any of the major foreign currencies.

<b>Question 5</b>
-------------------

5. (a) Money laundering is an activity which intends to change the sources of illegally obtained money into what appear to be legitimate sources.
- (b) Suspicious transactions
- Large cash deposits by an individual or a company whose business is not reflective of large cash takings.
  - Substantial increases in cash deposits by individuals or companies without any apparent reason.
  - Customers transferring large sums of money to and fro overseas locations with instructions to make payments in cash.
  - Customers seeking to exchange large quantities of low denomination notes for large ones.
  - 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 are inconsistent with the borrower's standing.
- (c) Tax avoidance is an exercise involving the structuring of a transaction within the legal framework of the law to minimise present or future tax liabilities. It is not illegal to undertake this form of tax planning strategy.
- (d) Tax evasion is an exercise to avoid tax obligation through illegal means. It is an unlawful act to intentionally avoid paying any taxes to the Inland Revenue Department.