

A NEW REGULATORY FRAMEWORK

FOR THE

FINANCIAL SERVICES SECTOR

IN MAURITIUS

*26 February 2001*

*Ministry of Economic Development, Financial Services and Corporate Affairs*

## FOREWORD BY THE MINISTER

It gives me great pleasure to release the Report of the Steering Committee that was set up by Government to advise on a new regulatory framework for the financial services sector in Mauritius. Government has agreed to the implementation of the recommendations of the Report and has indicated its full support to the achievement of the proposals contained therein.

After more than a decade of sustained expansion in the less traditional areas of financial services, it was time to decisively address the issue of proper regulatory oversight of the diverse financial activities being undertaken within and from Mauritius. We cannot aspire to make further headway in the provision of specialised financial services unless we co-ordinate effectively and efficiently the activities of the present regulatory bodies and ensure that there are no gaps in the monitoring and supervision of financial intermediaries and service providers. Our credibility as an international financial centre of repute and excellence would be jeopardised without a firm commitment on the part of the authorities to provide a coherent policy structure and a sound regulatory and supervisory environment.

In response to these exigencies, the Steering Committee has presented a clear, far-sighted, but practical, vision that will allow us to chart the future of the financial services industry with renewed vigour and optimism. I sincerely thank the Chairman and Members of the Committee for their contribution and dedication to the task entrusted to them.

Government will ensure that the proposals and recommendations of this Report become effective through the necessary legislative, institutional and administrative measures, in concert with practitioners and other stakeholders of the financial sector.

***Sushil K. C. Khushiram***

*Minister of Economic Development,  
Financial Services and Corporate Affairs*

*26 February 2001*

**REPORT OF THE STEERING COMMITTEE**

**ON THE**

**ESTABLISHMENT OF A**

**NEW REGULATORY FRAMEWORK**

**FOR THE FINANCIAL SERVICES SECTOR**

**IN MAURITIUS**

*5 February 2001*

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## FOREWORD

*A Steering Committee was set up by the Government in October 2000 to consider the establishment of a Financial Services Authority with the following terms of reference:*

- i. To advise Government on the scope, powers, structure and governance of the Financial Services Authority;*
- ii. To provide a clear proposal for a draft FSA Bill to be submitted for Government's approval within a period of three months; and*
- iii. To make appropriate recommendations and to assist in the process of implementation within a targeted period of one year.*

*The members of the Steering Committee are as follows:*

*Dev MANRAJ (Chairman)*

*Gilbert GNANY*

*B.R. GUJADHUR (Co-opted)*

*Uday GUJADHUR*

*Yvan LEGRIS*

*M. OOZEER (Co-opted)*

*Ashok PRAYAG*

*Iqbal RAJAHBALEE*

*(Co-opted with Muhammad. R.C. UTEEM as alternate)*

*Aisha C. TIMOL*

*Secretary: R. SOKAPPADU*

*The Committee met on a weekly basis or more frequently as required, beginning 6 October 2000 and completed its present proposals on 29 January 2001. In the course of its deliberations, the Committee held discussions with all the regulators of the financial services industry of Mauritius as well as other persons having international exposure in the field of its concern. The Committee also consulted documents relating to similar works carried out in Mauritius in past years and examined documents, laws and legislations pertaining to other jurisdictions on the subject matter. The Committee wants to place on record its appreciation of the efforts put in, at fairly short notice in some cases, by those who made oral and/or written representations of their views, all of which have been taken into consideration in the recommendations made.*

*The Report of the Committee, based on those deliberations, is presented in the text that follows.*

## **Structure of Report and Recommendations**

*This Report is presented in seven sections.*

- *Section I summarises previous attempts made to establish a unified regulatory body.*
- *Section II provides a brief overview of international experience and trends regarding the structures set up for financial sector supervision.*
- *Section III focuses on the evolution of the financial sector of Mauritius against a backdrop of macroeconomic performance review. It highlights the evolution of employment in the sector, its contribution to GDP and its prospects. It also deals with the current organisational structure and staffing.*
- *Section IV considers the future shape to be given to the sector on the basis of a SWOT analysis.*
- *Section V goes to the core of the problem and takes up the arguments for a unified financial regulatory authority. These encompass the mechanism for good governance, accountability, the scope of regulatory powers and*

*responsibilities as well as internal organisational structure of the authority.*

- *Section VI discusses the possible options to that end and makes proposals on how to propel Mauritius into a viable financial regional hub of international standard. This section includes proposals regarding the structure, staffing, human resources development and legislative framework*
- *Section VII proposes a phased implementation plan of the main recommendations made.*

*The main recommendations of the Committee are set out below.*

- (i) *A unified financial regulatory authority, covering both banking and non-banking activities, be established in a phased manner, as follows:*

*Phase 1. The establishment immediately of a Financial Services Commission.*

*Phase 2. The eventual integration of the Financial Services Commission with the Bank of Mauritius.*

- (ii) *The Financial Services Commission will be responsible for the licensing, regulation and supervision of all non-bank*

*financial services. It will also be responsible for the protection of the rights of consumers of financial services.*

- (iii) The Financial Services Commission will take over the duties and functions of the Stock Exchange Commission, the Insurance Division and the Mauritius Offshore Business Activities Authority (MOBAA) as well as the regulation of all presently unregulated activities in the financial sector.*
- (iv) The Financial Services Commission will be managed by a Board which will be chaired by the Managing Director of the Bank of Mauritius. There will also be a Vice Chairperson and such other members as may be appointed by the Minister.*
- (v) The Financial Services Commission will facilitate the smooth integration of the onshore and offshore activities.*
- (vi) An appropriate legal framework is proposed for establishing the Financial Services Commission.*
- (vii) A Financial Services Advisory Council be established with the objective of giving overall direction and advice towards the development of the financial services sector. The Chairperson and Vice-Chairperson of the Advisory Council will be the Minister of Finance and the Minister responsible for Financial Services respectively. The other members will be*

*the Governor of the Bank of Mauritius, the Chairperson and the Chief Executive of the Financial Services Commission, as well as practitioners from Mauritius and from overseas having an extensive exposure to financial sector development.*

*(viii) The establishment of a Financial Services Promotion Agency (FSPA) is being proposed as a separate entity. It will act as a one-stop-shop for the development and promotion of the financial services industry. The FSPA will work in close collaboration with the Board of Investment to devise strategies to attract investors to the financial sector of Mauritius. The FSPA will also be responsible for human resource development and keep abreast of technological advances in that sector.*

*The rationale of the abovementioned recommendations are given out in greater details in the text of the Report.*

*The Committee believes that the new regulatory structure which will emerge from the implementation of its recommendations will have the following benefits for Mauritius:*

- It will go a long way towards making the financial services sector a well regulated sector.*

- *It will achieve the overall objective of sustaining economic development by the creation of high value-added jobs.*
- *It will set the right environment for the efficient integration of the financial and capital markets, the onshore and offshore sectors and generate the desirable synergies in the system.*

5 February 2001

# I

## INTRODUCTION

### Summary

*This Section analyses dynamic changes which have been transforming the delivery of financial services at the global level, the lack of success of attempts made in the past to position Mauritius advantageously in this mainstream and the objectives which need to be pursued in the context of widespread international interest in the nature and scope of supervision practised by distinct jurisdictions.*

1.1 Financial regulation and supervision has been organised over the years in Mauritius around specialist agencies having distinct and separate responsibilities for the banking, securities and insurance sectors. The common factor shared by the various regulators is that all the entities that are subject to their regulation belong to the financial sector. The emergence of complex financial structures with overlapping activities in different areas of the financial sector, both in Mauritius and elsewhere, and resulting interdependencies, lead to a perception that it might prove more efficient to carry out an integrated form of regulation and supervision of financial services in Mauritius.

1.2 The issue of whether to have separate specialist bodies or a unified supervisory agency continues to provoke intense debate amongst academicians, practitioners and in government quarters. This debate also involves the issue as to whether a single unified supervisory authority should concern itself exclusively with prudential regulation (i.e. safety and soundness) or whether it could also have the responsibility for conduct of business matters.

1.3 The structure of the financial services sector throughout the world is undergoing dynamic changes. Traditional product boundaries are becoming increasingly blurred. Activities are becoming more integrated. In this context, the lack of appropriate safeguards and inadequate supervision has had adverse impact in both developed and developing nations. This requires the supervisor to keep itself fully cognizant of the changing operational framework on markets and of the ensuing risks. With the rapid transformations in the monetary and other financial services fields seen over the last decade, a strong and coherent regulatory and supervisory framework, reflecting industry trend and apprehending all changes taking place, is called for. This is regarded as a precondition to evolve a sound monetary policy coupled with a strong financial services sector in order to guarantee macro-economic stability. The past failure of three domestic banks and three insurance companies in Mauritius underscores the need for vigilance and strong supervision in the maintenance of an overall stable financial system.

1.4 The extensive use of new technology and related practices, inter-linkages and dependence of the banking, securities and insurance sectors have led to question the role, definition and impact of conventional economic variables on which policy is based. For instance, how do we define money and formulate measures to harness any inflationary impact which e-commerce may have as it becomes more prevalent? Which measures should be put in place to address massive capital outflows in a liberalised financial market environment? Would it make better sense to build national institutions having a wider grasp of events in a globalising world, with distinct economic blocs? In some countries operators were disappointed with the existing financial sector supervision framework which failed to fully capture these dynamic changes and became

incapable of giving a comprehensive plan to follow to salvage the entire financial services sector from possible collapse, as in the case of the Mexican and East Asian crises.

1.5 When examining the case for an integrated financial regulatory authority, three main issues have to be addressed:

- (i) Under what conditions does a country consider a shift to an integrated model?
- (ii) The manner the integrated body would be structured, organised and managed; and
- (iii) How to implement and manage the integration process?

To answer these issues fully, the background to the different components of the financial sector, the objectives of reforms to be undertaken, the potential of the sector, its legal framework and the institutional set-up need to be studied in more details. The Committee went on to examine these issues, details of which are provided in the rest of the Report.

### *Previous work undertaken on a Unified Regulatory Body*

1.6 The idea of a single regulatory authority to co-ordinate the activities of various non-bank regulators<sup>1</sup> was first mooted in the 1994/95 Budget Speech. In that respect, several reports have been prepared with the assistance of experts from the Commonwealth Secretariat, from the UK law firm Norton Rose, Professor McKenzie (New Zealand) and Professor Joseph Norton (USA).

1.7 A Consultative Committee on the proposed setting up of a Financial Services Authority (FSA) was set up in January 1997. One of the assignments of the Consultative Committee was to review the various existing drafts of the FSA legislation and make recommendations thereon. A new draft FSA legislation was then prepared, in which provision was made for an Executive Chairman to preside over the FSA with an Alternate to replace him when needed, both to be appointed by the Minister of Finance. The existing regulatory bodies, namely the Stock Exchange Commission (SEC), Mauritius Offshore Business Activities Authority (MOBAA) and the Insurance Division, were to be absorbed within the Authority and thus cease to retain their specific identity. However, after discussions at the level of the Consultative Committee and representations made to the Ministry of Finance and through the press, the adoption of such a framework was felt to be premature, especially as regards the offshore sector where it was considered that the preservation of confidentiality of information was primordial.

1.8 A new draft proposal for an FSA was prepared in April 1998 by the Ministry of Finance. Accordingly, a non-executive Chairman and a Managing Director would head the FSA. Specified divisions were to be provided for in

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<sup>1</sup> These refer to the Stock Exchange Commission (SEC), Mauritius Offshore Business Activities Authority (MOBAA), and the Controller of Insurance

that legislation for the continuation of the operations of SEC, MOBAA and the Insurance Division. Criticism was levelled against this proposal in as much as too much power would be vested with the Directors of the various Divisions in the proposed FSA and ineffective power to the Managing Director.

1.9 Further consideration was given to the draft Bill by the Ministry of Finance and a new draft was prepared, where provision was made for the Chairman of the FSA Board to be also its Managing Director. In case the Chairman was a person other than its Managing Director, the latter would be appointed as a member of the Board and, as such, would be entitled to vote. The original provision for the Director of any Division to report directly to the Board of the Authority, when so directed, was removed with the Directors reporting directly to the Managing Director. A number of modifications were proposed as consequential amendments to the Stock Exchange Act, the MOBA Act and the Insurance Act, having a bearing specifically on the powers of the Directors of the distinct Divisions operating within the FSA. The basic approach followed was that the Directors of the various Divisions would retain their operational powers under the respective Acts which they are administering while consideration of policy matters pertaining to their Divisions would rest with the Authority. However, no final decision was taken.

1.10 As shown in the previous paragraphs, several attempts have been made to reform the regulation of the financial sector. Efforts have been made to establish the foundations on which the potential of the financial sector could be strengthened. However, the determination and resolution to go far enough with the proposed reforms and to move rapidly into action has been missing. Attempts to develop Mauritius into a substantial financial centre, comparable to those of Ireland and Singapore, have met with limited success. During the same

time frame, Ireland established itself as a major financial centre having successfully attracted global financial institutions of high repute. Singapore also consolidated its position as a major financial centre. Of direct relevance to Mauritius, both countries created significant numbers of high value-added jobs for nationals, involving the transfer of know-how by way of an influx of foreign nationals to work in their financial services sector.

1.11 The Mauritian financial sector has progressed during the last decade and it has, as such, created the potential to become a leading growth sector in terms of income, employment or value-added. This potential will materialize provided structural and timely reforms are introduced. So far, reforms have been *ad hoc* and piecemeal. This approach has stifled the exploitation of the full potential of the financial services sector. Further, proposed reforms have to be viewed against a backdrop of current worldwide developments, which act to ensure compliant behaviour on the part of regulators in accordance with international norms for regulatory and supervisory framework. The OECD onslaught on Harmful Tax Competition as well as the roles of the Financial Action Task Force on Money Laundering and the Financial Stability Forum represent initiatives which may induce the strengthening of domestic supervisory structures of financial centres in general and offshore financial centres in particular.

1.12 Reforms to be carried out in this respect entail reviewing the existing legislative, institutional and regulatory framework. The main objects of such an exercise should be to:

- (i) formulate strategy and policies for the development of Mauritius as an international centre of high standing;
- (ii) enhance the international competitiveness of operators;

- (iii) maintain high standards of supervision and regulation consistent with international guidelines; and
- (iv) consolidate lines of communication with international regulatory agencies.

1.13 The next section considers some of the typical responses that countries have adopted against the background of extensive transformations taking place in the delivery of financial services under liberalised market conditions.

## II

### LEARNING FROM INTERNATIONAL EXPERIENCE

#### Summary

*There is no single recipe on which to determine a universally acceptable institutional model for carrying out effective financial supervision. Each jurisdiction has its own historical background and comparative advantages on which its supervisory structure is based. Taking into account both changing technology contents of financial services and strong business reasons for a small jurisdiction, such as Mauritius, to become a credible global player in the financial field, this section sets out the arguments in favour of an integrated financial regulation framework for Mauritius.*

2.1 As the complexity of the financial services has increased since the mid 1980s at a global level, systemic risks involving financial sectors of one or several countries came to be seen as a reality. In response, a number of industrialised nations chose to integrate the various supervisory functions into a single agency. This factor has even given rise to an informal club of integrated supervisors<sup>1</sup>. In addition, transition economies of Europe and Central Asia have been examining the case for integrated financial supervision. The Asian financial crisis and ensuing contagion led many countries to look for an alternative providing a global system approach that will meet the new challenges of (a) financial stability, (b) price stability, (c) integrity of the financial system while simultaneously (d) providing safeguards to operators and savers.

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2.2 As mentioned, technological improvements and globalisation have resulted in the blurring of boundaries among the banking, securities and insurance sectors to quite an extent. In this regard, there is a view that a single integrated body responsible for overall supervision would create an enabling climate for better convergence of policies by bringing all regulatory functions together in a harmonious manner. Compared with single specialist regulatory agencies, the merit of the integrated approach is the lower likelihood of specific regulatory gaps within the same or different regulatory jurisdictions, as amongst activities which carry the same types of risks.

2.3 Integrated Financial Regulation (IFR) was initiated in Scandinavia in the mid-1980s, starting with Norway. The Scandinavian agencies share some common characteristics. The underlying motives for the introduction of IFR is quite pertinent to developing and transition economies. Countries with comparatively small financial sectors, like Mauritius, eager to build supervisory capacity, have much to learn from the Scandinavian experience.

2.4 One of the arguments in favour of IFR is linked to financial trends, more particularly the creation of new financial instruments. The main benefit from bringing all the regulatory functions under one umbrella is stated to be scale economies in the use of regulatory resources in a relatively small but highly concentrated financial system dominated by conglomerate groups. It is also argued that this set-up assists in the development of specific human expertise. Another argument put forward in support of IFR relates to the development of financial conglomerates that combine interest and expertise in broad areas,

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<sup>1</sup> The integrated supervisors comprise Australia, Canada, Denmark, Japan, Korea, Norway, Singapore, Sweden and the United Kingdom.

including banking, securities and insurance businesses. These conglomerates eventually come to play a dominant role in the economic arena, on a global scale.

2.5 The rationale for integration can also be traced to the Norwegian Royal Commission Report, which proposed supervision with two main limbs, namely:

- (i) integrated supervision would enable more effective supervision of financial conglomerates; and
- (ii) the merger would lead to scale economies in regulatory activities, owing to better deployment of resources in terms of administration and infrastructure support.

2.6 The case for an integrated regulator model is supported by a formidable bundle of convincing arguments:

- (i) Financial market structures have undergone rapid changes as a result of acceleration in financial innovation. This has led to the assumptions underlying the structures of regulatory organisation being called into question because the existing institutional set-up may not mirror the precise evolution of the financial sector structure.
- (ii) Since the existing financial architecture has stemmed from a set of *ad hoc* and pragmatic policy initiatives associated with banking crises and dislocation, a more coherent structure is called for.
- (iii) With the emergence of financial conglomerates, the financial services sector has grown in complexity. Such a development is confronting policy makers with the daunting challenge of whether a few supervisory agencies can be effective in capturing the intricacies of developments in the many other institutions as well as assessing impact and transmission signals in the system as a whole.

- (iv) Developments in the capital market have led to a fresh need for an enhanced regulation in the conduct of business. New financial products in pension provision and insurance, for instance, call for greater protection and guidelines in the public interest.
- (v) Financial innovation has engendered changing risk characteristics of financial firms.
- (vi) Growing internationalisation of financial service providers has vital implications for the institutional structure of supervisory agencies at both the national and international level.

Superimposed on these six factors are other country-specific factors that can be quite significant, as borne out by Northern European experience.

2.7 The emergence of “*bancassurance*” business created new financial conglomerates, combining banking and insurance activities. The need to supervise such financial conglomerates was a powerful reason underlying integrated supervision. Other arguments are summarised below:

- (i) Insurance companies played a vital role as investment brokers with growing cooperation between banking and insurance business.
- (ii) Both the legislative framework and supervision of banking and insurance shared common characteristics.
- (iii) Licensing and other structural tasks would be better coordinated under an integrated regulatory system.

2.8 The Norwegian experience was the outcome of a fairly long process of consolidation of its regulatory system but did not involve any significant dilution of the central bank’s authority. Both the Danish and Norwegian banking

supervisory authorities had for long been agencies outside the central bank. The Danish system combines prudential supervision of non-bank securities firms with traditional banking supervision. In the Danish case, there was no fundamental review of legislation since the Danish single financial authority operates under a number of different structures inherited from predecessor organisations, which have been adjusted and harmonised during the 1990s. In the Swedish case, the creation of the single financial authority took place against a backcloth of growing banks and insurance linkages. This evolution was motivated by the desire to achieve scale economies and to enhance Sweden's international stature. The Swedish banking crisis (1990-91) and the experience of other Scandinavian countries were also key factors leading to a policy shift towards IFR. The Finnish example shows that the FSA can share the support infrastructure of the central bank and develop significant professional synergy.

2.9 With regard to the second limb of justification, it was recognised that centralising regulatory functions and activities would lead to scale economies as a result of joint administrative, IT and other support functions. It would assist in the recruitment and retention of qualified human expertise. The latter would perceive greater career prospects in an integrated organisation than in a series of specialist agencies. It would also permit to maximise efficiency in the deployment of staff with rare intellectual capacity. The gathering and utilisation of know-how in specialist areas is another argument quite relevant to small island economies.

2.10 Financial supervision in the UK evolved along different lines compared to Scandinavia. In the UK, an intense debate preceded the setting up of the Financial Services Authority (FSA) as the unified regulator for the entire financial services sector. The Bank of England had over time developed considerable

banking supervisory capacity and the London financial market had an undisputed reputation as a well governed market when it was decided to establish the FSA. A greater degree of emphasis was placed on conduct of business as against prudential aspects. The UK is reputed to be a dynamic international financial centre. Its domestic services are considerably larger, and more diversified than those of its Scandinavian counterparts. In contrast to the Scandinavian experience, the FSA of UK is responsible for both prudential aspects and conduct of business regulation. Compared with the long process of agency consolidation in Scandinavia, the UK Financial Services Authority is considered a radical 'Big Bang' measure, unifying no fewer than nine existing regulatory agencies, with different and diverse experience and cultures which are based, however, on a series of self regulating agencies.

2.11 The case to keep monetary policy formulation and banking supervision in the same body was supported on the grounds that

- (i) it will encourage vital synergies;
- (ii) it will permit market intelligence to be shared; and
- (iii) inter-dependence of monetary and financial stability is increasing.

2.12 In Australia the main issue, as contained in the deliberations of the Wallis Committee (1996), seems to be on the organisational structure of regulation. Australia adopted a "twin peaks" structure with agencies specialising on

- (i) prudential supervision; and
- (ii) conduct of business regulation.

In the case of South Africa, however, the supervision of the banking system is entrusted to the South African Reserve Bank whereas non-banks are under the responsibility of another regulatory body, the Financial Services Board.

2.13 However, a unified supervisory system is not the only way to achieve such economies. A single financial services regulator can suffer from a “Christmas tree” effect. This is because heterogeneous responsibilities are gradually added to its range of functions. As a consequence, it becomes overburdened with numerous functions attached to the agency’s primary objective but of which government departments wish to divest themselves.

2.14 Small island jurisdictions, such as Jersey and Guernsey, which are also offshore centres, combine all financial sector regulatory supervisory activities in a single financial services commission. This structure, besides being centralising for the supervisory function, permits smaller numbers of supervisory staff to be employed by the concerned jurisdictions. By contrast, in the case of Malta, the supervision of domestic banks is entrusted to the Central Bank whereas the Malta Financial Services Centre is responsible for the supervision of all offshore entities. The entire Irish financial services sector, except insurance in the Irish Financial Services Centre is, on the other hand, supervised by the Central Bank of Ireland. This is also the case for the Monetary Authority of Singapore which combines both central banking and supervisory functions while also supervising the insurance sector. Ireland and Singapore are two highly successful modern financial centres.

### ***Global forces at Work in the Financial Industry***

2.15 Globalisation and consolidation have been and still are the major forces at work in the financial industry worldwide. Advances in technology, namely in the

information and communication industries, product and service innovation as well as rapid and wide ranging deregulation are the key drivers.

2.16 Technology is changing the economics of the business. The Internet is bringing about new ways of doing business from product innovation to distribution, risk management and customer relationship management. The Internet is producing capabilities for new delivery channels that cut across geographical and regulatory borders. It is enabling companies to create totally new business models like virtual banks and banks selling financial as well as non-financial consumer products through their websites. For instance, large companies are transacting all their foreign currency conversions for amounts of up to US\$ 10 million through an automatic Internet based system with no human intervention within the bank. Finally, communication technology has given rise to the outsourcing of non-critical activities. Banks are increasingly entering into strategic alliances with software and data processing companies for their routine processing, such as credit card operations and back office processing of their financial market activities.

2.17 Advances in risk management are enabling institutions to offer hybrid products that would cut across the traditional business boundaries. For example, banks are able to offer capital protection and guaranteed return mutual funds. Insurance companies are offering life insurance products that are linked with investment products. Commercial banks need no longer keep loans extended by them on their books. They can either securitize or sell these loans. Furthermore, with the use of credit derivatives, banks can minimize the credit risk of their loan portfolio.

2.18 Finally, rapid deregulation, coupled with technology, is creating new players. This is intensifying competition, forcing institutions to restructure, merge and consolidate in order to survive. Financial institutions are racing to grow in size. Size, as measured by market capitalization, is one of the key drivers for survival. Size brings economies of scale and allows the execution of large and complex financial transactions. It enables the global reach in terms of distribution network and market coverage.

2.19 Customers are becoming more sophisticated and demanding. They have access to a wider range of services and markets. They are no longer restricted to invest in their domestic market. They can trade via the Internet on a 24-hour basis in the stock, bond and foreign exchange markets. The trend is for customers to move away from being savers to becoming investors. In Mauritius, bank deposits account for about 92 per cent of GDP, compared to 44 per cent in the US where banks have seen their deposits falling for many years, reflecting the scope for significant structural changes under dynamic market conditions.

2.20 Regulators are responding to new challenges arising from these new trends. They are adopting another mindset, which is that regulation and supervision must be flexible to adapt to continuous change. They must work in close collaboration with the supervised institutions in order to shape supervision responses to new risks. In addition, regulators are recognizing the need to harmonize and integrate regulatory and supervisory practices across financial activities in order to minimize the possibility of gaps in regulation and, hence, regulatory arbitrage. Thus, the trend is towards a single regulatory body for the entire financial industry due to the operation of all these factors. There is closer collaboration worldwide between the various regulators of the different segments

of the financial industry. World associations of securities regulation bodies, insurance regulators and central bankers are working together to ensure coordination among themselves and the adoption of best practices in matters of regulation and supervision.

2.21 The next sections sets out to examine the basic structure of financial intermediation in Mauritius and the amount of scope available therein to accommodate the changes operating in dynamic financial markets, as highlighted above, to enable Mauritius to join the mainstream of viable and vibrant international financial centres.

### III

## THE MAURITIAN FINANCIAL SYSTEM

### Summary

*This Section examines the nature of financial sector activities undertaken in Mauritius, their recent evolution and growing complexity, concentration of specific financial activities among a few top players, the uneven distribution of responsibility for supervision amongst different supervisory bodies and some financial sector activities which go unsupervised. This analysis of the present set-up, when compared to achievements made in other similarly situated jurisdictions, would indicate that the potential of Mauritius to transform its financial services sector into an important contributor to GDP and to employment generation has been frustrated by the lack of a strong and unified supervisory direction capable of attracting major international operators to locate in Mauritius.*

3.1 The foregoing review of prevailing practices in several jurisdictions and analysis of international developments suggest a strong case in favour of a unified supervisory authority for financial services in Mauritius.

3.2 Before examining the case for a unified supervisory authority in Mauritius, however, it is appropriate to place in proper context the role of financial services in the economy of Mauritius. The financial sector has evolved over the years to pose as a potential area of change in terms of

- (i) generating further growth,
- (ii) ensuring price stability, and
- (iii) contributing to productive employment.

3.3 Since the mid 1980's, financial activities in Mauritius have experienced a gradual shift away from the dominance of banks and insurance companies. A number of non-bank financial institutions have emerged to play a vital role in mobilising savings, stimulating investments and providing financial support to other productive economic sectors. The responsibility to regulate bank and non-bank activities falls on different regulators. In this regard, the regulatory approach has been product based, such as for banking and insurance. As a result, some conglomerates are competing across a wide product range through subsidiaries and affiliates, subject to regulation by different bodies and, in some cases, no regulation at all.

3.4 In the second half of the 1980's, the growth performance of Mauritius was remarkable. The economy grew at an average rate of 7.3 per cent. Underpinning this favourable development, a broad-based liberalization of the economy took place. The Stock Exchange was set up in 1989. The Banking Act was revised in 1988, providing *inter alia* for the licensing of offshore banks. Steps were also taken to prepare legislation for the authorisation of non-bank offshore companies.

3.5 As from the beginning of the 1990's, the economy began to face new challenges: in particular, increased wage and price pressures threatened the economy's competitiveness in export markets. With the economy at near full employment, the strategy was to regain the competitive edge through enhanced labour productivity and export diversification. That required new investments to substitute existing technologies for more capital intensive ones, as well as investments in new product lines. To achieve this, it was of utmost importance

that the level of domestic savings be increased and the allocation of investable funds be further improved.

3.6 Between 1990 and 2000, the combined contribution of the three main sectors of the economy, namely Agriculture, Manufacturing and Tourism to GDP went down from 38.9 per cent to 35.9 per cent. It was expected that their share would continue to decline whereas that of the other services sector would increase.

3.7 Against this background, the authorities embarked on an economic diversification programme with a view to developing financial services as the fourth pillar of the economy contributing to the creating of high value-added jobs. It was felt that a policy emphasizing the diversification of the economy would be more effective in increasing the growth of saving and investment. The MOBA Act was enacted in 1992 and the Freeport was established in the same year, thereby emphasizing the external sources on which further financial sector development would be based, in the context of global financial sector liberalisation.

3.8 The range of current financial services includes payment services, credit services, asset accumulation, protection and real estate. In addition, corporate finance, risk management and financial data processing are other types of financial services being provided to the business sector. It is foreseen on present trends that these services could potentially be provided by new entrants on the market in competition with the existing ones. For instance, payment services could in future be provided not only by banks, but also by software companies, telecom companies and money-changers.

3.9 The range of services provided by financial institutions has also been growing in past years. In the insurance sector, in addition to the traditional life and non-life insurance products, companies also provide asset accumulation, re-insurance, consultancy services, risk assessment and claim settlement services. In the banking sector, the scope of services has widened to include asset accumulation, participation in issues of securities, settlement and clearing services, provision and transfer of financial information, custodial services and financial data processing.

3.10 The number of financial operators, too, has increased during past years. Together with banks and insurance companies, stockbrokers, insurance brokers, investment companies, venture capital companies, fund managers, foreign exchange dealers, money-changers, leasing companies, credit institutions and bond dealers occupy the grounds. The nature and scope of business undertaken in this context tend to blur the conventional distinction between banking and non-banking business. Moreover, falling telecommunication and computing costs have, by improving access to computers and the Internet, led to new ways of doing banking business. The concept of intra-day fixed banking hours is rapidly changing as banking business can be carried out on a 24-hour basis thanks to technology. It is not known yet what will be the final form of electronic banking, but new delivery channels or standalone entities and new processes for the payment and settlement of banking transactions will emerge on the basis of foreseeable developments. In any event, these changes imply that regulators of the financial system should be in a position to track them closely, both from technical and technological angles.

### ***Banking sector***

**3.11** Statistics on the financial sector of Mauritius show that banks' total assets amounted to Rs 111.2 billion as at June 30,2000. Two banks, namely the MCB and the SBM, holding about 70 per cent of all banking assets, dominate the sector. Deposits held with banks totalled Rs 84.4 billion, of which Rs 8.2 billion were in foreign currencies.

### *Insurance sector*

**3.12** Likewise, according to 1998 figures, the insurance industry is highly concentrated. Three companies, namely the SICOM, the Anglo-Mauritius and BAI, accounted for about 73 per cent of total sector assets of Rs 16.7 billion. The three largest Life Offices wrote 77 per cent of the total long-term insurance premium income of Rs 3.5 billion. Of the total short-term premium of Rs 1.8 billion, the largest underwriter accounted for 39 per cent of the total non motor premium, while the top 2 and top 7 general insurers wrote 56 per cent and 88 per cent respectively. Mortgage loans accounted for 25 per cent of the value of total assets, representing the largest asset class. The industry ceded 75 per cent of short-term insurance premium, excluding motor premium, to re-insurers. The dependence of the domestic insurance industry on reinsurance is striking: explained partly by the low level of capitalization of the companies, but also attributable to the lopsided distribution of risks which is a direct result of the dominance of conglomerates in the economy. This over reliance on risk transfer to re-insurers inhibits the growth in the capital base of the domestic insurance industry and, therefore, its capacity to retain more premium in the country.

### *Securities*

**3.13** In the stockbroking sector, three companies, namely General Brokerage, MCB Stockbrokers and SBM ABN Amro, account for some 75 per cent of total market turnover. The leasing industry is also very concentrated, with three

players, namely Finlease, Mauritius Leasing and SBM Lease, holding 75 per cent of total assets.

### ***Pensions***

3.14 The pension sector is characterised by a fragmented licensing regime across the different economic sectors of Mauritius and an absence of effective regulation. There are no official statistics on this sector but the total assets of pension funds, including the NPS, are estimated to be in the region of Rs 30 billion.

3.15 All approved pension funds are licensed by the Income Tax Department. In addition, pension funds not managed by an insurance company are registered with the Registrar of Associations and must submit annual accounts to the Registrar. There is effectively no supervision and regulation of the activities of pension funds.

### ***Contribution to the economy***

3.16 Most notable is the increasing contribution of the financial and other business services sector, excluding ownership of dwellings, which rose from 10.1 per cent in 1992 to an estimated 13.8 per cent of GDP in 2000. In addition, it is estimated that between 1994 and 2000, value-added by banks, insurance companies and other financial institutions has grown from Rs 5,476 million to Rs 14,035 million.

### ***Employment***

3.17 It is estimated that between 1996 and 1999, employment in the financial and other business services sector grew at a compound rate of 5.8 per cent a year, compared to 2.2 per cent for the whole economy. In absolute terms,

employment in the sector went up from 14,900 to 17,900 over the same period. Within the financial and other business services sector, however, employment creation in banks, insurance companies and other financial institutions has stagnated, growing from 6,328 in 1996 to an estimated 6,673 in 2000.

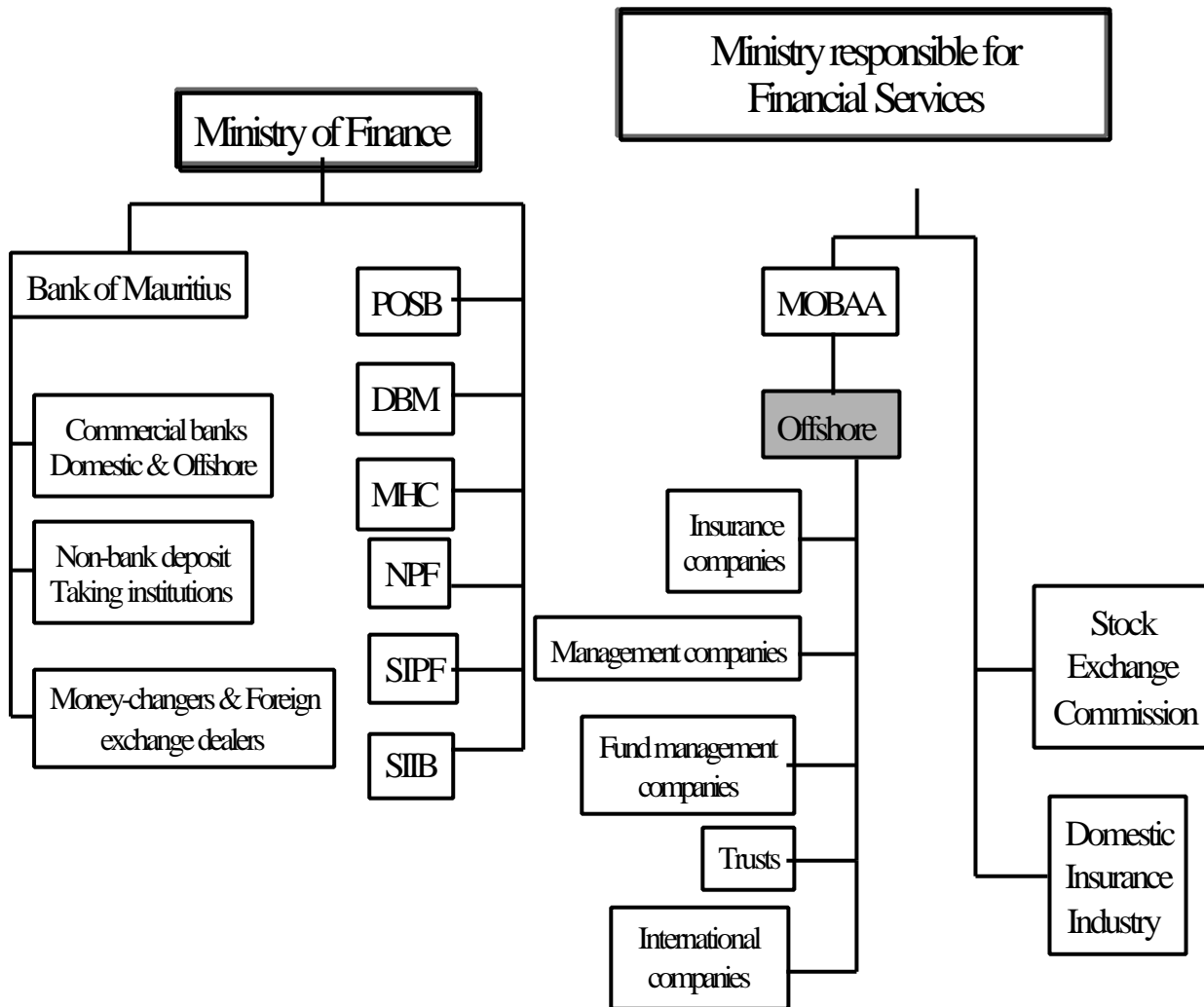
### ***Salaries and Wages***

3.18 Employment in the financial and business services sector is highly remunerative. Between 1994 and 1999, wages in this sector have risen at an annual compound growth rate of 9.0 per cent, compared to 8.8 per cent for the economy as a whole. In absolute terms, average monthly earnings have increased from Rs 7,980 in 1994 to Rs 12,300 in 1999. Between 1996 and 2000, average monthly earnings in banks and other financial institutions have gone up from Rs 11,364 to Rs 15,558 while increasing from Rs 9,109 to Rs 13,004 in the case of insurance companies during the same period.

### ***Regulation of the Financial Services Industry***

3.19 The Financial services industry is supervised and regulated under a legal framework under the responsibility of the Ministry of Finance. More recently, that duty is shared with the Ministry responsible for financial services, as outlined in Table 1 below:

**Table 1 :Regulation and Supervision structure of the Financial Services Industry in Mauritius**



3.20 Four different bodies have responsibility for the regulation of the financial services sector.

### 3.20.1 **Banking Sector**

- Regulator: Bank of Mauritius
  
- The banking sector, both domestic and offshore, is licensed, regulated and supervised by the Bank of Mauritius under the Banking Act. Ten domestic commercial banks (with some 130 branches) and eleven offshore banks fall under the supervision of the Central Bank. In addition, it regulates foreign exchange dealers and money changers licensed under the Foreign Exchange Dealers Act as well as non-bank financial institutions authorised to take deposits under the Banking Act, as amended.
  
- The Bank of Mauritius was established in 1966 under the Bank of Mauritius Act. It is headed by a Governor, who is also the Chairman of the Board of Directors. The Governor is appointed by the Prime Minister as the principal representative of the Bank and is responsible for the general supervision of the Bank. The Managing Director, who is also appointed by the Prime Minister, is responsible for the day-to-day management of the Bank's affairs and business.
  
- The Bank of Mauritius is auto-financed. Any surplus fund (profits) is transferred to the Consolidated Fund.
  
- The Bank of Mauritius has the powers to recruit its own staff for the smooth running of its operations. The Bank, which falls outside the purview of the

Pay Research Bureau, has some 260 staff on its establishment. The current organisational chart of the Bank of Mauritius is given in Annex 1.

- Acts / Regulations under the responsibility of the Bank of Mauritius:

**Acts**

Bank of Mauritius Act

Banking Act

Foreign Exchange Dealers Act

Exchange Control Act (suspended as from July 1994)

**Regulations**

Bank of Mauritius Regulations 1968

### 3.20.2 Insurance

- Regulator: Controller of Insurance
- The Insurance Act 1987, which replaced the Insurance Ordinance of 1960, sets out the legal framework for the conduct of insurance business in Mauritius, and provides for the prudential supervision of the insurance industry by ensuring control over and transparency in the conduct of insurance business, and for the protection of policyholders and members of the general public. Pension schemes operated by insurance companies also fall under the Insurance Act. All powers are vested in the Controller of Insurance, except when the Controller of Insurance proposes to cancel the registration of an insurance company or refuses to grant a licence to a company, the company may then appeal to the Minister responsible for the insurance sector against the decision of the Controller of Insurance. The Controller of Insurance is supported in his task by the inspectors of insurance.

- The Office of the Controller of Insurance has under its supervision 24 insurance companies, 105 insurance agents, 7 insurance brokers and 2360 insurance salesmen. Total assets of insurance companies amounted to an estimated Rs 19.2 billion as at 31 December 1999, up by 15% over a year ago. The bulk of assets consists of investments in Government and private securities and shares, and as mortgage loans.
- The Insurance Division, which is financed from the Consolidated Fund, is under the direct control of the parent Ministry. Recruitment is done through the Public Service Commission. The salary scales of the insurance cadres are fixed by the Pay Research Bureau.
- The Insurance Division has twelve (12) professional/ technical cadres on its establishment as follows:

Controller of Insurance	1
Chief Inspector of Insurance	1
Principal Inspector of Insurance	3
Senior Inspector of Insurance	3
Inspector of Insurance	4

- Only three are currently in post, namely the Controller of Insurance, the Chief Inspector of Insurance and one Principal Inspector of Insurance. All the other posts are vacant. Three officers from the Finance and General Services are presently giving assistance to the Controller of Insurance against payment of an allowance.

- Due to the above, the Office of the Controller of Insurance no longer makes on-site inspections and is confined to office work.
- Acts/ regulations under the Controller of Insurance

**Acts**

Insurance Act 1987

**Regulations**

Insurance Regulations 1959

Insurance (Exemption) Regulations 1975

Insurance Regulations 1988

### 3.20.3 Stock Exchange

- Regulator: Stock Exchange Commission
- Operator: the Stock Exchange of Mauritius Ltd.
- The Stock Exchange Commission (SEC) was set up under the Stock Exchange Act 1988. SEC regulates and supervises the operations of the Stock Exchange of Mauritius Ltd (company which manages the Port Louis Stock Exchange), the Central Depository and Settlement Co. Ltd (set up under the Securities (Central Depository, Clearing and Settlement) Act 1996), capital market intermediaries (stockbroking companies and stockbrokers) and “Approved Investment Status” institutions (i.e, unit trusts, investments trusts and investment companies).
- The Commission is managed as a body corporate and is financed partly from fees charged on the transactions on the stock exchange and partly from the Consolidated Fund.

- The Chief Executive is the responsible officer and is answerable to the Stock Exchange Commission, a body that is headed by a Chairman and six Directors. The Chairman and the other Directors are appointed by the Minister responsible for financial services. Recruitment at the Stock Exchange Commission is done by the Commission, with the approval of the Minister. The salaries of the staff of the Commission are fixed by the Pay Research Bureau. The Chief Executive is supported by five technical cadres and one administrative staff.
  
- Acts/Regulations under the responsibility of the Stock Exchange Commission

### **Acts**

The Stock exchange Act 1988

The Unit Trust Act 1989

The Securities (Central Depository, Clearing and Settlement) Act 1996

### **Regulations**

The Stock Exchange (Licensing) Regulations 1989

The Stock Exchange (Stockbrokers Examinations) Regulations 1993

The Stock Exchange (Over the Counter Market) Regulations 1990

The Stock Exchange (Dealer`s Representatives` Examinations) Regulations 1992

The Stock Exchange (Listing Committee) Regulations 1993

The Stock Exchange (Brokerage) Regulations 1989

Brokerage (Amendment) Regulations 1996

Brokerage Fee for Debenture 1999

## **Rules**

The Stock Exchange (Register of Interests in Securities) Rules 1989

The Stock Exchange (Approved Investment Institution) Rules 1992

The Stock Exchange (Investment Clubs) Rules 1994

The Stock Exchange (Investment by Foreign Investors) Rules 1994

### **3.20.4 Non-bank offshore**

- Regulators: Mauritius Offshore Business Activities Authority
- The Mauritius Offshore Business Activities Authority (MOBAA) was set up under the Mauritius Offshore Business Activities Act 1992 to regulate and supervise the non-bank offshore sector.
- MOBAA is managed by a Board of Governors, who are appointed by the Minister responsible for financial services. The Authority is administered by a Director, who is appointed by the Board of Governors. The Board has powers to make the recruitment of the necessary staff as may be required. The salaries are fixed by the Board and are, in some cases, negotiable.
- MOBAA is funded by the licensing fees paid by registered companies
- More than 14,000 offshore companies are on the register of MOBAA. They are serviced by some 60 offshore management companies.
- The MOBAA is supported by a team of highly qualified staff. However, there are some important positions, particularly that of Head of licensing and compliance, which are vacant.

- Acts/ Regulations under the responsibility of MOBAA

#### **Acts**

The Mauritius Offshore Business Activities 1992

The International Companies Act 1994

The Offshore Trusts Act 1992

The Protected Cell Companies Act 1999

#### **Regulations**

The Mauritius Offshore Business Activities (Fees) Regulations 1992

The Mauritius Offshore Business Activities (Companies) Regulations 1995

The Offshore Insurance Regulations 1992

The International Companies (Fees) Regulations 1994

### **3.20.5 Unregulated financial Sector Activities**

The following activities/ bodies are not regulated:

- **Leasing companies and Venture Capital Funds:** No authority has been specifically appointed to regulate and/or supervise the activities of these companies.
- **The Post Office Savings Bank,** was set up under the Post Office Savings Bank Act and is managed by the Post Office Department. The Post Office Savings Bank, which falls under the responsibility of the Ministry of Finance, is not subject to formal regulation or supervision.
- **The Sugar Insurance Fund Board,** set up under the Sugar Insurance Fund Act, which specialises in the provision of insurance cover to the sugar industry. It does not fall within the purview of the Insurance Act 1987.

- **Asset management companies and companies providing investment advisory and other services in the financial services sector:** these activities are not subjected to regulation or supervision by any specific body.
- **Pension Funds:** excepting pension funds managed by insurance companies, there is no direct regulatory body to oversee and supervise the activities of pension funds in Mauritius.
- **Commercial Credit Institutions:** No regulation or supervision of their activities is undertaken by any specific regulatory agency.

3.21 The foregoing information shows that the winds of change that have been transforming the provision of financial services in other markets have also touched Mauritius in successive waves. Nonetheless, both in terms of contribution to output and creation of employment, the financial services industry has not assumed the leading position which could have made the financial services sector a successful fourth area of economic diversification. The level of supervision given to diverse segments of the financial sector differs significantly from one sector to another whereas there are certain activities that do not benefit from any supervision at all. This state of affairs may expose certain segments of the Mauritian financial sector to reputational and other risks, including fraud and malpractices. Furthermore, the absence of consistent supervisory direction may also explain the relatively inadequate development of financial services in the economy.

3.22 The strengths and weaknesses of the Mauritian financial framework are considered in the next Section with a view to identifying a coherent framework in

which supervision of financial services may be carried out efficiently and effectively.

## A SWOT ANALYSIS OF THE FINANCIAL SERVICES INDUSTRY OF MAURITIUS

### *Summary*

*This Section considers the strengths, weaknesses, opportunities and threats relating to the financial sector of Mauritius in the present context. It is reckoned that the institutional, legal and infrastructure set-ups of the financial sector of Mauritius are, by and large, sound. The main weaknesses stem from substantial supervisory gaps across different financial sector activities, with banking being regulated at international standards whereas other sectors are under-regulated or not regulated at all. Further, there is an inadequate response by Mauritius to wide sweeping changes taking place at the international level in terms of technology adoption and evolution of financial products. On balance, there are sufficient strong elements on which a new direction may be given to our financial services sector.*

The Committee considered at length relevant factors in the establishment of a stronger supervisory framework. In particular, a SWOT analysis was carried out to identify the way forward. The following paragraphs summarise the main findings.

### **Strengths**

4.1 Mauritius has most of the ingredients to develop into an international financial centre, namely political stability, a competitive fiscal incentive package, a large network of double tax avoidance treaties and a strong and reputable banking regulatory environment.

4.2 Mauritius has well-established and fairly well developed banking and insurance sectors with a few prominent and professionally managed domestic companies.

4.3 The banking and insurance sectors have a relatively small pool of professionals, comprising bankers admitted to the Chartered Institute of Bankers, London and Chartered Insurance Practitioners and Actuaries, many of whom have qualified and practised in advanced financial centres.

4.4 The enviable democratic history of the country, underpinned by the rule of law formulated by an elected legislature, and administered by an independent judiciary with the ultimate appellant body being the Queen's Privy Council, is a unique asset and provides essential comfort to investors and economic operators.

4.5 Commercial, civil and criminal law codes are well developed and are, by and large, based on and inspired from the French code and English law; this has ensured clarity in, and acceptance of, the outcome of the litigation process, which is often an essential recourse in the resolution of complex claims.

4.6 Mauritius also has a few financial institutions which could develop, with the right strategy and management, into regional players. These institutions have been in existence for many decades and have accumulated a wealth of knowledge and experience that could be leveraged for regional expansion.

4.7 Though not perfect, Mauritius has the institutional framework for a dynamic capital market. It already has a stock exchange that would soon be on

an automated trading system. Settlement of listed and quoted shares and corporate bonds is done through the Central Depository System (CDS).

4.8 It has a strong banking regulator, the Bank of Mauritius. The payment system operates on a real time basis (RTGS) through the Mauritius Automated Clearing and Settlement System (MACSS) and is linked to an efficient and reliable international payment system infrastructure, i.e. SWIFT.

4.9 Mauritius has no exchange control. It hosts a number of domestic and offshore banks, including excellent international names. This element reflects recognition of high standards of banking regulation practised by the regulator and constitutes a significant basis for future build-up.

## **Weaknesses**

4.10 The main weakness of the present financial system is the regulatory framework. Governing legislation has not kept pace with developments in the sector. In certain areas, like insurance, current law inhibits and hampers the supervisory authority from taking prompt action against sick units. The insurance law in its present form may give the impression that the supervisory authority is not totally shielded from undue political pressure in the exercise of its duties. There is a lack of a unified and harmonized approach to supervision and regulation of the entire industry. This leaves room for regulatory arbitrage. Some financial sector activities are not regulated or supervised.

4.11 The operation of too many small players may become the source of systemic risk. In the insurance sector, for example, the presence of some marginal, undercapitalised, illiquid and poorly staffed companies operating at the fringe of the market, and, writing mostly motor insurance at uneconomic terms, may be viewed as a source of risk. Most of them would not have the capital

resources to invest in technology and risk management processes to stay competitive.

4.12 The dominant position of a handful of players inhibits competition and innovation. There is no innovation in terms of products and business models. Other than the secondary securities market developed by the Bank of Mauritius, there is barely significant secondary market trading in stocks and shares.

4.13 The failure of three insurance companies, transacting primarily motor insurance business, in the last decade may have shaken public confidence in the insurance sector, and, has raised questions about the effectiveness of insurance supervision.

4.14 The apparent over-dependence on reinsurance impedes the progressive fortification of the capital base of the domestic insurance industry, and, may perpetuate its state of undercapitalisation. There may thus not be sufficient scope and possibility to build increased financial capacity to assume risk domestically, and, to expand across national borders into the surrounding region where opportunities may emerge.

4.15 Inadequate supply of skilled manpower having international exposure could be one of the reasons for the observed insufficient innovation in the provision of financial services. The industry has no institutional set-up for the continuing training and upgrading of skills of its human resources. There is no defined policy to encourage the employment of foreign skilled manpower in new areas such as assets securitization and financial engineering.

4.16 The lack of regulation of supervision of the pension sector is giving rise to insufficient asset accumulation to finance the future pensions of the current employed work force. The existence of pension funds may create the illusion that pension needs are being catered for with the result that the employees are not conscious of the need to set aside additional savings for their retirement. The outcome could be an impoverished pensioner population which would act as a drain on future economic resources. Most pension funds are severely underfunded with the result that the financial burden is being passed on to future generations. With the rapid ageing of the population of Mauritius, the impact of inadequately financed pension systems could be severely destabilising for the economy and could require disproportionate future tax increase in order to finance the shortfalls.

4.17 The capital market is underdeveloped. The Stock Exchange of Mauritius is marked by low volume, poor liquidity and lack of depth. Local investors, private and institutional, are reluctant to invest in the traded securities, preferring to be savers with banks. This absence of a strong domestic investor base and the unsophisticated behavioural pattern of institutional investors have resulted in a lack of demand for already undervalued stocks, resulting in further downward pressure on prices. The over-concentration of stock market activities on equities, in the absence of a full-fledged secondary market for corporate and Government bonds, has also hampered the development of a fully integrated financial sector in Mauritius.

4.18 The money and capital markets are prone to malfunctioning. Poor disclosure practices by companies hinder the proper evaluation of business and credit risk. In the present circumstances, there is a risk that some areas may not develop the required scope to remain in business or to have a meaningful market

presence. This leads to potential errors and inherent weaknesses in the pricing of financial assets such as equities, insurance policies, debentures and bank loans. In addition, with the exception of the banking sector, there is a lack of risk management culture across the financial services industry. The end result could be a misallocation of capital that would in the long run weaken the financial position of some financial institutions operating in Mauritius and, hence, the entire system. A revamping of the stock market as well as the development of an active and vibrant debt market is urgently needed.

4.19 The development of the financial services industry has reached a stage where it is no longer feasible and practical to have the industry evolving along two distinct sectors, namely domestic and offshore. The current structure has shown its deficiencies in certain areas such as supervision and taxation policy. These areas may continue to be challenged by certain international bodies such as the OECD. However, it should be ensured that the integration of the offshore with the domestic sector does not weaken in any way the strong and high level of supervision practised in some areas of the domestic sector. Separation of the offshore sector from the domestic sector stands as a handicap in the further development of the industry. The different tax regimes in the two sectors allows for tax arbitrage, for example, in the banking sector, and have led to misperceptions about the system at the international level. In an environment in which the Exchange Control Act has been suspended, the necessity to distinguish and keep separate the domestic sector from the international and global economy cannot be justified on the face of it. It is urgent that Mauritius should engineer its financial services industry in such a manner as to project an integrated image of the entire sector, keeping in view competition challenges from other financial centres.

4.20 The pace of economic development of the countries forming part of the region surrounding Mauritius is comparatively slow. These countries are not attracting significant foreign investment, equity or debt. Hence, Mauritius is prevented from effectively playing the role of the regional financial centre to channel funds to these countries.

## **Opportunities**

4.21 The financial services industry has considerable further scope to fully realize its potential. In this respect, it would be useful to learn from the experience of Ireland and Singapore. In Ireland, the unemployment rate has decreased from 17 per cent in 1986 to an estimated 5 per cent in 2000, largely in view of strong demands for labour from the finance industry. Singapore has created 150,000 jobs in the financial and business services sector during the period 1987-1997. In contrast, employment creation has stagnated in the banking, insurance and other financial institutions sector of Mauritius, as mentioned earlier. A well-centred financial sector holds the scope for upholding employment creation in Mauritius.

4.22 Mauritius can focus at becoming a financial centre meeting specific needs of companies world-wide. It already has in place some of the key ingredients of success that were mentioned earlier. In addition, some of the domestic players can potentially become important players in the region after some consolidation among themselves.

4.23 As the population of Mauritius embraces the global trend by shifting from savers into becoming investors, deposit-taking institutions, banks and non-banks, will lose their share of deposits. These deposits will flow into investment

products. Therein lies both an opportunity for and a threat to the domestic financial services industry. It would be an opportunity if the domestic financial institutions would be innovative enough to offer investment products that would meet the needs of domestic investors. It would be a threat if domestic consumers do not find the right investment products in the domestic market and hence invest their savings with financial institutions operating in foreign jurisdictions. This move from savings to investment has already started. There has recently taken place, for instance, a net outflow of funds from Mauritius by local investors that has affected the liquidity of the foreign exchange market, thus exposing its insufficient depth and resilience.

4.24 Fund management is one of the fastest growth segments of the financial services industry worldwide in the context of globalisation. Capital will flow to areas and countries that would provide superior returns on capital for a given level of risks. At the same time, asset managers want to manage funds invested in a particular market or country in or near that market or country. The trend to shift out of saving accounts with banks into investment products will accelerate in countries surrounding Mauritius and create opportunities if Mauritius inspires the necessary investor confidence and has the appropriate products to offer by revamping its financial sector.

4.25 Mauritius can position itself into:

- (i) becoming the centre that would attract and manage these funds to be invested in the regional markets and the conduit through which these funds are being invested in markets in Europe, North America and Asia.

- (ii) becoming the centre where foreign fund managers would locate their fund managers to manage money from Europe, North America and Asia that are intended for investment in the region.

These could be the long-term goals of Mauritius and there would be a need to build the required skilled manpower to handle this type of business.

4.26 In the near term, Mauritius can bring to itself the necessary equipment and skills to position itself, for instance, to be the back-office centre of financial institutions operating in Europe. Mauritius has a pool of literate manpower that can process financial operations and this may need to be suitably supplemented. Mauritius also needs enough communication bandwidth at costs that are relatively cheaper than those in Asia and Africa to attract these types of operations.

### ***Threats***

4.27 The main threat is the inability of the industry to adapt to and embrace the globalisation trend. The existing dominant players in each segment could become complacent and satisfied with their market positions. Satisfied with their inward-looking status quo and with no challenge from existing foreign institutions operating in the domestic market, the dominant players could fail to respond to the new needs of the investing public. Gradually and surely, the end result would be the transfer of domestic savings out of Mauritius into global markets via more efficient global financial institutions. There is evidence that this process is already at work.

4.28 In this regard, there is a need to consolidate and better integrate the industry. Amongst others, such consolidation and integration involves rethinking

the regulatory framework and the number of players. Two to three large players dominate each segment of the industry with many small players holding the remaining 25-30 per cent of the market. A few major players from the domestic market could aspire to become major players at the regional level. Domestic players will increasingly face competition from foreign institutions that have the advantage of both size and global reach. It must be realised that these institutions do not need to physically have offices in Mauritius. They can reach the customers in Mauritius through the Internet.

4.29 The foregoing analysis sets the stage for establishing a coherent regulatory and supervisory framework to be adopted by Mauritius, drawing on its existing strengths and the opportunities that are opening up at both the regional and global levels. This is taken up in the next Section.

## SHIFTING TO A COHERENT SUPERVISION SYSTEM

*This Section presents a case for the establishment of a single supervisory authority to oversee the whole range of financial services. It establishes the urgent need for a coherent approach to supervision of financial services, taking into consideration global changes taking place in the finance industry and the inherent potential of Mauritius to move forward in the required direction. The analysis concludes that a single supervisory authority for the whole of financial sector of Mauritius will lend more credibility to the centre and constitute a strategic tool towards attracting world class business players to Mauritius.*

5.1 To translate its goals into action, Mauritius has to respond more forcefully to its dynamic environment. Policies should be strengthened to reassure investors of the solidity of the economic sectors and the transparency with which economic information is disseminated to economic operators and users. Such an approach would promote good governance and investor confidence, which, in turn, would contribute to sustained economic growth. The setting up of coherent supervisory standards can help meet these objectives.

5.2 As discussed in Section II, the benefits, as borne out from international experience, can be varied and numerous. Some of these, at the risk of repetition, are summarised in this paragraph:

- A single regulator can take advantage of a single set of central support services. It can lead to increased efficiency in allocation of regulatory resources both across regulated firms and types of regulated activities. The integrated regulator can resolve efficiently and effectively the conflicts that inevitably emerge between the different objectives of regulation.
- Over time, as a result of multiple specialist regulations, inconsistent rules have developed. This has given rise to unjustified differences in supervisory approaches, e.g. in terms of capital adequacy requirements, transparency and public accountability. Finally, if an integrated regulator is given a clear set of responsibilities, then it should be possible to increase supervisory transparency and accountability.

5.3 Since the Government has decided to bring some order in the area of regulation, it would be useful to clearly spell out the reasons driving the current revamp of the regulatory framework. The main reasons for a strong and coherent regulatory framework are:

- (i) the rapid changes taking place in the financial services industry world-wide;
- (ii) the need for a credible regulatory environment and a credible, single regulator; and
- (iii) the ambition of Mauritius to develop into a world-class financial centre.

5.4 As observed earlier, substantial changes are taking place in the financial services industry worldwide. Banks investing huge amounts of money in technology target the seamless delivery to customers of an ever increasing array of products catering for the needs of both individuals and companies. Few upfront financial institutions can claim that they have the right business model that would enable them to recoup their huge investment costs in technology. Profits may accordingly shrink in the short term. Those institutions that have enough capital to withstand such decrease in profit in the short term stand a good chance to survive. Otherwise, they would have to merge with other players or go out of business. In this context, one must be prepared to see more consolidation in the financial services industry in Mauritius.

5.5 Consumers' range of choice with regard to financial services have been growing. They may choose to do business with global financial institutions instead of sticking to domestic institutions if there is any doubt about the financial soundness of, lack of confidentiality in, or poor level of services offered by, local financial institutions.

5.6 While the financial services industry will be undergoing major changes, Mauritius will need a credible regulatory environment and regulator to reassure:

- (i) the domestic consumer of the soundness of the country's financial system;
- (ii) the operators that they are getting a fair and impartial treatment; and
- (iii) potential world class operators intending to set up in Mauritius, that they will obtain a high standard of regulation and supervision which will keep their reputation intact.

5.7 One positive factor to the credit of Mauritius is that the standard of supervision practised by the Bank of Mauritius is fully compliant with international standards. Also, the Government has already confirmed to various international authorities its commitment to adhere to “the minimum international standards”. Despite some weaknesses, the financial services sector inclusive of banks, insurance companies and the stock exchange, adheres to quite an extent to the high international standards set for financial regulation. Furthermore, Mauritius is fully committed to the fight against money laundering and the creation of a propitious environment for legitimate cross border financial services. The recent enactment of the Economic Crime and Anti-Money Laundering Act 2000 will help maintain a clean business environment in Mauritius. Some of the commitments given to the OECD have already been incorporated in the Finance Act 2000 whereas the rest will be implemented in a phased manner by 2005.

5.8 As barriers between the sectors within the financial industry become blurred and new products which cannot be categorized as either banking products or insurance products, come into play, the current product based approach to regulation will take a back seat. The existence of regulatory gaps between different types of financial institutions will also fail to show a unity of purpose in the supervisory process. Moreover, the factor that certain activities such as asset management activities in Mauritius, is unregulated tends to press the case for an urgent review of the supervisory process. The differentiated levels of supervision allow for regulatory arbitrage arising from unequal treatment of similar products or activities. Taken together, these factors could endanger a financial institution and even the entire financial system by contagion effects.

The case for putting in place a harmonized and integrated regulatory framework cannot thus be over-emphasised in the present circumstances.

5.9 The presence of a strong and credible regulator of the financial services industry has been central to the success of both the Central Bank of Ireland and the Monetary Authority of Singapore (MAS). The Central Bank of Ireland is the regulator for all financial services activities, except insurance. While Ireland has had a long history of central banking, Singapore started as a third world country with no credible central bank. The Singapore government deliberately imposed the discipline and rigour on the MAS as a supervisor to permit it to earn its reputation as a credible and strong regulator. Today, the reputation of MAS is recognized worldwide. Mauritius can distil useful lessons from both these experiences.

5.10 Mauritius is, unwittingly perhaps, exposed to reputational risks at present due to its uneven system of financial sector regulation and supervision. There may exist certain deficiencies in terms of adequate supervisory oversight whereby no action would have been taken against certain businesses which should have been taken already under a proper system of supervisory governance. It is imperative to overcome such deficiencies. However, the wider objective may be to initiate action to round up the financial sector supervisory process in Mauritius into a world class standard so as to give Mauritius an international edge as a proactive regulator of financial services.

5.11 Mauritius cannot afford to take risks to which it is exposed on account of prevailing variances in terms of the extent of supervisory oversight on diverse financial sector activities. It is also a fact that supervisory skills of the standards recommended by international bodies are scarce. This leads to the task of

supervision being unevenly undertaken across different segments of the financial sector. The opportunity to build an adequate stock of high level supervisory skills would be created if the job of supervision benefited from a strong professional leadership and came to be treated as a key input in furthering financial sector development. Coherence of supervisory practices would automatically emerge in such an environment.

5.12 The achievement of these objectives will depend on the extent to which supervisors co-operate with each other on a professional basis rather than defending their separate turfs. The next section reflects the Committee's deliberations on this subject.

## VI

### PROPOSALS FOR A SINGLE REGULATORY AUTHORITY

*This Section contains the main recommendations made by the Steering Committee towards the establishment of a unified regulatory body. It recommends the setting up of a Financial Services Commission, of which the Bank of Mauritius shall be the anchor, to which will be entrusted the task of bringing under a common roof the supervision of the insurance, securities market and offshore sector activities in a bid to bring about integrated financial services supervision in a phased manner. These proposals may lead ultimately to the establishment of a single unified regulatory authority, which may encompass all the present functions of the Bank of Mauritius, including banking supervision, as well as the integrated financial sector supervision framework. It also advocates the creation of a Financial Services Advisory Council, which will discuss latest concepts and trends world wide and formulate suggestions on policies to be adopted to spearhead financial sector development. It goes on to recommend the establishment of a Financial Services Promotion Agency, which will have responsibility for promotion of the centre and meeting its skill base and training needs.*

#### *New Approach to Regulation and Supervision*

6.1 The Steering Committee recognizes that the Mauritian financial services industry has the potential to develop into a viable and dynamic sector capable of generating a large number of high value-added jobs. As a means to unlock this potential, the Committee recommends a unified approach to the regulation and the supervision of the financial services industry. Such an approach is already being embraced by major financial centres worldwide, as this approach places

the regulatory authority in the best position to respond promptly and effectively to the rapid changes that are now becoming characteristic of the industry. The Committee views that the unified regulatory approach encourages the supervised institutions to adopt the best practices currently employed in the world. Not only would this be in the best interest of the supervised institutions but it would also attest to the high standard of supervision practised in Mauritius. This fact in itself would prompt global institutions to consider establishing operations in Mauritius. In effect, in adopting a new approach to regulation and supervision, the single regulatory body aims to nurture the existing local players into financially secure and highly competitive domestic players with the potential to become regional actors. Accordingly, the single regulatory body will provide existing players with sufficient notice to comply with the new and revised regulations.

### ***Scope of the Single Regulatory Authority***

6.2 The Steering Committee examined the nature and adequacy of the supervisory framework currently obtaining in the different segments of the financial industry of Mauritius. It considered the consequences of pursuing regulation and supervision of financial sector activities in the present set-up and came to the conclusion that a major overhaul was urgently required in this respect, especially in view of the fact that there were supervisory gaps with respect to some financial sector activities but more so due to the unevenness of the level of prudential supervision applied to different operators within the sector.

6.3 The Committee also took into account international trends in the field of financial sector supervision, keeping in view the need to satisfy an increasing

number of international standards set by different institutions in the context of globalization and integration of financial markets worldwide. The Committee recognised that competition in the financial industry is becoming more intense. Financial institutions will increasingly need to cope with a more complex environment, particularly in the area of technology and risk management. In this regard, the set-up of a single regulatory authority should form part of a comprehensive reform package: -

- (i) to help improve efficiency and innovation in the financial industry through more competition and a level playing field; and
- (ii) to respond to the need to enhance the safety and stability of the financial system of Mauritius

6.4 The Committee is of the view that the current separation of the financial industry in two sectors: offshore and domestic, is no longer appropriate for the further development of the industry and Mauritius as an effective global financial centre. In this regard, members agreed that it is necessary that the new financial industry regulatory framework integrate both sectors into a single, unified structure.

6.5 The Committee recognizes that the setting up of a single regulatory authority should increase the attractiveness of Mauritius as a financial centre of high standing. Mauritius is a relatively small jurisdiction and it does not have the

advantage of having a long established track record nor an efficiently operating financial market geared to international standards, such as the established centres. Members consider it necessary therefore to heighten the credibility and the quality of financial sector regulation and supervision in a strategic approach to develop Mauritius as a more credible financial centre.

6.6 In this regard, the Committee is of the view that it is necessary for Mauritius to have a unified, single regulatory authority for all financial sector activities. This arrangement will provide for a consistent framework under which supervision of the financial industry, irrespective of the nature of activities, will be undertaken e.g. banking, insurance, securities, asset management and pensions. It will also permit the development of common intra-industry standards for the management of identical risks involving differentiated products.

6.7 The Committee is also of the view that the Bank of Mauritius has already attained and implemented a very high standard of supervision with regard to the banking sector. The Committee believes that the level of supervision of all sectors of the financial industry of Mauritius should be brought up to the same level currently practised by the Bank of Mauritius in order to eliminate any gap in the amount of supervision applicable to different financial sector activities. The objective of establishing a single supervisory and regulatory authority should, however, be implemented in such a manner as not to undermine the high level of supervision already achieved by the Bank of Mauritius. It should aim instead at creating sufficient across-the-board confidence and credibility such as to attract those global operators who feel comfortable in a well supervised environment.

6.8 The Committee agreed that the proposed single regulatory authority should be empowered to regulate all activities carried on within the financial

services industry of Mauritius. In this regard and as a first step, it must as a priority bring under regulatory and supervisory oversight all financial sector activities which are currently being carried on in Mauritius without regulation and supervision.

### ***Objects of the Single Regulatory Authority***

6.9 The main objective of the single regulatory authority should be to ensure that the investor/consumer receives adequate protection in his dealings with providers of financial services: -

- (i) at the macro level, the single regulatory authority has to ensure the soundness and stability of the country's financial system;
- (ii) at the micro level, the single regulatory authority has to provide a framework for adequate disclosure by providers of financial services and companies whose securities are traded publicly such that the investor/consumer has timely and adequate information to make investment decisions; and
- (iii) at the level of the consumer of financial services, the system should provide for quick-dispute settlement (e.g. a financial ombudsman) to guarantee that customers receive a fair, reasonable and equitable treatment from providers of financial services as well as expeditious resolution of disputes.

### ***Functions of the Single Regulatory Authority***

6.10 The single regulatory authority will have the following main functions:

- (i) to ensure that the proper regulatory framework exists to promote the development of the financial services industry and a world class financial centre in Mauritius;
- (ii) to license and supervise all business activities that shall be deemed to be financial service activities;
- (iii) to integrate the various sectors of the financial service industry into one harmonised, efficient and competitive industry;
- (iv) to work in close collaboration with the supervised institutions;
- (v) to act in anticipation of developments so as to position Mauritius to respond to new challenges and take full advantage of new opportunities in terms of economic development and job creation; and
- (vi) to advise on any matter relating to the financial services sector.

### ***Powers of the Single Regulatory Authority***

6.11 The Committee is of opinion that a single regulatory authority should be established which should have regulatory and supervisory responsibility over the entire financial industry. The legislative framework should include, among other measures, the following powers:

- (i) to declare any new activity that it deems to be a financial service a regulated activity;
- (ii) to license, regulate and supervise all providers of financial services;

- (iii) to issue standards and guidelines to the industry on various matters to ensure the soundness of the financial system and its participants, including risk management standards, disclosure requirements and corporate governance;
- (iv) to impose fines and penalty to enforce compliance with regulations; and
- (v) to collect such licensing and other fees from operators as may be determined by it from time to time.

### ***Structure of the Single Regulatory Authority***

6.12 Three options were examined by the Committee in achieving the objective of integrated financial supervision, as follows:

1. A separate Financial Services Authority be established immediately that would encompass all the licensing, regulatory and supervisory bodies, both banking and non-banking, under one roof.

2. A Financial Services Authority encompassing all non-bank financial services be immediately established under one umbrella while banking supervision would remain under the purview of the Bank of Mauritius.
3. A Financial Services Authority be established as under Option Two with a view to also integrate with it the supervision of banks eventually.

### ***Evaluation of Options***

6.13 Regarding Option One, the Committee was of the view that it was not a practical solution compatible with the Mauritius situation. This was so because the Mauritius financial industry does not have the coherent long-standing track record and reputation as well as established market practices evolving along the lines of a self-regulatory environment which would be compatible with this option. In addition, the financial industry in Mauritius does not possess the vast array of skills and historical networking which would make such an institution viable. Members nevertheless considered that it was of strategic importance for Mauritius to immediately have an internationally credible regulatory authority as a platform on which to base the further development of its financial industry. It was argued that it would take much time for the proposed new authority under this option to acquire the necessary international recognition and become fully geared to the highly demanding task on hand. It will also take far too long to become effective and efficient, given the absence of a long-standing reputation and international contacts which such a body should have. Further, such a body will not have the hard core of recognized supervisory practices to support itself.

6.14 Regarding Option Two, the Committee was of the view that this option would not meet the consensus view that Mauritius would be best served by a

single regulatory and supervisory authority. Members evaluated that Option Two would also not be cost effective and may end up perpetuating the prevailing situation in which there are unacceptable divergences in the levels of regulation and supervision applied to operators in distinct areas of the financial sector, even though this option was appealing from a practical point of view in the current circumstances.

6.15 The Committee examined the implication of Option Three and agreed that this was the correct platform on which to launch the single regulatory authority for Mauritius. However, it was of the opinion that it should be the Bank of Mauritius which should be the anchor of the system towards which the supervision of all other financial sector activities should gravitate within a given time frame. This will amount to building up the single authority around a firmly grounded regulator and supervisor. Accordingly, the Bank of Mauritius would become the nucleus around which the single regulatory authority should be built up. This arrangement will ensure that -

- (i) the existing strong leadership in the area of regulation of the Bank of Mauritius will not be diluted or lost;
- (ii) the strength of the Bank of Mauritius would be used to promote the same high level of supervision throughout the entire non-bank financial services sector;
- (iii) the reputation and recognition that Bank of Mauritius enjoys as a serious regulatory authority among the international financial community would enhance the attractiveness of Mauritius as a recognised financial centre;

- (iv) the one-stop-shop is established to facilitate the tasks of foreign financial institutions setting up operations in Mauritius; and
- (v) there is an appropriate supervisory framework, given the size and present status of the Mauritius jurisdiction.

6.16 In other words, the Committee recommended that Option Three be re-stated as follows:

***Bank of Mauritius will spearhead the integrated supervision of all activities in the financial sector within a given timeframe in a phased manner with a view ultimately to operate as a single unified regulatory authority.***

6.17 To this effect, members made the following recommendations:

- (i) That a Financial Services Commission (FSC) be created, through a Financial Services Development Act, to bring the Insurance Division, the Stock Exchange Commission, the MOBAA and all such activities which may be declared as financial sector activities under one regulatory umbrella.
- (ii) In this context, the FSC will, after the appropriate legislative changes and in a first phase, take over the duties and functions of the Stock Exchange

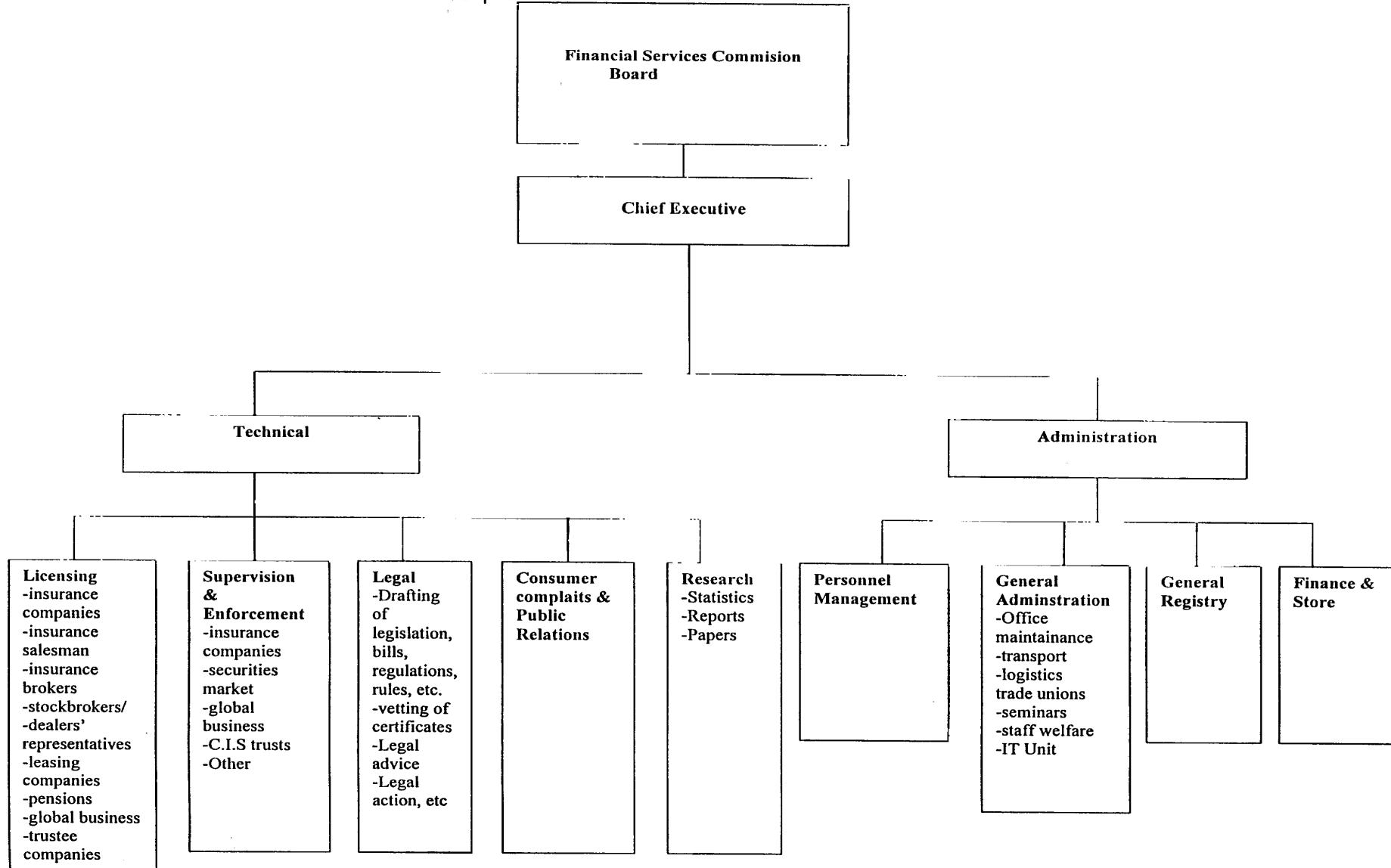
Commission, the Insurance Division and the MOBAA as well as the regulation of all presently unregulated activities in the financial sector. The FSC will be administered and managed by a board chaired by the Managing Director of the Bank of Mauritius.

- (iii) The FSC will facilitate the smooth integration of the offshore and on-shore sectors.
- (iv) It will also be responsible for the protection of the interests of consumers of financial services.
- (v) At the end of the first phase of the integration process, a review exercise will be carried out, taking into account both global and local developments in financial services. In the light of this review, the full integration of the FSC with the Bank of Mauritius into a single unified regulatory authority may be undertaken.
- (vi) That a Financial Services Advisory Council (FSAC) be established with the Minister of Finance and the Minister responsible for Financial Services as Chairperson and Vice-Chairperson respectively. The other members will be the Governor of the Bank of Mauritius, the Chairperson and the Chief Executive of the FSC and six other members from amongst persons of high calibre and of international repute in their relevant fields. The Financial Services Advisory Council will act as a think-tank and serve as a platform for discussions with the aim of giving direction to the development of financial services in Mauritius, based on international trends.

### **Financial Services Promotion Agency**

- (vii) Provisions be made to establish a separate entity to be known as the Financial Services Promotion Agency (FSPA). The FSPA will be the one-stop-shop for the development and promotion of the financial services industry of Mauritius. To that effect, it will work in close collaboration with the Board of Investment to identify areas of growth and target potential institutions to carry on financial activities in Mauritius. The FSPA will devise non-fiscal incentives and make recommendations for fiscal incentives. In addition, the FSPA will develop and implement a human resource plan that would identify the skills needed by the financial services industry and encourage educational and training institutions to provide the training so identified.
  
- (viii) Following the establishment of the FSC, steps should be taken, with external technical assistance as may be necessary, to implement an efficient organizational structure, undertake recruitment and training of personnel and the formulation of clear operating procedures in the conduct of supervision and regulation of the different financial sector activities.
  
- (ix) The FSC, be operated on a functional rather than on a sector-wise basis. To this effect, the proposed organisational chart of the FSC is presented on the next page.

Proposed Structure of the Financial Services Commission



## *Confidentiality*

6.18 The FSC will keep all information gathered during its course of business confidential. It will require all staff to adhere to the same confidentiality requirement as that applied by the Bank of Mauritius.

## *Funding*

6.19 The FSC will be given the power to levy licence fees on an annual basis from all authorized non-bank financial institutions operating in Mauritius to cover all its expenses.

## *Staffing*

6.20 Another important matter is the issue of existing personnel at the many regulatory agencies that would see their functions transferred to the FSC or the FSPA. The Committee recommends that all existing staff be given the choice to join the new FSC or FSPA on terms and conditions that would be determined by the respective bodies, the integration of staff to be carried out in a phased manner at the pace of the setting-up of the two institutions. The Committee believes that the FSC and the FSPA will open new career opportunities for existing staff in the various regulatory agencies and provide opportunities to acquire new skills and knowledge and room for personal growth and development.

6.21 Given the nature and complexity of the task to regulate and supervise the entire financial industry, it is of utmost importance that the FSC is able to attract and retain highly qualified and competent personnel. In this regard, the Committee would like to give the FSC and the FSPA the flexibility to set their own remuneration policy.

6.22 The Committee recognizes that there would be an on-going need for training and development of the staff. Taking into account that supervision world-wide is gravitating more to a risk based approach and encourages market discipline to determine the success or failure of financial institutions, the Committee recommends that the FSC and the FSPA be given the flexibility in matters of training and development of their staff. Some suggested areas for training are risk management and control systems, disclosure standards and practices in major financial centres and working with industry players to keep up to date of new products and developments.

### ***Infrastructure and Logistics***

6.23 The Committee recommends that the FSC be housed in the same premises, as far as is feasible, or share premises with the Bank of Mauritius and uses the existing infrastructure and logistics of the Bank of Mauritius. This is to ensure that there is no duplication of systems, etc. that could become redundant upon the integration of the FSC with the Bank of Mauritius.

### ***Integration of the Offshore with the Domestic Sector***

6.24 The main attraction of Mauritius to companies that want to operate in its offshore sector is the tax treatment of revenues generated by these companies. On the one hand, revenues are subjected to a low tax régime and on the other hand, the tax treaties that Mauritius has signed with many countries, such as India, minimize and, in certain cases, eliminate withholding tax on dividends and capital gains received by these companies in the offshore sector.

6.25 Another attraction is the confidentiality that MOBAA and the Registrar of International Companies currently maintain regarding the beneficial owners and shareholders, clients, customers and employees or officers of certain companies carrying on offshore business activities.

6.26 Developments in international business practices, namely in Europe, are leading towards the reduction of the number of jurisdictions where companies could domicile a subsidiary and/or affiliate for tax avoidance purposes. At the same time, the major developing countries are becoming more serious in their fight against the laundering of money gained illegally or from drug traffic. It is therefore important for Mauritius to establish itself as a recognized international business centre with strict anti-money laundering laws and practices with a view to attracting businesses for reasons other than sheer tax treatment.

6.27 In this regard, steps taken to streamline integration of the offshore sector with the domestic one would help to enhance the reputation of Mauritius as a centre for international business. The Steering Committee feels strongly, however, that, in so doing, Mauritius should take all the necessary precautions to retain those companies that are already operating in the offshore sector and which it would make sense to preserve in the consolidation of the finance industry at this stage of the sector's development.

6.28 Thus, to integrate the offshore banking with the domestic banking sector, two types of banking licences are recommended:

- (1) A full banking licence that would allow a bank to operate branches within Mauritius and carry on transactions in Mauritian Rupees (class A licence);
- (2) A restricted or international banking licence without the facility to operate branches within Mauritius that would allow a bank to operate in Mauritius but engaging in international banking essentially and carrying on transactions in all currencies except the Mauritian Rupee on terms and conditions determined by the Bank of Mauritius. (class B licence).

6.29 Within each class, the authorities would be free to give specific approvals for banks to engage in specialised and approved lines of business, such as private banking, merchant banking , etc., and subject each class of bank to the appropriate supervisory oversight consistent with the practice followed in other identically placed jurisdictions and preserving the competitiveness of Mauritius-based operations.

6.30 Companies holding an offshore business certificate at present would be integrated on the same principles as in the case of banks into the domestic sector

by a change of their status and by a suitable amendment of the law. These companies would be governed by the existing Companies Act but would enjoy certain tax incentives due to the nature of their global activities. As in the case of banks, non-bank financial companies would fall in distinct classes and will be categorised in accordance with the nature of the businesses within each class.

6.31 The Committee feels that companies currently operating with an International Company certificate issued under the International Companies Act 1994 should be integrated into the domestic sector by:

- 1) transferring their registration to the Registrar of Companies;
- 2) bringing them under the provisions of the Companies Act with regard to the disclosure of the names of the beneficial owners and shareholders and enhancing their accountability and transparency.

6.32 Management Companies will, in this regard, be called upon to give the necessary comfort to the regulator and submit, as and when required, such supervisory information on the operations of these companies as may be called up.

### ***Legislative Harmonisation***

6.33 The process of integration of the financial services industry also implies a considerable degree of harmonisation of the core legislation. The creation of the

offshore regime has led to a major dichotomy not only in taxation and orientation of business activities but equally to a differential in the applicable laws. The Schedule to the MOBA Act caused the disapplication of a number of sections of the Companies Act 1984 to offshore companies which has come to be governed by new regulations. The Trusts Act 1989 was restricted in its application to only domestic trusteeships and was not extended to offshore trusts for which again a new Offshore Trusts Act 1992 was adopted. In other areas special legislation was introduced for innovative business trends in the offshore industry. Such an approach highlights the growing chasm that was developing between the domestic and the offshore financial services sectors, exposing Mauritius to increasing attack for the fragmentation of its financial services industry and resulting distortions in the economy.

6.34 It is imperative to reverse this trend. We have over the last decade overcome some of our misgivings about the offshore business and its characteristic flexibility. While keeping a firm grip over an acceptable threshold of transparency, regulation and orderliness, we can draw from our experience in the offshore business to instil in our own domestic laws an appropriate dosage of business-friendliness and simplification that would set off a new momentum to our local business ethos. It would also have the added advantage of allowing international operators to enjoy the facilities and hassle-free environment that they yearn for. The overall consequence is indeed a harmonious blending of the legislation establishing a level playing field and eliminating the unwanted differential between Mauritius residents and non-residents.

6.35 It is recommended that the Companies Act 1984 which takes its inspiration from the very turgid English Companies Act of 1948 be repealed to give way to a simplified form of corporate entities. This exercise is presently

being done and is nearing its final stage. A recent trend in company law has already started in the early 90's in New Zealand, Sri Lanka and other countries. Such a company law may in fact go a long way to answering the expectations of those who were led to espouse the International Companies Act (which is being severely criticised for its unacceptable opacity and looseness). The suggestion has been made earlier in a Ministry of Finance Seminar in 1994. A new Companies Bill is presently under presentation and is expected to be introduced together with the Financial Services Development Bill.

6.36 As regards the trust legislation, the domestic law has been poorly used due mainly to its impractical features. On the contrary, the Offshore Trusts Act 1992 has been quite useful. It is therefore suggested that a single trust legislation be prepared with a combination of features to meet the local Code Civil laws and the offshore mainstream and introduced at the same time as the new Companies Bill.

6.37 It is also suggested that a revision of the Bank of Mauritius Act and the Banking Act be carried out to reflect the changes being proposed.

6.38 With a view to give a concrete shape to the proposals contained in this Section, the next Section sets out a time table for a phased implementation of the establishment of a unified, strong and credible supervisory authority for Mauritius.

## VII

### **Implementation Plan**

*This section identifies the various milestones which will need to be met as a workable proposition in the implementation of the recommendations made by the Committee*

The recommendations made in the preceding Section will take concrete shape under an appropriate sequencing of events. The setting up of priorities is essential when moving from one stage to another. This will typically involve the drafting of legislative provisions in the first place followed by the appointment of executives and thereafter, the framework on which each activity will be consolidated. The annexure graphically depicts the establishment of a proposed timeframe for the implementation of the various recommendations made by the Committee from the presentation of its Report up to the proposed establishment of the single unified regulatory authority.

**Section VII  
Implementation Plan**

Task Name	Jan '01	Feb '01	Mar '01	Apr '01	May '01	Jun '01	Jul '01	Aug '01	Sep '01	Oct '01	Nov '01	Dec '01	Jan '02	Feb '02	Mar '02
Presentation of Steering Committee's Report															
Consideration by Government of the Committee's Recommendations															
Finalisation of the Draft Financial Services Development Bill															
Introduction of the Financial Services Development Bill, the New Companies Bill and the new Trusts Bill in the National Assembly															
Consequential Amendments to the Stock Exchange Act, the Insurance Act, the Protected Cell Companies Act, the Central Depository and Settlement Act and all other Acts where powers are being transferred															
Transfer of the International Companies Registry from MOBAA to Registrar of Companies															
Appointment of members of the Financial Services Commission															
Appointment of the Chief Executive of the FSC															
Drafting of conditions of service of employees of the FSC															
Transfer of the regulatory functions of Mauritius Offshore Business Activities Authority to the Financial Services Commission															
Transfer of the Insurance Division to the Financial Services Commission															
Setting up of the Financial Services Advisory Council															
Setting up of the Financial Services Promotion Agency															
Review of existing Acts and drafting of new legislation															
Transfer of the Stock Exchange Commission to the Financial Services Commission															
Preparation of manuals and issue of guidelines															

## Section VII Implementation Plan

Task Name	Jan '03	Feb '03	Mar '03	Apr '03	May '03	Jun '03	Jul '03	Aug '03	Sep '03	Oct '03	Nov '03	Dec '03	Jan '04
Review exercise in connection with the integration of the FSC and the Bank of Mauritius													
Drafting of the legislative proposal for the setting up of the single unified regulatory authority													
Finalisation of the Bill													
Introduction of the Bill in the National Assembly													
Integration of the Bank of Mauritius and the FSC													
The single regulatory authority operational (15 January 2004)													▲

**Annex**  
**BANK OF MAURITIUS - PRESENT ORGANISATIONAL STRUCTURE**

