INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

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Lisa Pezzack
Director
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Department of Finance
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Dear Ms. Pezzack:

Re: Draft Regulations Amending Certain Regulations Made under the Proceeds of Crime (Money Laundering) and Terrorist Financing Act, 2015 (the "Regulations")

The Investment Industry Association of Canada (the "IIAC") welcomes the opportunity to comment on the Regulations published on July 4, 2015. The IIAC and its members have also welcomed the numerous consultations with the Department of Finance over the last few years concerning proposed amendments. We appreciate that the amendments to the Regulations will further develop an effective anti-money laundering and anti-terrorist regime while at the same time ensure that the requirements do not impose an undue burden on our members as reporting entities.

The Regulations provide positive change for our members by applying more principles-based regulation with less prescriptive requirements, most significantly in the areas of identity verification. However, the IIAC has identified a number of challenges that the new Regulations will pose for our members. We have outlined these challenges as well as some proposed solutions in our responses below.

Measures for Ascertaining Identity and Record Keeping

As mentioned, the IIAC is pleased with broader and more flexible range of reliable and independent sources that reporting entities can use to verify the identity of clients.

The IIAC also appreciates that the Regulations move away from the distinction between face-to-face and non-face-to-face approaches to identity verification, both where the source is seen as sufficiently reliable to use on a single, stand-alone basis, and other sources which require a dual-method approach. Further, under the dual method, the Department of Finance has recognized that there are additional methods to verify identity other than those set out in the previous Regulations and allows reporting entities to consider reliable sources beyond those currently used.

The IIAC welcomes the fact that the intent is for FINTRAC to provide guidance on information that could be considered a "reliable source". In terms of the timing of FINTRAC guidance, however, we note that previously it was frustrating for the industry when FINTRAC guidance was only released on January 31, 2014, just a day before the AML regulations became effective on February 1, 2014. Members firms will need to update systems to accept new methods of identification, and engage in training of both back-office and client-facing staff. If FINTRAC is to provide guidance in respect of this or any other issues, it is critical that such guidance be provided well in advance of this implementation. It is also vital that the industry be given the opportunity to provide input to FINTRAC previous to the release of such guidance.

With respect to the use of a credit file in identity verification, we are particularly pleased to see that a credit file can be used on a stand-alone basis but are disappointed that our recommendation that the required length of credit file be reduced from three years to six months was not included. The requirement that a new customer have a three year Canadian credit file will mean that some individuals, such as those who are new to Canada or students, will not be able to satisfy the requirement nor avail themselves of online account opening. Other countries do not prescribe the length of the credit record that can be used for customer identification purposes and we suggest that it has little bearing on whether the customer is who they say they are.

In addition, the IIAC suggests that clarification be given in order to better define that a credit file should include some credit history, as a credit file could be empty in some cases.

The IIAC also notes that under subsection 64[1.3], information used to ascertain the identity of a client must not include an electronic image of the document. This is somewhat perplexing as many amendments to the Regulations are intended to address the changing online environment, yet the prohibition against electronic images means that a credit card statement or a utility bill that many clients only receive online, would not be an acceptable source of identification.

Further, the Regulations not only require that a firm refer to information from a reliable source but also verify the name, address and/or date of birth of the person. The IIAC is of the view that verification would not require another piece of identification to verify the first source, and that comparing information provided by the client verbally with the information in the identification would amount to verification.

The IIAC also seeks clarification regarding the record keeping requirements under section 64.2. For example, paragraph 64.2(a) requires that a member include in its records for an identification document "the issuing authority and, if available, the place it was issued and its expiry date." We would like to highlight that current member systems do not provide for any entry of an expiry date and this system build would be a significant cost for firms. In addition, we request clarification regarding what is meant by an "issuing authority" and the "place" it was issued. Are we referring to a country, city or province? What is the issuing authority for an Ontario driver's license? Is it the province of Ontario? Is it Service

Ontario or the Ministry of Transportation? We assume that the issuing authority will be equal to the province, state or country of the government that issued the identification so that in most cases the issuing authority will be the same as the place of issue.

Further clarification is also necessary with respect to the record keeping requirements for electronic signatures such as PINs or voice recordings. While the Regulations now provide that the definition of a signature card includes electronic data, which will facilitate account opening in a non-face-to-face environment, the Regulations fail to outline the information necessary to satisfy the record keeping obligations under section 64.2.

We would also request some further flexibility with respect to identifying the end client related to a power of attorney. If the legal power of attorney documentation is confirmed and identified, then perhaps a lower threshold could be considered for the incapacitated client. In many cases, they would be an elderly individual in a nursing home with no valid driver's license, recent credit file or passport. Perhaps in such situations a single source form of identification could be employed from those listed under the dual source method?

The IIAC does welcome the ability to rely on an affiliated entity who has previously ascertained the client's identity as well as the ability to rely on identification verification previously undertaken by an agent or mandatary, subject to certain conditions. This will greatly assist many firms in our industry. However, with respect to mandataries, we are somewhat concerned with the changes proposed in paragraph 71(1)(d) which would now require that mandataries be subject to the same ongoing compliance training program as those for employees and agents. It seems unduly onerous to expect that member firms provide as comprehensive an AML training program on an annual basis to mandataries as they would for employees. We suggest that the Department of Finance consider some less onerous requirements for satisfying this provision with respect to mandataries.

The IIAC notes that under section 67.3, a person or entity must keep a record that sets out the what reasonable measures were taken and why they were unsuccessful. We find this requirement serves no useful purpose and seems quite onerous to set out the reasons why certain measures undertaken were unsuccessful. As such, we suggest this section be removed. At the very least, should this provision remain, the procedures used by a firm should stand as the record of the reasonable measures taken and not require firms to record any additional information.

<u>Politically Exposed Persons (PEPs)</u>

Under section 57 of the Regulations there is now expansion of certain regulatory requirements that currently apply to foreign PEPs to include domestic PEPs, as well as heads of international organizations or family members of close associates of such persons.

The IIAC is pleased to see that under subsection 67.1(2), the requirements to establish the source of funds, obtain senior management approval and conduct enhanced ongoing monitoring of the activities of the account would only apply to domestic PEPs, heads of international organizations, their family members and close associates if there was judged to be a high risk of a money laundering or a terrorist activity financing offence. The fact that a person is a domestic PEP or one of the other listed categories, would not in itself trigger the enhanced measures, allowing firms instead to conduct their own risk assessments. However, with respect to requirements on account opening, members are required to

take reasonable measures to determine whether the account is for a domestic or foreign PEP, head of an international organization, a family member or a close associate of a foreign PEP.

These new provisions also extend to taking reasonable measures on a "periodic basis" to make this determination. Such requirements will require the building of systems and development of new processes and procedures for firms in order to ensure compliance. Currently, firms do not "screen" for domestic PEPs, heads of international organizations, family members or close associates of PEPs. It is unclear what would satisfy the requirement to "take reasonable measures."

New requirements under subsection 57(3) will require that if a firm detects a fact that could reasonably be expected to raise reasonable grounds to suspect that a person who is an existing account holder is a foreign or domestic PEP, a head of an international organization or a family member or a person who is closely associated with any one of those persons, the firm must take reasonable measures to determine whether the accountholder is such a person.

It could be quite difficult for firms to determine whether an individual is such a person and as such, it would be useful for FINTRAC to provide clear guidance as to what constitutes "reasonable grounds" as this will require significant monitoring procedures and systems requirements for firms. Is simply asking the question sufficient?

In addition, especially given the enhanced measures under subsection 67.1(1) that would apply to foreign PEPs or a family member or person who is closely associated with such a person, a definition of what a "close associate" is would be extremely helpful.

In most instances, many individual clients will not even know if they are a close associate of a PEP and member firms need some guidance as to what it means and how to make this determination. In the United Kingdom, for example, under the Joint Money Laundering Steering Committee's *Guidance for the UK Financial Sector, Part 1* a close associate is defined to include:

- any individual who is known to have joint beneficial ownership of a legal entity or legal arrangement, or any other close business relations, with a person who is a PEP; and

- any individual who has sole beneficial ownership of a legal entity or legal arrangement which is known to have been set up for the benefit of a person who is a PEP.

The Guidance goes on to state:

> For the purpose of deciding whether a person is a known close associate of a PEP, the firm need only have regard to any information which is in its possession, or which is publicly known. Having to obtain knowledge of such a relationship does not presuppose an active research by the firm.[1]

Further, the IIAC suggests that a clear definition of "international organization" would be useful.

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[1] See **http://www.jmlsg.org.uk/industry-guidance/article/guidance**; Paragraphs 5.5.23 and 5.5.24.

We would also suggest that consideration be given to reduce the prescribed time that a client's status as a domestic PEP or head of an international organization ceases from the 20 years currently required under subsection 1.1(2) of the Regulations to a shorter time frame such as five years, given the extensive burden and ongoing monitoring that is required.

The IIAC is pleased to note that the amendment to subsection 67.1(3) of the Regulations to extend the timeframe from 14 to 30 days for making a determination for a PEP or head of an international organization and any necessary due diligence measures. This longer time frame is much more reasonable for adherence by the industry.

Implementation Timelines

The IIAC supports the one year delay for the coming into force of new requirements in the Regulations such as the new PEP requirements, risk assessments and provisions related to reasonable measures. Although we welcome the attempt by the Department of Finance to allow firms to immediately implement the more flexible identification methods upon registration of the Regulations, this time frame will be overly ambitious for many firms to comply with given the time it will take from a development standpoint relating to the systems changes necessary to capture the new acceptable sources of identification as well as preparing new compliance procedures and amendments to existing client forms. As such, we would suggest that for these provisions the Regulations refer to an effective date which could occur immediately upon registration of the Regulations but also allow for a one year implementation date for firms to make the necessary changes internally.

Suspicious Transaction Reporting

Under the Suspicious Transaction Reporting Regulations, we note a change made to subsection 9(2). The change inserts a new requirement that requires reporting when a fact is detected ***that could reasonably be expected to raise*** reasonable grounds to suspect that the transaction or attempted transaction is related to the commission of a money laundering offence or a terrorist activity financing offence. This language represents a significant change from the previous requirement that requires reporting of a fact that "constitutes reasonable grounds" to suspect.

The IIAC is of the view that the addition of this language lowers the threshold for entities to report suspicious transactions and could result is over-reporting of transactions in order to ensure that anything that may be seen as "reasonably expected to raise reasonable grounds" is reported. In addition, the language seems to suggest that reporting would occur far earlier than what presently occurs where the entity has a fact that constitutes reasonable grounds. Instead, under the proposed Regulations, the entity would have to file a report if a fact might be expected to raise reasonable grounds in the future. We recommend that this new language be removed.

Proposed Amendments not Addressed in the Regulations

The IIAC wishes to point out a number of provisions that we understood were to be amended, which were either outlined in the December 2011 Consultation Paper and/or stakeholder consultations with the Department of Finance in 2014, have not been included in the proposed Regulations. We hope to see these amendments included in subsequent regulatory packages that the government indicated will be forthcoming in the future.

Removal of the $75 Million Asset Requirement

Under paragraph 62(2)(m) of the Regulations, reporting entities are not required to ascertain identity or to keep records when conducting transactions with pubic bodies or corporations with a minimum of $75 million net assets whose shares are traded on a Canadian or other designated stock exchanged. The IIAC has argued in the past that the $75 million test should be removed given that listed corporations whose shares trade on a Canadian stock exchange or a stock exchange designated under subsection 262(1) of the *Income Tax Act*, and operates in a country that is a member of the Financial Action Task Force, are subject to stringent listing, reporting, transparency and other regulatory requirements. Disclosure regarding listed companies is readily available through SEDAR, EDGAR or equivalent regulatory sources, stock exchanges, news wires and other public media sources. As a result, the current $75 million monetary threshold has little or no relevance and should be removed from the exemption for designated listed companies set out in Section 62(2)(m) of the Regulations.

Exemption from Ascertaining Identity of Authorized Signers

For numerous years, the IIAC has recommended that any regulatory amendments incorporate an exemption for authorized signing officer verification of foreign public bodies. Canada is not aligned with the United States or the EU by requiring signing officer identification for these clients.

Insofar as foreign public bodies are concerned, reporting entities need to ensure that they mitigate, and monitor for, the risk of corruption. Verifying the identity of authorized signing officers of accounts owned by foreign pubic bodies does not mitigate corruption risk and refraining from doing so does not increase the risk. Consequently, we are of the view that it is critical that foreign public bodies be included in the list of entities for the purpose of exemptions from signing officer identity verification.

The underlying rationale for exemptive relief currently contained in subsection 62(2) for Canadian regulated entities is, at least in part, due to the regulatory oversight of these entities provided by a government regulatory body or an industry-specific self-regulatory organization. They are already subject to significant registration requirements, disclosure, audit and reporting obligations and enhanced regulatory scrutiny of their business conduct and operations. Foreign regulated entities that are subject to similar regulatory regimes in their home jurisdictions should be eligible for comparable exemptive relief under the Regulations.

As the IIAC has outlined in earlier submissions, where a securities dealer outside of Canada opens an institutional account for a Canadian regulated entity, it is not required to obtain copies of corporate documents and identity information regarding authorized officers, nor is it required to verify such identity information through face-to-face meetings with its employees or agents or other means. Foreign dealers are permitted to rely on information posted on SEDAR, EDGAR, and other government and regulatory sources and public databases in conducting due diligence in order to satisfy AML concerns relating to identity and record-keeping. As a result, when our members ask a foreign regulated entity for its corporate documents and detailed information and for a face-to-face verification meeting, many of these entities balk at the request, electing instead to take their business elsewhere because of the inconvenience to them. They can easily

open an institutional account with a SEC or FSA registered securities dealer, for example, without similar onerous requirements.

Our purpose in seeking the proposed amendments to subsection 62(2) is to address this disparity and to enable our members to compete more effectively and on an equal footing as other securities dealers in the global capital markets for foreign investments from foreign regulated entities.

Thank you for considering our submission. The IIAC would be pleased to respond to any questions that you may have in respect of our comments.

Yours sincerely,

M. Alexander