
FATF MUTUAL EVALUATION OF CANADA'S ANTI-MONEY LAUNDERING MEASURES

*By Nancy E. Claridge and Terrance S. Carter**

A. INTRODUCTION

In a report entitled “6th Follow-Up Report: Mutual Evaluation of Canada” released on February 17, 2014 (the “2014 Mutual Evaluation”),¹ the Financial Action Task Force (“FATF”) praised Canada for making “significant progress” in addressing deficiencies in its anti-money laundering and anti-terrorist financing regime. These deficiencies were raised in 2008 in FATF’s Third Mutual Evaluation on Anti-Money Laundering and Combating the Financing of Terrorism for Canada (“2008 Mutual Evaluation”).² As a result of the “significant progress”, the 2014 Mutual Evaluation recommends removing Canada from the FATF’s regular follow-up process, which has required Canada to undergo annual FATF audits. This *Anti-terrorism and Charity Law Alert* provides a summary of the findings and recommendations in the 2008 Mutual Evaluation and 2014 Mutual Evaluation.

B. THE 2008 AND 2014 MUTUAL EVALUATIONS

The FATF employs a peer-evaluation process to monitor member-state compliance with the FATF Recommendations, a set of 40 recommendations that provide counter-measures against money laundering. The 2008 Mutual Evaluation raised concerns with Canada’s anti-money laundering and anti-terrorist financing legislation, particularly regarding legislative requirements in key areas. Accordingly, it found

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¹ FINTRAC, *6th Follow-Up Report: Mutual Evaluation of Canada*, February 17, 2014, online: <http://www.fatf-gafi.org/media/fatf/documents/reports/mer/FUR-Canada-2014.pdf>

² FINTRAC, *Third Mutual Evaluation on Anti-Money Laundering and Combating the Financing of Terrorism for Canada*, February 29, 2008, online: <http://www.fatf-gafi.org/media/fatf/documents/reports/mer/MER%20Canada%20full.pdf>

that Canada was not in full compliance with a number of FATF Recommendations, most notably Recommendations 5, 23 and 26.

However, the tone in the 2014 Mutual Evaluation was markedly different from the 2008 Mutual Evaluation, and praised Canada for the “significant improvement” on its level of compliance with the FATF Recommendations. Although the 2008 Mutual Evaluation deemed Canada to be only partially compliant with Recommendations 23 and 26, significant progress was made by the February 2009 follow-up process, and Canada was found to have reached an adequate level of compliance. However, at that time, Canada was deemed to remain non-compliant with Recommendation 5. Canada has since attempted to be in compliance with Recommendation 5.

Particularly, the 2014 Mutual Evaluation noted that key measures taken by Canada to comply with the Recommendations included:

- Adapting the legal framework with key measures in the fields of Customer Due Diligence through amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (“PCMLTFA”) and the *Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations* (“PCMLTFR”), in particular with measures in relation to the circumstances in which customer due diligence has to take place, enhanced due diligence and ongoing due diligence;
- Strengthening its Financial Intelligence Unit, Financial Transactions and Reports Analysis Centre of Canada (“FINTRAC”), with additional resources and by reinforcing its compliance programme with a new range of administrative sanctions. Implementing a federal registration regime for money service businesses; and
- Expanding the anti-money laundering and anti-terrorist financing regime to additional Designated Non-Financial Business and Professions, in particular, British Columbia Notaries and dealers in precious metals and stones.³

³ FINTRAC, “Canada – Mutual Evaluation of the Canada: 6th Follow-up Report”, online at: <http://www.fatf-gafi.org/countries/a-c/canada/documents/fur-canada-2013.html>

The following commentary provides an overview of a select number of the key deficiencies identified in the 2008 Mutual Evaluation and the steps Canada has since taken to address these deficiencies, as discussed in the 2014 Mutual Evaluation.

C. RECOMMENDATION 5 – DUE DILIGENCE AND RECORD-KEEPING

1. The 2008 Mutual Evaluation

Recommendation 5 falls under the general heading of “Measures to be taken by Financial Institutions and Non-Financial Businesses and Professions to Prevent Money Laundering and Terrorist Financing.” More specifically, it addresses customer due diligence and record-keeping, establishing that financial institutions should not keep anonymous accounts or accounts in obviously fictitious names and providing instances when financial institutions should verify the identity of their customers, including when there is a suspicion of money laundering or terrorist financing. Recommendation 5 further provides four specific customer due diligence measures to be taken. In this regard, Canada was found to be non-compliant, as the following key issues were found:

- Financial institutions were neither required to understand their customer’s ownership and control structure nor to identify the natural persons ultimately owning or controlling the customer;
- Enhanced due diligence for higher-risk customers was not required;
- There were insufficient customer due diligence requirements, as well as too many exemptions for performing customer due diligence; and
- With one exception, there were no requirements to conduct ongoing due diligence, including identifying customers for large cash transactions and electronic fund transfers.

2. The 2014 Mutual Evaluation

Since the 2009 follow-up process, Canada has made amendments to the PCMLTFR. The 2014 Mutual Evaluation states that these amendments “significantly improve Canada’s level of compliance with Recommendation 5.” The updates to Canada’s legislation, described below, were entered into law on January 31, 2013 and came into effect on February 1, 2014.

Section 11.1 (1) and (2) of the PCMLTFR were amended to strengthen third party determination and identification of beneficial owners, and now require financial entities, securities dealers, life insurance

companies and life insurance brokers or agents to identify and confirm the accuracy of all corporate directors and anyone owning 25% or more of a corporation's shares, trustees and beneficiaries of a trust, and anyone owning or controlling 25% or more of a non-corporate entity.

Additionally, section 71.1 was modified to require enhanced due diligence and risk-mitigating measures when faced with higher risk categories customers, business relationships and transactions identified by a risk assessment under section 9.6(2).

While section 9.6 of the PCMLTFA has contained customer due diligence obligations regarding transactions, products and customers since the 2008 Mutual Evaluation, the new section 62(5) of the PCMLTFR came into force on February 1, 2014 and creates further customer due diligence obligations and provides that the exemptions to customer due diligence found in sections 62(1)-(3) do not apply in particular circumstances.

The amendments also introduced new sections 54.3, 56.3, 57.2, 59.01 and 61.1, which require specific financial institutions to conduct ongoing monitoring of their business relationships and keep records of measures taken and information obtained from the monitoring. Conducting ongoing monitoring includes conducting ongoing due diligence and ensuring that customer due diligence information is always up-to-date.

D. RECOMMENDATION 23 – REGULATION AND SUPERVISION OF FINANCIAL INSTITUTIONS

1. The 2008 Mutual Evaluation

Recommendation 23 falls under the same general heading as Recommendation 5 regarding anti-money laundering and anti-terrorist financing measures, and addresses more specifically the regulation and supervision of financial institutions. This regulation and supervision is targeted at ensuring that financial institutions are implementing the FATF Recommendations.

In this regard, Canada was found to be partially compliant, with the following key issues identified:

- Certain financial sectors were excluded from the anti-money laundering and anti-terrorist financing regime without proper risk assessment;

- Financial institutions subject to the PCMLTFA saw an unequal level of supervision for anti-money laundering and anti-terrorist financing compliance, with insufficient control over certain bodies;
- The “fit and proper” requirements for market entry were not comprehensive, with no specific obligation for federally regulated financial institutions to implement screening procedures for employees or Board members; and
- There was no registration regime for money service businesses.

2. The 2014 Mutual Evaluation

While the 2009 follow-up process effectively stated that Canada had sufficiently implemented and complied with Recommendations 23 and 26, it recommended continued monitoring of its progress. The 2014 Mutual Evaluation found that factoring and leasing companies remained excluded from the anti-money laundering and anti-terrorist financing regime, although there is a possibility that they meet the “proven low risk” threshold. Additionally, other sectors continue to remain excluded, though the 2014 Mutual Evaluation states that there is a “relatively minor set” of such sectors.

Concerning the unequal level of supervision, Canada was found to have largely addressed this by strengthening FINTRAC’s compliance staff for supervising reporting entities. Additionally, Canada addressed the registration regime for money service businesses by creating a federal registration regime and requiring money services businesses to register with FINTRAC. However, Canada was found to not have taken any further action regarding the “fit and proper” requirements for market entry.

E. RECOMMENDATION 26 – ESTABLISHING A FINANCIAL INTELLIGENCE UNIT

1. The 2008 Mutual Evaluation

Recommendation 26 falls under the general heading of “Institutional and Other Measures Necessary in Systems for Combating Money Laundering and Terrorist Financing” and recommends that member-states establish a financial intelligence unit to receive, analyse and disseminate suspicious transaction reports and other information regarding potential money laundering and terrorist financing activity.

In this regard, Canada was found to be partially compliant, with the following key issues identified:

- As Canada's financial intelligence unit, FINTRAC did not have sufficient access to financial information and intelligence from authorities and reporting entities
- FINTRAC was understaffed in the area of analyzing potential money laundering and terrorist financing situations
- Very few convictions resulted from FINTRAC's disclosure of financial intelligence.

2. The 2014 Mutual Evaluation

As stated above, the FATF recommended continued monitoring of the progress of Canada's compliance with Recommendation 26. As such, the 2014 Mutual Evaluation made some observations in this regard. Canada was found to have substantially addressed FINTRAC's access to financial intelligence by expanding connections with law enforcement authorities and providing it with indirect access to the CSIS database. Additionally, although FINTRAC is constitutionally prohibited from retrieving additional information from reporting entities on previously filed suspicious transaction reports, an information sharing mechanism has been implemented to improve the quality of information provided by reporting entities and to reduce the need for additional information from suspicious transaction reports.

Canada also addressed FINTRAC's problem with understaffing by hiring more employees and, through doing so, has doubled its analytical capacity despite a sharp increase in suspicious transaction reports received. Regarding the low number of convictions, the 2014 Mutual Evaluation found that FINTRAC intelligence was used in the investigation of money laundering and terrorist financing. However, it was unable to review the extent to which this intelligence was used in investigations, and found no information on convictions. Nonetheless, it concluded that the issue had been partially addressed.

F. CONCLUSION

The 2014 Mutual Evaluation is a welcomed report that shows that Canada is sufficiently in compliance with FATF Recommendations 5, 23 and 26. While the 2014 Mutual Evaluation indicates that there continue to be a number of deficiencies, the amendments undertaken by Canada since the 2008 Mutual Evaluation have brought significant changes to Canada's anti-money laundering and anti-terrorist financing regime. These changes, according to the 2014 Mutual Evaluation, warrant removing Canada from the FATF's regular follow-up process involving annual audits. Each of these changes is an improvement in this realm, and should lead to greater effectiveness in Canada's anti-money laundering

and anti-terrorism financing as Canada continues to address its deficiencies and to comply better with the FATF Recommendations.



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