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Diane Lafleur
Director, Financial Sector Division
Department of Finance
140 O'Connor Street
Ottawa, Ontario
K1A 0G5

Dear Ms. Lafleur:

Re. Proposed Regulations Amending Certain Regulations Made Under the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*

Advocis appreciates the opportunity to provide its comments to the Department of Finance on the Federal Government's proposed *Regulations Amending Certain Regulations Made Under the Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (the "Regulations").

Advocis, the Financial Advisors Association of Canada, is a national professional association that is committed to preparing, promoting and protecting financial advisors in the public interest. We do this by providing a professional platform including career support, designations, best practices direction, education, timely information and professional liability insurance. This strengthens the relationship of trust and respect between financial advisors and their clients, the public, and Government. Advocis is Canada's oldest and largest voluntary professional membership association of financial advisors representing life and health insurance licensees, and mutual fund and securities registrants across the country.

We agree with the Government that it is vital to ensure that Canada's anti-money laundering and terrorist financing regime is in line with international standards in combating money laundering and terrorist financing activities and maintaining the credibility and soundness of our financial system. According to the *Regulatory Impact Analysis Statement* released with the proposed Regulations, the new requirements will integrate the level of money laundering or terrorist financing risks in Canada with existing business practices in the sectors covered by the Act in order to balance the objective of achieving international standards without diminishing competition in the financial sector while minimizing the compliance burden of reporting entities. We commend the Government for taking this balanced approach. It is within this context that we offer our comments on the proposed Regulations.

Advocis has participated throughout the Government's consultation process to amend the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (the "Act") under Bill C-25, and wishes to ensure that the proposed Regulations achieve their objectives. Anti-money

laundering and anti-terrorist financing legislation and regulations apply to financial advisors to the extent that they operate as insurance brokers or agents and persons authorized to engage in the business of dealing in securities.

The proposed amendments to the Regulations enhance significantly client identification and transaction reporting requirements of financial intermediaries. The Government rightly recognizes that the implementation of these enhanced due diligence measures will require financial institutions and intermediaries to devote substantial resources to ensure that sufficient compliance systems are established under the Act and proposed Regulations.

However, in many instances, new requirements to develop internal policies and procedures, provide appropriate training, assess money laundering and terrorist financing risks and change information technologies will apply equally to large financial entities and to financial intermediaries, many of whom operate as small businesses or even sole proprietorships. As a result, while large financial entities processing huge volumes of financial transactions would face high absolute costs, small financial intermediaries such as independent insurance and investment advisory firms will be facing disproportionately higher costs per client or transaction. The reason for this is that large entities have the benefit of economies of scale and information systems that can integrate new requirements much more cost effectively. It is important then to ensure that the proposed Regulations do not unintentionally create undue burdens on small financial advisory firms.

Attempted Suspicious Transactions

The proposed Regulations under subsections 11 (a) through (j) integrate the concept of an attempted transaction into the anti-money laundering and terrorist financing regime, which, in our view, constitutes a significant change in the way reportable activities are defined. This will undoubtedly result in significantly more transactions being reported. Furthermore, subsection 9(1) of the proposed amendments to the Regulations would require all reporting entities to obtain information on their clients whenever they have *reasonable grounds to suspect* that a transaction or suspicious attempted transaction is linked to money laundering or terrorist financing activities. Under subsection 52.1(1), these provisions would not apply if obtaining such information would alert the client that the reporting entity is filing a report, which is a welcome relaxation of the rule as originally proposed. However, the reporting entity, which had already ascertained the identity of the client or potential client prior to the suspicion, would have to ascertain the identity again if there is any doubt about the authenticity of the information collected. This could create additional undue costs for small financial advisors. Therefore, it is extremely important to establish well defined parameters for what constitutes *"reasonable grounds to suspect"* that a transaction or suspicious transaction is linked to illegal activities.

It is our understanding that compliance with these new requirements would be supplemented by the publication of sector-specific guidelines on what constitutes a suspicious attempted transaction. We are encouraged that the Government will be providing guidance to reporting entities to assist them in determining when to report attempted transactions. This is important, especially under certain circumstances where little if any client information may be obtainable. For example, advisors often meet clients for the first time, as they seeking some initial financial advice or guidance. This may not result in a transaction. Moreover, the client may not retain the services of the advisor in an official capacity through a signed letter of engagement at that time. A significant amount of information pertaining to the client is often only obtained when the client approves an initial transaction with a financial advisor. Therefore, it would be

extremely important to establish guidelines to outline specific sets of circumstances and timing regarding what constitutes an attempted transaction. In addition, any sector specific guidelines such as within the insurance or investment industries should be developed in consultation with all key stakeholders within the respective distribution channels. Financial advisors have the most direct links with consumers and bring a unique perspective to the transaction process in the provision of financial products and services to the Canadian public. We urge the Department of Finance and the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) to work with financial advisors to ensure that industry specific guidelines are developed in such a way as to reflect this unique perspective. Advocis would be pleased to assist in the facilitation of an exchange of information in this regard.

Assessing Risk

The proposed Regulations build on the obligations outlined in Bill C-25 requiring all reporting entities to conduct an assessment of the money laundering and terrorist financing risks in the course of their business activities. This would entail reporting entities to take reasonable measures, where it is determined that a client represents a higher risk, taking into account the type of customer, the type of product, the delivery channels, geographic location, and other such key factors. The purpose of this would be to conduct ongoing monitoring of the transactions and to keep client information up to date. In addition, the risk assessment and the compliance policies and procedures that reporting entities are required to implement would have to be reviewed at least every two years.

Advocis wishes to ensure that appropriate guidelines are established for intermediaries within each of the main distribution channels for the insurance and investment industries. Some financial advisors operate under an employer-employee relationship model within vertically integrated financial entities, while others are independently contracted advisors. The differences in financial services distribution networks need to be taken into consideration when developing regulations and guidelines to ensure that guidelines are applied appropriately and ensure a level playing field exists between different distribution channels within the same sector.

Low Risk Situations

Advocis applauds the Government for identifying a significant number of low risk situations and for recognizing these situations in the form of exemptions within the Regulations. Section 62 of the proposed Regulations introduces new product, transaction and activity exemptions to the client identification and record-keeping requirements in low-risk situations of particular relevance to financial advisors, including:

- Subsection 62(1) exempts low-risk activities such as the sale of mutual funds for which an account has been opened or the transaction is part of a series of transactions that includes a sale in circumstances where the mutual fund advisor has reasonable grounds to believe that the identity has been ascertained by a securities dealer;
- Subsections 62(2) exempts a number of low risk insurance transactions; and
- Under subsection 62(3), reporting entities would no longer have to ascertain the identity of the members of a group plan if the contributions are made by means of payroll deductions.

As part of its ongoing review of the Act and the Regulations in the future, we encourage the Government to continue to work with the industry to determine what other activities or

transactions pose relatively low risks and to add those situations from time to time to the list of currently proposed exemptions.

The Regulations also identify circumstances where insurance brokers or agents are not required to ascertain the identity of clients. Specifically, subsection 56(2) does not require a life insurance broker or agent to ascertain a person's identity where there are *reasonable grounds* to believe that the person's identity has already been ascertained by another life insurance company, broker or agent. We are pleased that our recommendation concerning this type of low risk situation has been given serious consideration. While agents and brokers deal directly with clients, and maintain client information, insurance companies approve insurance policy applications and maintain detailed client information as a matter of policyholder approval. Therefore, requiring brokers or agents to maintain the level of detailed client information does little to enhance safeguards to the anti-money laundering tracking system. In developing the new guidelines, and specifically outlining what constitutes "*reasonable grounds"* to believe that identity has already been ascertained, we believe that the information obtained by insurance companies and securities dealers in the policy approval and investment verification process, respectively, should be sufficient thus relaxing the requirement of the intermediary to ascertain client information in those circumstances.

Information on Directors and Partners of Corporations

Under the proposed amendments, customer due diligence standards would be strengthened. According to Subsection 11.1(1) of the proposed amendments, some reporting entities would have to take additional steps when entering into a business relationship with an entity. Financial entities, securities dealers, life insurance companies, life insurance brokers and agents would have to take *reasonable measures* to obtain information on directors or partners of a corporation or other entity or on persons who own or control 25% or more of that corporation or entity.

Furthermore, in response to the evolving technologies used to deliver financial products and services, new methods to ascertain the identity of a person in a non-face-to-face environment would be made available to all reporting entities. These methods include the use of third-party sources such as credit bureaus and agents. Financial advisors routinely gather and obtain a significant amount of vital information pertaining to their clients before making recommendations on appropriate financial products and services in meeting clients' needs. In developing the guidelines on methods of verifying this type of client information and information required in other parts of the proposed Regulations, we encourage the Government to seriously take into consideration the relatively limited capability of small independent financial advisors to undertake in-depth verification activities in finalizing the Regulations and developing guidelines. We urge the Government to consult directly with the financial advisor community to determine the challenges facing small and medium-sized operations to incur such costs.

Politically Exposed Foreign Persons

Financial entities, securities dealers, life insurance companies, life insurance brokers and agents would have to determine whether purchasers of insurance, account holders or persons sending large electronic fund transfers or making large payments are *politically exposed foreign persons* (as defined in subsection 9.3(3) of the Act) and, if so, conduct enhanced scrutiny of such transactions and of their business relationships with such clients. For example, subsection 20.1 defines the type of information that must be kept on record in the

case where a *politically exposed foreign person* purchases an immediate or deferred annuity or a life insurance policy for which the client may pay $10,000 or more over the duration of the annuity or policy, regardless of means of payment.

We encourage the Government to provide further guidance on complying with these requirements, especially where verification of information is required and in attempting to ascertain sources of funds. Moreover, establishing management systems to monitor ongoing business relationships can be onerous for individual financial advisors and smaller financial advisory firms. In devising regulations and guidelines, it is important to take into account the challenges faced by financial advisors in complying with onerous reporting and monitoring systems, compared to the capacity and wherewithal of larger financial institutions to comply.

Conclusion

Advocis would appreciate the opportunity to provide the Government with further insights into the operational challenges facing small independent financial advisors as it and FINTRAC develop its guidelines that will eventually accompany the final Regulations.

We believe that building awareness of regulatory obligations with respect to the Proceeds of Crime (Money-Laundering) and Terrorist Financing Act and Regulations will be a crucial component to ensure widespread compliance. For its part, Advocis is in the process of developing a new section in its Best Practices Manual relating to the amended Act and Regulations and, once finalized, will be promoting the new material to all of its members. In addition, we have developed a comprehensive Continuing Education module, which will be rolled out once the final Regulations are in place. These programs will reach thousands of financial advisors across Canada through our network of 48 Chapters. We would like to work closely with FINTRAC to ensure that the guidelines being produced reflect the business realities of financial advisors, and to ensure that the regulators' expectations are being met.

We look forward to working with the Department of Finance and FINTRAC in developing an appropriate set of anti-money laundering and anti-terrorist financing guidelines to assist in meeting its objective of being at the forefront in the global fight against these crimes and in improving public safety in Canada and worldwide.

Sincerely yours,