MEMBER REGULATION

INVESTMENT DEALERS ASSOCIATION OF CANADA

notice

ASSOCIATION CANADIENNE DES COURTIERS EN VALEURS MOBILIÈRES

Contact:
L. Boyce: (416) 943-6903 – lboyce@ida.ca

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Revised *Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations*

New Regulations pursuant to the *Proceeds of Crime (Money Laundering) and Terroris*
There are three principal parts:

1. The Regulations make a number of changes to the current client identification and verification requirements which come into effect on June 12, 2002. These are:
   - the addition of third party determination requirements with exceptions;
   - revisions to the identification and verification requirements for individual accounts, including changes to exceptions;
   - additional requirements for identification of corporate and other non-individual accounts, including changes to exceptions;
   - a requirement to implement a regime for complying with PCMLTFA and the Regulations
2. The Regulations implement, effective November 30, 2002, a requirement to report to the Financial Transactions Reporting and Analysis Centre of Canada ("FinTRAC") cash receipts in excess of $10,000.
3. The Regulations amend certain provisions of the *Proceeds of Crime (Money Laundering) Suspicious Transaction Reporting Regulations* and renames them the *Proceeds of Crime (Money Laundering) and Terrorist Financing Suspicious Transaction Reporting Regulation* ("the STR Regulations"). The amendments come into effect on June 12, 2002.

In addition, FinTRAC has published revised versions of its Guideline 1: Backgounder (Atttachment B) and Guideline 2: Suspicious Transactions (Attachment C). Further guidelines on submitting reports to FinTRAC, implementing a compliance regime, submitting terrorist property reports, and record keeping and client identification are to be published May 31. Guidelines on large cash transactions and electronic funds transfers are to be published June 30. These will be provided to Members as they become available.

I. Important Definitions

The following definitions in section 1(2) of the Regulations are important in relation to various exceptions:

"financial entity" means:

- a bank to which the *Bank Act* applies or an authorized foreign bank within the meaning of section 2 of the *Bank Act* in respect of its business in Canada[1].
- a cooperative credit society, savings and credit union or caisse populaire that is regulated by a provincial Act or an association that is regulated by the Federal *Cooperative Credit Associations Act*
- a trust or loan company to which the Federal *Trust and Loan Companies Act* applies or that is regulated by a provincial Act
- a department or agent of Canada or a province when it accepts deposit liabilities in the course of providing financial services to the public.

"public body" means:

- any Federal or provincial department or agency
- an incorporated municipal body (city, town, village, township, etc.) or its agent
- an organization that operates a public hospital and is designated by the Minister of National Revenue as a hospital authority under the *Excise Tax Act*.

"securities dealer" is defined to include all provincial registrants including portfolio managers and investment counselors.

II. Third Party Determination

Under section 9(1) of the Regulations, when opening an account, Members must "take reasonable measures to determine whether the account is to be used by or on behalf of a third party." This provision does not apply to financial entities and Canadian securities dealers.[2]

While there is no exemption from making the section 9(1) determination for other parties, there are conditional exemptions, further described below, from having to determine the identity of the third party where the account is being opened for a foreign securities dealer or a legal counsel, accountant, real estate broker or real estate sales representative.

If the account is to be used by or on behalf of a third party, the Member must record the name, address and nature of the principal occupation or business of the third party; the nature of relationship between the third party and the accountholder and, if the third party is a corporation, its incorporation number and place of issue (presumably of the incorporation number)[3].

[1] A list of authorized foreign banks can be found on the Web site of the Office of the Superintendent of Financial Institutions at http://www.osfi-bsif.gc.ca/eng/whoweregulate.asp?s=1&g=1
[2] Section 9(4)
[3] Section 9(2)

There are three forms of exemption from recording third party information for securities dealers "engaged in the business of dealing in securities only outside of Canada[4]."

a) There is no requirement to record third party information if the dealer is in a member country of the Financial Action Task Force ("FATF"). The following (in addition to Canada) are FATF member countries:

Argentina	Finland	Ireland	New Zealand	Switzerland
Australia	France	Italy	Norway	Turkey
Austria	Germany	Japan	Portugal	United Kingdom
Belgium	Greece	Luxembourg	Singapore	United States
Brazil	Hong Kong	Mexico	Spain	
Denmark	Iceland	Netherlands	Sweden	

b) There is no requirement to record third party information if the dealer is in a country that is not an FATF Member but has implemented the FATF recommendations relating to customer identification. However, when the account is opened the Member must obtain from the foreign dealer a written assurance that the country has implemented those recommendations. Members cannot, of course, accept such assurances when the country is on the FATF list of Non-cooperating Countries and Territories ("NCCTs").[5]

c) If the foreign dealer is located in a country that is not an FATF Member and has not implemented the FATF recommendations on customer identification, the Member need not identify the client for specific transactions if, when the account is opened, the Member ascertains the identity of all third parties relating to the account. This provision requires the Member not only to obtain the names of all of the foreign dealers' clients who might trade through the Member, but to verify their identities through identity documents or their having accounts in their names at financial entities *as defined above*. This provision is not, therefore, practicable.

Members are also not required to obtain and record information about the third parties for an account opened by a lawyer, accountant, real estate broker or real estate sales representative if the Member has reason to believe that the account will be used only for clients of the accountholder[6].

III. Changes to Identification and Verification Requirements for Individual Clients

While Members are still required to obtain a signature card, account operating agreement or account application form bearing the signature of any person authorized to give instructions for the account of an individual, there are two significant changes to the requirement:

1. the definition of "signature" includes an electronic signature[7]

2. the document must set out "the account number of a financial entity account, *if any,* that is in the name of" the accountholder or the person authorized to give instructions for the account

[4] Section 9(5)
[5] For the current list of NCCTs, see Member Regulation Bulletin MR-0100 dated September 28, 2001 or the FATF Web site, http://www1.oecd.org/fatf/NCCT_en.htm. The Association will endeavour to inform Members of changes in the list as they occur.
[6] Section 9(6)
[7] Section 1(2)

[emphasis added][8]. Because the previous Regulation did not include the words "if any," it was technically impossible for a Member to comply with the Regulation if the accountholder did not have an account at a Canadian deposit-taking institution. Although technically this change does not require recording of an account number at a non-Canadian bank or other deposit-taking institution, Members should nonetheless obtain and record such information as part of its normal know-your-client procedures.

While the obtaining of a signed document as noted above is mandatory for all individual accounts, verification of the client's identity is no longer required for the following types of accounts:

- accounts opened solely to hold and sell shares received from demutualizations, employee stock purchase plans or privatization of Crown corporations;

- registered plan accounts including locked-in retirement plans, RRSPs and group RRSPs[9]

- an account opened for the sale of mutual funds if the Member has reasonable grounds to believe that the person's identity was verified according to the Regulations by the dealer that sold the mutual funds to the client[10]. However, if the account is to be used beyond the sale of all or part of those funds, the normal verification requirements apply.

The three available methods of identity verification have not changed from the previous Regulation. However, the financial entity account or cheque methods are now described as available "where the person is not physically present[11]." This addition clearly confirms that verification through review of identity documents can only be done when the person whose identity is being verified is physical present before an employee or agent acting on behalf of the Member. Furthermore, the new Regulations specify that only original documents are acceptable, not copies[12].

The recording requirements for identity verification have also been changed. When an individual's identity is verified by a review of identity documents, the individual's date of birth must now be entered on the signature card, account agreement or account application form which bears the individuals signature. The type and reference number of the identification document must also be recorded on the same document, as was required under the previous Regulations[13].

The record keeping requirements for the cheque or financial entity account methods are unchanged.

IV. Identification and Verification of Corporate and other Non-Individual Clients

This section describes the identification and verification requirements when opening non-individual accounts. Where there is no exception to verification requirements for persons authorized to trade in non-individual accounts, the same record keeping requirements apply as those applying to individual accounts – i.e. the recording of the person's date of birth and details of the verification method.

[8] Subsection 23(1)(a)(ii)
[9] Subsections 57(2)(b) and (c)
[10] Section 57(5)
[11] Subsection 64(1)(c)(ii)
[12] Section 64(3)
[13] Section 67(a) and (b)

Corporations

When opening an account for a corporation, Members are required under the revised Regulations to obtain "a copy of the part of official corporate records that contains any provision relating to the power to bind the corporation in respect of that account." The corporate resolution identifying the parties authorized to enter orders for the account normally obtained by Members for corporate accounts will meet this requirement[14]. There are no exceptions to this provision, even for financial entities and other securities dealers[15].

Verification of the Identity of Corporations and Individuals Authorized to Trade

Within six months of opening an account for a corporation, a Member is required to confirm its name and address and the names of its directors. This can be done by referring to its certificate of corporate status, an annual filing required under applicable provincial securities legislation or by any other means. The means can be a publicly available electronic source, such as SEDAR filings[16].

If the confirmation is in the form of a paper record, a copy of the record must be maintained. Where it is by reference to an electronic source, a record of the corporation's registration number, the type of record and the sources of the electronic version must be kept.

Members are also required to obtain a signature card, account operating agreement or account application bearing the signature of everyone authorized to give instructions for a corporate account. However, the Member must verify the identity of only three of those persons.[17].

Exceptions

The exceptions to the verification requirements for corporate accounts have been expanded, as follows:

1. the exception for publicly traded companies having a minimum of $75 million on their last audited balance sheet has been expanded to include not only companies listed on Canadian and certain U.S. stock exchanges and NASDAQ, but also those listed on any stock exchange prescribed by section 3201 of the *Income Tax Regulations* that operates in an FATF Member country[18]. The relevant exchanges are:

American SE	Hong Kong SE	Oslo SE
Australian SE	Intermountain SE	Pacific SE
Boston SE	Italian Exchange	Philadelphia SE
Cincinnati SE	Irish Stock Exchange	Singapore SE
Copenhagen SE	London SE	Spokane SE
Deutsche Borse	Madrid SE	Stockholm SE
Euronext – Amsterdam	Midwest SE	SWX Swiss Exchange
Euronext – Brussels	NASDAQ	Tokyo SE
Euronext - Paris	New York SE	Vienna SE
Helsinki Exchanges	New Zealand SE	

[14] Section 23(1)(b)
[15] Section 23(2)
[16] Sections 57(3), 65(1) and 65(2)(d)
[17] Sections 23(1)(a) and 57(2)(a)
[18] Section 62(2)(b)

2. There is a new exception for accounts of foreign affiliates of financial entities[19].

3. The asset test for Canadian pension funds has been eliminated. Previously it was limited to Canadian pension funds having minimum net assets of $75 million; the new regulations extend it to all Canadian pension funds regulated under federal or provincial legislation.[20]

4. There continues to be an exception from verification requirements for individuals authorized to trade for the accounts of public bodies. However, there are two changes in the definition of public bodies that narrow the exception:

   - Canadian educational institutions were excepted under the previous Regulations but are not included in the definition of public bodies in the new Regulations;

   - the previous Regulations gave a general exception for Canadian hospitals, where the new Regulations contain the definition noted above that may narrow the applicability of the exception[21].

Other Entities

For new accounts for entities that are not corporations, Members must record the entity's name, address and principal business or occupation[22], and, subject to exceptions noted below, obtain a signature card, account operating agreement or account application form bearing the signature of every individual authorized to trade in the account. There is no similar limit to the number of individuals whose identity must be verified as is allowed for corporate accounts.

Verification of the existence of the entity must be confirmed within six months of the opening of the account, by referring to a partnership agreement, articles of association or a similar record, either on paper or from a publicly available electronic source. The Member must retain a copy of a paper record or, if the verification is from an electronic source, record the entity's registration number, the type of record referred to and the source[23].

There are no specific exceptions for non-corporate entities. However, the following general exceptions apply:

a) the exception from having to obtain signed documents for financial entities and other Canadian securities dealers;

b) the exception to verifying identity of persons authorized to trade for:

   - accounts opened solely for the deposit and sale of shares from demutualizations, employee stock purchase plans or privatization of Crown corporations;
   - group RRSP accounts;
   - accounts of foreign affiliates of financial entities
   - accounts opened solely to sell mutual funds purchased at another securities dealer where the Member has reason to believe that proper verification was done at the other dealer

[19] Section 57(2)(d)
[20] Section 62(4)
[21] Sections 1(2) and 62(2)(b)
[22] Section 23(1)(c)
[23] Section 66

- public bodies, listed companies and pension funds as noted above for corporate accounts.

V. Other Provisions

Exceptions

General exceptions contained in the previous Regulations are retained in the new Regulations and are extended to include the new identification requirements for corporations and other entities. These are:

1. the exception from having to verify the identity of a client opening another account at the same Member[24]

2. the exception from having to verify the identity of a client when it has previously been verified by the same employee or agent of the Member. With individuals, the person who previously did the verification must recognize the client[25].

Records Retention

The records retention requirements are unchanged. Generally, client identification and verification documents must be kept for five years after the account is closed. Ongoing operating documents such as confirmations and monthly statements must be kept five years from their creation[26].

Records may be kept in machine-readable or electronic form provided that they can be produced in paper form and can be provided to an authorized person with 30 days of a request to produce it under section 62 of PCMLTFA[27].

VI. Large Cash Transaction Reporting

Large cash transaction reporting comes into effect on November 30, 2002.

Under section 21 of the Regulations, Members must report to FinTRAC the receipt from a client other than a financial entity or public body of more than $10,000 in cash in Canadian currency or the equivalent in a foreign currency[28]. For this purpose, two or more cash receipts in the same 24 hours totalling more than $10,000 and known by an employee or senior officer to be by or on behalf of the same client are considered to be one transaction. The report must be made within 30 days of the transaction until November 30, 2003 and thereafter within 15 days[29].

Large cash transactions reports are to be filed electronically if the Member has facilities to do so, or on paper if not. The information to be filed is detailed on Schedule 1 – Large Cash Transaction Report

[24] Sections 62(2)
[25] Section 63
[26] Section 69
[27] Sections 68 and 70
[28] Under section 2 of the Regulations, the official conversion rate to be used is either (a) the official conversion rate of the Bank of Canada…as published in its *Daily Memorandum of Exchange Rates*, or (b) if there is no official conversion rate, the rate that the Member would use for that currency in the normal course of business at the time of the transaction.
[29] Section 5(2)

attached to the Regulations (Attachment A)[30]. Completion of the items on the schedule marked with an asterisk is mandatory. The items not marked with an asterisk need not be provided if, after taking reasonable steps to do so, the Member is unable to obtain the information[31].

Members must continue to retain large cash transaction records on the same cash transactions as under the previous Regulations, unless the information is readily obtainable from other records the Member is required to maintain under the Regulations[32].

Any Member receiving cash in an amount that triggers the requirement to keep a large cash transaction record is required to "take reasonable measures to determine whether the individual who in fact gives the cash…is acting on behalf of a third party[33]. This is a change from the previous requirement[34].

The nature of such reasonable measures is not spelled out, but clearly an active effort must be made, at a minimum directly asking the person making the deposit.

The records to be kept on the third party have also changed. In addition to the name, address and nature of the principal occupation or business of the third party, if the third party is a corporation the Member must record its incorporation number and place of issue [presumably of the incorporation number]. For all third party deposits, "the nature of relationship between the third party and the individual who gives the cash" must also be recorded[35].

If the Member has reasonable grounds to suspect that individual giving the cash is acting on behalf of a third party but is unable to make a determination, the Member is required to keep a record of whether, according to the individual, the transaction is for a third party and the reasonable grounds for suspecting that it is[36].

VII. Implementation of a Compliance Regime

Section 71 of the Regulations is new. It requires Members to implement a regime for compliance not only with the Regulations, but with PCMLTFA and all other regulations issued under PCMLTFA. The most important other Regulations are the suspicious transaction reporting regulations.

The compliance regime must include "as far as practicable" the following:

1. the appointment of a person responsible for implementing the regime;

2. the development and implementation of compliance policies and procedures;

3. a review of the policies and procedures "as often as necessary to test their effectiveness" by an internal or external auditor;

4. an ongoing compliance training program for employees and agents of the Member.

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[30] Guidelines for the filing of reports, both electronic and paper, can be found on FinTRACC's Web site at http://www.fintrac.gc.ca/reporting--declaration/1_e.asp
[31] Section 52(1)
[32] Section 52(2)
[33] Section 8(1)
[34] The previous requirement was triggered when the Member or an employee or director of the Member had "reason to believe that the individual from whom the cash [was] received [was] acting on behalf of a third party." Section 4(e) of the *Proceeds of Crime (Money Laundering) Regulations 1993*
[35] Section 8(2)
[36] Section 8(3)

This kind of requirement is not new to Members and such policies and procedures should already be in place under IDA Regulation 29.27.

VIII. Revisions to the Suspicious Transaction Reporting Regulations

The revisions to the suspicious transaction reporting requirements add to the regulations that came into effect in November, 2001[37] the reporting of transactions raising suspicions of terrorist financing activity.

The *Anti-terrorism Act,* 2001 amended section 7 of PCMLTFA to add a requirement to report to FinTRAC "financial transaction[s]…in respect of which there are reasonable grounds to suspect that the transaction is related to the commission of…a terrorist activity financing offence[38].

A terrorist activity financing offence is an offence under sections of the *Criminal Code* (see Attachment D)added by the Anti-*Terrorism Act*: sections 83.02, 83.03 or 83.04 or an offence under section 83.12 of the *Criminal Code* arising out of a contravention of section 83.08 of that Act[39].

The *Anti-Terrorism Act* also added new Section 83.1 to the *Criminal Code* requiring disclosure by anyone in Canada or any Canadian outside of Canada, to the Royal Canadian Mounted Police and the Canadian Security Intelligence Service, of:

> (*a*) the existence of property in their possession or control that they know is owned or controlled by or on behalf of a terrorist group; and
>
> (*b*) information about a transaction or proposed transaction in respect of property referred to in paragraph (*a*).

It also added a new subsection 7(1) to PCMLTFA requiring reporting to FinTRAC by parties subject to PCMLTFA of any information reported to the RCMP and CSIS under the above-noted section 83.1 of the *Criminal Code*[40].

The revisions to the STR Regulations add two types of reports on terrorist financing[41]:

1. An amendment to section 9(1) which adds transactions raising suspicion of terrorist activity financing offences to the existing requirement to report those raising suspicion of money laundering. The reporting is on the same schedule for both types of suspicious transactions. Reports must be filed within 30 days of the Member or any of its employees or officers detecting a fact about a transaction that raises reasonable grounds for suspicion.

2. Section 10 of the STR Regulations now requires reports to FinTRAC under section 7(1) of PCMLTFA to be made in a new format, Schedule 2, "without delay."

IX. Suggested Compliance Measures

Members should ensure that their policies and procedures are consistent with the requirements of Section 71 of the revised Regulations, including the appointment of a responsible person and implementation of a training program. Anti-money laundering training time is eligible, at the Member's discretion, to be

[37] See Member Regulation Notice MR-104, September 28, 2001
[38] *Anti-Terrorism Act*, Section 52
[39] *Anti-Terrorism Act*, Section 4
[40] *Anti-Terrorist Act*, Section 52
[41] Section 4 of the Amendments. The amendments also move the previous section 10 of the STR Regulations into section 9 to make room for the reporting requirement under Section 7.1 of PCMLTFA.

counted towards completion of the Compliance portion of Continuing Education requirements under IDA Policy 6, Part III.

Members should consider revising new account documents to include extra information required and questions to be asked. For example, there should be a place to record the details of identity verification such as date of birth and documents reviewed or obtained.

If a Member chooses to use publicly available electronic sources where permitted to do so by the Regulation, it would be prudent to retain a printed copy or electronic image of the source material, as changes to such records are outside of the Member's control and previous versions may not be readily available if needed.

Any Member choosing not to verify new client identity prior to opening an account should have a tracking system to ensure that verification is completed within 6 months of account opening.

The Association will be publishing further guidance on anti-money laundering procedures in the near future.