



# FINTRAC Report to the Minister of Finance on Compliance and Related Activities

September 30, 2019

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## I. EXECUTIVE SUMMARY

An essential part of FINTRAC's mandate is to work with Canadian businesses to ensure compliance with the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (the Act). Compliance with the Act helps to prevent and deter criminals from using Canada's economy to launder the proceeds of their crimes or to finance terrorist activities. This report presents the activities and various initiatives carried out by FINTRAC in the achievement of its compliance mandate during the 2018/2019 fiscal year. There are four central elements to this report:

- FINTRAC's Transparency Initiative
- Assistance to reporting entities and engagement with associations and regulators
- Assessment and enforcement activities
- FINTRAC's contributions to improving the AML/ATF Regime

Over the past year, FINTRAC has seen major developments in its compliance program. As part of its transparency initiative, FINTRAC published important and wide-ranging information about its compliance program in an effort to assist businesses in understanding their legislative and regulatory obligations as well as to strengthen the AML/ATF regime. Key publications include FINTRAC's Compliance Framework that captures the guiding principles shaping its compliance program, the Compliance Assessment Manual, the revised Administrative Monetary Penalties (AMPs) policy and calculation methodology as well as the notice on Voluntary Self-Declaration of Non-Compliance. These were shared widely with Canadian businesses via FINTRAC's website and well received by those businesses.

This report further describes the activities conducted under the three pillars of the Compliance Framework: *Assistance*, *Assessment*, and *Enforcement*. The 2018-19 fiscal year was marked with extensive outreach and engagement activities. First, FINTRAC assisted Finance Canada in delivering a robust regulatory consultation to inform businesses of proposed obligations which included an initial view as to how the Centre would interpret and enforce the regulatory amendments.

FINTRAC also hosted a forum and engaged with its major reporters on various issues to ensure that Canada's banks have the knowledge, tools and support they need to meet regulatory obligations. FINTRAC also participated in a myriad of other events such as the annual Association of Certified Anti-Money Laundering Specialists (ACAMS) conference in addition to leading broad consultations with Canadian businesses and their associations in the creation of new suspicious transaction reporting guidance.

Lastly, FINTRAC engaged extensively with real estate regulatory bodies, industry associations and businesses across the country to strengthen compliance in this sector. In an effort to facilitate the sharing of information and to coordinate risk-informed examinations in the British Columbia real estate sector, FINTRAC signed a new Memorandum of Understanding (MOU) with the Real Estate Council of British Columbia (RECBC).

*Assessment* activities are at the very core of FINTRAC's compliance mandate and allow FINTRAC to determine the extent to which all reporting entity sectors comply with their legal obligations. FINTRAC conducted 497 examinations in 2018-19. The report describes key examinations findings for the banking, real estate, MSB and casino sectors. The report also sets out the outcomes of follow-up examinations, which are indicative of positive changes in compliance behavior.

Assessment activities also include database examinations undertaken by FINTRAC to validate if identified deficiencies related to data quality reporting issues have been addressed by reporting entities. Database examinations are an effective tool to identify changes in reporting behaviour and select potential candidates for a follow-up examination. FINTRAC conducted 54 such reviews in 2018-19 and the results are presented in the report.

In 2018-19, FINTRAC undertook several *enforcement* activities to address instances of non-compliance. FINTRAC issued its first AMP since completing the review of its AMP policy and methodology as well as seven non-compliance disclosures to law enforcement to address the most serious cases of non-compliance.

FINTRAC is committed to improving the Canadian AML/ATF regime and, in addition to its core activities, has been working closely with Finance Canada on a number of initiatives such as the parliamentary review of the PCMLTFA. Upcoming priorities for FINTRAC include the British Columbia public inquiry into money laundering, the operationalization of regulatory amendments published in June 2019 which have significant impact on systems and programs, the implementation of its compliance engagement strategy to further educate businesses on AML/ATF obligations and continue improving compliance of Canadian businesses.

## II. ABOUT FINTRAC

As Canada's financial intelligence unit, FINTRAC is responsible for the detection, prevention and deterrence of ML/TF. FINTRAC delivers high-quality, relevant and timely financial intelligence to appropriate domestic law enforcement and intelligence agencies as well as to its foreign counterparts.

As a regulator, FINTRAC ensures the compliance of approximately 24,000 reporting entities with obligations under the PCMLTFA and associated regulations through assistance, assessment and enforcement activities. Compliance activities also serve to deter the criminal use of Canada's financial system.

In the 2018-19 fiscal year, the compliance sector had 83 Full Time Equivalents (FTEs) and a budget of \$8,771,695.<sup>1</sup> The sector is comprised of regional compliance officers involved in conducting examinations through the three FINTRAC regional offices. The regional offices are also responsible for providing assistance to reporting entities and maintaining key relationships with other regulators and industry associations. Last fiscal year, the regional offices had 46 FTEs, and a budget of \$4,410,609.

Divided among three unit functions, the headquarters (HQ) in Ottawa had 37 FTEs and a budget of \$4,361,086. HQ is responsible, among other activities, for coordinating the strategic and operational initiatives of the compliance program and providing national leadership for the regional operations, as well as providing assistance to reporting entities, managing the MSB registry, providing policy interpretations, administering FINTRAC's AMP and Non-Compliance Disclosures programs, and maintaining compliance MOUs with external regime partners.

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<sup>1</sup> The FTE count and budget figures in this report were calculated by using a different methodology than what is provided in the Departmental Results Report. The figures represent resources specifically allocated for compliance activities and do not cover internal services in support of those activities. The FTE count does not include students.

### III. COMPLIANCE ACTIVITY HIGHLIGHTS FOR 2018-19

#### A) Transparency Initiative

As part of its ongoing commitment to assist thousands of Canadian businesses in fulfilling their legislative and regulatory obligations and to strengthen the AML/ATF regime, FINTRAC launched a multifaceted transparency initiative in 2018-19. The initiative included extensive publication of information on its Compliance Program.

As a key element of its transparency initiative, FINTRAC published its *Compliance Framework*, which captures the guiding principles that shape its compliance program. It provides a comprehensive description of the services and tools that are available to assist businesses in complying with their obligations. The framework helps smaller businesses, in particular, in enhancing their efficiency of their compliance efforts and easing their burden.

The FINTRAC *Assessment Manual* was released earlier this year to assist businesses understand how FINTRAC assesses the effectiveness of their compliance programs and help them prepare for an examination. The manual provides a detailed, transparent and plain language account of FINTRAC's overall assessment process. The manual will also help businesses strengthen their compliance programs and prepare more efficiently for an examination.

FINTRAC also published, for the first time, its notice on *Voluntary Self-Declaration of Non-Compliance* (VSDONC) that encourages reporting entities to come forward voluntarily to share non-compliance issues that they may identify on their own. VSDONCs are an important tool for FINTRAC as they provide an opportunity for reporting entities to work with FINTRAC to resolve non-compliance without having preoccupations on potential repercussions for non-compliance. For example, the VSDONC process allows reporting entities to submit reports that they may have initially missed for various reasons. By promoting open dialogue and transparency, the notice is an effective tool to encourage reporting entity compliance and allows for swift remedial action without necessarily imposing penalties.

FINTRAC also made public this year its revised *Administrative Monetary Penalties policy and calculation methodology*. Over the last two years, FINTRAC has worked to review its AMP policy and calculation methodology to address Federal Court decisions in 2016. As part of this review, FINTRAC has reviewed its calculation methodology and crafted seven harm done guides that describe the approach for determining penalties for over 200 violations. This marked a culmination of collaboration and consultations

between key internal and external stakeholders, including Finance Canada. Moreover, FINTRAC is pleased to report that it received confirmation from a third party reviewer, who is a retired jurist and expert on administrative law, that the new AMP policy and seven harm guides go “above and beyond” the courts’ expectations in terms of providing sufficient and comprehensive information to explain the approach for penalty calculation.

## **B) Assistance and Engagement Activities**

### **1. Assistance to Reporting Entities**

Assistance to reporting entities is an important pillar of FINTRAC’s Compliance Framework and involves providing guidance and tools, outreach and engagement, and technical support. In 2018-19, FINTRAC engaged with its major reporters, presented at the ACAMS conference, and participated in 23 conferences, 24 teleconferences, and 88 meetings that included guidance consultations and pre-publication consultations held in the context of proposed regulatory amendments.

#### *FINTRAC Engages with Major Reporters*

In October 2018, FINTRAC held the 5<sup>th</sup> Annual Major Reporters Forum, bringing together a number of regime partners and Canada’s largest financial entities that provide over 90 percent of the reports that FINTRAC receives every year. The Forum highlighted key publications by FINTRAC to support reporting entities in meeting their obligations and to increase the transparency of the Centre’s compliance program. It also included a presentation from the Toronto Police Service illustrating how reports submitted to FINTRAC from reporting entities support law enforcement activities to counter ML/TF.

In the fiscal year 2018-19, the Director and Chief Executive Officer (CEO) of FINTRAC met with the CEOs, Chief Anti-Money Laundering Officers and Board of Directors of large banks. In these meetings, the Director of FINTRAC acknowledged the important role that these institutions play in Canada’s anti-money laundering and anti-terrorist financing (AML/ATF) regime. She also highlighted the need for continued investment to maintain and enhance their internal programs to address evolving ML/TF vulnerabilities.

#### **STR reporting trends of major reporters**

The “Big 8” financial entities<sup>2</sup> (B8) are responsible for 52% of the suspicious transaction reports (STRs) that FINTRAC received in 2018-19. In that fiscal year, the B8 submitted 123,993 STRs to FINTRAC. This represents a significant increase in suspicious transaction reporting since the previous fiscal: an increase of 67.2% for a total increase of

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<sup>2</sup> The B8 consist of the Banque Nationale du Canada, Caisses Populaires and the Fédération des Caisses Desjardins du Québec, Royal Bank of Canada, HSBC Bank Canada, the Canadian Imperial Bank of Commerce, the Bank of Montreal, the Bank of Nova Scotia, and Toronto Dominion Bank.

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49,828 reports. As illustrated in Figure 1 [REDACTED] the most significant increase in percentage variance of STRs, with an increase of 269%, followed by [REDACTED] with an increase of 228%.

**Figure 1: The net variance for STR reporting from the B8 over FY 2017-18 and 2018-19, in number of reports**



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FINTRAC primarily attributes the increase in suspicious transaction reporting to ongoing compliance activities such as examinations and outreach. Some of this increase is also attributable to systems limitations for reporting. FINTRAC’s reporting system requires reporting entities to file multiple STRs when more than 99 transactions are relevant to the same set of suspicions. Similarly, reporting entities are required to submit multiple STRs for transactions conducted at different locations.

Although reporting entities are submitting the accurate information that conforms to the requirements in the PCMLTFA and associated regulations, these systems limitations cause the submission of multiple STRs for the same set of suspicions. FINTRAC will seek to address this issue and identify other areas to increase reporting efficiencies through the new FINTRAC Reporting Working Group, established with industry, and in its broader project to review all reporting forms and align with regulatory amendments.

*FINTRAC Presents at the Annual ACAMS Conference*

The Director and CEO of FINTRAC was the keynote speaker at the annual ACAMS conference in Toronto. She spoke to FINTRAC’s maturing compliance program and its evolution in moving from an audit to an assessment approach for examinations, as well as



the Centre's commitment to supporting Canadian businesses in their AML/ATF programs and in understanding their obligations.

At the same conference, FINTRAC also participated in a panel and highlighted efforts to enhance the transparency of the compliance program by, for example, making more information available on its public website to help reporting entities better understand how FINTRAC works with them to ensure they meet their obligations. To this end, FINTRAC published its Assessment Manual, as well as the revised penalty calculation methodology of the AMP program in February 2019. Comments received during the conference and posted online indicate that FINTRAC's message and publications were very well received.

#### *FINTRAC updates its STR Guidance and STR Indicators to Assist Reporting Entities in Identifying Suspicious Transactions*

In January 2019, FINTRAC published new guidance targeting all sectors to assist reporting entities in complying with the requirements to report STRs. This is the first official guidance that explains the concept of the "reasonable grounds to suspect" threshold with respect to triggering the requirement to submit an STR to FINTRAC on suspicious transactions or attempted suspicious transactions.

FINTRAC also published new ML/TF indicators for all reporting entity sectors. FINTRAC developed these indicators by undergoing a three-year review of ML/TF cases, reviewing high quality STRs and literature by international organizations such as the Financial Action Task Force (FATF) and the Egmont Group, and consulting with reporting entities in all sectors.

FINTRAC expects that the new guidance products will contribute to the awareness of businesses of their reporting obligations and inform them on potential red flags to assist them in determining whether to submit an STR to FINTRAC.

#### *FINTRAC Conducts Outreach Activities to Help Reporting Entities Meet Obligations*

##### **Consultations on ongoing monitoring requirements**

FINTRAC led consultations with reporting entities to clarify FINTRAC and OSFI expectations regarding ongoing monitoring requirements. In doing so, FINTRAC learned more about the automated systems that some reporting entities use to conduct ongoing monitoring of their clients and how reporting entities can rely on these systems to meet their obligations under the regulations. FINTRAC will take this into consideration when conducting future examinations.

## **Regulatory consultations and preliminary guidance**

During the fiscal year, FINTRAC worked closely with Finance Canada to continue to review the drafting of regulatory amendments and to prepare for and participate in extensive consultations with stakeholders, including both private and public sector representatives.

To support the consultations, FINTRAC provided stakeholders with concept notes on new or revised obligations stemming from proposed regulatory amendments. The concept notes represented preliminary guidance and provided reporting entities with an initial view on how FINTRAC might interpret and enforce the amendments. FINTRAC also developed other facilitation tools, including a side-by-side comparison of the current and proposed regulatory text, and visual representations of changes to the reporting schedules. The latter aimed to help reporting entities and stakeholders better understand forthcoming expanded reporting requirements and give reporting entities a sense of how these changes may affect their internal processes and systems.

The 90-day consultation process was extremely successful in garnering valuable input from stakeholders on the proposed amendments. This success is a result of FINTRAC's close working relationship with Finance Canada, which has evolved over the life span of the regulatory development and consultation process.

The Centre also established a FINTRAC Reporting Working Group in partnership with industry to review regulatory changes to the schedules and implement improvements and efficiencies to all reporting forms. Since its creation in February 2019, the working group has met on a number of occasions and although the group is still in its early stages, it has experienced good collaboration and commitment from all stakeholders.

## **Policy interpretations**

FINTRAC provided 401 policy interpretations to reporting entities, federal and provincial governments, media and members of the public. These policy interpretations are in response to requests submitted to FINTRAC and explain how to comply with certain obligations.

Approximately half of the policy interpretation inquiries that FINTRAC received concerned questions regarding business models of MSBs, specifically in terms of businesses that deal in virtual currency. Under 2014 legislative amendments to the PCMLTFA that are not yet in force, dealing in virtual currency represents a new type of service under the definition of an MSB and will require that these businesses register with FINTRAC. However, this amendment will come into force in June 2020; therefore, these virtual currency dealers do not currently have obligations under the PCMLTFA.

In the last fiscal year, more than 200 such businesses have sought to register with FINTRAC. Starting in August 2019, FINTRAC began the early registration of businesses that wish to voluntarily register ahead of the coming into force of the new legislative requirements. The purpose of early registration is to streamline the MSB registration process and to reduce the burden on businesses that will be newly covered under the PCMLTFA.

## **2. Engagement with Canadian Regulators, Industry Associations and Foreign Counterparts**

The 2018-19 fiscal year marked important developments between FINTRAC and domestic regime partners, including the signing of a new MOU with RECBC, ongoing engagement with the Canadian Real Estate Association (CREA), and the development and publication of two operational alerts, as well as Canada's first Terrorist Financing Assessment.

### *A new MOU with RECBC Heightens Information Sharing with the Real Estate Regulator in British Columbia*

Combatting money laundering in the British Columbia real estate sector has been a priority for the Government of Canada and FINTRAC over the past several years, as demonstrated by the Centre's 2016 Operational Brief: *Indicators of Money Laundering in Financial Transactions Related to Real Estate*.

In an effort to work more closely with the British Columbia government to address money laundering vulnerabilities in the real estate sector, FINTRAC signed a Compliance MOU with RECBC in March 2019. This MOU strengthens FINTRAC's ability to ensure compliance in the sector in British Columbia. It also sends a strong message to the sector, and those that may look to exploit these businesses, that FINTRAC is committed to working with other regulators to protect Canadians and secure Canada's economy.

The MOU establishes a framework within which FINTRAC and RECBC can share compliance-related information. This sharing of information will result in more coordinated and risk-informed examinations and may reduce burden on reporting entities in this sector. The information sharing has already allowed FINTRAC to update its reporting entity population for real estate businesses licensed in the province of British Columbia. This will ensure that FINTRAC is aware of all real estate reporting entities in this province to allow for appropriate risk assessment and subsequent compliance activities.

### *FINTRAC Continues to Engage with CREA*

FINTRAC engaged CREA extensively by providing statistical information on the sector's examination results and expected areas of improvements, as well as to seek CREA's feedback on its revised guidelines, including the new suspicious transaction guidance. FINTRAC has also assisted CREA by reviewing and providing feedback on its training modules, and provided assistance to the Real Estate Council of Ontario in the development of a training module on regulatory obligations for its members.

### *Participation in the British Columbia-Canada Working Group on Real Estate*

FINTRAC is a member of the British Columbia-Government of Canada Working Group on Real Estate and has contributed to this group's work by delivering presentations, advancing a diagnostic of money laundering and compliance challenges affecting this sector, and defining the key issues that need to be addressed as the regime moves towards identifying policy options to address gaps.

FINTRAC has also contributed data and input to advance the British Columbia Expert Panel's understanding of the Centre's operations and mandate, as well as provided some data in support of the Panel's study of money laundering.

### *Operational Alerts Inform Reporting Entities, Government and Five-Eyes Partners and the Public of the Extent of ML/TF*

FINTRAC published two operational alerts: *Professional money laundering through trade and money services businesses* and *Laundering of the proceeds of romance fraud*. The alerts provide Government, members of the Five Eyes and the public with the latest information on ML/TF trends and can be leveraged by reporting entities for use in performing a risk-based assessment of their compliance programs.

### *FINTRAC's Terrorist Financing Assessment is the First of its Kind*

In December, FINTRAC published its 2018 Terrorist Financing Assessment, which provides a baseline assessment of the terrorist activity financing risks presented by various countries and terrorist organizations within those countries. The assessment's financial and geographic indicators, in particular, can assist Canadian businesses in better identifying and reporting suspected terrorist activity financing.

### *The International Supervisory Forum (ISF) Provides a Venue for Sharing of Information between Regulators*

The ISF provides members with a platform for actively sharing information and operational practices; consulting on common supervisory priorities and issues; and developing collaborative products and initiatives.

The fourth plenary meeting was held in Melbourne in November 2018. Members developed a mission statement *Unity in Global Supervision: Leading solutions to international crime* and agreed on a three-year work plan that identifies concrete deliverables. During the plenary, the United Kingdom was selected as the new chair of the ISF. Members continued to hold teleconferences every two months for ongoing information sharing of best practices following the plenary meetings.

The plenary also provided an opportunity to meet with counterparts to discuss, amongst other things, their experience in regulating businesses dealing in virtual currency. [REDACTED]

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*FinCEN Delivers Virtual Currency Training to Share Best Practices on Compliance Examinations*

Over the last three years, FINTRAC and FinCEN have participated in targeted bilateral engagement to share information and best practices on issues of mutual interest. In 2018-19, FINTRAC continued its exchange with FinCEN and took a proactive approach to the coming into force of new requirements for businesses that deal in virtual currencies by learning from its counterpart's experience in regulating these businesses.

FinCEN delivered a tailored training program on virtual currency, including its examination methodology for this sector, to raise awareness and share expertise with FINTRAC's compliance sector as it relates to conducting these examinations. The training provided an overview of the examination process and the variety of tools that FinCEN uses to plan for examinations of businesses dealing in virtual currency. As a result, FINTRAC is exploring how the use of tools, [REDACTED] can assist in preparing for these examinations.

## C) Assessment Activities

FINTRAC fairly and objectively uses many different compliance assessment tools to ensure that reporting entities meet their obligations. FINTRAC conducts onsite, desk and database examinations to assess reporting entities' compliance with AML/ATF obligations and to provide assistance where needed. FINTRAC also conducts ongoing monitoring of reports that entities submit to ensure quality and to address issues.

### 1. New developments in the Compliance Program

#### *Outcomes of Examinations are indicating Benefits of the Assessment Approach*

Over the past two years, FINTRAC has solidified its new assessment approach to compliance examinations. The approach places less emphasis on identifying technical deficiencies and more on the effectiveness of reporting entities in meeting obligations under the PCMLTFA, as well as on the impact of non-compliance on the objectives of the PCMLTFA and on FINTRAC's mandate. As such, when FINTRAC identifies technical non-compliance in an otherwise adequate system of policies, procedures, processes, and controls, it will notify the reporting entity of the non-compliance, but the technical deficiencies may not negatively affect the overall result of FINTRAC's assessment.

FINTRAC's compliance program is constantly evolving in stride with the AML/ATF regime to ensure compliance activities continue to be meaningful, while minimizing undue business disruptions. The shift toward an assessment approach represents a natural evolution: with the early context of a new regime and as FINTRAC progressively built up its examination program, its focus on technical compliance was a natural starting point. With time, FINTRAC progressively migrated from an audit to an assessment approach.

To solidify this approach, FINTRAC delivered scenario-based training sessions in each of its regional offices, receiving strong positive feedback from regional compliance officers. The intent of the sessions was to build a strong foundation upon which a formalized and comprehensive training program for the assessment approach will be developed and delivered progressively in the years ahead.

The outcomes of examinations completed over the last two years are an early indication of the benefits of the assessment approach in assisting reporting entities to address areas for improvement and encourage compliance, while taking enforcement action when

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**Case Example: Findings of a FINTRAC Examination of [REDACTED]**

FINTRAC conducted an examination of [REDACTED] It was on the examination plan for the 2017-18 fiscal year because of [REDACTED]

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## 2. Examinations Findings by Key Sectors

FINTRAC employs an examination framework to ensure that examinations are conducted in a consistent manner. Under this framework, FINTRAC conducts risk-based examinations, focusing its resources on examinations on areas of higher risk. This approach is dynamic: the risks identified one year may change in the next as new products are introduced or as new vulnerabilities emerge within the financial system. FINTRAC's risk-based approach ensures that compliance activities are proportionate to the risk of non-compliance.

Once it has evaluated a reporting entity's risks, FINTRAC selects assessment methods that it will use as part of its examination. FINTRAC uses the methods to assess how the reporting entity complies with the legal requirements set out in the PCMLTFA and associated Regulations. When applying assessment methods, FINTRAC reviews the reporting entity's documents, client records, records of transactions and financial transaction reports, as well as conducts interviews.

Examinations are broken down into three phase: planning and scoping; examination and assessment; and developing the findings and finalizing the examination. In the planning phase, FINTRAC selects the areas and requirements that it will examine and the assessment methods it will use. The "examination scope" is unique to every examination and considers the reporting entity's business model, environment, activities, operations, and risks.

In the last phase, FINTRAC assesses the harm done of identified deficiencies, the extent of non-compliance and any mitigating or aggravating factors. FINTRAC focuses less on technical non-compliance and more on the overall soundness of the reporting entity's compliance program.

After an examination, FINTRAC may follow-up to make sure that the reporting entity has addressed the deficiencies identified in FINTRAC's findings letter. FINTRAC may conduct a follow-up examination, monitor the reporting entity's transaction reports submitted to the Centre, and monitor progress in the reporting entity's action plan.

FINTRAC conducted a total of 497 examinations across all reporting entity sectors, as demonstrated in Table 1 below. The number of examinations is consistent with the 500 examinations conducted in the previous fiscal year, reflecting the complexity and resource intensive nature of examinations of large reporting entities. In 2018-19,



FINTRAC conducted two bank examinations. These required significantly more resources, specifically in terms of hours dedicated by regional compliance officers to prepare for and conduct these examinations compared to examinations in other sectors.

**Table 1: Examination Highlights 2018-19**

<b>Examinations per Sector</b>	
<b>Sector</b>	<b>Number of Examinations Completed in 2018-19</b>
Real Estate	190
Money Services Businesses	112
Securities Dealers	57
Dealers in Precious Metals and Stones	49
Financial Entities (i.e., banks, credit unions and caisses populaires)	45
British Columbia Notaries	24
Life Insurance Companies, Brokers and Agents	11
Casinos	5
Accountants	4
Total	497

### *Banking Sector*

Examinations in this sector are selected in coordination with OSFI and informed by FINTRAC's risk model and reporting data. In 2018-19, FINTRAC completed two onsite joint examinations of banks with OSFI. These two examinations marked the completion of the pilot of joint assessments with OSFI and will inform the way forward for AML/ATF assessments of FRFIs.

Overall, FINTRAC notes that banks are investing significant resources to their AML/ATF programs; however, each bank seems to be at a different level in terms of the robustness and sophistication of their processes. Therefore, FINTRAC examination results vary widely within this sector. For this reason, it is difficult to draw conclusions or to compare examination findings between banks in a given year or between fiscal years.

Generally, as banks represent the largest reporting entities, with multiple lines of business and presence throughout Canada and other jurisdictions, one of the key challenges they face as a sector is ensuring line of sight into and across bank operations to monitor clients, transactions and STR indicators. FINTRAC examinations in this sector often identify a lack of awareness or consistent application of AML/ATF policies, procedures and training within bank operations.

### Banking Sector Examination Findings

During its examination of the two banks, [REDACTED] FINTRAC found that [REDACTED]

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FINTRAC's examination provided the banks with guidance on improving the identified gaps. Each bank was required to submit an action plan [REDACTED]

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#### Case Example: Findings of a FINTRAC-OSFI Examination [REDACTED]

This was the first time FINTRAC conducted a comprehensive examination of [REDACTED]

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During its examination, FINTRAC conducted a number of interviews with the staff in the bank's branches. From these interviews, FINTRAC [REDACTED]

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As a result, FINTRAC required that the bank respond to examination findings by developing an action plan with specific milestone targets to meet the requirements. Additionally, FINTRAC [REDACTED]

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The main objective of FINTRAC’s compliance activities is to change the behaviour of compliance. Since the examination, the bank has

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FINTRAC will continue to monitor the bank’s action plan to confirm that it is fulfilling its commitments to ensure its ongoing compliance with AML/ATF requirements by

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**FINTRAC and OSFI’s new Approach to Examinations of FRFIs**

Since 2013, FINTRAC and OSFI have both engaged in concurrent and joint examinations to monitor and assess the AML/ATF programs of FRFIs. In the last two years, the agencies piloted the joint assessment approach. Based on feedback the agencies received from FRFIs during the pilot, the recommendations of the FATF Mutual Evaluation Report, and their own assessment, both OSFI and FINTRAC have concluded that a new approach to the AML/ATF assessment of FRFIs is required.

Under the new approach, FINTRAC will assume primary responsibility for conducting independent AML/ATF examinations of FRFIs to ensure compliance with the PCMLTFA and associated Regulations. OSFI will fully support FINTRAC in taking on its expanded role. The agencies informed Finance Canada about this approach, which will be implemented over the course of the next two fiscal years to allow for the gradual transfer of responsibilities and knowledge and to facilitate change management.

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### *Real Estate Sector*

FINTRAC continued to prioritize the real estate sector in its examination strategy in fiscal year 2018-19 due to sector-wide vulnerabilities to money laundering. FINTRAC examined 190 reporting entities in the real estate sector in 2018-19. This accounts for approximately 38% of all FINTRAC examinations during the fiscal year.

FINTRAC's approach to examinations of the real estate sector is evolving to better take into account the nature of real estate transactions. For instance, one obligation for all reporting entities is to assess the AML/ATF risks of their clients. However, based on the nature of this business, entities in this sector usually deal with one-off clients and do not usually build long-term business relationships with their clients. Therefore, when considering the effectiveness of a real estate entity's compliance program, FINTRAC will

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### **Real Estate Sector Examination Findings**

Reporting entities in the sector performed well with respect to their obligations to appoint a compliance officer (94% of real estate businesses were fully compliant with this requirement), to conduct third party determination (94%) and to verify the identity of their clients (74%), when these elements were scoped into the examination.

However, examinations uncovered deficiencies with the requirement to risk assess clients (64% were partially non-compliant with this obligation, and 31% were in complete non-compliance), when this element was scoped into the examination. The examinations uncovered that many real estate businesses use a risk assessment checklist provided by

CREA, but fail to supplement the information with a justification or rationale as to why a specific rating was assigned to a given risk factor. These businesses were therefore found to be partially non-compliant with the risk assessment obligation.

FINTRAC also found deficiencies with the requirement to document and implement policies and procedures (65% were partially non-compliant and 11% were in complete non-compliance), when this element was scoped into the examination. Reporting entities are responsible to document policies and procedures for all AML/ATF obligations applicable to their business. For businesses that were found to be partially non-compliant with the requirement, FINTRAC found that their policies and procedures were missing certain elements, such as documenting ongoing monitoring and business relationship requirements, as well as special measures implemented based on the business' risk assessment. Finally, although this did not occur frequently, FINTRAC uncovered certain instances of unreported STRs.

### **Challenges in Real Estate Examinations**

The size of the real estate sector represents a challenge for FINTRAC to maintain accurate and up-to-date data on these reporting entities. In 2018-19, FINTRAC dedicated some resources to identify new reporting entities across this sector. Some of these newly identified reporting entities have been placed on the examination plan for 2019-20. Moreover, the recent MOU with RECBC will allow FINTRAC to update its reporting entity population for real estate businesses licensed in British Columbia.

FINTRAC prioritizes a significant share of its examination resources to the real estate sector; however, the number of real estate examinations that FINTRAC can feasibly conduct in a given year remains very small, given its examination resources when compared to the thousands of real estate entities that operate across the country. The new funding FINTRAC received in Budget 2019 will allow FINTRAC to further increase its compliance outreach and examinations in the real estate and casino sectors, with a focus on British Columbia.

### ***Casino Sector***

FINTRAC follows a cycle-based examination strategy for the casino sector. The cycle ensures that all 18 casino reporting entities in this sector are examined every two to five years depending on their size, compliance history and risk factors. Last fiscal year, FINTRAC examined five casinos entities in four provinces.

Casinos have a unique challenge with customer due diligence obligations under the PCMLTFA. As approximately 90% of their relationships with customers are one-off transactions, only 10% involve regular transactions that constitute a business relationship

and therefore have ongoing monitoring requirements. Because of the nature of how casinos operate, they do not always know who their customers are and transactions often remain anonymous because there are no customer identification requirements until threshold transactions are conducted or an account is opened with the casino.

Overall, casinos remain cash intensive businesses and most clients continue to use cash for their casino play. As of January 2018, based on the recommendation of an independent investigation in money laundering in British Columbia casinos, all cash, bank drafts and certified cheque buy-ins of \$10,000 or more have to be accompanied by a receipt to confirm the source of funds. These receipts must show the financial institution, branch number and account. This has potential of limiting the risk associated with the validity of the funds.

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### Casino Sector Examination Findings

Examinations conducted in the casino sector found positive results regarding reporting obligations. FINTRAC found few issues with respect to quality, timing and volume of reporting obligations. Casinos were found fully compliant with obligations to identify clients and to keep records.

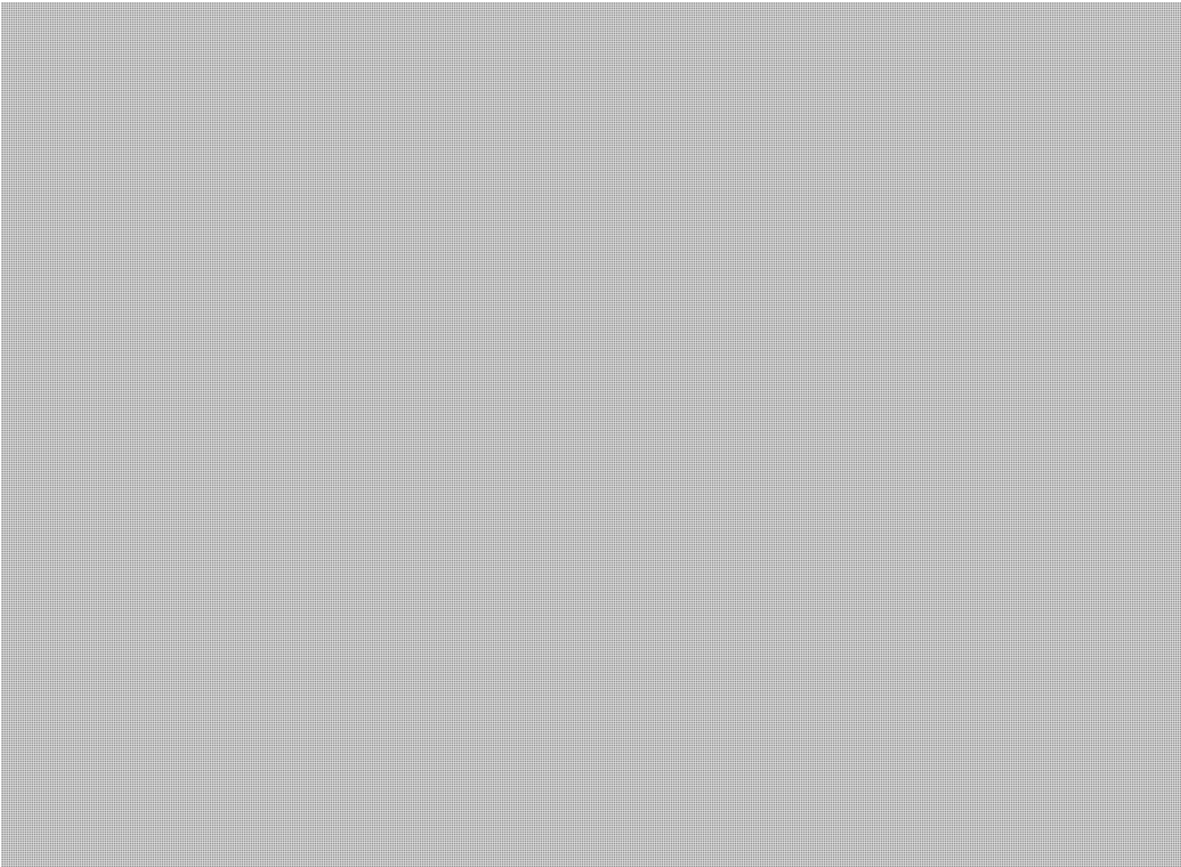
In relation to compliance program requirements,

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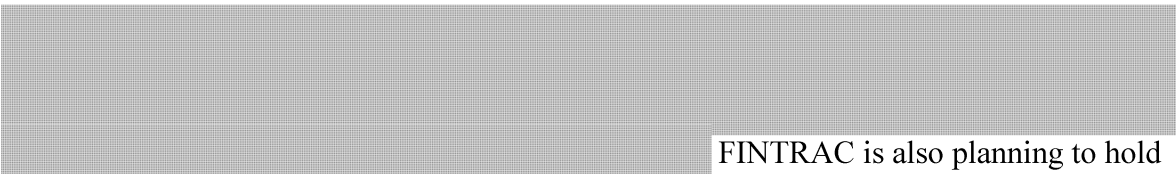
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**Challenges in Casino Examinations**

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FINTRAC is also planning to hold a Casino Forum in 2019-20, which will bring together all casino reporting entities as well as provincial gaming regulators for an open and transparent dialogue.

***Money Services Business Sector***

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FINTRAC examined 112 MSBs last fiscal year. Reporting entities were selected for an examination based on their [redacted] as assessed by FINTRAC's risk model. [redacted]



### **Money Services Business Sector Examination Findings**

In the examinations conducted in 2018-19, FINTRAC found that MSBs performed well in terms of their obligations to appoint a compliance officer (93% were fully compliant with the requirement), to verify the identity of clients (99%) and to conduct third party determination (100%), as well as on training obligations (83%), when these requirements were scoped into the examinations. MSBs also demonstrated positive results for meeting reporting obligations.

Some deficiencies were identified in the examinations, notably in incomplete policies and procedures (61% of MSBs were partially non-compliant with the obligation, and 11% were fully non-compliant) and in risk assessments (49% were partially non-compliant, and 18 were fully non-compliant), when these requirements were scoped into the examinations. However, it should be noted that a number of examinations conducted in this sector in the last fiscal year were of new MSBs that had never been previously examined by FINTRAC.

FINTRAC addressed instances of non-compliance in the MSB sector by including two reporting entities as candidates for follow-up examinations. Additionally, two MSB examinations that resulted in considerable non-compliance were recommended for a penalty. FINTRAC plans to issue a penalty on one of these MSBs this year. Moreover,

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### **Challenges in MSB Examinations**

FINTRAC has determined that the average lifespan of an MSB can be less than three years due to the transient nature of the sector. Often, MSBs will close after a very limited lifespan or reopen under a different name. The challenge to FINTRAC is to identify these MSBs early and ensure that a compliance examination takes place.

At times, the entities register with FINTRAC and do not contact the Centre for revocation of their MSB status. If such entities are selected for compliance examinations, on a risk-based approach, and are no longer operating, FINTRAC has to cancel these examinations.

FINTRAC conducts annual MSB validations to verify that MSBs that have expired, ceased, been revoked or denied registration are no longer operating. If there are indications that an MSB is operating but is not registered, FINTRAC contacts the business and takes appropriate follow-up action.



### 3. Results of Follow-Up Examinations

Follow-up examinations form part of FINTRAC's strategy to validate if non-compliance observed in previous examinations has been corrected. In this methodology, the scope of the examination remains consistent with the elements that were included in the previous examination to concretely measure the improvement in a reporting entity's compliance levels.

Of the 497 examinations that FINTRAC conducted in the 2018-19 fiscal year, 19 were follow-up examinations in a variety of sectors. Of these, FINTRAC found that 15 (79%) reporting entities in a variety of sectors demonstrated a positive change in behavior, and four (21%) showed negative change in behaviour. These results demonstrate the effectiveness of follow-up examinations as a tool to encourage compliance and measure behaviour change.

In the case of the four entities that demonstrated a negative change in behavior, the examination results led FINTRAC to consider issuing a penalty to one MSB and to require a large casino to submit an action plan. For the third reporting entity, FINTRAC determined that one real estate broker had made significant progress by filing nine STRs in the past 12 months. Therefore, FINTRAC did not take any follow-up action on this reporting entity. Finally, the fourth reporting entity was a small credit union, where the examination uncovered that the deficiencies were of lower harm.

### 4. Addressing Reporting Issues

*A New Approach for Resolving Reporting Issues of Large Reporting Entities is Showing Positive Results*

In 2018-19, FINTRAC took a holistic approach in addressing [REDACTED] reporting issues in an effort to [REDACTED]

The approach consisted of [REDACTED]

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Since its engagement with FINTRAC, [REDACTED] has demonstrated significant improvements in [REDACTED]

[REDACTED] In addition, the approach has created a mechanism for having other types of discussions with the reporting entity. [REDACTED]

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has also expressed appreciation for the opportunity to work more closely with FINTRAC and receive feedback. This approach was also used with [REDACTED] and is a viable solution to address reporting issues of other reporting entities.

*Examinations and Voluntary Self-Declarations of Non-Compliance Inform FINTRAC of Over-Reporting*

In the last fiscal-year, FINTRAC identified multiple instances of over-reporting. FINTRAC generally finds over-reporting by reviewing samples of an entity's submitted reports in the course of the examination process, as a result of ongoing monitoring of all reports submitted, or when a reporting entity provides a VSDONC. This has resulted in FINTRAC's segregation and deletion of over 12 million reports in the past fiscal year. The reporting entity is also contacted or instructed to delete the over-reported reports. This process ensures that FINTRAC is only retaining reports it has the authority to receive, ensuring the Centre's compliance from a privacy perspective.

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**Case Example: Large reports segregation case involving [REDACTED]**

Through FINTRAC's ongoing monitoring of all reports submitted by reporting entities, FINTRAC identified an abnormally large number of reports submitted by [REDACTED] that were triggered by FINTRAC's validation rules for the same reporting issue.

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FINTRAC requested an explanation from the bank. In response, [REDACTED] conducted an in-house review of its reports and identified roughly 9.1 million reports that they deemed as over-reporting. These reports should not have been reported to FINTRAC as they did not meet the 24-hour rule<sup>3</sup> and were submitted due to incorrect aggregation.

FINTRAC worked closely with [REDACTED] to identify all over-reported reports and [REDACTED] submitted an action plan to delete these in batches over 30-days. FINTRAC approved the proposal. Once [REDACTED] confirmed the deletion, FINTRAC queued these reports for segregation in its own database and reports were segregated within 30 days.

*Database Examinations Measure Improvements in Data Quality of Reports*

A database examination is an in depth analysis of a reporting entity's reporting deficiencies concerning the quality of data in reports based on findings of a previous FINTRAC examination. Its main purpose is to identify changes in reporting behaviour as well as select potential candidates for a follow-up examination.

<sup>3</sup> Under the 24-hour rule, transactions that are in amounts of less than \$10,000 each but that total \$10,000 or more within a 24-hour period are reportable to FINTRAC when they are conducted by or on behalf of the same client.

In 2018-19, FINTRAC conducted 54 such reviews, with the focus on assessing behaviour change by reviewing data quality deficiencies previously identified during the examination. Of the 54 such reviews, only 22 reporting entities had submitted sufficient reports to conclude behavior change. The in-depth review of those reporting entities found that they all (100%) demonstrated a positive change in behaviour, correcting data quality deficiencies identified during a FINTRAC examination. In other words, the change in behavior for those 22 reporting entities demonstrates the effectiveness of FINTRAC's compliance activities. FINTRAC will follow-up with another review for the remaining 33 reporting entities that could not be assessed due to insufficient data for a proper assessment.

These reviews demonstrate how FINTRAC examinations can directly affect positive changes in reporting entity behaviour in terms of improving the quality of data provided in reports.

### 5. STR Analysis

In the 2018-19 fiscal year, FINTRAC formalized a new approach to support more effective examinations. Under this approach, FINTRAC [REDACTED]

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[REDACTED] The purpose of this is to test the effectiveness of the examined entity's risk based approach with respect to identifying suspicious transactions. Under this approach, FINTRAC prepares its examination by [REDACTED]

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[REDACTED] The approach helps FINTRAC identify potentially suspicious transactions and verify whether the examined entity should have submitted STRs.

Initial indications are very promising as this approach is proving more effective in identifying reporting deficiencies compared to other approaches. Specifically, the STR analysis has significant potential for [REDACTED]

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[REDACTED] Moreover, FINTRAC regional compliance officers have provided positive feedback on the use of this approach and have highlighted that the methodology is highly useful in preparing for examinations.

## D) Enforcement Activities

When needed, FINTRAC uses a variety of enforcement tools to address non-compliance situations. This includes requiring reporting entities to submit action plans, conducting follow-up examinations to assess if previous non-compliance has been addressed, issuing penalties in cases of serious or repeat non-compliance and submitting non-compliance disclosures to law enforcement in cases of extensive non-compliance.

### 1. Administrative Monetary Penalties

RC6 Following the publication of its AMP policy as part of FINTRAC's Transparency Initiative, FINTRAC proceeded in 2018-19 with the issuance of its first penalty under the new AMP methodology. The AMP was issued to a MSB, [REDACTED]

[REDACTED] which paid the penalty in full without requesting a review of the AMP by the Director and CEO of FINTRAC.

### 2. Non-Compliance Disclosures to Law Enforcement

RC2 In the last fiscal year, FINTRAC made seven non-compliance disclosures [REDACTED]

RC6 [REDACTED] A non-compliance disclosure is made to law enforcement when there is extensive non-compliance with the PCMLTFA or little expectation of immediate or future compliance by the reporting entity. The disclosures were produced by FINTRAC as a result of information included in voluntary information records provided by law enforcement.

The large number of disclosures produced in 2018-19 demonstrates law enforcement's increased awareness and interest in investigating non-compliance offences under the PCMLTFA and associated regulations, as well as using FINTRAC non-compliance disclosures as a mechanism by which to achieve this.

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RC6 [REDACTED] non-compliant MSBs, and more specifically businesses that deal in virtual currency. FINTRAC cannot disclose on these businesses as they are not currently subject to the PCMLTFA until June 2020. However, this provided an opportunity to inform regime partners about FINTRAC's mandate, non-compliance offences, covered businesses, and upcoming legislative and regulatory amendment that will subject dealers in virtual currency to AML/ATF obligations.

### 3. Public Naming

Under the Parliamentary Review of the PCMLTFA, FINTRAC has worked with Finance Canada to strengthen the Centre's public naming authorities of its AMP program by proposing legislative amendments that would address outstanding issues of fairness, transparency and the deterrence effect of AMP public naming.

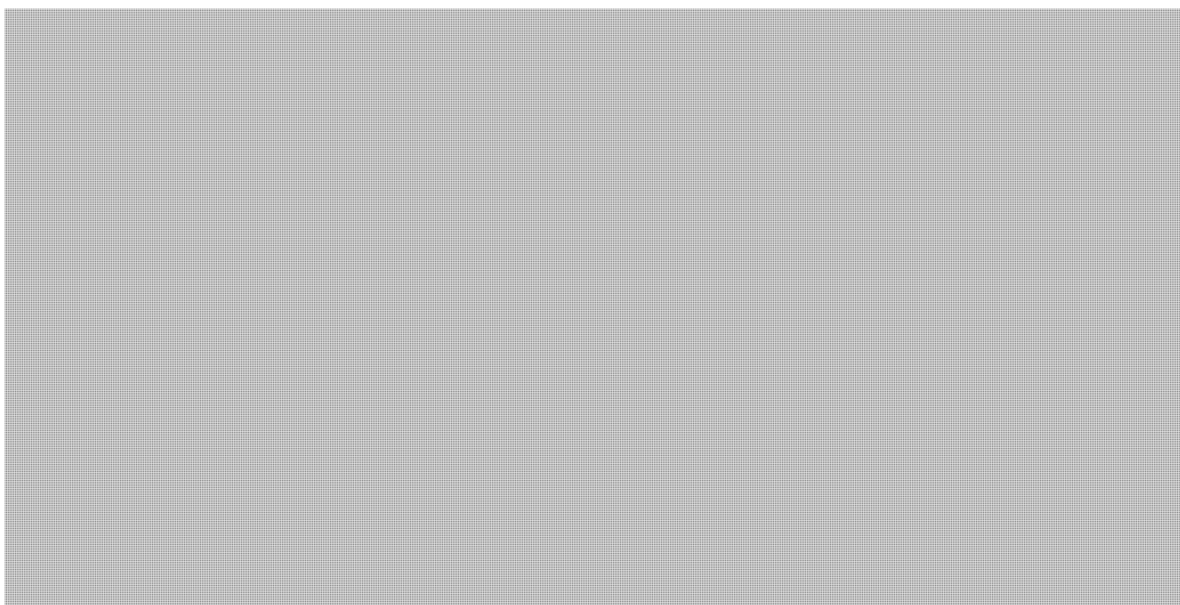
FINTRAC welcomes the adoption of recent legislative changes to the PCMLTFA which addresses outstanding issues with certain aspects of the Centre's public naming authority. FINTRAC must now publish information on all AMPs imposed. The amendment also now clearly sets out the different stages of the process when FINTRAC must publish this information. It also clarifies that certain information under the PCMLTFA, such as the identity of the reporting entity, the nature of a violation and the amount of an AMP, cannot be subject to a confidentiality order in the course of an appeal to the Federal Court.

FINTRAC's AMP policy and applicable templates have been updated to reflect the changes to the public naming authority. In accordance with its public naming authority, FINTRAC will also update its website to provide additional details on all AMP cases in response to the recommendations of the third party reviewer.

## IV. FINTRAC'S CONTRIBUTION TO IMPROVING THE EFFECTIVENESS OF AML/ATF EFFORTS

### A) Parliamentary Review of the PCMLTFA

FINTRAC continued to participate and monitor the House of Commons Finance (FINA) Committee review of the PCMLTFA. This included appearing before the Committee on multiple occasions to answer Parliamentarians' questions.



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### B) Upcoming Compliance Priorities

#### 1. British Columbia Public Inquiry

In response to three independent reports on the state of money laundering in British Columbia, the province will hold a public inquiry into money laundering.

The financial intelligence that FINTRAC generates and discloses to police, law enforcement and national security partners have supported ML/TF investigations and prosecutions across Canada and have been met with very positive feedback. FINTRAC is committed to making any improvements needed to ensure that it continues to deliver on its mandate to the highest standard possible for Canadians and working with the province in response to the public inquiry.

In 2018-19, FINTRAC provided 2,274 financial intelligence disclosures to regime partners, up nearly 100 percent over the past five years. Of these financial intelligence disclosures, 332 were provided to police and law enforcement agencies in British Columbia.

FINTRAC financial intelligence disclosures often show links between individuals and businesses that have not been identified in an investigation, and help investigators refine the scope of their cases or shift their sights to different targets. They are also used by law enforcement to put together affidavits in order to obtain search warrants and production orders. FINTRAC receives hundreds of feedback forms from disclosure recipients every year, with about 90 percent of them indicating that the Centre's financial intelligence was valuable in providing new information on known subjects, identifying additional or unknown subjects, verifying information already known and/or triggering a new investigation.

Notwithstanding these accomplishments, FINTRAC recognizes that outstanding challenges remain to Canada's AML/ATF regime, including the coverage of the legal profession, the level of compliance of the real estate sector and the need to enhance information sharing between regime partners. FINTRAC believes that current efforts, such as the newly signed MOU with RECBC and new public-private partnership initiatives under Budget 2019 will help meet some of recommendations raised in the independent reports. FINTRAC will continue to work with Finance Canada in strengthening Canada's AML/ATF regime and addressing these recommendations, while respecting the Charter rights of Canadians.

## **2. Implementation of New Regulatory Amendments**

The total cost of implementing systems changes required for Regulations Package #2 and ensuring compliance with the revised regulations was originally estimated by FINTRAC to be \$32.8 million. In its proposal to Finance Canada for Budget 2019, FINTRAC indicated that it would re-allocate \$15.9 million of existing resources over five years (with a peak of 39 FTEs in years two and three) and requested new funding of \$16.9 million over five years and \$1.4 million ongoing. However, Budget 2019 only provided \$9.7 million over five years, with a peak of 7 FTEs in year two, as well as \$0.5 million ongoing with two FTEs.

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### **3. FINTRAC's Compliance Engagement Strategy**

To further educate various reporting entity sectors on their AML/ATF obligations and improve their compliance, FINTRAC has developed a Compliance Engagement Strategy for 2019-20 to 2023-24 that consists of four priorities:

- 1) Work with existing and new reporting entities, industry associations and regulators to effectively implement regulatory amendments published in June 2019;
- 2) Work with the British Columbia government, as well as with the real estate and casino sectors (including businesses, regulators and associations) across Canada to enhance the understanding and compliance of these sectors with their PCMLTFA obligations;
- 3) Assess and strengthen relationships with current and new domestic and international MOU partners; and
- 4) Continue to engage with all sectors and other stakeholders through different forums and approaches.

Under each priority, a number of activities have been identified and will involve collaboration with other sectors in the Centre and different external stakeholders. For example, under the first priority, a series of information sessions are planned in November and December 2019 to inform reporting entity sectors on FINTRAC's interpretation of the recent regulatory amendments and explain how they will affect their respective sectors. In addition, FINTRAC will consult all sectors on draft guidance (new and existing) that FINTRAC will be developing in relation to these new regulatory provisions. FINTRAC also plans to explore new and innovative communications tools, under the second priority, to better educate the real estate sector on their obligations and on ML/TF trends.



## V. CONCLUSION

The 2018-19 fiscal year was marked by new developments in FINTRAC's compliance program, including: examination results that demonstrate the positive impact of the new assessment approach; FINTRAC's transparency initiative that provided more information to reporting entities and the public on FINTRAC's Compliance Framework such as its approach to examinations in the Assessment Manual and revised policies regarding the AMP program and public naming.

It was also a year marked by significant developments in FINTRAC's engagement with reporting entities and regime partners. The new approach between FINTRAC and OSFI to ensure the compliance of FRFIs will result in increased examination and relationship management demands for FINTRAC. The new MOU with RECBC represents an important step in further strengthening FINTRAC's regulatory oversight of the real estate sector in British Columbia. Ensuring compliance in this sector however remains a challenge and, as such, in 2019-20 FINTRAC will continue to allocate important resources to conducting examinations in this sector.