

## **Real Estate Developers Brought Within Ambit of Money Laundering Legislation**

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Even before the terrorist attacks of September, 2001, the government of Canada had embarked on a campaign to tackle money laundering. The first bill about money laundering was introduced in Parliament in 1987. Anti-terrorist provisions contained in the *Criminal Code* were first introduced in 2001 on the heels of the September 11 attacks. The two concepts, money laundering and terrorist financing are, of course, closely linked. One prong of the attack on these scourges has been brought by way of the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act, 2000, c. 17* (the "Act"). As of February 20, 2009, real estate Developers are subject to this legislation.

The theory behind the government's money laundering/terrorist financing legislation is that cash transactions of \$10,000.00 or more should be tracked by obtaining as much personal identification and transaction details as possible with respect to the participants in the transaction and the subject matter of the transaction. It is felt that the more light that is shone on a cash transaction, the less likely a money launderer/terrorist financier will chose Canada as the place for their illegal activities. Information regarding certain day-to-day business transactions is also subject to the legislation.

The government's approach recognizes, however, that not all businesses should be subject to regulation in the money laundering/terrorist financing context. Thus, the government has sought to legislate broader transaction reporting for businesses that are likely targets of money launderers and terrorist financiers. Financial services entities have been subject to the money laundering legislation since 2002. Life insurance companies, securities dealers, money service businesses, accounting firms, real estate brokers, casinos and departments and agencies of Her Majesty the Queen are also entities that are currently subject to the *Act*. These entities have been phased in over time. Law firms were brought within the legislation at December 31, 2008.

Bill C25, which received royal assent in December, 2006, includes a number of amendments that will come into force on February 20, 2009 and will extend the coverage of the *Act* to real estate Developers.

Specifically, real estate Developers will be brought into the legislation by virtue of Regulation SOR/2008-21, at Section 4. That section creates a new Section 39.5 to the main Regulation SOR/2002-184, so that real estate Developers are included in the money laundering legislation. Under that new section, a real estate developer is defined as a person or corporation who, in any calendar year after 2007, has sold to the public at least five new houses or condominium units, or at least one new industrial building or one new multi-unit residential building. Thus, a Developer under the legislation is, in fact, what is commonly referred to as a

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builder. Traditional Developers (i.e., those parties that are further upstream in the development process and sell lots on an aggregate basis) are not subject to the legislation.

Beginning in February, 2009, Developers, as so defined, will be obliged to keep records of sales, verify the identify of purchasers, report large cash transactions to a centre called the Financial Transactions and Report Analysis Centre of Canada (the "Centre") and establish an internal compliance program. These obligations will be discussed in greater detail below.

In the case of the money laundering/terrorist financing legislation, what Developers don't know can hurt them. Contravening the key provisions in the legislation can result in maximum fines up to \$2,000,000.00 and prison terms of up to five years (see ss. 74 to 77.1 of the *Act*). Under the legislation, officers, directors or agents of corporations are deemed to be parties to and guilty of any offences so long as they direct, authorize, assent to, acquiesce in or participate in the commission of an offence under the *Act* (see s. 78 of the *Act*). Persons charged under the *Act* can be exonerated if they establish that they exercised due diligence to prevent the commission of an offence under the *Act* (see ss. 77(2) and 79(b) of the *Act*).<sup>2</sup>

The six main areas of the money laundering/terrorist financing legislation are as follows:

1. **Reporting** - If a real estate Developer, after February 20, 2009, receives \$10,000.00 in cash or more in respect of a single transaction<sup>3</sup>, they are to report it to the Centre (see s. 39.6, SOR/2002-184 as amended), together with the information set out in [Schedule 1](#) of SOR/2002-184. The report is to be sent to the Centre within 15 days. A report is not required if the cash comes from a financial entity or public body. Schedule 1, which sets out the contents of a large cash transaction report is divided into seven sub-parts. In the standard real estate transaction, there are only five parts that are relevant to the Developer and, indeed, one of those parts only applies if the Developer is of the view that the transaction is being conducted by one person, on behalf of another. Thus, under Part A of Schedule 1, the Developer is to provide information about itself. This involves indicating what type of entity it is, within the framework of the money laundering legislation (i.e., real estate Developer). The full name of the reporting entity is to be set out. A name and phone number of a contact person is also required. Part B of Schedule 1 requires information on the transaction, including the date of it, the time, the posting date, the purpose and details of the transaction and how the funds were received. The method by which the transaction is conducted is to be included in Part B (i.e., in branch or office, ABM, armoured car, mail deposit, courier or other). Part C requires that account information be provided. The Regulation is unclear as to which account information is being sought. Since the report is triggered in the event of a cash transaction, it appears that the Regulation requires information in respect of the receiving entity's bank account in order to show where the funds were deposited. Part D requires information regarding the Developer's customer. Thus, their name, client number, address, personal telephone number, country of residence, identification reviewed by the Developer as part of its due diligence (discussed below), the customer's date of

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<sup>2</sup> See the FINTRAC web page at [www.fintrac-canafe.gc.ca](http://www.fintrac-canafe.gc.ca) for a helpful guide on how to comply with the *Act*.

<sup>3</sup> Cash transactions under \$10,000.00 must be reported, in writing, if they relate to the same client and, within a 24 hour period, add up to \$10,000.00.

birth, business telephone number and occupation are to be set out. If it is determined that the person who is present to conduct the transaction is actually conducting the transaction on behalf of a different person, similar identifying information is to be obtained in respect of the beneficial purchaser. If the beneficial purchaser is a corporation, basic corporate information (including the incorporation number and place of business) is to be obtained.

In addition to reporting prescribed transactions (i.e., cash transactions in excess of \$10,000.000), Section 7 of the *Act* mandates that Developers (and other entities) report any transaction reasonably suspected to be related to the commission of a money laundering offence or a terrorist activity financing offence. These types of offences are defined in the *Criminal Code*. A money laundering offence is defined in Section 462.3 (1) of the *Code*. Money laundering offences involve dealing with funds when one intends to conceal the fact that these funds were obtained as part of the commission of an offence. A terrorist activity financing offence is defined under Section 83.02 of the *Criminal Code* and involves providing or collecting funds so that they can be used to cause death or serious bodily harm to a civilian, with a view to intimidating the public or compelling a government to do or refrain from doing any act. If a Developer suspects that one of its property sales is part of money laundering or terrorist activity financing, it is to report to the Centre. The Developer must also report if it has property in its possession or control that it knows is owned by a terrorist or terrorist group.

2. **Verifying Identify** – When a Developer receives funds in any real estate Developer transaction, it is to ascertain the identity of every person who "conducts the transaction" (see s. 59.5 of SOR/2002-184 as amended). Although the legislation is not clear on this point, it appears that a person who conducts the transaction would be limited to the buyer or the person who is acting on behalf of a buyer. In other words, the person who is in the office signing the papers would be a person conducting the transaction. If the Developer determines that there is someone not present on who's behalf the transaction is being conducted, that person's identify must also be ascertained and verified.

When a Developer is conducting a transaction with a person who is present, the ascertaining of identity is relatively straightforward. The Developer should check the person's birth certificate, driver's licence, passport or other reliable photo identification (provincial health card is not acceptable), write down the type of personal ID chosen and the ID number.

If the person for whom the transaction is being conducted is not present, a highly complicated process ensues. One possibility is obtaining the name and date of birth of the not present person and confirming that the person has already had their identity ascertained by a major financial institution.

If the person conducting the transaction is not present and has not been cleared by a major financial institution, a five point ascertaining of identity process is activated. If the Developer's customer can meet any two of the five point test (except points (i) and (ii) below, which only count as one even if both are obtained and except points (iv) and (v) below, which only count as one even if both are obtained), their identity has been ascertained. Those five points are as follows:

- (i) the Developer obtains a reliable identification product, based on personal information and a Canadian credit history of that person that is at least six months old;
- (ii) the Developer confirms the name, address and date of birth of its customer by referring to a credit file that is at least six months old;
- (iii) a commissioner of oaths or guarantor (as defined) executes a confirmation of the person's identity on a legible copy of reliable photo identification;
- (iv) the Developer is provided with proof that a cheque has cleared an account that is not a business account, mutual fund sales account, life insurance account, other insurance account, RRSP, pension, account regulated by a securities regulations or a group plan account. In other words, a cheque has cleared on a personal account of the person; and
- (v) the Developer ascertains that the person has a deposit account that is not one of the prohibited accounts discussed in (iv) above. In other words, the person has a deposit account that is a personal account.

In the event the Developer is dealing with a corporation as its purchaser, the corporation's name, address and the names of its directors must be ascertained by referring to its certificate of corporate status, (the record that is required to be filed annually under the applicable corporations legislation or any other record that ascertains its existence as a corporation). In the event the Developer's customer is a partnership, that identity shall be confirmed by referring to a partnership agreement, articles of association or other similar record that ascertains the non-corporate, non-individual entity's existence.

The method by which identity was ascertained then has to be recorded, as does all the data that emerged from the identity ascertaining process. Details in this regard are set out in Section 67 of SOR/2002-184, as amended.

At times, the Developer will have an arm's length realtor act as its agent. It would appear that based on the law of principal and agent, the agent could conduct the verification and satisfy the obligation for the Developer. The Developer, however, has to obtain a copy of the realtor's verification file as part of its record keeping obligations (see below).

3. **Record Keeping** – In addition to ascertaining the identity of all the Developer's customers and reporting \$10,000.00 or more cash and other suspicious transactions, there is an obligation to keep extensive records relating to any receipt of funds (cash or otherwise) and every sale of a house or other unit (see s. 39.7 of SOR/2002-184 as amended). In respect of the receipt of funds, a receipt of funds record must be kept in respect of every amount that a Developer receives in the course of a single transaction (unless those funds are received from a financial entity or public body). A client information record must be kept in respect of every sale of a house or other unit. If the receipt of funds record or the client information record is in respect of a corporation, the Developer must obtain a copy of the part of the official corporate records that contains any provision relating to the power to bind the corporation in respect of the transaction in question. A receipt of funds record is not required if the same transaction

triggered the large cash transaction report obligation. Thus, there is some protection in the *Act* against redundancy. Receipt of funds records and client information records are defined in s. 1 of Regulation SOR/2002-184 and amount to no more than recording the incoming funds and ascertaining the identity of the person, corporation or other entity that has conducted the transaction.

4. **Establish Compliance Program** – Under Section 71 of Regulation SOR/2002-184 (as amended), extensive obligations for setting up a compliance program are mandated. The Developer must appoint a person responsible for implementing the program. The Developer must develop and apply written compliance policies and procedures that are kept up to date and approved by a senior officer. The Developer must assess and document the extent to which their business is an "at risk" entity in the sense of anticipating the extent to which the Developer will be the subject of a money laundering offence or a terrorist activity financing offence. The Developer must develop and maintain a written, ongoing compliance training program for employees and institute a review of the policies, risk assessments and training, which review is to be carried out every two years by an internal or external auditor.

5. **Other Issues** – In addition, under Section 69 of Regulation SOR/2002-184 (as amended), records are to be kept for five years, following the date of the transaction. There is some ambiguity in the Regulation about when the transaction is completed. Accordingly, it is suggested that records be kept for five years following the last transaction between the Developer and its customer - the outside date mandated under the *Act*. In the case of an electronic funds transfer, additional information, including the name, address and account number or other reference number of the electronic transfer must be maintained as part of the financial transaction record. Compliance measures are set out in ss. 62- 65 of the Act. These measures pertain largely to duties on the reporting entity to co-operate with officials in regards to inspection of records and general assistance, subject to lawyer/client privilege.

6. **Administrative Monetary Penalty Scheme** - A new administrative monetary penalty scheme came into force on December 30, 2008. The new Regulation SOR/2007-292, divides the various infractions of the legislation and Regulations in accordance with whether they are "minor", "serious" or "very serious". The penalties in respect of these administrative offences are financial as opposed to custodial. Minor offences attract a penalty of up to \$1,000.00. A serious violation attracts a penalty of up to \$100,000.00. A very serious violation attracts a penalty of up to \$500,000.00.

Having gone over the various obligations under the *Act*, it is interesting to note which violations the government sees as minor and which ones it sees as serious. From the real estate Developer's perspective, here are the main administrative penalties and their classification:

<b>Short Form Description of a Violation</b>	<b>Classification of Violation</b>
Failure to give assistance to the authorized person inspecting the business	Serious
Failure to report an electronic funds transfer no later than five working days after the transfer	Minor

<b>Short Form Description of a Violation</b>	<b>Classification of Violation</b>
Failure to implement a compliance program	Serious
Failure to develop compliance policies	Serious
Failure to assess and document the risk inherent in the business in respect of money laundering or terrorist activity financing	Serious
Failure to develop ongoing compliance training programs for employees	Serious
Failure to institute and document the two year review process	Serious
Failure to report a transaction where the entity suspects there has been a money laundering offence or a terrorist activity financing offence	Very serious
Failure of a real estate Developer to report the receipt of \$10,000.00 or more in cash	Minor
Failure of a real estate Developer to keep prescribed records when engaging in development activities	Minor
Failure of a real estate Developer to keep a large cash transaction record in respect of \$10,000.00 or more in cash received	Minor
Failure to take measures to ascertain the identify of a person conducting a transaction	Minor
The opening of an account for a client when the identity of the client cannot be established in accordance with prescribed measures	Serious
Failure of a real estate Developer to ascertain the identity of a person who conducts a prescribed transaction	Minor
Failure to confirm the prescribed information in respect of a corporation	Minor
Failure to confirm the existence of a non-individual, non-corporate entity	Minor

## SCHEDULE 1

(Paragraph 12(1)(a), sections 17 and 21, paragraph 28(1)(a), sections 33.1, 35, 38, 39.2 and 39.6, paragraph 40(1)(a), section 47 and subsections 52(1) and (3))

### LARGE CASH TRANSACTION REPORT

#### PART A — Information on Place of Business Where Transaction Occurred

- 1.\* Type of reporting person or entity, as described in paragraphs 5(a) to (h), (k) and (l) of the Act, and, if reporting person or entity is referred to in paragraph 5(i) or (j) of the Act, type of business, profession or activity of reporting person or entity, as described in sections 16, 34, 37, 45 and 46 of these Regulations
- 2.\* Identification number of place of business where transaction occurred (e.g., institution's identification number, licence number or registration number), if applicable
- 3.\* Full name of reporting person or entity
- 4.\* Full address of place of business where transaction occurred
- 5.\* Name and telephone number of contact person

#### PART B — Information on Transaction

- 1.\* Date of transaction or night deposit indicator
2. Time of transaction and, for a transaction for which the date is provided in item 1, the posting date (if different from the date of the transaction)
- 3.\* Posting date for a transaction for which night deposit indicator is provided in item 1, if date of transaction is not provided
- 4.\* Purpose and details of the transaction, including amount of transaction and currency of transaction
- 5.\* Disposition of funds, amount of disposition, currency of disposition and, if applicable, name and number of each other institution and name, account number and policy number of each other person or entity
- 6.\* Method by which the transaction is conducted (in branch or office, ABM, armoured car, mail deposit, courier or other)

#### PART C — Account Information (if applicable)

- 1.\* Account number
- 2.\* Branch number or transit number
- 3.\* Type of account (personal, business, trust or other)
- 4.\* Full name of each account holder
- 5.\* Type of currency of the account

#### PART D — Information on Person Conducting Transaction That Is not a Deposit Into a Business Account (if applicable)

- 1.\* Person's full name
- 2.\* Client number provided by reporting person or entity, if applicable
- 3.\* Person's full address
4. Person's personal telephone number
5. Person's country of residence
- 6.\* Person's type of identifier (e.g., driver's licence, birth certificate, provincial health insurance card — if such use of the card is not prohibited by the applicable provincial law — or passport) and identifier number
- 7.\* Place of issue of person's identifier (province or state, country)
- 8.\* Person's date of birth
9. Person's business telephone number
- 10.\* Person's occupation

PART E — Information on Person Conducting Transaction That Is a Deposit Into a Business Account Other Than a Night Deposit or a Quick Drop (if applicable)

- 1.\* Person's full name

PART F — Information on Entity on Whose Behalf Transaction is Conducted (if applicable)

- 1.\* Entity's full name
- 2.\* Entity's incorporation number and place of issue of its incorporation number, if applicable
- 3.\* Entity's type of business
- 4.\* Entity's full address
5. Entity's telephone number
6. Full name of each person — up to three — who is authorized to bind the entity or act with respect to the account

PART G — Information on Person on Whose Behalf Transaction is Conducted (if applicable)

- 1.\* Person's full name
- 2.\* Person's full address
3. Person's personal telephone number
4. Person's business telephone number
5. Person's type of identifier (e.g., driver's licence, birth certificate, provincial health insurance card — if such use of the card is not prohibited by the applicable provincial law — or passport) and identifier number
6. Place of issue of person's identifier (province or state, country)
7. Person's date of birth
8. Person's occupation
9. Person's country of residence
10. Relationship of person conducting the transaction to the person on whose behalf the transaction is conducted