



Guideline Impact Analysis Statement

B-8 Deterring and Detecting Money Laundering and Terrorist Financing

December 2008

I. Background

OSFI's Guideline B-8, Deterring and Detecting Money Laundering, was originally released in 1996 and was revised in 2003 and again in 2004 to reflect changes to Canadian legislation, notably amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (PCMLTFA), and also to reflect the introduction of OSFI's anti-money laundering assessment program.

In December 2006, the PCMLTFA was substantially revised (through Bill C-25) with the purpose of aligning it more closely to international anti-money laundering and anti-terrorist financing standards as articulated by the Financial Action Task Force (FATF), of which Canada is a founding member. Legislative and regulatory requirements came into effect on various dates. For federally regulated financial institutions (FRFIs), the most significant of these were changes to the PCMLTFA and consequential amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations* (PCMLTFR), which took effect on June 23, 2008.

Amongst other things, the amended legislation and regulations require FRFIs (in addition to taking prescribed measures to identify clients and keep records) to implement an anti-money laundering and anti-terrorist financing (AML/ATF) compliance program, including the development and application of policies and procedures to assess, in the course of their activities, the risk of a money laundering offence or a terrorist activity financing offence; and, if the FRFI considers that this risk is high, take prescribed special measures for identifying clients, keeping records, and monitoring financial transactions in respect of the activities that pose the high risk. A particularly significant provision is the requirement to apply risk based measures (termed "reasonable measures" in the PCMLTFA and PCMLTFR) to areas identified as higher risk.

This Guideline highlights the need for FRFIs (except property and casualty insurance companies, cooperative credit associations and fraternal benefit associations) to develop and operate AML/ATF programs that address the risk of ML and TF as well as ensure regulatory compliance. The measures introduced by Bill C-25, together with the requirement to establish AML/ATF programs, will further reduce the susceptibility of FRFIs to being used by individuals or organizations to launder funds, thereby reducing their exposure to damage to their reputation, a key asset in the financial services industry.

In addition to issuing the Guideline, OSFI will continue assessing the AML/ATF programs operated by FRFIs.



II. Problem Identification

Many of OSFI's AML/ATF assessment findings to date relate to matters that have been addressed by the current Guideline. However, the passage of Bill C-25 and its associated regulations, the passage of time, and a longer record of experience, has identified the need to substantially re-write the Guideline. Specifically:

1. Much of the content of the 2004 Guideline has now been codified into compliance requirements with the passage of Bill C-25.
2. The introduction of a risk based approach to some control measures has amplified the need for OSFI to identify effective measures and communicate these to FRFIs
3. In March 2008, the FATF published its Mutual Evaluation Report (MER) on Canada. This evaluation identified the need for OSFI to significantly expand its AML/ATF guidance and apply clearer expectations of the risk management controls that FRFIs need to implement.

III. Objectives

The objective of revising Guideline B-8 is to assist FRFIs to develop and implement effective AML/ATF risk management controls to manage their exposure to ML and TF risk, as part of their AML/ATF programs.

The requirements to apply risk based measures to identified areas of higher risk allow FRFIs more flexibility to determine for themselves how to achieve the prescribed outcomes provided that the measures chosen are "reasonable". To be reasonable, the measures used must achieve the prescribed outcome.

The revised Guideline does not create any new regulatory requirements. Rather, it identifies measures that OSFI has found to be reasonable when applied effectively – i.e. when they achieve the prescribed outcomes.

Effective controls over ML and TF risk, and related regulatory and reputation risk, are essential.

In order to achieve effective controls, FRFIs will adopt different approaches to their AML/ATF programs that take into account the nature, scope, complexity and risk profile of their institution. FRFIs are expected to take into account the contents of this Guideline when implementing their AML/ATF programs. OSFI's AML/ATF assessment program, which aims to assist OSFI in evaluating the effectiveness of controls, takes the foregoing into consideration in the assessment of individual institutions.

Consequential objectives of the revised Guideline include; discussing the relationship between the Guideline and OSFI Guideline E-17 Background Checks on Directors and Senior Management of FREs, as well as guidance published by Financial Transactions and Reports Analysis Centre of Canada (FINTRAC); indicating that guidance on designated name searching and sanctions will be the subject of a separate Guideline to be issued by OSFI in 2009; and that

FINTRAC retains responsibility for ensuring compliance with Part 1 of the PCMLTFA and PCMLTFR, including new powers to apply Administrative Monetary Penalties for violation of specific provisions of the PCMLTFA and PCMLTFR effective in December 2008.

IV. Identification and Assessment of Options

Option 1 - Revise Guideline B-8 to address the Objectives in this Analysis Statement.

Under this option, Guideline B-8 is rewritten to provide detailed guidance on the assessment of inherent ML and TF risks and control policies and procedures that address these risks. The Guideline would also be expanded to more clearly indicate that FRFIs are expected to develop and implement AML/ATF programs in line with regulatory requirements.

OSFI will not incur significant costs related to revising Guideline B-8.

FRFIs should not incur additional costs in implementing revised Guideline B-8, as the Guideline underpins regulatory requirements that have already come into effect and for which FRFIs have already incurred compliance costs. Revising Guideline B-8 enables FRFIs to apply controls which they know in advance should be acceptable to OSFI, which, in turn, will assist them to reduce unnecessary costs if the measures are effective.

This option also demonstrates that OSFI is ensuring its guidance remains relevant and on a par with international standards. In addition, it would result in a more “level playing field”, as all FRFIs would simultaneously be made aware of OSFI’s expectations of how they should deal with risk management issues with respect to their AML/ATF programs.

Option 2 - Status Quo - Do not revise Guideline B-8 or take other steps to achieve the objectives outlined in this Analysis Statement.

This option would present no incremental financial costs to OSFI and could be seen as limiting regulatory burden.

However, FRFIs that do not appropriately address AML/ATF risk management and compliance issues may be exposed to enhanced supervisory measures as well as legal or regulatory sanctions or penalties, and, hence, increased reputational risks. OSFI may also be exposed to reputational risk if it were determined that a lack of effective guidance contributed to FRFIs potentially facilitating inappropriate or illegal activities. In addition, OSFI could be criticized for not making improvements to its Guideline as suggested by the FATF.

Option 3 - Leave Guideline B-8 unchanged but communicate additional information and expectations to individual FRFIs when AML/ATF assessments are conducted.

Under this option, the Guideline would remain unchanged, but OSFI would communicate the additional information and expectations to FRFIs individually that would otherwise be included in a revised guideline.

For OSFI, this would be inefficient. Further, OSFI could be criticised for not communicating expectations to all FRFIs, resulting in uneven implementation across the sector if FRFIs do not appropriately address AML/ATF risk management and compliance issues in similar time frames or apply them inconsistently. The biggest drawback of this option is that FRFIs would not be subject to consistent and transparent expectations.

V. Recommendation

The most appropriate method of disseminating revised and upgraded expectations regarding AML/ATF programs is through the proposed re-write of the current Guideline (i.e. Option 1).

VI. Consultations

OSFI regularly communicates with FRFIs individually and collectively on AML/ATF issues. This outreach includes: regular information sessions hosted by OSFI on AML/ATF; participation in various industry conferences; and in consultations with industry associations on regulatory changes. In these fora, OSFI has indicated that it would be revising Guideline B-8 for the reasons noted above. In general, feedback has been positive because FRFIs recognize their inherent ML/TF risks and the need to have strong risk management controls in place. They therefore welcome guidance that assists them in strengthening controls and complying with legal requirements.

The consultation period for discussing the revised Guideline B-8 with FRFIs and industry associations has been shorter than that normally set for OSFI consultations on guidelines generally. The Department of Finance requested OSFI to use its best efforts to introduce a revised Guideline B-8 that would be in effect by mid-December, 2008. Under the FATF evaluation procedures, Canada's response to the FATF Mutual Evaluation Report (MER) on Canada will be considered by the FATF in February 2009 and will include measures Canada has taken to respond to AML/ATF deficiencies noted in the MER. These measures will be evaluated by the FATF and if deemed adequate, a less frequent follow up process by Canada may be allowed, thus signalling improvements to the Canadian AML/ATF regime. OSFI's Guideline B-8 was referred to extensively in the MER, and although the FATF did not make any formal recommendations for improvements to the Guideline, the Department of Finance believes that an upgraded and revised Guideline B-8 is a key component of Canada's response to the MER. Accordingly, OSFI requested industry associations and FRFIs to shorten the time allocated for the consideration of comments. OSFI is appreciative of industry associations for their efforts in providing commentary to OSFI within the requested timelines.

A confidential pre-consultation draft was sent to industry associations on October 10 and 14, 2008, with comments requested no later than October 24.

On November 7, 2008, OSFI issued for public comment a draft revised version of the Guideline, with comments to be provided no later than December 10, 2008.

Detailed comments on the November 7 consultation draft were received from: the Canadian Bankers Association and the Canadian Life and Health Insurance Association. OSFI also met with representatives of these two Associations to discuss their comments in more detail. In addition, comments were received from a group of credit card banks, other FRFIs and some individuals. All comments received have been studied in detail and OSFI has made several changes, reflected in the final version of the Guideline, to address many of the key issues raised. All commentators will be provided with appropriate feedback. OSFI is grateful to all commentators for providing helpful comments within the timelines provided.