

**CONFLICTS BETWEEN THE NEW CANADIAN MONEY LAUNDERING ACT  
AND THE RULES OF PROFESSIONAL CONDUCT  
AND ETHICS**

**By**

**RAYMOND DORAY  
Partner  
Lavery, de Billy  
1, Place Ville Marie  
Suite 4000  
Montréal (Québec)  
H3B 4M4  
Telephone: (514) 871-1522  
Fax: (514) 871-8977  
rdoray@lavery.qc.ca  
Web Site : [www.laverydebilly.com](http://www.laverydebilly.com)**

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# CONFLICTS BETWEEN THE NEW CANADIAN MONEY LAUNDERING ACT AND THE RULES OF PROFESSIONAL CONDUCT AND ETHICS

## INTRODUCTION

Having signed and ratified the UN Convention against illicit traffic in narcotics, drugs and psycotropic substances of 1988, and being a member of the Financial Action Task Force ("FATF"), Canada has pledged to the international community to strengthen its anti-money laundering measures. In 1998, the FATF issued its annual report in which Canada's performance in combating money laundering was generally praised but also criticized on some points. This report was the impetus for the Canadian Parliament to pass its new *Proceeds of Crime (Money Laundering) Act*. Following the attacks of September 11th on the United States, the Act was amended to include terrorist activities within its purview. The stated purpose of the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* ("*Money Laundering Act*") is to respond to the threat posed by organized crime and to assist Canada in fulfilling its international commitments to participate in the fight against trans-national crime. This new law creates a series of specific measures to detect and deter money laundering, namely record keeping and mandatory reporting. In this presentation, I will attempt to describe summarily the duties which lie on professionals under the provisions of the *Money Laundering Act* in Canada. I will then discuss how the record keeping and mandatory reporting duties intersect with the rules of professional conduct. Finally, I will discuss the legal challenge against the *Money Laundering Act* that is being brought by the professional bodies representing lawyers across Canada.

## I. SCOPE OF THE MONEY LAUNDERING ACT

The *Money Laundering Act* applies to a series of persons and entities in the private sector, namely: **(see slides 1 and 2)**

- Banks;
- Cooperative credit societies, savings and credit unions and caisses populaires regulated by a provincial act;
- Life insurance companies;
- Trust and loan companies;
- Trust companies regulated by a provincial act;
- Loan companies regulated by a provincial act;
- Persons engaged in the business of dealing in securities, including portfolio management and investment counseling;
- Persons engaged in the business of foreign exchange dealings;
- Persons engaged in a business profession or activity described;
- Lawyers, accounts and real estate agents;
- Casinos;
- Employees of said entities.

## **II. WHY SUBJECT PROFESSIONALS TO REPORTING AND RECORD KEEPING OBLIGATIONS?**

As the methods used for money laundering have become increasingly sophisticated, money launderers have come to retain the services of professionals (lawyers, accountants and other like experts) to devise and set up elaborate financial schemes in order to erase any audit trail. In a report discussing new trends in money laundering, the FATF noted that *"the legal and accounting professionals serve as a sort of "gate keeper" since they have the ability to furnish access (knowingly or unwittingly) to the various functions that might help the criminal with funds to move or conceal"*. Lawyers, accountants and other professionals may be of assistance at any stage in the money laundering process. Historically, money launderers have gone to lawyers for the initial "placement" stage, during which proceeds of crime are reintroduced into the financial

system, largely because lawyers are bound by solicitor-client privilege and enjoy a reputation above suspicion allowing them to move assets and large amounts of cash without raising questions. More recently, the services of professionals have proven invaluable to money launderers during the "layering stage", especially to set up corporate structures, create trusts and other like instruments which may be used to obfuscate criminal investigations.

### **III. RECORD KEEPING AND THIRD PARTY DETERMINATION**

Where, in the course of his business, a professional is asked to participate in a large cash transaction (cash transactions totaling or exceeding \$10,000) the *Money Laundering Act* requires that professional to keep a detailed record of said transaction. When required to keep a "large cash transaction record", the professional must also ascertain the identity of his client. This obligation is also known as the "know-your-client" provision. In addition, the professional must take reasonable steps to determine whether his client, which is implicated in a large cash transaction, is in fact acting on behalf of a third party.

### **IV. MANDATORY REPORTING**

Under the *Money Laundering Act*, there are two types of mandatory reports:

- large cash transactions reports (i.e. the cash transaction totals or exceeds \$10,000);
- suspicious transactions reports.

A suspicious transaction is broadly defined as any financial transaction that occurs in the course of the professional's activities and in respect of which there are reasonable grounds to suspect that the transaction is related to the commission of the money laundering offense. Fintrac, the Federal authority responsible for overseeing the implementation and compliance with the *Money Laundering Act*, has published guidelines to assist persons in determining how to spot suspicious transactions. The guidelines enumerate a series of red flags that are both general and industry specific. Here are some examples of general and specific indicators set out in the suspicious transactions guidelines **(see slides 3, 4, 5, 6, 7, 8 and 9)**.

There is no monetary threshold for a suspicious transaction. According to Fintrac: "*A transaction may be connected to money laundering or terrorist activity financing when you think that it (or a group of transactions) raises questions or gives rise to discomfort, apprehension or mistrust.*" If the client acts suspiciously (one or more red flags), the professional will then turn to a context based analysis in order to determine the appropriateness of said transaction in light of several factors that may on their own seem insignificant, but together may raise a "reasonable suspicion". Only then can the professional conclude that there is a reasonable suspicion triggering the reporting duty. The report, which must be filed electronically within 30 days, is extremely detailed **(see slides 10, 11, 12, 13 and 14)**.

Once a suspicious transaction report has been made, the *Money Laundering Act* prohibits the disclosure of this fact to the client. In other words, professionals are under the obligation, pursuant to the *Money Laundering Act*, to blow the whistle on their clients whom they suspect and withhold this information from the persons directly concerned.

## V. CROSS-BORDER CARRYING OR MOVING OF CASH

Under the *Act*, any person who has in his or her possession a sum of \$10,000 in cash or more is required to declare this fact to a Canadian border agent upon entering or leaving Canada. In addition, Canadian border agents will have the power to open and search mail entering or leaving Canada where they have reasonable grounds to suspect that a package contains a sum of \$10,000 in cash or more and if the package weighs more than 30 grams.

## VI. FINTRAC

A newly instituted federal authority, Fintrac is responsible for overseeing and enforcing compliance with the *Money Laundering Act*. Fintrac will serve as a central depository for the mandatory reports of large cash transactions and suspicious transactions made across Canada. Fintrac was meant to act as a sort of "buffer" agency between the declaring entities and persons on one side and the various law enforcement agencies in Canada on the other. The rationale behind this structure was to reassure critics that feared that privacy interests of Canadians would be jeopardized. Fintrac's main function will be to receive, classify and analyze the data stream coming from the private sector and then forward the investigatory leads to law enforcement agencies where the analysis of the data reveals probable cause of a money laundering offense, an offense under the *Immigration Act*, an offense under the *Federal Tax Statutes* or a threat to national security. Fintrac may also forward data for investigation purposes to the CSIS (the Canadian intelligence agency) and to other agencies across the world having similar responsibilities as those of Fintrac.

Fintrac is also responsible for providing assistance to the private sector entities and professionals who, under the *Money Laundering Act* regulations, must implement a money laundering compliance program. In order to fulfill its mission, Fintrac may also,

from time to time, conduct compliance audits. The Act empowers Fintrac agents, when conducting a compliance audit, to:

- Enter any premises, other than a dwelling house, where the agent has reasonable grounds to believe that there are records relevant to ensuring compliance;
- Use any computer system or data processing system in the premises to examine any data contained in or available to the system;
- Copy any record in the form of a print out and remove the print out for examination or copying;
- Use any copying equipment in the premises to make copies of any record.

The Act imposes upon the entities or persons being audited a formal duty to assist Fintrac agents acting within their authority. It also contains a provision intended to permit lawyers to protect privileged communications between the lawyer and his client. Note however that this protection does not extend to non-lawyers. The statutory mechanism provides that a lawyer may have the opportunity to claim privilege with regards to documents and obtain an order that they be sealed pending a judicial determination of the privileged nature of the documents. The onus lies entirely on the lawyer seeking to claim privilege to take positive steps and institute legal proceedings. Failure to do so may result in loss of privilege.

## **VII. PENALTIES FOR NON-COMPLIANCE**

Non-compliance with the *Money Laundering Act* may result in criminal charges being laid against professionals. Failure to report a suspicious transaction is a criminal offense

punishable by up to five years imprisonment and a \$2,000,000 fine. Likewise, failing to report a large cash transaction may entail a fine of up to \$500,000 and \$1,000,000 for a repeat offense. Failing to keep the prescribed documents and disclosing to a client that a report has been made are also criminally punishable offenses.

Critics have pointed out that, in light of the heavy fines and prison sentences that attach to the offenses under the *Money Laundering Act*, this new legislation "encourages" over-reporting. This is especially true since the Act contains an immunity clause which insulates from civil suits persons or entities whom have made a report in good faith. Faced with the decision to report a client where the facts are not necessarily clear cut, a professional might eschew his ethical judgment and favor a risk analysis. Such an approach focuses mainly on costs. Arguably, the costs related to a criminal investigation, which is highly disruptive of business operations and attracts negative publicity, are greater than those of running the risk of disciplinary actions. It follows then that even the best intentioned professionals will choose to file a report.

## VIII. RULES OF PROFESSIONAL CONDUCT

Many of the disclosure and record keeping requirements set forth in the *Money Laundering Act* and its regulations may engage certain rules of professional conduct. As a result, the professional may find himself in a double jeopardy situation: On the one hand, the professional can choose to comply with the Act and face disciplinary actions or even a civil suit brought by his aggrieved client; on the other hand, the professional can choose not to report the suspicious dealings of his client and risk facing criminal charges, entailing substantial fines and perhaps even imprisonment. In the discussion that follows, we explain how the rules set forth in the *Money Laundering Act* and its regulations conflict with the rules of professional conduct. **(see slide 15).**

In Canada, lawyers are bound by solicitor-client privilege, a duty historically rooted in common law which has now acquired the status of a fundamental civil right. Solicitor-client privilege owes this special status in Canadian law to the fact that it is seen as an integral component of the justice system. Without solicitor-client privilege, lawyers could be compelled as witnesses against their clients. Furthermore, confidentiality is essential in the adversarial system because it promotes trust and strengthens the lawyer-client relationship. On the one hand, if citizens could not confide in their lawyer and would likely forego legal representation entirely. On the other hand, lawyers could not represent their clients effectively if important elements were kept from their attention. This is precisely why Canadian courts have traditionally distinguished solicitor-client privilege from other special relationships, such as that between a physician and patient or a priest and a parishioner, which are certainly of great importance, but do not play a control role in the justice system. As courts in Canada have often pointed out, the privilege belongs to the client and he alone may waive this privilege. The corollary of this rule is that a lawyer must keep secret the communications between him and his client. However, the privilege only attaches to communications made with an expectation of confidentiality, to a lawyer acting in his professional capacity and for the purposes of legal advice. The Supreme Court of Canada has recognized that solicitor-client privilege comprises a substantive rule and an evidentiary rule: The substantive rule stipulates that the lawyer must not disclose to any third party (state, agents, police officers, etc.) information obtained in confidentiality from his client while the evidentiary rule provides that the lawyer, when testifying before a court of law or a tribunal, may refuse to answer on grounds that the information is privileged or a lawyer at trial may object to the putting into evidence of documents protected by solicitor-client privilege on grounds of inadmissibility.

In the Province of Québec, the legal situation is notably different. Privilege of communications not only extend to lawyers and notaries, but also to other professionals such as accountants and financial planners.

Solicitor-client privilege, or professional secrecy, should not be confused with the ethical duty of confidentiality, which forbids that a professional reveal any information about his or her client, however mundane that information may be. It is then plain to see that the *Money Laundering Act's* mandatory reporting requirements directly conflict with the professional's duties of professional secrecy and confidentiality.

In addition to the duty of confidentiality, professionals owe a general duty of candor towards their clients. A professional must provide his client with the explanations necessary to the understanding of the nature and extent of the foreseen transaction as it appears from the facts brought to his attention. For professionals caught by the *Money Laundering Act*, being candid with his or her client would also mean raising the issue of mandatory reporting beforehand, including the ensuing consequences in law. At first glance, the duty of candor does not seem to raise any concerns. However, once a transaction has been executed by a professional on behalf of his client, and that subsequently a report of a suspicious transaction was made to Fintrac, the Act forbids the professional from being candid with his client precisely with respect to the making of a report. Here again, the mandatory reporting rules set out in the Act directly conflict with the rules of professional conduct.

In the same way that withholding knowledge from a client that a suspicious transaction report has been made conflicts with the duty of candor, this prohibition most likely conflicts also with the professional's duty to render accounts. Professional codes of ethics generally require from a professional that he render account of any acts performed in the course of his mandate. While it can hardly be said that reporting suspicious activity to a government agency constitutes an act performed on behalf of the client, the duty to render account should properly be read as to include any acts performed incidentally to the execution of the mandate.

Codes of ethics require that professionals avoid putting themselves in a situation of conflicting interests. When compelled by law to disclose information obtained in

confidentiality relative to a client's business or affairs, the professional is in fact disregarding the interests of his clients for the benefit of the law enforcement interests of the State. Compelled legally to blow the whistle on his client, the professional is in fact an agent of the State. The mandatory reporting rules also blatantly conflict with the ethical duty to not use information from a client obtained in confidentiality for purposes that are prejudicial to the client's interests. Finally, the mandatory reporting rules compromise the ability of the professional to remain independent, that is to ignore any outside intervention by a third party in the course of rendering professional advice and services.

## **IX. CONSTITUTIONAL CHALLENGE BROUGHT AGAINST THE *MONEY LAUNDERING ACT***

Since the coming into force of the *Money Laundering Act* and regulations, the law societies of most provinces in Canada instituted separate legal proceedings in order to exempt lawyers from its application pending the outcome of a determination on the merits of the constitutional issues raised in the petition. Following the success of these proceedings in five provinces, the Attorney General of Canada agreed to stay the application of the Act with regards to lawyers across Canada, including notaries in Québec, pending the outcome of the trial and subsequent appeals. Notwithstanding, the *Money Laundering Act* still applies with full force to all other entities or professionals caught by this legislation.

The constitutional arguments put forward by the law societies in their challenge of the Act can be categorized under four separate headings (**see slide 16**): The constitutional principle of an independent bar, the right to freedom of expression, the right to life, liberty and security of one's person, and the right to be protected from unreasonable search and seizures.

The principle of an independent bar derives its legal foundation in the preamble of the *British North America Act of 1867*. Contrary to the view that the bar is a creation of the executive branch of government, this argument is premised on the idea that the law societies across Canada originated from civil society and as such were independent from the State. The historical basis for this argument can be traced back to 19th century England where tradition had always precluded the Crown from intervening in bar affairs. In a sense, the principle of an independent bar mirrors that of an independent judiciary, separate from the legislative and executive branches. It can be argued that many of the expressly protected rights under the *Charter of Rights and Freedoms*, such as the right to legal counsel, the right to a full answer and defense, and the right to obtain legal advice in strict confidentiality, would be meaningless if not for an independent bar made up of lawyers that are free to champion the cause of individuals against the interests of the State.

Section 2 par. b) of the *Charter of Rights and Freedoms* guarantees the right of freedom of expression. The provision in the Act prohibiting a lawyer from revealing to his client that he has been reported to Fintrac violates the lawyer's freedom to communicate with his client on matters of crucial importance to him. Secondly, it can be argued that the mandatory reporting provisions amount to unconstitutional compelled speech, where a lawyer is forced to reveal sensitive information obtained in confidentiality thereby harming the interests of his client and conducting himself unethically.

Section 7 of the *Charter of Rights and Freedoms* guarantees the right to life, liberty and security of the person. These rights cannot be abridged unless in accordance with the principles of fundamental justice. This being said, the constitutional jurisprudence in Canada has recognized that the principles of fundamental justice include the right to communicate with legal counsel in strict confidentiality, the right to informational privacy and the protection against self-incrimination. Clearly then, it is the law societies opinion that the mandatory reporting provisions in the *Money Laundering Act* provisions violate the constitutional guarantees under Section 7 of the *Charter*. As was discussed above,

the reporting requirements violate a client's privacy interests with respect to communications with his or her lawyer. Similarly, the reporting requirements violate the client's right against self-incrimination, since information shared with a lawyer by reason of the special relationship of trust between a client and a professional is co-opted against the client.

Finally, Section 8 of the *Charter of Rights and Freedoms* affords protection against unreasonable searches and seizures. Following long-standing constitutional jurisprudence in Canada, conducting searches and seizures is permissible provided it has been judicially authorized upon demonstration of probable cause of the perpetration of an offense and probable cause that the searched premises or that the seized materials will furnish evidence relevant to the investigation. Once again, the provisions of the *Money Laundering Act* pertaining to mandatory reporting, opening and searching of mail and conducting compliance audits fall short of the constitutional safeguards against unreasonable searches and seizures. In fact, all these provisions allow for warrantless searches and seizures, with little, if any, factual grounds to support them.

If the court accepts these arguments on the merits, the burden will lie with the Attorney General to show that the violations of fundamental rights are justified in a free and democratic state, pursuant to section 1 of the *Charter of Rights and Freedoms*. To do this, the Attorney General must show that the *Money Laundering Act* is directed at a serious and pressing concern, that the measures taken are rationally connected to the stated purpose of the law and constitute a minimal impairment of rights, and the legal response is proportional to the harm.

## **X. CONCLUSION**

The passing of the new *Money Laundering Act* in Canada marks a paradigmatic change in the way the State combats crime. Instead of investigating crimes in the traditional

manner, law enforcement will now focus on passive intelligence gathering while a constant stream of leads is "volunteered" to a Federal agency. With this legislation, the State's antennas reach deeper into the private sector, in effect collapsing the dividing line between the public and the private. It goes directly to the first principles on which the liberal state is premised. Prominent scholars and jurists have warned that Canada has come a step closer to institutionalizing a police State.

For professionals and professional orders, the *Money Laundering Act* poses novel concerns and challenges. The notion of trust, central to the professional relationship, is seriously called into question and is being redefined. The "liberal profession", once a symbol of the western liberal state, is under attack. From an normative point of view, it begs to be asked whether our society still values the idea that men and women of judgment, bound by common training and experience, are capable of self-regulation.