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September 10, 2018

Lisa Pezzack
Director General
Financial Systems Division
Financial Sector Policy Branch
Department of Finance
90 Elgin Street
Ottawa, ON, K1A 0G5

Submitted via email: **fin.fc-cf.fin@canada.ca**

Dear Ms. Pezzack,

Electronic Transactions Association ("**ETA**") submits these comments in response to the invitation for submissions issued by the Department of Finance (the "**Department**") in respect of the Regulations Amending Certain Regulations Made Under the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (the "**Proposed Regulations**") published in the Canada Gazette on June 9, 2018.

ETA is the leading trade association for the payments industry, representing over 500 companies that offer electronic transaction processing products and services. ETA's members include financial institutions, mobile payment service providers, mobile wallet providers and non-bank online lenders that make commercial loans, primarily to small businesses, either directly or in partnership with other lenders. ETA member companies are creating innovative offerings in financial services, revolutionizing the way commerce is conducted with safe, convenient and rewarding payment solutions and lending alternatives.

ETA and its members support Canada's anti-money laundering ("**AML**") and anti-terrorist financing ("**ATF**") regime and its importance in the detection and deterrence of criminal activities. However, after reviewing the Proposed Regulations, the ETA has concerns with certain of the amendments and the implications that the Proposed Regulations will have for our members. We have highlighted our concerns below.

A. PRIVACY ISSUES

The Proposed Regulation, among other things, introduce enhanced identity verification, suspicious transaction reporting, and record-keeping requirements, which will require regulated entities to collect significantly more personal information from clients, much of which was not previously required. ETA believes that the requirement to collect such large amounts of personal information is not justified from a policy or privacy perspective.

As a starting point, we believe that the over collection of data could result in regulated entities being overwhelmed and unable to use the information that they have collected effectively for AML compliance and monitoring purposes. Moreover, we believe that the burden imposed on our members to undertake such collection would outweigh any AML/ATF benefit that comes from collecting such vast amounts of personal information. Finally, ETA believes that the proposed enhanced due diligence requirements do not adequately reflect a risk-based approach.

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We note that the Privacy Commissioner, in his appearance before the House of Commons Standing Committee on Finance on February 18, 2018, noted similar privacy concerns in respect of the Canadian AML and ATF regime. He noted that while a holistic approach to the collection and sharing of information might be useful to identify money laundering and terrorist financing threats, unless appropriate privacy safeguards are adopted, there are significant concerns with respect to proportionality. The Commissioner suggested that a risk-based approach be adapted in order to minimize the risk of over-collecting and retaining the financial and personal information of law-abiding individuals.

Although our members are supportive of performing due diligence in respect of their clients, from a policy and a privacy perspective, we believe that further consideration must be given by the Department to proportionality in respect of the collection of such vast amounts of personal data from clients.

B. PREPAID DUE DILIGENCE

A significant change to Canada's AML and ATF regime is the introduction of the regulation of prepaid products under the Proposed Regulations. While ETA is not adverse to the regulation of prepaid products in Canada, we are concerned that some of the new provisions in the Proposed Regulations do not reflect the ever-changing prepaid environment, and as a result, will stifle innovation in the prepaid sector in Canada.

The Proposed Regulations provide the following definitions for "prepaid payment product" and a "prepaid payment product account" ("**PPPA**"):

> *A "prepaid payment product" is defined as a product that is issued by a financial entity and that enables a person or entity to engage in a transaction by giving them electronic access to funds or virtual currency paid to a prepaid payment product account held with the financial entity in advance of the transaction.*
>
> *A "prepaid payment product account" is in turn defined as an account that is connected to a prepaid payment product and that permits:*
>
>> *(a) one or more transactions that total $1,000 or more to be conducted within a 24-hour period; or*
>>
>> *(b) a balance of funds or virtual currency available of $1,000 or more to be maintained.*

(i) <u>Identity Verification Requirements</u>

Based on the above definitions and the proposed identity verification requirements for prepaid products under the Proposed Regulations, regulated entities will be required to verify the identity of PPPA account holders (a requirement that is similar to the traditional requirement to verify the identity of a holder of a bank account). However, in addition to this requirement for account holders, regulated entities would also be required to verify the identity of every individual that is issued a card under a PPPA, since such individuals would be considered "authorized users" of the account.

We are concerned with this latter requirement in the context of government assistance programs, corporate incentive programs, employer reimbursement and payroll programs, and emergency relief programs ("**Programs**") as it would require regulated entities to verify the identity of authorized users. However, because authorized users under these programs have no ability to load any personal funds onto these cards or to the underlying PPPA they pose minimal to no AML/ATF risk. Imposing an identity verification requirement in these circumstances would seriously impact the ability of regulated entities to offer these types of Programs.

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(ii) <u>Record-keeping requirements</u>

ETA is also concerned with certain of the new record-keeping requirements applicable to prepaid, and in particular, the requirement to maintain a prepaid payment product slip ("**PPPS**") for every payment that is made to the PPPA (the "**PPPS Requirement**"). A PPPS is defined under the Proposed Regulations as follows:

> *prepaid payment product slip means a record that sets out:*
>
> *(a) the date of a payment to a prepaid payment product account;*
>
> *(b) the name of the person or entity that makes the payment;*
>
> *(c) the type and amount of each of the funds or virtual currencies involved in the payment;*
>
> *(d) the method by which the payment is made;*
>
> *(e) the name of each holder of the prepaid payment product account;*
>
> *(f) the account number and, if it is different, the number that identifies the prepaid payment product that is connected to the account; and*
>
> *(g) every other known detail that identifies the payment.*

Based on a review of the Proposed Regulations, the PPPS definition largely mirrors that of a deposit slip for regular bank accounts. However, because prepaid cards have a very different distribution model compared to traditional banking products, we do not believe that it is appropriate to simply impose the traditional deposit slip requirements on prepaid without consideration of the unique characteristics of prepaid distribution channels.

Many elements of a PPPS can be gathered by a regulated entity (where the PPPA is held). However, because prepaid products are often reloaded through retailers, there are a number of elements required under the PPPS Requirement that, practically speaking, can only be obtained at retail locations. This would impose a significant burden on retailers selling prepaid and offering reloading services to collect the information despite not being equipped with the systems or security protocols to deal with the stringent record-keeping requirements. This is especially so given the expansive information requirements, such as the requirement to collect "every other known detail that identifies the payment". We are concerned that the foregoing PPPS Requirement will make it difficult for retailers and our members to meet these new record keeping requirements.

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Given the rapidly changing pace of technology and the new prepaid access products that will be introduced into the Canadian market in the coming months and years, we believe it is essential that any requirements respecting prepaid use a risk-based approach and be sufficiently flexible so as to allow regulated entities to implement client due diligence based on the unique risk factors that are inherent in their prepaid product offerings, whatever they may be. The Competition Bureau has touched on this point in its report *Technology-led innovation in the Canadian Financial Services Sector* (December 2017), where it noted that it is important that the regulatory frameworks applicable to the financial services and banking sectors do not inadvertently deter innovation and the competitive benefits that follow.

ETA is concerned that the new provisions respecting prepaid products under the Proposed Regulations, including the due diligence requirements, do not adequately reflect a risk-based approach, and as a result, will stifle innovation in the prepaid sector.

C. VIRTUAL CURRENCY

ETA is supportive of the introduction of "virtual currency" under the Proposed Regulations and the regulation of those that "deal in virtual currencies". However, we are concerned that the definition of "virtual currency" as set out in the Proposed Regulations is not clearly articulated and will therefore lead to uncertainty in the industry.

In that regard, "virtual currency" is defined under the Proposed Regulations as follows:

> *(a) a digital currency that is not a fiat currency and that can be readily exchanged for funds or for another virtual currency that can be readily exchanged for funds; or*
>
> *(b) information that enables a person or entity to have access to a digital currency referred to in paragraph (a).*

ETA does not believe that the Proposed Regulations provide sufficient guidance as to what constitutes a virtual currency since virtual currency is defined as digital currency and the term "digital currency" is not defined in the Proposed Regulations.

In addition, ETA is concerned that the use of the phrase "that can readily be exchanged for funds" in the definition of virtual currency creates further uncertainty as to what exactly constitutes virtual currency under the Proposed Regulations. For instance, does "readily exchangeable" include a virtual currency that can only be obtained by an accredited investor, or is the ability to exchange it on a secondary market the standard to make it "ready exchangeable"? We believe that it would be helpful for the Department to release guidance on the interpretation of what exactly a virtual currency is to complement the Proposed Regulations.

D. FOREIGN MSBS

ETA is concerned with the preliminary guidance the Department released for money services businesses ("**MSBs**") in respect of foreign MSBs, which states that:

> *A foreign MSB may determine that its client is in Canada even though the client is temporarily located outside Canada when conducting a transaction. The foreign MSB should still consider its client to be in Canada in the following instances:*
>
> - *the client is working or living temporarily outside of Canada;*
> - *the client is teaching or attending school in another country;*
> - *the client is regularly commuting from Canada to a place of work in the United States;*
> - *the client is vacationing outside of Canada.*

As set out in the relevant provisions of the PCMLTFA, a foreign MSB is defined to include a person or entity that engages in the business of providing certain services that are directed at persons or entities in Canada and that provide such services to their customers in Canada. A key component of the definition of a foreign MSB is that it is providing services to their customers "in Canada".

Given this definition, it is clear that in drafting the PCMLTFA, the legislature granted FINTRAC authority to regulate foreign MSBs for services provided by those foreign MSBs to "their customers in Canada". However, this authority did not extend to regulation of services provided by those same foreign MSBs to Canadians that are <u>outside</u> of Canada. On that basis, ETA is concerned by the preliminary guidance regarding foreign MSBs, since the interpretation that FINTRAC has provided goes beyond the statutory

authority provided to FINTRAC to regulate foreign MSBs. In our view, when a Canadian citizen is living outside of Canada or going to school outside of Canada they are not a "customer in Canada".

ETA further believes that the implementation of the preliminary guidance is likely to be difficult if not impossible to implement. For instance, it is unfeasible for a MSB located in a foreign jurisdiction to determine if the person in front of them is a "Canadian", and even if they were able to make such a determination, it would impossible for the MSB to apply the requirements of the PCMLTFA to the transaction as they would not have the systems or capability to do so.

Based on the foregoing, ETA and its members believe that the interpretation of foreign MSBs under the preliminary guidance released by the Department is not in keeping with the scope of the PCMLTFA and the definition of a foreign MSB. On that basis, ETA respectfully suggests the modification of the preliminary guidance in respect of foreign MSBs to reflect the statutory language in the PCMLTFA.

E. 12-MONTH IMPLEMENTATION DEADLINE

The Proposed Regulations will require major systems modifications and upgrades to address the new information collection requirements, the new reporting schedules and other new enhanced record-keeping requirements. ETA is concerned that given these major upgrades, the proposed twelve-month implementation deadline (after registration of the Proposed Regulations) is too short of a timeline to allow our members sufficient time to meet these obligations.

Given the technical challenges and complexities that our members will face in complying with the technical side of the Proposed Regulations, we would encourage the Department to extend the implementation deadline by at least an additional twelve months. Furthermore, we note that our members will be unable to complete their systems upgrades until FINTRAC has itself completed its system upgrades and communicated technical specifications to regulated entities. As such, ETA requests that the implementation period for the Proposed Regulations begin only after FINTRAC has completed its required IT build and has communicated to regulated entities what the actual IT specifications are.

ETA believes that by extending the implementation deadline as proposed above, our members would have the time they require to undertake their own upgrades required to meet the new requirements, as well as test their systems and controls to ensure that they are fully functional and compliant prior to the in-force date of the Proposed Regulations.

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ETA thanks you for the opportunity to submit these comments. For more information, please contact Scott Talbott, SVP of Government Affairs at ETA. stalbott@electran.org