Proceeds of crime? From suspicion to belief: key points for financial institutions

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The problem: Funds are on account; provenance of funds is suspect, and an investigation brings into question whether there are 'reasonable grounds to believe' that the funds are directly or indirectly tainted as proceeds of crime. What next?

We consider the amorphous gap between a) the trigger of "reasonable grounds to suspect" being the threshold when a reporting entity must file a suspicious transaction report with FINTRAC; and b) the threshold of 'knowing, believing or being reckless as to whether' funds on account are proceeds of crime. We also explore part of the solution for bridging the exposure created by these circumstances.

The Criminal Code provisions and interplay with PCMLTFA

Section 354 (1) of the Criminal Code criminalizes possession of the proceeds of crime. Reporting entities are subject to the *Proceeds of Crime, (Money Laundering) and Terrorist Financing Act,* (PCMLTFA) and are required to report transactions to the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) if there are reasonable grounds to suspect that the transaction is linked to money laundering or terrorist financing. Section 8 of the PCMLTFA requires the no person disclose the filing or contents of a suspicious transaction report with the intent to prejudice a criminal investigation. The interplay creates challenges.

Section 462.31 of the Criminal Code criminalizes the act of money laundering, which includes dealing with proceeds with the intent to conceal or convert them, knowing or believing ***or being reckless whether*** they were obtained through the commission of a designated offence in Canada or an act elsewhere that would be considered a designated offence if committed in Canada. It may be inferred that an accused had knowledge or belief or demonstrated recklessness if satisfied that the way the accused dealt with the property, or its proceeds is markedly unusual, or the accused's dealings are inconsistent with lawful activities typical of the sector in which they take place.

Persons found guilty of possessing property obtained by laundering proceeds of crime face conviction and for financial institutions wrongly dealing with such property, severe

reputational harm. There is very little authoritative guidance to define when evidence to support the lower threshold of “reasonable grounds to suspect” meets the higher threshold of “reasonable grounds to believe”. Until authoritative guidance is developed, caution is warranted.

The issue

When a financial institution learns that funds may constitute proceeds of crime, either or both courses of action available to it–continuing to hold those funds or returning them to the depositor–run the risk of contravening s. 462.31 of the Criminal Code. This was the issue in *East West Investment Management Corporation v. Higgins et al.*, 2023 ONSC 5077:

- East West Investment Management Corporation is an Investment Fund Manager, Portfolio Manager, Commodity Trading Manager and Exempt Market Dealer registered with the Ontario Securities Commission, managing assets on behalf of investors, including family offices and high net worth Canadians. As such, East West is required to exercise its discretion and authority honestly, in good faith and in the best interest of its clients.
- East West received information about criminal proceedings pending in Germany related to a subsidiary of one of its clients. During its ensuing investigation, East West came to the view that there was a risk that some of the funds deposited with East West could constitute “proceeds of crime” as defined in s. 462.31 of the Criminal Code.
- East West filed suspicious transaction reports with FINTRAC in relation to deposits and withdrawals made, all as required pursuant to s. 7 of the PCMLTFA.
- The conundrum facing East West was that, since some of the funds on deposit may be proceeds of crime, either or both courses of action available to East West–continuing to manage those funds or returning them to the depositor–would likely contravene s. 462.31 of the Criminal Code.
- The traditional rule for payment of funds into court requires that there be two competing claimants to a fund and that a stakeholder in the middle, (usually a bank) is not able to determine lawful entitlement between the claimants. However, when a bank flags funds as potentially at issue under s.462.31 of the Criminal Code, potential claimants to the funds may be unknown, may have evaporated into the ether, or may be tainted third party dupes having questionable provenance to the funds due to ‘grey market’ dealings of their own. In the absence of legitimate competing claimants, stakeholders could be stuck holding funds indefinitely. East West solved this conundrum.

A possible solution: Paying funds into court

East West brought a court application relying on the Court’s inherent jurisdiction, seeking an order permitting it to pay the funds into Court to address its obligations under the Criminal Code and also in discharge of its obligations to its client. In the alternative, East West sought a declaration that the continued management of the funds did not contravene ss. 354 or 462.31 of the Criminal Code. The court allowed East West’s application and ordered that more than $4,000,000 be paid into court and allowed the applicant to be indemnified by deducting the substantial legal fees and disbursement of the court process from the funds paid into court.

When a bank pays funds into court that may be the proceeds of crime, it is navigating a complex intersection of legal, ethical and commercial responsibilities. By taking this step, the institution balances its obligation to act in a manner consistent with its obligations to its clients with its duty to comply with the Criminal Code–specifically Section 462.31–and Canada's broader anti-money laundering regime. Paying funds into court allows the bank to avoid facilitating a potential offence, while ensuring that the rightful ownership of the funds can be adjudicated transparently and lawfully. This conduct demonstrates the institution's commitment to legal compliance, supports law enforcement efforts to combat use of Canadian financial institutions for money laundering, and upholds the integrity of the Canadian financial system.

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