

# To MSB or not to MSB:

An Analysis of FINTRAC Guidance on the  
Interpretation of Money Services Business

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# Introduction

Canada's anti-money laundering/counter-terrorism financing ("**AML/CTF**") legislation, the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (the "**PCMLTFA**") and its associated regulations ("**Regulations**") apply only to certain entities. In some cases, the PCMLTFA applies to an entity by virtue of the type of entity, for example, a financial institution such as a bank, a credit union, or an insurance company. In other cases, the PCMLTFA applies to an entity by virtue of the fact that the entity performs a certain type of activity. This is the case for "money services businesses" ("**MSB**") which are defined in the PCMLTFA as "persons and entities engaged in the business of foreign exchange ("**FX**") dealing, of remitting funds or transmitting funds by any means or through any person, entity or electronic funds transfer network, or of issuing or redeeming money orders, traveller's cheques or other similar negotiable instruments except for cheques payable to a named person or entity."

Determining whether an entity is an MSB can be challenging, especially in the case of financial technology ("**Fintech**") entities. Fintech entities often have unique and innovative business models which can present complexities and ambiguities in determining whether they are operating as an MSB. The penalties, should an entity get this wrong, can be steep: the Financial Transactions and Reports Analysis Centre of Canada ("**FINTRAC**") has been particularly active in imposing administrative penalties against MSBs. Of the 79 administrative penalties issued by FINTRAC to date, the largest number (36) have been imposed on MSBs (with a total of \$814,805 in administrative penalties imposed against MSBs to date). In addition, under the national retail payments framework, as proposed by the Department of Finance Canada in July 2017, a payment service provider's registration under such regime could be denied or revoked as a result of the payment service provider's failure to register with FINTRAC as an MSB.

FINTRAC provides Policy Interpretations ("**Policy Interpretations**") and other guidance on its views as to when FINTRAC considers a business to be an MSB. This paper aims to shed some clarity on the issue of determining whether an entity is an MSB, through a review and analysis of the Policy Interpretations and guidance FINTRAC has provided.

On June 9, 2018, draft regulations ("**New Regulations**") were issued proposing a number of amendments to each of the existing Regulations under the PCMLTFA. The New Regulations specifically address some, but not all, of the ambiguities in FINTRAC's Policy Interpretations regarding MSBs. We explain the matters that have been clarified in the New Regulations in our discussion below. We also discuss the Policy Interpretations which provide guidance in the interim until the New Regulations come into force.<sup>1</sup>

<sup>1</sup> The New Regulations were open for comment until September 7, 2018 and will come into force 12 months after their registration.



# 1. Who does FINTRAC consider to be an MSB?

FINTRAC Interpretation Notice no. 1 – Criteria for “Engaged in a Money Services Business” (the “**MSB Interpretation Notice**”) provides additional guidance on the definition noted above. In particular, the MSB Interpretation Notice confirms, consistent with the PCMLTFA statutory definition, that any of the following three types of activities will result in a business being engaged in the activity of an MSB: “(1) foreign exchange dealing; (2) remitting or transmitting funds by any means or through any person, entity or electronic funds transfer network; or (3) issuing or redeeming money orders, traveller's cheques or other similar negotiable instruments except for cheques payable to a named individual or entity.” With respect to the second category, FINTRAC clarifies that an alternative money remittance system, such as Hawala, Hundi and Chitti, will be an MSB.

FINTRAC also outlines in the MSB Interpretation Notice that undertaking any of the following activities will result in a business being an MSB:

- Offering money transfer services in any amount;
- Issuing or redeeming money orders, travellers' cheques or other similar negotiable instruments for more than \$1,000 during a single transaction with the same individual or entity (a single transaction includes two or more transactions related to the redemption of money orders, travellers' cheques or similar negotiable instruments of less than \$1,000 each made within 24 consecutive hours that total \$1,000 or more);
- Conducting FX transactions for more than \$1,000 during a single transaction with the same individual or entity (single transaction includes two or more transactions related to an FX transaction of less than \$1,000 each made within 24 consecutive hours that total \$1,000 or more);
- Advertising (through newspaper, television, yellow pages, internet, any other media, or by an interior or exterior sign) the fact that a business is engaged in any of the money services business activities listed above;
- Holding a permit or license related to any of the money services business activities listed above;
- Being registered as someone carrying on any of the money services business activities listed above; and
- Reporting income from any of the money services business activities listed above as income from a separate business for tax purposes.

# 2. What does FINTRAC consider not to be an MSB?

The MSB Interpretation Notice clarifies those activities that FINTRAC does not consider to be activities relating to being “engaged in an MSB,” such as:

- conducting money services business activities solely as an agent or mandatary for another business that is an MSB; or
- carrying out money services business activities as part of other activities for which the entity is already subject to the PCMLTFA and Regulations.

# 3. Previously ambiguous activities clarified in the New Regulations

The New Regulations clarify ambiguities regarding the applicability of MSB requirements to dealers in virtual currency and foreign MSBs.

The following is a brief summary of the current situation in each of these areas and the changes that will come into effect under the New Regulations.

## **Dealers in Virtual Currency**

In 2014, the Government of Canada amended the PCMLTFA to include persons dealing in virtual currency as MSBs. However, these changes will not come into force until the New Regulations defining what it means to be dealing in virtual currency are enacted.

The New Regulations define “virtual currency” as “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 “information that enables a person or entity to have access to such digital currency”, for example, access to the private key of a cryptocurrency. The New Regulations do, however, exempt “a transfer or receipt of virtual currency as compensation for the validation of a transaction that is recorded in a distributed ledger; or an exchange, transfer or receipt of a nominal amount of virtual currency for the sole purpose of validating another transaction or a transfer of information”, for example, a reward for mining cryptocurrencies. “Distributed ledger” means “a digital ledger that is maintained by multiple persons or entities and that can only be modified by a consensus of those persons or entities”.

Persons dealing in virtual currency, which will include those offering virtual currency exchange services (i.e., the exchange of virtual currency for funds, or one type of virtual currency for another) and value transfer services, will be required to register with FINTRAC as an MSB and to have in place a full AML/CTF compliance program, including a chief anti-money laundering officer (“CAMLO”), AML/CTF policies and procedures, a training program and independent assessment of its AML/CTF compliance program, as set out below in our discussion of the implications of being an MSB.

When the New Regulations come into force, the list of activities that make a business an MSB will include dealing in virtual currency activities. In the interim, the Policy Interpretations provide some guidance from FINTRAC on how dealers in virtual currency are treated.

According to FINTRAC’s Policy Interpretations, if a business provides any of the aforementioned MSB activities (FX dealing, funds transfer or issuance/redemption of negotiable instruments) to clients through the use of virtual currencies, the business is required to register with FINTRAC as an MSB, even before the New Regulations come into force.

It is important to note that “virtual currency” while including the term “currency”, is not considered a currency for the purposes of determining whether the business is a foreign exchange dealer. Therefore, if a business exchanges Canadian dollars for bitcoin, it is not considered to be exchanging one type of currency for another currency (i.e. foreign exchange dealing); however, the business may still fit the definition of an MSB. For example, FINTRAC considers the following activities and business models to be MSBs:

- Exchanging fiat currency funds for virtual currencies at a local virtual currency exchange and then sending the virtual currency to a foreign virtual currency exchange to be converted back to fiat currency at a foreign virtual currency exchange;<sup>2</sup>
- Using virtual currencies as the underlying internal transfer technology or method of simplified monetary movement that allows clients to send remittances online and ultimately request the beneficiary in another country receive either Canadian fiat currency or fiat currency of another jurisdiction;<sup>3</sup> and
- Permitting clients to achieve fiat-to-fiat currency exchanges by combining trades of virtual currency with trades of fiat currency, for example by depositing Canadian dollars in their account, converting the funds into a virtual currency and then selling the virtual currency in exchange for US dollars or another fiat currency; this in FINTRAC's view would be providing a foreign exchange dealing service, which would constitute an MSB.<sup>4</sup>



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2 PI-6268

3 PI-6246

4 PI-6244

Therefore, while there is uncertainty in the industry, FINTRAC's Policy Interpretations indicate that many types of virtual currency businesses are currently required to register with FINTRAC as MSBs and be regulated even prior to implementation of the New Regulations. The New Regulations provide the additional detail required to implement the changes that explicitly bring virtual currency into the Canadian AML/CTF regime by defining "virtual currency" and exempting certain activities such as mining cryptocurrencies as described above. Accordingly, those dealing in virtual currency, offering virtual currency exchange services for funds or one type of virtual currency for another, or providing value transfer services, will be required to register with FINTRAC as an MSB. Section 5, below, explains the implications of registering as an MSB.

### **Foreign MSBs**

The PCMLTFA was amended in 2014 to extend to "foreign money services businesses", being MSBs that are persons and entities that: (i) do not have a place of business in Canada, (ii) are engaged in the business of providing such services directed at persons or entities in Canada, and (iii) provide those services to their clients in Canada. This would include foreign MSBs that offer services in Canada online. These amendments have not yet come into force, pending the New Regulations coming into force. The New Regulations now provide the additional detail required to implement such changes. Under the New Regulations, domestic and foreign MSBs will be subject to the same general requirements, including the requirements to register with FINTRAC.

In addition, if a foreign MSB fails to comply with the requirements of the PCMLTFA and Regulations, or is issued an administrative monetary penalty and does not pay that penalty, its MSB registration can be revoked, thus making it ineligible to do business in Canada. Financial entities will also be prohibited from opening or maintaining an account for, or having a correspondent banking relationship with, an unregistered foreign MSB.

Currently and until the New Regulations come into force, the Policy Interpretations indicate that in order for a foreign company to be considered an MSB subject to the PCMLTFA, the foreign company must have a "real and substantial connection" with Canada. The criteria considered to establish a real and substantial connection include whether the business:

- is incorporated in Canada;
- has agents in Canada;
- has physical locations in Canada;
- maintains a bank account in Canada; or
- maintains a server in Canada for the purposes of carrying out MSB activities.<sup>5</sup>

By capturing foreign companies that provide services to people located in Canada but that do not have a place of business in Canada, such as those offering money services through the Internet, the New Regulations widen the scope of the application of the Canadian AML/CTF regime to apply to additional multi-national organizations with exposure to Canada.

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<sup>5</sup> PI-6376.

# 4. Business models considered in the Policy Interpretations

The following tables represent the different types of business models that FINTRAC has received questions on and responded to through issuance of Policy Interpretations, which provide insight into the applicability of the MSB designation:

Payment Service Providers (PSP)	
<b>Summary of Policy Interpretations</b>	<p>As discussed above, entities engaged in remitting or transmitting funds by any means or through any person, entity or electronic funds transfer network are considered to be MSBs which would broadly include PSPs. However, as PSPs are not defined in the PCMLTFA or Regulations, there are exceptions when the transfer of funds is merely a corollary of their actual service. Services explicitly exempted by FINTRAC in the Policy Interpretations include:</p> <ul style="list-style-type: none"> <li>– Utility payments</li> <li>– Payroll and commission services</li> <li>– Mortgage and rent payment services</li> <li>– Certain tuition payment services</li> </ul>
<b>Examples</b>	<p>Examples where the company <b>qualified</b> as an MSB:</p> <ul style="list-style-type: none"> <li>– The entity uses its payment network to facilitate payments between Canadian businesses and their suppliers.<sup>6</sup></li> <li>– The entity introduces a new payment option for their small business client's customers to send payments directly into the small business' bank account through EFTs as an online bill payee.<sup>7</sup></li> </ul> <p>Examples where the company <b>did not qualify</b> as an MSB:</p> <ul style="list-style-type: none"> <li>– An entity engaged in the business of tuition payments sent to private education institutions.<sup>8</sup></li> <li>– The entity providing settlement services directly to merchants on behalf of their customers for the purchase of goods and services.<sup>9</sup></li> </ul>

6 PI-6364

7 PI-6110

8 PI-6405

9 PI-7670

## Global payments/FX provider

### Summary of Policy Interpretations

Based on our review of Policy Interpretations, the application of the funds remittance definition included in the MSB Interpretation Notice is quite broad as it relates to global payments providers. It effectively includes any company that facilitates the transfer of funds (regardless of amount) from a sender in one country to a beneficiary in another country when the funds flow through the company. A review of some of the business models considered by FINTRAC in its Policy Interpretations sheds some light on FINTRAC's views in this area.

Separately, FX providers are considered an MSB if their business conducts FX transactions for more than \$1,000 during a single transaction with the same individual or entity. For these purposes, a single transaction is defined as two or more transactions related to a FX transaction of less than \$1,000 each that are made within 24 consecutive hours and that total \$1,000 or more.

### Examples

Examples where the company **qualified** as an MSB:

- Web-based service which allows clients to convert currency and transfer/remittance the converted funds across the border between a foreign country and Canada qualifies as an MSB as both an FX dealer and funds remitter.<sup>10</sup>
- Web-based service that connects two individuals in different countries who wish to transfer money without the need for cross-border transactions. All transactions are conducted through the an e-commerce platform which matches a client in one country wanting to transfer funds to a receiver in another country with a client in that other country who wants to transfer funds to a receiver in the same country as the first client. The funds flow through the ecommerce platform company. While the funds technically are transmitted domestically, both cross-border transactions are executed. FINTRAC views this as the ecommerce platform company providing remitting and transmitting services, which are MSB activities.<sup>11</sup>
- The business provides small value vouchers that customers can purchase from Canadian merchants, and customers then send the voucher code to a third party outside of Canada to be redeemed for an equivalent value of goods (i.e. food, medicine) in another country. Because through the business the customer who purchases the voucher transmits the voucher code to a third party outside of Canada to be redeemed for goods denominated in a currency other than Canadian dollars, the business would be engaged in MSB activities.<sup>12</sup>
- Telecommunications company providing customers with the ability to use their debit/credit card on the provider's website to transfer \$500 or less per month to a mobile-wallet account anywhere in the world. Recipients can either cash out the mobile wallet or convert to customer airtime.<sup>13</sup>

There were no examples observed where a company was facilitating cross-border payments or FX transactions and was not considered to be an MSB.

<sup>10</sup> PI-6381

<sup>11</sup> PI-6358

<sup>12</sup> PI-6118

<sup>13</sup> PI-5687

## P2P Lending / Loan Providers

### Summary of Policy Interpretations

P2P Lending allows users to set up a funding campaign on an online platform, so once the campaign is fully funded, the funds will be transferred to the borrower and then repaid according to a repayment schedule.

Loan providers facilitate funds transfers such as the initial funding of the loan proceeds, as well as receiving payments according to a repayment schedule. However, the funds transfers by P2P lending platforms and loan providers are a corollary of their actual service which is to provide loans to borrowers. And therefore, similar to payment service providers, loan providers are typically not considered to be an MSB.

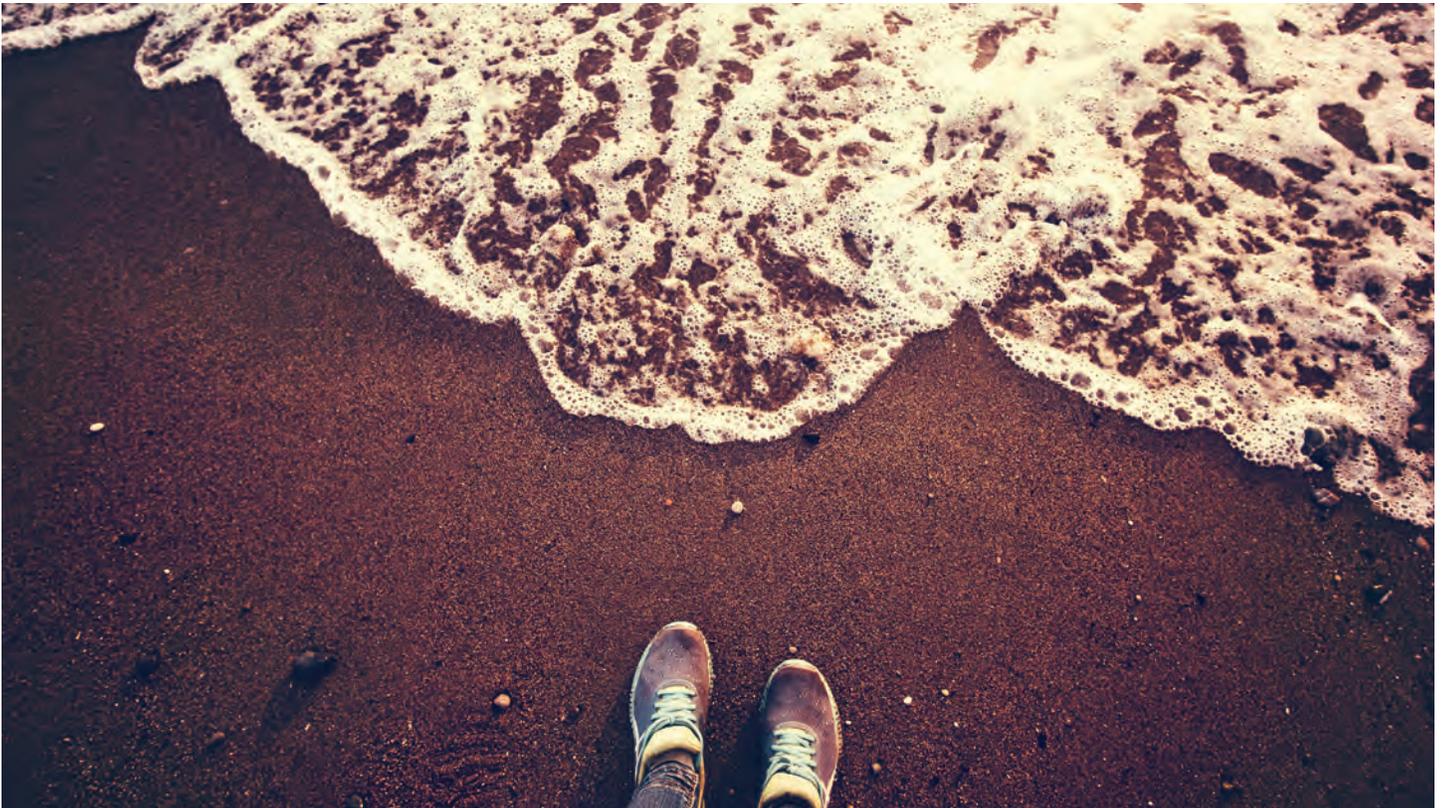
There is, however, a risk that the company may qualify as a financial entity and be subject to the requirements for financial entities under the PCMLTFA.

### Examples

There were no examples observed where a P2P lending platform or loan provider was considered to be an MSB.

Examples where the company **did not qualify** as an MSB:

- Company finances the purchase of goods by a Canadian business (borrower) from suppliers located outside of Canada . In addition to not being considered an MSB, it was not considered a financial entity according to FINTRAC as it was not subject to the *Trust and Loan Companies Act*.<sup>14</sup>
- An online platform that brings together lenders and borrowers to fund loans. Borrowers were described as able to make payments using their Canadian bank accounts. The funds from the loan would be sent to the borrower who would have their account automatically debited based on the repayment schedule.<sup>15</sup>



<sup>14</sup> PI-6339

<sup>15</sup> PI-6338



# 5. What are the implications of being an MSB?

An MSB must:

- Register with FINTRAC;
- Develop and put in place an AML/CTF compliance program;
- Appoint a compliance officer responsible for the implementation and oversight of the compliance program;
- Develop and apply written compliance policies and procedures that are kept up to date and approved by a senior officer;
- Apply, document and maintain a risk assessment, including mitigation measures and strategies;
- Develop and maintain a written training program for employees, agents, and others authorized to act on the MSB's behalf;
- Review its compliance program (policies and procedures, risk assessment and training program) every two years for the purpose of testing its effectiveness; and
- Comply with customer identification and know-your-client, record-keeping and reporting requirements.<sup>16</sup>

In addition to the federal PCMLTFA, MSBs should also be mindful of the separate legislation that applies to MSBs in Québec, the *Money-Services Businesses Act*. An MSB may also be required to register separately in Québec with the Autorité des Marchés Financiers.

Regardless of whether an entity is an MSB, it also will need to comply with the *Criminal Code* provisions relating to proceeds of crime and terrorism and sanctions laws. Therefore, it is recommended that every entity has in place a compliance program to prevent breaches of the Criminal Code and sanctions laws, whether or not it is an MSB with the additional requirement to have in place a compliance program as required by the PCMLTFA and Regulations.

<sup>16</sup> The New Regulations will introduce requirements to verify the identity of every person who requests an exchange of an amount of \$1,000 or more in a virtual currency exchange transaction and to maintain large virtual currency transaction records when they receive \$10,000 or more in virtual currency.

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