Part I
Introduction

My Terms of Reference require me to make findings of fact on the extent, growth, evolution, and methods of money laundering in various sectors; the acts and omissions of key actors in those sectors and of government officials; and the barriers to effective law enforcement in British Columbia. They also require me to make recommendations, including in respect of these matters, where I consider it necessary and advisable.

Before addressing these matters, it is necessary to consider some background concepts. What *is* money laundering? Who is involved in it? How much money laundering occurs? And, given that much of this activity occurs under the radar and does not directly result in physical harm, is money laundering a problem worth addressing? Part I addresses these questions.

Chapter 1
Introduction

On May 15, 2019, the Lieutenant Governor of British Columbia issued Order in Council No. 2019-238 establishing the Commission of Inquiry into Money Laundering in British Columbia and appointing me as the sole commissioner in accordance with section 2 of the *Public Inquiry Act*, SBC 2007, c 9. The Commission was established in the wake of significant public concern over the nature and prevalence of money laundering in British Columbia as well as the institutional effectiveness of those charged with detecting and combatting it. Media reports suggested that a staggering amount of money was being laundered through the BC economy and serious concerns were raised about the response of regulators and law enforcement agencies.

While most of these reports involved suspected money laundering activity in and around Lower Mainland casinos, concerns were also raised about money laundering in other sectors of the economy, including the corporate sector, where concerns were raised about the use of shell companies to launder illicit funds, and the real estate sector, where there were suggestions that money laundering activity was contributing to the rapid increase in housing prices in the Lower Mainland and other parts of the province.

The Order in Council and Terms of Reference[1] give me a broad mandate to inquire into and report on money laundering in British Columbia. I am required to conduct hearings and make findings of fact with respect to:

- the extent, growth, evolution, and methods of money laundering in various sectors of the economy, including the gaming sector, the real estate sector, financial institutions and money services businesses, the corporate sector, the luxury goods sector, and the professional services sector;

1 The Terms of Reference can be found at Appendix A.

- the acts or omissions of responsible regulatory agencies and individuals, including whether those agencies or individuals have contributed to money laundering in the province;
- the scope and effectiveness of the anti–money laundering powers, duties, and functions exercised or carried out by the regulatory agencies and individuals referenced above; and
- barriers to effective law enforcement.

In considering these issues, I have been directed to review and consider four recent reports commissioned by the provincial government on these matters:

- Peter M. German, QC, *Dirty Money: An Independent Review of Money Laundering in Lower Mainland Casinos Conducted for the Attorney General of British Columbia*, March 31, 2018 (*Dirty Money 1*);
- Peter M. German, QC, *Dirty Money, Part 2: Turning the Tide – An Independent Review of Money Laundering in B.C. Real Estate, Luxury Vehicle Sales & Horse Racing*, March 31, 2019 (*Dirty Money 2*);
- Dan Perrin, *Real Estate Regulatory Structure Review* (2018) (Perrin Report); and
- Maureen Maloney, Tsur Somerville, and Brigitte Unger, "Combatting Money Laundering in BC Real Estate," March 31, 2019 (Maloney Report).

I am also empowered to make any recommendations I consider necessary and advisable with respect to the conditions that have allowed money laundering to thrive.

Guiding Principles

In carrying out my mandate, I have been guided by the fundamental principle that the Commission is an independent body that owes its allegiance solely to the people of British Columbia. Independence is particularly important where, as here, the Commission has been called upon to examine the response of government to a pressing social problem. While I have been careful to ensure that the findings set out in this Report are based on evidence – as opposed to speculation or conjecture – I have not been hesitant to make findings critical of government where those findings are supported by the evidence.

Another principle that has guided the work of the Commission is the need to conduct open, public hearings with a view to making findings of fact, and informing and educating concerned members of the public. In *Phillips v Nova Scotia (Commission of Inquiry into the Westray Mine Tragedy)*, [1995] 2 SCR 97, Mr. Justice Cory explained these important public functions as follows:

> Commissions of inquiry have a long history in Canada. This Court has already noted (*Starr v. Houlden*, *supra*, at pp. 1410–11) the significant role that they have played in our country, and the diverse functions which they serve. As *ad hoc* bodies, commissions of inquiry are free of many of the institutional impediments which at times constrain the operation of the various branches of government. They are created as needed, although it is an unfortunate reality that their establishment is often prompted by tragedies such as industrial disasters, plane crashes, unexplained infant deaths, allegations of widespread child sexual abuse, or grave miscarriages of justice.
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> ...
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> One of the primary functions of public inquiries is fact-finding. They are often convened, in the wake of public shock, horror, disillusionment, or scepticism, in order to uncover "the truth". Inquiries are, like the judiciary, independent; unlike the judiciary, they are often endowed with wide-ranging investigative powers. In following their mandates, commissions of inquiry are, ideally, free from partisan loyalties and better able than Parliament or the legislatures to take a long-term view of the problem presented. Cynics decry public inquiries as a means used by the government to postpone acting in circumstances which often call for speedy action. *Yet, these inquiries can and do fulfil an important function in Canadian society. In times of public questioning, stress and concern they provide the means for Canadians to be apprised of the conditions pertaining to a worrisome community problem and to be a part of the recommendations that are aimed at resolving the problem ... They are an excellent means of informing and educating concerned members of the public*. [Emphasis added.][2]

In furtherance of those objectives, the Commission conducted 133 days of evidentiary hearings and heard *viva voce* evidence from 199 witnesses (with another 23 witnesses giving evidence by way of affidavit). With a few limited exceptions,[3] these hearings were live-streamed on the Commission website and remain available for public viewing. Transcripts of these hearings – along with the exhibits tendered during the Commission process – are also accessible on the Commission website (though some of these exhibits have been sealed or redacted to protect security and privacy interests).[4]

While the breadth of the Commission's mandate was such that not all possible lines of inquiry could be pursued, it is my sincere hope that these hearings have contributed to a

2 *Phillips v NS (Commission of Inquiry into the Westray Mine Tragedy)*, [1995] 2 SCR 97 at paras 60, 62.

3 Two days of evidence in the financial institutions sector were not live-streamed on the Commission website or otherwise made available to the public in order to maintain the secrecy of countermeasures used by financial institutions to identify and combat money laundering activity (see Ruling 24 – Application for *In Camera* Hearing (January 15, 2021)).

4 A copy of the Commission's *Rules of Practice and Procedure*, which address the manner in which evidence was presented (among other things), can be found at Appendix B. A copy of the Commission's *Rules for Standing* can be found at Appendix C.

deeper understanding of money laundering among concerned members of the public and that the continued availability of these materials on the website will provide an additional source of information for law enforcement, regulators, and other relevant stakeholders.

A third principle that has guided the work of the Commission is the need to respect the rights and interests of the many individuals and agencies that have participated in the Commission process as well as others who may be the subject of adverse comment in this Report. It is important to understand that a commission of inquiry is not a criminal trial. Nor is it an action for the determination of civil liability. There are no legal consequences attached to my findings and they do not bind courts considering the same subject matter.[5] At the same time, the findings made by a commission may have an impact on the reputations of the individuals and entities who are the subject of adverse comment in a final report and it is important that they be given notice of such findings as well as a fair opportunity to respond.

In order to ensure that those who could potentially be subject to adverse comment in the final report had a meaningful opportunity to respond, the Commission issued confidential notices to various individuals and entities advising that they could be subject to adverse findings and setting out the particulars of the alleged misconduct.

Notices of Anticipated Evidence were also issued to certain individuals at the beginning of the hearing process to ensure they had the ability to cross-examine witnesses and otherwise participate in the Commission process from an early stage.

While I appreciate that the receipt of these notices can sometimes come as a shock to the recipient,[6] it is important to reiterate that the purpose of these notices is to give the recipient notice of *potential* findings that could be made and to ensure that they have the opportunity to respond. In every case where a notice was issued, I was careful to not prejudge the issue and carefully reviewed any submissions and further evidence received by the recipient with a view to determining whether the potential findings set out in the notice were supported by the evidence. I also considered whether it was necessary for me to make those findings in order to fulfill my mandate.

In many cases, I chose not to make some or all of the findings set out in a notice either because the evidence did not support a particular finding or because it was not necessary for me to make that finding in order to fulfill my mandate (or both).

Constitutional Limitations

While there can be little doubt that the Province has a legitimate constitutional interest in calling a public inquiry to address the nature and prevalence of criminal activity

5 *Canada (Attorney General) v. Canada (Commission of Inquiry on the Blood System)*, [1997] 3 SCR 440 at para 34 citing *Beno v Canada (Commissioner and Chairperson, Commission of Inquiry into the Deployment of Canadian Forces to Somalia)*, [1997] 2 FC 527 at para 23.

6 On this point see Simon Ruel, *The Law of Public Inquiries in Canada* (Toronto: Thomson Reuters Canada Limited, 2010), p 141.

within the province, it is important to recognize that this is a provincial commission and that there are a number of established constitutional principles that must be respected.[7]

First, it is well established that the Commission cannot allow its process to be transformed into an investigation of specific offences alleged to have been committed by specific persons. Not only would that encroach on the exclusive jurisdiction of the federal government to enact legislation relating to the criminal law, but it would also compromise the substantive and procedural rights guaranteed to those being investigated.[8] While not strictly a constitutional issue, it is also a well-established principle that public inquiries should avoid making findings with respect to civil liability. In *Canada (Attorney General) v Canada (Commission of Inquiry on the Blood System),* [1997] 3 SCR 440 (*Krever*), Mr. Justice Cory expressed these principles as follows:

> A public inquiry was never intended to be used as a means of finding criminal or civil liability. No matter how carefully the inquiry hearings are conducted they cannot provide the evidentiary or procedural safeguards which prevail at a trial. Indeed, the very relaxation of the evidentiary rules which is so common to inquiries makes it readily apparent that findings of criminal or civil liability not only should not be made, they cannot be made.[9]

At the same time, it is important to note that a commission of inquiry is not precluded from making findings relevant to its mandate, including findings that individuals or organizations are at fault in some way. Indeed, the efforts of most commissions would be pointless if they could not make findings about what went wrong and why. What is to be avoided are findings that incorporate a judgment based on a legal standard or that otherwise reflect the requirements of civil or criminal liability:

> The restriction against making determinations of criminal or civil liability does not mean a commission of inquiry is precluded from making findings of fact. Rather, speaking generally, it means commissions may not assess factual matters with reference to normative legal standards.[10]

Second, it is a well-established constitutional principle that a provincial commission of inquiry cannot make findings or recommendations with respect to the internal administration and management of federal agencies. In *Quebec (AG) and Keable v Canada (AG),* [1979] 1 SCR 218, Pigeon J. expressed that principle as follows:

7 For the proposition that the province has a legitimate interest in calling a public inquiry to address the nature and prevalence of criminal activity within the province, see *Di Iorio v Warden of the Montreal Jail,* [1978] 1 SCR 152 at p 201; *Quebec (AG) and Keable v Canada (AG),* [1979] 1 SCR 218 at p 254–55 [*Keable*] ("[t]he investigation of the incidence of crime or the profile and characteristics of crime in a province, or the investigation of the operation of provincial agencies in the field of law enforcement, are quite different things from the investigation of a precisely defined event or series of events with a view to criminal prosecution. The first category may involve the investigation of crime generally and may be undertaken by the invocation of the provincial enquiry statutes"); and *O'Hara v BC,* [1987] 2 SCR 591 at p 610.

8 *Starr v Houlden,* [1990] 1 SCR 1366 at p 1397–1398.

9 *Krever* at para 53.

10 *Hartwig v SK (Inquiry into Matters Relating to the Death of Neil Stonechild),* 2008 SKCA 81 at para 35. See also *Bentley v Braidwood,* 2009 BCCA 604 at para 45 and *Krever* at paras 38, 57, 62.

> I thus must hold that an inquiry into criminal acts allegedly committed by members of the R.C.M.P. was validly ordered, but that consideration must be given to the extent to which such inquiry may be carried into the administration of this police force. It is operating under the authority of a federal statute, the *Royal Canadian Mounted Police Act,* (R.S.C. 1970, c. R-9). It is a branch of the Department of the Solicitor General, (*Department of the Solicitor General Act,* R.S.C. 1970, c. S-12, s. 4). Parliament's authority for the establishment of this force and its management as part of the Government of Canada is unquestioned. It is therefore clear that no provincial authority may intrude into its management. *While members of the force enjoy no immunity from the criminal law and the jurisdiction of the proper provincial authorities to investigate and prosecute criminal acts committed by any of them as by any other person, these authorities cannot, under the guise of carrying on such investigations, pursue the inquiry into the administration and management of the force.* [Emphasis added.][11]

While that principle prevents me from interfering in the management and administration of federal agencies, I do not understand it to prohibit a consideration of the federal anti–money laundering regime as a whole, or the effectiveness of federal entities such as the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), the Royal Canadian Mounted Police (RCMP) and the Canada Border Services Agency (CBSA). Such inquiries are necessary "in order to explain what took place during the relevant time frame"[12] and make effective recommendations to the provincial government about steps that must be taken to address money laundering activity.

I have paid close attention to both constitutional principles in making the findings of fact and recommendations contained in this Report. While I have made a number of factual findings concerning the activities of those alleged to be involved in money laundering activity, the purpose of these findings is to shed some light on the methods used by organized crime groups to launder illicit funds and to evaluate the response of provincial regulatory agencies. I have not assessed their conduct against any legal standard, and it is not my intention to suggest that the elements of criminal or civil liability are satisfied. Likewise, I have conducted a comprehensive review of the federal anti–money laundering regime and considered the effectiveness of federal agencies such as FINTRAC and the RCMP in responding to money laundering in the province of British Columbia. However, I have, at all times, been mindful of the prohibition against interference in the management and administration of federal agencies.

Commission Counsel

One of my first tasks as Commissioner was to put together the senior leadership team that would be responsible for managing the substantive work of the Commission.

11 *Keable* at p 242.

12 Reply of the Attorney General of Canada, October 19, 2021, p 127.

In May 2019, I appointed Brock Martland, QC, and Patrick McGowan, QC, as senior Commission counsel. Both have significant knowledge, expertise, and experience in the conduct of public inquiries, and I have relied on them to manage the substantive work of the Commission. Mr. Martland and Mr. McGowan were assisted by a talented team of associate and junior counsel, which included Alison Latimer, QC, Nicholas Isaac, Eileen Patel, Kyle McCleery, Kelsey Rose, Steven Davis, and Charlotte Chamberlain.

In December 2019, Tam Boyar, a senior lawyer with a broad range of experience, was appointed as policy counsel. Mr. Boyar was assisted in that work by Dahlia Shuhaibar, who made significant contributions to the Inquiry in her role as junior policy counsel.

I would also be remiss if I did not express my gratitude to Dr. Leo Perra, the executive director of the Commission, Cathy Stooshnov, manager of finance and administration, and Keith Hamilton, QC, who shared his wisdom and experience with members of the legal and policy teams.[13]

Over the life of the Commission, Commission counsel acted as the alter ego of the Commissioner and were responsible for various tasks including:

- preliminary investigations;
- witness interviews and document production;
- consultation with experts and investigators;
- preparation of overview reports;
- communications with participants;
- organization and presentation of evidence;
- examination of witnesses;
- legal and policy research;
- advising and assisting with evidentiary and procedural rulings;
- advising and assisting with the Interim Report; and
- advising and assisting with the Final Report.

While I freely conferred with Commission counsel on most issues, there were a few instances in which it was necessary to take a different approach. On contentious applications where Commission counsel took a position, Commission counsel were divided into two groups: a legal team responsible for responding to the application (in a visible way, for all participants to see) and a separate advisory team responsible for advising and assisting with my eventual ruling.

13 A full list of Commission staff can be found at Appendix D.

The purpose of that division was to ensure that those who took an adversarial stance on the application were not advising or otherwise assisting me in preparing my ruling.

I also issued a ruling on May 5, 2021, in which I restricted the role of hearing counsel (i.e., Commission counsel who participated in the gathering and presentation of evidence) in the consideration of certain evidence tendered during the Commission process.[14]

Participants

Because of the breadth of the Commission's mandate, I considered it necessary and appropriate to hear from a wide range of voices. I granted participant status to various individuals and organizations. Some of these participants were given standing with respect to all issues before the Commission, while others were given standing with respect to specific issues. In what follows, I provide some information on each of these participants and comment on the perspectives they brought to the Commission.[15]

Province of British Columbia

The Province of British Columbia initially sought to participate in the Inquiry through the Ministry of Finance and the Gaming Policy and Enforcement Branch, and as such, I initially granted standing to those two provincial bodies. Both entities were highly responsive to the many document and interview requests made by Commission counsel, and I am very grateful for the efforts of these entities and their counsel.

The Ministry of Finance has responsibilities in many of the sectors identified in the Terms of Reference, including the real estate, corporate, and financial sectors. It has also been involved in the development and implementation of the provincial anti–money laundering strategy.

The Gaming Policy and Enforcement Branch is responsible for the overall integrity of gaming and horse racing in the province and has regulatory oversight of the gaming and horse-racing industries.

It is also responsible for providing advice to the Attorney General on all gaming policy matters, including both regulatory and operational matters.

On December 4, 2020, I issued a ruling in which I replaced the separate grant of participant status given to the Ministry of Finance and the Gaming Policy and Enforcement Branch with a single grant of participant status to Her Majesty the Queen in Right of the Province of British Columbia (HMTQ). I gave HMTQ standing with respect to all matters set out in my Terms of Reference.

14 For a more detailed discussion of that issue, see Ruling 32 (May 5, 2021). A full list of rulings made during the Commission process can be found at Appendix E.

15 A list of all participants and their counsel can be found at Appendix F.

Government of Canada

The Government of Canada (Canada) plays a central role in the fight against money laundering and has put in place an anti–money laundering regime made up of various agencies and institutions. The *Proceeds of Crime (Money Laundering) and Terrorist Financing Act,* SC 2000, c 17 (*PCMLTFA*), is the centrepiece of the federal anti–money laundering regime. Broadly speaking, that legislation creates mandatory record-keeping and reporting requirements for financial institutions and other businesses, such as casinos, where there is a risk of money laundering occurring.[16] Examples of these requirements include suspicious transaction reports, which must be filed where there are reasonable grounds to suspect that a transaction is related to the commission or attempted commission of a money laundering offence; large cash transaction reports, which must be filed when reporting entities receive $10,000 or more in cash in a single transaction; and electronic funds transfer reports, which must be filed when reporting entities process cross-border electronic funds transfers of $10,000 or more.[17]

The *PCMLTFA* also creates a financial intelligence unit (FINTRAC) that is responsible for receiving and analyzing information relating to money laundering activity. Under section 55(3), FINTRAC is required to disclose certain information to law enforcement agencies where it has reasonable grounds to suspect that the information is relevant to the investigation or prosecution of a money laundering offence. Moreover, it is authorized to conduct research into money laundering trends and developments and to inform reporting entities, law enforcement authorities, and the public about the nature and extent of money laundering in Canada and internationally.

Other federal agencies involved in the fight against money laundering include the Office of the Superintendent of Financial Institutions, the Public Prosecution Service of Canada, the RCMP, the Canada Revenue Agency, and the Canada Border Services Agency.

The Office of the Superintendent of Financial Institutions is responsible for supervising and regulating more than 400 federally regulated financial institutions and 1,200 pension plans. While it does not manage the substantive operations of these institutions, it plays an important regulatory and oversight role in assessing the strength of their regulatory compliance and risk management practices.

The Public Prosecution Service of Canada generally prosecutes criminal offences under federal statutes other than the *Criminal Code,* RSC 1985, c C-46. Examples include the *Controlled Drugs and Substances Act,* SC 1996, c 19; the *Income Tax Act,* RSC 1985, c 1 (5th Supp); the *Immigration and Refugee Protection Act,* SC 2001, c 27; and the *Firearms Act*, SC 1995, c 39. In prosecuting such offences, it can seek authorization from the province to prosecute related offences such as those set out in sections 354 and 462.31 of the *Criminal Code*. It also has the power to seek the forfeiture of illegal proceeds and offence-related property in the sentencing process.

16 Examples of these entities (sometimes called "reporting entities") include banks, credit unions, life insurance companies, trust and loan companies, real estate agents, notaries, accountants, and casinos.

17 *PCMTLFA*, ss 7, 9, 12.

The RCMP, Canada Border Services Agency, and Canada Revenue Agency play critical roles in the investigation of money laundering offences, often in conjunction with provincial and international partners such as the US Drug Enforcement Administration.

In light of the central role it plays in the fight against money laundering, I gave the federal government participant status in all sectors identified in my Terms of Reference.

Law Society of British Columbia

The Law Society of British Columbia (Law Society) is responsible for the regulation of lawyers in the province. It operates independently of government and is responsible for upholding the public interest in the administration of justice, including the integrity, independence, honour, and competence of lawyers practising in British Columbia.

The Law Society was given participant status in various sectors identified in my Terms of Reference, including the real estate sector, financial institutions and money services businesses, the corporate sector, luxury goods, and the professional services sector.

Society of Notaries Public of British Columbia

The Society of Notaries Public of British Columbia is responsible for the regulation of notaries in British Columbia. Under section 18 of the *Notaries Act*, RSBC 1996, c 334, notaries are entitled to provide a range of legal services in the province, including services relating to the purchase and sale of real estate.

The Society of Notaries Public of British Columbia was granted participant status in the real estate sector and the professional services sector.

British Columbia Lottery Corporation

The BC Lottery Corporation is a Crown corporation responsible for the "conduct and management" of gaming in the province.[18] In furtherance of that mandate, it has entered into operational service agreements with gaming service providers, who are responsible for the day-to-day operation of casinos. These agreements incorporate detailed standards, polices, and procedures that must be followed by gaming service providers in operating their facilities. The BC Lottery Corporation also has various reporting obligations under the *PCMLTFA* and the *Gaming Control Act*, SBC 2002, c 14. The BC Lottery Corporation was granted participant status in the gaming and horse-racing sector.

Great Canadian Gaming Corporation

The Great Canadian Gaming Corporation (Great Canadian) is a publicly traded corporation that operates gaming facilities in British Columbia, Ontario, Nova Scotia,

18 *Gaming Control Act*, s 7.

and New Brunswick. At the time it applied for participant status, it operated 10 gaming facilities in British Columbia, including two of the largest casinos in the province (the River Rock Casino Resort and the Hard Rock Casino Vancouver) and the only two racetracks that continue to host live horse racing.[19] Great Canadian was granted participant status in the gaming and horse-racing sector.

Gateway Casinos and Entertainment Inc.

Gateway Casinos and Entertainment Inc. (Gateway) is a gaming service provider that operates three of the largest gaming and entertainment facilities in the Lower Mainland as well as a number of smaller gaming sites in Vancouver, on Vancouver Island, and in the Okanagan Valley.[20] Gateway was granted participant status in the gaming and horse-racing sector.

Canadian Gaming Association

The Canadian Gaming Association is a not-for-profit organization that works to advance the evolution of Canada's gaming industry; promote the economic value of gaming in Canada; use research, innovation, and best practices to help the industry advance; and create productive dialogue among relevant stakeholders.[21] Its members include leading gaming operators such as Gateway and Hard Rock casinos as well as law firms and suppliers to the industry.[22] The Canadian Gaming Association was granted participant status in the gaming and horse-racing sectors.

British Columbia Government and Service Employees' Union

The British Columbia Government and Service Employees' Union (since renamed the British Columbia General Employees' Union) is one of the largest labour unions in British Columbia. It represents more than 80,000 members who work in almost every sector of the economy, including the public service, the financial services industry, and the gaming sector. The BC Government and Service Employees' Union was granted participant status in the following sectors: gaming and horse racing, real estate, financial institutions, the corporate sector, luxury goods, and the professional services sector.

19 Each of these facilities is operated by Great Canadian's wholly owned subsidiaries: Great Canadian Casinos Inc., Hastings Entertainment Inc., Orangeville Raceway Limited, Great Canadian Entertainment Centres Ltd., and Chilliwack Gaming Ltd.

20 Gateway also operates the Grand Villa and Starlight casinos in Edmonton and various gaming and entertainment facilities in Ontario.

21 Application for standing (Canadian Gaming Association), para 3.

22 Opening statement of the Canadian Gaming Association, p 2.

BMW Canada Inc. and BMW Financial Services

BMW Canada Inc. (BMW) is the Canadian subsidiary of BMW AG, a German multinational company that manufactures and distributes luxury vehicles and mobility services through its retail network in Canada. BMW Financial Services, a division of BMW, provides financial services, including leasing and financing of vehicles, to BMW customers in Canada. BMW was granted participant status in two sectors: luxury goods and financial institutions.

Chartered Professional Accountants of Canada

The Chartered Professional Accountants of Canada (CPA Canada) is the national organization that represents Canada's accounting profession domestically and internationally. CPA Canada was formed through the unification of Canada's three legacy accounting designation bodies: the Canadian Institute of Chartered Accountants, the Society of Management Accountants of Canada, and the Certified General Accountants Association of Canada. It has over 220,000 members who have obtained the chartered professional accountant designation or possess a legacy designation.

CPA Canada is not a regulator but works co-operatively with provincial and territorial regulatory bodies, including the Chartered Professional Accountants of British Columbia.

CPA Canada was granted participant status in the professional services sector.

Chartered Professional Accountants of British Columbia

The Chartered Professional Accountants of British Columbia (CPABC) is a statutory corporation that exercises responsibilities under the *Chartered Professional Accountants Act,* SBC 2015, c. 1 (the *CPA Act*). CPABC is currently the sole statutory professional regulatory body for professional accountants in British Columbia.

CPABC was granted participant status in the professional services sector.

British Columbia Civil Liberties Association

The British Columbia Civil Liberties Association is a non-profit advocacy group with a mandate to defend, maintain, and extend civil liberties and human rights in Canada. It has expertise in a wide range of civil liberties matters, including criminal law reform, police accountability, access to justice, due process, and the impact of investigative and enforcement mechanisms on privacy interests.

The BC Civil Liberties Association was given participant status in all sectors identified in my Terms of Reference and has brought an important civil liberties perspective to the work of the Inquiry, particularly as it relates to the potential

expansion of police and regulatory powers, the increased collection of personal information, and the introduction of measures such as unexplained wealth orders (discussed below).

Canadian Bar Association and the Criminal Defence Advocacy Society

The Canadian Bar Association is a professional organization representing the interests of more than 36,000 legal professionals, including lawyers, law students, academics, and judges. Founded in 1896, the Canadian Bar Association was formally incorporated by an Act of Parliament in 1921 and has branches in every province and territory. The British Columbia branch has more than 7,000 members in a wide range of practice areas, including criminal justice, real estate, corporate law, family law, and civil litigation.

The Criminal Defence Advocacy Society was founded in 2015 by members of the criminal defence bar in British Columbia. It is particularly concerned with the rule of law, the independence of the bar, and the constitutional rights of accused persons.

Because of the substantial overlap between the proposed contributions of these organizations, I directed that they share a single grant of standing in relation to all sectors identified in my Terms of Reference.

British Columbia Real Estate Association

The British Columbia Real Estate Association is a professional association representing more than 23,000 commercial and residential realtors in the province. It does not have any legislative or regulatory powers and works with its member boards on matters such as professional development, advocacy, economic research, and the development of standard forms.

The BC Real Estate Association was granted participant status in the real estate sector.

Transparency International Canada, Canadians for Tax Fairness, and Publish What You Pay Canada

Transparency International Canada, Canadians for Tax Fairness, and Publish What You Pay Canada (Transparency Coalition) is a coalition of public interest advocacy groups that has been campaigning to increase corporate transparency and establish a publicly accessible beneficial ownership registry in Canada.

The Transparency Coalition was given a single grant of standing in relation to financial institutions, the real estate sector, and the corporate sector.

James Lightbody

James Lightbody is the president and chief executive officer of the BC Lottery Corporation. He has held that position since February 2014, when he was promoted from vice-president of casino and community gaming. Mr. Lightbody was granted participant status in relation to the gaming and horse-racing sector.

Robert Kroeker

Robert Kroeker has held a number of senior positions in the gaming industry, including chief compliance officer and vice-president of legal, compliance, and security at the BC Lottery Corporation and vice-president of compliance and regulatory affairs at Great Canadian. Mr. Kroeker was also involved in the creation and operation of the BC Civil Forfeiture Office, where he worked extensively with police and other enforcement agencies in British Columbia and beyond. Mr. Kroeker was granted participant status in the gaming and horse-racing sector.

Brad Desmarais

Brad Desmarais is currently the vice-president of casino and community gaming at the BC Lottery Corporation and has been with the BC Lottery Corporation in various other capacities since 2013. Before joining the BC Lottery Corporation, he worked as a police officer with the Vancouver Police Department and the RCMP.

Mr. Desmarais was granted participant status in the gaming and horse-racing sector.

Paul Jin

Paul Jin came to the attention of the Commission as someone who was potentially involved with the lending of cash to gamblers through his association with an unregistered money services business in Richmond, British Columbia.

Mr. Jin sought and was granted standing to question witnesses, make submissions, and exercise the rights of a participant in relation to evidence that affects his interests or engages him specifically.[23]

After granting participant status to Mr. Jin, I was asked to make various rulings relating to his participation in the Inquiry and the process adopted by the Commission for making findings and recommendations that could affect his interests. These rulings include:

- Ruling 26, which dealt with an application brought by Commission counsel concerning Mr. Jin's ability to access to documents produced by other participants;

23 Ruling 14 – Application for Standing (November 5, 2020), para 16.

- Ruling 32, which dealt with an application brought by Mr. Jin for various orders and directions relating to the process for making findings of fact and recommendations concerning Mr. Jin;
- Ruling 34, which dealt with an application brought by Mr. Jin for an order that Commission counsel provide him with the definition of the term "loan shark" as that term will be used and applied by the Commission in analyzing the evidence and considering and formulating findings and recommendations;
- Ruling 36, which dealt with an application brought by Mr. Jin for various orders relating to an overview report sought to be tendered by Commission counsel concerning Mr. Jin's private lending activity; and
- Ruling 37, which dealt with an application brought by Mr. Jin to compel information and documents relating to the process adopted by the Commission for the issuance of summonses as well as certain interviews conducted by Commission counsel.

I have followed the process outlined in these rulings and given careful consideration to the oral and written submissions made by Mr. Jin (and his counsel) in every instance where I have made findings of fact and recommendations that could affect his interests.

Kash Heed

Kash Heed has had a long career in public service, having served as a member of the Vancouver Police Department from 1979 to 2007, Chief Constable of the West Vancouver Police Department from 2007 to 2009, and Minister of Public Safety and Solicitor General from June 10, 2009 to April 9, 2010, and again from May 4 to May 5, 2010.

On November 12, 2020, I granted him participant status for the limited purpose of cross-examining Fred Pinnock, a former RCMP officer who has levied public criticisms of his superior officers, and others, for their alleged failure to take steps to abate money laundering activity in the gaming industry. I return to these issues in Part III.

Ross Alderson

Ross Alderson was an employee of the BC Lottery Corporation from 2008 to 2017 and served as the director for anti–money laundering, investigations, and intelligence from 2015 until his resignation in 2017. Mr. Alderson first sought participant status by way of an application dated September 4, 2019, but subsequently withdrew that application.

On May 24, 2021, Mr. Alderson submitted a renewed application for standing in which he took the position that the evidence led through the Inquiry process has given rise to allegations of misconduct, unlawful behaviour, and mental health issues in relation to his employment at the BC Lottery Corporation. He also took the position that

he has "extensive knowledge of the gambling industry" and it has become evident that he is a "key witness with intimate knowledge of events between 2009–2017."[24]

On June 25, 2021, I granted him limited participant status to address matters involving his personal conduct and respond to evidence that could adversely impact his legal, reputational, or privacy interests.[25]

Public Meetings

From October 23 to November 14, 2019, the Commission held public meetings in Vancouver, Victoria, Kelowna, Prince George, and Richmond. The purpose of these meetings was to seek input from the communities most affected by money laundering.

While participants were free to speak on any topic relevant to the Commission's mandate, the following questions were posed in advance of the meetings:

- What are the most significant money laundering issues facing your community in British Columbia and in Canada?
- What areas of our mandate would you like us to focus on or address in our process?
- What have been the major consequences of money laundering in your community?
- What do you think is required to address the issues you have identified?
- How can the Commission keep you informed on our activities and findings?
- How can community members participate or stay involved in the process?

I would like to thank the many individuals who attended and made presentations at these public meetings. The thoughtful presentations I heard gave me considerable insight into the perspectives and concerns of members of the public.

In the five sections that follow, I provide a summary of the ideas and concerns expressed by members of the public at each of these meetings.

Vancouver

On October 23, 2019, the Commission held a public meeting in Vancouver and heard concerns regarding:

- the increase in criminal activity on the streets of Vancouver;
- the prevalence of money laundering in the gaming industry, including the lack of meaningful action taken by the Gaming Policy and Enforcement Branch, the BC

24 Ruling 33 – Application for Participant Status (June 25, 2021), paras 15–16.

25 Ibid.

Lottery Corporation, and gaming service providers to combat money laundering in BC casinos;

- the involvement of lawyers in money laundering activity, including the absence of any reporting obligations under the *PCMLTFA* and the use of trust accounts to facilitate illegal transactions;
- the suppression of relevant information and evidence by different levels of government;
- the need to strengthen whistle-blower protections, particularly in the gaming industry;
- the use of illicit funds to purchase real estate in British Columbia;
- the infiltration of casinos by organized crime figures; and
- the failure of law enforcement and regulatory agencies to actively (or effectively) prosecute money laundering offences.

Many of the presenters spoke to their personal experiences and observations with these matters, including efforts to inform the RCMP and other relevant authorities about suspicious activity they believed to be connected to money laundering.

Kelowna

On October 29, 2019, the Commission held a public meeting in Kelowna.

One of the presenters was a former manager of a real estate company who expressed concerns about the process for tracking money in real estate transactions as well as the lack of compliance with FINTRAC regulations. They also expressed concern about the potential use of rental income as a way of laundering illicit funds.

I also heard concerns about the ability of the BC Securities Commission to properly regulate the market and the extent to which organized crime and money laundering has infiltrated the community.

Victoria

On November 4, 2019, the Commission held a public meeting in Victoria where presenters addressed a number of topics, including:

- the high proportion of money laundering cases involving white-collar professionals;
- the need to better regulate lawyers;
- the lack of compliance among reporting entities with the *PCMLTFA*;

- the prevalence of money laundering in BC casinos, including the perception that government has largely "ignored" the problem;
- the need to protect whistle-blowers;
- the impact of money laundering on housing affordability; and
- the lack of enforcement of anti–money laundering laws in comparison with other countries.

One of these individuals spoke to the "regrettable" decision to disband the Integrated Proceeds of Crime units and suggested that substantial money laundering leads submitted to the RCMP have not been acted upon. He also suggested that the sanctions for failing to report suspicious transactions to FINTRAC were not significant enough to act as an effective deterrent and that the centre should take additional steps to audit reporting entities to ensure compliance.

Among the solutions these individuals proposed were a beneficial ownership registry and the use of unexplained wealth orders.

Richmond

On November 7, 2019, the Commission held a public meeting in Richmond and heard presentations from a number of concerned individuals. A consistent theme in these presentations was the impact of money laundering on the real estate sector, including the impact on housing affordability and the construction of "mega mansions" on agricultural land. Presenters expressed concern that such encroachment pulls good farmland out of production, drives up the cost of real estate, and allows criminals to enjoy the proceeds of crime. Other concerns included:

- the prevalence of money laundering in the gaming sector;
- the exemption of lawyers from the financial reporting requirements set out in the *PCMLTFA*;
- cash payments in the construction industry as a potential weakness in the current anti–money laundering regime;
- lack of compliance with reporting obligations under the *PCMLTFA*, particularly among realtors; and
- the lack of any meaningful enforcement of anti–money laundering laws by law enforcement agencies.

A few of these speakers expressed the view that the current state of affairs is contrary to Canadian values, discouraging for British Columbians, and a "black eye" on

the history of our country. They also expressed considerable support for unexplained wealth orders as well as increased corporate transparency, including the creation of a beneficial ownership registry in the corporate sector.

Prince George

On November 14, 2019, the Commission held its fifth public meeting, in Prince George, where several speakers expressed concern that the Commission's work may have no lasting effect, particularly when law enforcement agencies have been subject to significant cutbacks and have failed to act on matters related to money laundering.

Written Submissions

In addition to holding public meetings, the Commission invited members of the public who could not attend a public meeting or preferred to share their perspectives in writing to make written submissions to the Commission. The Commission has received a large number of written submissions from concerned members of the public.

These submissions are largely consistent with the perspectives and concerns raised at the public meetings reviewed above. I am grateful to the many citizens of our province who have taken the time to share their thoughts and perspectives with the Commission. Each of these submissions has been reviewed and considered.

Sources of Evidence

In order to develop an evidentiary basis for the findings of fact and recommendations mandated by my Terms of Reference, the Commission received and considered evidence from a variety of sources. Each of these sources are discussed below.

Terms of Reference Reports

One of the first steps taken by the Commission in furtherance of its mandate was to thoroughly review and analyze the Terms of Reference Reports along with various other studies and reports concerning money laundering in British Columbia.

While these reports were invaluable in identifying issues to be investigated and solutions to be explored, I have not considered or otherwise relied on these reports in making findings of fact on contentious issues or in making findings that could reflect adversely on any party.

A full review of the key findings and recommendations contained in the Terms of Reference Reports, along with the responses of each participant with standing in the Inquiry, is contained in my Interim Report released in November 2020.

Overview Reports

On December 5, 2019, the Commission enacted *Rules of Practice and Procedure* in accordance with section 9 of the *Public Inquiry Act*.

Rule 32 allows Commission counsel to prepare "overview reports" containing core or background information with respect to issues being considered. These reports were then circulated to participants, who had the opportunity to comment on the information contained in those reports before they were entered into evidence. Because of the breadth of the Commission's mandate, and the sheer volume of evidence tendered on each issue, these reports were invaluable in putting relevant evidence before the Commission in an efficient manner. A total of 57 such reports were entered as exhibits.

Witness Testimony

Witness testimony was a critical source of evidence for the Commission in making the findings of fact and recommendations contained in this Report.

The Commission heard *viva voce* evidence from 199 witnesses, with another 23 witnesses giving sworn evidence by way of affidavit.

Many of these witnesses were highly qualified experts who gave evidence with respect to various topics including:

- money laundering typologies (i.e., the methods used by those involved in money laundering activity to launder illicit funds);
- the Financial Action Task Force and other components of the international anti–money laundering regime;
- the Canadian anti–money laundering regime;
- legal and regulatory responses to money laundering in other countries, including the United Kingdom, the United States, Ireland, Australia, and New Zealand;
- quantification (i.e., estimates of the total volume of illicit funds laundered through the BC economy);
- legal and regulatory responses to money laundering in specific sectors of the economy, including the gaming sector, real estate, financial institutions, the corporate sector, luxury goods, professional services, and cryptocurrency;
- law enforcement responses to money laundering in Canada and other jurisdictions, including the United Kingdom, the United States, and New Zealand;
- information sharing and privacy; and

- asset forfeiture, including the asset forfeiture regime in jurisdictions such as the United Kingdom, the United States, Ireland, New Zealand, and Manitoba.[26]

I am very grateful for the knowledge, experience, and insight that these witnesses brought to the work of the Commission.

Exhibits

A total of 1,063 exhibits were entered through the Commission process, including the 57 overview reports referenced above. These exhibits include a wide range of reports, affidavits, briefing notes, slide decks, memos, emails, and other documents that contain a wealth of information on a wide range of money laundering topics.[27]

Additional Research and Study

Finally, it is important to note that the Commission was established as both a hearing commission and a study commission under section 20 of the *Public Inquiry Act*.

In accordance with its study commission mandate, the Commission has conducted additional interviews and research to supplement the evidence tendered through the hearing process. I note, however, that the information received through the study commission process was not considered in making any findings of misconduct.

The COVID-19 Pandemic

The COVID-19 pandemic has impacted the Commission – and the province – in ways that would have been unimaginable at the time the Commission was established.

Like most individuals, organizations, and businesses, the Commission was required to adapt to the reality of the pandemic and find new ways to conduct its work.

One of the key challenges faced by the Commission was the need to conduct virtual hearings. I am extremely grateful to Leo Perra, Shay Matters, Kelsey Rose, Linda Peter, Phoenix Leung, Natasha Tam, Sarah LeSage, John Lunn, Mary Williams, and Scott Kingdon for their dedicated efforts to create and run a virtual courtroom on very short notice.

I would also like to thank participants, witnesses, and counsel for their continued engagement with the Commission during these difficult times. In the best traditions, they adapted to, and facilitated, our shift to an entirely virtual hearing process, in a co-operative fashion. I remain grateful for their approach.

26 A full list of witnesses with links to hearing transcripts and webcasts can be found at Appendix G.

27 A list of exhibits tendered during the Commission process can be found at Appendix H.

In the next chapter of this Report, I provide a high-level overview of money laundering, including the methods commonly used by offenders to launder illicit funds.

I then provide an overview of the individuals and groups involved in money laundering activity, followed by a discussion of quantification (i.e., estimates of the volume of illicit funds laundered through the BC economy).

I conclude Part I with a discussion of the harms caused by money laundering, including the impact it has on individuals and communities throughout the province.

Chapter 2
What Is Money Laundering?

Section 1 of my Terms of Reference defines money laundering as "the process used to disguise the source of money or assets derived from illegal activity."[1] Other commonly cited definitions include "the process by which one converts or transfers cash or other assets generated from profit-oriented crimes in order to conceal their illegal origins,"[2] "any act or attempted act to disguise the source of money or assets derived from criminal activity,"[3] and "the process used by criminals to conceal or disguise the origin of criminal proceeds to make them appear as if they originated from legitimate sources."[4] The *Criminal Code,* RSC 1985, c C-46, creates the criminal offence of money laundering in Canada. It provides, in relevant part:

> **Laundering proceeds of crime**
>
> **462.31 (1)** Every one commits an offence who uses, transfers the possession of, sends or delivers to any person or place, transports, transmits, alters, disposes of or otherwise deals with, in any manner and by any means, any property or any proceeds of any property with intent to conceal or convert that property or those proceeds, knowing or believing that, or being reckless as to whether, all or a part of that property or of those proceeds was obtained or derived directly or indirectly as a result of

1 Terms of Reference, para 1.

2 Exhibit 6, Stephen Schneider, *Money Laundering in British Columbia: A Review of the Literature,* p 12.

3 Exhibit 3, Overview Report: Documents Created by Canada, Appendix A, Canada, Parliament, Senate, Standing Senate Committee on Banking, Trade and Commerce, *Follow the Money: Is Canada Making Progress in Combatting Money Laundering and Terrorist Financing? Not Really, Report of the Standing Senate Committee on Banking, Trade and Commerce,* 41st Parl, 1st Sess (March 2013) (Chair: Irving R. Gerstein), p 1.

4 Ibid, Appendix B, Canada, Department of Finance, *Assessment of Inherent Risks of Money Laundering and Terrorist Financing in Canada, 2015* (Ottawa: 2015) [2015 National Risk Assessment], p 9.

a) the commission in Canada of a designated offence; or

b) an act or omission anywhere that, if it had occurred in Canada, would have constituted a designated offence.[5]

Section 462.3(1) defines the term "designated offence" as (a) any offence that may be prosecuted as an indictable offence under the *Criminal Code* or any other Act of Parliament, other than an indictable offence prescribed by regulation or (b) a conspiracy or an attempt to commit, being an accessory after the fact in relation to, or any counselling in relation to an offence referred to in paragraph (a). Examples include drug trafficking, human smuggling, counterfeiting, illegal gaming, and certain types of fraud.

While the primary objective of money laundering is to conceal the true origins and ownership of illicit funds, a comprehensive money laundering scheme will also seek to "legitimize" those funds (that is, to make it appear that they have been derived from legitimate sources, such as a legal business). Stephen Schneider, a professor at St. Mary's University, Halifax, and one of Canada's foremost authorities on organized crime, financial crime, and money laundering, distinguished between these two objectives as follows:

> You can conceal criminal activity or a criminal source through what's called layering, and that is … transaction upon transaction upon transaction through numerous financial instruments or commercial sectors to try to basically obfuscate any kind of paper trail between the asset or the funds and the criminal source. So that is in itself an important step in the process or an important objective. *But again, on top of that, to really truly satisfy the process, it's not good enough just to conceal it. You want to have that legitimate source. I mean, some examples of creating a legitimate source … the most common … is setting up a shell company or even a real company that produces legitimate revenue. You would like a company that in its normal line of business produces cash … like a bar or a restaurant, and you commingle your drug proceeds with the cash from [a] legitimate [source] and then you deposit into a commercial bank account … [T]hat's a typical example of creating legitimacy. You … are concealing the criminal sources, but more importantly you're creating the guise of legitimacy. And there's various techniques to use to create that legitimacy.* [Emphasis added.][6]

5 *Criminal Code*, RSC 1985, c C-46, ss 462.31(1). Note that the *Criminal Code* definition of money laundering is narrower than the definition contained in my Terms of Reference and that I have been guided by the definition in my Terms of Reference. Nothing in this Report is intended as a finding that any particular individual or entity is guilty of any criminal offence.

6 Transcript, May 25, 2020, pp 31–32. See also Exhibit 23, Money-Laundering Typologies: A Review of their Fitness for Purpose (October 31, 2013), p 8, where Professor Michael Levi of Cardiff University, an expert in money laundering and transnational organized crime, states that the "central purpose" of money laundering is to ensure a legitimate appearance of what is in fact the proceeds of crime; Evidence of Simon Lord, a money laundering expert at the National Crime Agency in the United Kingdom, Transcript, May 28, 2020, p 10 ("Money laundering at its most basic is the act of making the origin of criminally derived funds appear legitimate"); and Evidence of Robert Wainwright, Transcript, June 15, 2020, p 17 ("[Money laundering] is the process of … concealing – disguising the identity and ownership of illegally obtained proceeds in a way that makes the origin appear legitimate while leaving no link to the real source of funds").

In what follows, I make some general comments about money laundering and introduce some of the themes that have emerged during the Commission process.

Predicate Offences

From the outset, it is important to recognize that money laundering is inextricably tied to revenue-generating criminal offences. Such offences (sometimes referred to as "predicate offences") include drug trafficking, fraud, human trafficking, counterfeiting, and a variety of other offences that have as their primary objective the generation of illicit funds through criminal activity. A 2015 risk assessment conducted by the federal Department of Finance (the National Risk Assessment) describes the threat actors perpetrating profit-oriented crime as ranging from unsophisticated, criminally inclined individuals and street-gang members to criminalized professionals[7] and transnational organized crime groups such as Mexican and Colombian cartels.[8] The report goes on to identify 22 profit-oriented crimes and evaluates the money laundering threat associated with each of those crimes, using the following criteria:

- **Sophistication**: the extent to which the perpetrators have the knowledge, skills, and expertise to launder criminal proceeds and avoid detection by authorities;
- **Capability**: the extent to which the perpetrators have the resources and network to launder criminal proceeds (e.g., access to facilitators and links to organized crime);
- **Scope**: the extent to which the perpetrators are using financial institutions and designated non-financial businesses and professions (such as lawyers and accountants) to launder criminal proceeds; and
- **Magnitude**: the estimated dollar value of the illicit funds being generated annually from the profit-oriented crime.[9]

Nine offences were rated as having a very high money laundering risk. These offences were capital markets fraud, commercial trade fraud, corruption and bribery, counterfeiting and piracy, illicit drug trafficking, mass-marketing fraud, mortgage fraud, third-party money laundering, and tobacco smuggling and trafficking.[10]

Eight offences were rated as having a high money laundering risk. These offences were currency counterfeiting, human smuggling, human trafficking, identity theft and fraud, illegal gambling, payment-card fraud, pollution crime, and robbery and theft.[11]

7 "Criminalized professionals" are defined in that report as individuals who hold or purport to hold a professional designation and title in an area dealing with financial matters and who use their professional knowledge and expertise to commit or willingly facilitate profit-oriented criminal activity. Examples include lawyers, accountants, notaries, investment and financial advisors, stock brokers, and mortgage brokers.

8 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 18.

9 Ibid, p 19. For additional commentary on the four criteria used in this Report, see Evidence of S. Schneider, Transcript, May 25, 2020, pp 45–47.

10 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 19.

11 Ibid.

Four offences were rated as having a medium money laundering risk. These offences were firearms smuggling and trafficking, extortion, loan sharking, and tax evasion / fraud.[12]

One offence (wildlife crime) was rated as having a low money laundering risk.[13]

In what follows, I make some general comments about these offences and the associated money laundering risk.

Capital Markets Fraud

Capital markets fraud involves a wide range of illicit activities relating to capital markets. Examples include investment misrepresentation, insider trading, and pyramid schemes.

The National Risk Assessment notes that capital markets fraud is a "rich source" of illicit funds that can generate millions of dollars in profits. It also notes that capital markets frauds are often perpetrated by criminalized professionals and accompanied by sophisticated money laundering schemes designed to integrate the profits of these schemes into the financial system.

In his testimony before the Commission, Professor Schneider expressed the view that law enforcement bodies tend to focus on crimes such as drug trafficking and do not pay sufficient attention to financial crime, despite the significant impact it has on society:

> [W]e talk about proceeds of crime, we tend to focus on … organized crime, like drug trafficking, prostitution and tobacco smuggling and people smuggling and gambling, but even though I'm loath to try to estimate the scope of any kind of crime … certainly we do not pay sufficient attention to the type of commercial crimes that occur in society, the impact that has on society and the amount of proceeds of crime and money laundering that accompany these economic crimes.[14]

While the relative priority given to financial crime is beyond the scope of this Report, these comments are important insofar as they highlight the wide range of offences giving rise to money laundering activity. Moreover, it is important to note that there can be significant organized crime involvement in certain types of financial crime, with the lucrative financial returns being laundered and used to fund other types of criminality.[15]

12 Ibid.

13 Ibid.

14 Transcript, May 25, 2020, p 51.

15 Exhibit 1017, Overview Report: Criminal Intelligence Service Canada National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud (2020), Appendix A, Criminal Intelligence Service Canada, *National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud 2020* (Ottawa: 2020), p 4 ("Financial crime, often seen as 'white collar' crime, is committed by highly capable criminals and interconnected [organized crime groups], both in Canada and abroad, with some Canadian [organized crime groups] directly involved in running boiler rooms (i.e., telemarketing centres used in fraud), and others simply collect a portion of profits. The lucrative financial returns produced by frauds are likely used to fund other criminal activity, primarily drug importation and trafficking").

Commercial Trade Fraud

While commercial trade fraud is not specifically defined in the 2015 National Risk Assessment, I understand it to involve the intentional misrepresentation of information declared to customs services in order to evade import duties and tariff quotas or to conceal the movement of restricted goods.[16] Joel Gibbons, a senior analyst with the Canada Border Services Agency's Trade Fraud and Trade-Based Money Laundering Centre of Expertise, described commercial trade fraud as follows:

> What is trade fraud? It's the intentional misrepresentation of information that is declared to custom services like the CBSA and often the shipping and the sales documents that are related to those, the goods in question. Trade fraud has really been happening for as long as there have been customs authorities. It's a form of crime that enables a wide variety of criminal activity. In the more traditional customs context, trade fraud techniques are primarily used to evade paying import duties or to evade tariff quotas on certain goods. So it's really to evade controls that are established to ensure that the Government of Canada is collecting the appropriate amount of revenue for goods that are entering into the country. And when we talk about trade fraud techniques, what we're primarily talking about is misdescription. And we're talking about misdescribing a number of different elements on, again, primarily customs documents but also shipping documents as well. And some of the elements that we would be talking about include the price of goods or the value of goods, the description of the goods … the quantity of the goods, the weight of the goods, potentially even the quality of goods that are declared on customs documents.[17]

Some estimates suggest that, globally, less than 2 percent of shipping containers are physically examined and that criminals "routinely" take advantage of customs processes by intentionally misstating the value, quantity, quality, weights, and descriptions of commercial goods in order to evade duty and regulatory requirements and smuggle restricted goods into and out of the country.[18] Concerns have also been raised about organized crime groups "profiteering" from illegally smuggled goods.

The National Risk Assessment notes that the transnational organized crime groups, terrorist actors, and networks that operate in this sphere are "very sophisticated and capable, with the knowledge, expertise and international relationships to manipulate multiple trade chains and trade financing vehicles, often operating under the cover of front and/or legitimate companies."[19] It further notes that the sophistication and capability of these groups in conducting commercial fraud also extends to laundering its proceeds.[20]

16 Evidence of J. Gibbons, S. Sharma, and B. Gateley, Transcript, December 10, 2020, p 22.

17 Ibid, pp 22–23.

18 Exhibit 357, Canada Border Services Agency, *COVID-19 Implications for Trade Fraud* (April 2020), para 3.

19 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 20.

20 Ibid.

Corruption and Bribery

The National Risk Assessment states that corruption and bribery in Canada come in many different forms ranging from small-scale bribe-paying activity to large-scale bribery schemes aimed at illegally obtaining lucrative public contracts. It goes on to state that the money laundering threat from corruption and bribery was given a very high rating "principally due to the size of the public procurement sector and the opportunities that this presents to illegally obtain high-value contracts."[21]

The *Report of the Commission of Inquiry on the Awarding and Management of Public Contracts in the Construction Industry* (also known as the Charbonneau Commission Report, after the head of the inquiry, Madam Justice France Charbonneau) provides considerable insight into this type of criminality in the Quebec construction industry. The report outlines the various schemes used to manipulate the public procurement process as well as the extent to which organized crime groups have infiltrated the Quebec construction industry.

Of equal if not greater concern are corruption and bribery offences carried out by foreign officials and organized crime groups in other jurisdictions. While such conduct may be outside the reach of Canadian law, the proceeds of that unlawful activity often make their way to countries such as Canada, the United Kingdom, and the United States.

Counterfeiting and Piracy

The National Risk Assessment states that the number and selection of counterfeit and pirated products has grown significantly over the last decade, with Toronto, Montreal, and Vancouver being the key entry points for these products. It also states that organized crime groups appear to have tapped into global illicit distribution channels, allowing them to bring increasingly more counterfeit products into Canada and to launder the proceeds derived from the sale of counterfeit goods.[22] All indications suggest that the counterfeit and pirated goods market is substantial and continues to grow rapidly. As a result, authorities can expect an increase in money laundering activity associated with this type of criminality.

Illicit Drug Trafficking

The National Risk Assessment indicates that the illicit drug market is the largest criminal market in Canada, with cannabis, cocaine, amphetamine-type stimulants, and heroin making up a significant share of the market.[23] Since the release of that report, fentanyl and fentanyl-adulterated substances have taken over 90 percent of the opioid market in British Columbia and resulted in significant public harm, including the deaths of thousands of drug users. By 2016, fatal overdoses from fentanyl exposure

21 Ibid, p 21.

22 Ibid.

23 Ibid.

had increased to 8.4 per 100,000 in Canada, and more Canadians died from fentanyl-contaminated opioid use than were killed in motor vehicle accidents.[24] By 2018, the rate of fatal overdoses from opioid use reached 12 per 100,000 – approximately 85 percent of the province's fatal overdoses.[25]

A research report prepared for the Commission by Dr. Martin Bouchard (the Bouchard Report), a criminology professor at Simon Fraser University, sets out the reasons that fentanyl is attractive to those involved in drug trafficking:

> High mortality from fentanyl exposure stems from its potency – reported to be nearly 25 times more potent than heroin (Pardo et al., 2019). Fentanyl is cheaper than heroin too, which means its emergence has been motivated by traffickers' desire to cut costs and increase profits (Caulkins et al., 2021). Fentanyl's high potency means traffickers can make considerable profits by smuggling very small quantities (Caulkins et al., 2021). And its production chain is shorter compared to heroin, which reduces overall manufacturing costs. Fentanyl is manufactured from chemical precursors, so traffickers bypass the first part of the heroin distribution chain (i.e., farmers cultivating opium from poppy fields). Although bought and sold itself, fentanyl contaminates large quantities of heroin, opioids, and stimulants sold on the street (Bardwell, Boyd, Arredondo, et al., 2019).[26]

The Bouchard Report also estimates the size of the fentanyl market in British Columbia and concludes that retail sales of fentanyl – as well as fentanyl-contaminated opioids and stimulants – are in the range of $200–$300 million annually.[27] These numbers provide some insight into the size of the fentanyl drug market in British Columbia as well as the financial opportunities available to organized crime groups and other threat actors intent on making a profit from the sale of illicit drugs.

The Criminal Intelligence Service Canada (CISC) estimates that more than 90 percent of organized crime groups are involved in at least one illicit drug market and that these groups directly control or indirectly influence all aspects of the illicit drug market, including production, importation, and distribution.[28] While recognizing that many of these groups were involved in the cannabis market leading up to the

24 Exhibit 335, Research Report: Estimating the Size of the Fentanyl Market in British Columbia (October 26, 2020) [Bouchard Report], p 7.

25 Ibid.

26 Ibid. The full references in the quotation are as follows: B. Pardo, J. Taylor, J. Caulkins, et al, *The Future of Fentanyl and Other Synthetic Opioids* (Santa Monica, CA: RAND Corporation, 2019); J.P. Caulkins, A. Gould, B. Pardo, et al, "Opioids and the Criminal Justice System: New Challenges Posed by the Modern Opioid Epidemic" (2021) 4 *Annual Review of Criminology* pp 353–75; G. Bardwell, J. Boyd, J. Arredondo, et al, "Trusting the Source: The Potential Role of Drug Dealers in Reducing Drug-Related Harms via Drug Checking" (2019) 198 *Drug and Alcohol Dependence* pp 1–6.

27 Bouchard Report, p 47.

28 Exhibit 3, Overview Report: Documents Created by Canada, Appendix F, Criminal Intelligence Service Canada, *2018-19 National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Illegal Drugs* (Ottawa), pp 3, 5.

October 2018 enactment of the *Cannabis Act,* SC 2018, c 16, CISC's intelligence indicates that almost all these groups are involved in at least one other illicit drug market and will likely increase their involvement in those other markets to counteract the displacement of their share in cannabis. It also suggests that these groups will pursue other adaptive strategies, such as exporting cannabis to countries where it remains illegal, focusing on more potent cannabis products, targeting consumers who are unable or unwilling to purchase cannabis from legitimate suppliers, and exploiting regulatory differences.[29]

After reviewing this evidence, I am satisfied that illicit drug trafficking remains one of the most financially lucrative criminal markets for transnational organized crime groups (and other criminal actors) and is one of the most significant sources of illicit funds in this province.

Mass-Marketing Fraud

"Mass-marketing fraud" is an umbrella term for fraudulent schemes that use mass-communication media, including telephones, the internet, mail-outs, television, and radio, to defraud the victim.[30] Common forms of mass-marketing fraud include

- government services scams, where an individual or a group poses as a government representative in order to mislead victims into revealing sensitive financial or personal information, with the objective of stealing their money or identity;[31]
- phishing scams, where criminals contact victims from what appear to be reputable agencies in order to induce the disclosure of sensitive information;[32]
- romance scams, where victims are lured into a false relationship with a fraudster, often through the use of information that has been posted online;[33]
- ransomware scams, where criminal actors deploy malicious software to attack computer networks by encrypting files and holding data hostage until payment is made;[34] and

29 Ibid, p 3.

30 Exhibit 1017, Overview Report: Criminal Intelligence Service Canada National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud (2020), Appendix A, Criminal Intelligence Service Canada, *National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud 2020* (Ottawa: 2020), p 18.

31 Ibid. Although communication with victims often occurs through the use of telephone and email, offenders are increasingly using social media platforms and text messaging to carry out this form of unlawful activity.

32 Ibid, p 19. Common forms of phishing scams include email phishing, where offenders target a large, indiscriminate number of people by email; spear phishing, which involves a targeted attack directed at a single person; and whale phishing, which involves a targeted attack on specific high-ranking employees such as CEOs.

33 Ibid.

34 Ibid, p 20. The Criminal Intelligence Service Canada estimates that Canadian individuals and institutions, including businesses, universities, banks, hospitals, and government agencies, are targeted by ransomware attacks approximately 3,200 times per day. On average, such attacks are estimated to cost between $1 million and $3 million per incident.

- elder-targeted scams, where criminals use a variety of techniques, including government service scams, romance scams, bank and investment schemes, and prize offers, to defraud seniors.[35]

The National Risk Assessment states that the majority of mass-marketing fraud scams in Canada are carried out by organized crime groups, which use a variety of methods and techniques to launder the illicit funds they generate.

While reported losses averaged approximately $60 million annually from 2009 to 2013 and totalled $73 million in 2014, the National Risk Assessment states that "actual losses are viewed as being much higher, in the hundreds of millions of dollars annually, given that [mass-marketing fraud] is generally under-reported by victims."[36]

Mortgage Fraud

Mortgage fraud includes a wide range of deceptive practices relating to the provision of mortgage financing. At its simplest, it includes false and misleading statements made by a borrower on a mortgage application. However, a large number of sophisticated schemes are used to defraud lending institutions and property owners.

The National Risk Assessment states that organized crime groups conduct the "vast majority" of mortgage fraud activity in Canada and are believed to rely on the assistance of professionals such as real estate agents, mortgage brokers, appraisers, and lawyers. Some estimates suggest that the total amount lost to mortgage fraud annually is in the hundreds of millions and could be as high as $500 million.

Third-Party Money Laundering

The National Risk Assessment states that large-scale money laundering operations, including those connected to transnational organized crime groups, frequently involve third-party money launderers (defined as individuals or groups who were not involved in the predicate offence). Examples include professional money launderers, nominee owners,[37] and money mules.[38]

Professional money launderers specialize in laundering large sums of money and generally offer their services to criminals for a fee. They are often the masterminds behind sophisticated money laundering schemes and are frequently

35 Ibid.

36 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 22. It is also noteworthy that cryptocurrency is one of the most common methods of payment for mass-marketing fraud: Exhibit 1017, Overview Report: Criminal Intelligence Service Canada National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud (2020), p 16, and Evidence of R. Gilchrist, Transcript, June 9, 2020, p 62.

37 Nominee owners hold assets in their names on behalf of the true owner – the beneficial owner.

38 Money mules are individuals not involved in the predicate offence who are used to physically transport money, goods, or other merchandise. In some cases, they are willing participants in the money laundering scheme. In others, they are unaware that they are being used to facilitate criminal activity.

used by the most powerful organized crime groups to launder domestic- and foreign-generated proceeds. Nominees and money mules are less of a threat but are nonetheless important because they may be critical in carrying out money laundering schemes (large and small).[39]

A full discussion of third-party money laundering is contained in Chapter 3.

Tobacco Smuggling and Trafficking

The National Risk Assessment states that organized crime groups have a high level of involvement in the smuggling and trafficking of illicit tobacco products, such as counterfeit cigarettes and "fine cut" tobacco imported illegally by Canadian-based manufacturers. It also indicates that the organized crime groups involved in that trade have the sophistication and capability to launder the significant cash proceeds generated from the sale of those products.[40]

Currency Counterfeiting

Large-scale currency counterfeiting is predominantly undertaken by organized crime groups that conduct currency counterfeiting alongside other profit-oriented criminal activities.

The National Risk Assessment states that these actors exhibit a high level of sophistication and capability. They also appear to have the network and the infrastructure in place to successfully launder the cash proceeds arising from such activity.[41]

Human Smuggling

The National Risk Assessment indicates that "Canada is a target for increasingly sophisticated global human smuggling networks."[42] Such activity, it continues, is believed to be carried out by a small number of well-established organized crime groups that have developed the sophistication and capability to smuggle humans across multiple borders.

Human smuggling requires international connections along with a high degree of organization and planning. The organized crime groups engaged in this type of criminality are believed to engage in sophisticated money laundering activity.

39 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 22.

40 Ibid, p 23. For an analysis of the illicit financial flows from the tobacco trade, see Exhibit 4, Overview Report: Financial Action Task Force, Appendix SS, *FATF Report: Illicit Tobacco Trade* (Paris: FATF, 2012).

41 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 23.

42 Ibid.

Human Trafficking

Human trafficking for sexual exploitation is the most common form of human trafficking in Canada. There have also been cases of labour trafficking in the construction and housekeeping sectors. The National Risk Assessment indicates that sex trafficking is largely perpetrated by criminally inclined individuals who are not thought to have a high level of sophistication in terms of money laundering. Such individuals are believed to launder the proceeds of that activity for "immediate personal use, leveraging a very limited or non-existent network, and using a limited number of sectors and methods."[43] Organized crime groups are also involved in human trafficking and use their established infrastructure to launder the proceeds of that activity.[44]

Identity Crime

Identity crime – such as identity theft and identity fraud – is prevalent in Canada and is of particular concern because stolen identities are often used to support the conduct of other criminal activities. Stolen identities can also assist money laundering operations by giving offenders fake credentials to subvert customers' due diligence safeguards.[45]

The National Risk Assessment states that the organized crime groups conducting identity crime are "well-established and resilient, and have well-developed domestic and international networks."[46] I also heard evidence that a significant percentage of organized crime groups involved in this type of activity are located in British Columbia and that many of those groups have international connections.[47]

Illegal Gaming

Illegal gaming consists of a variety of activities, including private betting or gaming houses, unregulated video gaming and lottery machines, and unregulated online gambling. The National Risk Assessment identifies organized crime as the major provider of illegal gambling opportunities in Canada, though there are some smaller operations. The National Risk Assessment also notes that the illegal gambling market appears to be small in terms of the number of threat actors but is believed to be highly profitable for those involved.[48]

43 Ibid. For additional commentary on the illicit financial flows generated by human trafficking, see Exhibit 4, Overview Report: Financial Action Task Force, Appendix KK, *FATF Report: Financial Flows from Human Trafficking* (Paris: FATF, 2018).

44 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 23.

45 Ibid, p 24.

46 Ibid.

47 Exhibit 1017, Overview Report: Criminal Intelligence Service Canada National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud (2020), Appendix A, Criminal Intelligence Service Canada, *National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud 2020* (Ottawa: 2020), p 18.

48 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 24.

Organized crime groups involved in illegal gambling conduct these activities in a sophisticated manner. They are believed to have the capability to use a variety of sectors and methods to launder the proceeds of that activity.

Payment-Card Fraud

The National Risk Assessment notes that credit-card fraud increased significantly from 2010 to 2015, while debit-card fraud decreased over that period. Like many other profit-oriented criminal activities, organized crime groups are heavily involved in payment-card fraud, which includes card thefts, fraudulent applications, fake deposits, skimming, and card-not-present fraud.[49] These groups are sophisticated and have specialized technical knowledge that allows them to carry out this type of fraud. They also exhibit very high levels of sophistication and capability in laundering the proceeds of this activity.

A 2020 report from the Criminal Intelligence Service Canada indicates that financial institutions reimbursed approximately $862 million to Canadian credit-card customers in 2018. However, it is unclear how much of that total is attributable to organized criminal activity, as opposed to opportunistic use of credit cards by criminally inclined individuals.[50]

Pollution Crime

Pollution crime is generally understood as unlawful activity that directly harms the environment. Examples of such activity include the improper disposal of hazardous materials and the importation of counterfeit products that do not meet Canada's environmental standards (e.g., vehicle engines).[51]

The National Risk Assessment raises a particular concern about organized crime groups infiltrating the waste-management sector as a tool to generate illicit profits and launder proceeds from other types of profit-oriented criminal activity.[52]

Robbery and Theft

While small-scale thefts and robberies carried out by opportunistic criminals and petty thieves do not raise any significant money laundering concerns, it is important to recognize that organized crime groups are heavily involved in large-scale motor

49 The 2015 National Risk Assessment defines card-not-present fraud as "the unauthorized use of a credit (or debit) card number, the security code printed on the card (if required by the merchant) and the cardholder's address details to purchase products or services in a non–face-to-face setting (e.g., online, telephone)." It identifies card-not-present fraud as the most significant type of credit-card fraud in Canada, followed by credit-card counterfeiting.

50 Exhibit 1017, Overview Report: Criminal Intelligence Service of Canada National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud (2020), Appendix A, Criminal Intelligence Service Canada, *National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Money Laundering and Fraud 2020* (Ottawa: 2020), p 22.

51 Exhibit 3, Appendix B, 2015 National Risk Assessment, p 25.

52 Ibid, p 25.

vehicle, heavy equipment, and cargo theft. The most sophisticated and capable threat actors in this area have well-established auto theft networks that are used to supply foreign markets with stolen Canadian vehicles.

The National Risk Assessment indicates that these organized crime groups are believed to use a range of trade-based fraud and money laundering techniques to disguise the illicit origin of the automobiles and to move the illicit proceeds back into Canada.[53]

Firearms Smuggling and Trafficking

Firearms smuggling and trafficking has been assessed as having a medium money laundering risk in Canada. The National Risk Assessment states that very few organized crime groups are involved in the trafficking or smuggling of firearms in this country for the purpose of generating illicit profits. Instead, these groups use firearms to strengthen their position within other criminal markets (such as the illicit drugs market).[54]

Extortion

The National Risk Assessment indicates that organized crime groups often use extortion in furtherance of other crimes such as drug trafficking, illegal gaming, and human trafficking. For example, there is evidence of extortion being used as a tool to obtain money and property, control the distribution of illicit drugs, force the payment of illegal gambling debts, and gain access to ports of entries. It also states that the organized crime groups operating in this space vary in their level of sophistication and capability.[55]

Loan Sharking

The National Risk Assessment indicates that loan-sharking activity appears to be undertaken by a small number of sophisticated organized crime groups, as well as a small number of independent operators who have a relatively high level of sophistication and capability when it comes to laundering the illicit funds generated by this activity.[56]

Importantly, loan sharking has also been used as a way of laundering illicit funds generated by organized crime groups involved in other types of profit-oriented crime. These groups will provide the illicit cash generated by that activity to a loan shark, who will use it to make a loan to the borrower. In many cases, the loan will be secured through a lien registered against property. When the borrower repays the loan, the loan shark will receive "clean" funds in exchange for the illicit cash.

53 Ibid.

54 Ibid, p 25.

55 Ibid, p 26.

56 Ibid.

Tax Evasion

Tax evasion is carried out in many different forms in Canada. The ultimate objective of these schemes is to avoid the payment of taxes owing (or to unlawfully claim refunds or tax credits).

The National Risk Assessment indicates that tax evasion generally involves ordinary individuals using tax-evasion techniques of low sophistication. The ensuing money laundering activity is also believed to be relatively unsophisticated. However, it is important to note that some tax-evasion schemes – particularly those involving shell companies and offshore financial havens – can have a high level of sophistication and involve significant sums of money.[57]

Wildlife Crime

Although wildlife crime was assessed as having a low money laundering risk, an illicit market exists for certain types of Canadian species, including narwhal tusks, polar bear hides, peregrine falcon eggs, and wild ginseng. Black-market prices for these species are high and have risen significantly in recent years. The National Risk Assessment indicates that wildlife crime is largely conducted by opportunistic, criminally inclined individuals who, from a money laundering perspective, exhibit low levels of sophistication.[58]

The Three Phases of Money Laundering

Under the traditional conception of money laundering, there are three distinct phases in the money laundering process: (a) placement, where illicit funds are placed into the legitimate economy, usually by way of a deposit in a financial institution; (b) layering, where the criminal enterprise carries out various transactions to hide the true source and ownership of illegally acquired funds and obscure any paper trail that may lead back to the original offence; and (c) integration, where the illicit funds are fully integrated into the financial system and put back into the hands of the offender. Professor Schneider testified that these phases should be viewed more as individual functions within the money laundering process as opposed to a sequential series of steps undertaken every time someone seeks to launder illicit funds:

> I think the important point is not to necessarily look at this through a linear process, or even as phases, but [to] look at these as each individual function within the laundering process that satisfies the objective. Again, with the key objective of obviously getting the proceeds of crime back into the hands of the offender, repatriate it back to the offender.[59]

57 Ibid.

58 Ibid.

59 Transcript, May 25, 2020, pp 39–40. See also pp 40–41, 43 ("[T]here's a misconception that these phases operate in a sort of unilateral sequential manner, and they don't always do so, so in some cases I think they're better referred to as functioning phases").

At present, there is an active debate among experts and academics as to the descriptive accuracy and utility of the three-stage model. In what follows, I review the traditional three-stage model and then comment on some of its shortcomings.

Placement

Placement refers to the process by which illicit funds generated by other forms of criminality are introduced (or "placed") into the financial system. Professor Schneider describes placement as the most difficult stage for those involved in money laundering activity. He testified that most of the anti–money laundering regulations that have been put in place – such as the requirement that financial institutions report cash deposits exceeding $10,000 – revolve around the placement stage and that this stage is where offenders are most vulnerable.[60] He also observed that one of the reasons that commercial crime such as capital markets fraud and mass-marketing fraud is given such a high threat rating is that the illicit funds generated by that type of activity are *already* in the financial system:

> [O]bviously, the cash transaction reporting requirements of the legislation revolve around cash placement. So, in this case, what you have is many of these [commercial] offences don't produce cash, they produce – if it's mass marketing fraud, you're basically asking your victim to send in a cheque or to wire transfer or to do an account transfer or an Interac transfer. And so that's why [commercial offences] are rated such a high threat, because the proceeds of crime are in a non-cash form, and in some cases they're in an electronic form.
>
> ...
>
> And that makes it ... easier to integrate the proceeds of crime and launder it, and it makes it more difficult to detect the proceeds of crime ... [I]f you don't have the cash to start with, that makes the laundering just so much easier and more efficient.[61]

One of the most common placement techniques is for the offender to deposit the cash at a financial institution. In order to avoid the mandatory reporting requirement for cash deposits in excess of $10,000, offenders will often make a series of smaller deposits under the $10,000 threshold (a technique known as "structuring") or engage a number of other individuals to make cash deposits on their behalf (a technique known as "smurfing").[62]

Establishing a commercial bank account and depositing the criminal proceeds in the name of the company is another placement technique that allows the offender

60 Transcript, May 25, 2020, p 49. Canadian anti–money laundering regulations, such as the requirement that financial institutions report cash deposits exceeding $10,000, are reviewed in detail in Chapter 7.

61 Ibid. See also pp 50–51.

62 The term "smurf" is derived from popular culture and connotes the image of a large group of small, blue, humanoid creatures working together to achieve a larger goal.

to legitimize (or "justify") the illicit funds by claiming the proceeds of crime as legitimate revenue earned by the business.[63] In some cases, the illicit funds are commingled with legitimate revenue (such as revenue from restaurants, bars, supermarkets, and/or gas stations).[64] In other cases, the funds are solely the product of criminal activity.

Outside of financial institutions, a variety of techniques are used by offenders to introduce cash proceeds into the legitimate financial system. These techniques include the purchase of real estate and luxury goods with the cash proceeds of criminal activity, and the use of money services businesses to convert cash proceeds to larger denominations (or other currencies) and send those proceeds to other individuals. Without proper safeguards, casinos can also be used as a portal to introduce illicit proceeds into the financial system through the purchase of casino chips.

While federal legislation requires certain transactions to be reported to the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), there are a variety of ways to circumvent those reporting requirements. Moreover, some sectors, such as the luxury vehicle sector, have no reporting obligations, and offenders can make large cash purchases with very little scrutiny. The vehicles can then be sold or exported to other countries, allowing the purchaser to realize a significant profit.

I provide a more detailed description of these techniques – along with some specific case studies – in subsequent chapters of this Report.

Layering

Once illicit funds are placed in the legitimate financial system, the offender will often carry out various transactions to hide the true source and ownership of the illicit funds and obscure any paper trail that may lead back to the original offence. Professor Schneider describes this phase of the money laundering process as an attempt to "distance" the illicit proceeds from their criminal source.[65] While there are many ways to achieve that objective, the most common involve nominee ownership, shell companies, and the use of offshore financial havens.[66]

Nominee Ownership

Nominee ownership refers to the practice of putting an asset – whether it is land, a luxury vehicle, or even a bank account – in the name of someone else (sometimes

63 Evidence of S. Schneider, Transcript, May 25, 2020, p 84.

64 Exhibit 6, S. Schneider, *Money Laundering in British Columbia: A Review of the Literature,* pp 92–94. Professor Schneider states that these types of businesses are particularly attractive to money launderers because they process a high volume of cash transactions.

65 Exhibit 6, S. Schneider, *Money Laundering in British Columbia: A Review of the Literature,* p 39. See also Evidence of S. Schneider, Transcript, May 25, 2020, p 37.

66 Exhibit 6, S. Schneider, *Money Laundering in British Columbia: A Review of the Literature,* p 39. Of course, there are many other methods of achieving this objective.

referred to as the "nominee") to hold on behalf of the true owner (sometimes referred to as the "beneficial" owner).[67] The nominee is often a family member or a friend with no criminal record, making it difficult for law enforcement to trace the asset back to any criminal activity.[68]

While legal professionals use nominee ownership for a number of legitimate and important purposes, it is also a very effective way to put distance between the offender and the proceeds generated by criminal activity.

Shell Companies

Shell companies are at the centre of most sophisticated money laundering operations and provide virtually unlimited opportunities for offenders to launder illicit funds. While there is no legal definition of a shell company, they are generally understood to be companies that exist only on paper and do not have active operations. There are legitimate ways that shell companies are used. However, they are also employed for illegitimate purposes such as money laundering or fraud.

In some cases, shell companies are incorporated and registered by the offenders themselves. In other cases, they are purchased from a company formation agent complete with a corporate bank account. These companies are sometimes referred to as shelf companies because they are purchased "off the shelf" from another party.[69]

Ownership of these companies is often obscured through the use of nominee directors and shareholders, making it difficult, if not impossible, for authorities to determine who owns and controls them. Moreover, it is common for offenders to create (or purchase) multiple shell companies in various jurisdictions and have them loan or otherwise transfer money to one another in order to further obscure the true ownership and origins of illicit funds.[70]

Jason Sharman, a professor of international relations at King's College, Cambridge, explains the vulnerability associated with shell companies in the following terms:

> Shell companies create vulnerability because … an expendable legal person can set up in dozens of jurisdictions online very quickly for perhaps a few hundred dollars and, as a legal person … it can be the owner of the property, it can hold a bank account, and it can act as the screen or a veil to separate and conceal the underlying real owner, the beneficial owner.

67 In legal terms, legal title to the asset is registered in the name of the nominee and held in trust for the beneficial owner of the asset.

68 Exhibit 6, S. Schneider, *Money Laundering in British Columbia: A Review of the Literature*, p 40.

69 Evidence of S. Lord, Transcript, May 28, 2020, p 33.

70 Evidence of S. Schneider, Transcript, May 25, 2020, pp 73–74.

> Again, this means that suspicious transactions are less likely to be flagged as such and secondly, it means that investigations can stop dead. If you find out that company A, B, C is involved and then you can't find who actually owns company A, B, C, then that's that in terms of the investigation most often.[71]

While these companies are often incorporated in offshore jurisdictions such as the Cayman Islands, it is important to note that these countries are merely "transit" points for the illicit funds. What is really happening is that the money is moving from China to Vancouver or from Russia to London or from Equatorial Guinea to Paris with a complex series of transactions in the middle.[72] It is also important to note that Western countries such as Canada, New Zealand, and the United States can provide similar functions to the classic offshore financial centres.[73]

Offshore Financial Havens

Offshore financial havens such as the Cayman Islands, Panama, and St. Kitts provide fertile ground for money laundering. Such countries are attractive because of their strict secrecy laws, relaxed money laundering regulations, and the array of facilities and services offered to foreign investors reluctant to disclose their identity. Once illicit funds are transferred to a shell company in one of these jurisdictions, or cash is smuggled into one of these jurisdictions and deposited in a numbered account, it is infinitely more difficult to trace the criminal funds back to the offender.

Oliver Bullough, an investigative journalist and the author of *Moneyland: The Inside Story of the Crooks and Kleptocrats Who Rule the World*,[74] coined the term "Moneyland" to refer to the labyrinth of countries, companies, and transfer mechanisms used to obscure the ownership and origins of illicit funds. His point, as I understand it, is that these transfer mechanisms are constructs created by legal professionals to hide the movement of money so that it no longer resides in any geographic location that we would recognize as a country:

> If you put your money in Moneyland, it drops off the map. It no longer is registered as existing anywhere that we would recognize as a country. So you have this hole in the global balance sheet … The assets and liabilities of the world don't match. It's as if Mars was a major investor in the world, which obviously it isn't … [I]n order to make the list of countries add up so that the assets and liabilities add up, I decided to add another country to the list, and that's the country I called Moneyland.[75]

71 Transcript, May 6, 2021, p 30.

72 Evidence of O. Bullough, Transcript, June 1, 2020, p 33.

73 Exhibit 959, Jason Sharman, Report to the Cullen Commission, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, pp 14–18.

74 New York: St. Martin's Press, 2019.

75 Transcript, June 1, 2020, p 20.

Mr. Bullough also described the manner in which offenders, with the help of their legal and professional advisors, can bounce the money through six or seven jurisdictions in one afternoon, making it "astonishingly difficult" to find.[76] He states:

> If you … bounce the money through multiple bank accounts in multiple jurisdictions, each of them owned by a different corporate structure or registered again in different jurisdictions … you confuse the picture so hugely that it becomes very, very hard to follow what's going on, particularly if you don't move the money around in a lump sum that's always the same size. You know, if you have a lawyer's escrow account and you send the money in in a million dollars, and then bring it out in 33 packages of $33,000, then it becomes much harder to trace what's really going on.[77]

I return to the manner in which illicit funds are transferred between different companies and corporate structures in subsequent chapters of this Report.

Integration

While commonly described as the third "phase" of the money laundering process, the integration of the illicit funds into the legitimate economy is better viewed as the end goal rather than a distinct stage in that process. Moreover, it is important to reiterate that one of the goals of money laundering is to create a veneer of legitimacy and that many of the transactions carried out as part of the money laundering process are undertaken with that in mind. Examples include

- depositing cash into a bank account under the guise of revenue from a legitimate business;
- making a cash deposit to "hold" a luxury vehicle, with the funds being returned, by cheque, when the prospective purchaser changes his or her mind;
- loan-back schemes, where nominees or shell companies "loan" illicit funds back to the offender under the guise of a loan agreement; and
- selling property financed with the proceeds of crime to a legitimate buyer pursuant to a contract of purchase and sale.

It is also important to recognize that the illicit funds are not always returned to the jurisdiction where the predicate offence occurred. For example,

- illicit funds generated from criminal activity in British Columbia can be smuggled to countries such as Mexico, where high-ranking cartel members reside;
- illicit funds generated from criminal activity in British Columbia can be used to purchase illicit products, such as drug precursors, in other countries;

76 Ibid, pp 9, 10.

77 Ibid, p 56.

- illicit funds generated from criminal activity in foreign countries can "transit" through British Columbia;[78]
- illicit funds generated from criminal activity in other countries can pass through the bank account of a shell company based in British Columbia (or whose directors and/or shareholders are based in British Columbia);[79] and
- illicit funds generated from criminal activity in other countries can make their way to British Columbia and be used to purchase property and other assets.[80]

These possibilities illustrate the complexity of the problem and highlight the need for a co-operative approach among provincial, federal, and international agencies.

Criticisms of the Three-Stage Model

While the three-stage model (placement, layering, and integration) continues to be cited in academic literature and training materials, it was developed more than 30 years ago, when anti–money laundering efforts were focused on the *cash* proceeds of drug trafficking activity and may no longer be a useful or informative way of thinking about money laundering.

Simon Lord, one of the world's leading experts on money laundering, testified that the three-stage model has become "truth by repetition," but it is not the typical money laundering structure.[81] He explained that the methods employed by offenders may change from week to week depending on what they want to achieve:

> [T]he view I take – and this is what I always say when I'm beginning a lecture on money laundering – is essentially you have to look at the criminal decision-making process. So the first element of that would be the criminal makes money from organized crime in some way – so he might sell a kilo of cocaine or heroin or sell some illicit cigarettes or commit a robbery or something like that. So once he's actually got the money, the second thing he's going to say to himself is: What do I want or what do I need to do with this money now I've made it? The third process is: Where do I need it to be in order to achieve that, and in what form? And the fourth point is: How am I going to get it there? And that is actually what [indiscernible] how money laundering works. You have to consider the criminal has got the money and wants to do something with it. And that is how … they're going to think. And the important thing

78 For some of the reasons that Canada is attractive as a "transit" country for money laundering, see Evidence of S. Schneider, Transcript, May 25, 2020, p 54.

79 See Evidence of J. Sharman, Transcript, May 6, 2021, pp 94–95, and Exhibit 959, J. Sharman, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, p 18.

80 See, for example, Exhibit 6, S. Schneider, *Money Laundering in British Columbia: A Review of the Literature*, p 23.

81 Transcript, May 28, 2020, p 10.

> that follows on from that is that … the funds arising from [different types of criminality] are not always going to be laundered in the same way. So as an example, you could be in the situation where a criminal sells a kilo of cocaine this week, and because he's bought it on credit he needs to pay his supplier. Now, in the UK, there's a good chance his supplier might be in somewhere like the Netherlands or overseas. In which case the criminal would probably want the money in euros, because that's the currency of the country where it needs to go, and so he might need – and he might elect to do something like hide it in the car and drive it out of the UK to the Continent.
>
> The following week, he might sell another kilo of cocaine. He's paid off his supplier, and so this time he decides he wants to buy a car with it. So somehow he's got to get that money into the financial system in such a way as to make the person who's selling him the car believe that it's legitimate. *And so the predicate offence is the same two weeks running but the money has been laundered in two totally different ways. And I think it's really important to understand that because I think there is a general perception amongst some areas of society that drug trafficking – money laundering always happens in this particular way … whereas in fact it's entirely down to what the criminal wants to do with it.* [Emphasis added.][82]

Likewise, Professor Michael Levi, an expert in money laundering and transnational crime, argues that the three-stage model may have been appropriate at the early stages of the anti–money laundering movement, but must be reconfigured to account for the diversity of sources, transfer mechanisms, and destinations of proceeds of crime. He writes:

> The placement / layering / integration model was developed at a time (1988–89) when drugs trafficking was the principal predicate offence in law and in practice, following the Vienna Convention and the creation of [the Financial Action Task Force]. Indeed, my discussions with those present at the Sommet de l'Arche make it clear that the model was firmly urged on the nascent FATF at its travaux préparatoires. In that era and place, models of Italian-American and rival syndicated crime groups were prominent, and it was generally accepted that this avenue from organised crime to social and political respectability constituted what the sociologist Daniel Bell (1953) termed "the queer ladder of social mobility." So the focus of the typology was appropriate at the time. However we are now almost a quarter of a century on, and reconfiguring the process is also appropriate, in the light of our more developed understanding and the arrival of new technologies. Whether this means substituting it for one other "one size fits all" typology is more questionable, however. Rather

82 Ibid, pp 11–13.

> we need to stop using the placement-layering-integration process as a comfort blanket and think about the diversity of sources, transfer mechanisms and destinations of proceeds of crime (and, in the case of terrorism and WMD [weapons of mass destruction], preceeds [preceding events] of crime).[83]

While the debate about the descriptive accuracy of the three-stage model may seem academic, the use of a flawed model can have significant implications for the ability of law enforcement, regulators, and other stakeholders to recognize and identify money laundering activity. In *Money Laundering: A Concise Guide for All Business,* Doug Hopton describes the implications of using a flawed model as follows:

> [The] three-stage model, while a convenient way of describing the activity, is a little simplistic and does not fully reflect what really happens. It relates back to the common historical definition of money laundering discussed earlier. While they are examples of money laundering, they do not define what money laundering actually is. This has led to those with the duty of recognising money laundering having insufficient knowledge to be able to identify it in all its guises. *Too often we have looked at money laundering from the aspect of what we expect it to look like, rather than by reference to what it actually is. Numerous cases have come to light where employees have failed to identify relationships in which property has been laundered, simply because what happened did not match with what they had been taught to expect such activity to look like. So while the traditional model is useful, it does not adequately cover all situations in which money laundering occurs.* [Emphasis added.][84]

I agree with these commentators that the time has come to move away from the three-stage model. While useful in the early stages of the anti–money laundering movement, the three-stage model provides little insight into the methods actually used by offenders to launder illicit funds and has arguably stood in the way of developing better ways of responding to the money laundering threat.[85] For example, the three-stage model fails to fully account for money laundering techniques such as informal value transfer and trade-based money laundering, which many experts view as the largest and most pervasive methodologies in the world (see below).[86]

It is also a poor fit for economic crimes – such as capital markets fraud – where the illicit proceeds are transferred electronically and do not need to be "placed" into the financial system. Indeed, it is common for fraudsters who have received electronic funds transfers from their victims to make cash withdrawals in order to break the audit trail.

83 Exhibit 23, M. Levi, Money-Laundering Typologies: A Review of their Fitness for Purpose, pp 34–35.

84 Ibid, pp 11–12, citing D. Hopton, *Money Laundering: A Concise Guide for All Business*, 2nd ed (Aldershot, UK: Gower, 2009), pp 2–3. See also Evidence of M. Levi, Transcript, June 5, 2020, pp 27, 28.

85 Exhibit 23, M. Levi, Money-Laundering Typologies: A Review of their Fitness for Purpose, p 14.

86 See Evidence of S. Schneider, Transcript, May 25, 2020, p 42; Evidence of J. Cassara, Transcript, December 9, 2020, pp 43–47; and Exhibit 341, Statement to the Cullen Commission of Inquiry into Money Laundering in British Columbia by John A. Cassara, p 18.

Another way of conceptualizing the money laundering process is to think of it as a chain of transactions (and other forms of money movement) which aim to move the funds acquired through profit-oriented crime to a setting in which criminals can use it freely.

In an expert report prepared for the Commission by Christian Leuprecht, Jeff Simser, Arthur Cockfield, and Garry Clement (the Leuprecht Report), the authors describe the money laundering process as follows:

> Money laundering requires moving value acquired as the result of a crime (the "predicate offence") to a setting in which the criminals can use it freely; in other words, money laundering tries to break the connection between the crime and the use of the value it produced. Using a chain (or better still a network) of movements makes it more difficult to find and demonstrate the connection. There is a fundamental asymmetry between criminals and law enforcement because adding more complexity to the chain is relatively easy for criminals but disproportionately increases the effort to follow the chain for law enforcement. Each link in the chain is detectable in principle because the movement of value creates data that can be captured and analysed using data-analytic techniques. However, there are several kinds of links that do not leave a trace, and so break the chain required to prosecute the offence of money laundering.[87]

While these movements can include the physical movement of cash or the transfer of illicit funds through the financial system, offenders can use a wide range of other methods to break the connection between the predicate offence and the illicit funds it produces.

In subsequent chapters of this Report, I move away from the three-stage model and undertake a more detailed examination of the mechanisms used to launder illicit funds. I also make a number of recommendations aimed at giving law enforcement agencies, regulators, and the private sector the information they need to recognize money laundering activity in all its various forms.

The Underground Economy

While a significant portion of this Report is devoted to the six economic sectors identified in my Terms of Reference, it is important to recognize that a great deal of money laundering activity occurs in the informal or "underground" economy. What distinguishes this form of money laundering is that much of it occurs outside the regulated financial system and may not be caught by the countermeasures put in place by countries that have adopted the Financial Action Task Force model (such as the

87 Exhibit 828, Collaborative Report, *Detect, Disrupt and Deter: Domestic and Global Financial Crime – A Road-map for British Columbia* (March 2021), p 6.

requirement that private-sector entities report suspicious transactions to a central financial intelligence unit).[88]

John Cassara, a former US law enforcement official and an expert on trade-based money laundering, testified that these forms of money laundering are still not recognized as significant threats even though they are among the largest and most pervasive methodologies in the world.[89]

In what follows, I provide an overview of three such techniques: bulk cash smuggling, informal value transfer, and trade-based money laundering.

Bulk Cash Smuggling

Bulk cash smuggling is one of the oldest and most basic forms of money laundering. However, it remains a significant problem. Some estimates suggest that the total amount of illicit cash smuggled across international borders each year could be in the order of hundreds of billions of dollars.[90] Professor Schneider testified that bulk cash smuggling is favoured by many organized crime groups that use shipping containers, human "mules," and a variety of other methods to smuggle cash across international borders. Once the funds have been moved, they can be used for various purposes, including the payment of employees and suppliers, the purchase of weapons, and the payment of protection money and bribes. The movement of funds across international borders allows the offender to distance illicit funds from the predicate offence and break the audit trail, making it extraordinarily difficult for law enforcement to investigate and prosecute money laundering offences:

> One of the primary drivers for laundering money derived from criminal activity is to conceal its illegitimate origins, and one of the simplest methods of doing this is to remove it from the jurisdiction in which the predicate offence was committed …
>
> The movement of funds in the form of cash from one country to another fulfils numerous requirements for a criminal. Primarily, it makes

88 Note, however, that it is something of a misnomer to say that these activities take place in the "underground" economy. In many cases, they occur in plain sight. Moreover, it cannot be said that such activity occurs outside the regulated financial system entirely. At some point, the illicit cash generated by profit-oriented criminal activity will re-enter the legitimate economy. However, that may occur in another jurisdiction or by co-opting individuals with no connection to the underlying criminal activity.

89 Transcript, December 9, 2020, pp 43–47. See also Evidence of J. Sharman, May 6, 2021, p 24; and Exhibit 1020, Overview Report: Information Relating to the FATF & Egmont Group Trade-Based Money Laundering Report, Appendix A, FATF & Egmont Group *Report on Trade-Based Money Laundering: Trends and Developments* (December 2020), p 4. For a contrary view, see Evidence of R. Wainwright, Transcript, June 15, 2020, p 21 ("[T]he regulated financial sector remains the primary means by which criminal funds are laundered").

90 Exhibit 4, Overview Report: Financial Action Task Force, Appendix LL, *FATF Report: Money Laundering Through the Physical Transportation of Cash* (Paris: FATF, 2015), p 3. For the proposition that bulk cash smuggling remains a serious problem, see also Evidence of J. Sharman, Transcript, May 6, 2021, pp 15–16 ("[C]ash is probably still one of the most important mechanisms for laundering the proceeds of crime").

> the tracing of the proceeds of a crime very difficult for the authorities. Police investigating a crime may never be able to identify the money generated from it if they have been unable to identify any evidence leading them to believe that the cash has been smuggled out of their jurisdiction. Even if the cash is detected in the destination country at some stage of the process, the legal and practical implications of information and intelligence exchange and evidence gathering between the countries of origin and destination can frustrate law enforcement efforts to prosecute offenders and seize the cash.[91]

Offenders can also move illicit funds to jurisdictions with less diligent regulatory oversight, making it easier for the offender to place those funds into the legitimate financial system for use at a later date. I return to this topic in Chapter 36.

Informal Value Transfer Systems

Informal value transfer systems (sometimes referred to as "underground banks") are another mechanism used by offenders to launder illicit funds.[92] In basic terms, these systems allow people to move value from one location to another without transferring funds through the regulated financial system. While each system is slightly different, the operators of these systems typically have "pools" of cash available to them in different locations, usually in different countries. When clients need to transfer funds from one location to another, the money will be paid into the cash pool in the first location and paid out of the cash pool in the jurisdiction where they need the money. The money paid into the first pool will be held in that location until another client needs to transfer funds into that jurisdiction. Over time, the operator may need to reconcile the cash pools to keep them in balance. However, there is no transfer of funds on an individual basis.

Mr. Lord described the operation of informal value transfer systems as follows:

> Essentially, it's money transmission at its most basic. Quite a lot of the time these types of systems are tied to specific geographic regions, ethnic communities and what have you, and essentially what they do is they arrange for transfer and receipt of funds or equivalent value without the physical need to transfer the funds themselves. So you're transferring value but not necessarily the funds. So there won't be a straight line remittance from point A to point B through the banking system … [S]omeone will make a deposit of funds in one location and will receive an equivalent value in another location, less fees and commission, but

91 Exhibit 4, Overview Report: Financial Action Task Force, Appendix LL, *FATF Report: Money Laundering Through the Physical Transportation of Cash* (Paris: FATF, 2015), p 37.

92 Note, however, that these systems are also used for legitimate purposes in countries where the financial system has collapsed or is otherwise unreliable: see Evidence of S. Lord, Transcript, May 28, 2020, pp 56, 57, 58. See also Evidence of J. Sharman, Transcript, May 6, 2021, pp 21–23.

> without there actually being a physical connection between the two. And they generally involve a process which I generally refer to as cash pooling. So the people who are involved in these types of networks have available to them pools of funds in different locations, not always cash. Sometimes it's money in bank accounts, sometimes it's trade. But pools of funds in different locations, and you receive the payment into one of those pools and make a payment out of another one. And then over time there will be a settlement arrangement between the pools to keep them in balance. Because, obviously, if all the money went one way, you would end up with lots of money in one place and not in another, and you would have to have some sort of settlement mechanism in place. So settlement can take place through trade, through cash, through net settlements over a long period of time, quite often through the banking system. They're often informal in so far as this type of stuff often happens outside of the formal financial system, but by no means all the time. They often interact with financial systems as well.[93]

Over the past 10 to 15 years, informal value transfer has been used to launder substantial sums of money through the British Columbia economy using a money laundering technique known as the Vancouver model. Under that model, organized crime groups operating in the province deposit the cash proceeds of their illegal activity with the operator of an informal value transfer system in the Lower Mainland and receive an equivalent value (less the commission earned by the operator) in countries such as Mexico and Colombia. The cash received by the operator is then repurposed and provided to wealthy Chinese nationals who are unable to move their wealth to British Columbia because of the currency restrictions imposed by the Chinese government. Those individuals make payments to the operator of the informal value transfer system in China and receive the equivalent value in cash when they arrive in British Columbia.

While a significant portion of that cash was used to make large cash buy-ins at Lower Mainland casinos, it is important to note that the cash can be used for any legitimate or illegitimate purpose, including the purchase of real estate and luxury goods. It is also important to note that the individuals seeking to move their wealth from China to British Columbia are not necessarily involved in criminal activity and may well have acquired that wealth through legitimate means. The problem, however, is that most, if not all, of the actual cash provided to those individuals in British Columbia is derived from profit-oriented criminal activity and is being paid out by the operator of the informal value transfer system in furtherance of a money laundering scheme. I return to informal value transfer systems in Chapter 37.

93 Transcript, May 28, 2020, pp 57–58.

Trade-Based Money Laundering

Trade-based money laundering is a related form of money laundering that involves the use of trade transactions to avoid the scrutiny of more direct forms of transfer and to move illicit funds (or more accurately, value) from one location to another. It can also help to legitimize illicit funds by making them appear to be generated through a legitimate commercial transaction.

Invoice fraud is one of the primary techniques used by offenders to transfer illicit funds from one jurisdiction to another. Under this form of value transfer, a company in one country will ship goods to another country at significantly overvalued or undervalued prices. For example, an importer in British Columbia could transfer money overseas by overpaying for goods (real or fictitious) that it has "imported" from another country. The shipment of goods and the accompanying documentation provide cover for the transfer of money.

Other techniques used to transfer value between jurisdictions include multiple invoicing, falsely describing goods and services, short-shipping, and phantom shipping.

While there is general agreement that trade-based money laundering is a significant threat and one of the largest and most pervasive methodologies in the world, it is not well understood and has not – to date – been the subject of any meaningful enforcement action in Canada and many other countries. I return to this topic in Chapter 38.

Chapter 3
Who Is Involved in Money Laundering?

In order to understand the nature and prevalence of money laundering activity in the province, it is useful to examine the individuals and groups typically involved in such activity. A 2015 risk assessment conducted by the federal Department of Finance (the National Risk Assessment) describes these groups as ranging from unsophisticated, criminally inclined individuals to criminalized professionals and transnational organized crime groups.[1] It also raises the spectre of professional money laundering organizations and networks that offer money laundering services to individuals and groups involved in profit-oriented crime.[2]

Each of these groups presents a different money laundering threat and poses different challenges for regulators and law enforcement agencies.

Transnational Organized Crime

Transnational organized crime has been described as one of the pre-eminent criminal threats to Canada and its global partners.[3] It is also a significant money laundering threat because of the volume of illicit proceeds generated by these groups and the "intensity" of their money laundering efforts, which almost always involve the use of professional money laundering networks to move illicit funds to various locations around the globe.

1 Exhibit 3, Overview Report: Documents Created by Canada, Appendix B, Canada, Department of Finance, *Assessment of Inherent Risks of Money Laundering and Terrorist Financing in Canada, 2015* (Ottawa: 2015) [National Risk Assessment], p 18.

2 Ibid.

3 Exhibit 757, Transnational Organized Crime in "E" Division: RCMP, "E" Division Federal Serious and Organized Crime, Major Projects [Transnational Organized Crime], p 2.

While there is no single definition of transnational organized crime, it is generally understood to include associations of criminally minded individuals who conduct illegal activity in multiple jurisdictions. Such groups often have economic gain as their primary goal and frequently protect their illegal activities through a pattern of violence and corruption.[4] They may also seek to exploit differences between countries to further their objectives and insulate their leadership and membership from detection, sanction, and/or prosecution.[5]

British Columbia has long been viewed as one of four key organized crime hubs in Canada (with the others being Ontario, Quebec, and Alberta).[6] It is attractive to organized crime because of its proximity to smuggling routes from Mexico to Los Angeles, its international flights and marine ports, and its orientation toward the burgeoning markets of Asia.[7] It also has a "vibrant" drug production industry that includes both the marijuana industry and the production of synthetic drugs such as methamphetamine.[8]

Calvin Chrustie, a former RCMP officer with significant experience in the investigation of transnational organized crime, testified that he has witnessed the convergence of three main organized crime groups in British Columbia over the past decade:

- Mexican and Colombian cartel networks;
- Middle Eastern organized crime networks; and
- Asian organized crime networks.[9]

Mexican cartels have been assessed as a high-level threat in British Columbia and are heavily involved in the movement of South American cocaine through the Mexico / Central American corridor to consumer countries such as Canada and the United States.[10] They are also increasingly involved in the movement of methamphetamine and fentanyl precursors into British Columbia. In *Hunting El Chapo, The Inside Story of*

4 Ibid, p 12. See also *Criminal Code*, s 467.1, and Evidence of S. Sharma, Transcript, December 10, 2020, p 61.

5 Exhibit 757, Transnational Organized Crime, p 12. See also Evidence of R. Gilchrist, Transcript, June 9, 2020, pp 44-45.

6 Evidence of R. Gilchrist, Transcript, June 9, 2020, p 44.

7 Peter German, *Dirty Money: An Independent Review of Money Laundering in Lower Mainland Casinos Conducted for the Attorney General of British Columbia*, March 31, 2018 [*Dirty Money 1*], para 119. See also Evidence of R. Gilchrist, Transcript, June 9, 2020, p 43, and Evidence of S. Schneider, Transcript, May 25, 2020, pp 53–54, and May 26, 2020, p 44.

8 See Evidence of S. Schneider, Transcript, May 25, 2020, p 53, and May 26, 2020, p 44. See also Evidence of R. Gilchrist, Transcript June 9, 2020, pp 70–71, and Exhibit 3, Overview Report: Documents Created by Canada, Appendix F, Criminal Intelligence Service Canada, *2018–2019 National Criminal Intelligence Estimate on the Canadian Criminal Marketplace: Illegal Drugs* (Ottawa), pp 7–8 ("[t]he majority of methamphetamine consumed in Canada will continue to be produced domestically in illegal-clandestine laboratories. In 2018, 23 assessed [organized crime groups] are involved in methamphetamine production, with the majority of groups based in British Columbia and Ontario").

9 Evidence of C. Chrustie, Transcript, March 29, 2021, pp 12–13. See also Evidence of B. Baxter, Transcript, April 8, 2021, pp 77–78, where he discusses Asian organized crime groups acting as a "depository" for other organized crime groups and assisting them to launder illicit funds.

10 Exhibit 757, Transnational Organized Crime, p 3. While Canada is viewed as a consumer country for most illicit drugs, it has also emerged as one of the top "transit" countries for the movement of cocaine to places such as Australia and New Zealand.

the American Lawman Who Captured the World's Most-Wanted Drug Lord, Andrew Hogan, an investigator with the US Drug Enforcement Administration (DEA), wrote that he was "caught off guard" by the Sinaloa Cartel's deep infiltration of Canada.[11]

Mr. Hogan goes on to describe the extent to which Mexican cartels co-operate with other organized crime groups, including outlaw biker gangs, to move cocaine into Canada:

> Chapo's men had connections with sophisticated Iranian organized-crime gangs in Canada who were facilitating plane purchases, attempting to smuggle ton-quantity loads using GPS-guided parachutes, while sending boxes of PGP-encrypted smartphones south to Mexico at Chapo's request. A network of outlaw bikers – primarily Hells Angels – were also moving his cocaine overland and selling it to retail dealers throughout the country.[12]

Asian and Middle Eastern groups have also been assessed as a high-level threat, in part because of their skill in moving large sums of money around the world. Money service businesses associated with Middle Eastern organized crime groups have long been involved in the movement of illicit funds through the Lower Mainland. However, there is increasing concern within law enforcement about the volume of illicit funds being laundered by individuals associated with Asian organized crime groups.

Mr. Chrustie described a meeting with Colombian and American authorities where he learned about the "extreme volumes of money that were being moved around the world related to a phone number with [a British Columbia prefix]."[13] He also spoke about the increased levels of co-operation between transnational organized crime groups in recent years, particularly as it relates to money laundering:

> [O]ften … we look at these crime groups in terms of limited or linear type of interactivity amongst them, but what we saw of interest was that certain crime groups had unique relationships that appeared to be significant based on the timing of the meetings, the level of the meetings and the sensitivity of the meetings.
>
> So, for instance, when top Sinaloa Cartel members arrived in Canada or arrived in Vancouver, say, theoretically at 10 o'clock at night, at 11 o'clock at night showing up at the residence would be Iranian networks … [W]e saw that quite a bit.
>
> And then we also saw periodically the convergence with the Chinese networks, say, for example, dropped calls and then when we looked at

11 Andrew Hogan and Douglas Century, *Hunting El Chapo* (New York: HarperCollins, 2018), p 110.

12 Ibid, p 111.

13 Evidence of C. Chrustie, Transcript, March 29, 2021, p 17. See also Exhibit 757, Transnational Organized Crime, pp 3–4, and John Langdale, "Chinese Money Laundering in North America" (2021) 6(1) *European Review of Organized Crime*, pp 10–35. For some of the challenges faced by law enforcement entities in responding to the threat posed by transnational organized crime, see Evidence of R. Wainwright, Transcript, June 15, 2020, pp 24–27.

> dropped calls on digital number recorders we would see that some of the dropped calls came from somebody that was formally known to be affiliated closely with a Hezbollah-related network, i.e., Iranian proxy network. We would see some triad networks receiving security from Iranian networks.
>
> So we saw the convergence. We weren't too sure if this was by coincidence, so we worked with our international partners … to research if this was coincidental engagement or if there was something more significant to it. And our partners involved in the intelligence work globally confirmed with us repeatedly that there appeared to be a convergence of these three networks dominating the Vancouver area becoming a very significant threat.[14]

While the three groups discussed above pose a unique threat to Canada and its global partners, there are a wide range of other organized crime groups operating in British Columbia, including outlaw motorcycle gangs (which are among the most prominent organized crime groups in Canada and often have operations across the globe), drug-trafficking networks, and violent street gangs.[15] Many of these groups pose a significant public safety concern because of their frequent involvement in violent conflicts with other organized crime groups. They also pose a significant money laundering threat because of the considerable profits they generate from various forms of criminal activity, including fraud and drug trafficking.[16]

A 2019 report on organized crime in Canada identified 14 organized crime groups as posing a high-level threat to Canadian interests.[17] Moreover, it appears that a disproportionate number of these groups have connections to British Columbia. Chief Superintendent Robert Gilchrist, the director general of Criminal Intelligence Service Canada (CISC), testified that 10 of the 14 organized crime groups posing a high-level threat to Canadian interests are linked to British Columbia.18 He also identified 35 medium-level threat groups and 83 low-level threat groups with links to this province.[19]

Chief Superintendent Gilchrist went on to testify about the number of organized crime groups involved in money laundering activity and the methods used by those groups to launder illicit funds. For example, he testified that 176 of the 680 organized crime groups assessed by CISC as part of the 2019 integrated threat assessment process were identified as

14 Evidence of C. Chrustie, Transcript, March 29, 2021, pp 19–21. See also Evidence of R. Wainwright, Transcript, June 15, 2020, pp 19–21, where he discusses the increasing professionalization of transnational organized crime networks and the marked change he has seen over the past 10 years.

15 Exhibit 3, Overview Report: Documents Created By Canada, Appendix E, Canada, Criminal Intelligence Service Canada, *Public Report on Organized Crime 2019* (Ottawa, 2019), p 9.

16 Ibid, pp 12–13. These groups may also provide transportation and support for transnational organized crime groups. Wayne Rideout, the assistant deputy minister and director of police services in the BC Ministry of Public Safety and Solicitor General, emphasizes that the violence they perpetrate is not "street gang" violence but "organized crime violence" perpetrated by groups operating at a very high level of sophistication and managing to garner attention at the national and international level: Transcript, April 6, 2021, pp 58–59.

17 Ibid, p 4.

18 Evidence of R. Gilchrist, Transcript, June 9, 2020, p 45.

19 Evidence of R. Gilchrist, Transcript, June 10, 2020, p 2.

being involved in money laundering, with 28 percent of those groups using private sector businesses to launder illicit funds, 9 percent using money services businesses or informal value transfer systems, 10 percent using casinos, 7 percent using real estate, 3 percent using cryptocurrency and 2 percent using trade-based money laundering techniques.[20]

While these numbers may provide a useful starting point for an analysis of these issues, there are a number of significant gaps in the underlying intelligence, which make it difficult to draw any definitive conclusions.

First, the numbers provided by Chief Superintendent Gilchrist reflect the money laundering habits of 176 organized crime groups, but there are an estimated 1,850 such groups operating across the country. Chief Superintendent Gilchrist was unable to provide any information regarding the groups that were not assessed as part of the 2019 threat assessment, and it may be that no such information is available because these groups are using more sophisticated money laundering techniques.[21]

Second, the numbers are not specific to British Columbia and they may reflect money laundering techniques that are not possible or not frequently used in this province. For example, a money laundering technique used to launder illicit funds through the gaming sector in other provinces may not be possible in British Columbia because of new measures introduced by the province in response to *Dirty Money 1*.[22]

Third, the information used to generate these numbers was acknowledged to be imperfect. Both Chief Superintendent Gilchrist and Ryland Wellwood, the current analytics manager with Criminal Intelligence Service British Columbia / Yukon Territory, agreed that the level of organized crime involvement in money laundering is likely under-reported, especially with respect to more sophisticated techniques such as trade-based money laundering, which many experts view as one of the largest and most pervasive methodologies in the world.[23] Mr. Wellwood also testified that the numbers produced by Criminal Intelligence Service BC / Yukon are largely based on *indicators* of money laundering (rather than specific intelligence) and that much of the information it receives is quite incomplete. He stated:

> The first comment that I wanted to pass along was that when [Criminal Intelligence Service BC / Yukon] examines money laundering in general, we are looking at indicators … [W]e don't work with evidence necessarily, we work with a lot of information, some of which is quite incomplete, and

20 Evidence of R. Gilchrist, Transcript, June 9, 2020, pp 47–49, 54.

21 See, for example, Evidence of R. Gilchrist, Transcript, June 9, 2020, pp 54–55.

22 Ryland Wellwood, the current analytics manager with Criminal Intelligence Service BC / Yukon, provided a breakdown of the four most common typologies seen in British Columbia but was unable to provide a breakdown of percentages: see Evidence of R. Wellwood, Transcript, June 9, 2020, p 52. However, he did indicate that 37 of the 176 groups identified by Criminal Intelligence Service Canada as being involved in money laundering had a presence in British Columbia and that nine of these groups were considered to have a higher level of capability defined as the ability to conduct money laundering activity on behalf of other groups or criminal networks: Evidence of R. Wellwood, Transcript, June 9, 2020, p 51.

23 Evidence of R. Gilchrist, Transcript, June 9, 2020, pp 54, 55, 57; and June 10, 2020, p 54.

> we typically are … making use of indicators on a frequent basis for the work that we do in the assessments we produce.[24]

Fourth, the numbers provided by Chief Superintendent Gilchrist tell us the percentage of organized crime groups using each sector of the economy to launder illicit funds. However, they tell us nothing about the volume of illicit funds being laundered through each sector of the economy.[25] A sophisticated money laundering technique such as informal value transfer could be used by a small minority of organized crime groups to launder the majority of illicit proceeds generated by criminal activity in this province.[26] Likewise, a more prevalent technique such as the use of private businesses could be used by large number of relatively unsophisticated groups to launder a small fraction of the illicit funds generated in this province.[27]

While I appreciate that money laundering is a complex and secretive activity, it is essential that government agencies do more to study and gather specific intelligence concerning money laundering threats. In subsequent chapters of this Report, I recommend that the Province create a new office of the Legislature to provide independent oversight of the provincial anti–money laundering regime and assess the money laundering risks facing this province. I have also recommended the creation of a designated provincial money laundering intelligence and investigation unit responsible for developing proactive, actionable intelligence with respect to money laundering threats. It is my sincere belief that the collection of better intelligence with respect to these issues will enable law enforcement agencies, regulators, and government to respond to the significant threats posed by organized crime in a more effective way.

Politically Exposed Persons

Politically exposed persons are generally defined as individuals who are or have been entrusted with a prominent public function. Examples include heads of state, senior politicians, senior government staff, judicial or military officials, senior executives of state-owned corporations, and important political officials. Politically exposed persons are often discussed in conjunction with heads of international organizations, defined as persons who are or were, within a prescribed period, the head of an international organization or the head of an institution of any such organization. Because of the nature of their positions, politically exposed persons and heads of international organizations are at a higher risk of becoming involved in bribery and corruption offences, which gives rise to the need to launder the unlawful profits they receive.[28]

24 See Evidence of R. Wellwood, Transcript, June 9, 2020, p 50. See also Evidence of R. Gilchrist, Transcript, June 9, 2020, p 48.

25 Evidence of R. Gilchrist, Transcript, June 10, 2020, p 60.

26 Ibid, p 61.

27 Ibid.

28 Exhibit 959, J. Sharman, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, p 12.

While Canadian officials are not immune from bribery and corruption, the bigger risk arises from foreign corrupt officials who seek to protect the proceeds of their unlawful activity by moving them to countries such as Canada, the United Kingdom, and the United States. Jason Sharman, the Sir Patrick Sheehy Professor of International Relations at the University of Cambridge, testified that this is an issue of real concern for British Columbia and Canada:

> [A]s a multicultural society with a large stable financial sector, there's temptation for foreign corrupt officials to use the Canadian financial system or perhaps bits of it, like Canadian shell companies, to help in laundering money derived from corruption offences committed in other countries.[29]

Professor Sharman explained that the same factors that attract legitimate money – stable financial systems, predictable property rights, and sophisticated business professionals – attract criminal funds.[30] He indicated the real estate sector is particularly vulnerable to this type of money laundering insofar as it provides a store of value as well as a "vault" or "escape post" for foreign corrupt officials fleeing their home country.[31]

The *Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations*, SOR/2002-184 [*PCMLTF Regulations*] seek to limit the extent to which these individuals can launder funds through the BC economy by imposing enhanced due diligence requirements on financial institutions and other businesses dealing with politically exposed persons. For example, the regulations require that financial institutions take reasonable measures to determine whether a person is a politically exposed person or head of an international organization, a family member, or a close associate of such an individual before opening an account or processing an electronic funds transfer of more than $100,000 for or on behalf of that person.[32]

On June 1, 2021, the federal government expanded these due diligence requirements to designated non-financial businesses and professions such as casinos, dealers in precious metals and stones, real estate agents, accountants, and notaries. While these regulations make it more difficult for foreign corrupt officials to launder illicit funds through the Canadian economy, there remains a risk that these regulations can be circumvented through the use of shell companies and professional intermediaries such as lawyers, accountants, and real estate agents.[33] For example, Professor Sharman gave evidence that lax beneficial ownership

29 Transcript, May 6, 2021, pp 82–83. See also Exhibit 959, J. Sharman, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, p 12: "[a]s a large, multi-cultural country that attracts migrants from all over the world, including highly corrupt countries, Canada also to a certain extent imports some of the corruption problems of these countries, in the sense of accepting assets that are the proceeds of foreign corruption offences."

30 Transcript, May 6, 2021, p 82–83.

31 Ibid, pp 26, 88–89.

32 *PCMLTF Regulations*, s 116(1). Where a financial institution determines that a person is a politically exposed person, it must take reasonable measures to establish the source of funds that have been or are expected to be deposited into the account, obtain the approval of senior management to keep the account open, and conduct enhanced monitoring of the account for the purpose of detecting and reporting suspicious transactions: *PCMLTF Regulations*, s 121(1).

33 Evidence of J. Sharman, Transcript, May 6, 2021, pp 27–30. See also p 95.

standards in countries such as the United Kingdom, New Zealand, and the United States have allowed foreign corrupt officials to launder their tainted wealth through those jurisdictions and that Canadian corporate vehicles are at risk of being used for the same purpose.[34]

Another challenge that arises in this context is the difficulty of determining who is a politically exposed person, the head of an international organization, or a family member or close associate of a such a person. Commercial databases that provide information on politically exposed persons are not always comprehensive, reliable, or up to date. Moreover, the cost of these services may be prohibitive for professionals such as accountants, real estate agents, lawyers, and notaries.[35]

Other methods of determining whether a client is a politically exposed person – such as open-source research and customer declarations – are similarly problematic, especially where the politically exposed person is not forthcoming about their current or former position.[36] A research memorandum prepared for the Federation of Law Societies of Canada Anti–Money Laundering and Terrorist Financing Working Group describes some of these problems:

> The practical issue remains that there is no clear way to designate and identify PEPs [politically exposed persons] due to the lack of available and useful information about the identity of PEPs around the world. There are private providers of PEP databases, however the information contained in them and the ability to positively match the client with a PEP in a database can be challenging. In addition, there is a cost to this service which could be significant to law firms. Also, PEPs are becoming more creative in finding ways to avoid detection, such as opening accounts in the names of corporations instead of their own names, so the PEP lists may not be effective. Using name checking lists is not easy as many PEPs may have numerous "Also known as" alternative names. Also, naming customs and protocols from other countries are not always understood, many names are the same, and there are not unique identifiers, such as an address or a date of birth.[37]

Professor Sharman testified that general improvements to the Canadian anti–money laundering regime (such as a beneficial ownership registry) would improve the situation to some extent. However, he opined that a comprehensive response to the problem would require the creation of a specialized unit akin to those developed in the United States, the United Kingdom, and Switzerland with responsibility for investigating

34 Exhibit 959, J. Sharman, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, p 14.

35 Exhibit 1046, Overview Report: New Developments & Miscellaneous Documents, Appendix F, *FATF Guidance Report: Politically Exposed Persons* (June 2013), paras 61–62.

36 Ibid, paras 60 and 64–78.

37 Exhibit 210, Federation of Law Societies of Canada: Memorandum from CIV [Client Identification and Verification] Subgroup – FLSC AML Working Group to FLSC AML Working Group, re: Report on CIV Issues Review, April 24, 2019, p 17. See also Exhibit 3, Overview Report: Documents Created by Canada, Appendix C, Canada, Parliament, House of Commons, Standing Committee on Finance, 42nd Parl, 1st Sess, *Confronting Money Laundering and Terrorist Financing: Moving Canada Forward, Report of the Standing Committee on Finance* (November 2018), pp 19–20.

money laundering by politically exposed persons.[38] While I accept that the creation of a specialized foreign corruption unit would bolster attempts to combat money laundering in British Columbia, I have decided not to recommend the creation of a provincial foreign corruption unit for three principal reasons.

First, the creation of a specialized unit would require a significant investment of public funds in circumstances where there is little, if any, specific evidence about the extent of the problem. While there is generalized evidence that British Columbia is an attractive destination for foreign officials seeking to hide their ill-gotten wealth, such evidence cannot, in my view, justify that type of expenditure.

Second, it may well be that the Province can make meaningful progress on this issue through other means, including the creation of a beneficial ownership registry and an enhanced asset forfeiture regime. Professor Sharman notes that the successes of the specialized foreign corruption units created in the United States, the United Kingdom, and Switzerland have rarely been the result of criminal convictions. Instead, he emphasizes the importance of non-conviction-based asset forfeiture in addressing this issue.[39] Moreover, it seems to me that unexplained wealth orders (discussed below) may be a particularly useful tool in addressing the problem of foreign officials parking their illicit wealth in the British Columbia real estate market. Such orders would serve as a deterrent for the purchase of real estate and other assets with illicit funds and allow for these assets to be repatriated to their country of origin.

Third, it seems to me that the creation of a specialized unit to investigate foreign corrupt officials is properly a federal responsibility. While constitutional constraints prevent me from making recommendations aimed at the federal government, I would strongly encourage further study of this issue to determine whether the creation of this type of unit is a necessary and proportionate response to the money laundering threat posed by politically exposed persons and heads of international organizations.[40]

Another solution that has been proposed is the creation of a central registry or database of politically exposed persons and heads of international organizations to make it easier for smaller non-financial businesses and professions – such as lawyers, accountants, and real estate agents – to determine whether a client (or potential client) is a politically exposed person or head of an international organization.

In its closing submissions, the Law Society of British Columbia asks me to recommend that the federal government create and maintain a registry of politically exposed persons and heads of international organizations that is available to regulators, financial institutions and designated non-financial businesses and professions:

38 Exhibit 959, J. Sharman, *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment,* pp 18–20.

39 Ibid, pp 18–20.

40 I understand there are currently units within the RCMP which investigate offences under the *Corruption of Foreign Public Officials Act,* SC 1998, c 34, along with other international offences (such as war crimes). However, I do not understand these units to have a specific focus on the movement of foreign corruption proceeds to Canada.

> The work of FATF [Financial Action Task Force] and the United Nations has resulted in heightened due diligence requirements related to foreign PEPs [politically exposed persons], but many industry stakeholders experience challenges in meeting these requirements due to inconsistent definitions and methods for identifying PEPs. The same challenges arise with regard to identifying HIOs [heads of international organizations]. A government-created and maintained registry of PEPs and HIOs that is free and easily accessible would assist regulators, industry stakeholders and professionals in carrying out more effective and consistent due diligence activities. The federal government is best placed to create and maintain such a database, which should be made broadly available, taking into consideration relevant privacy legislation.[41]

While such a database would undoubtedly be difficult and costly to maintain, I believe it would provide a valuable resource for reporting entities including, in particular, smaller non-financial businesses and professionals such as real estate agents, accountants, and notaries. These entities have recently acquired obligations to determine whether a client or potential client is a politically exposed person and may not have the resources to subscribe to a commercial database or otherwise determine whether a client is a politically exposed person.

Indeed, it is unlikely that the legislative amendments introduced by the federal government on June 1, 2021, which expand the due diligence requirements for designated non-financial businesses and professions dealing with politically exposed persons and heads of international organizations, will have their intended effect if these businesses and professions are not given the tools they need to determine whether an individual is a politically exposed person.[42]

While it is theoretically possible for the province to create and maintain a list of politically exposed persons, I am of the view the federal government should have primary responsibility for creating and maintaining that list. Not only are the enhanced due diligence obligations imposed by federal legislation, but the federal government is in a better position to acquire the information needed to create the list as a result of its constitutional responsibility over international relations. It is also better positioned than the province to share relevant information with governments of other states.

I would therefore encourage the BC Minister of Finance and Minister of Public Safety and Solicitor General to work with their federal counterparts to study the viability of a database of politically exposed persons and heads of international organizations.

41 Closing submissions, Law Society of British Columbia, July 9, 2021, paras 83–84.

42 In making these comments, I acknowledge the risk that non-financial businesses and professions will come to rely exclusively on that database instead of critically evaluating whether a client is a politically exposed person. However, it seems to me that the creation of such a database would give smaller businesses and professions an additional tool to determine whether their clients are politically exposed persons and that anti–money laundering efforts would be further ahead by the creation of that database than they would be without it.

If created, the database should be updated as frequently as possible and include a list of politically exposed persons and heads of international organizations as well as their family members and close associates. Moreover, it should make use of photographs and affiliated companies and businesses, include alternative (or "also known as") names, take into account naming conventions in other countries, and allow these names to be searched in an intuitive way. It may also be useful to compile a list of positions and functions that are considered to be prominent public functions (i.e., positions held by politically exposed persons) for as many countries as possible.

Professional Money Launderers

Professional money launderers are individuals or groups that provide money laundering services to other criminals in exchange for a commission, fee, or profit. While not typically involved in the predicate offence, they have close connections to organized crime and are the architects of many sophisticated money laundering schemes.[43]

In most cases, the illicit funds generated by organized crime groups will be transferred to the professional money launderer, who will use a range of money laundering techniques to clean the illicit funds and return them to an account owned or controlled by the offender.[44] In some cases, the professional money launderer will also invest the illicit proceeds in real estate, luxury goods, and other investment vehicles.[45]

A Financial Action Task Force report on professional money laundering notes that many countries limit money laundering investigations to self-launderers (i.e., criminals who launder the proceeds of their own criminal activity) and have largely ignored professional money laundering organizations.[46] The report goes on to state that the dismantling of professional money laundering organizations "requires focused intelligence collection and investigation of the laundering activities."[47] However, the disruption of these organizations can have a significant impact on their criminal clients and be an effective interdiction strategy against numerous high-level criminal targets.[48]

43 Exhibit 4, Overview Report: Financial Action Task Force, Appendix Q: FATF, *Professional Money Laundering* (Paris: FATF, 2018) [*Professional Money Laundering*], pp 10–11. See also Evidence of R. Gilchrist, Transcript, June 9, 2020, pp 46–47; Evidence of S. Lord, Transcript, May 28, 2020, pp 15–16; Evidence of S. Schneider, Transcript, May 25, 2020, pp 27–28, 47–48; and Evidence of R. Wainwright, Transcript, June 15, 2020, pp 19–20, 22. Predicate offences, which are revenue-generating offences, are discussed in Chapter 2.

44 Exhibit 4, Appendix Q, *Professional Money Laundering*, pp 18–19.

45 Ibid, p 19.

46 Ibid, pp 6–7.

47 Ibid, p 7.

48 Ibid. See also Evidence of P. Reuter, Transcript, June 8, 2020, pp 40–41; and Evidence of P. Payne, Transcript, April 16, 2021, pp 121–122. Of particular note is the fact that many professional money laundering operations maintain a "shadow" accounting system that contains detailed records about their activities, including client names, funds laundered, the origin and destination of funds moved, relevant dates, and commissions received. These records represent an invaluable resource for investigators: Exhibit 4, Appendix Q, *Professional Money Laundering*, p 12. *Note also that a non-public version of the FATF report, which includes practical information with respect to the investigation, detection, and prosecution of professional money launderers, is available to law enforcement on request.*

I agree that greater priority should be given to the investigation of professional money laundering operations and review the key characteristics of these operations below.

Individuals, Organizations, and Networks

The Financial Action Task Force report divides professional money launderers into three categories: individuals, organizations, and networks.[49]

Individuals

Individual professional money launderers are defined as persons who provide specialized money laundering services to criminal clients.[50] These services can include registering and maintaining companies and other legal entities; serving as nominees for companies and accounts; creating false documentation; commingling legal and illegal proceeds; indirectly purchasing and holding assets; orchestrating lawsuits; and recruiting and managing money mules.[51]

In many cases, these services are provided by professionals such as accountants and lawyers who otherwise act in a legitimate capacity. However, it is important to distinguish between professionals who knowingly assist criminal clients in laundering illicit funds and those who unwittingly become involved in a money laundering scheme. While both groups present a money laundering risk, the former group presents a particular challenge for law enforcement because of their specialized knowledge and expertise, as well as their status as professionals (which can aid in avoiding detection).[52]

Organizations

Professional money laundering organizations are defined as groups of two or more individuals acting as autonomous, structured units. While each organization is slightly different, they typically have a strict hierarchical structure, with each member playing a specific role within the organization.[53] These roles may include:

- leaders and controllers who are responsible for the strategic direction of the organization and have decision-making power with respect to matters such as the manner in which illicit funds are laundered, the commission charged by the organization, and the salaries paid to each member of the group;
- introducers and promoters, who are responsible for bringing clients to the organization and managing communications with those clients;

49 Exhibit 4, Appendix Q, *Professional Money Laundering*, pp 12–13.

50 Ibid, p 12.

51 Ibid, p 15.

52 I return to these matters in Chapters 25–33.

53 Exhibit 4, Appendix Q, *Professional Money Laundering*, pp 12–13.

- infrastructure managers, who are responsible for the creation of money laundering infrastructure such as shell companies and bank accounts;
- document managers, who are responsible for the creation of the documentation needed to facilitate the money laundering process (e.g., fraudulent invoices or account statements);
- transportation managers, who are responsible for receiving and forwarding goods internationally, and preparing relevant customs documentation;[54]
- investors and purchasers, who are responsible for purchasing items such as real estate or luxury vehicles when needed to store value for later sale;
- collectors, who are responsible for collecting illicit funds from the client and, in some cases, "placing" the funds into the legitimate financial system;[55] and
- transmitters, who are responsible for moving illicit funds through the money laundering infrastructure established by the organization.[56]

In my view, it is essential for law enforcement officials to understand these roles in order to fully dismantle a professional money laundering organization.[57] For example, the arrest of a promoter, transmitter, or collector may have little effect on the operations of a professional money laundering organization if the leaders and controllers are not arrested and prosecuted.

Networks

Professional money laundering networks are formal or informal collections of associates working together to facilitate money laundering schemes and/or subcontract their services for specific tasks. These networks can operate globally and may involve two or more professional money laundering organizations working together to launder illicit cash.[58] Collaboration with other money laundering professionals allows these networks to diversify the channels through which illicit funds can pass, thereby reducing the risk of detection and seizure. It also allows them to access the money laundering infrastructure controlled by other groups in order to better serve their criminal clients.[59]

54 Transportation managers are particularly important for professional money laundering organizations that rely on trade-based money laundering to support their money laundering operations: Exhibit 4, Appendix Q, *Professional Money Laundering*, pp 16–17.

55 These individuals are at the highest risk of identification by law enforcement but are typically at the lower end of the hierarchy: ibid.

56 Ibid.

57 Ibid, p 16.

58 Ibid, p 13.

59 Ibid.

Types of Money Laundering Organizations and Networks

The Financial Action Task Force report identifies four key types of professional money laundering organizations and networks: (a) cash controller networks; (b) money mule networks; (c) digital money and virtual currency networks; and (d) proxy networks.[60]

Each of these networks is supported by an array of money laundering techniques, including bulk cash smuggling, informal value transfer, and the use of shell companies to obscure the true origins and ownership of illicit funds.

Cash Controller Networks

Cash controller networks allow criminal organizations to transfer vast sums of illicit cash throughout the world through the use of informal value transfer systems and other types of account settlement mechanisms.[61]

Generally speaking, these networks consist of a controller who directs multiple collectors and coordinators stationed in various countries throughout the world. While each system is slightly different, the controller will typically have pools of cash available to them in different locations. When a client needs to transfer funds from one location to another, the money will be paid into the cash pool in the first location and paid out of the cash pool in the jurisdiction where the client needs the money. The money paid into the first pool will be held in that location until another client needs to transfer funds into that jurisdiction. Over time, the operator may need to reconcile the cash pools to keep them in balance. However, there is no transfer of funds on an individual basis.[62]

One of the benefits of this business model is that criminal organizations can move value from one country to another without the need to transport cash across an international border or transfer the funds through the regulated financial system. It also allows criminal organizations to obfuscate any paper trail that may lead back to the original offence and receive legitimate funds at the conclusion of the money laundering process.

Money Mule Networks

As the name suggests, money mule networks use individuals to transfer (or smuggle) illicit funds under the direction of the professional money laundering operation.

The Financial Action Task Force report states that cash transportation services are increasingly being outsourced to "specialized cash transportation networks that are responsible for collecting cash, transporting it to pre-determined locations and facilitating its placement in the financial system."[63] It also notes that many money mule networks are "well-resourced and highly effective" in moving illicit funds from one location to another.[64] While money mules can be unaware they are being used to facilitate criminal

60 Ibid, p 19.

61 Ibid, p 19.

62 Ibid, pp 19–22. See also Evidence of S. Lord, Transcript, May 28, 2020, pp 65–66.

63 Exhibit 4, Appendix Q, *Professional Money Laundering*, p 21.

64 Ibid, p 23.

activity, they are often willing participants who participate in the money laundering scheme in return for off-the-record cash payments and free travel.[65]

Money mules can also be used to open bank accounts to facilitate the movement of illicit cash through the global financial system. In these schemes, the professional money laundering operation will create apparently legitimate businesses and hire unsuspecting individuals whose job responsibilities involve setting up bank accounts to pass along supposedly legitimate payments. In reality, these unsuspecting individuals act as money mules, processing illicit funds and wiring them to other individuals involved in the operation.[66]

Digital Money and Virtual Currency Networks

Professional money laundering operations also allow criminals to "cash-out" proceeds generated in virtual currency via online markets such as dark web drug trafficking sites. In such cases, the professional money laundering operation will transfer the virtual currency through a complex chain of e-wallets to enhance the anonymity of the virtual currency transaction. The funds will then be sent back to the e-wallet of the organized crime group, transferred to bank cards, and withdrawn in cash.[67] Money mules employed by professional money launderers may also conduct ATM withdrawals on behalf of the organized crime group to further enhance anonymity.[68]

Proxy Networks

Proxy networks are professional money laundering operations that seek to clean illicit funds by moving them through a complex series of transactions within the legitimate financial system. These schemes typically involve multiple layers of shell companies in different jurisdictions, which have been established purely to redistribute funds and obfuscate the trail of financial flows.[69] The Financial Action Task Force report indicates that these schemes typically have the following structure:

- Client funds are transferred or deposited in accounts opened in the name of shell companies owned or controlled by the professional money laundering operation.
- The funds are moved through a complex chain of accounts established by domestic shell companies under fictitious contracts.[70]
- The funds are transferred abroad under fictitious trade contracts, loan agreements, and securities purchase agreements.

65 Ibid, p 22.

66 Ibid, p 23.

67 Ibid, p 25.

68 Ibid.

69 Ibid, p 26.

70 Funds from different clients are mixed within the same accounts, making it difficult for investigators to trace the funds back to a particular client: ibid, p 26.

- The funds are moved through a complex chain of international transfers using bank accounts set up by shell companies in various locations.
- The funds are returned to accounts owned or controlled by the client, the client's close associates, or affiliated legal entities. Alternatively, the professional money laundering organization may purchase goods and services (including real estate) on behalf of the client.

The report notes that the networks that facilitate cross-border movement of funds often tie into a wider global network of professional money launderers.[71] The use of professional money launderers located in different countries, combined with the different methods of transferring funds internationally (e.g., fictitious trade contracts, loan agreements, and securities purchase agreements), ensures the diversification of financial transactions and reduces the risk of detection.[72]

Complicit Professionals

A final point raised by the Financial Action Task Force report is the involvement of professionals such as bankers, lawyers, and accountants in money laundering schemes. The report notes that professional money laundering operations "actively seek out insiders as potential accomplices to help launder illicit proceeds."[73] It also emphasizes the fact that these individuals have insider access and may be able to falsify documents or initiate transactions in order to bypass anti–money laundering regulations. For example, a complicit bank employee may perform functions such as:

- creating counterfeit cheques;
- coordinating financial transactions to avoid reporting requirements;
- accepting fictitious documents provided by clients as a basis for transactions without asking appropriate questions; and
- performing transactions to avoid scrutiny (for example, transferring funds on behalf of their clients without a change in the net balance in the account at the beginning and end of a working day).[74]

Lawyers and accountants can also be involved in setting up many of the corporate structures and offshore vehicles used to conceal the ownership of illicit funds and facilitate the movement of criminal proceeds throughout the world. In many cases, these professionals may use solicitor-client and other, similar forms of privilege to mask the movement of these funds.

71 Exhibit 4, Appendix Q, *Professional Money Laundering*, p 28.

72 Ibid.

73 Ibid, p 35.

74 Ibid, p 39. In rare cases, a professional money laundering operation may be able to compromise entire institutions or businesses by acquiring control of the institution and appointing its own criminal management: ibid, p 36.

Case Study – The E-Pirate Investigation

One of the most prominent examples of money laundering activity in British Columbia comes from a 2015 RCMP investigation named Project E-Pirate,[75] which is the only major money laundering investigation in this province to result in criminal charges in the five-year period from 2015 to 2020.[76] The Commission's purpose in inquiring into and discussing this project is not to make findings of criminal liability, but to learn from the observations of law enforcement and other agencies about money laundering in the province and possible approaches to preventing and combatting it.

Project E-Pirate was commenced in response to information provided by the BC Lottery Corporation concerning the activities of an individual named Paul Jin.[77] For many years, the BC Lottery Corporation had been trying to get the attention of law enforcement to investigate Mr. Jin's involvement in providing suspicious cash to high-stakes gamblers at Lower Mainland casinos. An affidavit sworn by RCMP Corporal Melvin Chizawsky suggests that Mr. Jin and his associates were identified by the BC Lottery Corporation as being connected to 140 casino transactions totalling more than $23 million in the three-year period from June 27, 2012, to June 24, 2015.[78]

In February 2015, Brad Desmarais, the BC Lottery Corporation's vice-president of corporate security and compliance had an informal meeting with Mr. Chrustie, a former RCMP officer with significant experience in the investigation of transnational organized crime, at a coffee shop in North Burnaby. At the time, Mr. Chrustie was a senior member of the RCMP's Federal Serious and Organized Crime section.

75 An RCMP "project" file such as E-Pirate typically involves multiple investigative units and uses different techniques to gather information with respect to serious criminal offences. Such investigations are far removed from investigations conducted by front-line police officers that can be handled by just a few officers. The "E" in E-Pirate refers to the fact that the investigation is being conducted by "E" Division (which is responsible for policing in British Columbia).

76 Note, however, that the Crown entered a stay of proceedings on November 22, 2018, with the result that the matter did not proceed to trial: Exhibit 663, Affidavit of Cpl. Melvin Chizawsky, February 4, 2021, Exhibit A, para 125 [Affidavit of M. Chizawsky].

77 More specifically, the investigation was commenced in response to information provided by Brad Desmarais to Mr. Chrustie (who was, at the time, the officer in charge of the RCMP Federal Serious and Organized Crime Major Projects). Mr. Desmarais had been trying to secure the co-operation of other law enforcement agencies to conduct the investigation and approached Mr. Chrustie to ask for his help: Evidence of C. Chrustie, Transcript, March 29, 2021, pp 62–63. Note, however, that the issue of money laundering in Lower Mainland casinos was previously investigated by the RCMP's Integrated Proceeds of Crime Unit from 2010 to 2012. However, the investigation was terminated when these units were disbanded: see Evidence of B. Baxter, Transcript, April 8, 2021, pp 21–79.

78 Exhibit 663, Affidavit of M. Chizawsky, para 33. See also Evidence of M. Chizawsky, Transcript, March 1, 2021, pp 40–41.

Mr. Desmarais expressed his frustration that the issue of cash facilitation at Lower Mainland casinos was not being treated seriously and Mr. Chrustie agreed to assign a few of his investigators to look into the issue.[79]

In April 2015, the RCMP began conducting surveillance of Mr. Jin and his associates. Mr. Jin was the target of surveillance on 40 days between April 16, 2015, and February 24, 2016.[80] On numerous occasions during that time frame, he was observed to frequent the offices of Silver International Investment Ltd. (Silver International). According to the police, Mr. Jin would often leave Silver International with bags and/or suitcases and attend at a property on Jones Road in Richmond, British Columbia (the Jones Road Property). A short time later, he would leave the Jones Road Property with smaller bags and attend at other locations in the Lower Mainland, where he would give the smaller bags to other individuals. On multiple occasions, these individuals attended at Lower Mainland casinos shortly after meeting Mr. Jin and conducted large cash buy-ins.[81]

As a result of that surveillance, investigators came to believe that Mr. Jin was moving cash from Silver International to the Jones Road Property for repackaging, and that Mr. Jin would subsequently provide that money to customers who were converting it into casino chips at Lower Mainland casinos.[82] Investigators also came to believe Mr. Jin was running an unlicensed gaming house on No. 4 Road in Richmond, British Columbia (the No. 4 Road Property), and accumulating large sums of cash at a condominium on Brighouse Way (the Brighouse Way Property).[83]

On October 15, 2015, the RCMP executed search warrants at Silver International along with various other locations, including the Jones Road Property, the No. 4 Road Property, and the Brighouse Way Property. These searches resulted in the seizure of large sums of cash as well as financial ledgers and daily transactions logs that appeared to record cash flows into and out of Silver International. An analysis conducted by Elise To, a financial analyst with the RCMP's Federal

79 Evidence of B. Desmarais, February 1, 2021, pp 118–119; Evidence of C. Chrustie, March 29, 2021, pp 62–63.

80 Exhibit 663, Affidavit of M. Chizawsky, para 116.

81 On two occasions the buy-ins were $50,000 and $99,900, respectively: Exhibit 663, Affidavit of M. Chizawsky, paras 40 and 57–58. See also Evidence of M. Chizawsky, Transcript, March 1, 2021, pp 52–53.

82 Exhibit 663, Affidavit of M. Chizawsky, para 107. In a statement given to police on February 24, 2016, Mr. Jin confirmed that he was in the business of loaning money and received funds from Silver International. He also described himself as a loan shark: ibid, para 93.

83 Ibid, paras 38, 108, 115. A report prepared by an RCMP analyst indicates that the net profit of the unlicensed gaming house from June 11, 2015, to October 8, 2015, was in the range of $32,716,719: ibid, para 106.

Serious and Organized Crime, Financial Integrity Group, concluded that Silver International had conducted 474 debit transactions totalling $83,075,330 and 1,031 credit transactions totalling $81,462,730 for the 137-day period between June 1, 2015, and October 15, 2015.[84] On an annual basis, that corresponds to approximately $221 million in debit transactions and $217 million in credit transactions.[85]

Simon Lord, a senior officer with the UK's National Crime Agency and one of the world's leading experts on money laundering, was retained by the RCMP to give expert evidence in connection with Project E-Pirate. While not authorized to speak to all aspects of the investigation, he testified that the evidence he reviewed was consistent with an underground banking scheme whereby large amounts of money were being transferred to various locations using an informal value transfer system. He went on to explain that large amounts of cash were being delivered to Silver International and stored temporarily at its Richmond office. The principals of that company would then facilitate token-based cash handovers in places like Mexico City, with the cash delivered to Silver International being repurposed and given to individuals who wanted to gamble in legitimate or underground casinos but could not move their money out of China because of currency restrictions imposed by the Chinese government.[86]

Corporal Chizawsky gave evidence to the same effect. He testified that the international gambler would deposit money into a bank account owned or controlled by Silver International in China. Once those funds were received, Silver International would release an equivalent amount

84 Ibid, para 99. In accounting terms, a "debit" is an accounting entry that increases an asset or decreases a liability, and a "credit" is an accounting entry that increases a liability or decreases an asset: ibid, Exhibit 53, p 3. These terms can be somewhat counterintuitive. For the Silver International ledgers, the debit entries could be interpreted as money coming into the account, while the credit entries could be interpreted as money taken out of the account.

85 Ibid, paras 99–106; Evidence of M. Chizawsky, Transcript, March 1, 2021, p 95. Although Mr. Jin's legal name is not used in these ledgers, I accept the evidence of Cpl. Chizawsky that the entries referring to "XB," "Xiao Bao," "Xiao Bao XB," and "Bao" in fact refer to Mr. Jin and that Mr. Jin was responsible for the withdrawal of approximately $26,996,935 from Silver International between June 1, 2015, and October 15, 2015. First, it appears that Xiao Bao and Siu Bo are Mr. Jin's street names: Exhibit 663, Affidavit of M. Chizawsky, para 100. More importantly, the RCMP was able to match up the entries made in each of these ledgers with the closed-circuit television footage seized from Silver International as well as surveillance conducted by the RCMP to confirm that these entries refer to Mr. Jin: ibid, para 105; Evidence of M. Chizawsky, Transcript, March 1, 2021, pp 54–55 and 97–99. Mr. Jin's admission that he received funds from Silver International also supports that conclusion.

86 Evidence of S. Lord, Transcript, May 28, 2020, p 9, and May 29, 2020, pp 2–3. It also appears that Mr. Jin was conducting a private lending business in which he was lending large sums of money to borrowers in British Columbia. These loans were collateralized through mortgages and enforced using civil claims and charges placed against properties owned by the borrowers or their immediate family members: Exhibit 1052, Overview Report: Paul Jin Debt Enforcement Against BC Real Estate.

to Mr. Jin (who would subsequently provide it to his client).[87] Importantly, however, there was no electronic accounting between the two countries. Nor were there any electronic funds transfers. The money paid to Silver International in China stayed in that country (at least temporarily), and the client was paid out from the "pool" of funds maintained by Silver International in Canada.[88]

On the evidence before me, it seems clear that Silver International was using an informal value transfer system to move funds (or more accurately, value) from China to British Columbia, where it was being used by high-stakes gamblers to make large cash buy-ins at Lower Mainland casinos. While the evidence is less clear that the cash received by Silver International and provided to Mr. Jin in British Columbia was derived from profit-oriented criminal activity such as drug trafficking, there is, in my view, an unavoidable inference that most, if not all, of the cash being left at Silver International was derived from criminal activity and that Silver International was assisting one or more organized crime groups to launder those funds.

Corporal Chizawsky testified that the individuals who deposited these funds would enter Silver International with suitcases or boxes full of cash, walk directly to the back part of the office, drop the suitcases or boxes, and depart very quickly.[89] Corporal Chizawsky described the behaviour of these individuals as "almost the exact opposite" of how one conducts business when making a deposit of lawfully obtained money. He also testified that the behaviour of these individuals was markedly different from other customers of Silver International, who would present their identification and spend anywhere from five to 15 minutes in the office.[90]

Another factor suggesting that the cash was derived from criminal activity relates to the manner in which it was packaged. Unlike bills received from a financial institution, the number of bills in each bundle was not consistent, the bills were not oriented in the same direction, and the bundles were held together with different-coloured elastic bands that

87 Evidence of M. Chizawsky, Transcript, March 1, 2021, pp 72–74 and 82–85.

88 Ibid. Although Cpl. Chizawsky gave this evidence in response to questions regarding statements made by Mr. Jin in a police interview, I understood his answer to be based on all the evidence, including but not limited to Mr. Jin's statement. For example, Cpl. Chizawsky states that Mr. Jin's statement "solidifies our belief [in] the underground Chinese banking system" and that Mr. Jin has "reinforced" the underground banking theory (ibid, pp 83–84).

89 Ibid, pp 56–58. More specifically, Cpl. Chizawsky testified that the amount of time these individuals would spend in the office would be "probably two minutes at the most, maybe less, maybe up to five": ibid, p 57. At least one of the individuals who deposited cash in this manner had known links to organized crime.

90 Ibid, pp 57, 125–126.

broke easily. Such indicators are commonly used by experts to distinguish legitimate cash from "street" cash (i.e., cash derived from criminal activity).[91] Melanie Paddon, former lead investigator on Project E-Pirate and an expert on cash bundling, made the following comments regarding the nature of the cash moving through BC casinos during this timeframe:

> Well, yes, definitely I believed it was criminal. I mean, so basically cash coming in bags, suitcases, boutique bags is not normal practice … [I]n my opinion illegal cash is basically held together in bricks, and they're sub-bundled with elastic bands on them usually in amounts of … 1,000, 2,000 or 5,000 which makes up the actual brick. Often the bills would be facing in different directions.
>
> Criminals basically take their cash whereas a bank would put together a bundle of cash – it would be 100 notes of one specific denomination. Criminals don't. They basically take their brick of cash, and it's made up in dollar amount, so it would be in even dollars of 5,000, 10,000, that kind of idea. It's not in hundred-note amounts. There are no paper bands around it. It's held together with elastics on both ends, sometimes in the middle.
>
> The bricks are put together and they're often thrown into a boutique bag. They often tend to use … grocery bags, plastic grocery bags, they're concealed in compartments in vehicles, they're hidden in briefcases and they're basically brought into the casino.
>
> That is dirty cash. I mean, that is … not from a legal source. A bank would never distribute cash like that.[92]

One of the lessons that can be drawn from this investigation is that professional money laundering operations are highly opportunistic and flexible. They constantly seek to take advantage of changing geopolitical forces and lax regulatory environments. In this case, the transactions facilitated by Silver International were made possible by a confluence of

91 Exhibit 663, Affidavit of M. Chizawsky, para 97. For additional evidence concerning the methods commonly used by experts to distinguish legitimate cash from street cash, see Evidence of S. Lord, Transcript, May 29, 2020, pp 10–12; Evidence of D. Dickson, Transcript, January 22, 2021, pp 83–84; Evidence of B. Baxter, Transcript, April 8, 2021, p 36; and Evidence of M. Paddon, Transcript, April 14, 2021, pp 16–20. Although Mr. Lord's evidence that the principals of Silver International were facilitating token-based cash handovers in places such as Mexico City would ordinarily be compelling evidence that Silver International was receiving illicit cash, the documents relied upon by Mr. Lord in coming to that conclusion are not in evidence, and I have decided not to give any weight to that evidence.

92 Evidence of M. Paddon, Transcript, April 14, 2021, pp 16–19.

geopolitical factors including: (a) the need for organized crime groups to get rid of the cash proceeds of criminal activity in BC and move the profits of that activity to places like Mexico City; (b) the restriction of capital outflows by the Chinese government; and (c) the willingness of the gaming sector to accept large sums of cash from wealthy Chinese gamblers.[93] The lack of attention to this issue by law enforcement also contributed to the unchecked growth of money laundering activity in the gaming sector from 2010 to 2015.

I return to the operations of Silver International and the regulatory environment that made it possible in subsequent chapters of this Report.

93 Mr. Jin's private lending business was also made possible by rising real estate prices, which created the equity that allowed wealthy gamblers to take out those loans.

Chapter 4
How Much Money Is Laundered in BC?

In coming to grips with money laundering in British Columbia, an obvious question presents itself: how much money gets laundered in this province in a given year? Can a total dollar figure be ascribed to money laundering? Quantifying this activity could contribute significantly to our understanding of the scope of the money laundering problem. And it could serve as a useful measurement – both of the problem, and the success of initiatives aimed at combatting the problem.

Section 4 of my Terms of Reference requires me to make findings of fact about money laundering in British Columbia, including its extent in several sectors.[1] In my Interim Report, I considered the issue of quantification, and recognized that, if it were possible to quantify, there would be value in a reliable measurement of money laundering. Now, having the benefit of the entirety of the evidence led in the Inquiry, and the participants' submissions, I have an even greater appreciation of the inherent and inescapable difficulties with quantification. But that does not mean throwing up one's hands, as I will explain.

Some experts say that estimates made using quantification methodologies are so imprecise they are simply not useful in creating and evaluating anti–money laundering policies.[2] Others maintain that quantification efforts *are* worthwhile, even though challenging, because decision-makers must be able to understand the extent of money laundering in order to make informed choices about the extent to which – and how – they will resist it.[3]

1 Terms of Reference, para 4(1)(a).

2 Evidence of P. Reuter, Transcript, June 5, 2020, p 52 ("… you have to work out how to … make policy here without numbers because the numbers are going to be so crude you couldn't possibly tell whether things have gotten better or worse, just with a set of numbers").

3 Evidence of S. Lord, Transcript, May 28, 2020, p 19.

In my Interim Report, I commented that a key question for the Commission is whether quantification methodologies (either individually or in combination) can provide a reliable estimate of the volume of money laundering activity in British Columbia or, at the very least, whether they can give policy-makers a sense of the magnitude of the problem. In this chapter, I return to the topic. I proceed in this sequence:

- First, I discuss whether quantifying the extent of money laundering in British Columbia is a useful exercise.
- Second, I provide a brief summary of existing estimates of money laundering in British Columbia.
- Third, I canvass the methods for quantification that are identified in the literature.
- Fourth, I outline the Commission's efforts at quantification of money laundering in the province;
- Fifth, I set out my conclusion on the extent of money laundering in British Columbia.
- Sixth, I discuss ways of improving money laundering estimates.
- Finally, I make a few comments about evaluating the effectiveness of anti–money laundering efforts.

Why Try to Estimate Money Laundering?

The literature shows that there are several methods that purport to estimate the extent of money laundering – in a sector, in a particular geographic region, or globally. But there is no consensus on which method, if any, can reliably estimate the extent of money laundering. The fact that it is hard to measure money laundering is not surprising, given the activity at issue. For certain criminal activity, it may be feasible to obtain accurate measurements, perhaps by adding up how many cars were stolen in a year or how many banks were robbed. But money laundering is not like that. Such activity is evasive of review. It is not well understood (many people, including police, are not well versed in the area and may not recognize when money laundering is happening). It is constantly changing (with new typologies and modifications of existing ones regularly appearing). It is not reliably reported to police or regulators. And money laundering is not organized in any way that allows for a straightforward estimation of the total activity. It is secretive and the goal is to remain in the shadows, out of view. This is one thing all experts agree on: because money laundering

takes place in secret, it is impossible to directly measure, and it is very hard, if not impossible, to reliably estimate.[4]

As noted, my Terms of Reference direct that I inquire into the extent of money laundering in British Columbia. While the challenges of quantification are large, in my view there are three sound reasons why estimating money laundering would be useful.

First, reasonable estimates could help government determine whether the problem is one worth putting resources into at all. In its closing submissions, British Columbia took the position that money laundering estimates provide a useful indication of the magnitude of the problem.[5] Similarly, the coalition of Transparency International Canada, Canadians for Tax Fairness, and Publish What You Pay Canada (whom I refer to as the Transparency Coalition) argues that understanding the scale of money laundering is necessary in order to appreciate its effects and to decide on the scale of resources that should be devoted to its suppression.[6]

Professor Brigitte Unger testified that money laundering estimation is very important in order to alert politicians that money laundering is a serious issue that must be tackled.[7] If policy-makers were to proceed only when they had measured, observed, or recorded cases – rather than estimates of the extent of money laundering – then nothing would be done, because they would not understand the scope of the problem.[8] Professor Peter Reuter said the principal utility in having an estimate of money that needs to be laundered is to help provide a sense of how important money laundering controls might be in impacting predicate offences (that is, the original and underlying offence, such as drug trafficking, that produced the illicit money).[9] If only a small amount of money is laundered, then taking steps to make money laundering more difficult does not provide much benefit. But if a great deal is laundered, then money laundering controls may be an effective way to target the underlying illegal market. Similarly, Simon Lord stated that "you have to be able to understand and make … informed choices about the extent to which you're going to … try and regulate that informal economy."[10]

4 Evidence of B. Unger, Transcript, December 4, 2020, pp 9–10, 55; Exhibit 341, J. Cassara – Final Statement to the Cullen Commission, p 9; Evidence of S. Lord, Transcript, May 29, 2020, pp 29, 31, 60–61 and May 28, 2020, pp 86–87 ("… if anyone says that they can accurately quantify this, then they're lying, quite frankly, because there are so many different things that emerge and there's so many different systems and so many different ways of measuring it"); Evidence of S. Schneider, Transcript, May 26, 2020, pp 38–39 and Transcript, May 27, 2020, pp 24–25; Evidence of O. Bullough, Transcript, June 1, 2020, p 89; Evidence of M. Levi and P. Reuter, Transcript, June 5, 2020, pp 48–55; Evidence of R. Gilchrist, Transcript, June 9, 2020, p 40; Evidence of B. Ogmundson, Transcript, February 17, 2021, pp 169–70; Evidence of B. Pereboom, Transcript, March 11, 2021, p 29; Evidence of H. McCarrell, Transcript, March 11, 2021, p 114; Exhibit 330, Maureen Maloney, Tsur Somerville, and Brigitte Unger, "Combatting Money Laundering in BC Real Estate," Expert Panel, March 31, 2019 [Maloney Report], pp 1–2, 114.

5 Closing submissions (other than gaming sector), Government of British Columbia, p 2.

6 Closing submissions, Transparency Coalition, p 4, para 1.

7 Evidence of B. Unger, Transcript, December 4, 2020, pp 9, 155.

8 Ibid, pp 10–11.

9 Evidence of P. Reuter, Transcript, December 8, 2020, pp 12–13.

10 Evidence of S. Lord, Transcript, May 28, 2020, p 19.

Second, reasonable estimates would help governments develop policy aimed at addressing money laundering most effectively. This would include deciding to prioritize attention on certain sectors or approaches and deciding how best to expend anti–money laundering resources and efforts. Estimating the quantity of money being laundered can assist government in focusing on specific problematic sectors, and in formulating a suitable policy or enforcement response.[11] Professor Reuter suggested that knowing the extent of money laundering in a specific market, like the fentanyl market, can help authorities decide their priorities.[12] As Mr. Lord said:

> [T]he role of the NECC [the UK National Economic Crime Centre] is to understand the threat initially, and to a large extent that's where I come in because the understanding that comes out of the National Assessment Centre helps the NECC to understand the threat. Then, once you understand the threat, then you can define the priorities that you have in terms of tackling the threat and also what partnerships you have available to you which might help you work on your priorities.
>
> Then you can task and coordinate the response … getting other agencies on board, working in partnership with different people in order to address the issue. And then you have to essentially drive the delivery and assess the impact of what it is you've done.[13]

Third, having a baseline of the extent of the problem could provide a benchmark against which to assess the utility of steps taken to address money laundering.[14] Professor Michael Levi maintained that we need to measure the effectiveness of anti–money laundering strategies, because without measuring how much money laundering there was before or after certain policies are implemented, we may not actually be doing much about money laundering.[15] He testified:

> Evaluation is the touchstone of contemporary policy making; good policy requires systematic and transparent evaluation and [anti–money laundering] is just the kind of broad policy intervention that requires evaluation to improve its design and operation, if not to justify its existence.[16]

I am of the view that if quantification of money laundering is possible, it would undoubtedly prove useful. It would equip government, regulators, and authorities – and the public – with important insights about money laundering and about how well countermeasures are working. The *value* of quantification is obvious. The challenge is *how*, and, indeed, whether it is possible to accurately quantify money laundering.

11 Evidence of B. Unger, Transcript, December 4, 2020, pp 155, 157.

12 Evidence of P. Reuter, Transcript, December 8, 2020, p 14.

13 Evidence of S. Lord, Transcript, May 28, 2020, p 22.

14 Ibid.

15 Evidence of M. Levi, Transcript, June 5, 2020, pp 21–22.

16 Exhibit 26, Michael Levi, Peter Reuter, and Terence Halliday, "Can the AML System Be Evaluated Without Better Data?" (2018) 69 *Crime, Law and Social Change*, p 310; Evidence of P. Reuter, Transcript, June 5, 2020, p 61.

Previous Estimates of Money Laundering in British Columbia

I heard evidence about three previous efforts to quantify money laundering in British Columbia. I outline these here.

The Expert Panel Report (Maloney Report)

In September 2018, the British Columbia Minister of Finance appointed Professors Maureen Maloney, Tsur Somerville, and Brigitte Unger to look at money laundering in the British Columbia real estate sector (I refer to their report as the Maloney Report, though it is also known as the Expert Panel Report).[17] My Terms of Reference specifically direct me to review and take into consideration this report. In the Maloney Report, the authors employed a method called the "gravity model" to estimate the amount of money laundered annually in Canada and British Columbia.

Using the Walker and Unger gravity model (which I discuss in more detail below), the Expert Panel estimated annual money laundering activity in Canada in 2015 at $41.3 billion and in 2018 at $46.7 billion.[18] For British Columbia, the estimates for 2015 and 2018 were $6.3 billion and $7.4 billion, respectively.

The authors could not get the data required to fine-tune the gravity model so that it could be applied properly to British Columbia.[19] When testifying at this Commission, Professor Unger told me that she does not know how good the model is when it is applied to sub-regions, such as a province rather than the entire country, because it has not yet been used in this way.[20] There was no way to test the results because the authors did not have the data needed to do so. Professor Unger said their effort was to divide Canada into six regions and treat each one like a nation. But without FINTRAC data, and having never compared intra-country regions, this proved challenging.[21]

The Expert Panel likewise went on to attempt an estimate of how much of the money was laundered in British Columbia and then invested in real estate.[22] In an appendix to Chapter 19, I describe the tentative analytical path used to generate the panel's estimate of money laundering in real estate. Their conclusion was a wide range, *between $800 million and $5.3 billion per year*. The panel went on to estimate that using the upper range of illicit funds invested into real estate would result in an increase to housing prices, because of money laundering, of *3.7 to 7.5 percent higher*.[23]

17 Exhibit 330, Maloney Report.
18 Ibid, pp 1, 47–48.
19 Evidence of B. Unger, Transcript, December 4, 2020, pp 122–23.
20 Ibid, pp 126–28.
21 Ibid, pp 125–28.
22 Exhibit 330, Maloney Report, pp 50–61.
23 Ibid, p 61.

Professor Somerville testified that the Expert Panel's estimate of money laundering in the real estate sector was made cautiously, not because it was a conservative estimate, but because it was an estimate with a "very, very large number of assumptions and caveats" underlying those assumptions.[24]

The Maloney Report sought to use a "red flags" analysis – that is, looking at indicators consistent with money laundering to then identify certain transactions as suspicious. The hope was that such an analysis might help identify the amount of money laundering that was transpiring.[25] But it proved difficult to apply broad indicators associated with money laundering to existing data sets. This was because details of real estate transactions that might qualify as red flags were often found in disparate data sources or were not readily identifiable. The authors were also unable to identify a database that identified transaction characteristics proven to be related to money laundering.

Nevertheless, the Expert Panel conducted some sample calculations of money laundering using publicly available data from the Land Title Registry and from the British Columbia Property Assessment Roll.[26] They chose three indicators easily identified in these data sets. The chosen indicators, each of which was identified as a money laundering red flag by the Financial Action Task Force, were as follows: (1) ownership of real estate by legal persons (that is, not actual people but legal constructs like companies); (2) purchase or ownership of properties without a mortgage; or (3) financing of real estate with mortgages from individuals or unregulated lenders.[27]

The Maloney Report emphasized limitations on data and time available, but concluded that the indicators of money laundering were widespread in real estate. The authors wrote:

> The overall findings are that the identified vulnerabilities occur with incidence across all geographies and property types. The incidence rate is typically higher for condominium units than for single family homes. Rates are also higher for properties with the highest assessed values. Whistler, where an extremely high share of properties are vacation properties and which draws skiers from all around North America, shows higher rates for all measures for all types of residential properties. In much the same way, commercial investment properties generally show demonstrably higher rates of incidence than do residential properties. [28]

The Expert Panel concluded that (1) beneficial ownership disclosure was needed to make ownership by legal persons a useful indicator, and (2) the other two indicators were unlikely to be useful because purchase / ownership without a mortgage was so

24 Evidence of T. Somerville, Transcript, February 18, 2021, p 90.

25 Exhibit 330, Maloney Report, pp 58–60.

26 Ibid, pp 58–60 and Appendix I, p 142.

27 Ibid, p 59.

28 Ibid, p 143.

common across the province, and there are *bona fide* legal reasons for using unregulated lenders. The authors suggested it might be necessary to combine indicators, including indicators based on data from other sources (e.g., like financial suspicious transaction reports) to narrow results.

RCMP Estimates in 2017 and 2018

There are two partial estimates of money laundering in the province made by the RCMP. In November 2017, the RCMP tried to estimate Vancouver-area property transactions linked to criminality.[29] The RCMP study used data from the Real Estate Board of Greater Vancouver. The study looked at residential properties bought in 2015–16 and valued at more than $3 million. Addresses were reviewed in the BC Online Land Titles database to identify property owners. The names of the property owners were then checked against the PRIME-BC database (a database of police records), to determine potential criminality and criminal involvement. Initial findings indicated about *10 percent of property purchasers were linked to some level of criminality* – including suspicious currency transactions, drugs (importation / production / trafficking), gaming activity, fraud, extortion, and proceeds of crime. The study did not cross-reference or validate its results against historical or current investigations, intelligence, or open or closed data sources.

In 2018, the RCMP's Federal and Serious Organized Crime unit produced a draft report estimating the value of transactions facilitated by one unlicensed, British Columbia-based money services business.[30] The data came from electronic and handwritten corporate financial ledgers, domestic bank accounts, and electronic devices (accessed by way of judicial authorization orders). The value of transactions flowing through the business approached *$1 billion per year*, a striking figure for a single money services business in BC. The RCMP acknowledged that this study had methodological limitations, particularly because of information gaps and overlaps.

Quantification Methods in the Literature

As I note above, because money laundering is an attempt to legitimize the proceeds of illegal activities, it is usually conducted in secret, which makes its estimation very difficult. Direct measurement is not possible. In this section, I briefly summarize the money laundering quantification methods from the Commission's literature review. These methods are also described in overview reports on quantification prepared by the Commission[31]

29 Exhibit 322, Overview Report: Simplified Text on Quantification of Money Laundering [OR: Quantification], para 84 and references therein.

30 Ibid.

31 Ibid; Exhibit 323, Overview Report: Quantification of Money Laundering. As set out in the Commission's Rules of Practice and Procedure, overview reports are prepared by Commission staff, circulated to all participants (who have an opportunity to correct and comment on them), finalized, and filed as evidence before me.

and in my Interim Report.[32] They are (a) the International Monetary Fund (IMF) consensus range, (b) extrapolation from capital mobility data and discrepancies, (c) extrapolation from measurements of the shadow (or underground) economy, (d) extrapolation from suspicious transaction reports or other indicators of potential money laundering, and (e) extrapolation from proceeds-of-crime data.

I have briefly summarized these five methods below.

The IMF Consensus Range

An oft-cited number in agency reports and the academic literature is that money laundering constitutes 2 to 5 percent of global GDP.[33] This range has, for some, attained the status of accepted wisdom, but on closer examination of its origin, it is more a product of rhetorical speculation than scientific rigour. The 2 to 5 percent of GDP figure originated in a 1998 speech by Michel Camdessus, who was then managing director of the IMF. Although frequently used as a reference point, the methodology used to arrive at that estimate has never been shared.[34] Questions have been raised about the applicability of the estimate in the Canadian context, as well as the continued relevance of this quantification method, given the evolution of both financial crime and the world economy in the years since Mr. Camdessus arrived at his estimation.

Extrapolation from Capital Mobility Data and Discrepancies

Several quantification methods seek to use capital mobility data to estimate the total amount of money laundering activity worldwide.[35] "Capital" in this sense means money and liquid assets (that is, assets that can be converted into cash quickly and easily). "Capital mobility" is the ability of capital to move from one country to another. The movement of capital between countries can take a few forms – for example, foreign direct investment, movement of money through portfolio flows (short-term capital), and bank transfers. These money laundering quantification methods include:

- **the hot money method**, which relies on net errors and omissions in balance of payments accounts and recorded capital outflows from the private sector, in order to estimate the total amount of money laundering activity;
- **the residual method**, which seeks to measure capital flight by looking at the difference between unrecorded inflows and outflows of funds;
- **the Dooley method**, which uses capital outflows within a country's balance of payments account and adjusts them to detect unrecorded capital outflows, using

32 Interim Report, pp 68–70.

33 Exhibit 322, OR: Quantification, paras 7–8; Interim Report, pp 68–69.

34 Evidence of B. Unger, Transcript, December 4, 2020, pp 12–13, 17.

35 For a more detailed discussion, see Exhibit 322, OR: Quantification, paras 9–18.

errors and omissions as well as changes in external debt and international market interest rates; and

- **the Global Financial Integrity method**, which uses a combination of the trade mispricing method (discussed in relation to extrapolation from suspicious transaction reports) and either the residual or the hot money method to estimate the extent of money laundering activity.

All of these methods seek to quantify the extent of money laundering using analyses of statistical discrepancies. They all suffer from data limitations and problematic assumptions that cast doubt on the reliability of the resulting estimates. The primary drawbacks of each method are as follows:

- **the hot money method**: (a) net errors and omissions data capture statistical errors in balance of payments that are difficult to separate from money laundering; (b) the method only captures a small part of illicit flows; and (c) data are missing for many countries;
- **the residual method**: (a) illegal outflows may be overestimated because some unrecorded government foreign debts come from legitimate sources; and (b) there are questions about how well the residuals reflect capital flight and to what extent capital flight (which includes, but is not limited to, money laundering and tax evasion) measures money laundering;
- **the Dooley method**: (a) data on short-term private sector capital flows required to generate the estimate are no longer available; (b) there are other data limitations and statistical problems; and (c) it may only reveal the inability of a country to attract foreign investment to compensate for external debt and may not explain the capital that has been transferred offshore for money laundering; and
- **the Global Financial Integrity method**: the same limitations that apply to the trade mispricing, residual, and hot money methods.[36]

Extrapolation from Estimates of the Shadow or Underground Economy

A third approach to quantification seeks to estimate the extent of money laundering by extrapolating from the shadow or underground economy. Methods include:

- **the currency demand method**, which compares the amount of money printed with the amount of money circulating – or compares electrical consumption (or another indicator or overall economic activity) and GDP;

36 Exhibit 322, OR: Quantification, paras 13–14, 16, 19.

- **latent variable approaches** such as the Dynamic Multiple-Indicators Multiple Causes (DYMIMC) model, which seeks to use two sets of observable variables to estimate the total amount of money laundering within a particular jurisdiction; and
- **the two sector / general equilibrium model**, which uses economic theory to estimate the value of the underground economy as a measure of money laundering.

Among the criticisms of these approaches is the fact that not all activity in the shadow or underground economy constitutes money laundering. This can lead to a significant overestimate of the amount of money being laundered through the economy.[37] Further criticisms of these approaches include: (a) the currency demand model does not account for the use of the regular financial or trade systems to launder money even though cash is not the only way, or perhaps no longer the predominant way, of holding illegal money; (b) the DYMIMC model uses values from other estimations, and uses arbitrary variables, which are not empirically based; and (c) the theoretical reasoning underpinning the equilibrium model requires simplification and abstraction to such an extent that it is removed from reality, and the model relies on a variety of assumptions without observed data.[38]

Extrapolation from Suspicious Transaction Reports and Other Indicators of Money Laundering

A fourth approach to quantification seeks to estimate the total amount of money laundering by extrapolating from suspicious transaction reports (STRs) and other indicators of money laundering.[39]

STRs are not always indicative of money laundering activity. In many cases, STRs are filed in respect of legitimate financial transactions that are not related to money laundering.[40] The method is also under-inclusive because it is well recognized that many suspicious transactions escape the notice of reporting entities. Another problem relates to the fact that multiple reports can be filed in respect of the same funds, leading to double or even triple counting.[41] Finally, STRs are subject to multiple interpretations, and may not always include the value of the transaction.[42] Professor Reuter offered the opinion that we cannot learn anything about the effectiveness of anti–money laundering controls by comparing volumes of financial STRs:

> Q You raise the concept in this article of responsibilization, a shifting of the burden of crime control on the private sector and reporting entities. You review some figures in there about suspicious

37 Ibid, paras 20–21.

38 Ibid, paras 24–25, 29, 32.

39 Ibid, paras 33–35.

40 Ibid, para 35.

41 Ibid.

42 Ibid.

> transaction reporting in the US and Europe and the UK. And I guess this is a question for both of you and it maybe touches on the quantification question, but also on the effectiveness question, which is: what can we learn, if anything, about the effectiveness of anti–money laundering controls by comparing volumes of suspicious transaction reporting?
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> A PROF. REUTER: Okay. Well, I mean, the answer is, it is totally inappropriate to make such comparisons. I went back and read the article that Mike and I wrote with Terry Halliday about the … role of data in assessing money laundering controls, and referred back to the mutual evaluation report for Germany 10 years ago. And Germany only had 7,000 suspicious activity reports whereas back in those days, already the UK had 200,000, something like that. And the FATF [Financial Action Task Force] assessment team said, yeah, they're not … sending in enough suspicious activity reports, to which the Germans correctly said, we have a different process. That is, the bank does some preliminary investigation before sending this off, whereas in the UK system, which is what the FATF prefers, everything is sent to the Financial Investigative Unit and it's up to the FIU to sort through this very noisy set of reports. And you can say, well, why exactly would you want the public sector to take on this responsibility for the preliminary investigation? It could be done at private expense by the bank itself.[43]

The Trade Mispricing Method

Another quantification method is **the trade mispricing method**, which relies on trade data to identify anomalous transactions. (I use this term, trade mispricing, to refer to what John Zdanowicz calls over- and undervaluing and over- and under-invoicing.) I heard evidence from Dr. Zdanowicz who developed software that identifies anomalous pricing in trade data, which he says may be indicative of money laundering, tax avoidance, tax evasion, or capital flight.[44] The method estimates the extent of money laundering based on observations of abnormal pricing, such as the under-invoicing and over-invoicing of imports and exports. In 2009, Dr. Zdanowicz analyzed monthly data in the United States Merchandise Trade Data Base. He compared a country's average price of an export with the world average price for the same (as far as possible) product. He classified all transactions with a price below 5 percent or above 95 percent of the average prices as trade-based money laundering. In simple terms this approach took the farthest extremes of the transactions and considered them to indicate money laundering was occurring. The study assumed product prices were normally distributed, and that unusual prices had a criminal intention and were not

43 Evidence of P. Reuter, Transcript, June 5, 2020, p 57.

44 John Zdanowicz, Transcript, December 11, 2020, pp 121–63; Exhibit 371, TBML in Canada and BC, 2015–2019 (undated); Exhibit 372, Slide Presentation by John Zdanowicz, TBML (undated).

just errors made by customs officials. No matter how great the price fluctuations were, the model classified 10 percent of all transactions as suspicious (the upper and lower 5 percent) even though pricing within that 10 percent might arise for other reasons, like evasion of trade duties.

The trade mispricing method has some limitations: (a) there are reasons unrelated to money laundering for mis-invoicing (e.g., terrorism financing, income tax avoidance, capital flight, avoiding export surcharges, concealing illegal commissions, increases in tax subsidies[45]); (b) not all mis-invoiced trade results in a difference between export and import values; (c) trade transactions concluded by word-of-mouth or using informal financial institutions are not represented; (d) collusion between importers and exporters to fake invoices is not accounted for; and (e) estimates do not include proceeds of smuggling.[46] Also, the trade mispricing method cannot detect service-based trade-based money laundering because there is no database of these transactions.[47]

Dr. Zdanowicz says that, while some analyses of trade-based money laundering start at the macro level and then drill down to specifics (i.e., a top-down approach),[48] his method starts with the micro level and looks at every single suspicious transaction, working up to an estimate. He thinks this is a better way to estimate money laundering because it does not just measure the macro variables, but identifies actual transactions. "You're looking for a needle in a haystack, and the best thing is to start with the needles and see which needles are strange, and so I take it from that perspective."[49]

Extrapolation from Proceeds-of-Crime Data

A fifth approach to quantification involves extrapolation from proceeds-of-crime data.[50] The basic idea is that one can use proceeds-of-crime estimates reported by police and law enforcement to determine the total amount of money laundered in that jurisdiction.

No matter the specific quantification method, extrapolation from proceeds-of-crime data has three primary problems: (a) it is not known how representative police data on proceeds of crime actually are, in relation to the total amount of money laundering; (b) it depends on access to reliable quantitative data about the amount of crime and the amount of money generated by different crimes; and (c) it depends on being able to accurately estimate the percentage of the proceeds of crime that are laundered for each type of crime considered.[51]

45 Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 122, 124, 126; Exhibit 341, J. Cassara – Final Statement to the Cullen Commission, p 11.

46 Exhibit 322, OR: Quantification, para 18.

47 Evidence of J. Zdanowicz, Transcript, December 11, 2020, p 195.

48 Ibid, p 174.

49 Ibid.

50 Exhibit 322, OR: Quantification, paras 36–57.

51 Ibid, para 36.

In Professor Reuter's opinion, proceeds-of-crime estimates are *not* good proxies for estimating the volume of money laundering.[52] Despite his 2004 work, discussed in his 2007 book, Professor Schneider says that estimates of the volume of money laundering are invariably flawed, and the full extent of money laundering in Canada remains unknown.[53]

The Gravity Model

The Walker and Unger gravity model – the approach used by the authors of the Maloney Report – is a more sophisticated attempt to quantify money laundering activity using proceeds-of-crime data. The model uses this data, and econometric modelling, to estimate the total amount of money laundering activity within a particular jurisdiction.[54] The model was first developed by John Walker in 1999 using Australian crime data.[55] The basic approach is to first estimate the quantity of money laundered in each country using proceeds-of-crime data, and then model the quantity of illicit money flowing to each country.[56] The model's estimate of the amount of money laundered in each country is dependent upon its estimates of:

- the nature and extent of crime in a country;
- the proceeds of crime per reported crime and the amount laundered for each type of crime;
- the economic environment in which crimes and laundering take place; and
- variables of attractiveness and distance used in the model (meaning, attractiveness to money launderers, and distance from the source or destination country).

The first (Walker 1999) version of the model did not produce accurate estimates of money laundering flows.[57]

In 2006, Professor Unger and her colleagues modified the gravity model's distance and attractiveness indices. The model uses these variables to estimate money flowing into and out of a country to and from all other countries.[58] This version of the model was used in a 2009 paper co-authored by Professor Unger and Mr. Walker.[59] The model assumes:

- there is a global amount of crime;

52 Evidence of P. Reuter, Transcript, June 5, 2020, p 53.

53 Evidence of S. Schneider, Transcript, May 27, 2020, p 24.

54 Exhibit 322, OR: Quantification, paras 43–57.

55 Exhibit 327, John Walker, "How Big is Global Money Laundering?" (1999) 3(1) *Journal of Money Laundering Control*.

56 Exhibit 326, John Walker and Brigitte Unger, "Measuring Global Money Laundering – The Walker Gravity Model" (2009) 5 *Review of Law and Economics* [Walker Gravity Model], pp 836–37; Evidence of B. Unger, Transcript, December 4, 2020, pp 71–72.

57 Evidence of B. Unger, Transcript, December 4, 2020, pp 27–28.

58 Exhibit 326, Walker Gravity Model, pp 841–42; Evidence of B. Unger, Transcript, December 4, 2020, p 36.

59 Exhibit 326, Walker Gravity Model; Evidence of B. Unger, Transcript, December 4, 2020, p 35; Exhibit 331, United Nations Office on Drugs and Crime Research Report, *Estimating Illicit Financial Flows Resulting from Drug Trafficking and Other Transnational Organized Crimes* (October 2011).

- some proceeds of crime stay in a country, and some are sent to one or more countries;
- income from crime depends on the prevalence of different types of crime and the average proceeds per crime;
- not all money is laundered; and
- there are reasons why money is kept in a country or moved to another country.[60]

The Walker 1999 gravity model used physical distance between countries, but the Walker and Unger gravity model now considers physical distance less important for money laundering. The current model uses "distance" measures such as each country's language and colonial background, as well as geographical distance (later, religion was also added).[61] The attractiveness index was changed to include a country's financial deposits and another measure of anti–money laundering effort (whether a country is a member of the Egmont Group).[62] The Walker and Unger gravity model was used in the Maloney Report.[63]

The gravity model can be applied to all countries and jurisdictions in the world. It combines expertise from criminology, economics, and finance. But it also has several limitations.[64]

First, using proceeds of crime to estimate money laundering depends on access to reliable and abundant crime data.[65] There is likely a large margin of error in model estimates because of the lack of measured and reliable crime data. Crime reporting is uneven across countries – particularly for bribery, corruption, and tax evasion – and some transactions are not typically included in crime statistics.[66] Professor Unger spoke about this issue at the hearing. She said the use of police files and statistics as sources for proceeds-of-crime data is not feasible because the stricter the fight against money laundering, the more eagerly police record money laundering cases.[67] This dynamic means that, perversely, the more the police do to tackle money laundering, the bigger the problem will appear to be – on paper, though not in reality. Indeed, if one were to look at the number of money laundering cases pursued in British Columbia, one might incorrectly conclude that there is not a problem.

60 Exhibit 326, Walker Gravity Model, pp 835–36; Evidence of B. Unger, Transcript, December 4, 2020, pp 60–61, 64, 66, 68–69.

61 Exhibit 326, Walker Gravity Model, p 842; Evidence of B. Unger, Transcript, December 4, 2020, pp 38, 40.

62 Exhibit 326, Walker Gravity Model, pp 841–42; Evidence of B. Unger, Transcript,December 4, 2020, pp 36, 38.

63 Exhibit 330, Maloney Report, p 45.

64 Exhibit 322, OR: Quantification, paras 50–57.

65 Ibid, para 52.

66 As one example, environmental crimes may result in illegal savings that are not captured by conventional crime statistics.

67 Evidence of B. Unger, Transcript, December 4, 2020, pp 57–59.

Professor Unger also acknowledges the model's reliance on *reported* crime remains problematic.[68] She notes that even where data are available, they only reflect reported aspects of money laundering. Reported crime is different from the total amount of crime. And it stands to reason that unlike the sorts of crimes that are likely to lead to police reports (such as stolen cars, in which there are good reasons to call the police and very few reasons not to), with money laundering, it is not obvious that the police will be called even when it is suspected or detected. In addition, to be able to extrapolate from reported crime to total crime, one must know the probability of being caught.[69] Professor Unger says this is not a problem if one knows the probability of a crime being recorded; the Walker 1999 paper tried to do this.[70] Professor Reuter said reliance on crime statistics from enforcement actions (or reports by financial institutions) is not a problem if we know what fraction this represents of total money laundering. But because there is no systematic way of assessing this, he testified, we are "in the realm of making up numbers."[71] In his opinion, it is unclear with existing data how we can estimate how much money is laundered.[72] If "all we know is what's reported by enforcement agencies and financial institutions, we cannot credibly estimate the amount of money that's laundered."[73]

Second, the reliability and accuracy of the gravity model are contingent on the accuracy of the percentage of proceeds laundered for various types of crimes.[74] As noted above, the Walker and Unger gravity model uses "percent-money laundered of total proceeds of crime" estimates from Walker 1999. Using these percentages to estimate money laundered is not likely to be accurate for other countries; it may not even be accurate for Australia any longer (if it ever was). Also, some researchers have faulted Walker's use of experts (usually police officers) to estimate how much money is generated by particular crimes, and how much of it is laundered, because of their potential bias.[75] Police officers may tend to give estimates that are shaped by their training and experiences, and sometimes by their biases, rather than detached scientific estimations. And the people interviewed may have perception biases (for example, the authorities who fight money laundering may tend to overestimate it, or law enforcement and regulators who feel they are effective and efficient at combatting money laundering may tend to underestimate it). As such, the calibration of proceeds of crime for a particular offence may be flawed because the expert sample is not representative and the data sources are prone to influence.

68 Ibid, pp 28–29, 50–51, 107, 159–60.

69 Ibid, pp 51–52.

70 Ibid, pp 52, 109–10.

71 Evidence of P. Reuter, Transcript, June 5, 2020, p 49.

72 Ibid, p 50.

73 Ibid, p 50.

74 Exhibit 322, OR: Quantification, para 53.

75 Evidence of P. Reuter, Transcript, June 5, 2020, p 54.

Professor Unger acknowledged at the hearings that a crucial shortcoming with the model is its continued reliance on the Walker 1999 estimates of proceeds of crime and the amount of money laundered per crime.[76] She says that such data are non-existent outside of the Walker 1999 estimates, and so these estimates continue to be used (although now there is an adjustment for each country according to its purchasing power). Professor Reuter says the Walker 1999 estimates of total revenues – generated by drug sales and the proportion requiring laundering – has no empirical foundation.[77] In his view, one needs at least a series of case studies where drug dealers talk about how they handle their money, and he has never seen any such database.[78] This means that weak data and a series of assumptions and approximations serve as the foundation for proceeds of crime–based money laundering estimates. Professor Michael Levi agrees.[79] He says the Walker and Unger gravity model is not useful in terms of estimating money laundering, although it may be useful for thinking about the process of where money goes, what jurisdictions are attractive to money launderings, and the extent to which money launderers and criminals simply move countries and carry on.

Third, the Walker and Unger gravity model is not underpinned by any economic theory. An economic foundation requires understanding the behaviour of money launderers, including what makes them send their money to a specific country.[80]

Fourth, there are problems with the model's mathematical specifications when they are applied domestically.[81] Model parameters that may work when applied across a range of countries in the world may be less accurate when applied to a subset of countries or regions. For example, while parameters based on economic data will vary across Canada, other parameters (e.g., the rule of law and the banking system) do not differ. In the Expert Panel Report, this meant parameters like provincial GDP and crime rates end up having greater weight than do non-economic parameters. There is a further problem of a statistical nature: the frequency distribution of criminal income is skewed. There are likely to be many low-income criminals but only a few high earners. Extrapolating from the arithmetic mean, in this situation, is likely to prove inaccurate.

76 Evidence of B. Unger, Transcript, December 4, 2020, pp 28–29, 50–51, 53, 72, 159–60.

77 Evidence of P. Reuter, Transcript, June 5, 2020, p 53.

78 Ibid, pp 53–54.

79 Evidence of M. Levi, Transcript, June 5, 2020, pp 54–55.

80 Exhibit 322, OR: Quantification, para 54.

81 Ibid, paras 55–56.

Finally, the gravity model does not work for estimating trade-based money laundering.[82]

Despite the criticisms, Professor Unger thinks the Walker and Unger gravity model performs well in estimating money laundering activity.[83] She acknowledged that some people believe that estimates have nothing to do with the truth. But, she said, if you focus only on "the truth," that is, the specific counts of measured money laundering, you can make a bigger mistake than trying to estimate the total size of the problem.[84] Professors Reuter and Levi disagree.[85] They say that the range of plausible estimates is so large that it will not provide guidance to decision-makers. If one cares about whether the amount of money laundering is getting larger or smaller, given the margins of error with the gravity model, you cannot answer such questions about expansion or shrinkage.[86]

In a 2020 study with Utrecht University colleagues, Professor Unger estimated there was US$37.8 billion laundered annually in Canada.[87] The largest component was domestic criminal money.[88] While flowthrough was also high, money from foreign countries that settles in Canada is lower than Professor Unger would have thought.[89] However, she thought the results for Canada are not realistic because proceeds-of-crime data from China are heavily underestimated.[90]

The Commission's Quantification Efforts

Quantification, despite its obvious challenges, holds out promise. If achieved with some measure of accuracy, quantification offers a way of understanding the scope of the money laundering problem. It also provides a useful yardstick with which to

82 Evidence of B. Unger, Transcript, December 4, 2020, p 146; Exhibit 332, Joras Ferwerda, Mark Kattenberg, Han-Hsin Chang, Brigitte Unger, Loek Groot and Jacob A. Bikker, "Gravity Models of Trade-Based Money Laundering" (2013) 45(22) *Applied Economics*. I would also comment on one further criticism of the Walker and Unger gravity model: its dependence on "attractiveness" and "distance" indicators to refer to how appealing the foreign jurisdiction will be as a destination, because of cultural and linguistic similarity and proximity. These indicators were said to be arbitrarily weighted and not based on facts. In response to such criticisms, Professor Unger and her colleagues published a 2020 paper that instead used a data set of Dutch suspicious transactions to serve as a proxy for the amount of money laundering to estimate the coefficients of "attractiveness" and "distance." See Exhibit 329, Slides – Scientific Reports 2020 (B. Unger, J. Ferwerda, M. Getzner, A. van Saase); Exhibit 328, Joras Ferwerda, Alexander van Saase, Brigitte Unger, and Michael Getzner, "Estimating Money Laundering Flows with a Gravity Model-Based Simulation" (2020) 10 *Scientific Reports*; Evidence of B. Unger, Transcript, December 4, 2020, pp 25, 30, 34, 40; Exhibit 326, Walker Gravity Model, pp 849–50; Exhibit 322, OR: Quantification, para 57.

83 Evidence of B. Unger Transcript, December 4, 2020, pp 105, 107.

84 Ibid, pp 110–11.

85 Evidence of P. Reuter, Transcript, June 5, 2020, pp 53–54; Evidence of M. Levi, Transcript, June 5, 2020, p 54–55.

86 Evidence of P. Reuter, Transcript, June 5, 2020, p 54.

87 Exhibit 328, Ferwerda et al, "Estimating Money Laundering Flows with a Gravity Model-Based Simulation," p 6; Exhibit 329, Slides – Scientific Reports 2020 (B. Unger, J. Ferwerda, M. Getzner, A. van Saase); Evidence of B. Unger, December 4, 2020, p 90.

88 Exhibit 328, Ferwerda et al, "Estimating Money Laundering Flows with a Gravity Model-Based Simulation," p 6; Evidence of B. Unger, December 4, 2020, p 90.

89 Evidence of B. Unger, December 4, 2020, pp 90–91.

90 Ibid, pp 91–92.

assess the success of anti–money laundering initiatives. With a view to ascertaining if quantification of money laundering in this province could be done, the Commission undertook some independent research, which I turn to next.

Bouchard Report

The fentanyl crisis in this province is a matter of grave concern to British Columbians. This pernicious drug trade has generated staggering levels of criminal proceeds for those engaged in the trade, just as it has put the lives of British Columbians at risk. Given the close connection of this crisis to British Columbia and its obvious role in generating significant criminal proceeds that must be laundered, the Commission enlisted the assistance of Dr. Martin Bouchard, a professor of criminology at Simon Fraser University, to supervise a study. He sought to quantify the illicit proceeds derived from the sale of fentanyl in British Columbia.[91] His team analyzed data collected by the British Columbia Centre on Substance Use, in order to calculate the proceeds derived from the sale of fentanyl in British Columbia. In a simple way, he sought to determine the size of the fentanyl trade in terms of dollars spent. An estimate of money laundering requires real data, and this study had as its goal to furnish a data point. (From this figure, it may be possible to then determine what amount of money from fentanyl dealing would be laundered in a given year.)

In this study, Dr. Bouchard and his colleagues calculated the size of the fentanyl market based on data as to the frequency of use of fentanyl (or fentanyl-contaminated opioids or stimulants) in Vancouver's Downtown Eastside. Then, these results were extrapolated to the entire province.[92] The study estimates the amount (in grams) of fentanyl use per day. Next, using prices for fentanyl obtained from the Vancouver Police Department, it calculates a "dollar amount spent per day" for each type of user.

Bouchard et al. estimate retail expenditures at $200 to $300 million per year.[93] They conclude this amount is quite conservative, and it may be a "floor" to market size estimates.[94] In particular, the authors could not determine the extent to which bartering for drugs may have altered the estimate.[95] At the hearings, Dr. Bouchard and Dr. Michael-John Milloy explained to me that, in order to improve estimates of fentanyl market size, they would need more information: specific spending behaviour data; data from other regions in British Columbia; purity data on fentanyl; better measures of drug consumption; and information on what dealers are doing with their revenues.[96] (Both

91 Exhibit 335, Martin Bouchard, Mitch Macdonald, Carlos Ponce, M-J Milloy, Kanna Hayashi, and Kora DeBeck, Research Report: Estimating the Size of the Fentanyl Market in British Columbia (October 26, 2020) [Bouchard Report], p 1; Evidence of M. Bouchard and M-J Milloy, Transcript, December 7, 2020, pp 6–7.

92 Exhibit 335, Bouchard Report, p 1; Evidence of M. Bouchard, Transcript, December 7, 2020, pp 8–10.

93 Exhibit 335, Bouchard Report, p 5; Evidence of M. Bouchard, Transcript, December 7, 2020, pp 10, 95.

94 Evidence of M. Bouchard, Transcript, December 7, 2020, pp 102–3.

95 Evidence of M-J Milloy, Transcript, December 7, 2020, pp 105–6.

96 Evidence of M. Bouchard, Transcript, December 7, 2020, pp 111–14; Evidence of M-J Milloy, Transcript, December 7, 2020, p 121.

Dr. Bouchard and Dr. Milloy were frank to say there was absolutely no data available about what dealers are doing with their sales proceeds.[97])

Reuter and Caulkins White Paper

As outlined, the Bouchard Report sought to determine expenditures on (or, put differently, revenue from) fentanyl drug use in British Columbia. The authors were clear that obtaining *revenue* figures would not indicate how much of that revenue would be *laundered*[98] – in other words, how much of the revenue could be counted to measure the quantum of money laundering arising from this drug trade.

With a view to helping tackle that question, the Commission obtained an expert opinion from Professor Reuter and Professor Jonathan Caulkins. Their paper, which I refer to as the White Paper, sought to answer how one might determine the percentage of illegal drug trade proceeds that are laundered.[99] To be clear, the White Paper does not (and did not try to) estimate the share or percentage of the British Columbia illegal drug market that is laundered. Rather the authors came up with a computational framework. The idea was that, once it was possible to obtain empirical estimates of key parameters, they could be inserted into their framework.[100] And the framework would then produce dollar values of money laundered per year in that drug market.

The framework is a way to model the relationship of a drug market's total retail sales to the amount of money at various levels of the distribution chain, which may need laundering. The aim is to identify the key variables for a specific market, and likewise to identify the sources of data that could be used to try to estimate those variables.[101]

Before coming up with their model, the authors canvassed the literature to identify studies that addressed the proportion of illegal drug revenue that is ultimately laundered.[102] However, they could not find any systematic effort to distinguish between drug revenues and drug money laundering.[103]

The model developed by Professors Reuter and Caulkins suggests that only 25 to 50 percent of what heroin users spend in British Columbia would need to be laundered.[104] Their paper suggests that the laundering needs vary depending on the position or level of the drug dealer. The model suggests that most street-level dealer revenue is laundered by paying the everyday living expenses of the dealer, and by higher-level dealers by paying

97 Evidence of M. Bouchard, Transcript, December 7, 2020, pp 113–14.

98 Exhibit 335, Bouchard Report, pp 5–6.

99 Exhibit 337, Jonathan Caulkins and Peter Reuter, White Paper on Relating the Size of Illegal Markets to Associated Amounts of Money Laundered (November 19, 2020) [White Paper]; Evidence of J. Caulkins, Transcript, December 8, 2020, p 10.

100 Exhibit 337, White Paper, p 3.

101 Evidence of J. Caulkins, Transcript, December 8, 2020, p 10.

102 Evidence of P. Reuter, Transcript, December 8, 2020, pp 21–22.

103 Ibid.

104 Exhibit 337, White Paper, p 3.

their employees.[105] In some instances the amount of money left in the hands of dealers may be even less than the White Paper assumed, because of in-kind purchases using stolen goods, trades for services, self-dealing, and less than full-time dealing.[106] First-level wholesaler earnings may be laundered without recourse to highly skilled specialists.[107] A relatively small number of people at the top of British Columbia's drug distribution networks earn enough money to need more formal money laundering approaches; this may not be more than 10 percent of what users spend on drugs. (This figure refers to the upper echelon of dealers, whose profits are big enough to justify more sophisticated money laundering techniques.) A further 10 percent of what users spend on drugs may be paid to foreign suppliers, and this money is prime for laundering through the "Vancouver model."[108] However, the authors acknowledge the amounts wholesalers or importers may need to launder is very much in the "realm of guessing."[109]

While the model's numbers are not exact, they serve the White Paper's goal of showing what information is needed in order to estimate money laundering demand as a proportion of the money users spend on drugs.[110] The authors suggest this information can be learned from undercover purchases, forensic lab testing, police wiretaps, court documents, and interviews with higher level traffickers.[111] Other sources of data include surveys of drug users, as well as ethnographic studies, and interviews of retail drug sellers.

The authors assessed the relationship between how drug dealers must launder cash and their ability to spend it.[112] This analysis showed that if criminals have trouble spending cash, then most of the demand for money laundering services will come from the large number of lower-level dealers and staff.[113] Conversely, if it is easy to spend cash, then only the relatively small number of higher-level dealers – the big timers – will make so much money they need to purchase money laundering services. The study also emphasized the need to determine how drug prices change when one moves up or down the ladder of dealers: how does the price change when it goes from the mid-level supplier or "road boss" to a low-level street dealer, and hence, how much profit does each level of dealer make?

Overall, the authors say the "take home" message from their model and analyses is that a modest research program to better understand prices at each market level can pay big dividends. It can improve our understanding about how much money is retained at each market level, and in turn shed light on how much money might need to be laundered informally (for retailers and wholesalers) and professionally (for importers and suppliers).[114]

105 Exhibit 337, White Paper, p 7; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 40–41.
106 Evidence of J. Caulkins, Transcript, December 8, 2020, pp 41–42.
107 Exhibit 337, White Paper, p 7.
108 Ibid, pp 7 and 12.
109 Evidence of J. Caulkins, Transcript, December 8, 2020, p 44.
110 Exhibit 337, White Paper, p 7.
111 Ibid, p 7, 21–23.
112 Ibid, pp 7–13; Evidence of J. Caulkins, Transcript, December 8, 2020, p 47–48.
113 Exhibit 337, White Paper, p 9; Evidence of J. Caulkins, Transcript, December 8, 2020, p 48.
114 Exhibit 337, White Paper, p 13.

Professors Reuter and Caulkins also discuss a theoretical model that explains what they see with their computational framework.[115] This is the "risks and prices" model. The model suggests that most of the cash dealers receive, above their business and labour expenses, represents *compensation for risks*.[116] The model assumes that mature drug markets are typically in equilibrium (i.e., prices at each market level are reasonably stable and uniform); prices are justified (i.e., increments in prices from one level to the next represent fair compensation for effort and risks); and the market is not "free entry," with anyone bidding down prices (because of non-monetary costs such as the risk of arrest or violence).[117]

The "risks and prices model" helps explain why so much of illegal drug trade proceeds remain at the retail levels. It can inform how we think about ways of changing the demand for money laundering services.[118]

The White Paper suggests prescription opioid abuse and dependence probably has very little direct effect on the demand for money laundering.[119] Generally, there are no higher levels in the distribution chain, because drugs are sourced at low levels in the chain. The more people who use prescription opioids, the more likely they will "trade down" and go to the illegal market for opioids like heroin or fentanyl, so the increase in prescription opioids may over time increase the total demand and size of the "down" (heroin plus other depressant hard drugs) market.[120] The White Paper computational framework can account for this change, which is just an increase in total demand, which would scale up all the output numbers.[121] The proportions of user spending that need to be laundered does not change.

The impact of the fentanyl and synthetic opioid market on the White Paper model is not yet clear. To date, there is not a noticeable difference in the user price of heroin as compared to fentanyl.[122] However, fentanyl is about 25 times more potent per unit mass than heroin and may be about 90 percent less expensive per unit mass, so, according to the White Paper authors, there should be an impact on the heroin supply chain.[123] The authors look at two possible ways the entry of fentanyl into the opioid market might impact their computational framework.[124]

Under an additive model, with the entry of fentanyl into the opioid market, importers do not have to pay foreign suppliers as much money, but there are no other

115 Ibid, pp 14–16.
116 Ibid, p 15.
117 Ibid, p 14.
118 Ibid, pp 15–16; Evidence of P. Reuter, Transcript, December 8, 2020, pp 64–65.
119 Exhibit 337, White Paper, p 17; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 71, 73.
120 Evidence of J. Caulkins, Transcript, December 8, 2020, pp 72–73.
121 Ibid, p 73.
122 Ibid, pp 77, 82, 84–85.
123 Ibid, p 78.
124 Ibid, pp 86–87.

price changes.[125] This means there are no changes for wholesalers or retailers in terms of their demand for money laundering. The amount of money going to foreign suppliers is less, so they have less demand for money laundering and importers' net income increases sizably, as does their need for money laundering.[126] This outcome would not be likely five to 10 years from now because eventually the market would respond, although this could be particularly slow at the importer level because there are relatively few players, and these people have some specialized skills.[127]

Under a multiplicative model, all prices in the supply chain fall by the same amount and retailers, wholesalers, and importers are back to where they were in terms of the proportions of user money that each retains.[128] As total cash revenues for everyone decrease, the total market worth is much smaller, and everyone can spend more of the cash they get. This means the demand for money laundering largely goes away, especially at the dealer level.[129] Foreign suppliers would get 12 to 25 percent of what users spend on drugs, but that amount in absolute dollars would be much smaller.[130]

The authors briefly canvass other illegal markets (cocaine and other traditional expensive drug markets, drug markets in other provinces, prostitution and human trafficking, and wildlife trafficking) and consider whether their computational framework would have to be modified if it were to be used in understanding money laundering in these markets.[131] Professors Reuter and Caulkins conclude their model would likely apply to cocaine, crack cocaine, and methamphetamine markets, but not to the illegal cannabis market.[132]

Whether British Columbia launders much of the criminal cash generated in central or eastern Canada might depend on whether the cost to move cash cross-country is more like the cost of shipping everyday items, or more like the cost of transporting illegal cannabis during prohibition.[133] The initial analysis of prostitution and human trafficking markets suggests the structure of money flows is different than for heroin or other expensive drugs, and the authors speculate there may be a greater demand for money laundering services from pimps, rather than from higher-level traffickers.[134]

Finally, Professors Reuter and Caulkins say that if the challenges in converting the illegal drug market to a cashless system are overcome, and net revenues are in electronic form, it might change the type of money laundering occurring, but not the amount of money laundering.[135] Going cashless would convert the money laundering

125 Ibid, pp 87–88.
126 Exhibit 337, White Paper, p 19; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 87–88.
127 Evidence of J. Caulkins, Transcript, December 8, 2020, p 88.
128 Exhibit 337, White Paper, p 19; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 89, 92.
129 Exhibit 337, White Paper, p 19; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 89, 92.
130 Exhibit 337, White Paper, p 19.
131 Ibid, pp 24–28.
132 Ibid, pp 24–26.
133 Ibid, pp 26–27.
134 Ibid, pp 27–28.
135 Ibid, p 32.

problem of drug dealers into the money laundering problem already typical of most other beneficiaries of large and regular criminal revenues. One impact of this would be to increase the demand for money laundering services at lower levels of the illegal drug supply chain.[136]

The authors conclude the two central insights from the White Paper are: (1) only a minority of the money that drug users spend in British Columbia needs to be laundered in the more professional sense because street-level dealers spend most illegal drug market revenue; and (2) the proportions of the money retained at each level in the distribution chain are driven by the prices at each level and/or the price markups from one level to the next.[137] Professor Reuter suggests the first insight indicates that anti–money laundering efforts would have more of an effect at the higher levels of the supply chain.[138] Another insight from the White Paper is that each specific market must be considered separately.[139] The model also gives a general sense of the potential scale of money laundering in the heroin market.[140]

To populate the White Paper computational framework with real numbers, the following is required:

- total value of the drug market (e.g., by demand-side estimates like the Bouchard Report; supply-side estimates if available; waste water monitoring methods[141]);[142]
- prices at various market levels;[143]
- cash spending by various actors in the supply chain;[144] and
- branching factors – how many people are involved with each level of the distribution chain and how many levels are in the chain.[145]

To obtain good information, in addition to the sort of interviewing work noted earlier, Professor Reuter thinks it would be very useful to have research criminologists working for the RCMP, because law enforcement priorities are different than what economists or criminologists would prioritize for information gathering.[146] For spending

136 Evidence of P. Reuter, Transcript, December 8, 2020, pp 122–23.

137 Evidence of J. Caulkins, Transcript, December 8, 2020, pp 26, 28.

138 Ibid, pp 45–46.

139 Ibid, p 107.

140 Exhibit 337, White Paper, p 3.

141 Waste water monitoring is, as the name suggests, a method that tests sewage and waste water chemically, to measure the prevalence of drug-use by-products or residue. (It has been used recently to determine COVID-19 exposure.) In this context, such studies give data about the use of various drugs in a particular area or community.

142 Exhibit 337, White Paper, pp 3, 20–21; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 95, 97.

143 Exhibit 337, White Paper, pp 3, 20–21; Evidence of P. Reuter, Transcript, December 8, 2020, pp 97, 99.

144 Exhibit 337, White Paper, pp 3, 20–21; Evidence of P. Reuter, Transcript, December 8, 2020, pp 101, 103.

145 Exhibit 337, White Paper, pp 3, 20–21; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 103–4.

146 Evidence of P. Reuter, Transcript, December 8, 2020, pp 98–100, 105.

habits at different levels of the distribution chain, such information would have to come from investigations and perhaps from interviews. However, Professor Reuter is not sure these data would allow for generalizations.[147] Professor Caulkins is more optimistic.[148]

Zdanowicz Trade Mispricing Estimates

Dr. John Zdanowicz is Professor Emeritus of Finance at Florida International University, and a pioneer in the research of illicit financial flows through international trade. He is a consultant working for various government, law enforcement, and financial organizations.[149] As noted above, he developed a method to examine US trade data to detect and measure the flow of illicit funds or trade-based money laundering.[150] The Financial Action Task Force and Dr. Zdanowicz define trade-based money laundering as the process of disguising the proceeds of crime and moving value using trade.[151] I discuss trade-based money laundering, and indeed Dr. Zdanowicz's work, in considerably more detail in Chapter 38.

There are no known official estimates of the global or country-specific magnitude of trade-based money laundering.[152] In John Cassara's opinion, because the issue impacts national security, the integrity of the global financial system, law enforcement, and the collection of national revenue, it is remarkable that trade-based money laundering has not been systematically examined.[153] According to Global Financial Integrity, trade mis-invoicing accounts for nearly 80 percent of all illicit financial outflows that can be measured with available data.[154]

The Commission was able to obtain Canadian trade data from Statistics Canada for between 2015 and October 2020. The Commission provided this data to Dr. Zdanowicz, who applied his trade mispricing method to it. Dr. Zdanowicz produced several reports for the Commission and testified before me. He explained how, in order to move money *out of a country* undetected, a person can undervalue exports or overvalue imports. To move money *into a country* undetected, one can overvalue exports and undervalue imports. When Dr. Zdanowicz's trade mispricing method detects a suspicious export or import price, there are three plausible and mutually exclusive explanations: (1) the price is right, (2) the price is wrong, or (3) the price is abnormal.[155] If abnormal, then the price anomaly likely indicates money laundering.

147 Ibid, pp 101–102.

148 Evidence of J. Caulkins, Transcript, December 8, 2020, pp 102–3.

149 Evidence of J. Zdanowicz, Transcript, December 11, 2020, p 106.

150 Ibid, p 111.

151 Ibid, pp 121–22.

152 Exhibit 341, J. Cassara – Final Statement to the Cullen Commission, p 11.

153 Ibid, p 11.

154 Ibid, p 11, citing "The Economist Highlights the Scourge of Trade Mis-invoicing," *Global Financial Integrity* (May 2, 2014), online: https://financialtransparency.org/the-economist-highlights-the-scourge-of-trade-misinvoicing/.

155 Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 161–62.

Dr. Zdanowicz produced "macro reports" showing the amount of money potentially moved in and out of Canada and each province from 2015 to 2019.[156] For example, his 2019 macro report shows undervalued exports from Canada totalling $45 billion and overvalued imports into Canada totalling $44 billion, for a total of $90 billion moved out of Canada.[157] Total money moved into Canada through overvalued experts and undervalued imports was $144 billion. For British Columbia, he estimates $8 billion in undervalued exports and overvalued imports moving out of the province[158] and $16.5 billion moved into the province.[159]

Dr. Zdanowicz's "micro reports" look at the annual data in detail.[160] This involved examining all the transactions falling into the 5th and 95th percentiles of average country price (his "international price profiling system") and drilling down to the product being shipped, its description, province, quantity, units of measure, and total value of the shipment. By determining the price per unit of suspicious transactions, and generating the difference between this amount and the average price per unit for that type of product, he estimated the amount of suspicious money being moved into or out of British Columbia.[161] The micro report for 2019 identifies 10,000 suspicious transactions of overvalued imports, undervalued exports, undervalued imports, and overvalued exports.[162]

Dr. Zdanowicz concludes there are quite a few suspicious trade transactions in Canada and British Columbia, which would concern a bank in terms of financing and would be something regulatory or law enforcement should look at.[163] In his opinion, those interested in preventing money laundering should be looking at statistical analyses of the trade database because this can help detect, investigate, and mitigate trade-based money laundering.[164] The data can allow law enforcement to evaluate in real time the nature of a transaction and determine whether it is anomalous.[165] For example, Canada has trade data with exporter and importer names (names that can be ascribed to the data and transactions identified through the Zdanowicz method), and so Canada could run an analysis to identify companies and individuals routinely conducting anomalous trade transactions or even generate

156 Ibid, pp 114–15; Exhibit 362, Canada International Trade Pricing Analysis 2015; Exhibit 363, Canada International Trade Pricing Analysis 2016; Exhibit 364, Canada International Trade Pricing Analysis 2017; Exhibit 365, Canada International Trade Pricing Analysis 2018; Exhibit 366, Canada International Trade Pricing Analysis 2019 [Trade Analysis 2019].

157 Exhibit 366, Trade Analysis 2019; Evidence of J. Zdanowicz, Transcript, December 11, 2020, p 167.

158 Exhibit 366, Trade Analysis 2019; Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 168–69.

159 Exhibit 366, Trade Analysis 2019.

160 Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 116–17; Exhibit 367, Excel Spreadsheet, BC Money In – Exports Over 2019; Exhibit 368, Excel Spreadsheet, BC Money In – Imports Under 2019; Exhibit 369, Excel Spreadsheet, BC Money Out – Imports Over 2019; Exhibit 370, Excel Spreadsheet, BC Money Out – Exports Under 2019.

161 Evidence of J. Zdanowicz, Transcript, December 11, 2020, p 117.

162 Ibid, pp 170, 189.

163 Ibid, pp 114–15.

164 Ibid, pp 143, 172.

165 Ibid, pp 176–77.

a list of companies and individuals with the highest dollar value of anomalous transactions for British Columbia.[166]

While Dr. Zdanowicz's trade mispricing work yields significant insights and information – as I discuss in detail in Chapter 38 – it does not (and does not try to) produce a total amount of money laundered in British Columbia, and it does not consider illicit funds generated in this province. Nonetheless, this sort of analysis has relevance to quantification, as it may furnish a strong indication of the magnitude of trade-based money laundering activity engaging this province and Canada generally.

Conclusion on Extent of Money Laundering in BC

I conclude that it is not possible to determine with precision the amount of money laundered in British Columbia in terms of a dollar value. Each quantification method has its own challenges and limitations. No single method on its own provides a reliable and accurate estimate. All the methods are based on multiple assumptions and generally lack reliable data.

Nevertheless, considering collectively all the information from these various imperfect methods, together with the body of evidence before me and the literature, I am left with no uncertainty about whether money laundering is a problem. Very substantial amounts of illicit funds are laundered through, and in, the British Columbia economy. The problem warrants significant attention at a number of levels. To my mind, it would be foolish to wait, doing nothing in the vain hope that someday a formula will yield a precise calculation and hoping things are not as serious as they appear to be. Without being able to say how large the money laundering problem is in this province, I have no hesitation concluding that it is large indeed, and it merits strong and immediate action.

Based on the evidence and analyses described above, there is consistent support for the general conclusion that vast amounts of money are laundered in British Columbia every year. Even though the methods of quantifying money laundering are diverse (they differ both in method of analysis and data inputs), they share in common the basic point: this is a large problem.

To put it the other way around, none of the attempted estimates suggest that this is a non-issue – or that the amount of money laundered in the province is miniscule, such that the problem is not worth focusing on.

In support of this, I would highlight these conclusions from the quantification attempts I have discussed in this chapter:

- **As a matter of inexorable logic**, given the manner in which organized crime occurs, profitable crimes generate dirty money that needs to be cleaned. If there are

166 Ibid, pp 189, 177–178.

proceeds of crime beyond what can be spent on daily living and so-called "business" expenses, then excess monies will be laundered in some way. These "excess earnings" are illicit, but the criminal will seek to have the dirty money acquire the appearance of legitimacy, and that means he or she will launder it. It is not hard to conclude that, for numerous profitable crimes like drug dealing, money laundering will result, and it goes hand-in-hand with the crime itself.

- **Combining the Bouchard Report with the Reuter and Caulkins White Paper**, it becomes apparent that a large amount of drug money will be laundered every year in British Columbia.

    - First, the Bouchard Report illustrates the magnitude of the money generated in just one product in one corner of the criminal economy. The study conservatively estimates that expenditures in the province's fentanyl market amount to $200 to $300 million per year.[167]

    - Secondly, the White Paper work on the province's heroin market, and the amount of money moving through the provincial heroin distribution lane, can be layered onto the fentanyl estimates. If 25 to 50 percent of the expenditures (revenue) from fentanyl dealing need to be laundered, then taking the $200 to $300 million figure, the result ranges from $50 to $150 million per year that will be laundered from fentanyl sales alone.[168] That figure relates to only one product amid a wide array of drugs, as well as other criminal activities in this province. While that is a broad range, it demonstrates that a significant volume of money is laundered, all the more so when one steps back to think not just about fentanyl, but other drugs, other profit-driven crimes, and proceeds of crime from outside the province.

- **The gravity model**, despite its flaws and assumptions, suggests a massive problem – an iceberg largely under the waterline. Although Professor Somerville testified the Maloney Report estimates of money laundering in British Columbia (and in real estate) are very uncertain, in my view, although imprecise, they do provide some insight into the order of magnitude of the problem, and they suggest it is massive. The Maloney Report estimated annual money laundering activity in Canada in 2015 at $41.3 billion and in 2018 at $46.7 billion.[169] For British Columbia, estimates for 2015 and 2018 were $6.3 billion and $7.4 billion, respectively.[170]

- To similar effect, **RCMP estimates** in 2017 and 2018 suggest the same conclusion: that the extent of money laundering in BC is significant.[171] With respect to

167 Exhibit 335, Bouchard Report, p 5; Evidence of M. Bouchard, Transcript, December 7, 2020, pp 10, 95.

168 Exhibit 337, White Paper, p 3.

169 Exhibit 330, Maloney Report, pp 1, 47–48.

170 Interestingly, to go back to the "finger in the wind" estimate of 2 to 5 percent of GDP (the IMF figure), out of a provincial GDP of approximately $309 billion per year in 2019, the 2018 gravity model estimates the amount to more than 2 percent of the province's GDP.

171 Exhibit 322, OR: Quantification, para 85 and references therein.

Silver International and RCMP Project E-Pirate, there is a body of evidence that I have outlined above and detailed elsewhere in this Report suggesting that a single British Columbia money services business was handling questionable transactions approaching a staggering $220 million per year.[172] This computation about one gaming-related investigation does not establish the extent of money laundering in the province generally involving gaming or money services businesses. But it certainly supports the conclusion that a very significant amount of illicit funds may be moved through sophisticated money laundering schemes operating in this province.

- **Dr. Zdanowicz's work** focusing on trade transactions supports this point too. It indicates that in 2019 there were suspicious trade transactions of up to $8 billion moved out of the province and $16.5 billion moved into the province.[173] His micro report for 2019 identifies 10,000 suspicious trade transactions in the province that may be related to money laundering.[174]
- **The 2020 Ferwerda et al. study** estimates that US$37.8 billion is laundered every year in Canada.[175] The largest component is domestic criminal money.[176]

All these very different studies and analyses support the same basic conclusion: that *the amount of money laundered in this province is enormous.*

In Chapter 5, I address the question of whether money laundering is a problem worth addressing. It is. There are innumerable ways that money laundering has a severe negative impact on the social and economic well-being of our communities – as well as on the province's reputation.[177]

Our federal and provincial governments appear to be in agreement with these points. Canada, in its submission to me, says that, while a precise quantification of the money laundering threat has proven elusive, there is a strong international consensus that it is an important policy problem, and that it requires a coordinated international response.[178] The Province submits:[179]

172 Ibid; Exhibit 663, Affidavit of Cpl. Melvin Chizawsky made on February 4, 2021, paras 98–106; Evidence of M. Chizawsky, Transcript, March 1, 2021, pp 94–98; Evidence of C. Chrustie, Transcript, March 29, 2021, pp 66–70. For a full discussion of these numbers and projections, including the manner in which they were generated, see Chapter 3.

173 Exhibit 366, Canada International Trade Pricing Analysis 2019; Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 168–69.

174 Evidence of J. Zdanowicz, Transcript, December 11, 2020, pp 170, 189.

175 Evidence of B. Unger, December 4, 2020, p 90.

176 Ibid.

177 Exhibit 330, Maloney Report, p 1; Exhibit 821, A Resourcing Overview of Major Money Laundering Investigations in BC, prepared by RCMP "E" Division in partnership with CFSEU-BC's Strategic Research Office, p 6; Exhibit 803, Doug LePard and Catherine Tait, Review of the Joint Illegal Gaming Investigation Team (JIGIT) (November 2020), pp 131–32.

178 Closing submissions, Government of Canada, p 4, para 11.

179 Closing submissions (other than gaming sector), Government of British Columbia, p 2, para 3.

> While the scope of money laundering is difficult to measure, the social and economic harms caused by money laundering and its underlying predicate crimes are well-known and wide-reaching. There is a human cost to money laundering, and it undoubtedly impacts the lives of British Columbians.

Ultimately, though evasive of any precise quantification, I find it inarguable that money laundering in British Columbia is a significant problem. Canada says that the lack of an exact dollar value assigned to money laundering should not prevent action.[180] The Province urges that risks and vulnerabilities need to be addressed. I agree.

Improving Money Laundering Estimates

Many witnesses spoke about the problem, and indeed the impossibility, of accurate money laundering estimates. For example, the Criminal Intelligence Service Canada has not tried to quantify money laundering in Canada because it has proven to be "extremely difficult."[181] The agency closely follows estimates made by others, but only for contextual background given uncertainty in the estimates.[182] Below, I offer comments as to how to improve estimates of money laundering.

Although scientific precision may be unattainable, even partial success in determining the quantity of money laundering in the province is worth pursuing. Having an understanding of the volume of money laundering will be useful – both to appreciate the size of the problem, and to assess the effectiveness of policy and operational reforms.

Emerging from the evidence, there are a few avenues for quantifying money laundering that, I conclude, hold promise, and which I encourage the Province (and Canada) to pursue.

One course is to focus on developing market-specific estimates of money laundering. An example of this is the Walker 2011 work for the United Nations Office on Drugs and Crime, which estimates illicit financial flows resulting from drug trafficking and other transnational organized crimes.[183]

Another route worthy of attention is to develop the work described in the Reuter and Caulkins White Paper. In Professor Reuter's opinion, it is unclear, based on existing data, how we can estimate how much money is laundered.[184] However, if we restrict estimates to specific activities, then there *are* indirect ways of estimating the problem – such as by estimating the size of the drug market, using price data to estimate revenue and then, making use of data on spending, working out how much of illegal revenues

180 Closing submissions, Government of Canada, p 8, para 24.

181 Evidence of R. Gilchrist, Transcript, June 9, 2020, p 40.

182 Ibid.

183 Exhibit 331, UNODC, *Estimating Illicit Financial Flows* (October 2011).

184 Evidence of P. Reuter, Transcript, June 5, 2020, p 50.

need to be laundered.[185] The White Paper may provide a roadmap for further attempts at quantification with respect to profits derived from the drug trade in British Columbia and other predicate offences.

Another possible approach to quantifying money laundering in a specific sector is illustrated in the work done by the British Columbia-Canada Real Estate Working Group (Working Group, discussed in Chapter 18). The Working Group suggests that systematically identifying instances of money laundering in real estate through data can generate insights to drive policy and enforcement efforts.[186] It came up with an anti–money laundering framework that defines indicators of money laundering by enumerating money laundering schemes and the ways the schemes are visible within data.[187] The group assessed the availability of the data that would be required to construct each indicator. Eight schemes and 23 sub-schemes for money laundering in the real estate sector were broken down into 160 individual data points required for their detection.

The Working Group's work indicates that, in order to use indicators to identify money laundering in the real estate sector, one would need to have comprehensive coverage of real estate transactions and ownership arrangements within a given geographic area over time.[188] Several data gaps in current data holdings would need to be filled before an anti–money laundering framework in real estate would be able to produce indicators for most of the money laundering schemes and sub-schemes.[189]

I should add that there is real merit in pursuing more promising quantification efforts, one example being the trade mispricing analysis of Dr. Zdanowicz.

Such efforts will require access to data. As the Province noted in its closing submissions to me, a broad theme from the evidence is that understanding the nature and scope of the money laundering in any sector requires good data and analytical capabilities.[190] Witnesses were unanimous in their view that, no matter the method, the data to estimate money laundering are lacking.

In Chapter 39, I recommend a new approach by law enforcement agencies engaged in the investigation of profit-oriented criminal activity. I expect that significantly more data will become available if that recommendation is followed.

The AML Commissioner, a new office that I recommend in Chapter 8, will be well placed to help advise on what sort of quantification efforts should be undertaken by

185 Ibid; Evidence of J. Caulkins, Transcript, December 8, 2020, pp 38, 58, 107.

186 Exhibit 725, Work Stream 1 – Data Collection and Sharing Work Stream Report, Executive Summary (PowerPoint by BC Canada Real Estate Working Group) [Work Stream 1], p 5.

187 Exhibit 725, Work Stream 1, p 5.

188 Ibid, pp 5–6.

189 Ibid, p 5 and see Recommendation 7 on p 14; Evidence of B. Ogmundson, Transcript, February 17, 2021, pp 169–70; Evidence of B. Pereboom, Transcript, March 11, 2021, pp 29–30.

190 Closing submissions (other than gaming sector), Government of British Columbia, p 2.

the Province. The commissioner's office will develop expertise that will enable the commissioner to give knowledgeable input on quantification.

As the Province (and Canada) engages in reforms to combat money laundering, it should always have its eye on the ball. Even if an exact measurement or quantification may be elusive, the government should always consider:

- Are there imperfect or inexact – but still insightful – ways to understand the extent of money laundering and the effect of policy reforms?
- When a new policy or operational change is made, what are the goals of that measure, and are there strategies that can be used to measure outcomes, to see if the goals were achieved, and to assess the costs and benefits?
- Can better data be developed to allow for measurement and comparisons over time?

In this chapter I have described the various ways that quantification of money laundering can be attempted. One theme emerging from this survey of quantification is that there *are* examples, where data are available, that offer real insight into how much money laundering is occurring. Quantification efforts appear to be particularly successful where a money laundering operation that typically lurks in the shadows is forced into view. For example, one aspect of the Vancouver model of money laundering – the purchase of casino chips with cash – could only occur in plain sight, in a highly regulated and monitored environment, which produced detailed data. This data – what was observable in the visible phase of the money laundering method – provides a real lens into the activity and the impact of anti–money laundering measures designed to target the illicit activity. Similarly, the Zdanowicz method of analyzing trade mispricing information, is especially effective, because import / export records exist and such trade data provide real insights into both the activity and the measures taken to stem such activity. To be effectively laundered, dirty money needs to be exposed in bulk to some public scrutiny at some point. The key to identifying and quantifying it lies in determining when and where that point is, through some objectively reliable process (such as trade data).

The Province should look for opportunities to develop data wherever possible, as such data may lend real insight into the nature and extent of money laundering and the movement of illicit funds.

Chapter 5
Is Money Laundering a Problem Worth Addressing?

The utility of addressing the problem of money laundering was raised as an issue in the Commission's Interim Report issued in November 2020. The question posed by the Interim Report – whether money laundering was a problem worth addressing – was answered provisionally after a summary review of some of the important policy and political considerations at play in the national and international conversations about the benefit of adopting a robust anti–money laundering regime to counter money laundering's impact on a country's economic and political regime.

In broad terms, after acknowledging there are limitations on measuring the scope and the effect of money laundering in British Columbia, the Interim Report concluded that to not take meaningful action against money laundering would "[leave] custodians of the political and economic system open to criticism that they are complicit in that enterprise of criminality"[1] and that their quiescence would encourage those involved in that type of criminality to continue their unlawful behaviour, whether in relation to money laundering or the offences that create the need to launder illicit funds.

Before reaching that conclusion in the Interim Report, I outlined some of the views expressed by the expert witnesses whom I heard from. These witnesses addressed some of the issues that surround money laundering and the anti–money laundering regime that has grown up in response to its perceived threat to "financial markets, on economies, on companies, or society as a whole."[2] In particular, I noted that Professor Stephen Schneider "provided a critical perspective on what he termed the 'dominant

1 Commission of Inquiry into Money Laundering in British Columbia, Interim Report, November 2020 (Interim Report), p 68.

2 Ibid, p 65, footnote 16.

narratives on the effects of money laundering,'"[3] which he described as "a very small proportion of [the Canadian economy], very tiny, and really doesn't have an impact."[4]

I also noted that Professor Schneider was skeptical of the claim that money laundering "'perpetuates' organized crime and argued that it is demand (rather than the ability to launder the proceeds of crime) which drives 'consensual crimes' such as drug trafficking, bookmaking, prostitution, or human smuggling."[5]

I noted that Professor Schneider cast doubt on a study by J. McDowell and G. Novis entitled "The Consequences of Money Laundering and Financial Crime." That paper posited that "[M]oney laundering has potentially devastating economic, security, and social consequences," and "[l]eft unchecked, it can 'erode the integrity of a nation's financial institutions,'" including by "adversely [affecting] currencies and interest rates."[6]

I also referred to Professor Schneider's testimony where he based his skepticism about money laundering's impact on the lack of rigorous models that show economies are seriously affected by money laundering.[7]

Finally, I quoted from Professor Schneider's evidence in which he attributed the most dire arguments about the devastating effects of money laundering to "government and law enforcement agencies that 'have a clear vested interest in … drawing attention to the high … threat of a particular problem.'"[8] Professor Schneider described the United States as "[inflating] the scope of the problem" while "trying to impose their anti–money laundering system … for years."[9]

I also noted in the Interim Report that Professor Schneider's views about the lack of reliable data to support the view that money laundering caused significant negative consequences were shared by Professors Michael Levi, Peter Reuter, and Terence Halliday in an article marked as Exhibit 26: "Can the AML System Be Evaluated Without Better Data?" (2018) 69 *Crime, Law and Social Change* pp 307–328.

In the article, the authors contend that there has been "minimal effort at AML evaluation at least in the sense in which evaluation is generally understood by public policy and social science researchers, namely, how well an intervention does in achieving its goals."[10]

As I noted in the Interim Report, the authors "[expressed] the view that anti–money laundering systems 'will continue to reflect faith and process rather than build upon reliable evidence of actual positive impacts on institutions and social wellbeing.'"[11]

3 Ibid, p 65, footnote 16.
4 Ibid, p 65, footnote 16.
5 Ibid, p 65, footnote 17.
6 Ibid, p 65, footnote 20.
7 Ibid, p 65.
8 Ibid, p 65.
9 Ibid, p 65, footnote 22.
10 Exhibit 26, p 310.
11 Interim Report, p 66, footnote 25.

Professor Peter Reuter testified before the Commission. In the Interim Report I noted that his evidence reflected the view that anti–money laundering was useful "not because it could reduce money laundering, but [because] it could reduce the activities that generate money laundering."[12] As I noted in the Interim Report, Professor Reuter cited the contention of one author, Joras Ferwerda, that there were "25 distinct possible harms from money laundering."[13] But Professor Ferwerda went on to opine that there is "no evidence of any of them, 'in the sense that nobody has done a study which has shown that money laundering has generated these specific harms to any large extent.'"[14]

Professor Michael Levi, who also testified before the Commission, expressed the view that "we need to think much more clearly about the harms of money laundering than we often do."[15]

An important question confronting the Commission is whether (and if so, to what extent) money laundering has affected the province's institutional integrity. Has it resulted in a political and/or economic regime that has, at least, some historical complicity with those seeking to disguise their tainted wealth as legitimately acquired?

That question involves considering the quantum of criminalized money that needs to be laundered in British Columbia and the extent to which it is laundered with or without the knowing assistance of those positioned and obliged to prevent it.

The quantum of money in British Columbia that needs to be laundered is the subject of the previous chapter in this Report. The extent to which it is laundered with the knowing or unknowing participation of those with some responsibility to resist it, although a different question, is hard to separate in the context of the issue raised in this chapter: "Is money laundering worth addressing?" Both the amount of money laundering taking place in British Columbia and the extent to which it is enabled, knowingly or not, by those responsible for resisting it, are important questions that underpin the fundamental question posed by this chapter.

If the question is whether money laundering is worth addressing, the instinctive response is that it is, because tackling money laundering will reduce crime. This answer is premised on the logical assumption that thwarting money laundering would weaken the criminal organizations that rely on it. As Professor Levi put it in his evidence:

> [Y]ou could see that without the possibility of laundering money, organized crime would be much weaker and would not find its way into the tentacles of some parts of the … political system, though they didn't think of that in a very high-up way.[16]

12 Ibid, p 66, footnote 26.

13 Ibid, p 66.

14 Ibid, p 66, footnote 28.

15 Evidence of M. Levi, Transcript, June 8, 2020, p 27; Interim Report, p 67.

16 Evidence of M. Levi, Transcript, June 5, 2020, p 17.

Despite that instinctive response, there are some doubts expressed by those who study money laundering as to the efficacy of combatting it.

As is apparent from previous chapters in this Report, the main form of resistance to money laundering internationally, nationally, and in British Columbia is guided by the Financial Action Task Force (FATF) rules. However, academics have raised issues about the effectiveness of those rules in combatting money laundering.

As Professor Reuter expressed it in his evidence before the Commission:

> And so every country basically follows the FATF rules. As we argued, there's very little evidence that the rules have been effective, and the interesting question is: why is it that this particular transnational legal order is subject to … so little criticism? It's very modest.[17]

Even the effectiveness of gauging the quantification of money laundering in a particular jurisdiction (which seems important as a measure of the effectiveness of remedial action taken) is called into question. In his testimony, Professor Reuter put it thus:

> It is not clear how, with the existing data, you get to estimate how much money is laundered … you can estimate the size of drug markets through a combination of different kinds of surveys and indicators, and from that with some price data you can establish how much revenue there is, and then with some other data you can work out how much might need to be laundered as opposed to just plain money that low level retailers … spend on staying alive, and you might be able to come up with some … estimate of how much money is being laundered from drug markets.
>
> …
>
> [I]f all we know is what's reported by enforcement agencies and financial institutions, we cannot credibly estimate the amount of money that's laundered.[18]

Professor Reuter emphasized that the size of the drug and fraud markets is not a good proxy for measuring the volume of money laundering, describing it only as "a starting point."[19]

As to the gravity model, Professor Reuter testified that "the range of plausible estimates [at each step] is just so large that they're not going to give you any guidance."[20] He described the gravity model's assumptions not as "heroic assumptions," but rather as "hubristic assumptions."[21]

17 Evidence of P. Reuter, Transcript, June 5, 2020, p 14.

18 Ibid, p 50.

19 Ibid, p 54.

20 Ibid, p 54.

21 Ibid, p 54.

Professor Reuter identified the problem as one of uncertainty. He noted that the drug market in the US is "something between $50 billion and $200 billion … [which is] a huge range of potential estimates."[22] You have to learn "how to … make policy here without numbers because the numbers are going to be so crude you couldn't possibly tell whether things have gotten better or worse, just with a set of numbers."[23]

It was Professor Reuter's contention that anti–money laundering has no assessment of effectiveness. He asserted:

> I think I know this field reasonably well and I cannot think of anything, any study that has claimed to show that as a result of AML in Canada or AML in Australia, crime has been reduced by X or that it has generated a thousand additional convictions … do we know how much AML has contributed to the accomplishment of these objectives? And the answer is that there are no such studies.[24]

Professor Reuter opined that "measuring the volume of money laundering doesn't serve as a useful measure of effectiveness because money laundering itself does not cause harm."[25] Acknowledging that was "a controversial statement," Professor Reuter went on to describe money laundering as being "a part of the activity of a set of criminal activities that we do care about"; he said that "[we] can use AML to reduce those activities, whether they be crime or terrorism."[26]

Professor Reuter acknowledged that despite his contrary assertion, "there may indeed be serious consequences of money laundering, but we have no empirical evidence to say that they're substantial enough to be worth mentioning."[27]

Professor Levi pointed out that "one of [the] social objectives in controlling money laundering might be to stop [criminal] organizations [from] getting more powerful."[28]

Professor Reuter estimated the banks in Europe spend in the tens of billions of dollars on anti–money laundering. "AML is clearly very important and [learning] how to do it better matters."[29]

The Criminal Intelligence Service Canada (CISC) assesses the threat of serious and organized crime impacting Canada. It has 10 provincial intelligence bureaus and comprises approximately 400 member agencies.[30]

22 Ibid, p 52.
23 Ibid, p 52.
24 Ibid, p 62.
25 Ibid, pp 65–66.
26 Ibid, pp 62–63.
27 Ibid, p 25.
28 Evidence of M. Levi, Transcript, June 8, 2020, p 39.
29 Evidence of P. Reuter, Transcript, June 8, 2020, p 26.
30 Evidence of R. Gilchrist, Transcript, June 9, 2020, p 3.

CISC issued a public report on organized crime in 2019. According to that report, there are 1,850 organized crime groups operating in Canada. Of those, 680 have been assessed by CISC using its integrated threat assessment process. Of the 680, 176 are believed to be involved in money laundering activities, although that number may be under-reported. Chief Superintendent Robert Gilchrist testified that

> quantification [of money-laundering] has proven to be extremely difficult. There's a number of estimates that are out there, provided by other organizations. However, in general, CISC has not undertaken a study to try to quantify the exact amount of money laundering in dollar terms. We do follow the estimates that are provided by others … And we rely upon it for contextual background … beyond [serving] as a general … background point, it's limited to that use by CISC.[31]

Chief Superintendent Gilchrist elaborated on the focus of organized crime groups in Canada:

> the highest number of organized crime groups thought to be involved in money laundering … are reported primarily in three provinces. Ontario, followed by British Columbia, and then followed by Québec, with all three of those provinces collectively representing more than 76 percent of the … assessed organized crime groups involved in money laundering.[32]

As to the impact of money laundering on the social and political order of the countries in which it appears most persistently, mainly the most affluent countries in the world, Sir Robert Wainwright was asked "why … money laundering is a problem for society and [what are] the harms it causes that motivate the action to confront it."[33]

Mr. Wainwright spent a significant time as the executive director of Europol from 2009 until 2018. Europol is "constituted to act as facilitator and a supporter of international police cooperation in Europe."[34] There are approximately 40 different countries that are part of a coordinated information sharing network through Europol.[35] His response to the question posed to him concerning the harms and problems for society that money laundering presents was as follows:

> Yes. In Europol … we described it as an engine of organized crime because it was at the heart of – of – is at the heart of the criminal economy, because it's about, of course, as I said earlier, for criminals finding ways to make crime pay essentially. And that in itself, if they can do that in an effective way is of course a huge incentive to engage in crime in the first place, a stimulus for exponential increase, and it also acts, importantly, as a funding source for

31 Ibid, p 40.

32 Ibid, p 53.

33 Evidence of R. Wainwright, Transcript, June 15, 2020, p 18.

34 Ibid, p 7.

35 Ibid, p 7.

> further illicit activities, and not only for drug traffickers, not only in drugs but in other very important offences that impact society, such as terrorism and modern slavery.
>
> I think its intrinsic role as a key enabler of organized crime is important. Why is it a problem? Also because of the scale and the way … in which the globalized criminal economy has grown. Our conservative estimates while I was at Europol was that around 120 billion euros were produced in annual revenue relating to the criminal economy in Europe. Actually global estimates – the one most reliably quoted, most often quoted from the UN points to something like two trillion U.S. dollars, which is over three percent of global GDP. And of course, when it's at that scale, it has a serious polluting effect on the integrity of our financial markets, on our economies. And of course, it has this very adverse societal impact because not only does it fuel the crime itself, it fuels corruption around that to enable the crime. It drives illicit labour markets. And we've seen all of that – a microcosm of all of that in the last three months with the COVID impact, for example. We've seen certain sectors that have declined as a result of the economic downturn associated with COVID. Some of those sectors have become more vulnerable to criminal exploitation and even takeover.
>
> And where we see, for example, difficulty in accessing capital because of that, they turn unknowingly maybe to loan sharks involved in processing criminal profits. And of course, a rise in investment scams.
>
> So I think money laundering, the scale of it, the impact of it, has in driving this global criminal economy is a serious problem actually on many levels to our interests in society.[36]

Although, academically, a case might be made for treating money laundering as not worthy or capable of being addressed, as I see it, some academic commentary on the subject has missed important considerations. As I noted in Chapter 4, some experts contend that quantification may be vital to understand the scope and nature of the money laundering problem and to measure the success of initiatives aimed at combatting it. Moreover, given the acknowledged "enormous" difficulties associated with determining quantification, it may be difficult, if not impossible, for those with the responsibility to resist money laundering to make informed choices about the extent to which – and how – they will try to regulate it.

In the Interim Report, I explained the Commission's approach to the question that underlies this chapter: whether a robust anti–money laundering regime is justifiable. In addressing that question in the Interim Report, I noted that:

36 Evidence of R. Wainwright, Transcript, June 15, 2020, pp 18–19.

> Ultimately, the question of whether combatting money laundering is an important priority can be definitely answered only by increasing our understanding of its nature, its extent, the implications of addressing it, and how it can be addressed most effectively.[37]

I also noted that despite "the problems associated with measuring the size and impact of money laundering activity as well as the effectiveness of the proposed solutions,"[38] there is importance in recognizing "that it may be necessary to take action against the threat [of money laundering] even though it cannot be empirically measured."[39]

There is, in my view, considerable evidence of serious problems arising from the tolerance of money laundering. In the face of that, to sit idly by insisting on incontrovertible proof, is untenable. The risks are, at this point, clear and identifiable, even if evasive of precise measurement. I do not consider it prudent or responsible to be passive about money laundering. Citizens, experts, and governments have rightfully become concerned about the continuing prevalence of money laundering, and there is much room for improvement in this area.

In his report to the Commission titled *Money Laundering and Foreign Corruption Proceeds in British Columbia: A Comparative International Policy Assessment*, Jason Sharman, the Sir Patrick Sheehy Professor of International Relations at the University of Cambridge noted, "[the fact] that in a 16-year period, Canada has had only 316 money laundering convictions, while in 2017 alone Britain has had 1,435, is a staggering contrast. Money launderers in BC and Canada more generally face an open goal."[40]

The relative paucity of prosecutions and convictions for money laundering in Canada and British Columbia is not a reflection that we are relatively free of money laundering activity. Rather, it is a reflection of regimes that have relied too heavily on building up formal anti–money laundering structures and not heavily enough on building a substantive enforcement component to those structures to come to grips with the challenges of tracking the proceeds of crime as they are integrated into the legitimate economy. In that sense, the prevailing anti–money laundering regime can be likened to a Potemkin village, which relies on the appearance of effective structures rather than their reality.

Nevertheless, as is apparent from the previous chapter, and, indeed from the evidence called at the Inquiry generally, although the extent of money laundering in British Columbia is not presently conducive to quantification, I am satisfied that there is a "substantial" body of money in British Columbia that requires laundering on an ongoing basis, either informally or through professional money laundering services.

37 Interim Report, pp 67–68.

38 Ibid, p 68.

39 Ibid, p 68.

40 Exhibit 959, p 5.

Even though the adequacy of the different measurement models may be difficult to assess and the "estimates [and extrapolations] of money laundering [remain] wild and imprecise, if not downright wrong,"[41] there is a strong rationale for invoking anti–money laundering measures to take a principled stand against allowing money laundering to infect the political and economic integrity of the province.

Money laundering has an impact on British Columbians. That impact occurs collectively and individually. The introduction of illicit money into the economy distorts markets. It courts imbalance and inequity among those seeking economic toeholds for their businesses and for themselves and their families.[42]

British Columbians rightfully expect a governance system in which there are equal and fair opportunities to grow and prosper. There can be few things more destructive of a community's sense of well-being than a governing regime that fails to resist those whose opportunities are unfairly gained and come at the expense of others.

Money laundering is not the only activity that profits from that form of unfairness, but it does stand out. It allows the predatory to use the money gained at the expense of the vulnerable, by disguising it with a patina of legitimacy, and permits them to compete in the marketplace with those who feel constrained to earn their money honestly and pay their fair share of the burden of maintaining the benefits of living in a community.

Perhaps even more importantly, as I noted in the Interim Report, resisting money laundering resists those who would engage in activities

> [t]hat strike at the heart of our collective values. Money laundering is a crime that occurs in the aftermath of other, more overtly and directly destructive offences: drug trafficking, human trafficking, prostitution, extortion, theft, fraud, and trafficking in child pornography. Deterring money laundering thwarts those for whom the crime is motivated by profit and repudiates the evils of the offences that produce the demand for it.[43]

In my view, the failure to respond to the money laundering activity, which is undoubtedly occurring in numerous sectors of the BC economy, would send a message that unlawful and socially destructive behaviour will be tolerated and allow those who prey on the most vulnerable in society to continue if not expand their operations and reap the rewards of their unlawful conduct. It would also result in a lost opportunity to target and disrupt the activities of organized crime groups and other criminal actors operating within the province.

41 Exhibit 322, Overview Report: Simplified Text on Quantification of Money Laundering, p 2.

42 On this point see Evidence of S. Cassella, May 10, 2021, p 63; Evidence of G. Clement, April 9, 2021, pp 56–57; Evidence of S. Cassella, May 10, 2021, pp 63–64; and Exhibit 396, Department of Finance Canada, *Assessment of Inherent Risks of Money Laundering and Terrorist Financing in Canada* (2015), p 67.

43 Interim Report, p 68. See also Evidence of N. Maxwell, Transcript, January 14, 2021, pp 45–47.