



Federation of
Law Societies
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Fédération des ordres
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du Canada

Anti-Money Laundering and
Terrorist Financing Working
Group

Red Flag Guidance on the Source of Funds

Client Identification and Verification

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A. Fulfilling the source of funds obligations

Legal professionals retained to provide legal services that involve a financial transaction¹, must obtain and record, with the applicable date, information about the **source of funds** being paid, received or transferred, unless one of the exemptions from the client verification requirements apply.

Understanding the source of funds to be used in a transaction is key to fulfilling the obligation legal professionals have to maintain vigilance and mitigate the risks of facilitating fraud, crime or illegal conduct, such as money laundering.² Reasonable inquiries should be made about the transaction, including the source of funds, and supporting documents should be obtained, particularly if there are suspicious circumstances. The legal professional must objectively assess the information they receive.

What is the “source of funds”?

The “source of funds” means the origin of the particular funds that are used, or to be used, in a particular transaction. This includes the economic activity or action generating the funds, information that identifies the person or entity providing the funds, if other than the client, and the relationship of the client to the person or entity providing the funds.

Information about the source of funds

In making source of funds inquiries, the information that a legal professional obtains from the client should include:

- the payer’s full name, occupation and contact information;
- the relationship of the payer to the client (the payer may be the client);
- the date on which the funds were received by the legal professional from the payer;
- the economic activity or action that generated the funds (e.g., sale of property, bank loan, savings from salary, settlement funds);
- the form in which the funds were received by the legal professional (e.g., cheque, bank draft, electronic funds transfer);
- the full name and address of all financial institutions or other entities through which the payer processed the funds or transmitted the funds to the legal professional; and
- any other information relevant to determining the source of funds.

See the attached sample form: **INFORMATION ABOUT THE SOURCE OF FUNDS**.

Exemptions

¹ A financial transaction is the receipt, payment or transfer of funds handled or instructed by a legal professional in the course of providing legal services to a client.

² Legal professionals have a duty not to engage in any conduct that they know or ought to know assists in or encourages any dishonesty, crime or fraud. These obligations are found in sections 6(1)(a), 9 and 10 of the Model Rule on Client Identification and Verification and in rules 3.2-7 and 3.2-8 of the Model Code of Professional Conduct



The Model Rule on Client Identification and Verification (“Model Rule”) does not require legal professionals to obtain information about the source of funds if:

- the client is a “financial institution”, “public body” or “reporting issuer”;
- the funds are transferred using an “electronic funds transfer”; or
- the funds involved are:
 - paid by or to a “financial institution”, “public body” or “reporting issuer”;
 - received by a lawyer from the trust account of another “lawyer”;
 - received from a peace officer, law enforcement agency or other public official acting in an official capacity;
 - paid or received to pay a fine or penalty or bail; or
 - paid or received for “professional fees”, “disbursements” or “expenses”.³

Legal professionals should be aware that even if an exemption applies, it may still be necessary to make reasonable inquiries about the source of funds, including obtaining supporting documents, to comply with their ethical duty not to facilitate any dishonesty, crime or fraud, including money laundering.

Timing

Information about the source of funds should be obtained from a client when verifying the client’s identity and before the funds are paid, received, or transferred,

B. Other considerations

Is the client’s information about the source of funds sufficient?

In the absence of unusual, inconsistent, or suspicious circumstances, a legal professional may accept a client’s information about the economic activity or action that generated the funds to be used in the financial transaction (e.g., inheritance, savings from salary, life insurance proceeds) without obtaining supporting documents.

Where information appears unusual, inconsistent, including with the client’s profile, or suspicions are raised, legal professionals must make further inquiries, assess the risks, and be satisfied that they are not assisting the client in fraud, crime or illegal conduct, such as money laundering. If the legal professional is not satisfied that the client’s legal matter and the transaction are legitimate, they must not act on the matter.

Is there an objective threshold for when a legal professional should obtain documents to substantiate a client’s explanation about the source of funds?

There is no hard and fast threshold; the need to obtain supporting documents about a client’s source of funds will depend on the circumstances.

³ Words in quotations are defined in section 1 of the Model Rule.



For example, if a dispute between two neighbours regarding a fence between their properties was settled for \$10,500, a legal professional may feel no need to obtain supporting documents about the source of funds from the client employed as a teacher who provides a \$10,500 personal cheque for the settlement. The legal professional will already have asked the client for their information on the source of funds and recorded the information for the purposes of Model Rule section 7 (Record Keeping and Retention).

However, if a client with an occupation such as “bank employee” from outside of Canada wants to wire funds from a foreign bank to the legal professional’s trust account to complete a multi-million-dollar residential property purchase, enhanced due diligence would be required. The legal professional would be expected to make sufficient enquiries about the client and the source of funds and obtain supporting documents.

Examples of red flags that should prompt legal professionals to make further inquiries

The source of funds information provided by the client should align with information known about the client and the transaction. In some circumstances, the legal professional may receive information that raises or ought to raise suspicions, or red flags. Some examples of potential red flags related to the source of funds include:

- the money comes from a source that is unusual in the circumstances, unexplained, appears unusually complex or cannot be verified
- multiple sources of funds are used, such as several bank accounts or numbered company’s accounts, without reasonable explanation
- funds are drawn from a foreign bank with no apparent connection to the client, or the bank is in a jurisdiction that is high risk for money laundering
- a disproportionate amount of funding comes from bank drafts, cash or complex crypto assets
- financing is provided by a lender other than a bank or credit institution with no logical explanation or economic justification
- the funds provided for a transaction appear to be large relative to the client’s income without logical explanation
- there has been a significant increase in capital for a recently incorporated company or large, successive contributions over a short period of time to the same company, with no logical explanation

Additional information on red flags is available [here](#).

Examples of source of funds supporting documents

The following is a non-exhaustive list of examples of documents that legal professionals may request depending on the client’s source of funds information:

- employment pay statements or other proof of earnings
- tax return



- agreement of purchase and sale
- bill of sale
- loan agreement
- court judgment
- minutes of settlement
- will or gift letter
- life insurance pay out statement
- lottery or gambling win receipts and documentation
- share or asset purchase agreement
- partnership agreement
- capital raise or contribution documentation
- debt instrument documentation

Assessing supporting documents on the source of funds

Legal professionals should review supporting documents to see if they are consistent with the client's information about the source of funds and whether concerns about unusual circumstances, inconsistencies with the client profile, or the retainer are resolved by the documents.

If the documents do not resolve concerns, do not align with the client's information about the source of funds, or raise new concerns, legal professionals should make further inquiries of the client and, based on the information obtained, assess whether they can act or continue to act for the client on the matter.

If a legal professional is objectively satisfied with the documents and the responses, they may proceed with the matter in the normal course. They should also:

- Create a record of the documents reviewed and their assessment in the client file.
- Make copies of the supporting documents.
- Continue to assess risk for the purposes of ongoing periodic monitoring (see below).

If a legal professional is not satisfied with the documents and/or responses and they know or ought to know that they would be assisting a client with fraud or illegal conduct by accepting the retainer, they must decline or withdraw from representation.

Source of funds information to obtain if receiving funds from the other side's legal representative

Both the legal professional receiving the funds and the other side's legal representative have source of funds obligations. If a legal professional is receiving funds on behalf of their client, they must obtain and record information about the source of funds for the financial transaction.

If, however, the funds are not coming directly from another party (e.g., a purchaser) or their legal representative, or there are red flags associated with the source of funds (e.g., it is a high value transaction that does not require financing), a legal professional may need to make follow-



up inquiries and obtain supporting documentation. In all cases, legal professionals should maintain and retain a record of their source of fund inquiries and the information they obtain.

Assessing the source of funds when monitoring the professional business relationship

While a legal professional is retained in a matter involving a financial transaction, they must periodically monitor the professional business relationship with clients. This includes periodically monitoring the client's information about the source of funds used in the financial transaction and assessing whether there is a risk that the legal professional may be facilitating fraud, crime or illegal conduct, such as money laundering. The frequency of periodic monitoring and what information should be recorded will depend on what is reasonable in each case.

Legal professionals must keep a record, with applicable dates, of measures taken to comply with the periodic monitoring obligation and the client information obtained.

More detailed guidance on the monitoring obligation is available [here](#).

When to consult a practice advisor

Legal professionals are encouraged to contact a practice advisor for further guidance on what may be required to fulfil their obligation to obtain information about the source of funds and supporting documentation (if enhanced due diligence is required), and assess risk based the information obtained in a particular matter.

Duty to withdraw representation

If while retained, including in the course of obtaining the required information and taking the steps under the monitoring requirements, the legal professional knows or ought to know that they are or would be assisting a client in fraud or illegal conduct, they must withdraw from representation of the client.⁴

⁴ See Model Rule on Client Identification and Verification ss. 9(1) and 11.

Appendix A

CLIENT IDENTIFICATION AND VERIFICATION INFORMATION ABOUT THE SOURCE OF FUNDS

Overview

A key component of client identification and verification is the requirement to obtain information from the client and record, with the applicable date, information about the source of funds when the legal professional engages in or gives instructions in respect of the receiving, paying or transferring of funds. Legal professionals have a positive duty to make inquiries about any financial transactions that they facilitate. This may include obtaining supporting documents if the circumstances warrant (e.g., high-value transaction, presence of suspicious circumstances)

1. Purpose of the financial transaction:

2. Type of “funds” (as defined) and amount:

“Funds” means cash, currency, securities and negotiable instruments or other financial instruments that indicate the person’s title or right to or interest in them

3. Information about payer:

See *Client ID Documents and Resources* for further guidance on identifying the red flags of money laundering, fraud or terrorist financing <https://nsbs.org/legal-profession/your-practice/responsibilities-requirements/client-id/>

a. Full name:

b. Occupation:

c. Contact information:



d. Relationship of payer to the client(s) (if the payer is not the client):

4. Date funds received by the legal professional:

5. Economic activity or action that generated the funds:

Economic activity or action includes such things as a bank loan, savings from salaried employment, settlement funds etc.

6. Form of funds received by the legal professional:

Form of funds includes cheque, bank draft, wire transfer etc.

7. Name and address of financial institutions or other entities through which the funds were processed or transmitted:



8. Other information relevant to determining the source of funds:

In the absence of suspicious circumstances, a legal professional may accept a client's explanation regarding the economic activity or action that generated the client's source of funds (e.g., inheritance, savings from salary, life insurance proceeds) without obtaining copies of the documents to support the client's explanation. However, where there are suspicious circumstances, legal professionals must make further inquiries and assess the risk of participating in a financial transaction for that client.

Responsible Lawyer: _____

Name of person completing the form: _____

Date: _____

Attach copies of any relevant documents

