

# **Cullen Commission of Inquiry into Money Laundering in British Columbia**

**February 24 to 26, 2020**

## **BMW's Opening Submissions**

### **Introduction**

1. We are counsel for BMW Canada Inc. and BMW Financial Services, a division of BMW Canada Inc. (collectively, "**BMW**") in the Cullen Inquiry (the "**Inquiry**").
2. BMW Canada Inc. 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 provides financial services, including leasing and financing of vehicles, to BMW customers in Canada.
3. As a globally recognized manufacturer and marketer of motor vehicles, the BMW name and brand is well known. BMW's vehicles are marketed under the following brands: BMW, MINI, and Rolls-Royce.
4. BMW has a substantial presence in Canada, with 51 BMW retailers, 30 MINI retailers, 4 Rolls-Royce retailers, and 20 BMW Motorcycle retailers nationally.
5. In British Columbia, BMW, MINI, and Rolls-Royce vehicles are sold through authorized retailers in Vancouver, North Vancouver, Richmond, Langley, Victoria, Nanaimo, and Kelowna.
6. Additionally, BMW vehicles are heavily traded on the Canadian used car market by both authorized and unauthorized dealers.

### **Why is BMW participating in the Inquiry?**

7. BMW is the only luxury vehicle manufacturer, seller and financier who has applied for and has been granted standing as a participant in this Inquiry. BMW is privileged to be taking part in this historic Inquiry as a participant and to have this opportunity to address the Commission today.
8. BMW sought participation in the Inquiry because, as an industry leader, it believes it can help the Commission fulfil its mandate by assisting the Commission to make fair, accurate, and helpful findings and recommendations for the benefit of the automotive industry and British Columbia consumers.
9. The scope of the Commission's mandate is broad. It has been called upon to make findings of fact and recommendations respecting money laundering in British Columbia, including the:

- a. extent, growth, evolution, and methods of money laundering in various sectors, including financial services and luxury goods;
  - b. the acts or omissions of regulatory authorities or individuals with powers, duties or functions in respect of various sectors, including financial services and luxury goods, to determine whether those acts or omissions have contributed to money laundering in British Columbia and whether those acts or omissions have amounted to corruption;
  - c. the scope and effectiveness of the powers, duties and functions exercised or carried out by those regulatory authorities or individuals; and
  - d. the barriers to effective law enforcement respecting money laundering in British Columbia.
10. As money laundering is insidious in nature, it is important for those who may have on-the-ground indicators about its extent, growth, evolution, or methods of money laundering to share their experiences and insights with the Commission.
11. We cannot forget that this Inquiry was established for the benefit of the British Columbia public. Money laundering is a serious problem in British Columbia. It will continue to flourish if action is not taken. The people of British Columbia are concerned. BMW is concerned, as are its customers.
12. As Peter German writes:
- All those attributes which make Greater Vancouver a very desirable region in which to live, also make it desirable to organized crime. In recent years, the region has acquired an unenviable reputation for serving as a site for money laundering, drug trafficking, and capital flight.
- It is both an embarrassment and a threat to society that adheres to the Rule of Law, for organized crime to take advantage of all that is good in our society and subvert it for pecuniary advantage.<sup>1</sup>
13. BMW seeks to contribute to the Inquiry by being open and transparent about its insights, experiences, and industry leading practices. It has been granted standing in relation to the luxury goods and financial services sectors.

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<sup>1</sup> Peter German, QC, PhD. Dirty Money – Part 2: Turning the Tide – An Independent Review of Money Laundering in Real Estate, Luxury Vehicle Sales & Horse Racing (March 31, 2019) at pages 11-12 [The Second German Report].

### **The luxury vehicle market in B.C.**

14. Vancouver is known as the “luxury car capital of North America”.<sup>2</sup> As you will know, it is not unusual to see many high end luxury vehicles on the streets of Metro Vancouver at any time and on any given day of the week.
15. Not only is there a huge market for luxury vehicles in British Columbia, there is even a demand for luxury housing of luxury vehicles. A development called “Trove” located in Richmond is currently selling auto storage condominiums to luxury vehicle owners. Trove promises to “redefine what it means to own a luxury vehicle in Vancouver”. The base price for one unit is \$600,000 and owners can choose to pay more to customize their units.<sup>3</sup>
16. Given the climate and appetite in British Columbia for luxury vehicles and their high end accessories, perhaps unsurprisingly, the Terms of Reference direct the Commission to review and consider the report of Peter German, Q.C., dated March 31, 2019, entitled “Vancouver at Risk – Turning the Tide – An Independent Review of Money Laundering in B.C. Real Estate, Luxury Vehicle Sales & Horse Racing”. We will refer to this report as the “Second German Report” throughout our submissions.
17. The Second German Report engages in an extensive review of the luxury vehicle market and its use in money laundering and grey market schemes, making findings and comments relating to:
  - a. Cash sales of luxury vehicles as a means to launder proceeds of unlawful activity;
  - b. The use of straw buyers and nominees to effect illegal export of luxury vehicles for grey market schemes in China and elsewhere, including tax refund schemes;
  - c. The export of luxury vehicles for the purposes of laundering money for criminal organizations and terrorist organizations; and
  - d. Theft of luxury vehicles for money laundering purposes.
18. As one of the world’s leading luxury vehicle manufacturers and brands, BMW has important information to present to the Commission relating to the unlawful export of BMW vehicles and the use of straw buyers and nominees to conduct those exports. Additionally, BMW will share with the Commission the various efforts BMW already undertakes to combat this issue.
19. BMW will also provide the Commission with recommendations which would ensure a balance between the efficient growth of the luxury vehicle industry while building in safeguards to combat money laundering.

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<sup>2</sup> The Second German Report at page 184.

<sup>3</sup> Jennifer Palmer. Luxury condos for Vancouver’s supercars? ‘Why not?’ people say (Global News, August 9, 2018), <<https://globalnews.ca/news/3745970/luxury-condos-supercars-vancouver/>>.

### **What is the vehicle grey market?**

20. The Financial Action Task Force defines trade-based money laundering as “the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illegal origins or finance their activities”.
21. The Financial Action Task Force considers trade-based money laundering one of the principle methods by which criminal organizations and terrorist financiers move money for the purpose of disguising its origin and integrating it into the formal economy.<sup>4</sup>
22. A grey market exists where a brand owner or manufacturer’s products are purchased and then resold outside of approved distribution networks. Money laundering through exporting vehicles purchased for domestic use, known as the vehicle grey market, is an example of trade-based money laundering.<sup>56</sup>
23. The grey market export scheme is further described by Peter German in his Second Report at page 196 as follows:

The grey market export of vehicles in B.C. is a significant and rapidly growing problem. There has been an explosion in the number of grey market vehicles exported to China since 2013 growing from less than 100 vehicles in 2013 to over 4,400 vehicles in 2018.

These vehicles are purchased for domestic use by straw buyers, working for a fee or commission on behalf of exporters, who then rapidly ship the vehicles overseas where international price differentials ensure huge profits. B.C.’s unique geographic location and ethnography make it an incredibly attractive venue for this activity.

A straw buyer is not the true purchaser of an asset but represents that he or she is. An exporter of luxury cars will employ networks of family, friends, or sometimes people recruited online or via word of mouth. These straw buyers or agents will sign the paperwork at dealerships, buy cars, and then drop them off to be exported. In return, they receive a small commission on the vehicle, typically ranging up to a few thousand dollars and corresponding less than 5% of the vehicle’s value.

Because the grey market vehicles are being exported with appropriate taxes paid and are not reported as stolen, [Canadian Border Services Agency] has neither the mandate nor the authority to detain or seize the vehicles prior to export, even if trade-based money laundering is suspected.

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<sup>4</sup> The Second German Report at pages 194-195.

<sup>5</sup> The Second German Report at pages 194-195.

<sup>6</sup> The Second German Report at page 196.

**BMW and the vehicle grey market**

24. BMW is aware of, and actively works to combat, the grey market for its vehicles.
25. In BMW's experience, the unlawful export of its vehicles typically occurs in the following manner:
- a. A straw buyer or nominee presents at a BMW dealership seeking to purchase a vehicle;
  - b. The straw buyer or nominee enters into an agreement for the purchase of the vehicle, pursuant to which a down payment is to be made, followed by payment of the balance of the purchase price, typically to be made in installments for a specified term (either as a lease or loan);
  - c. The straw buyer or nominee provides the down payment to BMW, usually in the form of bank draft as opposed to cash;
  - d. The straw buyer or nominee takes delivery of the vehicle;
  - e. Shortly after entering into the agreement for the purchase of the vehicle, the straw buyer or nominee contacts BMW to request a quote for an early payout of the financing attendant to purchase price of the vehicle;
  - f. Soon after this, the straw buyer or nominee provides a bank draft to BMW, representing the balance of the purchase price for the vehicle (i.e., a buyout of either the lease or loan contract);
  - g. The circumstances in which the bank draft is sent to BMW are routinely suspicious, leading BMW to suspect that the vehicle has already been transferred to an unknown third party, without BMW's consent in breach of the lease or finance agreement. BMW attempts to exercise its rights to periodically determine the location of the vehicle under the agreement, by:
    - i. Using GPS tracking equipment to determine the location of the vehicle. However, through human intervention, the GPS tracking equipment can be rendered non-responsive, resulting in a failure to indicate the vehicle's location. The failure of GPS tracking equipment, on its own, to indicate a vehicle's location is rare and unusual.
    - ii. Demanding that the straw buyer or nominee advise BMW of the vehicle's location and produce the vehicle for inspection. Again typically, the straw buyer or nominee reneges on producing the vehicle, or fails or refuses to do so.
  - h. BMW cannot determine the location of the vehicle.

- i. The vehicle is never recovered.

**Why is the vehicle grey market a problem for BMW?**

26. Customers who purchase, lease, or finance certain BMW models in Canada must sign a non-export agreement. The export of these specific models from Canada, within a certain timeframe after the customer takes delivery of the vehicle, constitutes a breach of the non-export agreement.
27. BMW has been and will continue to vigorously enforce its non-export agreements through civil litigation. As a good corporate citizen, it has committed to combatting money laundering. It upholds its commitment by seeking the assistance of the courts when necessary.
28. Additionally, BMW is aware of global trends and tactics in relation to money laundering. It has first hand indicators that exporters seeking to unlawfully export BMW vehicles often set up a scheme through which straw buyers or nominees are hired to carry out the purchase, lease, or finance of the vehicles. Through such schemes, illegitimate monies may be converted into a tangible asset, being a BMW vehicle, which is then exported from Canada and sold at a great profit in external markets.
29. Further, as Peter German describes in his Second Report, the grey market for the export of luxury vehicles takes advantage of current legislation to avoid paying provincial sales tax, which is not payable if the vehicle is purchased with the intent to resell.<sup>7</sup>
30. As exporters are legally entitled to have the provincial sales tax refunded, this results in a significant burden to the Ministry of Finance, as substantial time is required to process such tax return claims by civil servants.
31. Further, the Province of British Columbia loses millions of dollars in lost provincial sales tax revenue. On luxury vehicles in British Columbia, the provincial sales tax equals 10% of the purchase price of vehicles worth \$57,000 to \$124,999.99, 15% on vehicles \$125,000 to \$149,999.99, and 20% on vehicles worth \$150,000 and more.<sup>8</sup>
32. In this way, the vehicle grey market scheme interfaces with the legitimate economy.
33. The Commission and the people of British Columbia should be troubled that this is happening. BMW is troubled. BMW wishes to assist the Commission to make recommendations to curb the proliferation of the vehicle grey market. It is costing the Province significant money, while exporters make great profits, profits which may not be reported as income to the Canadian Revenue Agency and are therefore not taxed.

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<sup>7</sup> The Second German Report at page 198.

<sup>8</sup> The Second German Report at page 198.

**What has BMW been doing to combat unlawful exports?**

34. BMW is regarded as a leader in the automotive community in its commitment to combatting the unlawful export of its vehicles from Canada. This is why it asked to participate in the Inquiry.
35. The mechanisms that BMW employs to combat unlawful export activity include:
- a. The implementation of an export prevention policy applicable to BMW retailers across Canada, which mandates the use of a “know your customer” process and a “red flag checklist” to determine whether a sale, lease, or finance of a BMW vehicle should be completed;
  - b. The continual education of BMW retailers;
  - c. The auditing of BMW retailers;
  - d. The use of non-export agreements; and
  - e. The enforcement of non-export agreements through civil litigation.

***Internal policies***

36. BMW has implemented certain policies applicable to all BMW retailers across Canada designed to curb unauthorized reselling and unlawful export of its vehicles. These policies set out a series of mandatory steps its retailers are obliged to follow when selling, leasing, or financing certain BMW models.
37. As an industry leader, BMW revisits and amends these policies on a regular basis, to ensure that its practices effectively address the changing methods by which money laundering occurs in the luxury vehicle market. As part of this process, BMW conducts meetings with its retailers to ensure that lessons learned from the retail network are meaningfully incorporated into its policies and practices.
38. As mentioned, one of the mechanisms through which BMW attempts to curb unlawful export of its vehicles is through the implementation of a mandatory “know your customer” process. This process applies to all BMW retailers nationally and must be carried out each and every time a BMW vehicle is being sold, leased, or financed in Canada.
39. In certain circumstances, retailers are encouraged to carry out enhanced measures on top of the mandatory “know your customer” process, such as when the customer resides at great distance from the retailer or is new to BMW. In these circumstances, retailers may request additional financial or employment information from those customers to ensure sufficient credit-worthiness and to minimize the risk that the vehicle is not purchased with illegitimate funds.

40. Additionally, BMW retailers are required to use a “red flag” checklist in determining whether or not to complete a sale, lease, or finance of a BMW vehicle. This checklist asks the retailer to take into account a number of considerations about the customer, including:
- a. Whether the retailer that the customer is attending at is the closest retailer to the customer’s home or place of business;
  - b. Whether the customer is attempting to purchase multiple vehicles; and
  - c. Whether the customer is attempting to conduct the sales transaction via phone or email.
41. This checklist also asks the retailer to consider how the vehicle is being financed. There is a note warning that some schemes may involve financed or leased vehicles, with large cash down payments and minimal financing.
42. Another mechanism that BMW employs to curb money laundering is through the continual education of BMW retailers. For example, BMW leadership has clarified with its national retailer network that the practice of placing personal property liens on its vehicles will not provide the retailer with any additional protection to prevent unlawful export of vehicles as such liens can be paid out by a customer immediately.
43. By participating in the flow of information within the BMW retail network, BMW ensures that its authorized retailers maintain an accurate understanding of how unlawful export activity may be curbed effectively.
44. In addition, BMW conducts export compliance prevention audits of its retailers to ensure compliance with its non-export policies. At a minimum, BMW conducts audits on retailers whose reseller/export index is >3% of its total retail volume per calendar year.
45. In summary, BMW has established certain mandatory internal policies that bind all its retailers across Canada, including the obligation to carry out the “know your customer” process, the use of the “red flags checklist” each time a BMW vehicle is sold, leased or financed, and through the use of non-export agreements. Further, BMW conducts export compliance prevention audits of its retailers. As an industry leader, BMW’s approach to combatting the unlawful export of its vehicles and money laundering is comprehensive, employing the use of various safeguards.

***Non-export agreements and enforcement***

46. As set out previously, BMW employs the use of non-export agreements to curb unlawful export activity. Customers intending to purchase, lease, or finance certain BMW models in Canada must sign a non-export agreement as part of the transaction. Currently, this policy applies to BMW X5 and X7 vehicles sold, leased, or financed in Canada. The X5 and X7 models are luxury sport utility vehicles. These vehicles are particularly desirable for



exporters, as they may be sold abroad for a large profit and are seen as a status symbol due to their exclusive nature.

47. Material terms of the current version of the non-export agreement include:

- a. That the customer will not export the vehicle or permit the vehicle to be exported from Canada without the written consent of BMW within 12 months of receipt of the vehicle; or
- b. Enter into or acquiesce in any agreement whereby the vehicle is leased or sold for use outside of Canada.

48. Additionally, under the current version of the non-export agreement, BMW Canada has the right to periodically determine the location of the vehicle for the 12 months following a customer's receipt of the vehicle, or for the entire duration of the lease or financing of the vehicle through BMW Canada. It may do so by accessing the vehicle's GPS and/or other technology to confirm that the vehicle is located in Canada, as well as through automatic alerts that the vehicle has entered high risk zones associated with export activities, such as borders or ports.

49. Enforcement is a necessary part of BMW's multi-pronged approach to actively combatting money laundering. On May 9, 2019 alone, BMW commenced four actions in the British Columbia Supreme Court against individuals located in Coquitlam, Richmond, Surrey, and Burnaby, in breach of contract, conversion, and wrongful detention of BMW property. This series of litigation has been reported by the media, including by CBC News.<sup>9</sup>

50. In one such action, the defendant entered into an agreement to finance a BMW X5 vehicle with a purchase price of \$94,206.54. A down payment in the amount of \$24,955.74 was provided to BMW by the defendant. The balance of the purchase price was to be paid over a 60 month term. Approximately 10 months into the term, the defendant mailed a bank draft to BMW for the sum of \$59,600.68, representing the balance of the purchase price at that time. The bank draft was provided to BMW under suspicious circumstances, including that:

- a. It was sent in the same Canada Express Post envelope as another early payout bank draft for a separate BMW vehicle purchased by a different individual;
- b. Both bank drafts were from the same TD Bank account;
- c. Both bank drafts were issued on the same day; and
- d. Both bank drafts appear to have been signed by the same individual, whose name was not decipherable from the signature.

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<sup>9</sup> Jason Proctor. 'Do not be duped': BMW targets 'straw buyers' in race to stop luxury SUV exports'. (CBC News, May 29, 2019), <<https://www.cbc.ca/news/canada/british-columbia/bmw-export-money-laundering-1.5153224>>.

51. Similarly, each of the defendants in the other three actions commenced by BMW on May 9, 2019 also made large payments representing the balance of the purchase price of the vehicle by way of bank draft early on into the financing term:
- a. In one action, the balance of \$73,205.75 was paid out 6 months into the 60 month term;
  - b. In another action, the balance of \$93,726.67 was paid out 2 months into the 48 month term; and
  - c. In the third action, the balance of \$57,275.83 was paid out 6 months into the 60 month term.
52. In BMW's experience, the use of bank drafts to pay off manufacturer loans is commonly used in schemes to unlawfully export luxury vehicles.
53. Although the actions we described are still ongoing, BMW advises the Commission and the people of British Columbia that through the civil litigation process, it has successfully recovered vehicles destined for export in multiple cases.
54. BMW supports the imposition of regulatory requirements prohibiting cash transactions for vehicles in amounts above \$10,000.
55. BMW further supports the prohibition of the use of cash and cash-like instruments to pay off manufacturer loans, except where an instrument has sufficient information on it to link it to a specific account at an existing reporting entity, such as at a financial institution.
56. Completely barring the use of bank drafts would be unduly restrictive and impractical for BMW and its customers. For example, if a nominee purchased a luxury vehicle on a financing plan and then sought to pay off the balance, the province could require that funds must be sourced from a financial institution that is a "reporting entity". This would make these funds traceable and dramatically improve transparency, without relying entirely on the industry's own methods to combat these practices. This approach is highly efficient and significantly mitigates the need to expand the list of "reporting entities" under the federal regime.

### **Enforcement at ports**

57. In addition to adhering to internal policies designed to curb unlawful export of its vehicles and enforcing non-export agreements through the civil litigation process, BMW works with Canadian Border Services Agency ("**CBSA**") and police services, wherever possible, to prevent export of its vehicles through location and recovery. BMW seeks civil remedies to seize vehicles found in those circumstances, including vehicles financed and/or leased by BMW.

58. Sometimes these vehicles are driven from a BMW retailer's lot directly to a port for export. For example, in one instance, a BMW found at the port had only 10 km in mileage. When BMW vehicles are found for export, CBSA may contact BMW to determine if it has an interest in the vehicles. However, Canadian ports, including at Vancouver, Surrey, and Prince Rupert do not have a dedicated police presence, therefore resulting in a gap in law enforcement.<sup>10</sup> This makes it more difficult for BMW to identify and recover vehicles destined for unlawful export.
59. If BMW has an interest in the vehicle, it must make arrangements to recover the vehicle. CBSA has limited authority to assist BMW in recovering the vehicle, which is not considered a stolen vehicle by police services, as enforcement of non-export agreements is considered a civil, not criminal matter.
60. Practically, BMW will be advised as to the location of the vehicle, such as whether the vehicle is situated inside a container at a port or has been brought to a nearby towing yard, so BMW can arrange for pickup of the vehicle.
61. In BMW's experience, enforcement and transparency at ports should be dramatically improved. BMW is appreciative of the collaborative efforts of the CBSA and of local police – however, the volume of exports from Canada's ports exceeds the abilities of any one regulatory body to police those exports.
62. Accordingly, BMW seeks to work with the Commission to develop recommendations in relation to the increasing of assistance and enforcement at Canadian ports.
63. Specifically, BMW asks the Commission to consider recommending that the provincial and federal government regulate the export of vehicles from British Columbia and Canada.
64. This regulatory regime could impose transparency and reporting requirements on the exporters. In whatever form it takes, there should be enhanced regulatory requirements imposed on exporters that increase the difficulty of exporting vehicles unlawfully.
65. Currently, the industry, BMW, and its retailer network must dedicate its own resources to this problem without being able to rely on a regulatory framework or enforcement agency dedicated to preventing unlawful exports. Industry efforts on this issue alone can never be sufficient or comprehensive enough to provide maximum deterrence. BMW cares but it needs help.

## **Conclusion**

66. Money launderers will continually reform their methodologies to evade regulation. Any new provincial regime or expansion of the federal regime should carefully consider whether the new anti-money laundering requirements properly balance the additional compliance costs

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<sup>10</sup> The Second German Report at page 175.

and complexity imposed on industry against the ability of money launderers to evade the new requirements.

67. As the Inquiry progresses, BMW urges the Commission to remember that industry – especially the automobile retail sector – is not a regulator or a police service. It should not be expected to investigate into the possibility of predicate crimes or itself attempt to search through the chain of nominees and beneficial owners, which are often obfuscated.
68. An effective regime would ensure that any form of reporting and compliance is easy to implement at the level of the immediate transaction. It would also ensure that industry can benefit from and rely on pre-established registries. For example, a new regime could include reasonable “know your customer” requirements for certain kinds of purchases but also permit industry entities to rely on corporate beneficial ownership registries established, maintained, and enforced by government.
69. In summary, BMW has sought participation in this Inquiry because, as an industry leader, it believes it can assist the Commission in fulfilling its mandate in making findings of facts and recommendations with respect to money laundering in the luxury goods and financial services sectors. It is the only luxury vehicle manufacturer, distributor, and financial services provider who has applied for and been granted standing as a participant in this Inquiry.
70. Throughout the course of the Inquiry, BMW will engage in open and transparent dialogue with the Commission. In doing so, BMW is hopeful that Commission’s work will yield practical recommendations to curb and restrain money laundering in the province of British Columbia.