

ANTI-MONEY LAUNDERING GUIDELINES

FOR REAL ESTATE PROFESSIONALS

OVERVIEW

The crime of money laundering continues to be a growing area of concern in the United States. Therefore, law enforcement agencies and the financial sector devote considerable time and resources to combatting these illegal financial activities. However, many non-financial businesses and professions are also vulnerable to potential money laundering schemes. Real estate professionals are a category of the non-financial business sector that may encounter persons engaging in money laundering activities. The purpose of this fact sheet and suggested voluntary guidelines is to increase real estate professionals' awareness, knowledge, and understanding of the potential money laundering risks surrounding real estate and enable them to identify practical measures to mitigate the risks.

What Is Money Laundering?

Money laundering is the process criminals use to disguise the illegal origin of their funds. Certain criminal activities generate substantial proceeds. Legitimizing, or "laundering" this money through the financial system, is a critical component for criminals to hide their activities and not draw attention to their illegally derived proceeds.

The actual process of money laundering is a three step process that is initiated by introducing the illegal proceeds into the financial system, e.g., breaking up large amounts into small deposits or by purchasing financial instruments, such as money orders, which is referred to as placement. This is typically followed by distancing the illegal proceeds from the source of the funds through layers of financial transactions, referred to as layering, and finally by returning the illegally derived proceeds to the criminal from what appears to be a legitimate source, known as integration. A real estate transaction can be used in any one of the three stages of money laundering. For example, if an individual purchases a home and uses illegal funds as part of the down payment, this would be considered integration.¹

Generally speaking, most money laundering activities are concentrated in the financial sectors. Therefore, banks and other financial institutions are subject to anti-money laundering/counter-terrorist financing (AML) laws and regulations, primarily the Bank Secrecy Act (BSA), and have safeguards in place to help detect and mitigate money laundering activity. But other industries, such

¹ Financial Enforcement Crimes Network, Suspected Money Laundering in the Residential Real Estate Industry, April 2008.

as real estate, can also be exposed to questionable business practices and be utilized as a vehicle for money laundering activities.

The Role of Real Estate Agents

As a general matter, the real estate agent's AML risk is substantially mitigated by the fact that the great majority of real estate transactions involve regulated entities such as banks and non-bank mortgage companies, which have BSA obligations. However, when a transaction steps outside the norm or in cases where certain risk factors are present, as detailed below, a real estate agent faces an elevated chance of encountering a possible money-laundering scheme and should consider taking measures to address the risk.

As a real estate professional, knowledge of how real estate transactions normally progress and the resulting ability to recognize and evaluate whether variances from the norm may signify an enhanced AML risk is an important way real estate agents can help to mitigate AML risk in real estate transactions. This requires brokers and agents to be aware of how real estate transactions may be used in illegal financing schemes and what steps should be taken to detect and deter those activities. Being familiar with the signs of money laundering activity in the real estate market will help real estate agents to:

1. Identify potential money laundering activities;
2. Take appropriate steps to mitigate the money laundering risk; and
3. If necessary, alert the proper authorities to help deter and mitigate the use of real estate in money laundering schemes.

GUIDELINES

Law enforcement and financial experts have identified some of the warning signs of money laundering activity in connection with real estate. By familiarizing oneself with these voluntary guidelines, real estate agents can assist and help minimize the risk of real estate becoming a vehicle for money laundering activities.

Know Your Business

Every broker and agent should be aware of certain characteristics of a real estate transaction that may be indicative of illegal financing activities. A real estate agent's familiarity with the normal course of business will help them to identify any unusual or suspicious patterns. Law enforcement, regulators and the international community have identified multiple money laundering risk factors. In general, these risk factors (red flags) can be grouped in the three categories: country/geographic, customer, and transaction risk.

Geographic Risk:

Geographic risk may arise because the customer and/or the source of the customer's funds are located in a jurisdiction that has a weak AML regime, supports or funds terrorism, or has a high

degree of political corruption. Although there is no definitive list of such jurisdictions, one good source is the list of jurisdictions subject to sanctions of the Office of Foreign Assets Control (OFAC) of the U.S. Treasury Department. OFAC administers and enforces economic and trade sanctions based on U.S. foreign policy and national security goals. OFAC-administered sanctions can be either comprehensive or selective, and generally restrict or prohibit dealings (including business and financial activities) by U.S. persons or in the United States that involve countries (or persons) subject to OFAC sanctions. Countries subject to comprehensive OFAC sanctions include Iran, Cuba, and Syria. The names of individuals, groups, and entities subject to OFAC sanctions are generally listed on OFAC's List of Specially Designated Nationals and Blocked Persons.²

Customer Risk:

- Location of property in relation to the buyer.
 - Is there a large unexplained geographic distance between the two?
- Unusual involvement of third parties.
- Titling a residential property in the name of third party; for example, a friend, relative, business associate, or lawyer. Use of legal entities (corporations, LLCs or partnerships) that obscure the identity of the person who owns or controls them without a legitimate business explanation.
- High-ranking foreign political officials or their family members.

Transaction Risk:

- Under or over-valued properties.
 - For example, is the property owner selling the property for significantly less than the purchase price?
 - Does the seller seem disinterested in obtaining a better price?
- Use of large amounts of cash.
 - Buyer brings actual cash to the closing.
 - The purchase of a property without a mortgage, where it does not match the characteristics of the buyer.
 - While rules and regulations governing the financial sector are designed to detect situations where large amounts of cash are being introduced, real estate agents should keep this factor in mind when evaluating whether a transaction seems suspicious.
- Property purchases inconsistent with the individual's occupation or income.
 - Is the property being purchased significantly beyond the purchaser's means?
- Immediate resale of the property.
 - Especially if the sale entails a significant increase or decrease in the price compared to the prior purchase price, without a reasonable explanation.

² See www.treasury.gov/ofac/.

- Speed of transaction (without reasonable explanation).
- Unusual source of funding.
 - Example: use of third-party funds to purchase a property where it doesn't make sense, i.e. third-party is not a parent, sibling, etc., use several different sources of funds without logical explanation, funding coming from a business but property not being held in business' name, or purchase of property doesn't match the business' purpose.
- Purchases being made without viewing the property, no interest in the characteristics of the property.
- Any other activities which demonstrate suspicious behavior and do not make professional or commercial sense based on the agent's familiarity with the real estate industry and the normal course of business.

WHAT REAL ESTATE PROFESSIONALS CAN DO TO MITIGATE RISK

The presence of a single risk factor, or even multiple factors, does not necessarily mean the purchaser or seller is engaging in money laundering activities. The role of real estate agents is to be familiar with these risk factors, and exercise sound judgment based on their knowledge of the real estate industry, and when a combination of these factors truly raises a red flag, know the proper action to take.

Know Your Customer/Customer Due Diligence (CDD)

This is a critical component of the role real estate professionals can play in helping to identify and combat money laundering. Knowing an agent's true customer and understanding their interest and planned use for a property will help agents evaluate a situation where one or more red flags are raised.

The process by which the real estate agent forms a reasonable belief that he/she knows the true identity customer and is then able to assess AML risk, is commonly referred to as know-your-customer or customer due diligence (CDD). In cases where red flags are present, the agent should apply increased levels of CDD, which could include the following:

1. Obtain additional information, a driver's license, passport or other reliable identification document, to confirm the true identity of the customer.
2. If a legal entity is involved, such as a corporation or LLC, take additional measures to identify who actually controls or owns the entity and take risk based measures to verify the identity of the owner. This is commonly referred to as beneficial ownership information.
3. Obtain other appropriate information based on the agent's experience and knowledge to understand the customer's circumstances and business.

In addition, depending on the size of the firm, it may be appropriate for the agent to notify and discuss with senior management the higher risk customer or a particular situation that raises red flags, and to monitor the relationship if there are a series of transactions with the customer.

Reporting Suspicious Activity

When confronted with suspicious activity, real estate agents always have the option of reporting the information to local law enforcement or the FBI.

In addition, agents may also consider filing a suspicious activity report, or SAR, which is reported to the U.S. Treasury's Financial Crimes Enforcement Network (FinCEN). SARs are primarily designed for use by financial institutions and are a significant tool for enforcement agencies to combat money laundering. Real estate professionals are not required to file a SAR, but should be aware of the availability of this tool to the extent that they have reasonable suspicion that a transaction may be a vehicle for illegal financing activity.

The electronic SAR form is available at: <http://bsae filing.fincen.treas.gov/main.html>.

For further information or assistance regarding how to file a SAR, real estate professionals may call FinCEN's Regulatory Helpline 1-800-949-2732.

It is important to note that while the Bank Secrecy Act contains a safe harbor shielding financial institutions from civil liability in connection with the filing of a SAR, there is no precedent to suggest that the safe harbor would extend beyond financial institutions to real estate professionals. Therefore, a real estate agent should be prudent and file a suspicious activity report only after thoroughly evaluating the circumstances surrounding the suspicious activity, and additionally should consider consulting an attorney on the matter prior to filing a SAR. Otherwise, a real estate agent could subject themselves to civil liability as a result.

Form 8300

A Form 8300 must be filed by a business that receives more than \$10,000 in cash in the course of a single transaction or two or more related transactions. It is not a SAR and is not used to report suspicious activity. Form 8300 is an information report that is required to be filed by any trade or business (such as a car or boat dealer) that receives in excess of \$10,000 in cash in a single transaction. Therefore, if for any reason a real estate agent or broker receives more than \$10,000 in cash from a buyer or seller in the course of a real estate transaction, the form must be filled out and filed, and can be found at <http://www.irs.gov/pub/irs-pdf/f8300.pdf>.

Cash, for purposes of this requirement, includes cash equivalents such as cashier's checks, bank drafts, money orders. If the cash equivalent instrument is for more than \$10,000, the transaction will be reported by the issuing bank, and the agent does not need to also file a Form 8300. If, however, an agent receives a cashier's check or other cash equivalent of less than \$10,000, but which in combination with other cash or cash equivalents totals more than \$10,000, a Form 8300 must be filed.

CONCLUSION

While the illicit finance risk for real estate agents is often mitigated by the involvement of financial institutions already subject to strict AML laws, the use of real estate in money laundering schemes continues to be an area of concern to the government. Adherence to these voluntary guidelines will help the real estate agent identify potential money laundering risks. These voluntary guidelines will also help real estate agents be effective partners with enforcement agencies in detecting and addressing the use of real estate in illegal financing activities.