

## CLIENT ALERT

### FinCEN Finds Indications of Crime in Purchases of Luxury Real Estate, Expands GTOs to Six Major Metropolitan Areas

August 17, 2016

FinCEN has looked under the hood of luxury real estate purchases in Manhattan and Miami, does not like what it sees, and now has expanded its investigation to include six major metropolitan areas.

On July 27, the Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) announced new Geographic Targeting Orders (GTOs or Orders) temporarily requiring certain U.S. title insurance companies that receive the Orders to identify and report the natural-person beneficial owners of legal entities used to purchase high-end residential properties without external financing in six major metropolitan areas.

Title insurance companies that receive the GTOs also will be required to report details about the natural person that represents the legal entity making the purchase and about the legal entity itself. The new Orders take effect on August 28, 2016, and last until February 23, 2017.

They expand on GTOs FinCEN issued in January of this year for purchases of luxury real estate in Manhattan and Miami-Dade County (the January GTOs), which are set to expire on August 27, 2016. The expanded GTOs deepen FinCEN's efforts to investigate and take action against the use of residential real estate for money laundering, and increase the likelihood that FinCEN eventually will issue new rules on real estate under the Bank Secrecy Act (BSA).

#### The January 2016 GTOs for Manhattan and Miami-Dade

The January GTOs require that title insurance companies receiving the Order identify the beneficial owners of legal entity purchasers in certain real estate purchases valued at more than \$3 million in Manhattan and more than \$1 million in Miami-Dade County. These include purchases that were made at least in part using currency, money orders, or various types of checks, and without external financing.

The Orders require affected title insurers to obtain copies of driver's licenses or passports for beneficial owners and to report information from these documents to FinCEN. Please see Crowell & Moring's previous analysis of [those Orders here](#).

The Orders define beneficial owners as individuals who, directly or indirectly, own 25 percent or more of the equity interests of the entity that purchased the property. The Orders also require affected title insurance companies to obtain and report similar information on the primary representative for any legal entity purchaser and for the entity itself. The Orders require title insurers to record copies of the documents used to verify identity, to store these and other records relating to the insurer's compliance with the GTO for five years in a reasonably accessible manner, and to make them available to FinCEN or to "any other appropriate law enforcement or regulatory agency, upon request."

#### The Expanded GTOs

The new Orders expand these same reporting and recordkeeping requirements to include six major metropolitan areas, including the Boroughs of New York City; Miami-Dade County and two counties immediately north; Los Angeles County; the counties covering the San Francisco area; San Diego County; and the county that includes San Antonio, Texas. Each area has separate real estate threshold values for reporting purposes:

1. \$500,000 or more in Bexar County, Texas, which includes San Antonio.
2. \$1,000,000 or more in Miami-Dade, Broward, and Palm Beach Counties, Florida.
3. \$1,500,000 or more in the Boroughs of Brooklyn, Queens, Bronx, and Staten Island, New York City, New York.
4. \$2,000,000 or more in San Diego, Los Angeles, San Francisco, San Mateo, and Santa Clara Counties.
5. \$3,000,000 or more in the Borough of Manhattan, New York City, New York.

The Orders provide that covered entities and their officers, directors, employees and agents may be subject to civil and criminal penalties for violations of the orders.

### **The Possibility of New AML Rules for Real Estate**

FinCEN is using the GTOs to assess the risk that "corrupt foreign officials or transnational criminals" may be purchasing premium residential real estate in the name of shell corporations as a means of investing the proceeds of criminal activity while disguising their involvement. Information reported under the GTOs is shared with law enforcement agencies. FinCEN also anticipates that the GTOs will make it more difficult for individual purchasers behind covered transactions to disguise their involvement, mitigating the key vulnerability of such "all cash" transactions.

In a press release announcing the expanded GTOs, FinCEN confirmed that the January GTOs have provided law enforcement with valuable information about possible criminal activity and about additional assets relating to existing criminal suspects, and relied on these findings as a basis for expanding the GTOs to include premium real estate in other major metropolitan areas.

FinCEN is seeking information on real estate purchases without external financing in part because its existing regulations already provide some insight into and protection against financed real estate purchases through anti-money laundering (AML) regulation of banks, housing-related government sponsored enterprises, and residential mortgage loan originators. FinCEN estimates that existing Bank Secrecy Act (BSA) regulations already cover 78 percent of real estate purchases, and is using the GTOs to investigate the remaining 22 percent of purchases that fall outside coverage because they are made without external financing.

The agency also has taken other, broader steps to increase the availability of beneficial ownership information. On May 6, 2016, FinCEN issued a rule that now explicitly requires banks, brokers or dealers in securities, mutual funds, futures commission merchants, and introducing brokers in commodities to obtain and periodically update beneficial ownership information for their legal entity customers as part of their AML program obligations under the BSA. Please see Crowell & Moring's [analysis of that rule here](#).

These actions on beneficial ownership come against the backdrop of media reporting that the leaked "Panama papers" documents identify the use of shell companies by persons allegedly involved in criminal activity to purchase real estate assets anonymously in Miami and elsewhere, as well as a recent \$1 billion civil forfeiture complaint by the Department of Justice

alleging the use of proceeds of official corruption to purchase real estate in Manhattan, Los Angeles and Beverly Hills, all locations covered by the expanded Orders.

FinCEN has hinted that its GTOs may lead to new rules imposing AML obligations with respect to real estate. In the press release announcing the expanded GTOs, FinCEN said that the January GTOs were "informing future regulatory approaches" and that the new GTOs likewise would help the agency to "determine our future regulatory course." In a presentation to industry in April of this year, FinCEN's Director said that data collected from the GTOs would "help us gather information while furthering our incremental, risk-based approach to regulating this industry."

The BSA allows FinCEN to impose AML requirements on "persons involved in real estate closing and settlements" because such persons are within the Act's broad definition of "financial institutions." In 2003, FinCEN published an Advance Notice of Proposed Rulemaking (ANPRM) specifically to consider the imposition of AML requirements on persons involved in real estate settlements and closings. In the ANPRM, the agency recognized that real estate had been and might continue to be used for money laundering, and suggested that its definition of the term "persons involved in real estate closing and settlements" might include: "[a] real estate broker or brokers ... [o]ne or more attorneys, who represent the purchaser or the seller, ... [a] bank, mortgage broker, or other financing entity, ... [a] title insurance company, ... [a]n escrow agent, and ... [a]n appraiser." Ultimately, however, the agency never issued a rule. In her April 2016 presentation, FinCEN's Director noted that "[w]e have more data now than in 2003 to inform our decision-making."

### **Practical Considerations**

In the same April 2016 speech, FinCEN's Director also said that "[i]t was troubling to read that some legal and real estate experts mobilized immediately after the [January] GTOs were announced to provide suggestions about ways to evade the reporting requirements." This seems a clear warning from the agency about attempts to evade the terms of the GTOs, and should be read in conjunction with provisions in the BSA that prohibit the structuring of transactions to avoid BSA reporting requirements, including GTOs. Title insurance companies should be on the lookout for transactions that appear structured so as not to trigger reporting under the GTOs; changes made after the insurer informs potential purchasers of its obligations under the GTOs are especially suspect.

Title insurance companies that receive GTOs also should consider how they will gather the required information and who will be responsible for obtaining and reporting it. FinCEN's new beneficial ownership rule provides some guidance for reporting on beneficial ownership, including standard forms used to obtain this information that may be useful in deciding how to respond to the GTOs. Although that rule allows some reliance on representations by company officers of who the beneficial owners of a legal entity customer are, financial institutions receiving certifications of beneficial ownership still appear to be responsible for incorrect reporting where there are "facts that would reasonably call into question the reliability of such information."

Title insurance companies should be on the lookout for instances where there is an obvious disconnect between the information provided by the legal entity or its representative and other information available to the title insurer.

Title insurers also should consider the impact of any beneficial ownership information they receive on their obligations under sanctions administered by the Treasury Department's Office of Foreign Assets Control (OFAC).

Beneficial ownership information may reveal that sanctioned parties hold an interest in legal entity clients or in a real estate transaction, and prohibit U.S. persons from being involved.

Finally, title insurers should consider whether beneficial ownership information imparts actual or constructive knowledge that the transaction involves the proceeds of criminal activity, such that further participation in the transaction may give rise to criminal liability for money laundering.

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