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Client Alert

FinCEN Uses Updated Authority in New Sanctions Legislation to Expand Geographic Targeting Orders on Luxury Real Estate Purchases

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Relying on new statutory authority contained in the sanctions legislation recently signed by President Trump, FinCEN announced on August 22 that it would expand the scope of its Geographic Targeting Orders ("GTOs") on luxury residential real estate purchases to now cover transactions involving wire transfers. FinCEN also expanded the geographic scope of its GTOs to include a seventh major metropolitan area, Honolulu, Hawaii. FinCEN also has released new frequently asked questions, and new guidance that increasingly suggests that FinCEN is likely to issue new rules in the future that may impose anti-money laundering requirements on real estate brokers, escrow agents, title insurers, and other real estate professionals.

Earlier GTOs

The new orders represent a significant increase in FinCEN's efforts in this area. Starting in January 2016, FinCEN began to issue GTOs to require U.S. title insurance companies to, among other things, identify and report beneficial ownership information on legal entity purchasers making all-cash purchases of luxury residential real estate. The first GTO covered only two markets—Manhattan and Miami-Dade—and was for only a six-month duration that began in March 2016. After seeing substantial indicators of money laundering and other criminal activity from that initial trial, FinCEN expanded the order to cover all five 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. FinCEN has continued to renew the requirement through September 21, 2017. FinCEN has said that more than 30% of the transactions reported in response to the orders are the subject of independent suspicious activity reports ("SARs") filed by financial institutions on potential criminal activity.

The New GTOs, as Expanded by CAATSA

The newly announced GTOs require title insurance companies involved in "Covered Transactions" to collect and report to FinCEN information on the identities of the purchaser, the individual primarily responsible for representing the purchaser, and the beneficial owners of the purchaser (defined as each natural person who, directly or indirectly, owns 25% or more of that legal entity). "Covered Transactions" are defined as those in which a legal entity purchases residential real property at a price that meets or exceeds the threshold set for each of the geographic areas covered by the order (*e.g.,* $3 million for the borough of Manhattan, $1 million for Miami-Dade and surrounding counties), provided that the purchase is made without a bank loan or similar form of external financing and that it is made, at least in part, using currency or a cashier's check, a certified check, a traveler's check, a money order in any form, or a funds transfer (*i.e.,* a wire transfer). The new GTOs will run from September 22, 2017 to March 20, 2018.

The expansion of reporting requirements to include transactions involving wire transfers was made possible by new language in Section 275 of the "Countering America's Adversaries Through Sanctions Act" ("CAATSA"), the sanctions legislation concerning Russia, Iran, and North Korea signed into law on August 2, 2017. Section 275 of CAATSA amended the GTO provisions of the Bank Secrecy Act ("BSA"), which previously allowed FinCEN to impose temporary recordkeeping and reporting requirements with respect to transactions in "United States coins or currency" or "monetary instruments," to encompass transactions in "funds," thereby allowing FinCEN to demand information on wire transfers and addressing what some had viewed as a loophole in earlier real estate GTOs.

The Advisory, and the Likelihood of New Rulemaking

In its related advisory, FinCEN notes that it has authority under the BSA to regulate "persons involved in real estate closings and settlements" as "financial institutions," and suggests that this term "may include real estate brokers, escrow agents, title insurers, and other real estate professionals." While FinCEN notes that it "currently has exempted" such persons from the broader AML obligations that apply to regulated financial institutions, including the requirement to report suspicious activity, it has taken the unusual step of encouraging these unregulated parties to file voluntary SARs, and has clarified its view that they are protected by a safe harbor from liability in the BSA for doing so. FinCEN provides red flags of potentially suspicious activity to aid such persons in doing so, which also may be useful to regulated financial institutions. FinCEN's repeated references to "current" conditions, its unusual step of encouraging voluntary SAR reporting by parties not subject to AML program requirements, and its repeated expansions of the real estate GTOs and announcements of strong indications of criminal activity in this area all suggest an increased likelihood that FinCEN is considering a rulemaking in this area. Its suggested definition of "persons involved in real estate settlements and closings" provides further indication that FinCEN is considering what a rule might look like, and provides a window into who might be covered by one. This builds on previous statements by the agency that these GTOs are "informing future regulatory approaches" to this issue and will help the agency to "determine [its] future regulatory course."

Meanwhile, section 243 of CAATSA specifically references FinCEN's real estate GTOs in the context of Russian money laundering, requiring Treasury to produce an annual report to Congress describing interagency efforts to combat Russian illicit finance, including a summary of efforts by Treasury to "[e]xpand the number of real estate geographic targeting orders or other regulatory actions, as appropriate, to degrade illicit financial activity relating to the Russian Federation" in the United States. The reporting requirement, as well as the new statutory authority relating to wire transfers, appears to indicate that Congress is actively encouraging FinCEN to continue to explore new ways to use its GTO authority in the future.

FinCEN also notes in the advisory that persons involved in real estate settlements and closings are not entirely unregulated. Like any trade or business not subject to a separate "currency transaction report" ("CTR") requirement, persons involved in closings and settlements must report transactions in currency and certain monetary instruments to FinCEN on a Form 8300.

The FAQs

The FAQs clarify that a reporting title insurer "may reasonably rely" on the beneficial ownership information provided to it by the purchaser. This is a concept taken from BSA requirements on banks and other financial institutions to obtain and verify beneficial ownership information. It means that, although title insurers normally may rely on a purchaser's representation of who its beneficial owners are, in cases where the title insurer has information indicating that the beneficial ownership information provided by a purchaser may not be correct, it has an obligation to investigate further to determine whether the information is correct.

Separately, the FAQs confirm that a transaction must be reported under the GTOs where any part of the purchase price is paid using currency, a funds transfer, or the various types of monetary instruments described in the orders.

Practical Considerations

FinCEN notes in its FAQs that it "expects a Covered Business to implement procedures reasonably designed to ensure compliance with the terms of the GTOs, including reasonable due diligence to determine whether it (or its subsidiaries or agents) is involved in a Covered Transaction and to collect and report the required information." It also provides that covered businesses must keep all records relating to compliance with the GTOs for a period of five years. Title insurers that receive the order should take these obligations seriously. FinCEN previously has expressed its disapproval over reports of parties trying to evade reporting under previous real estate GTOs, and CAATSA also elevates the importance of the orders. Both make enforcement of any violations of the GTOs more likely.

Separately, banks need to prepare for the fact that real estate professionals involved in closings and settlements may begin filing voluntary SARs on real estate transactions, some part of which may flow through the bank. This is especially likely for real estate transactions that involve wire transfers. Banks will want to avoid situations where real estate professionals are reporting suspicious activity that the banks are not, and may wish to step up their scrutiny of transactions potentially subject to the new orders.

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