FinCEN Sets Its Sights on Luxury Real Estate

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Overview

On January 13, the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) issued Geographic Targeting Orders (GTOs) that will temporarily require title insurance companies to report the identities of the natural persons behind companies paying cash for high-end residential real estate in Manhattan and Miami-Dade County. FinCEN exercised its authorities under the Bank Secrecy Act (BSA) to impose these new requirements, which become effective March 1, 2016.[1]

The issuance of the GTOs marks the first time that the federal government has required real estate companies to disclose the names behind cash transactions. The GTOs reflect FinCEN's concern that some individuals use all-cash purchases, made without bank financing, to “hide their assets and identity.”[2] Information gathered pursuant to the GTOs will be stored in a FinCEN database intended to help law enforcement identify the natural persons involved in transactions vulnerable to money laundering abuse.

The GTOs are indicative of a recent increase in law enforcement scrutiny of the real estate industry. Treasury and federal law enforcement officials have signaled their interest in investigating luxury real estate sales that involve LLCs, partnerships, and other legal entities as buyers. Governmental interest is due partly to media reports on the rising use of companies by foreign buyers to shelter money in the United States. For example, an investigation by *The New York Times* found many hidden owners of high-end real estate who were the subjects of government investigations, including foreign government officials.[3] In addition, the FBI recently created a new unit to focus on money laundering, for which real estate will be one main focus, and Justice Department lawyers have begun to build cases around money laundering in real estate deals.[4]

GTO Requirements

The GTOs require certain title insurance companies to identify the beneficial owner behind a legal entity involved in residential real estate transactions worth more than $3 million in Manhattan and more than $1 million in Miami-Dade County. The GTOs define “beneficial owner” as “each individual who, directly or indirectly, owns 25 percent or more of the equity interests” of the legal entity that bought the property. The title insurance company must identify the beneficial owner(s), obtain and record each beneficial owner's driver's license or passport, and report the names of the beneficial owner(s) to FinCEN using Form 8300 within 30 days of the closing of the transaction.[5] The Form must also contain the identity of the individual primarily responsible for representing the purchasing legal entity. The GTOs require title insurance companies to retain all records relating to compliance with the GTOs for five years and to make the records available to FinCEN, other agencies, and law enforcement upon request.

Title insurance companies subject to the GTOs must “supervise, and [are] responsible for, compliance by each of [their] officers, directors, employees, and agents.”[6] Emphasizing the role of individuals, the GTOs require the title insurance companies to transmit a copy of the order to their CEOs, as well as to their agents. Title insurance companies should be aware of the GTOs' requirements and prepare compliance strategies.

The GTOs require reporting on transactions conducted in part via currency, cashier's, certified or traveler's checks, or money orders. This conforms to existing Form 8300 requirements. Real estate transactions conducted entirely through wire transfers, which are more transparent than cash transactions, are not subject to the GTO reporting requirements.

In addition to the definition of “beneficial owner” set forth in the GTOs, another component of the orders is likely to increase the information collection burden with respect to LLCs. FinCEN's instructions regarding the completion of Form 8300 require title insurance companies to provide the name, address, and taxpayer identification number of all LLC members. Given that LLCs are often the preferred vehicle for real estate purchases, title insurance companies should be prepared to collect and document substantially more information on these legal entities

Further, the new orders will affect a large number of real estate transactions. The relatively low dollar amounts mean that mainstream buyers may be caught in the net of the new GTOs.[7] In addition, it is common for buyers to mask their identities by using more than one company to purchase real estate and by filling out forms to create companies with the names of lawyers, other placeholders, or “nominees.” The GTOs are intended to shed light on the natural persons behind these companies. FinCEN already requires non-bank residential mortgage lenders and originators to maintain anti-money laundering (AML) programs and report suspicious activity,8 but until now, FinCEN exercised little oversight of cash buyers.

Potential Expansion

In 2001, the USA PATRIOT Act required the Treasury Department either to issue AML rules for real estate professionals, or to grant an exemption. In 2003, FinCEN issued an advance notice of proposed rulemaking seeking comments on how the real estate industry could help prevent money laundering.9 In light of industry concerns that the burden of new regulation would outweigh the benefit, FinCEN later declined to issue a final rule. Real estate professionals have instead operated under a regulatory exemption for over a decade.[10] In 2015, FinCEN Director Shasky Calvery suggested that FinCEN was contemplating ending the exemption when she told the West Coast AML Forum that “greater transparency of beneficial ownership information would make it more difficult for criminals to hide their purchases of luxury real estate through the use of shell companies."[11]

While the GTOs are limited in time and in geographic scope, it is possible that FinCEN will issue similar orders in different cities or lengthen the period of applicability. The issuance of the GTOs brings the United States more in line with the United Kingdom, where real estate agents are required to submit Suspicious Activity Reports to the government when they suspect a transaction involves funds from a criminal source

Order Period and Penalties

As noted, the GTOs take effect on March 1, 2016, and expire 180 days later, on August 27, 2016, although the record retention requirements continue for five years after the expiration date. FinCEN may elect to extend the order period, and/or impose additional requirements. According to FinCEN, title insurance companies and their officers, directors, employees, and agents may be liable "without limitation" for civil or criminal penalties for violating the terms of the GTOs.[12] The BSA provides for civil or criminal penalties for financial institutions or other persons who violate the Act or its regulations or orders.[13]

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[1] Financial Recordkeeping and Reporting of Currency and Foreign Transactions Act of 1970, 31 U.S.C. § 5311 *et seq*. (commonly referred to as the "Bank Secrecy Act"). Treasury has delegated to FinCEN its authority to issue GTOs pursuant to 31 U.S.C. § 5326. See Treasury Order 180-01; 31 C.F.R. § 1010.370.

[2] Press Release, FinCEN, FinCEN Takes Aim at Real Estate Secrecy in Manhattan and Miami (Jan. 13, 2016), https://www.fincen.gov/news_room/nr/pdf/20160113.pdf.

[3] *See* Louise Story & Stephanie Saul, "Towers of Secrecy: Stream of Foreign Wealth Flows to Elite New York Real Estate," *N.Y. Times* (Feb. 7, 2015).

[4] An example of a case involving alleged money laundering in real estate transactions is *United States v. Prevezon*, in which prosecutors allege that a portion of funds stolen from the Russian treasury passed through several shell companies, eventually ending up in Manhattan real estate holdings. 13-CV-06326 (S.D.N.Y. filed Sept. 10, 2013).

[5] Form 8300 is not a new report. It is also used by persons engaged in a trade or business to file a report with the IRS upon receipt of cash payments over $10,000. See https://www.irs.gov/pub/irs-pdf/f8300.pdf.

[6] FinCEN, Geographic Targeting Order, at III.E.

[7] For the week ending January 6, 2016, the average listing price for a New York City home on Trulia, a real estate website, was $3,957,049, suggesting that many properties will meet the threshold set out in the GTOs. Real Estate Data for New York, http://www.trulia.com/real_estate/New_York-New_York/market-trends/ (last visited Jan. 15, 2016).

[8] See 31 C.F.R. §§ 1029.291 (anti-money laundering programs for loan or finance companies),

1029.320 (reports by loan or finance companies of suspicious transactions).

[9] Anti-Money Laundering Program Requirements for “Persons Involved in Real Estate Closings and Settlements,” 68 Fed. Reg. 17,569 (Apr. 10, 2003).

[10] 31 C.F.R. § 1010.205.

[11] Jennifer Shasky Calvery, Director, FinCEN, Address at the West Coast AML Forum (May 6, 2015), https://www.fincen.gov/news_room/speech/html/20150506.html.

[12] FinCEN, Geographic Targeting Order, at III.F.

[13] 31 U.S.C. §§ 5321(a), 5322(a).

Authors

Paul Jakubowski

RETIRED PARTNER

paul.jakubowski@wilmerhale.com

+1 617 526 6948