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Real Estate Transactions Are FinCEN Targets: Far-Reaching Impact of Two Proposed Rules

*By Aurelie Ercoli, Katrina A. Hausfeld and Deborah R. Meshulam**

The Financial Crimes Enforcement Network of the Department of the Treasury closed the comment period for its advanced notice of proposed rulemaking, aimed at bolstering anti-money laundering regulations relating to real estate transactions. This rulemaking comes on the heels of FinCEN's separate notice of proposed rulemaking regarding the implementation of the beneficial ownership information reporting provisions of the Corporate Transparency Act. In this article, the authors provide background and highlight some of the key comments which could shape any final rule.

The Financial Crimes Enforcement Network (“FinCEN”) of the U.S. Department of the Treasury recently closed the comment period for its advanced notice of proposed rulemaking, aimed at bolstering anti-money laundering (“AML”) regulations relating to real estate transactions (the “Real Estate ANPRM”). FinCEN received over 148 comments from stakeholders on its proposal.

This proposed rulemaking, issued in December 2021, seeks to prevent and address money laundering through non-financed U.S. real estate transactions by creating a system to collect and report information related to such transactions.

And, it is not the only proposed rule promulgated by FinCEN which may have far-reaching impacts on real estate market participants. The Real Estate ANPRM comes on the heels of FinCEN's separate notice of proposed rulemaking (“NPRM”) regarding the implementation of the beneficial ownership information reporting provisions of the Corporate Transparency Act (“CTA”) (the “Beneficial Ownership NPRM”).¹ The Beneficial Ownership NPRM, for which the comment period also recently closed, seeks to require

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¹ Beneficial Ownership Information Reporting Requirements, Notice of Proposed Rulemaking, 86 Fed. Reg 69 (December 8, 2021) available at <https://www.federalregister.gov/documents/2021/12/08/2021-26548/beneficial-ownership-information-reporting-requirements>.

corporations, limited liability companies, and other similar entities formed or registered to do business in the United States to report their beneficial owners.

With the likelihood of new regulations from FinCEN this year, an overview of the proposals serves as a reminder of this administration's commitment to the fight against corruption and illicit finance in the U.S. real estate market, as well as other key industries. Both proposals were issued in the wake of the administration's announcement earlier in 2021 that the fight against corruption is a core U.S. national security interest, and just hours after the release of the first U.S. Strategy on Countering Corruption on December 6, 2021.

This article provides background and highlights some of the key comments which could shape any final rule.²

THE REAL ESTATE ANPRM

The Existing Real Estate Anti-Money Laundering Framework

The Bank Secrecy Act of 1970 ("BSA"), as amended by the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the "PATRIOT Act") and the Anti-Money Laundering Act of 2020 (the "AML Act"), among other legislation, imposes requirements for recordkeeping, monitoring and reporting on certain financial activity. FinCEN has the responsibility for implementing and enforcing the BSA. In particular, the existing AML framework requires financial institutions (as defined by the BSA) to establish and implement AML/CFT programs to detect and report suspicious transactions in order to combat money laundering, terrorism financing, and other illicit financing.

Two types of real estate transactions are currently covered under this framework, which account for over 80 percent of real estate transactions in the United States:

- *Financed residential and commercial transactions.* These transactions include those that involve a financial institution—such as a bank, mortgage lender or other equivalent entity—which is subject to AML/CFT reporting obligations. Banks, non-bank residential mortgage lenders and originators ("RMLOs"), and housing-related government sponsored enterprises ("GSEs") involved in those transactions currently bear the burden of collecting and reporting information

² Anti-Money Laundering Regulations for Real Estate Transactions, Advanced Notice of Proposed Rulemaking, 86 Fed. Reg 69 (December 6, 2021) available at <https://www.federalregister.gov/documents/2021/12/08/2021-26549/anti-money-laundering-regulations-for-real-estate-transactions>.

under the existing AML framework.

- *All-cash residential real-estate transactions over \$300,000 in specific cities.* This requirement currently applies only to residential real estate transactions in 12 cities (Boston, Chicago, Dallas-Fort Worth, Honolulu, Las Vegas, Los Angeles, Miami, New York City, San Antonio, San Diego, San Francisco, and Seattle) and is implemented through geographic targeting orders (“GTOs”) issued by FinCEN. Title-insurance companies currently bear the burden of reporting these transactions.

The remaining 20 percent of real estate transactions are exempt from reporting requirements. FinCEN now seeks to change that.

The Proposed Rules and Their Implications

Through the proposed rules, FinCEN intends to institute a broader regulatory framework to ensure consistent reporting nationwide and curb illicit financial activities involving non-financed real estate transactions.

According to a senior Biden administration official, the new regulations could include the imposition of controls and reporting requirements such as collecting, reporting, and retaining information about non-financed real estate purchases across the United States.³ In addition to the proposed rules, the U.S. Department of Treasury also established a three-year whistleblower program to reward those who help recover foreign-corruption linked assets, including those converted into U.S.-based property.⁴ The U.S. Agency for International Development (“USAID”) is launching a series of programs with similar goals.⁵

³ Remarks by Secretary of the Treasury Janet L. Yellen at the Summit for Democracy, U.S. Department of Treasury, December 9, 2021.

⁴ On January 1, 2021, the U.S. Congress overrode the president’s veto to enact the 2021 National Defense Authorization Act (the “NDAA”), which includes the Kleptocracy Asset Recovery Rewards Act (“KARRA”). KARRA authorizes Treasury to develop and implement a pilot program aimed at rewarding whistleblowers (up to \$5 million) who provide information leading to the restraint, seizure, forfeiture, or repatriation of assets held in U.S. financial accounts that are derived from foreign government corruption.

⁵ USAID, through its anti-corruption task force (“ACTF”), initiated a suite of programs addressing the localized drivers, enablers and manifestation of corruption. These programs include, among others: (i) the Empowering Anti-Corruption Change Agents Program, which, among other things, aims to promote protective measures for whistleblowers, civil society watchdogs, journalists, and others at risk for their work on corruption, and (ii) the Global Accountability Program, aimed at preventing, detecting, and mitigating corruption and building regional networks to take joint action against transnational corruption, kleptocracy, illicit finance, and strategic corruption.

The Real Estate ANPRM posed over 80 questions to market participants and others, and invited comments on the potential scope of the rule, particularly on the following topics:

- To whom new requirements should apply;
- Which transactions should be covered;
- The dollar-value reporting threshold;
- What information should be reported;
- How information should be reported; and
- Who should be responsible for reporting that information.

The BSA's Reporting Requirements Could Be Extended to Cover Virtually All Real Estate Transactions

The proposed rules would apply to “non-financed” real estate transactions, which the Real Estate ANPRM defines as “any real estate purchase or transaction that is not financed via a loan, mortgage, or other similar instrument, issued by a bank or non-bank residential mortgage lender or originator, and that is made, at least in part, using currency or value that substitutes for currency . . . or a cashier’s check, a certified check, a traveler’s check, a personal check, a business check, a money order in any form, or a funds transfer.”⁶

These so-called “non-financed” transactions could include purchases of real estate using cryptocurrency, which could be considered a “value that substitutes for currency.”

The Real Estate ANPRM contemplates expanding reporting requirements beyond the limited metropolitan areas specified by GTOs to cover the entire country.⁷ If the rules are adopted, any non-financed real estate transactions, regardless of its geographic location or value, would be covered under the BSA’s reporting requirements.

⁶ Anti-Money Laundering Regulations for Real Estate Transactions, Advanced Notice of Proposed Rulemaking, 86 Fed. Reg 69 (December 6, 2021) available at <https://www.federalregister.gov/documents/2015/09/01/2015-21318/anti-money-laundering-program-and-suspicious-activity-report-filing-requirements-for-registered>.

⁷ The current nine metropolitan areas include (1) the Texas counties of Bexar (includes San Antonio), Tarrant, and Dallas; (2) the Florida counties of Miami-Dade, Broward, and Palm Beach; (3) all New York City boroughs: Brooklyn, Queens, Bronx, Staten Island, and Manhattan; (4) the California counties of San Diego, Los Angeles, San Francisco, San Mateo, and Santa Clara; (5) the City and County of Honolulu in Hawaii; (6) the Nevada county of Clark (includes Las Vegas); (7) the Washington county of King (includes Seattle); (8) the Massachusetts counties of Suffolk and Middlesex (includes Boston and Cambridge, respectively); and (9) the Illinois county of Cook (includes Chicago).

Comments submitted by the U.S. office of Transparency International (“TI-US”) propose that FinCEN replace the existing GTOs with an even broader set of rules than that proposed by the Real Estate ANPRM.⁸ Specifically, TI-US makes eight recommendations on key aspects of a new AML rule for the real estate sector, which should:

- 1) Be permanent;
- 2) Be expanded to cover the entire country;
- 3) Eliminate dollar thresholds;
- 4) Include commercial real estate transactions;
- 5) Align the definition of beneficial owner with the definition used in the Corporate Transparency Act;
- 6) Expand coverage to include trusts;
- 7) Expand the information to be collected to include more traditional AML requirements, such as documentation relating to the source of the funds; and
- 8) Ensure at least one responsible party, and consider the primary responsible party to be title insurance companies, followed by escrow agent, the lawyer and then real estate agent.⁹

Conversely, comments submitted by the National Association of Realtors (“NAR”) support limited AML reporting requirements that would cover only non-financed residential real estate transactions and for which title insurance companies should be exclusively responsible.¹⁰ NAR strongly opposes FinCEN’s alternative proposed regulation to mandate full AML/CFT program requirements, including the establishment of AML compliance programs and a mandatory filing of Suspicious Activity Reports (“SARs”), which it views as overly burdensome and less effective than a beneficial ownership record keeping and reporting requirement. NAR points out that 87 percent of NAR’s members

⁸ Comments on FR Doc # 2021-26549 submitted by the TI-US, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0115> (last visited Feb. 26, 2022).

⁹ Comments on FR Doc # 2021-26549 submitted by the TI-US, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0115> (last visited Feb. 26, 2022).

¹⁰ Comments on FR Doc # 2021-26549 submitted by NAR, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0128> (last visited Feb. 26, 2022). The Consumer Data Industry Association (CDIA) also highlights the complexity and singularity of commercial real estate transactions and urge FinCEN to address these transactions separately from residential real estate. Comments on FR Doc # 2021-26549 submitted by CDIA, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0010> (last visited Feb. 26, 2022).

are independent contractors, small businesses and sole proprietors which, unlike banks, do not have the means to implement sophisticated AML/CFT programs.

Likewise, the American Land Title Association (“ALTA”) opposes any proposed rules that would subject title companies to bank-like AML requirements.¹¹ ALTA notes that imposing bank-like AML requirements on title companies would not enhance transparency and only add unnecessary and excessive costs to real estate transactions because (i) money utilized in a real estate transactions—whether financed or not—already flows through U.S.-based financial institutions that have AML requirements, and (ii) title companies do not have a continuing relationship with the buyer or seller, given that the average buyer will own their home for 13 years after purchase.

ALTA also recommends that FinCEN (i) hold off on proposing a rule until it finalizes its implementation of the CTA; (ii) develop a real estate specific transaction reporting program; (iii) address residential and commercial real estate transactions separately; and (iv) meet with industry software providers and commercial title data providers.

The Proposed Rules Could Expand Reporting Obligations to Virtually All Service Providers Involved in a Real Estate Transaction, Including Natural Persons

To fully address concerns related to illicit real estate transactions, the proposed rules would also broaden the categories of service providers subject to recordkeeping and reporting requirements for non-financed real estate transactions.

Under the current framework, title insurance companies are required to report non-financed real estate transactions above the \$300,000 threshold in the covered areas. While the scope of the Real Estate ANPRM is still undefined, reporting requirements could be expanded to other service providers involved in real estate transactions, such as real estate brokers, attorneys, title insurance companies, closing agents, appraisers, and/or inspectors. FinCEN specifically sought comment on:

- Which service providers should be required to collect information, maintain records, and report information on non-financed purchases of real estate; and
- Whether it should employ a hierarchical, cascading reporting obligations on different entities involved in the transactions to ensure there is always an entity required to report.

¹¹ Comments on FR Doc # 2021-26549 submitted by ALTA, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0020> (last visited Feb. 26, 2022).

Comments submitted by the American Bar Association (“ABA”) strongly oppose any proposed rules that would require lawyers who provide legal representation to a client in these transactions to disclose the identity and beneficial ownership of their clients or to report information about their clients’ transactions.¹² The ABA highlights the importance of preserving lawyer-client confidentiality “for the rule of law, for protecting the rights of the client, and as a primary line of defense against money laundering and other illicit activities.”

The ABA also strongly opposes “any proposals that would regulate lawyers as financial institutions or nonfinancial trades or businesses under the BSA and subject them to the suspicious activity reporting, due diligence, independent audit, and other AML requirements of the BSA.”

Conversely, ATLA notes that FinCEN should place reporting obligations on the party most likely to possess or collect the data or be in the most direct contractual relationship with the customer.¹³ Thus, according to ATLA, if FinCEN wants information about the transactions, the burden should be placed directly on the person conducting the settlement, such as title agents, direct operations of the title insurers or attorneys. If FinCEN wants additional information about the buyers, ATLA recommends that the agency impose the reporting obligations on their representatives: the buyer’s real estate broker/agent and their attorney.

The Real Estate ANPRM also contemplates including certain real estate purchasers within the rule’s scope, including:

- *Shell companies*: FinCEN considers such structures as frequently used to obscure the ultimate owner of real estate.
- *Trusts*: Several high-profile DOJ enforcement actions have involved the use of a trust to conduct corrupt and illicit real estate transactions. FinCEN believes consideration of any proposed rule should also include the risks presented by U.S. and foreign trusts.
- *Natural persons*: FinCEN is concerned about real estate money laundering risks involving the use of nominees or “straw-man” purchasers. It is interested in comments addressing the appropriate way to treat natural persons in regulations addressing money laundering through real estate transactions.

¹² Comments on FR Doc # 2021-26549 submitted by the ABA, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0018> (last visited Feb. 26, 2022).

¹³ Comments on FR Doc # 2021-26549 submitted by ALTA, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0020> (last visited Feb. 26, 2022).

In its comments, Global Financial Integrity (“GFI”) pointed out that much of the information FinCEN recommends for collection and reporting is information that is already routinely collected by the industry in the singular course of business, both for the purchase of a home or when a rental application is filed.¹⁴ GFI posited that filing parts of this information with FinCEN would be a simple additional step and require a process that could be easily adopted and automated if a rule were to apply across the country.

Separately, comments submitted by the Financial and International Business Association (“FIBA”) urge FinCEN to codify any new rules with clear definitions, limitations, qualifications and exemptions, to permit compliance departments of banks and other financial institutions subject to an AML program requirement to understand effectively and efficiently whether a Non-Financed Covered Real Estate Transaction is subject to FinCEN reporting requirements.¹⁵

THE BENEFICIAL OWNERSHIP NPRM

The Real Estate ANPRM is not the only proposed rule that could have consequences for the real estate industry. The CTA requires certain “reporting companies” to disclose beneficial ownership information to FinCEN, including each beneficial owner’s full name, date of birth, current address, and unique identifying number from a valid passport, driver’s license, or other state-issued identification document.

The proposed rules laid out in FinCEN’s Beneficial Ownership NPRM are designed to implement several key disclosure requirements of the CTA and to “combat, to the broadest extent possible, the proliferation of anonymous shell companies that facilitate the flow and sheltering of illicit money in the United States.”¹⁶ It was the first of three anticipated FinCEN rulemakings related to the implementation of the CTA’s beneficial ownership reporting requirements.¹⁷

¹⁴ Comments on FR Doc # 2021-26549 submitted by GFI, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0102> (last visited Feb. 26, 2022).

¹⁵ Comments on FR Doc # 2021-26549 submitted by FIBA, available at <https://www.regulations.gov/comment/FINCEN-2021-0007-0142> (last visited Feb. 26, 2022).

¹⁶ Fact Sheet: Beneficial Ownership Information Reporting Notice of Proposed Rulemaking (NPRM), December 7, 2021, available at <https://www.fincen.gov/news/news-releases/fact-sheet-beneficial-ownership-information-reporting-notice-proposed-rulemaking>.

¹⁷ Other anticipated rulemakings related to implementation of the CTA’s requirements for access to and disclosure of beneficial ownership and updating FinCEN’s existing customer due diligence rule so that it is consistent with new beneficial ownership reporting rules.

Entities Subject to Beneficial Ownership Information Reporting Requirements

The Beneficial Ownership NPRM identifies two types of reporting companies: domestic companies and foreign companies registered to do business in the United States, including corporations, limited liability companies, limited partnerships, business trusts, and other entities created by or registered by filing a document with a secretary of state or similar state or tribal office.

The NPRM proposes exempting 23 categories of entities from the new reporting requirements, including, for example, banks, entities registered with the SEC, large companies, or certain trusts to the extent that they are not created by the filing of a document with a secretary of state or similar office—largely because they are already subject to similar requirements or receive additional regulatory scrutiny.¹⁸

Exemption from reporting will extend to all subsidiaries wholly owned by a parent company that qualifies for an exemption—but, conversely, will not extend to entities whose ownership interests include even a minority interest held by an entity required to report. Comments from interested stakeholders, such as the Private Investor Coalition, urged FinCEN to also exempt single-family offices from the new reporting requirements, due to privacy and national security risks. It remains to be seen whether FinCEN will grant this request.

These new proposed reporting requirements are particularly significant to real estate market participants because the exemptions will apply primarily to large market participants, leaving non-exempt market participants subject to the new reporting and recordkeeping requirements. These new reporting and record-keeping requirements may be particularly compelling if FinCEN's final rule leans toward mechanisms similar to bank-like AML requirements. Such a rule could impose a significant burden on non-exempt real estate market participants in particular, which consist of independent contractors, small businesses and sole proprietors that may not have the means to implement these

¹⁸ The following entities are exempt from those new reporting requirements: securities issuers, domestic governmental authorities, banks, domestic credit unions, depository institution holding companies, money transmitting businesses, brokers or dealers in securities, securities exchange or clearing agencies, other Securities Exchange Act entities, registered investment companies and advisers, venture capital fund advisers, insurance companies, state licensed insurance producers, Commodity Exchange Act registered entities, accounting firms, public utilities, financial market utilities, pooled investment vehicles, tax exempt entities, entities assisting tax exempt entities, large operating companies, subsidiaries of certain exempt entities, and inactive businesses.

new requirements. As pointed out by NAR, regardless of how broadly FinCEN decides to expand AML requirements applicable to the real estate sector, to achieve effective implementation of these regulations the Agency will need to ensure robust education and training for real estate professionals.

Beneficial Ownership Information to Report

The Beneficial Ownership NPRM would require the “company applicant” of non-exempt companies to file a Beneficial Ownership Information (“BOI”) report with FinCEN, which must identify and certify each beneficial owner and the “company applicant.”

Under the Beneficial Ownership NPRM, beneficial owners include all individuals who either exercise substantial control over the entity or who own or control at least 25 percent of the ownership interest of the entity.¹⁹ A company applicant is the individual who files the document that forms the entity for a domestic entity or the individual who files the document that first registers the entity to do business in the United States for a foreign entity.

As proposed, the BOI report would include each individual’s:

- 1) Full legal name;
- 2) Date of birth;
- 3) Current residential or business street address; and
- 4) Unique identifying number from an acceptable identification document (e.g., passport or FinCEN identifier).²⁰

In addition, each non-exempt reporting entity must report its name, any alternative names through which the entity is engaging in business (d/b/a names), its business street address, its jurisdiction of formation or registration, as well as a unique identifier number such as the Taxpayer Identification Number (“TIN”), Dun & Bradstreet Data Universal Numbering System

¹⁹ The proposed rule sets forth three specific indicators of substantial control: (1) Service as a senior officer of a reporting company; (2) authority over the appointment or removal of any senior officer or dominant majority of the board of directors (or similar body) of a reporting company; and (3) direction, determination, or decision of, or substantial influence over, important matters of a reporting company. The proposed rule would also include a catch-all provision to make clear that substantial control can take additional forms not specifically listed. Each of these indicators supports the basic goal of requiring a reporting company to identify the individuals who stand behind the reporting company and direct its actions (i.e. individuals with nominal de jure or functional de facto authority). The proposed rule also notes that control that is “exercised in novel and unorthodox ways can still be substantial.”

²⁰ The NPRM specifically requires a scanned copy of the identification document from which the unique identifying number of the beneficial owner or company applicant is obtained.

(“DUNS”) number, or Legal Entity Identifier (“LEI”). Comments submitted by the American Bar Association urged FinCEN to clarify the type of information to report about company applicant, and also recommended that FinCEN develop a plan to educate reporting companies about these new reporting obligations.

Under the proposed rule, the timing for filing a BOI report would depend on (i) when a reporting company was created or registered, and (ii) whether the report at issue is an initial report, an updated report providing new information, or a report correcting erroneous information in a previous report.

Additionally, non-exempt companies created before the effective date of the final regulation would have a year to file their initial report and those created or registered after the effective date would have 14 days after their formation to file a BOI report with FinCEN.

The U.S. Small Business Administration expressed concerns about the economic burden that these new reporting requirements would create on small businesses and encouraged FinCEN to review this timeline for compliance and to align with Congress’ initial proposal that non-exempt entities comply with those new reporting requirements up to two years after the effective date of the regulations.

At the close of the comment period, more than 240 comments had piled up from stakeholders—including the U.S. Small Business Administration’s Office of Advocacy, the American Banking Association, Transparency International, the Private Investor Coalition, and the Business Law Section of the American Bar Association—seeking clarity or expressing concern regarding burdens imposed by the rules. While FinCEN said it would consider requests from some commentators, and possibly reopen the comment period, it noted that subsequent proposals will address many of the concerns raised in comments.

The rule comes after longstanding international criticism that the United States lacks appropriate measures to ensure corporate transparency. While it is being hailed by advocates as crucial to a jurisdiction’s resilience against corruption and directly related to the effectiveness of an AML framework, critics are concerned about the undue burdens that may be imposed on reporting companies. Privacy and national security concerns have also been raised.

KEY TAKEAWAYS FOR REAL ESTATE MARKET PARTICIPANTS

Real estate market participants should expect greater FinCEN scrutiny of transactions, with the potential for significant new burdens imposed on entities and individuals currently exempt from BSA reporting obligations.

In particular, a broader range of real estate service providers may soon be required to adopt AML/CFT policies and procedures, designate an AML/CFT compliance officer, establish an AML/CFT training program for appropriate employees, and conduct independent testing of the program to ensure compliance.

In addition, these service providers may also be required to report certain information regarding virtually every real estate transaction in which they participate. And, to further increase transparency and ensure that U.S. real estate markets cannot be utilized to launder illicit funds, certain market participants may soon be required to submit their beneficial ownership information to FinCEN in order to participate in the U.S. real estate market.

As the proposed rules evolve, market participants should expect expanded recordkeeping and disclosure requirements and should consider their ability to respond.