



NATIONAL ASSOCIATION
OF REALTORS®

430 North Michigan Avenue
Chicago, IL 60611-4087

Catherine Whatley, CIPS, CRS, GRI, LTG
President

Telephone: 312/329-8411
Fax: 312/329-5962

The Voice for Real Estate®

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Financial Crimes Enforcement Network (FinCEN)
P.O. Box 39
Vienna, VA 22183-0039

ATTN: Section 352—Real Estate Settlements. Financial Crimes Enforcement Network: Anti-Money Laundering Program Requirements for “Persons Involved in Real Estate Closings and Settlements”

Dear Sir/Madam:

The NATIONAL ASSOCIATION OF REALTORS® (NAR) appreciates the opportunity to submit these comments in response to the above Advance Notice of Proposed Rulemaking (ANPR). The NAR is America's largest trade association, representing more than 910,000 members involved in all aspects of the residential and commercial real estate industries.

NAR is very supportive of the Administration's efforts to implement and enforce rules to detect and prevent money laundering schemes and the financing of terrorism. It is unfortunate that we are now living in a time when such measures must be given strong consideration. NAR appreciates the Financial Crimes Enforcement Network's (FinCEN's) attempt through this Advance Notice to collect as much information as necessary before proceeding to regulate individuals involved in real estate closings. This is a sensible approach and we hope our comments assist the agency in this process.

The prospect of imposing anti-money laundering obligations on real estate brokerages is troublesome for a number of reasons. First, it is inappropriate to impose law enforcement responsibilities on an industry comprised of small businesses that are not trained in such matters, such as real estate brokerages. Second, it is questionable whether expanding Anti-Money Laundering (AML) coverage to real estate brokers, agents and others is a necessary step in the fight against money laundering and the financing of terrorism. The agencies have not been able to provide much evidence to support the need for additional safeguards. Current AML regulations as well as state real estate license laws already require record keeping and reporting of certain financial activities. Until a thorough analysis of specific money laundering techniques in the real estate transaction can be identified that are not already adequately addressed by current law or regulation, it would be premature to impose a new regulatory burden on this industry. This will not yield the desired results and may cause harm to the industry.

I will elaborate on these concerns by responding to the 4 questions in the proposal.

1. What are the money laundering risks in real estate closings and settlements?

According to FinCEN and others, there has been very little evidence to substantiate the claim that the real estate transaction is a money laundering risk. The proposal references a 1992 report written

by the National Institute of Justice (NIJ), International Money Laundering: Research and Investigation Join Forces. In an otherwise very detailed account of international money laundering practices and law enforcement strategies to address these practices, the report includes a very brief discussion of why the authors feel real estate transactions offer "excellent money laundering opportunities". The only indication of how they come to this conclusion is derived from their description of potential money laundering schemes involving real estate.

Three examples, not actual cases, are provided for how real estate can serve as a money-laundering vehicle. However, each example is clearly an exaggerated, worst-case scenario that involves back door cash payments of \$1-\$2 million dollars to willing participants in the transaction, i.e. the buyer or seller, and various contractors. It would be irrational to think that an AML program by a real estate practitioner will address these scenarios. Since all of these examples include large cash payments, existing reporting requirements are in place to document this activity.

The APNR also cites money laundering court cases that involved real estate. However, a review of those cases illustrates that the illegal activity that took place in these cases will not effectively be addressed by further regulating the real estate brokerage industry. The following is a summary of those cases:

In United States v. High, 117 F.3d 464 (11th Cir. 1997), defendants owned and operated a commercial and residential real estate business in the Atlanta metropolitan area. The defendants used their business to help drug dealers convert cash from drug sales into real estate assets by structuring the transactions to conceal the source of money in order to evade the currency transaction reporting requirements.

Similarly, one of the defendants in United States v. Leslie, 103 F.3d 1093 (2d Cir. 1997), used his own real estate company to launder the proceeds of drug sales by accepting \$750,000 in cash in exchange for checks drawn on the account of his real estate company. The defendant knew the cash came from the sale of cocaine because he was told so by undercover federal agents. This case is distinguishable from the others in that no property was used to launder money. The defendant claimed that he intended to purchase property with the illegal funds, but he was convicted for exchanging ill-gotten cash for checks. Any company with a checking account is subject to abuse in the same manner.

The defendants in United States v. Nattier, 127 F.3d 655 (8th Cir. 1997), were principals in their own real estate investment firm. One of the defendants abused his position at a bank to embezzle funds from one account into the account of the defendants' investment firm. Using the embezzled funds, defendants purchased property through the account of the investment firm in an attempt to launder the funds.

In each of these cases, the principals of real estate companies willingly participated in the criminal enterprise and were convicted as criminals. None of these cases demonstrate how an innocent real estate broker or agent was duped into helping launder illegal funds through the purchase of real estate or furthered a criminal enterprise. The facts are quite the opposite. Therefore, requiring real estate brokers to adopt and implement anti-money laundering programs would not alter the outcome of cases such as these.

2. How should persons involved in real estate closings and settlements be defined?

Under the Act, the term "financial institution" includes "persons involved in real estate closings and settlements". This phrase is not otherwise defined and there is very little in the way of legislative history to guide the agencies to determine which parties to the transaction should be included.

According to the ANPR, the term might reasonably include:

- A real estate broker or brokers,
- One or more attorneys, who represent the purchaser or the seller,
- A bank, mortgage broker, or other financing entity,
- A title insurance company,
- An escrow agent, and
- An appraiser, who may assess the condition and value of the real estate, as well as various inspectors

The above list more appropriately describes, "persons involved in real estate transactions" rather than "persons involved in real estate closings or settlements." If the purpose of the question is to specifically identify those who play a role in a closing or settlement, then the list becomes much shorter. Many of the providers listed above complete their work before the closing and therefore are not a necessary party to the closing. This would be true for real estate brokers and agents, appraisers, inspectors, mortgage lenders, and others. On the other hand, in addition to the buyer and seller, the closing or escrow agent serves an integral role in the closing or settlement. The closing agent can be a title company, an escrow company, a lawyer, and in some limited cases a real estate broker. Whether or not they should be subject to additional regulation is questionable.

While most real estate agents accompany their clients to the closing or settlement, they are not sufficiently involved in the process to warrant regulation. Real estate licensees are already highly regulated by state license laws that strictly govern the handling of deposits and escrow monies. In addition, earlier amendments to the Bank Secrecy Act (BSA) require licensees and others, to file reports with the federal government when they are in receipt of \$10,000 or more in certain types of currency. These reports must contain: (1) the name, address, and such other identification information of the person from whom the coins or currency was received; (2) the amount of coins or currency received; (3) the date and nature of the transaction; and (4) such other information, including the identification of the person filing the report, as the Secretary may prescribe. In addition, Form 8300, used to report cash payments of over \$10,000 contains a box to check if the person completing the form wants to report suspicious activity voluntarily, and the directions to the form include the telephone number for the IRS Criminal Investigation Division.

3. Should any persons involved in real estate closings or settlements be exempted from coverage under section 352?

Yes. At a minimum, NAR believes for reasons already stated real estate brokers and agents should be exempt from this rule. Real estate transactions can be very complex and involve a number of professional service providers. Each serve different functions in the transaction and possess varying

amounts of knowledge about the transaction, the property and the parties to it. For example, the home purchase transaction usually involves 3 steps: 1) the home selection, 2) the mortgage financing, and 3) the closing or settlement.

The Home Selection Stage

The real estate broker/ agent facilitates the home selection stage of the transaction. **While the level and range may vary per transaction**, some of the more common services provided by an agent when working with a homebuyer include the following:

- Identifies available properties that match the needs and desires of the homebuyer, i.e. size, style, features, location, accessibility to schools, transportation, shopping and other personal preferences.
- Helps the purchaser determine what they can afford
- Recommends lenders and other third party providers services such as home inspectors
- Facilitates the negotiating process between the buyer and seller to reach agreement on specific transaction details such as the purchase price, the inclusion or exclusion of repairs and furnishings, contingencies, appropriate inspections and disclosures, and the date of possession
- Schedules many of the inspections and third party services, i.e. home inspection, appraisal to ensure a timely progression of the transaction.

On the selling side of the transaction, the real estate broker/agent typically provides the following services:

- Helps seller establish a selling price or range utilizing a comparable market analysis
- Provides advice on how to improve the appearance of home for sale
- Markets the property to homebuyers and other agents by utilizing various means, i.e. newspapers, Internet, MLS, open houses
- Reviews with seller offers from buyers and negotiates the best deal for the client
- Collects and deposits into a trust account earnest money deposits from buyers
- Ensures all required disclosures are made and the purchase contract is complete and accurate.
- Coordinates with buyer's agent and third parties to meet deadlines to ensure a timely progression of the transaction

These services do not present opportunities to identify potential money laundering activities. The only time an agent will be in receipt of funds is when an earnest money deposit is required to accompany the sales offer. Very strict state license laws prescribe the handling of these funds, therefore making additional reporting or record keeping requirements redundant. In most cases, the funds collected are in the form of a personal or certified check.

For example, Michigan's state license law requires a bookkeeping system that consists of the following:

(a) a record which shows the chronological sequence in which funds are received and disbursed, as follows:

- (i) For funds received, the record shall include all of the following information:
 - (A) The date of receipt and the date of deposit.
 - (B) The name of the party who provided the funds to the broker
 - (C) The name of the seller
 - (D) The amount of the funds
- (ii) For funds disbursed, the record shall include all of the following information:
 - (A) The date of disbursement
 - (B) The payee
 - (C) The check number
 - (D) The purpose of disbursement
 - (E) The amount of the disbursement

Most state laws have similar record keeping requirements. In addition, if a buyer submits cash in excess of \$10,000, a federal reporting requirement is triggered to provide very detailed information about the individual to the IRS. The business must also maintain these records for 5 years.

Real estate brokers that handle commercial transactions pose no greater risk of abuse by money launderers than residential practitioners. In general, the mechanics of a closing for commercial property is the same as a residential transaction. The same people perform the same functions. However, real estate brokers are less likely to attend commercial closings because they are not a necessary party to the closing and commercial clients need less counsel from their brokers. Like their residential practitioner counterparts, commercial brokers focus on marketing the property and bringing the buyer and seller together.

The Financing and Settlement Stage

The other stages of the transaction include the financing and the settlement process. The financing process in both the residential and commercial transaction includes several steps such as the collection of information and reports about the borrower and the property, verification of personal and financial information and documentation of every characteristic of both the borrower and property. Lenders typically do not attend the closing, however they are in possession of more information about the borrower than anyone else in the transaction. If the lender is a bank or credit union, existing AML requirements apply.

The settlement is the final stage in the transaction. While the title or escrow company by function come the closest to meeting the test of "persons involved in real estate closings and settlements", it is questionable as to how much information they actually possess to be able to identify money laundering activities. The closing or escrow agent functions as an impartial third party that facilitates the legal transfer of title to the property and funds. They ensure that "concurrent performance" takes place, that the deed transferring title from the seller to the buyer takes place on the same day that the buyer's money is released to the seller. By this time, any questionable funds that may have entered the

transaction have already been reported by the bank involved, the wire transfer service or any party who has been in receipt of \$10,000 in cash. Therefore, additional rules are unnecessary.

4. How should the anti-money laundering program requirement for persons involved in real estate closings and settlements be structured?

When prescribing minimum standards for money laundering programs, the Treasury Secretary is directed to “consider the extent to which the requirements imposed are commensurate with the size, location and activities of the financial institutions to which the regulations apply.”

The minimum requirements set out in the ANPR would be extremely burdensome to small companies. While NAR is a large association, sixty-seven percent of its residential brokerages have a sales force of five or fewer agents. It would be very difficult for these offices to hire a compliance officer, create a training program and to contract with an independent auditor to test the program. Real estate companies are not financial institutions in the true sense and therefore do not possess the knowledge or experience in what will effectively become a new law enforcement duty. Most companies will have to hire this expertise or dedicate the time and resources to develop and train existing personnel.

Rather than impose additional requirements, the agency should look to the existing body of law to identify areas that can be enhanced to provide the information being sought. Several laws already require the reporting of certain activities. For example, every real estate transaction that closes must be reported to the IRS by the closing agent on Form 1099-S. Banks and other financial institutions must also file Currency Transaction Reports (CRT's) for the receipt and disbursement of cash in excess of \$10,000. IRS Form 8300 must be filed by any person involved in a business that receives cash payments in excess of \$10,000 in a single transaction or a series of related ones. Bank employees are required to file a Suspicious Activity Report (SAR) when they have reason to suspect a person of money laundering. The real estate brokerage community is also heavily regulated by state license laws that place strict rules on the handling of funds. These existing requirements of maintaining records and filing reports with the government help to create a paper trail for law enforcement when investigating money-laundering schemes. Before adding to this ever-growing compliance burden, the agency should evaluate the effectiveness of these existing requirements.

Conclusion

The ANPR discusses the three stages of money laundering: placement, layering and integration. In the placement stage illegal funds are first placed into the financial system. The ANPR uses the example of a drug dealer purchasing a property with large cash down payment. However it is unclear how a real estate practitioner would be able to identify potential money laundering schemes such as this one. Existing reporting requirements of the cash receipt will identify this transaction and allow for voluntary suspicious activity reporting. In addition, the large cash down payment assumes there will be financing involved. Financial institutions such as banks and credit unions already have in place AML programs. To place additional or duplicative responsibilities on other parties to the transaction may not yield additional benefits.

It becomes even more questionable how a real estate practitioner can be of help in the next stages of layering and integration. In these stages, attempts are made to further disguise the already partially cleansed illegal funds and make them appear legitimate. One way this might be done is through cash rich businesses such as restaurants and bars. These seemingly legitimate businesses can be used to launder money acquired through illegal means. However, it is difficult to see how a real estate practitioner or any other party to the transaction would be able to detect future illegal activity at the time of the property sale. At this stage, it would be difficult for anyone other than law enforcement to detect such practices.

There is little doubt that real estate is subject to abuse by money launderers. The issue for Treasury to determine, however, is whether the benefit of having "persons involved in real estate closings and settlements" adopt and implement anti-money laundering programs would outweigh the burden to the industry. From the perspective of a real estate broker, the answer is clearly "no." Real estate brokers are not persons involved in real estate closings and settlements. Their role in the transaction is to market the seller's property or assist the purchaser in identifying a suitable property and negotiating a purchase contract. Without evidence suggesting that regulation would substantially benefit the fight against money laundering, the burden on brokers of having to adopt and implement anti-money laundering programs clearly outweighs any perceived benefit.

NAR appreciates the opportunity to present our views and we look forward to working with you in the future on this very important issue.

Sincerely,



Catherine B. Whatley, CIPS, CRS, GRI, LTG
2003 President NATIONAL ASSOCIATION OF REALTORS®