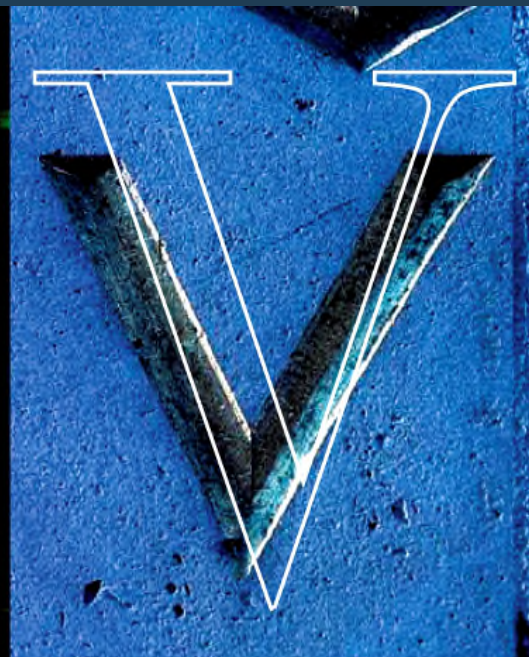


# VENABLE<sup>®</sup>LLP

## *Anti-Money Laundering Controls for Residential Real Estate Transactions*

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## Topics covered

- Focus on three sets of controls
  - Anti-money laundering
  - Economic sanctions
  - Foreign Investment
- Explain control structures
- Outline scope of controls
- Discuss recent cases
- Questions



# Purposes of Financial Controls

- Law Enforcement
- Foreign Policy
- National Defense
- Economic Controls
- Capital Flight
- Tax Avoidance



## Financial Controls: U.S. Treasury

- Money Laundering -- Financial Crimes Enforcement Network (FinCEN)
- Economic Sanctions -- Office of Foreign Assets Control (OFAC) (State sets policy)
- Foreign Purchasers -- Committee on Foreign Investment in U.S. (CFIUS)



# Setting the Stage – Money Laundering

## How did we get here?

- What is Money Laundering?
  - Introduction of dirty money into the legitimate financial system, “layering” the money through a series of transactions to separate the money from its illicit origins, and “integrating” the dirty money into legitimate commerce.
- Not to be confused with Terrorist Finance
  - May be dirty money, but frequently is clean money used for terrorist purposes.



# Anti-Money Laundering: Drug Wars to 9/11

- Politics of Contraband
- Kilo of Cocaine v. US Street Money equivalent
- Layering & Integration = Clean Money
- Enormous Quantities to Very Finite Amounts
- Result is complex compliance structure



# Drug Money Characteristics

- Bulk Cash -- \$20 bills
- Problem in Entry into Financial System
- Dirty Money Cycled to Legitimacy
- To Fund “Clean” Businesses
- Drugs and Corrupt Money.
  - UN Estimate: \$800 Billion to \$2 Trillion/year



# Terrorist Money Characteristics

- Small amounts
- Plain vanilla transactions using normal channels
- A needle in a needle stack
  - 9/11: AA FI 11 (BOS-LAX)(North Tower)
    - \$184,098.24 (from 1/2000 to 9/11/2001, five people, cash, lodging, auto, flight lessons, airline tickets, food, *etc.*)
  - *USS Cole*: Less than \$10,000 (2000)
  - Hotel in Jakarta: ~\$30,000 (2003)
  - Madrid subway: ~\$10,000 (2004)





## AML Controls: Financial Institutions

- Bank, thrift, credit union, trust company;
- Dealer in securities;
- Money services business (exchange, money orders, *etc.*);
- Insurance company;
- Prepaid access; and,
- Dealer in precious metals and stones.

### **BUT NOT:**

Real Estate Mortgage Lender or Originator  
(RMLO)



# AML Controls: Basic Program Elements (Applies to RMLOs)

1. Risk-based AML Program – in Writing, Approved by Senior Management
2. Compliance Officer
3. Ongoing Employee Training
4. Independent Audit Function



# AML: RMLO v. Financial Institutions

## RMLO Required

- AML Program
- SARs
- Form 8300
- 314(a)
- 314(b)
- FBARs
- CMIRs

## Not Required

- CTRs
- CIP
- Special recordkeeping
- Section 311



# AML & Real Estate Transactions: Red Flags

- Location of Property in Relation to Buyer
- Economic purpose of transaction
- Buyer
  - Identification
  - Location (country, address (P.O box))
- Intermediaries, family members, shell companies
- Relationship of Buyer and Seller
- Payment
  - Source
  - Type



# Current Regulatory Focus and Trends

## AML as Compliance Priority

- Renewed Focus on BSA/AML
  - Compliance Culture
  - Tailored Risk Management Systems
  - Information Technology (“IT”) Strength
  - Resources
- New (and old) Challenges
  - Not required of RMLOs, but: Know your customer (beneficiaries and owners too)
  - Expectation for entities to “police” business partners and service providers
  - \$10,000 Cash
  - Foreign Bank Account Reports
  - Currency or Monetary Instrument Reports



# Current Regulatory Focus and Trends

## Other Areas of Focus

- Transparency: Promoting a Culture of Compliance
- Trade based money laundering
- Human Trafficking
- Cash Couriers
- Funnel Accounts
- Geographic Targeting Orders
- Marijuana Banking

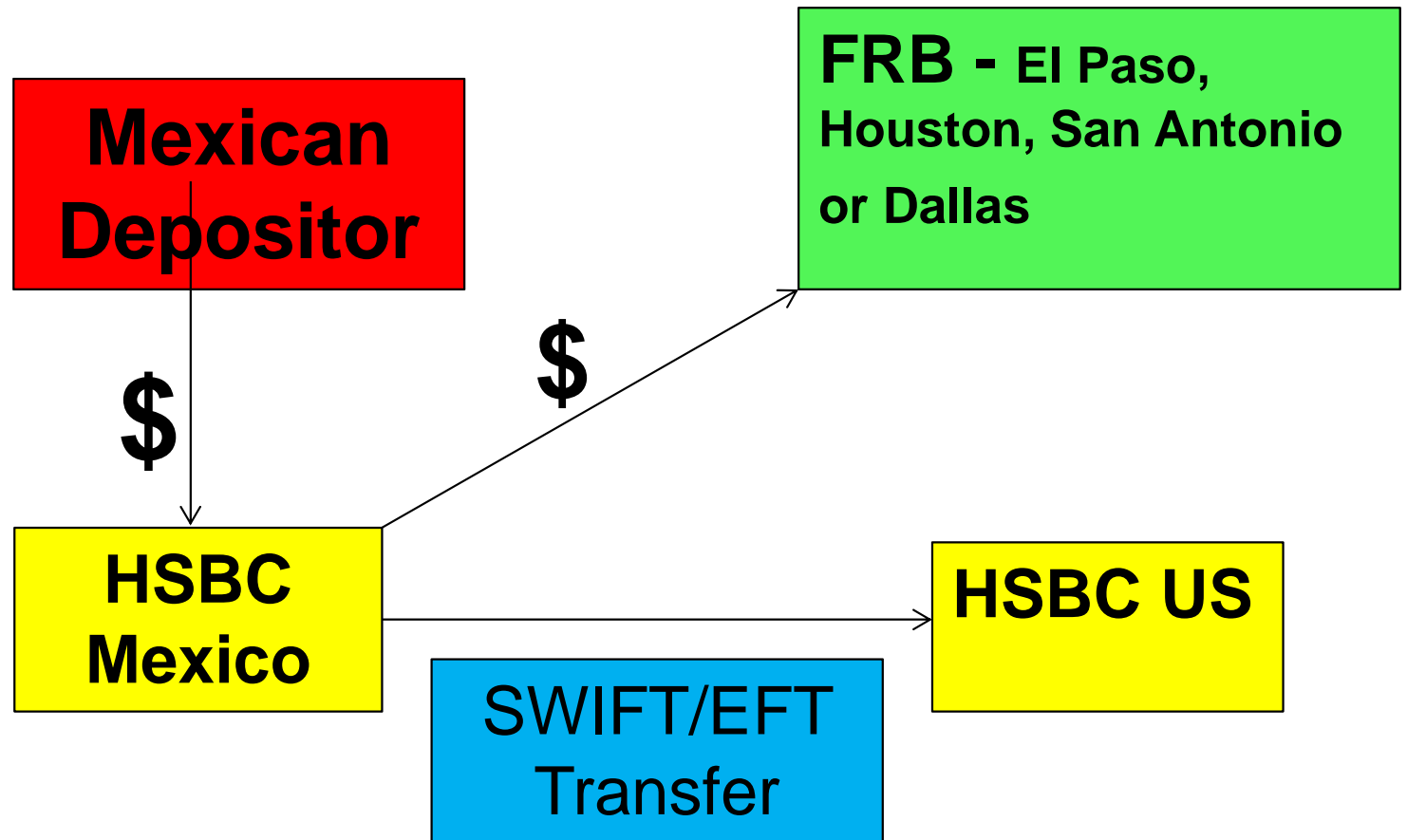


# Recent Enforcement Actions

- Recent High-Profile Enforcement Activity
  - Enforcement and examination regulators focused on BSA/AML compliance
    - Large and small financial institutions
    - Individual officers and directors
  - Expect continued escalation of fines and other sanctions (e.g., growth limits, activity restrictions, individual sanctions and, for banks, in egregious cases, charter revocation)



# HSBC -- \$500 Million Fine





# Economic Sanctions: Foreign Policy Controls

- Block assets for use as bargaining chips
- Freeze assets or refuse to deal to encourage change in behavior
  - Change in government
  - Change in actions
  - Change in policies
- Unilateral and multilateral sanctions
- Increasing law enforcement component



# Different Types of Targets

- Economic sanctions programs imposed by the President or Congress against
  - Countries (Russia, Iran, Sudan, Cuba, N. Korea)
  - Foreign Groups or Persons
    - Terrorist Organizations & Terrorists
    - Political Parties
    - Drug Kingpins & Drug Traffickers
- Which or Who “pose a threat to the National Security of the United States”



# OFAC: Office of Foreign Assets Control

- Part of the Office of Intelligence and Terrorism Finance, U.S. Treasury:
  - Director Appointed by Secretary
  - Reports to Undersecretary for Intelligence and Terrorism Finance
- “Economic Warriors” of the U.S.



# OFAC Compliance: Coverage

- All U.S. Persons, wherever located:
  - Legal Entities
    - U.S. Government and Government sponsored
    - U.S. Company, Partnership, wherever operating
    - Non-U.S. Subsidiaries of U.S. companies as to Cuba and North Korea only
  - U.S. Citizens, wherever located
  - U.S. Permanent residents, wherever located
  - Anyone in the U.S.
- Property in U.S. of Anyone on “List”



# OFAC & Commercial Transactions

- “Property or Interest in Property”
  - Could not be defined more broadly.
  - Direct or indirect interest
- Responsibility for compliance may not be delegated
  - Reliance on lenders, suppliers, *etc.*, is not protection.
  - Down (and Up) stream due diligence required
- Important distinction from anti-money laundering controls



## Minimum OFAC Compliance:

- Routine Procedures for Screening all Transactions, Investors, Counterparties against SDN List (Wells Fargo, 6/27/13)
- Clear Representations and Warranties
- Swift, Accurate Reporting to OFAC
- Lack of Electronic Systems at Company's Peril
- Attorney Responsibilities

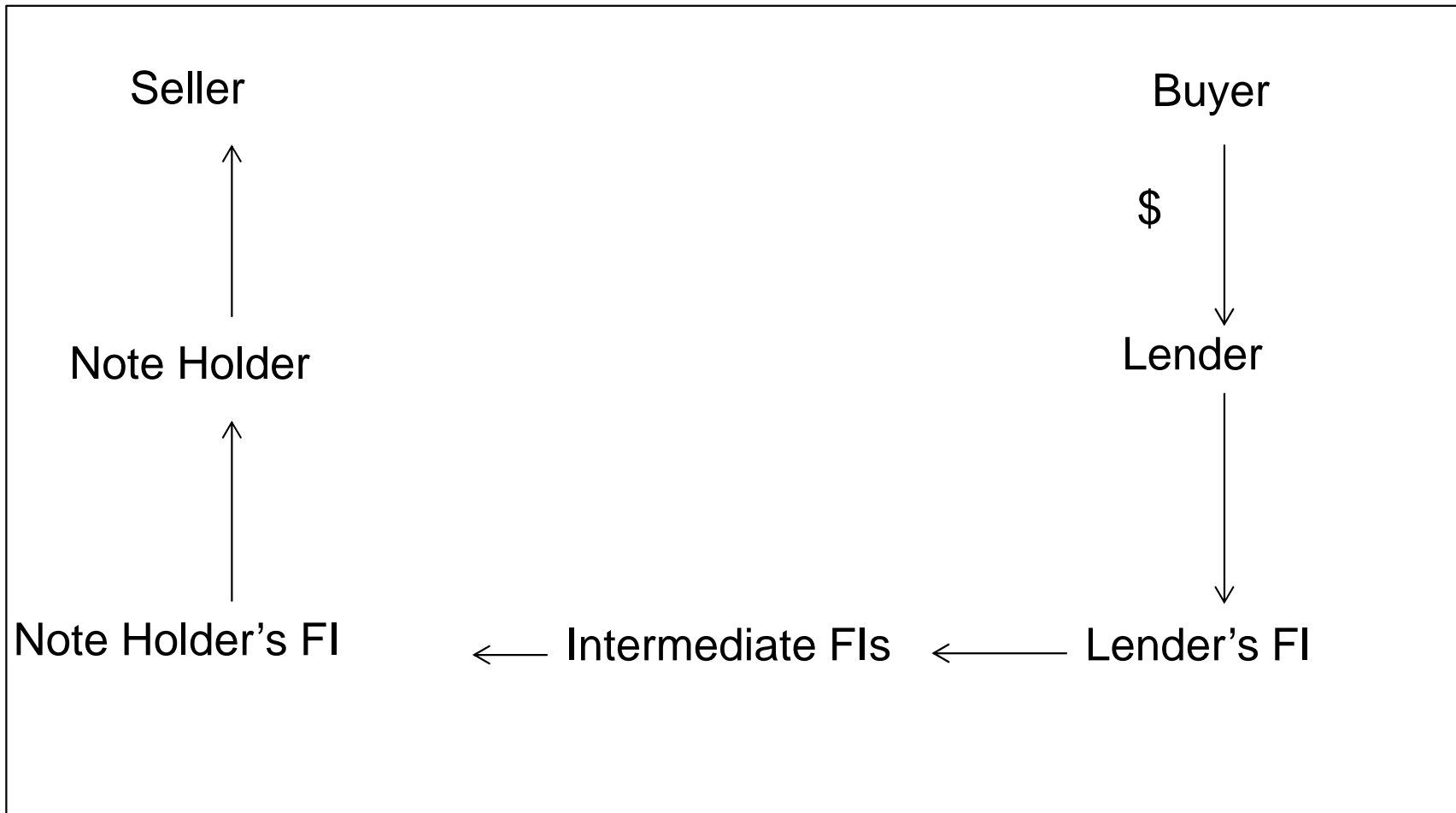


## OFAC: Compliance Objective

- Exclude contact with a person or entity on the List of Specially Designated Nationals (SDN List) or State List
- Push obligation to check and responsibility for compliance as far away from our clients as possible (risk reduction)
- BUT: Strict liability statutes



# OFAC: Risk Assessment & Checking the List



FI= Bank, Brokerage, etc., see AML Slides





# Recent Enforcement Actions

## OFAC

- Sept. 2014 – Citigroup agreed to pay \$217,841 to settle potential civil liability for eight alleged violations of the Iranian Transactions and Sanctions Regulations, 31 C.F.R. part 560 (ITSR), and other sanction programs
- Dec. 2013 - Royal Bank of Scotland paid \$33,122,307 (part of global settlement involving Fed. Reserve, and the New York Department of Financial Services) to settle allegations regarding wire transfers involving Cuba, Burma, Sudan, and Iran.
- Dec. 2012 – HSBC settlement of \$1.9 billion for “particularly egregious” conduct
- Dec. 2012 – Standard Chartered paid \$132 million to settle allegations of Iran sanctions violations.



# Best Practices and Red Flags

## Common Problems

- Weak compliance culture
  - No Management/Board accountability for ensuring effectiveness of BSA/AML and OFAC compliance
  - Insufficient financial and staffing resources
- Missing or weak components of AML or OFAC programs
  - Weak enterprise-wide risk management system,
  - Inadequate IT and monitoring processes
  - No business line accountability for BSA/AML compliance
  - Lack of independent audit function
- Compliance risks arising from the use of third-party service providers
- Failure to update BSA/AML programs to account for evolving risk or new products and services



# Best Practices and Red Flags

## Preparation and Avoidance

- Develop Strong Compliance Culture
- Designation of a BSA/AML Compliance Officer with sufficient authority and resources (staff and systems)
- Lines of communication between BSA/AML function and Board and senior management
- Adequate financial and staffing resources
- Ongoing, relevant training of employees
- Independent testing and review



# Best Practices and Red Flags

## Preparation and Avoidance

- Additional considerations to minimize risk
  - Enterprise-Wide Risk Management
    - Early intervention
    - Coordination between different business lines
  - Automated Monitoring Systems and Technologies
    - Ensure systems provide effective and timely feedback to both compliance staff and management
    - Understand vulnerabilities of systems/controls
    - Technology maintenance and upkeep
    - Leverage technology to create “feedback loop” that can be used to further refine compliance policies and procedures



# Best Practices and Red Flags

## Preparation and Avoidance

- OFAC Compliance Program should include the following minimum requirements:
  - Risk Assessment: tailored to specific product lines, customer base, the nature of transactions and identification of higher-risk areas for OFAC transactions
  - Policies and procedures and internal controls
  - Screening transactions (and updating of OFAC lists)
  - Blocked/Rejected transactions and reporting to OFAC



# OFAC/AML: Transactional Language

- Avoid:
  - “USA PATRIOT Act”
  - Executive Order having any number, such as 13221, 13224
  - Limiting economic sanctions language to the U.S. Treasury
  - Limiting to Anti-terrorism “programs”
- “Prohibited Parties:” Definition very important
- Examples



# CFIUS: What is It?

- U.S.' method of regulating foreign direct investment ("FDI") in the U.S. and protecting critical U.S. assets from foreign control.
- Interagency committee chaired by the Treasury Secretary and staffed by career civil servants.



# CFIUS: Closing Considerations

- Failure to Subject Transaction to CFIUS Review Means CFIUS may review and unwind at any time.
- Process is informal, but structured:
  - Time lines are enforced unless extension requested/granted.
  - Penalties for non-compliance with information requests are substantial (\$250,000 civil, criminal referral)
  - Confidentiality is guaranteed, but as of yet, not tested.





# Best Practices and Red Flags

## Looking Ahead

- The pressure stays on
- Increased focus on banks as gate-keepers
- Increased focus on third-party vendors, payment system participants
- Increased emphasis on cybersecurity
- Alternative currencies
- Increased focus on C-Suite involvement and compliance



*Anti-Money Laundering  
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Estate Transactions*

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