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Money Laundering through Real Estate

How can Real Estate be used in Criminal Activity?

This is one of the oldest ways that criminals have converted their illicitly gained funds into a legitimate and lucrative investment. The real estate sector is very attractive to criminals for abuse due to property prices which are usually considered stable and are likely to appreciate over time. Property obtained with illicit funds can be used as a second home, rented property or other income generating possibilities.

The real estate sector creates opportunities for criminals to integrate black (illegal) funds into the legal economy while providing a safe investment. It allows criminals to enjoy assets and illicitly derived funds having camouflaged the origin of the money used for payment. A number of techniques can be used to disguise the origin of illegally gained funds:

- Cash financing schemes;
- Overvalued or undervalued prices of property;
- The use of non-transparent companies and trusts; or
- The use of third parties that act as legal owners.

Additionally, property can be used to facilitate terrorist activity. Hence, the real estate agent must apply appropriate measures to safeguard the sector from misuse in criminal activity.

Characteristics of Real Estate Money Laundering

Real estate money laundering usually occurs at the third stage of money laundering: integration. At this stage, illicit money is integrated legally into the economy through the purchase of property. Additionally, income can be earned through the sale or rental of property bought with illegal funds hence making these sources of income/transactions legal. There are some key characteristics of real estate money laundering that agents should be cognizant of:

- Use of complex loans & mortgages schemes - Loans and mortgages can be used as a cover for laundering proceeds of crime, and their repayment can be used to mix illicit with legitimate funds.

- Manipulation of Property Values - Criminals can collude with third parties such as Real Estate Agents to underestimate or overestimate the value of a property. Additionally, there may be the manipulation of the appraisal or valuation of property to quote inaccurate values of property.

- Rental Income to Legitimize Illicit Funds- Criminals lease out their properties, providing tenants with illicit funds to cover the rental payments, in order to legitimize the illicit funds.

- Use of Third Parties- Criminals may buy real estate using a third party or family member (often someone with no criminal record) as the legal owner. Property is either purchased on their behalf, or proceeds of crime are deposited into their bank account to make the purchase. This method allows criminals to avoid direct involvement in the money laundering process. Additionally, criminals may also buy property in a third party's name and pay that third party rent using illicit funds. By 'renting' their own property via a third party, criminals can disguise illicit funds and ownership.

- The use of front companies, shell companies, trusts and corporate structures by criminals to disguise the true owner of the property.

Three Ways to Stop Money Laundering through Real Estate

1. Regulate Gatekeepers

Real Estate Agents are required to conduct due diligence procedures in accordance with the Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) Laws and Regulations. Failure to comply would result in penalties outlined within the AML/CFT Laws and Regulations.

2. Establish Source of Wealth

Real Estate Agents should collect the relevant information to determine a client's source of wealth and ability to purchase property.

3. Report Suspicious Activities

This is one of the key components of combating money laundering and terrorist financing. Real Estate Agents are required to report any suspicious activity noted when conducting business.

<u>TOPICS DISCUSSED</u>

Characteristics of Real Estate Money Laundering (cont'd)

- Renovations & Improvements to Property- Criminals use illicit funds to pay for renovations, thereby increasing the value of property. The property is then sold at a higher price. The proceeds from this transactions are now legal funds.
- The rise in income, financial means and assets which are inconsistent with the clients occupation, nature of business or expected activity.
- The lack of interest in obtaining a better price for the property.
- The buyer is willing to purchase the property without viewing it or without any kind of interest in the characteristics or condition of the property.

Real Estate Agents as Gatekeepers

Real Estate Agents involved in transactions for a client concerning the buying and selling of real estate have been designated by the Financial Action Task Force (FATF) as Designated Non-Financial Businesses and Professions (DNFBPs). As DNFBPs, Real Estate Agents are required to develop policies, procedures and internal controls in accordance with the International Standards developed by the FATF, hence real estate agents are considered gatekeepers. In Schedule 1 of the Proceeds of Crime Act (POCA), Cap 4.28, real estate business is listed as a regulated activity and as such is governed by the obligations and requirements of the Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) Laws and Regulations of St. Kitts and Nevis.

Identifying and Mitigating Risks

As gatekeepers, Real Estate Agents should apply a risk based approach (RBA) to identifying, detecting and monitoring risks associated with clients and report suspicious activities, if necessary. Applying a RBA, would assist the real estate agents in determining the level of customer due diligence (CDD) required and enhanced due diligence (EDD) when high risk has been identified.

The real estate agent should consider the following risks:

Customer/Client risk **-** This risk is assessed to determine whether the customer/client is:

- An individual or an entity;
- High-ranking foreign officials;
- Politically Exposed Person (PEP);
- Listed on any Sanctions/Watch List.

Transaction Risk **-** This risk is assessed to determine the following regarding the property/transaction:

- Questionable source of funds
- Type of property (Also, the property does not match the characteristics of the buyer)
- Use of cash or complex loans
- Undervaluation or overvaluation of property

Geographical Risk - This risk is assessed to determine whether the geographical location posed a risk if the property is located in a jurisdiction with weak AML/CFT Laws.

How to be Effective Gatekeepers

In order to combat money laundering, Real Estate Agents must be vigilant and aware of the red flags and possible indicators of this crime *(see Characteristics of Real Estate Money Laundering)*. Once the risks have been identified, the Real Estate Agent can apply measures which are in accordance with the requirements of AML/CFT Laws and Regulations:

- Customer Due Diligence - apply identification procedures for client prior to establishing a business relationship. Additionally, the Real Estate Agent must ensure identification documents remain current and up-to-date throughout the course of the business relationship. In the case of a company, the Real Estate Agent should establish the beneficial owner through the same identification procedures *(Regulations 4 - 6 of the Anti-Money Laundering (AMLR) Regulations, No. 46 of 2011 and Anti-Terrorism (Prevention of Terrorist Financing) Regulations (ATR), No 47 of 2011)*
- Record Keeping - Information, data and documentation collected during the course of business must be maintained for a minimum of five (5) years. *(Regulation 8 of the AMLR and ATR)*
- Reporting of Suspicious Activity - If suspicion has been noted based on the red flags and indictors identified, the Real Estate Agent is required to report the suspicion to the Financial Intelligence Unit (FIU) within 24 hours. *(Regulation 11 of the AMLR and ATR)*
- Appoint a Compliance Officer - The Real Estate Agent should appoint a senior officer who would be responsible for establishing and maintaining a Compliance Program in accordance with the requirements of the AML/CFT Regulations. *(Regulation 11 of the AMLR and ATR)*

References:

- *Anti-Money Laundering (AMLR) Regulations, No. 46 of 2011*
- *Anti-Terrorism (Prevention of Terrorist Financing) Regulations (ATR), No 47 of 2011*
- *https://www.transparency.org/news/feature/three_ways_to_stop_money_laundering_through_real_estate*
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