Lowenstein Sandler

Client Alert

Anti-Money Laundering

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The Real (Estate) Deal: FinCEN's New Reporting Requirements for Property Transfers

By Robert A. Johnston Jr., Paula A. Ladd, Ryan E. Fennell, and Samantha Sigelakis-Minski

In response to illicit finance risks identified in the U.S. residential real estate sector, the U.S. Department of Treasury's Financial Crimes Enforcement Network (FinCEN) has announced the issuance of its long-anticipated final rule (RIN 1506-AB54, the "Final Rule")[1] concerning anti-money laundering (AML) regulations for specified real estate transfers. As discussed in our prior Client Alert,[2] the Final Rule will require "reporting persons" involved in certain residential real estate transactions to submit reports to FinCEN and maintain records of cash residential real estate transactions with legal entities or trusts.

Although the Final Rule will not take effect until December 1, 2025, one thing is immediately clear: significant changes are coming for the real estate sector.

Reportable Transfers

A reportable transfer occurs where (i) the property is "residential real property" that is located in the United States; (ii) the transfer is non-financed–i.e., is an all-cash purchase; (iii) the property is transferred to a legal entity or trust; and (iv) an exception does not apply.

- Residential Real Property–As adopted in the Final Rule, FinCEN's definition of "residential real property" encompasses (A) real property located in the United States containing a structure designed principally for occupancy by one to four families; (B) land located in the United States on which the transferee intends to build a structure designed principally for occupancy by one to four families; (C) a unit designed principally for occupancy by one to four families within a structure on land located in the United States; or (D) any shares in a cooperative housing corporation for which the underlying property is located in the United States.

  While this represents FinCEN's attempts to provide clarifications and responses to criticism regarding the proposed rule,[3] its primary focus will be on properties located in the United States that are principally designed for occupancy by one to four families (or, in the cases of vacant or unimproved land, that will be occupied by one to four families). It remains less clear, however, how FinCEN's interpretation will be reflected in the case of mixed-use properties, such as a single-family residence that is located above a commercial enterprise, as their guidance only indicates that such circumstances "may be reportable."[4]

- Non-Financed Transfers–For a transfer to be classified as "non-financed," it must not involve an extension of credit that is (A) secured by the transferred property and (B) provided by a covered financial institution that is required to maintain an AML program and file suspicious activity reports (SARs) under the Bank Secrecy Act (BSA) and its implementing regulations. According to FinCEN's guidance in the Final Rule, transfers that do not meet both criteria may still be considered potentially reportable non-financed transfers.

- Reportable Transferees: Transferee Entities and Trusts–Subject to the 16 exceptions set forth in 31 CFR 1031.320(n)(10)(ii)(A-P), a "transferee entity" would include any legal entity other than a "transferee trust." In a notable deviation from FinCEN's proposed rule, however, its Final Rule now excludes from the definition of a transferee entity any "legal entity controlled or wholly owned, directly or indirectly, by [an excepted legal entity]."[5]

  Conversely, the term "transferee trust" will mean any "legal arrangement created when a person (generally known as a grantor or settlor) places assets under the control of a trustee for the benefit of one or more persons (each generally known as a beneficiary) or for a specified purpose, as well as any legal arrangement similar in structure or function to the above, whether formed under the laws of the United States or a foreign jurisdiction." Although a trust will be deemed to be a transferee trust regardless of whether the residential real property is titled in the name of the trust itself or in the name of the trustee in the trustee's capacity as the trustee of the trust, the Final Rule does also specify certain exclusions pursuant to 31 CFR 1031.320(n)(11)(ii).

- Excepted Transfers–Despite being adopted largely as proposed, FinCEN's Final Rule incorporates several additional exceptions beyond those originally referenced in the agency's notice of proposed rulemaking. Specifically, the Final Rule provides that a reportable transfer does not include:

  - Grant, transfer, or revocation of an easement;
  - Transfers resulting from the death of an individual, whether pursuant to the terms of a decedent's will or the terms of a trust, the operation of law, or by contractual provision;
  - Transfers incident to divorce or dissolution of a marriage or civil union;
  - Transfers to a bankruptcy estate;
  - Transfers supervised by a court in the United States;
  - Transfers made without consideration by an individual, either alone or with the individual's spouse, to a trust of which that individual, that individual's spouse, or both of them, are the settlor(s) or grantor(s);
  - Transfers to a qualified intermediary for purposes of 26 CFR 1.1031(k)-1; or
  - Transfers for which there is no "reporting person."

Reporting Persons

The reporting person will generally be the entity or individual engaged in the real estate closing and settlement services within the U.S., which may include settlement agents, title insurance agents, escrow agents, or attorneys. Although only one reporting person will be required for a particular reportable transfer, the way the reporting person will be determined may vary on a case-by-case basis:

- Reporting Cascade–The reporting cascade method will consist of a list of seven different functions that a real estate professional may perform in a transfer of residential real property, with the reporting obligation for any such transfer applying to the professional who performed the function that appears highest on the list. For example, the first function on the list is the professional listed as the agent on the closing or settlement statement. If no such professional is involved in the transfer, then the reporting obligation applies to any professional who performed the second function on the list (i.e., the professional who prepared the closing or settlement statement), and so on down the list.

- Designation Agreement (i.e., real estate professionals decide)–With an aim toward providing flexibility to the industry and reducing potential burdens associated with compliance, the real estate professionals who perform the functions described in the cascading list may also enter into a written agreement with each other to designate the professional who will file the report for the transfer where required.

Real Estate Reports

Where required, a Real Estate Report must be filed electronically with FinCEN by the end of the month following the closing date or within 30 days of the closing, whichever is later. The reporting person will also need to provide comprehensive information regarding the transaction, which must include information regarding:

- The reporting person;
- The legal entity (transferee entity) or trust (transferee trust) receiving ownership of the property;
- The beneficial owners of the transferee entity[6] or transferee trust,[7] as applicable;
- Certain individuals signing documents on behalf of the transferee entity or transferee trust during the reportable transfer;
- The transferor (e.g., the seller);

- The residential real property being transferred; and
- The total amount paid or to be paid by the transferee entity or transferee trust for the reportable transfer, as well as the total amount paid or to be paid by all transferees involved in the reportable transfer, and whether the reportable transfer involved credit extended by an entity that is not a financial institution with an obligation to maintain an anti-money laundering program and file SARs.

FinCEN will, however, seek public comments on the form of the report ultimately mandated by the Final Rule in accordance with the Paperwork Reduction Act.

Reasonable Reliance

Reporting persons may rely upon information provided by others "absent knowledge of facts that would reasonably call into question the reliability of the information provided to the reporting person." When reporting beneficial ownership, however, a stricter standard will apply: the reporting person can rely upon the information provided by the transferee or their representative, but only where such information is certified as certified in writing to the best of the information provider's own knowledge.

Recordkeeping

Reporting persons are required to retain copies of certifications and designation agreements for five years, but the reporting person is not required to retain a copy of the Real Estate Report.

Exemptions

As adopted, FinCEN's Final Rule also contemplates two notable exemptions:

- The confidentiality provisions under 31 U.S.C. 5318(g)(2) (i.e., the provisions of the BSA relating to SAR filings and the attendant confidentiality restrictions) do not apply to reporting persons or their agents.
- Reporting persons are exempt from the requirement to establish an anti-money laundering program, as specified in 31 CFR 1010.205(b)(1)(v) (i.e., the provisions of the BSA relating to Customer Identification Program requirements).

Next Steps

Real estate professionals should begin preparing for compliance with these changes and stay informed about further developments. Lowenstein Sandler is closely monitoring updates regarding the Final Rule. For more information or assistance on the Final Rule or this client alert, please contact our team at LSAMLTeam@lowenstein.com.

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[1] *See* "Federal Register: Public Inspection: Anti-Money Laundering Regulations for Residential Real Estate Transfers," Aug. 29, 2024, available at https://www.federalregister.gov/documents/2024/08/29/2024-19198/anti-money-laundering-regulations-for-residential-real-estate-transfers.

[2] "U.S. Treasury Issues Notice of Anti-Money Laundering Regulations for Residential Real Estate Transfers," Aug. 29, 2024, available at https://www.lowenstein.com/news-insights/publications/client-alerts/us-treasury-issues-notice-of-anti-money-laundering-regulations-for-residential-real-estate-transfers-aml.

[3] *Id.* at footnote 1.

[4] *Id.*

[5] *Id.*

[6] To be a beneficial owner of a transferee entity, an individual must, either directly or indirectly, exercise "substantial control" over the transferee entity, or own or control at least 25 percent of the transferee entity's ownership interests. This definition is consistent with the definition of a beneficial owner in FinCEN's Beneficial Ownership Information Reporting Rule. *See* https://fincen.gov/boi.

[7] The beneficial owner of a transferee trust is any individual who is a trustee or otherwise has authority to dispose of transferee trust assets; is a beneficiary who is the sole permissible recipient of income and principal from the transferee trust or who has the right to demand a distribution of, or to withdraw, substantially all of the assets of the transferee trust; is a grantor or settlor of a revocable trust; or is the beneficial owner of an entity or trust that holds one of these aforementioned positions in the trust.

Contacts

Please contact the listed attorneys for further information on the matters discussed herein.

ROBERT A. JOHNSTON JR.
Partner
T: 212.419.5898 / 202.549.5948
rjohnston@lowenstein.com

PAULA LADD
Senior Counsel
T: 646.414.6975
pladd@lowenstein.com

RYAN E. FENNELL
Counsel
T: 862.926.2781
rfennell@lowenstein.com

SAMANTHA SIGELAKIS-MINSKI
Associate
T: 646.414.6934
ssigelakisminski@lowenstein.com