Client Due Diligence: Anti-Money Laundering and Ethical Obligations for Lawyers

By Peter D. Hardy and Siana Danch

When the so-called "Panama Papers" scandal broke in 2016, it cast an unpleasant spotlight on the potential role of lawyers across the globe assisting—knowingly or unknowingly—their clients in money laundering, tax evasion, and other illegal activity.[1] Moreover, the Panama Papers scandal re-energized efforts to identify the true beneficial owners of legal entities, due to concerns that bad actors were using shell companies to obscure their activities through the misuse of corporate forms.

Other, similar scandals have followed the Panama Papers, such as, most notably, the "Pandora Papers."[2] Lurking behind these scandals and the predictable reactions and rhetoric of law enforcement, regulators, watchdog groups, and legislators was the perception that the United States—perhaps, ironically—actually has served as one of the world's greatest havens for global tax evasion and money laundering for illicit actors from around the world.[3] This perception lingered primarily because it was relatively easy to incorporate legal entities in the United States without disclosing beneficial ownership. This perception also potentially arose because the United States has a stable and safe economy and, therefore, serves as a good place to invest assets, legally or illegally obtained, including in the high-end real estate market.

The attention generated by the Panama Papers and the Pandora Papers is undeniable. But what has actually happened in the United States in a concrete fashion on the enforcement and regulatory fronts since then? On the one hand, only a single attorney allegedly involved in assisting a "Panama Papers" client has been prosecuted.[4] And generally, prosecutions of U.S. lawyers for allegedly assisting clients in money laundering, tax evasion, or other illicit schemes remain exceedingly rare, putting aside a few attorneys charged with promoting domestic tax shelter schemes.

On the other hand, the United States has made great strides towards expanding its regulatory net regarding beneficial ownership reporting—for legal entities created in the United States, and potentially for certain real estate transactions. These regulatory developments have implications for business and transaction lawyers of

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all types, including tax lawyers serving both domestic and foreign clients. Further, although Congress recently failed to pass the ENABLERS Act,[5] which would have imposed certain anti-money laundering (AML) obligations on lawyers, accountants, and other professionals, it is clear that the motivation to impose some degree of AML regulations on lawyers—directly or indirectly—is growing. And even if no statutory AML duties are ultimately imposed upon lawyers, ethical obligations to conduct sufficient client due diligence of course remain.

This article will examine these regulatory developments and will focus in particular on efforts by the Financial Crimes Enforcement Network (FinCEN), the agency charged with regulating the Bank Secrecy Act (BSA).[6] As Internal Revenue Service (IRS) Criminal Investigation recently has stressed, approximately 83% of its investigations recommended for prosecution involved a primary target identified in a BSA filing.[7] This trend of expanding BSA/AML regulations reveals the current priorities of enforcement agencies and, further, increases the potential risks—simply due to the expanding universe of required filings—for individuals making representations on behalf of possible bad actors who seek to conduct business or create entities within the United States. These risks are exacerbated by the current broad sweep of U.S. sanctions regimes, particularly those involving Russia and Ukraine. All of these considerations underscore the potential and sometimes surprisingly broad legal and ethical exposures faced by gatekeepers, such as attorneys, accountants, and financial advisors, to money laundering and other charges for assisting in related financial transactions.

Finally, we must caveat this article somewhat by acknowledging the limited budget of FinCEN, a small unit within the U.S. Department of Treasury. Although FinCEN recently obtained a significant increase in its funding,[8] relatively speaking, it faces daunting legal and logistical demands in the near future to attain the many goals set by Congress for FinCEN. Nonetheless, the ethical and legal obligations faced by lawyers in regard to potential illicit activities by their clients exist entirely independent of government budgets. And no lawyer or law firm wants to get ensnared in the "enforcement lottery," even as "just" a potential government witness.

Focus on Lawyers: AML Due Diligence

Much media ink has been spilled regarding the ENABLERS Act. Specifically, on July 13, 2022, the House of Representatives adopted an amendment to the 2023 National Defense Authorization Act (NDAA), inserting into the NDAA a version of the "Establishing New Authorities for Business Laundering and Enabling Risks to Security Act," otherwise more commonly known as the ENABLERS Act.[9] The amendment's "findings" section cataloged instances of alleged kleptocratic and corrupt behavior, including but not limited to the disclosures of the Pandora Papers; a notorious instance of investigative journalism in which an investigator for a non-profit posed as an adviser to an apparent African kleptocrat and enticed, on audio and video tape, various New York lawyers to provide alleged advice on the use of so-called shell companies; a company owning a $15 million mansion in Washington, D.C., linked to an ally of Vladimir Putin; and the fact that the 2021 "United States Strategy on Countering Corruption"[10] stressed AML deficiencies tied to lawyers, accountants, trust and company service providers, and incorporators. The amendment claimed to provide "the authorities needed to require that professional services providers who serve as key gatekeepers to the U.S. financial system adopt anti-money laundering procedures that can help detect and prevent the laundering of corrupt funds."

The ENABLERS Act did not pass.[11] It died in the Senate in late 2022, and presumably, it will be a dead letter for some time, barring some downstream change in the makeup of the U.S. House of Representatives. We therefore address it at a high level only, as an example of the growing focus on lawyers and their required client due diligence, and how these issues may play out in the future. It also illustrates what it can mean, specifically, to have statutorily mandated AML duties.

The amendment would have broadened the BSA to include a wide variety of individuals and entities under the definition of a "financial institution" covered by the BSA. Specifically, the amendment in part would have expanded the BSA to apply to any person engaging in:

- corporate or other legal entity arrangement, association, or formation services;
- trust services;
- third-party payment services; or
- legal or accounting services that involve (a) financial activities that facilitate corporate or other legal entity arrangement, association, or formation services; (b) trust services; or (c) third-party payment services; and are not direct payments or compensation for civil or criminal defense matters.

Although the full scope and nuance of the BSA are well beyond the scope of this article, parties covered by the

BSA can have a spectrum of possible monitoring and reporting obligations, some of which are quite onerous. The ENABLERS Act directed the Secretary of the Treasury to require each type of the newly defined "financial institutions" to be subject to at least one (or more) of five traditional BSA obligations: a customer identification program (CIP) and customer due diligence (CDD) during client onboarding; the establishment of a "full" AML program, which would have required ongoing transaction monitoring; the filing of Suspicious Activity Reports (SARs) on clients; other potential record-keeping and reporting obligations; and enhanced due diligence for relationships with foreign persons. Thus, different gatekeepers could have different AML responsibilities. Presumably, the baseline requirement for almost every gatekeeper would have been CIP and CDD. The notion that certain attorneys could be subject to SAR filing requirements on their clients was groundbreaking and controversial, to say the least.

Even though it did not pass, the ENABLERS Act was not an accident. The legislation had gained ground within a particular context. Specifically, it was proposed and advanced because of the widespread perception in the United States and abroad that U.S. lawyers and other professionals assist clients in committing money laundering and tax evasion, particularly through the use of corporate forms. For example, on May 13, 2022, the U.S. Treasury released its 2022 Strategy for Combating Terrorist and Other Illicit Financing (2022 Strategy).[12] The 2022 Strategy identified lawyers, accountants, and trust or company service providers as possible gatekeepers who cannot be permitted to evade scrutiny for facilitating illicit financing. For years, global watchdog groups and authorities, including the Basel Institute on Governance,[13] the Financial Action Task Force (FATF),[14] and the European Parliament (EP),[15] have advocated this same message. The EP actually has praised U.S. tax lawyers, stating that a "critical mass" of U.S. tax lawyers appear to see themselves "both as advocates (for their clients) and as trustees (to assist clients in complying with the law and its purpose to protect the integrity of the legal system)."[16]

As we will discuss, even if the United States has not passed AML legislation specifically applicable to lawyers, other considerations still apply. Lawyers always must consider the general U.S. federal money laundering statutes, which apply to everyone handling U.S. transactions, as well as ethical standards regarding client due diligence, which continue to evolve and expand incrementally.

Money Laundering Basics

When Congress and watchdog groups say that they are concerned that some attorneys and other so-called "gatekeepers" are assisting clients in laundering money, what exactly does that mean? "Money laundering" is a phrase that is commonly used but not always fully understood from a technical, statutory perspective. As we will discuss, the U.S. federal money laundering statutes are very broad and can apply to a wide variety of conduct.

Typically, the key element in money laundering cases focused on a third-party advisor or professional—*i.e.*, the lawyer, accountant, financial advisor, real estate agent, or other professional who had no involvement in committing the underlying "specified unlawful activity," or SUA, but who later assisted the person who committed the underlying criminal scheme with subsequent financial transactions involving the resultant proceeds—is knowledge: when the lawyer helped the business person set up a company to hold assets, did the lawyer know that those assets were derived from illegal activity?

Very generally, the offense of money laundering under 18 USC §§1956 and 1957 involves a financial transaction conducted with the proceeds of an SUA while knowing that the proceeds were earned through illegal activity. The list of potential SUAs identified by Congress is specific but also extremely long (over 200 separate crimes—but it does *not* include Title 26 criminal tax violations.[17] Thus, in the normal course, transactions involving proceeds earned through tax fraud cannot support money laundering charges. But prosecutors sometimes can overcome that obstacle by labeling a tax fraud scheme as a wire or mail fraud scheme. And other conduct besides the filing of tax returns can constitute a fraudulent scheme.

Code Sec. 1956 generally requires the defendant to also act with one of four possible intents—(i) an intent to conceal or disguise the nature, location, source, ownership, or control of the SUA proceeds; (ii) to promote the underlying SUA; (iii) to avoid a transaction reporting requirement, such as a SAR; or (iv) to commit the offense of tax evasion or filing a false tax return.[18]

Code Sec. 1957—the so-called "spending" money laundering statute—merely requires a transaction involving over $10,000 and knowledge that the proceeds are derived from criminal activity.[19] It does not require any one of the specific intents listed above. Code Sec. 1957 is therefore extremely broad and can apply to seemingly mundane transactions that are otherwise completely

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transparent—for example, a fraudster using scheme funds to buy a residence in his own name—so long as the transaction exceeds $10,000 and the requisite level of knowledge exists.

Other illegal conduct committed in foreign countries may readily lend itself to supporting money laundering charges for subsequent transactions conducted in the United States. For example, if an individual acting abroad has committed a more straightforward violation of U.S. law—such as the Foreign Corrupt Practices Act[20] or a violation of a U.S. embargo, subject to prosecution under the International Economic Emergency Powers Act[21] or similar statutes—and then attempts to move the proceeds of such offenses from abroad and into the United States, the legal analysis under the money laundering statutes is generally much more straightforward: such proceeds clearly will represent SUA funds because the foreign conduct itself represents a violation of U.S. law. Under this scenario, the issues are limited to proof of sufficient mental state and, under Code Sec. 1957, also whether the financial transaction involved over $10,000. Likewise, Code Sec. 1956 defines SUA in part to specifically include a broad variety of foreign offenses, so long as the later financial transaction at issue was conducted in whole or in part in the United States.[22]

Moreover, Code Sec. 1956(f) explicitly extends jurisdiction over extraterritorial conduct when "the conduct is by a United States citizen or, in the case of a non-United States citizen, the conduct occurs in part in the United States," and the transaction has a value exceeding $10,000.[23] Thus, Code Sec. 1956(f) applies to *transactions* that occur in whole or in part in the United States; it does not require a physical presence in the United States. Likewise, "conduct" occurring in the United States is not limited solely to physical activity; electronic conduct, such as a wire transfer into the United States from abroad, might satisfy Code Sec. 1956(f) and provide U.S. prosecutors with jurisdiction.

The international transfer of funds can itself represent money laundering. Code Sec. 1956 contains a separate prong that prohibits "international" money laundering that applies to transportation or transfers of funds in or out of the United States. This prong contains three alternative intent requirements: (i) an intent to promote an SUA; (ii) knowledge that the transaction is designed to conceal the proceeds of an SUA; or (iii) knowledge that the transaction is designed to avoid a transaction reporting requirement.[24] Although the statute is not a model of clarity, it arguably does not even require the funds involved in the transaction to be actual SUA funds.[25]

Finally, we note the presence of civil forfeiture statutes.[26] Although this is a huge topic well beyond the scope of this article, it is worth remembering that the U.S. Department of Justice (DOJ) can institute civil forfeiture proceedings against assets—including funds held in law firm bank accounts—if those funds were derived from illicit activity, including money laundering. Indeed, the forfeiture of assets held in U.S. law firm bank accounts was at issue in the long-running DOJ enforcement actions pertaining to the 1MDB corruption scandal involving high-level members of the Malaysian government, their family members, their bankers, and other associates.[27]

New Reporting Duties Regarding Beneficial Owners: The Corporate Transparency Act

On January 1, 2021, Congress passed the Corporate Transparency Act (CTA).[28] The CTA requires defined entities—including most domestic corporations and foreign entities registered to do business in the United States—to report beneficial owner information (BOI) and company applicant information to a database created and run by FinCEN upon the entities' creation or registration within the United States. This database will be accessible to U.S. and foreign law enforcement and regulators and to certain U.S. financial institutions (FIs) seeking to comply with their own AML and CDD Rule compliance obligations under the BSA.

Congress passed the CTA because the ability to operate through legal entities without requiring the identification of BOI has been regarded as a key AML risk for the U.S. financial system.[29] The stated primary goal of the CTA was to enable law enforcement and regulators to obtain information on the "real" beneficial owners of so-called "shell companies," including foreign entities registered in the United States, in order to "crack down" on the misuse of corporate forms for potential money laundering, tax evasion, and other offenses. FinCEN already has issued a final rulemaking regarding who and what must report BOI[30]; further, FinCEN has issued proposed rules regarding who may access BOI, for what purposes, and how.[31] FinCEN still needs to issue proposed rules to revise the CDD Rule applicable to FIs to conform with the CTA regulations.

The CTA will have a broad effect. FinCEN estimates that over 32 million initial BOI reports will be filed in the first year of the CTA taking effect and that in each

subsequent year, approximately 5 million initial BOI reports and over 14 million updated reports will be filed (due to broad updating requirements). The CTA is a complicated topic, and we only summarize it here. Our point is that the CTA creates another BSA reporting document—and therefore another legal exposure—for business clients and potentially their legal and professional advisors. Indeed, and as we discuss, covered companies will have to report not just their BOI, but also their "company applicants," which could include lawyers, accountants, or other third-party professionals. But more broadly, the reporting form currently proposed by FinCEN (which has several flaws, as we will describe) implicates the issue present throughout this article: when attorneys or other advisors are assisting clients in filling out government forms, what degree of client due diligence is sufficient or required?

BOI Reporting Obligations

CTA reporting obligations take effect on January 1, 2024. Companies subject to the BOI reporting rules (Reporting Companies) created or registered before the effective date will have one year, until January 1, 2025, to file their initial reports of BOI. Reporting Companies created or registered after the effective date will have 30 days after creation or registration to file their initial reports. Reporting Companies also will have to file updates within 30 days of a relevant change in BOI.

Subject to 23 defined exemptions, BOI reporting requirements apply to all domestic entities that are created by filing a document with a secretary of state or other similar offices of a State or Indian tribe. FinCEN believes this will exclude many sole proprietorships, general partnerships, and trusts, subject to applicable State or tribal law. The reporting requirements also apply to foreign entities that have registered to do business in any State or Indian tribal jurisdiction.

Domestic entities formed or foreign entities registered after January 1, 2024, must file an initial report with FinCEN within 30 days after formation or registration. An initial report must include the following information about the Reporting Company: (i) full name and address; (ii) trade or fictitious names used; (iii) address of the principal place of business; (iv) jurisdiction of formation or, in the case of a foreign company, jurisdiction in which first registered; and (v) taxpayer Identification Number (TIN), or where a foreign reporting company has not been issued a TIN, a tax identification number issued by a foreign jurisdiction.

The initial report also must include the following information about each beneficial owner and the company applicant: (i) full legal name; (ii) date of birth; (iii) current address; (iv) a unique identifying number from a non-expired passport, driver's license, government-issued ID, or identification document issued by a State or local government or tribe; and (v) an image of the document showing the unique identifying number.

FinCEN has defined a "beneficial owner" as (i) any individual who, directly or indirectly, owns or controls at least 25% of the ownership interest of the reporting company, and (ii) *any* individual who exercised "substantial control" over the company. The regulations set 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 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.

As the Final Rule explains, these indicators support "the basic goal of requiring a reporting company to identify the key individuals who stand behind the reporting company and direct its actions." While the first indicator aims to identify individuals with nominal or *de jure* authority, the latter two indicators identify individuals with functional or *de facto* authority. The definition is broad and reflects FinCEN's desire to collect information on all true beneficial owners and to avoid true beneficial owners hiding behind a designated nominee. However, the breadth of the definition will create legal and compliance headaches as Reporting Companies attempt to draw lines regarding who precisely exercises "substantial control."

As noted, the Reporting Company's "company applicant" also must be reported. A company applicant is defined as the individual who directly files the document that creates or registers a Reporting Company, as well as the individual who is primarily responsible for directing or controlling such filing. The requirement to provide BOI for company applicants applies only to Reporting Companies created or registered on or after the effective date of January 1, 2024. Notably, FinCEN anticipates that lawyers, accountants, or other third-party professionals may constitute applicants whose information must be reported: "In many cases, company applicants may be employed by a business formation service or law firm. For example, there may be an attorney primarily responsible for overseeing the preparation and filing of incorporation

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documents and a paralegal who directly files with a state office to create the reporting company."[32] According to FinCEN, *both* the lawyer and the paralegal are "company applicants."

Access to BOI

Under the CTA and the regulations proposed by FinCEN, five broad categories of recipients will have access to the database under certain circumstances and requirements.

(1) Federal, state, local, and Tribal government agencies engaged in national security, intelligence, or law enforcement activities;
(2) Foreign law enforcement agencies, judges, prosecutors, central authorities, and competent authorities;
(3) FIs using BOI to facilitate compliance with their own CDD Rule requirements and that have received the Reporting Company's prior consent;
(4) Federal functional regulators and other appropriate regulatory agencies acting in a supervisory capacity assessing FIs for compliance with the CDD Rule; and
(5) U.S. Department of Treasury, which will have "relatively unique access" to BOI tied to an officer or employee's official duties requiring BOI inspection or disclosure, including for civil tax administration.

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BOI Certification

Each person filing a report must certify that the report is accurate and complete. FinCEN rejected comments to the proposed rule that the certification standard should include a requirement regarding knowledge or other such qualification, *e.g.*, persons certifying "to the best of their knowledge after reasonable and diligent inquiry." This is because FinCEN wanted to stress that Reporting Companies are responsible for accurately identifying their beneficial owners.[33] Violations of the CTA carry civil penalties of up to $500 for each day of continuing violations, and up to two years of imprisonment for criminal violations.

Despite these requirements, and the fact that the government's ability to accomplish the stated goals of the CTA hinge as a practical matter on the actual BOI reporting form, the draft reporting form proposed by FinCEN[34] (Draft Form) seemingly provides its filers with multiple opportunities to avoid the statutory dictates of the CTA.

Specifically, the Draft Form repeatedly allows filers to not answer any of the core questions for beneficial owners and company applicants, and instead simply state that required information is "unknown" or not available. This includes basic information under the CTA regarding names, addresses, and other identifying information. This problem appears to be an oversight by FinCEN and possibly is a function of the fact that the CTA did not address good-faith filers encountering difficulty in obtaining complete information—a legitimate and real-world issue. Regardless, the Draft Form appears to invite, unwittingly, widespread game-playing by bad actors, both in the United States and abroad, who may claim that key BOI, unfortunately, just could not be obtained. Nor does the Draft Form ask filers to describe the efforts made to collect purportedly non-obtainable BOI. Likewise, FinCEN to date has not addressed how to handle filers who simply respond, "I don't know." Given the fact that FinCEN estimates that over 30 million BOI reports will be filed in the first effective year of the CTA, it is easy to imagine that obfuscation by bad actors will be lost within the data haystack—a phenomenon on which bad actors can rely.

Presumably, and hopefully, FinCEN will address these flaws when it issues the final version of the BOI reporting form. These flaws are not just a potential issue for regulators, law enforcement, and FIs using the BOI database to comply with the CDD Rule: although flexibility can be good, and there will be many instances in which BOI information legitimately will not be readily identifiable, creating opportunities for potential bad actors to obfuscate can also create headaches for practitioners.

Expanding BSA Reporting Duties for Beneficial Owners: Real Estate Transactions

In addition to the CTA, any practitioner representing clients in regard to residential or commercial real estate deals should be aware that FinCEN issued on December 6, 2021 an Advanced Notice of Proposed Rulemaking (ANPRM) to solicit public comment on potential requirements under the BSA for persons involved in real estate transactions to collect, report, and retain information.[35] If finalized—and FinCEN has indicated that proposed regulations likely will be issued in April 2023[36]—such regulations could affect a whole new set of professionals and one of the largest industries in the United States (an industry which, heretofore, has not been subject to the requirements of the BSA, with limited exceptions). The proposed rules contemplate

imposing reporting requirements similar to the CTA on other key players in these types of real estate purchases, such as attorneys, real estate brokers and agents, closing agents, appraisers, and property inspectors, among others. Notably, FinCEN suggests that any new rule may cover attorneys and law firms, along with other client-facing participants. FinCEN also is considering issuing regulations applicable to both residential *and* commercial real estate transactions.

The ANPRM envisions imposing nationwide record-keeping and reporting requirements on specified participants in transactions involving non-financed real estate purchases,[37] with no minimum dollar threshold. Fundamentally, FinCEN highlights two alternate, proposed rules. One proposed option would involve implementing specific and relatively limited reporting requirements, similar to those currently required of title insurance companies in the non-financed real estate market. This rule would require covered persons to collect and report certain prescribed information, such as, presumably, beneficial ownership, similar to the CTA. Alternatively, FinCEN is considering imposing more fulsome AML monitoring and reporting requirements, including filing SARs and establishing AML and Countering the Financing of Terrorism (CFT) compliance programs. This latter, much more demanding option would require covered persons to adopt AML/CFT policies, designate an AML/CFT compliance officer, establish AML/CFT training programs, implement independent compliance testing, and perform customer due diligence. The ANPRM concedes that its potential applicability is vast: in 2020, and putting aside the amount of commercial deals, there were almost 6.5 million residential real estate transactions in the United States.

FinCEN's ANPRM appears to represent the culmination of an inevitable march towards the issuance of regulations under the BSA regarding real estate transactions, following years of increasing focus by the U.S. government and others on perceived AML risks in the real estate industry, including those relating to lawyers. According to the ANPRM, "[s]everal key factors contribute to the systemic vulnerability of the U.S. real estate market to money laundering. Those factors include, but are not limited to, lack of transparency, attractiveness of the U.S. real estate market as an investment vehicle, and the lack of industry regulation."

Importantly, FinCEN has authorized since 2016 Geographic Targeting Orders (GTOs), which impose certain requirements on title insurance companies for transactions occurring in particular locations around the United States that are not financed by loans from FIs. These transactions represent approximately 20% of real estate transactions. Since then, FinCEN has extended the GTOs every six months. Under the GTOs, U.S. title insurance companies must identify the natural persons behind legal entities used in purchases of residential real estate performed without a bank loan or a similar form of external financing. The monetary threshold for these transactions has been $300,000 and the GTOs cover purchases involving virtual currency as well as "fiat" currency, wires, personal or business checks, cashier's checks, certified checks, traveler's checks, money orders in any form, or a funds transfer. The current GTO applies to nine districts.[38] The government has been analyzing information obtained through the GTOs[39] and using the data not only for initiating and assisting investigations, but also to build a case for permanent regulations applicable to the real estate industry—as the ANPRM reflects. Further, the U.S. Department of Treasury's National Strategy for Combating Terrorist and Other Illicit Financing has stressed for years the need to combat money laundering relating to real estate transactions and gatekeeper professions in general, such as lawyers, real estate professionals, and other financial professionals, particularly high-value real estate transactions involving shell companies or straw purchasers.[40]

Commenting upon the commercial real estate industry in particular, the ANPRM states that, "[b]roadly speaking, FinCEN has serious concerns with the money laundering risks associated with the commercial real estate sector." The ANPRM further observes that "[t]he commercial real estate market is both more diverse and complicated than the residential real estate market and presents unique challenges to applying the same reporting requirements or methods as residential transactions." FinCEN regards such complexity as a reason to develop and impose regulations:

> In part due to such added complexity and opacity, the risks and vulnerabilities associated with the residential real estate sector covered by the [GTOs] may be compounded in transactions involving commercial real estate, as there are additional types of purchasing options and financing arrangements available for parties seeking to build or acquire property worth up to hundreds of millions of dollars. Lawyers, accountants, and individuals in the private equity fields—all positions with minimal

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to no AML/CFT obligations under the BSA—often facilitate commercial real estate transactions, working at different stages of the transaction and operating with differing amounts of beneficial ownership and financial information related to buyers and sellers. Commercial real estate transactions also often involve purpose-built legal entities and indirect ownership chains as parties create tailored corporate entities to acquire or invest in a manner that limits their legal liability and financial exposure. The result is an opaque field full of diverse foreign and U.S. domiciled legal entities associated with transactions worth hundreds of millions of dollars that makes up one of the United States' most lucrative industries.[41]

FinCEN therefore has sought comments as to which transaction participants would be best situated to identify and report on the identity of the buyer, other parties to the transaction, and the nature of their involvement. For instance, those directly involved in marketing and structuring the real estate deal, as well as those involved in the transfer of purchase funds, may be more exposed to money laundering activities and better able to collect and report relevant information. On the other hand, those with non-customer-facing roles, or property-focused roles, may have no knowledge of the financing and therefore be unable to collect requisite data for reporting.

To ensure that at least one entity involved in every non-financed real estate deal is responsible for the relevant reporting, FinCEN is considering implementing a hierarchical, cascading reporting system, similar to the IRS' regulation for Form 1099-S, *Proceeds from Real Estate Transactions*. This approach would recognize that different transactions involve different parties. In the event that the type of entity assigned the primary reporting responsibility is not involved in a given transaction, the reporting responsibility would fall on another party involved. FinCEN has sought feedback on how the reporting hierarchy should be structured among title insurance companies, title or escrow companies, real estate agents or brokers, real estate attorneys or law firms, and settlement or closing agents, among others.

These potential BSA reporting obligations in the real estate industry can have practical consequences for U.S. businesses, transactions, and tax lawyers. The high-end domestic real estate market has been the recent focus of particular government scrutiny—including as to the role of lawyers—in regard to transactions involving alleged violations of Office of Foreign Assets Control (OFAC) sanctions relating to Russia and Ukraine.[42] Likewise, FinCEN issued in December 2022 a "Financial Trend Analysis" for FIs regarding BSA filings from March to October 2022 reflecting financial activity by Russian oligarchs since the time of Russia's invasion of Ukraine. Overall, FinCEN found that BSA data filed on financial transactions of Russian oligarchs, high-ranking officials, sanctioned individuals, and their family members showed suspicious transactional patterns indicative of corruption and sanctions evasion, including (i) the movement or transfer of funds or ownership of assets and trusts; (ii) the purchase of high-value goods or property; and (iii) changes in financial flows with links to property or companies in the United States.[43]

Ethical Standards for U.S. Lawyers and Client Due Diligence

In February 2023, the American Bar Association (ABA) passed a resolution opposing any legislation requiring lawyers to file SARs on their own clients, arguing such a requirement would violate client confidentiality rules.[44] This resolution clearly was directed at any effort to resurrect the ENABLERS Act, discussed *supra*, although it was couched as a response to the CTA and its final and pending implementing regulations.[45] Simultaneously, the ABA stated that it is supporting further education and voluntary guidance on AML procedures in order to address rising concerns regarding the role lawyers may play, wittingly or unwittingly, in financial crimes by clients.[46]

The ABA acknowledges that lawyers have certain client due diligence obligations adjacent to AML concerns, even if the BSA does not and should not apply directly to lawyers. These obligations may be ethical in the view of the ABA, but as a practical matter they are also rooted in the Title 18 money laundering statutes and BSA reporting obligations discussed *supra*.

In April 2020, the ABA issued an important opinion, Opinion 491,[47] reminding lawyers that they are responsible for conducting a sufficient inquiry into the facts and circumstances of a matter a client or prospective client asks them to undertake if there is a "high probability" that the client is seeking to use the lawyer's services to commit a crime. But what does that mean in practice?

As we have discussed, there are many and increasing ways that lawyers can face ethical or criminal liability for professional work performed for clients. The need for

lawyers to be on guard against potential money laundering activity by clients is a primary focus of Opinion 491. It states:

> [W]here facts known to the lawyer establish a high probability that a client seeks to use the lawyer's services for criminal or fraudulent activity, the lawyer has a duty to inquire further to avoid advising or assisting such activity .... Even if information learned in the course of a preliminary interview or during a representation is insufficient to establish "knowledge" under [Model] Rule 1.2 (d), other rules may require the lawyer to inquire further in order to help the client avoid crime or fraud, to avoid professional misconduct, and to advance the client's legitimate interest .... If the client or prospective client refuses to provide information necessary to assess the legality of the proposed transaction, the lawyer must ordinarily decline the representation or withdraw under [Model] Rule 1.16

Opinion 491 cites numerous cases, including Supreme Court precedent, incorporating the doctrine of willful blindness into the legal definition of "knowledge." Opinion 491 makes it clear that when there is a "high probability" based on the available facts that the client "seeks to use the lawyer's services for criminal or fraudulent activity," a lawyer cannot proceed without making further inquiry. If not satisfied, the lawyer must turn down the representation or withdraw.

In particular, Opinion 491 references the guidelines developed by the FATF and the need to do a "risk-based approach" to legal engagements to screen for potential money laundering activity. The FATF published a report in 2013 outlining the AML vulnerabilities of legal professionals.[48] In this report, the FATF outlined 42 risk indicators of potential money laundering; some indicators include a client's reluctance to provide information, data, or documents in order to facilitate the transaction. The FATF also issued in 2018 a special report on so-called "professional money launderers," who knowingly provide third-party money laundering services to the direct earners of illicit proceeds in exchange for a commission, fee, or other profit.[49] The special report stressed the need to focus on professionals who could provide a "veneer of legitimacy to criminals."

Prior Opinion 463[50] issued by the ABA had noted that lawyers should engage in due diligence "to avoid facilitating illegal activity or being drawn unwittingly into a criminal activity .... An appropriate assessment of the client and the client's objectives, and the means for obtaining those objectives, are essential prerequisites for accepting a new matter or for continuing a representation as new facts unfold." However, Opinion 491 also makes clear that "as long as the lawyer conducts a reasonable inquiry, it is ordinarily proper to credit an otherwise trustworthy client where information gathered from other sources fails to resolve the issue, even if some doubt remains."

It can be easy to declare the principle that a lawyer or other professional should apply a "risk-based approach" and perform adequate "due diligence" in regard to a client or transaction. However, operationalizing those abstract concepts in the real world can be more daunting, particularly given potentially competing duties such as the need for zealous representation, client confidentiality, and loyalty. Opinion 491 tries to provide some guidance to lawyers about what concrete steps they might take to satisfy their ethical and legal obligations to avoid helping clients engage in illegal or fraudulent activity by providing specific hypotheticals of possible representations that easily could cross over into facilitating money laundering or other offenses.

For example, Opinion 491 presents a hypothetical client who has overseas income and funds held in a foreign bank in the name of an unnamed corporation, but the funds have not been disclosed to taxing authorities. Further, the client refuses to provide any detail about the source of the funds, the name of the bank, or the nature of his employment.

Another example in Opinion 491 of a suspicious potential client is reminiscent of a well-known segment on 60 Minutes, *Anonymous*, *Inc.*,[51] involving an undercover journalist who conducted a "sting" operation by meeting with various lawyers and posing as the representative of a potential foreign client apparently involved in an official corruption scheme:

> A prospective client tells a lawyer he is an agent for a minister or other government official from a "high risk" jurisdiction who wishes to remain anonymous and would like to purchase an expensive property in the United States. The property would be owned through corporations that have undisclosed beneficial owners. The prospective client says that large amounts of money will be involved in the purchase but is vague about the source of the funds, or the funds appear to come from "questionable" sources.

Opinion 491 provides other, more mundane examples. One example involves a long-time client who wants to form LLCs to buy real property. Absent other red flags,

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one presumably would conclude that this representation would be appropriate.

Conclusion

The key takeaway of Opinion 491 underscores the theme of this article: lawyers must assess the circumstances of a client's request and be attuned to any red flags. FinCEN and other regulators continue to increase AML-related reporting requirements that can implicate lawyers, at least occasionally or indirectly, such as through the CTA and the impending regulations regarding the real estate industry. If the legal profession cannot self-regulate effectively as to AML risks, then the government may regulate directly, as reflected by recent efforts to pass the ENABLERS Act.

ENDNOTES

1 Peter D. Hardy, Scott Michel & Fred Murray, *Is the United States Still a Tax Haven? The Government Acts on Tax Compliance and Money Laundering Risks*, J. TAX PRACT. PROC., June–July 2016, at 33. Specifically, the former Panamanian law firm Mossack Fonseca was the subject of a breach of approximately 11.5 million financial and legal documents in April 2016. These leaked documents became known as the "Panama Papers" and were publicized through an international consortium of journalists; they allegedly revealed a global system of undisclosed offshore accounts, money laundering, and other illegal activity.

2 *Pandora Papers,* International Consortium of Investigative Journalists, *www.icij.org/investigations/pandora-papers/* (last visited Feb. 28, 2024).

3 *Financial Secrecy Index 2020 reports progress on global transparency—but backsliding from US, Cayman and UK prompts call for sanctions*, Tax Justice Network (Feb. 28, 2023, 9:30 am), *taxjustice.net/press/financial-secrecy-index-2020-reports-progress-on-global-transparency-but-backsliding-from-us-cayman-and-uk-prompts-call-for-sanctions/*; Eur. Parl., *EU-US trade and investment relations: Effects on tax evasion, money laundering and tax transparency* (2017), *www.europarl.europa.eu/RegData/etudes/IDAN/2017/598602/EPRS_IDA(2017)598602_EN.pdf*.

4 *See* Press Release, Dep't of Just., *Four Defendants Charged in Panama Papers Investigation for Their Roles in Panamanian-Based Global Law Firm's Decades-Long Scheme to Defraud the United States* (Dec. 4, 2018), *www.justice.gov/opa/pr/four-defendants-charged-panama-papers-investigation-their-roles-panamanian-based-global-law*.

5 Establishing New Authorities for Businesses Laundering and Enabling Risks to Security Act, H.R. 5525, 117th Cong. (2022), §5401 (as adopted by H.R., Jul. 13, 2022).

6 The Bank Secrecy Act, or BSA, is found at 31 USC §§5311–5336.

7 Press Release, Internal Revenue Service Criminal Investigations, *BSA data serves key role in investigating financial crimes* (Jan. 18, 2023), *aboutbtax.com/6pX*.

8 Transportation, Housing and Urban Development, Agriculture, Rural Development, Energy and Water Development, Financial Services and General Government, Interior, Environment, Military Construction, and Veterans Affairs Appropriations Act, 2023, H.R. 8294, 117th Cong (2022).

9 *See supra* at n. 5.

10 *See* The White House, *United States Strategy On Countering Corruption* (Dec. 2021), *www.whitehouse.gov/wp-content/uploads/2021/12/United-States-Strategy-on-Countering-Corruption.pdf*. The 2021 Strategy identified unregulated gatekeepers, such as lawyers, accountants, trust and company service providers, and others, as a deficiency in the U.S. regulatory framework. The 2021 Strategy noted that such gatekeepers are not presently required to conduct diligence on the nature or source of income from their clients or prospective clients, which could result in them being access points to the U.S. and international financial systems for corrupt actors. The 2021 Strategy proposed a multi-pronged approach, including working with Congress to secure additional regulatory authority; seeking professional sanctions against gatekeepers who facilitate corruption and money laundering; and expanding government engagement with gatekeepers, including through information sharing.

11 Will Fitzgibbon, *US Senate blocks major anti-money laundering bill, the Enablers Act*, International Consortium of Investigative Journalists (Dec. 12, 2022), *www.icij.org/investigations/pandora-papers/us-senate-blocks-major-anti-money-laundering-bill-the-enablers-act/*.

12 *See* U.S. Dep't of the Treas., *National Strategy for Combating Terrorist and Other Illicit Financing* (May 13, 2022), *home.treasury.gov/system/files/136/2022-National-Strategy-for-Combating-Terrorist-and-Other-Illicit-Financing.pdf*.

13 *See* Basil Institute on Governance, *Basel AML Index 2022: 11th Public Edition Ranking money laundering and terrorist financing risks around the world* (Oct. 2022), *index.baselgovernance.org/api/uploads/221110_Basel_AML_Index_2022_b705cc0842.pdf*. The Basel Institute's 2022 AML Index finds that "designated non-financial businesses and professionals" (DNFBPs), such as lawyers, accountants, and real estate agents, should play an important role as "gatekeepers" of their countries' financial security.

14 *See* FATF, *Professional Money Laundering* (Jul. 26, 2018), *www.fatf-gafi.org/content/dam/fatf/documents/Professional-Money-Laundering.pdf*. The FATF has identified lawyers, accountants, financial advisers, bankers, money value transfer services providers, trust and company service providers, and real estate professionals as potential "Professional Money Launderers" who "can provide a veneer of legitimacy to criminals" and organized crime groups.

15 Peter D. Hardy & Alicia M. Went, *Lawyers as "Gate Keepers"—The European Parliament Examines the Roles of Attorneys in Tax Evasion and Laundering Schemes*, Money Laundering Watch (May 1, 2017), *www.moneylaunderingnews.com/2017/05/tax-evasion/*.

16 *Id*.

17 18 USC §1956(c)(7).

18 The prong involving an intent to commit the crimes of tax evasion or false tax return of course still must involve proceeds earned through the commission of an earlier SUA—and, as noted, the above tax crimes are not included in the statutory list of offenses qualifying as SUAs.

19 18 USC §1957.

20 15 USC §§78dd-1–78dd-3.

21 50 USC §§1701–1707.

22 18 USC §1957(c)(7)(B) provides that the following foreign offenses represent SUAs:

> (i) the manufacture, importation, sale, or distribution of a controlled substance ...;
> (ii) murder, kidnapping, robbery, extortion, destruction of property by means of explosive or fire, or a crime of violence ...;
> (iii) fraud, or any scheme or attempt to defraud, by or against a foreign bank ...;
> (iv) bribery of a public official, or the misappropriation, theft, or embezzlement of public funds by or for the benefit of a public official;
> (v) [certain specified] smuggling or export control violations ...;
> (vi) an offense with respect to which the United States would be obligated by a multilateral treaty, either to extradite the alleged offender or to submit the case for

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prosecution, if the offender were found within the territory of the United States; or (vii) trafficking in persons, selling or buying of children, sexual exploitation of children, or transporting, recruiting or harboring a person, including a child, for commercial sex acts[.]

[23] 18 USC §1956(f).
[24] 18 USC §1957(a)(2).
[25] Peter D. Hardy, Criminal Tax, Money Laundering And Bank Secrecy Act Litigation Ch. 3.III.C (BNA Bloomberg 2010).
[26] *See, e.g.,* 18 USC §981.
[27] *See* Press Release, U.S. Dep't of Just., *United States Reaches Settlement to Recover More Than $700 Million in Assets Allegedly Traceable to Corruption Involving Malaysian Sovereign Wealth Fund* (Oct. 30, 2019), *www.justice.gov/opa/pr/united-states-reaches-settlement-recover-more-700-million-assets-allegedly-traceable*.
[28] The CTA is Title LXIV of the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, Public Law 116-283 (Jan. 1, 2021).
[29] *See* section 6402 of the CTA.
[30] FinCEN, *Beneficial Ownership Information Reporting Requirements*, 87 FR 59498 (Sep. 30, 2022) (to be codified at 31 CFR §1010.80).
[31] FinCEN, *Beneficial Ownership Information Access and Safeguards, and Use of FinCEN Identifiers for Entities*, 87 FR 77404 (Dec. 16, 2022).
[32] *Beneficial Ownership Information Reporting Requirements*, 87 FR at 59537.
[33] *Id.* at 54514.
[34] FinCEN, *Agency Information Collection Activities; Proposed Collection; Comment Request; Beneficial Ownership Information Reports*, 88 FR 2760 (Jan. 17, 2023).
[35] FinCEN, *Anti-Money Laundering Regulations for Real Estate Transactions*, 86 FR 69589 (Dec. 8, 2021). As of this writing, FinCEN has not yet issued proposed regulations for the real estate industry, although FinCEN may have done so by the time of publication.
[36] Dep't of the Treas., *Semiannual Agenda and Regulatory Plan*, 88 FR 11278, 11279 (Feb. 22, 2023).
[37] The ANPRM defines the terms "non-financed purchase," "non-financed transaction," "all-cash purchase," and "all-cash transaction" as referring to "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 (including convertible virtual currency (CVC)), 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." *Anti-Money Laundering Regulations for Real Estate Transactions*, 86 FR at 69589 n. 1.
[38] FinCEN, *Geographic Targeting Order Covering Title Insurance Company* (Oct. 26, 2022), *www.fincen.gov/sites/default/files/shared/Real%20Estate%20GTO_102622_Order_508.pdf*.
[39] FinCEN, *GAO-20-546, FinCEN Should Enhance Procedures for Implementing and Evaluating Geographic Targeting Orders* (Jul. 2020), *www.gao.gov/assets/gao-20-546.pdf*.
[40] *See, e.g.,* endnote 12, *supra*, at 10.
[41] *Anti-Money Laundering Regulations for Real Estate Transactions*, 86 FR at 69595.
[42] *See* Press Release, U.S. Dep't of Just., *Russian Intelligence Agent Charged with Fraud and Money Laundering in Connection with Purchase and Use of Luxury Beverly Hills Real Estate* (Dec. 7, 2022), *www.justice.gov/usao-edny/pr/russian-intelligence-agent-charged-fraud-and-money-laundering-connection-purchase-and*; Press Release, U.S. Dep't of Just., *Associate Of Sanctioned Oligarch Indicted For Sanctions Evasion And Money Laundering* (Feb. 7, 2023), *www.justice.gov/usao-sdny/pr/associate-sanctioned-oligarch-indicted-sanctions-evasion-and-money-laundering*.
[43] FinCEN, *Financial Trend Analysis—Trends in Bank Secrecy Act Data: Financial Activity by Russian Oligarchs in 2022* (Dec. 22, 2022), *www.fincen.gov/sites/default/files/2022-12/Financial%20Trend%20Analysis_Russian%20Oligarchs%20FTA%20_Final.pdf*; *See also* Siana Danch, *Russian Oligarchs and Suspicious Financial Flows: A FinCEN Analysis*, Money Laundering Watch (Jan 3, 2023), *www.moneylaunderingnews.com/2023/01/russian-oligarchs-and-suspicious-financial-flows-a-fincen-analysis/*.
[44] *ABA House adopts host of new policies, including support for ethics code for U.S. Supreme Court*, A.B.A. (Feb. 6, 2023), *www.americanbar.org/news/abanews/aba-news-archives/2023/02/midyear-house-actions-recap/*; *Resolution 704*, A.B.A. (adopted Feb. 6, 2023), *www.americanbar.org/content/dam/aba/directories/policy/midyear-2023/704-midyear-2023.pdf*. *See also* Dylan Tokar, *ABA Passes Resolution Opposing Suspicious-Transaction Reporting Rule for Lawyers*, Wall St. J. (Feb. 7, 2023, 3:54 pm ET), *www.wsj.com/articles/aba-passes-resolution-opposing-suspicious-transaction-reporting-rule-for-lawyers-11675803291*.
[45] *See Resolution 704, supra.* Specifically, the Executive Summary of Resolution 704 states:

> This Resolution also urges that any disclosure requirements [under the CTA] must protect constitutional rights and confidentiality interests, not conflict with the ethical duties, professional conduct requirements, and regulations imposed on the legal profession by a state, territory or tribe's highest court, and not undermine the applicable rules of professional conduct to which lawyers are subject.
>
> This Resolution also reaffirms the vital importance of lawyer-client confidentiality for the rule of law; recognizes that a client's confidence in lawyer-client confidentiality is essential to ensure effective assistance of counsel in criminal, civil, and administrative proceedings and be able to advise a client against a course of action that could be illegal or improper; and thus urges that any beneficial ownership transparency system be designed and administered to best protect and preserve lawyer-client confidentiality while urging Congress to not enact legislation that would regulate the legal profession.

[46] *Id.* Again, the Executive Summary of Resolution 704 states:

> This Resolution urges state, territory, tribal, local, and specialty bar associations and law schools to educate lawyers and law students about the scope of money laundering laws and the anti-money laundering requirements that apply to lawyers to prevent the profession from being used to facilitate money laundering, terrorist financing, corruption, human rights violations, including human trafficking, forced labor, and modern slavery, criminal conduct, and U.S. national security violations.
>
> This Resolution also urges state, territory, tribal, local, and specialty bar associations, and other appropriate constituencies within the legal profession, with the assistance of the American Bar Association, to develop and keep current appropriate voluntary risk-based guidance for client due diligence that will assist lawyers in detecting and preventing money laundering, terrorist financing, corruption, human rights violations, and U.S. national security violations, and assist lawyers in taking appropriate steps to comply with requirements to that end.

Id. at 17 and 18.
[47] ABA Standing Comm. On Ethics & Prof'l Responsibility, Formal Op. 491 (2020).
[48] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013), *www.fatf-gafi.org/content/dam/fatf/documents/reports/ML%20and%20TF%20vulnerabilities%20legal%20professionals.pdf.coredownload.pdf*.
[49] *See Professional Money Laundering*, *supra* endnote 14.
[50] ABA Standing Comm. On Ethics & Prof'l Responsibility, Formal Op. 463 (2013).
[51] *See* Steve Kroft, *Anonymous, Inc.*, CBS News (Jan. 31, 2016, 6:45 pm), *www.cbsnews.com/news/anonymous-inc-60-minutes-steve-kroft-investigation/*.

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