

# Best practices for real estate sector supervision in the Middle East

Various reports by vigilant international bodies during the last few years have mentioned that the real-estate sector is considered one of the many vehicles used by criminal organizations to launder their illicitly obtained money. This article will illustrate the primary ways that the real estate sector's activities can be used for money laundering and terrorists financing. The article will also recommend practices to avoid and mitigate such fraud in the Middle East.

For many decades the real estate sector has posed a high risk for money laundering around the world especially in the Middle East region. All the international organizations, those responsible for setting global standards and provisions including Financial Action Task Force (FATF) and World Bank, have focused on the various risks that this sector contains. These organizations have recommended that banks and real estate agents, and even governments, take specific steps to mitigate these risks.

From a regulatory and supervisory point of view, it is difficult for these entities to face these vulnerabilities in the battle against money laundering and terrorist financing alone. Since the dawn of anti-money laundering and combating terrorist financing worldwide, most Middle Eastern countries have taken little action to prevent the launderers from abusing this sector. However government agencies which regulate the real estate sector can play an important role.

## *Real estate practices in the Middle East and other developing countries*

In the Middle East, as well as in developing countries, real estate with a high-value for example, can be purchased multiple times in one month/week by carrying suitcases full of cash into the real estate registry office (registrar) to convey the ownership of that estate to the new buyer. The problem is that the registration officer fails to report cash transactions or ask the seller whether the payment was made. This is because it presently is not part of registration process. Furthermore, registrar and other registry office officials are not being trained on the money laundering trends and typologies or the launderers AML scenarios through real estate business.

From a banking perspective, such transactions are justifiable when the documents are issued by a real estate registry office — the governmental body responsible for regulating the real estate sector. These documents verify the sale, and that is sufficient for the bank and no suspicious transaction report is going to be filed.

From the real estate perspective, the majority of such transactions in the

Middle East occur between the seller and the buyer, and no real estate agents are involved in this process at all.

For the real estate registrar, the estate conveying process is made for administration purposes, the seller received the proceeds from the sale based on the value of the property. The government's main purpose for regulation is to assure registration and to collect fees. Unfortunately, no consideration is given to money laundering (ML) or terrorists financing (TF) threats. It is time for countries to focus on the ML/TF real estate threats and create a process of mitigating and preventing those risks. Once governments monitor these operations it will become difficult for criminals to manipulate this sector. Real-time transaction monitoring is key.

## *1. Real estate appraisers should be involved in the process of purchase.*

Most countries in the Middle East now rely on real estate appraisers (assessors) in the process of evaluating the real value for estates. Although the purpose behind this is for collecting registration fees, regulators can also benefit by deterring the use of price manipulation schemes. Whether the agreed value between two parties was higher or lower than the assessed value, the latter will be the registered price and the seller will get his/her money based on that assessment which was conducted by the registry office specialist.

## *2. Value of real estate should be paid using bank draft checks*

Some regulators rely on banks in different situations. For instance, when establishing a brand new company, it is a

regulatory requirement as part of getting registration and incorporation papers to require companies to present a bank statement showing the account balance representing the company's capital.

There is no need for cash to be circulated in the process of purchasing estates. The banking sector is the most compliant sector among other sectors in the Middle East with money laundering provisions, they know their customers better, and they are vigilant not to be vehicles for money laundering or terrorist financing. The question is why not relying on this sector to mitigate such risks?

This is the way the process should be carried out. Once the buyer has found the estate, and based on the assessor's price, it is highly recommended and suggested that money is to be paid via draft checks drawn on a buyer's reputable bank account. This way the buyer's money is previously being verified when it is first presented to the bank. When depositing the said check into the seller's bank account, the seller is required to clarify the source of the attached check with documents. As for checks, they should be issued to the first beneficiary with no endorsement restrictions. A copy for that check should be attached to relinquishment application documents and archived into registrar premises.

## *3. Implement of a monitoring system*

Many securities' regulators utilize surveillance systems to monitor trading in order to identify violations. When securities fall under a money laundering law, AML/CTF is often added to the function. Similarly, this approach can be applied to real estate transactions. No comprehensive

and effective regulation could be efficient without similar information technology support. Such technology needs to be added on the current registrar database to record abnormalities in transactions activities. Based on defined rules embedded in the registration system, it is possible through monitoring to raise red flags on a daily basis in the following scenarios:

- Estate being sold several times during a predefined period.
- Estate being sold in a value lower than the purchase price (previous price).
- Individuals who are not real estate agents or registered real estate merchants and are involved in several unreasonable purchasing transactions.

#### 4. Designation of compliance officer within the real-estate registrar

To prevent and identify money laundering and terrorist financing in the real estate sector, the government must provide staff to investigate the abnormalities identified by the monitoring system and appoint an official who will submit those red flags to the FIU.

Ideally, a new expert would be hired within the real estate registrar to watch the monitoring system performance and report to the Financial Intelligence Unit unreasonable transactions after investigating abnormalities. This person should be trained on real estate sector risks for money laundering and terrorist financing typologies.

#### Challenges:


Donations in the form of real estate present a significant problem in preventing and identifying ML/TF. Sometimes, an estate might be donated from one person to another and would want to convey the ownership of that estate to the new owner without money. Such activities may be regulated by notaries to verify the purpose and relationship between the two parties and must be reasonable. In these cases notaries should be alerted to the possibilities of ML/TF and maintain an appropriate AML/CTF program.

Some tax-haven countries may find a problem in implementing such practices for foreign investors because the real estate sector is very attractive to those entities. Tax-haven governments encourage investment in their countries; however, AML/CTF procedures could discourage foreign investors accordingly. These countries could face other negative impacts derived from the property held by money launderers. Often the launderers will abandon the property, leaving the country to suffer from the socioeconomic problems including increased crime and corruption, mistaken decisions regarding economic policy, economic distortion and disability, loss of tax and revenues and the reputational risk for the country.

#### Exemptions:

Each country, based on its legislations and circumstances, may exempt some parties from going through this practice. For example, in the case of inheritance; the heritage should be divided among inheritors. However, the properties' compliance officer can further investigate this situation and make his/her reports according to the findings.

#### Conclusion

Middle Eastern countries have witnessed a significant increase in real estate sales and real estate development and acknowledge the connection to AML/CTF. Registration of real estate is the key area in applying good AML/CTF practices. 

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