

Understanding How Money Laundering and Financing of Terrorism Are Conducted through the Real Estate Sector in the Middle East and North Africa Region

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Abstract—This research seeks to identify how money laundering activities are executed through the real estate sector. This article provides academics with literature on the topic and provides scholars, and practitioners with a better understanding of the risks and challenges involved. Data are gathered through survey in the Middle East and North Africa region and review of the available research. The results of the analysis will help identifying the factors attracting criminals to the real estate sector and develop an understanding of the methods used to launder illicit funds through this sector and the indicators of suspicion for reporting entities. Further analysis reveals the risks posed by money laundering and terrorist financing on the real estate sector and challenges facing states in this regard.

Keywords—Money laundering, terrorism financing, real estate sector, Middle East and North Africa.

I. INTRODUCTION

MONEY launderers and terrorists are constantly seeking new ways to circulate their money through the financial system and are actively examining several economic sectors to test their vulnerability to their operations and suitability to their objectives. The real estate sector is an active sector in the Middle East and North Africa Region and the high turnover of its operations constitute an attracting sector to criminals. This research relies on information collected in survey from supervisors and practitioners in Middle East and North Africa states in order to understand how laundering activities are being conducted through the real estate sector.

II. ATTRACTING FACTORS

The primary concern of money laundering operations is to provide legal cover to illicitly generated funds. Mainly this is possible when launderers find the proper environment to accommodate these funds within the community while being away from confiscation and evading punishment [1], such environment possesses attracting factors for criminals. The survey revealed several factors that make money laundering possible within the real estate sector:

1. Weakness or incompetence of the regulatory authorities supervising the Real Estate sector in the anti-money laundering context.

2. Regulatory authorities using outdated or traditional information systems which will hinder proper analysis of information to uncover Money Laundering cases.
3. Parties not fulfilling their obligation to report suspicious transactions to competent authorities, such as estate houses and real estate bureaus.
4. Lack of know-how or inexperience in detecting money laundering operations within the real estate sector (agents, brokers, etc...)
5. Inefficiency of measures taken by regulatory authorities over the real estate sector.
6. Spread of poverty in the society as well as soliciting bribes in the administration to facilitate transactions. This will lead employees to ignore their duties in reporting suspicion of money laundering cases.
7. Corruption at the state level: politicians will exercise influence to protect wrongdoers and cover violations.
8. Gaps and flaws in regulations and laws allowing attorneys to assist criminals in evading prosecution.
9. Instability in countries: Jurisdictions suffering from political or economic instability or wars constitute a suitable environment to receive illicit funds and abusing the real estate sector for money laundering purposes.
10. Low barriers for criminals: The size of the parallel economy and the possibility of conducting illegal activities within the real estate sector constitute factors attracting criminals to this sector as it provides them a cover to channel their illicit funds.
11. States shifting towards expansion and establishment of new cities and communities, as well as developing old neighborhoods in an initiative to deliver residential units convenient to various classes of income.
12. Reporting entities failing to monitor suspicious transactions
13. Difficulty in identifying the true beneficiary of real estate transactions whether in sale or purchase.

However, additional factors were revealed by the survey but rank as secondary to the previously mentioned factors:

- a) A variety in prices of properties based on property location and type, making the property more appealing to money launderers
- b) Having a cash-based society and active informal economy which significantly imposes high risks to infiltration of illegal money to the real estate sector.

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- c) Currency instability in some states, resulting in failure to control real estate prices.
- d) Legislations that are not properly enforced or amended when needed to be.
- e) Regulations lacking the provision to enforce compliance with anti-money laundering within the sector
- f) The characteristics of the real estate sector being a favored area for investment

III. METHODS USED

The success of laundering operations requires infiltration of the illicit funds into the financial system, namely banks, in order to proceed to further steps of the process. To achieve this, criminals aim at the appropriate methods given the sector they're laundering their funds within. Analysis of data surveyed survey revealed the following methods used:

1. Purchasing real estate using illicit funds: At a later stage the real estate will be sold in exchange for bankers' checks to be deposited then in bank accounts being the proceeds of legitimate transactions [2].
2. Acquisition of units in resorts using illicit funds for the purpose of lending and generating legal proceeds
3. Acquisition of property in large amounts of cash, while payment is possible in alternative payment methods.
4. Acquisition of luxurious units in privileged sites to ensure being sold later for high prices.
5. Acquisition of land by illicit funds, transformed later into housing project yielding residential units sold to generate allegedly "legal funds".
6. Conducting well documented fictitious real estate operations allowing funds to move through financial institutions.
7. Acquisition of real estate through loans, for which monthly installments are settled by illicit funds.

IV. RISKS POSED

Anytime criminals succeed in moving their illegally obtained funds through a specific sector in the economy, they will keep coming over and over especially if their methods used in the process are still uncovered to supervisors [3]. This will pose high risks to the country(ies) subject to their operations, this research revealed several risks of money laundering operations on the social and economic levels, stated as follows:

On the economic front:

1. Escalation in domestic prices will put the economy under inflationary pressures which in turn hinder social and economic growth.
2. Real estate prices will rise in a disproportionate way with the actual benefit from the property. This rise accompanied with a decline in purchasing power resulting in stagnation of the real estate sector.
3. A real estate sector infiltrated by money launderers will suffer from shortage in national income, which will divert states towards credits and external sources of financing

putting the country under debt and inability to settle these debts in the future.

4. Investment projects will turn into fictitious projects whose primary objective is to conceal Money Laundering operations and smuggle funds outside the economy.
5. Domestic investors will refrain from investing their money within the country preferring to move them overseas, this will result in deterrence of investment from the economy.
6. Increased public spending leads to the exhaustion of country's resources in countering this phenomenon [3].
7. Exchange rates become unstable within involved countries. There will be negative impact on currency and the exchange rate in both countries (issuing and receiving funds) [3].

On the social front:

1. Criminals succeeding in laundering money through real estate thus evading law enforcement reach and prosecution will keep repeating the same act resulting in spread of crime within the society.
2. Rise in unemployment: Success in laundering money through real estate will lead to circulation of laundered money outside the country depriving the economy from national income which will result in diminishing investment spending in such projects; therefore pertaining jobs will reduce [2].
3. Spread of crime in the society witnessing a decline in moral values and spread of the culture of quick and easy gain, allow more room for criminal acts to be executed.
4. Monopoly of the upper class to the principal proportion of national income leads to imbalance of its distribution among large segments of the society [4].
5. Looting people's wealth and stealing their earnings leads to spreading poverty
6. Propagation of the culture of easy gain and quick money leads to loss of the will to work hard.
7. Crime is widely spread, and people become unwilling to resist it.

The Financial Action Task Force being the primary standard setter in Anti Money Laundering and Countering Financing of Terrorism (AML/CFT), urged member states to implement their National Risk Assessment (NRA) which helps every country to identify, evaluate and understand their ML/TF risks. Once performed, the NRA will help jurisdictions to prioritize and efficiently allocate their resources by authorities to face inherent AML/CFT risks. A part of the survey addressed this matter, specifically whether NRA conducted at their states includes risks pertinent to the real estate sector, data gathered revealed that most of the states surveyed did not complete their NRA as it appears in Fig. 1.

It is worth to note that countries, who completed their national risk assessment, evaluated risks of money laundering in the real estate sector as moderate to high.

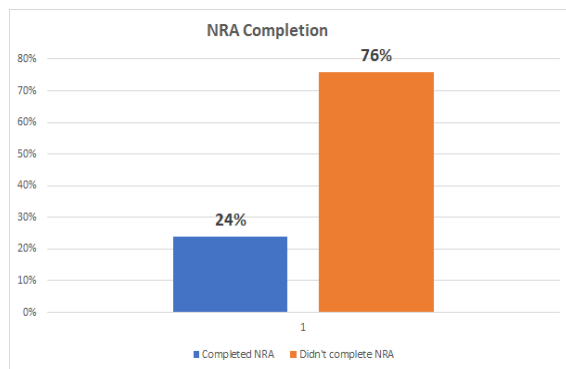


Fig. 1 NRA completion

V. CHARACTERISTICS OF SUPERVISORY AUTHORITIES

Regulatory authorities supervising the real estate sector must have specific characteristics in order to discharge their duties well in protecting the sector against intrusion of money launderers, the survey addressed that issue, analysis of answers regarding common competencies of the regulatory authorities revealed the following:

1. Authorities should possess the licensing powers for agencies or companies working in this domain. Unlicensed agencies should not be permitted to work.
2. Must have the powers of oversight and authority over companies/agencies working in the real estate sector.
3. Authorities should possess the powers to enforce sanctions.
4. Authorities must have the ability to exchange relevant information with competent authorities.

VI. CHALLENGES AND INDICATORS

Economic sectors are in risk of intrusion of money laundering operations, since criminals follow where money circulates, countries must raise the bar in fighting money laundering by understanding the before mentioned methods and risks in this particular sector and exercise due attention [1]. Several challenges will face regulators and supervisors in this regard; the survey resulted in the following challenges:

1. Lack or weakness of regulations imposing compliance with AML/CFT laws to employees
2. Lack of certification requirements for persons or agencies from competent authorities.
3. Absence of awareness expertise among real estate brokers in respect to risks of money laundering and methods in the real estate sector.
4. Inability to determine the extent the compliance of the real estate sector with the requirements of anti-money laundering.
5. Cash being accepted as payment method in real estate operations.
6. Lack of anti-money laundering requirements in regulations pertaining to real estate sector transactions.
7. Low transparency in real estate trading procedures.
8. Lack of sanctions on agencies and brokers non-complying with anti-money laundering requirements.

9. Presence of several properties/lands in unsettled zones or falling beyond the authority of the state.
10. Foreign real estate companies benefiting from the services of local companies to undergo sales or purchase transactions without verification of their compliance with anti-money laundering requirements.
11. Weak or inadequate monitoring to payment methods or transfer methods used among dealers in conducting real estate transactions.
12. The rise of the number of brokers, which requires reinforcement of supervision procedures.
13. Lack of awareness to risks of money laundering within parties working in the real estate sector.
14. Authorities regulating the real estate sector low on resources and possessing poor capabilities.

In the context of fighting money laundering within any economic sector, reporting entities (like banks, brokerage firms, real estate agents, notaries, etc...) rely on several indicators specific to each sector, for which the presence of any within a transaction constitutes a warning sign for possibility of money laundering and requires the reporting entity to apply scrutiny and enhanced due diligence over the transaction prior to approval. The survey collected several indicators of possibility of money laundering within the real estate sector, we mention the following:

1. A client selling property registered in their name to his own company
2. Sudden movement of the bank account of a real estate broker/agency and deposit/withdrawal of frequent checks or transfers.
3. Real estate brokers/agents providing justification documents pertaining to the same person showing different signatures.
4. Clients purchasing uninspected property
5. Real estate transaction executed faster than similar transactions
6. Purchase of several apartments in various towers within the same project
7. A remarkable good relation connecting the real estate agent with the buyer
8. Conducting purchase of real estate in the absence of the buyer (being on travel for example)
9. Issuing a bankers' check for an alleged real estate transaction, then retrieving it shortly.
10. Executing a real estate transaction that contains violations to registration procedures.

On the other hand, these reporting entities must fulfill their duties in reporting to competent authorities any suspicious transactions that may encounter. The survey touched on that issue and revealed the following entities that reported suspicious transactions in the real estate as appears in Fig. 2.

The highest ratio in reporting suspicious activities within the real estate sector belongs to banks being the main reporting entity; this may indicate weaknesses in the legal framework or absence of reporting requirement to some entities or low levels of awareness to money laundering risks within these entities.

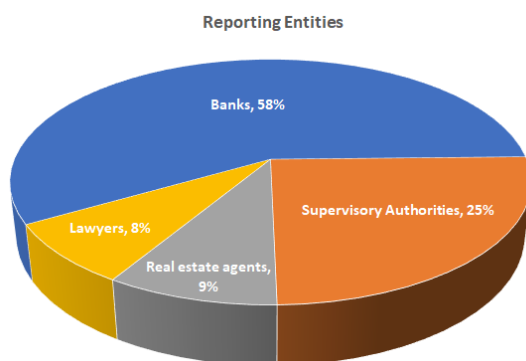


Fig. 2 Entities reporting suspicious transactions

VII. FACILITATORS AND OBSTACLES

Several factors act as facilitators to counter money laundering, analysis of surveys revealed the following factors:

1. Establishment of electronic communication channels between concerned authorities namely the Financial Intelligence Unit, law enforcement authorities and others...
2. Enforcement of compulsory policies and procedures mandating payment for real estate transactions through financial institutions.
3. Empowering employees and establishment an anti-money laundering function within the concerned authority of the real estate sector.
4. Implementing necessary amendments to legislations, policies and procedures governing real estate transactions.

On the international level, following the money trail outside the country requires international cooperation among involved states, enforcing confiscation measures and asset recovery procedures [5]. According to data gathered, obstacles on the international level pose as follows:

1. States unwilling to engage in multilateral or bilateral agreements to facilitate detecting money laundering offences through real estate transactions.
2. Difference in regulations and procedures for confiscation and asset recovery among states.
3. States unresponsive to Mutual Legal Assistance Treaties requests.
4. Delays in response from some countries which affect subsequent procedures or resulting in loss of asset value.
5. Financial Intelligence Units unwilling to sign Memoranda Of Understanding (MOUs) with other counterparts.
6. Difference in criminalization or characterization of the offence among states, impeding prosecution of perpetrators

Recommendations and suggestions:

1. Issuance of regulations or updating existing laws pertinent to the real estate sector in order to conform to local and international AML requirements and standards.
2. Establishing controls for ownership of real estate by foreigners, in addition to close monitoring of transaction conducted on their behalf.
3. Establishing mechanisms for coordination between local

agencies concerned with regulation and supervision of the real estate sector.

4. Verification of the authenticity and validity of the contracts and proxies issued by nationals living abroad or foreign persons allowing dealing in real estate on their behalf.
5. Implementing background checks on persons (natural or legal) applying for licenses to operate in the real estate sector.

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