

## FINANCIAL LAW

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### **REAL ESTATE IN THE SCHEMES OF LEGALIZATION: PREVENTIVE ASPECTS OF PREVENTION AND COUNTERACTION**

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*Analyzed schemes related to the legalization of illegally acquired real estate (including land plots). Disclosed preventive aspects of prevention and counteraction to legalization of assets derived from crime, on the real estate market. The role of realtors and notaries in these processes.*

***Real estate, realty, legalization, a realtor, a notary, typology,  
State Financial Monitoring Service of Ukraine.***

Striving against legalization of assets of criminal origin is an important question that requires constant determination and improvement in the conditions of a lawful state. For many years Ukraine has established a system of prevention and counteraction to legalization (laundering) of incomes obtained in a criminal way.

According to the national legislation, namely article 1 of the Law of Ukraine «On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing», under the proceeds of crime, shall mean any economic benefit resulting from the Commission of a socially dangerous act prior to the legalization (laundering) of income which may consist of material property or property rights, expressed in rights, and include movable or immovable property and documents confirming the right to such property or a share in it [1].

In this case, the legislator determined that a constituent element of criminally obtained revenues, among other things, may be also an immovable property.

In this context, the institutional and regulatory level implemented a number of activities to strive against the laundering of assets on the property market and to identify the relevant schemes of legalization.

With the study of this issue was engaged a great number of scientists and practitioners, including the works of S.G. Gurzhiy, A.T. Kovalchuk, O.E. Koristin, V.I. Kurilo, A.V. Matios, O.U. Feshchenko and others. Thus, despite the understanding of the topic, the problem of legalization of real estate market remains relevant and schemes of legalization in this segment requires generalization. Simultaneously overdue is a discussion of the changes regarding to the improvement of the relevant legislation on these issues.

The purpose of this article is the analysis of schemes related to the legalization of illegally acquired real estate, the overview of preventive aspects of prevention and counteraction to legalization of assets derived from crime, on the real estate market and search of proposals on improving the legal framework to strive against legalization of criminally obtained immovable property.

Schemes of money laundering on the real estate market can be complex, confusing, have a lot of branches, but they all consist of a relatively small number of ordinary operations.

Pursuant to part two of the article 18 of the Law of Ukraine « On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing» [1] the State Financial Monitoring Service of Ukraine:

- analyzes ML/TF methods and financial schemes;
- assists in the detection of indicators of criminal proceeds usage in financial transactions.

Considering the above mentioned by the State Financial Monitoring Service of Ukraine the typologies are developed and generalized, based on the schemes which are revealed by the State Financial Monitoring Service of Ukraine , law enforcement or other competent state bodies.

Entities that cooperate with the State Financial Monitoring Service of Ukraine with the purpose of prevention of legalization of the real estate market, are subjects of entrepreneurial activity, which provide intermediary services for purchase-sale of real estate (realtors) and notaries.

Starting from 2010, realtors, notaries have been related to the system of money laundering striving. They have the status of so-called specially designated by the entities of initial financial monitoring.

The study of the question of the legal status of realtors and notaries, as specifically identified subjects of primary financial monitoring shall be subject to a separate scientific research, therefore we won't pay attention to it now. However, in the framework of this research, the following subject should be addressed to this topic.

In accordance with the current legislation realtors, notaries report to the State Financial Monitoring Service of Ukraine about financial operations which are subject to internal financial monitoring with simultaneous coincidence of three conditions:

- 1) preparation, implementation or legitimization of buying-selling contract of real estate;
- 2) the sum of the transaction equals to or exceeds 400 000 UAH or equals or exceeds the amount of foreign currency equivalent of 400 000 UAH;
- 3) of suspicion that financial transaction might be related to ML or TF.

In other cases, realtors, notaries are not obliged to inform the State Financial Monitoring Service of Ukraine, but they have the right to initiate them by their own will.

Taking into account the fact that the obligation of notification to the State Financial Monitoring Service of Ukraine is not «automatically» natural and is conditional, the real estate market in this field with these entities is attractive for legalization (money laundering).

Abusing on the market of immovable property criminals use a variety of methods and mechanisms, the vast majority of which can be considered quite legal, however, there is a very big «but» – they use assets of illegal origin.

Criminals laundering money due to the operations of purchase and sale of objects of the real estate, investments in housing construction, misappropriate property etc.

The author's classification schemes of legalization of the real estate market are based on the analysis of typological research on this issue by the State Financial Monitoring Service of Ukraine [2, 3] which shows that the most typical schemes are related to:

- fraud in the real estate market;
- using fictitious transactions with immovable property;
- unlawful seizure of land by non-residents;
- manipulation of the property's market value.

Let us consider the scheme more detailed.

### ***Fraud in the real estate market.***

1. The Crime, which subject is property, covers a wide range of sections and articles in the Criminal code of Ukraine [4]. From the amount of crimes in the real estate sphere the most common is fraud (article 190 of the Criminal code of Ukraine).

The General scheme of fraud on the real estate market, as a rule, consists of four stages: The search of the victim; «processing» of the victim; primary alienation; final disposal.

1. The search of the victims. Information on persons from the «risk group» is going to or with the help of state institutions, which keep the

relevant records (housing operational office, passport offices, the police, social services, hospitals) or by non-governmental organizations, which sometimes present themselves as «charitable» (for example, soup kitchens for the homeless, etc).

2. «Processing» of the victim. Can be done in two ways: the first one is when «benefactors» come to the victims and starting to gain the trust, the second, one is when the brute force is used, namely, abduction, tin, violent signature of documents etc.

3. Primary alienation. The first sale is made in the name of a member of the group, the so-called «first strip», a group of people who have nothing to lose.

If, however, some relatives appear applying for an apartment, or the owner starts for active steps – then the so-called «second lining» is used, to which the apartment is resold on behalf of «the first lining ». Usually it is a member of the lower-level gangster group, the information about them is absent at the police. Such, who has a look of a respectable purchaser. The Apartment he usually buys under the power of attorney.

While the ongoing lawsuit (and this may take years), real estate property is used to get the maximum profit. Of the known cases: in such apartments are arranged brothel, transit points for illegal migrants, everything that can make a great income.

4. Final disposal. If after the first alienation it turns out that no one stood up for the victim, relatives of the victim did not appear, or the victim has run out of power to resist the advancement of religion - the apartment is sold to bona fide purchasers, i.e. ordinary buyers.

Part of the funds received from the sale of illegally obtained property is subsequently used for financing further illegal actions.

Of course in this case the criminals use the notary because he identifies appropriate sale of real estate. In addition, realtor can participate in the scheme.

Examples of such schemes are contained in the Typologies of legalization (laundering) of the proceeds of crime through the real estate market [2].

In this context, we can underline the scheme of appropriation of property (assets) of the founders of the construction financing Fund. The two main classification ways of appropriation of investors' funds during the construction period are frauds related with attraction of funds of clients (investors), without the intention to fulfill its obligations on the construction of housing and misappropriation of funds by investors service abuses by representatives of the companies-managers of funds and developers [3].

### ***Use of fictitious transactions with immovable property.***

Such schemes, in most cases, are parts of a more complex schemes of money laundering. The obligatory condition of this scheme is to falsify documents on object of the transaction.

The essence of the scheme is that the funds of illegal origin acquire legal settlements in transactions with immovable property. Money laundering occurs through the implementation of a fictitious sale of objects of the real estate.

In this scheme, suspicions of legalization can be based on such factors: the use of lost, false identity documents; the unknown origin of the capital involved in operations with the real estate; the buyer is a legal entity with an insignificant period activity (as a rule, such a period shall not exceed three months from the date of state registration); there is no contract of sale of immovable property; information in the contract of sale is inconsistent or incorrect.

### ***Illegal appropriation of land by non-residents.***

The essence of these schemes is obtained by residents from non-residents of the credit for realization of financial and economic activity. Received from non-resident funds are bought by the resident land plots and loan funds are simply not returned.

In accordance with part one-fourth of article 81 of the Land code of Ukraine [5] non-residents do not have the right to be owners of agricultural land in Ukraine. But no matter how paradoxically, in the case of delay or inability to return the loan, any immovable property may become property of a non-resident.

Thus, creates certain conditions for the misappropriation of land in Ukraine of specific non-resident, which makes it possible, on the account of the existence of legislative gaps, to circumvent the direct norms of laws that ban non-residents of the agricultural lands.

In this scheme, suspicions of legalization can be based on such factors: the origin of the capital involved in operations with immovable property, the unknown and abroad; the newly established enterprise is organized exclusively for the acquisition of land and no other financial and economic activity is not run and is not controlled by non-residents; purchase and sale of land at prices significantly different from the market; failure to meet the conditions of the loan, namely the abrupt cessation of the main payments and interest thereon; participants in the scheme are physical person, including the founders of legal entities at the age and/or physical condition which may indicate the impossibility of leading active business activities (under 25 or over 70 years).

### ***Manipulation of the property's market value.***

Manipulating the market price of the property may include both underestimation and overestimation, which accompanies the purchase/sale transactions. Market value of real estate can be difficult for evaluation, especially when it comes to non-standard real estate objects, such as hotel complexes, sports clubs. This trend is used by criminals, which facilitates the manipulation of market value.

The essence of the scheme of money laundering using speculative operations with real estate is that the mediator buys the object at a low price, by receiving money within crime, and then sells it to the attacker at a

much higher price. That is, thanks to artificial overstatement of property, the conciliator receives not only profit, but also legalizes criminal funds.

The distinctive feature of such schemes can be cyclical resale objects, as well as the participation of «transit», fictitious firms. You can use falsification estimated documentation for the real estate, purchase agreements.

In this scheme, suspicions of legalization can be based on such factors: the origin of the capital, attracted for conducting operations with real estate, unknown and abroad; member of the scheme is the person who is brought to criminal responsibility; the participants of the transboundary transfer does not have direct relations; operations of purchase/sale of immovable property is carried out in a very short period of time; resale of immovable property at a high/low prices is to provide capital type of legal origin.

To identify these and other schemes of legalization on the market of the real estate realtors, notaries should use Criteria for the risk legalization (laundering) of the proceeds of crime and terrorism financing, approved by the State Financial Monitoring Service of Ukraine [6].

The above mentioned shows that realtors and notaries can be used by criminals in the scheme, because they play a central role in the implementation of operations on the real estate market. Realtors and notaries can detect false data in signed documents which are given for the transfer of assets that may be persons who hold a financial operation, and subject of the transaction, a scheme to conceal the sources of funds, their owners, the location and control of assets derived from crime.

Finally, we cannot ignore the fact that at the present time, national legislation in the sphere of financial monitoring is the process of reform. This is due to the adoption in 2012, the new version of Standards of the Financial Action Task Force (FATF) – the FATF Recommendations [7].

With this in mind, the new draft proposed by the state financial monitoring Commission of Ukraine, Law of Ukraine «On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing», in December 2013 placed on the official web-site of the specified body [8] there will be some novelties relating to measures for prevention and counteraction to legalization of the real estate market, which will be accepted by real estate brokers, and notaries.

One of such events (and probably most important) is the abolition of the threshold amount of the transaction on purchase-sale of real estate, which currently amounts to 400 000 UAH and more (or foreign currency equivalent). It is proposed to establish that the participation of realtors and notaries in real estate transactions, irrespective of the amount thereof, is the basis for their financial monitoring and the provision in cases of suspicion of information the State Financial Monitoring Service of Ukraine.

Considering the above mentioned, the efforts of the developers of the new legislative initiatives are justified on the harmonization of the national legislation with international legal standards in the field of combating money laundering. Such actions, of course, are directed to the establishment and provision of legal bases of functioning real estate market and protection of the land, as the main national wealth.

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