Andrew O. Alcala

USA PATRIOT ACT AND THE GATEKEEPER INITIATIVE:

Surprising Implications for Transactional Lawyers

By Kevin L. Shepherd

Americans are asking: How will we fight and win this war? We will direct every resource at our command—every means of diplomacy, every tool of intelligence, every instrument of law enforcement, every financial influence, and every necessary weapon of war—to the disruption and to the defeat of the global terror network.

—President George W. Bush, Address to the Joint Session of Congress and the Nation, September 20, 2001.

Michelle Lynne is a successful and busy (albeit fictitious) real estate lawyer in Wichita, Kansas. Her thriving practice often involves the formation of limited liability companies (LLCs) and other entities to facilitate her clients' business needs. Lynne's activities include assisting her clients in opening bank accounts for the newly formed entities, filing the appropriate formation documentation with the state authorities, and advising her clients on entity selection and other related issues. Lynne also handles the closings for her clients' real estate transactions, often serving as escrow agent or as the title closing officer. A sole practitioner with a number of legal assistants, she provides legal advice embracing a wide realm of business and tax law.

In May 2002, an accountant refers one of his new clients, a Middle Eastern couple, to Lynne and she gladly accepts the referral. In their initial meeting with Lynne, the couple asks Lynne to assist them in

---

Kevin L. Shepherd is co-chair of the Real Estate Practice Group at Venable, Baetjer and Howard, LLP, in Baltimore, Maryland, and the Real Property Division Vice Chair of the Section. He is a member of the ABA Task Force on Gatekeeper Regulation and the Profession. The views stated herein are those of the author alone and not necessarily those of the Task Force or the ABA.

acquiring an undeveloped parcel of land in southeastern Kansas and to form an LLC to acquire title to the land. Lynne prepares the formation documentation, files it with the state, assists the couple in opening a new bank account for the newly formed entity, prepares and negotiates the contract of sale for the acquisition of the land, and prepares the title commitment for the parcel of land. When Lynne inquires about acquisition financing, the couple indicates that they plan to acquire the $900,000 parcel of land without financing.

Other than what she learned during her initial meeting with the couple and a subsequent meeting during which Lynne explained the documentation to the couple, Lynne knows nothing about the couple. She does not know their religion, politics, country of origin, whether the couple has any other relatives in the area, or whether the couple has the cash for the acquisition and, if not, where the couple plans to obtain the funds to pay the purchase price.

Several weeks later, Lynne handles the closing of the transaction. Lynne learns that the couple's closing funds are being wired to her escrow account from a U.S. bank's foreign office in Lebanon. Lynne receives the funds, the seller and buyer exchange the closing documentation, and the deal closes.

The type of transaction described above occurs countless times a year throughout the country. But the confluence of the United and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001 (Act), Pub. L. No. 107-56, 115 Stat. 272 (Oct. 26, 2001), the regulations issued under the authority of the Act, and the so-called "Gatekeeper Initiative" may impose unprecedented and far-reaching duties on a lawyer such as Lynne in her capacity both as a lawyer and as a person engaged in real estate closings and settlements. These duties run counter to the confidentiality and zealous representation obligations of lawyers.

Some believe that the special relationship between lawyers and their clients gives lawyers an early inside view into crimes that could make their insights invaluable in the war on domestic and international criminal activity.

Gatekeeper Initiative

A "gatekeeper" is one who controls access. MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY. In the context of international money laundering and terrorist financing, lawyers are viewed as "gatekeepers" to the domestic and international monetary system. Some believe that the special relationship between lawyers and their clients gives lawyers an early inside view into crimes that could make their insights invaluable in the war on domestic and international criminal activity. Indeed, the confidentiality obligations of lawyers make them particularly attractive to those who desire to engage in money laundering activities. John Gibeaut, *Lining Up Help Online*, A.B.A.J., Jan. 2002, at 49. The Gatekeeper Initiative is designed to create additional hurdles for those who seek to gain access to this monetary system.

The Gatekeeper Initiative, which seeks to define the roles and responsibilities of lawyers in combating money laundering activities, has its genesis in the Ministerial Conference of the G-8 Countries on Combating Transnational Organized Crime held October 19–20, 1999, in Moscow. In a document known as the Moscow Communiqué, the G-8 Members agreed to bring their respective anti-money laundering regimes into closer alignment and "to consider putting certain responsibilities, as appropriate, on those professionals, such as *lawyers*, accountants, company formation agents, auditors, and other financial intermediaries who can either block or facilitate the entry of organized crime money into the financial system." Communiqué available at **www.library.utoronto.ca/g7/adhoc/crime99.htm** (emphasis added).

The Gatekeeper Initiative derives additional support from the Financial Action Task Force on Money Laundering (FATF), which was created in 1989 at the G-7 Summit held in Paris in response to increased concern about money laundering. FATF is a 28-member international policymaking entity, with the United States among its members. In 1990, FATF issued 40 recommendations to combat money laundering. The 40 recommendations, which have been updated to reflect changes in money laundering, provide a range of countermeasures against money laundering covering the criminal justice system and law enforcement, the financial system and its regulation, and international cooperation. See Forty Recommendations, available at **www1.oecd.org/fatf/40Recs-en.htm** (FATF website).

In response to the September 11 terrorist attacks on the United States, FATF convened an Extraordinary Plenary on the Financing of Terrorism in Washington, D.C., on October 29–30, 2001. At this meeting, FATF expanded its mission beyond typical criminal money laundering to bring its expertise to bear on the global fight against terrorist financing. FATF issued a set of new international standards called the "Special Recommendations on Terrorist Financing" to combat terrorist financing and asked that all countries adopt and implement these new standards. Special Recommendations on Terrorist Financing, available at **www1.oecd.org/fatf/SrecsTF_en.htm**. FATF believes these new standards will more effectively deny terrorists and their supporters access to the international financial system.

FATF issued a Review of the FATF Forty Recommendations Consultation Paper (Consultation

The Task Force is charged with analyzing the broad legal implications of efforts to thwart international money laundering and the potentially profound impact those efforts could produce on relationships between lawyers and their clients.

Paper) on May 30, 2002. The Consultation Paper outlines the options that FATF member countries are evaluating on the Gatekeeper Initiative, i.e., what role and obligations should lawyers have in combating money laundering and terrorist financing. In connection with the Consultation Paper and FATF's efforts, the U.S. Department of Justice has engaged in an outreach effort to a number of professional organizations, including the American Bar Association, to develop an acceptable recommendation. The Justice Department is also working with the Treasury Department and its Financial Crimes Enforcement Network (FinCEN), the Securities Exchange Commission, and federal bank regulators on the Gatekeeper Initiative.

ABA Task Force

Because of the reach of the Gatekeeper Initiative and a desire to enable the ABA to have a meaningful role in advising federal policymakers as they examine anti-money laundering proposals, ABA President Robert E. Hirshon appointed the ABA Task Force on Gatekeeper Regulation and the Profession (the Task Force) on February 1, 2002. The Task Force is chaired by Edward J. Krauland, a member of the governing council of the ABA Section of International Law and Practice and a co-chair of that section's Anti-Money Laundering Task Force. The Task Force is charged with analyzing the broad legal implications of efforts to thwart international money laundering and the potentially profound impact those efforts could produce on relationships between lawyers and their clients.

Legislation in Other Countries

Several FATF members have already taken steps to implement the Gatekeeper Initiative.

The following highlights some of these approaches, organized from the least onerous to the most onerous regulatory regimes:

- *UK Approach.* Lawyers are subjected to suspicious activity reporting (SAR) requirements and internal compliance requirements. Under the UK approach, there is an exception for certain litigation matters. The UK approach makes it a criminal offense for a lawyer to alert a client that the lawyer is filing an SAR with the governmental authorities.
- *EU Directive Approach.* Under the European Union Directive approach, lawyers are subjected to the SAR requirement with a litigation exception and an exception for "ascertaining the legal position" of a client.
- *Switzerland/Channel Islands Approach.* Under the approach adopted by Switzerland and the Channel Islands (i.e., Jersey, Guernsey, Gibraltar, and the Isle of Man), lawyers are subject to registration with a regulatory body, licensing, anti-money laundering compliance programs, record-keeping, and SAR requirements.

Consultation Paper Options

Other options under review, as outlined in the Consultation Paper, include the following:

- *Education.* The ABA and other professional associations throughout the world should undertake a strong role in the development of anti-money laundering education (law school classes and CLE programs) and lawyer ethical responsibilities.
- *Scope of Legal Activities.* Many FATF countries have struggled with defining what legal activities should be the subject of governmental regulation. One approach is to include all activities of lawyers within the gatekeeper requirements. Another approach is to include only those activities that the U.S. government may view as not traditionally lawyering activities (e.g., the movement of money or financial assets, opening and operating client accounts, or otherwise dealing in financial assets, property, or company matters for a client, or acting as a fiduciary).
- *Due Diligence Requirements.* Due diligence, such as customer identification and verification of bona fides and record-keeping, could be imposed on lawyers. For example, FATF Recommendation 10 states that to fulfill identification requirements concerning legal entities, "financial institutions" should, when necessary, take measures to verify the legal existence and structure of the customer by obtaining either from a public register or from the customer, or both, proof of incorporation, including information concerning the customer's name, legal form, address, directors, and provisions regulating the power to bind the entity, and to verify that any person purporting to act on behalf of the customer is so authorized and identify that person. In terms of record-keeping, lawyers could be asked to maintain, for at least five years, all necessary records on transactions, both domestic and international, to enable them to comply swiftly with information requests from the competent authorities. These records

would have to be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved if any) so as to provide, if necessary, evidence for prosecution of criminal behavior.

- *STR Requirements.* The Consultation Paper contains an option that requires lawyers to report "suspicious transactions" of clients to a government agency or a self-regulating organization (SRO). It is unclear whether a lawyer would be allowed to tip off a client that the lawyer plans to file a suspicious transaction report (STR). Presumably, an STR requirement would not be imposed if the information giving rise to the suspicion is acquired by the lawyer in the context of the "legal professional privilege" (presumably including the attorney-work product privilege) or professional secrecy.

FATF entertained comments on the Consultation Paper through August 31, 2002. Based on these comments, FATF will convene a plenary meeting in October 2002 to evaluate the comments and then make final recommendations on the options contained in the Consultation Paper. The final recommendations made by FATF may differ markedly from the descriptions above. But if the United States elects to follow the course emanating from the EU Directive, it is possible that the U.S. options will adopt these types of features. It is also unclear at this writing whether the United States will attempt to use the Act as the basis for its authority to adopt regulations implementing these options or whether the Bush Administration will seek legislative authority from Congress.

USA PATRIOT Act

Shortly after the terrorist attacks on September 11, Congress enacted the 342-page USA PATRIOT Act to "deter and punish terrorist acts in the United States and around the world [and] to enhance law enforcement investigatory tools." USA PATRIOT Act, 115 Stat. at 272. Title III of the Act, known as the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001, is aimed at combating international money laundering and the financing of terrorist organizations. Id. §§ 301-77, 115 Stat. at 296-342. Title III amends various criminal money laundering laws and certain record-keeping and reporting requirements in the Bank Secrecy Act (BSA). 31 U.S.C. §§ 5311-5355. The purpose of Title III is to make it easier to prevent, detect, and prosecute international money laundering and the financing of terrorism. USA PATRIOT Act § 302(b)(1), 115 Stat. at 297.

Of particular interest to real property lawyers is the deferral during this six-month period of regulations governing "persons involved in real estate closings and settlements."

The Treasury Department has expressed concern that existing loopholes in the money laundering regime may force terrorists and money launderers to migrate toward less traditional financial institutions that are outside the government's regulatory control. See *The Patriot Act Oversight Investigating Patterns of Terrorist Financing: Hearing Before the Subcomm. on Oversight & Investigations, House Comm. on Financial Services*, 107th Cong. (Feb. 12, 2002) (testimony of Juan C. Zarate, Deputy Assistant Secretary, Terrorism and Violent Crime, Dep't of Treasury), available at **http://financialservices.hous.gov/media/pdf/o21202ja.pdf**.

As amended by Section 352 of the Act, the BSA now requires every "financial institution" to establish an anti-money laundering program that includes the following minimal elements: (1) the development of internal policies, procedures, and controls, (2) the designation of a compliance officer, (3) an ongoing employee training program, and (4) an independent audit function to test programs. USA PATRIOT Act § 352(a), 115 Stat. at 322. The BSA's definition of "financial institution" is extremely broad. It includes institutions that are already subject to federal regulation, such as banks, savings associations, credit unions, and registered securities broker-dealers and futures commission merchants. The definition also includes "money services businesses" (e.g., currency dealers or exchangers, check cashers, issuers of traveler's checks, money orders, or stored value cards, and money transmitters); dealers in precious metals, stones, or jewels; pawnbrokers; loan or finance companies; private bankers; insurance companies; travel agencies; telegraph companies; sellers of vehicles, including automobiles, airplanes, and boats; persons engaged in real estate closings and settlements; investment bankers; investment companies; and commodity pool operators and commodity trading advisors that are registered or required to register under the Commodity Exchange Act. Financial Crimes Enforcement Networks; Anti-Money Laundering Programs for Financial Institutions, 67 Fed. Reg. 21,110-01 (Apr. 29, 2002) (to be codified at 31 C.F.R. pt. 103).

The Treasury Department issued a series of regulations in April 2002 covering many of these financial institutions. See 67 Fed. Reg. 21,110-01 (banks, savings associations, credit unions, registered brokers in securities, futures commissions dealers, and casinos); 67 Fed. Reg. 21,114-01 (money services businesses); 67 Fed. Reg. 21,117-01 (mutual funds); 67 Fed. Reg. 21,121-01 (credit card systems). But the Department announced that it was temporarily

exempting other types of financial institutions, such as the following: dealers in precious metals, stones, or jewels; pawnbrokers; loan or finance companies; private bankers; insurance companies; travel agencies; telegraph companies; businesses engaged in vehicle sales (including automobiles, airplanes, and boats); persons involved in real estate closings and settlements; investment companies other than mutual funds; and commodity pool operators and trading advisors. 67 Fed. Reg. 21,110-01. Recognizing the complexity of requiring anti-money laundering programs for these remaining financial institutions, the Treasury Department remarked that many of these types of financial institutions "are small businesses that have never been subject previously to Federal anti-money laundering regulation, and the risks inherent in their operations will vary considerably." *Treasury Department USA Patriot Act Update*, TREASURY NEWS (Apr. 23, 2002), available at **www.treas.gov/press/releases/po3034.htm**.

Of particular interest to real property lawyers is the deferral during this six-month period of regulations governing "persons involved in real estate closings and settlements." The BSA does not define or elaborate on the meaning of "persons involved in real estate closings and settlements." Presumably, this language is aimed at title insurance companies, escrow agents, and title closing attorneys, because of their involvement with the movement of large sums of money through the monetary system. At a practical level, it is unclear whether sole practitioners and title agents who serve in a real estate closing role will have the expertise, funds, or knowledge to implement and administer an effective anti-money laundering compliance program consistent with the requirements of the Act. If so, the cost of such a program will unquestionably be passed on to the consumer.

The Act does not elaborate on what is meant by a person "involved" in real estate closings and settlements. For example, are real estate brokers "involved" in real estate closings and settlements? Are title abstractors, surveyors, and appraisers "involved" in real estate closings and settlements? Until the Treasury Department issues regulations later this year, the breadth and scope of these regulations will remain unclear. Representatives of the title insurance industry, including the American Land Title Association, are working with the Treasury Department to understand the issues involved in adopting these regulatory requirements.

What Is a Lawyer to Do?

The hypothetical described at the outset of this article illustrates the nuanced challenges involved in applying the Gatekeeper Initiative and the Act's regulations to transactional real estate lawyers. Lynne, the Kansas real estate lawyer, is a sole practitioner who has limited time, staff, and resources to adopt an effective anti-money laundering compliance program. Her new clients, the Middle Eastern couple, are mere acquaintances of Lynne. Is Lynne expected to undertake a comprehensive due diligence investigation of her clients' source of funds, political and religious persuasion, and financial activities? Even if Lynne knows that her clients' funds originate in a Middle Eastern country, is she expected to make further inquiry into her client as to the bona fides of these funds or the originating financial institution? If Lynne suspects (reasonably or otherwise) that these funds are derived from criminal activities, should she have an obligation to file an STR with the appropriate governmental authority or with an SRO? In that case, should she be allowed to "tip off" her clients that she plans to file an STR? In terms of record-keeping, Lynne will be required to maintain her records for at least five years and make them available for inspection by governmental authorities.

The Gatekeeper Initiative and the newly minted regulations from the Treasury Department have the potential for having a chilling effect on the attorney-client relationship. If a client no longer has the assurance that his or her disclosures to counsel will be kept in confidence, it is unlikely that the clients will confide in counsel and thus impair counsel's ability to dissuade the client from engaging in illegal activity or to advise the client of noncriminal means to attain the client's goals.

The role of lawyers as independent professionals and their ethical obligations to serve the interests of their clients objectively run counter to the gatekeeper notion that lawyers essentially act as government agents. The Gatekeeper Initiative increases the risk that changing the fundamental role of lawyers may adversely affect the legal profession, its ethical canons, and the attorney-client relationship.

The various options under the Gatekeeper Initiative, such as the STR requirement, will entail extensive line drawing and subjective calls. The government may have a difficult time in establishing the demarcation line between purely legal activities and those activities not exclusively performed by lawyers.

Finally, the United States will likely seek to enforce the adopted options through criminal sanctions. Lawyers will thus be exposed to criminal liability without, in all cases, the benefit of clear and unambiguous regulatory requirements.

Conclusion

The horrifying events of September 11 have led to comprehensive laws and regulations designed to prevent these events from occurring again. But the quest to extinguish all forms of money laundering and terrorist financing may have the real, but unintended, consequence of severely eroding the attorney-client relationship and forever altering this relationship of trust and confidence clients place in their lawyers. ■