

# Client Alert

International Trade &amp; Litigation Practice Group

November 23, 2011

## FinCEN Proposes Rules for Government-Sponsored Enterprises To Combat Mortgage Fraud

As part of its ongoing efforts to combat mortgage fraud and other related financial crimes, on November 8, 2011, the Financial Crimes Enforcement Network (FinCEN) published in the Federal Register a **Notice of Proposed Rulemaking** (NPRM) that imposes a requirement on certain housing government-sponsored enterprises (“Housing GSEs”) to develop anti-money laundering (AML) programs and to file suspicious activity reports (SARs) with FinCEN. GSEs subject to the NPRM are the Federal National Mortgage Association (“Fannie Mae”), Federal Home Loan Mortgage Corporation (“Freddie Mac”), and the Federal Home Loan Banks. FinCEN determined that these Housing GSEs are “financial institutions” subject to the AML program and SAR reporting requirements under the Bank Secrecy Act (BSA). Comments to the NPRM must be submitted to FinCEN on or before January 9, 2012.

In the NPRM, FinCEN points out that the main role of the Housing GSEs is to support the primary mortgage market and affordable housing programs through the purchase, guarantee, and securitization of mortgage loans, as well as the extension of loans secured primarily by mortgage loans and real estate related assets. Because the Housing GSEs are involved in providing financing to the residential mortgage market, they may be exposed to the risk of fraud, particularly when investing in whole mortgage loans. In other words, while purchasing mortgage loans, extending loans secured by mortgages and other real estate-related collateral, and engaging in a variety of related financial activities, the Housing GSEs have access to information on suspected mortgage fraud and money laundering valuable to law enforcement and regulators engaged in the investigation and prosecution of mortgage fraud and other financial crimes.

### Current Reporting Requirements

The Housing GSEs are currently required to file fraud reports with their regulator, the Federal Housing Finance Agency (FHFA) established under the Federal Housing Finance Regulatory Reform Act of 2008. The FHFA, in turn, files SARs with FinCEN when the facts in a particular fraud report warrant a SAR under FinCEN’s reporting standards.

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## NPRM Requirements

Under the NPRM, Housing GSEs are required to file SAR reports and to develop and implement AML programs in compliance with BSA's requirements. FinCEN delegated authority to examine compliance by the Housing GSEs with these requirements to the FHFA, where FinCEN will work with the FHFA to coordinate and direct such delegated compliance examination activities. FinCEN continues to retain enforcement authority for the imposition of civil penalties for violations of the requirements described in the NPRM.

### *SAR Reports*

The NPRM requires the Housing GSEs to file SAR reports directly with FinCEN. Specifically, pursuant to the NPRM, the Housing GSEs are required to report suspicious transactions that are conducted or attempted by, at, or through a Housing GSE and involve or aggregate at least \$5,000 in funds or other assets, regardless of whether they involve currency. The NPRM also encourages the reporting of transactions that appear relevant to violations of law even in cases in which the NPRM does not explicitly so require (e.g., when a transaction involves less than \$5,000 in funds).

Housing GSEs are required under the NPRM to report any of the following transactions if they "know, suspect, or have reason to suspect" that the transaction (or a pattern of transactions of which the transaction is a part):

- (1) Involves funds derived from illegal activity or is intended or conducted to hide or disguise funds or assets derived from illegal activity;
- (2) Is designed, whether through structuring or other means, to evade the requirements of the BSA;
- (3) Has no business or apparent lawful purpose, and no reasonable explanation exists for the transaction after examining the available facts; or
- (4) Involves the use of the Housing GSE to facilitate criminal activity.

Within 30 days after a suspicious transaction is discovered (or within 60 days in cases where no suspect is identified), the Housing GSE must report the transaction by completing a SAR and filing it with FinCEN. Supporting documentation relating to each SAR must be collected and maintained separately by the Housing GSE for a period of five years from the date of filing, and be made available upon request by FinCEN or any Federal, State, or local law enforcement agency, or any Federal regulatory authority that examines the Housing GSE for compliance with the BSA. For situations requiring immediate attention, Housing GSEs are required to telephone the appropriate law enforcement authority in addition to filing a SAR. Importantly, SARs and information that would reveal the existence of that SAR must be kept confidential and not be disclosed, except as authorized by FinCEN. Please see our [Client Alert](#) of December 29, 2010, discussing SARs confidentiality requirements.

Furthermore, while the obligation to identify and to report a suspicious transaction rests with the Housing GSE involved in the transaction, where more than one Housing GSE (or another financial institution with a separate suspicious activity reporting obligation) is involved in the same transaction, only one report is required to be filed. This report must contain all relevant facts and each financial institution must maintain a copy of the report and any related supporting documentation.

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## *AML Programs*

Each Housing GSE is required under the NPRM to develop and implement an AML program reasonably designed to prevent the Housing GSE from being used to facilitate money laundering or the financing of terrorist activities, and other financial crimes, including mortgage fraud. The program must be in writing, approved by senior management, and must ensure that all the information necessary to make its AML program effective is obtained. The AML program must also be made available to FinCEN upon request.

An AML program must contain the following elements:

- (1) Development of internal policies, procedures, and controls based on the Housing GSE's assessment of the risks of money laundering, terrorism finance and other financial crimes associated with its products, customers, distribution channels, and geographic locations, to include means to obtain customer information on individual borrowers and retail financial institutions that are customers of the Housing GSE;
- (2) Designation of a compliance officer to be responsible for administering the AML program and to ensure that the program is implemented effectively and updated as necessary. This person should be competent and knowledgeable with respect to applicable BSA requirements and be empowered with full responsibility and authority to develop and enforce appropriate policies and procedures;
- (3) Establishment of an ongoing employee training program; and
- (4) Creation of an independent audit function to periodically test the AML program to ensure that it complies with the requirements and that it functions as designed.

Moreover, Housing GSEs may conduct some of their operations through third parties and under some circumstances, elements of the AML program may best be performed by these third parties. In these cases, the NPRM permits a Housing GSE to delegate contractually the implementation and operation of certain relevant aspects of its AML program to a third party and to rely on the compliance program of the third party, if the third party is subject to an independent AML program requirement under the BSA. Importantly, any Housing GSE that delegates responsibility for aspects of its AML program to a third party, remains fully responsible for the effectiveness of the AML program, as well as ensuring that compliance examiners are able to obtain information and records relating to the AML program.

If you have any questions regarding the NPRM, please contact Jeff Telep at +1 202 626 2390 or Jane Cohen +1 202 661 7842.

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