

**ENHANCING COMPLIANCE: A PROPOSAL OF EARB AS THE SUPERVISORY
BODY THAT REGULATES REAL ESTATE AGENTS AGAINST MONEY
LAUNDERING**

Submitted in partial fulfilment of the requirements of the Bachelor of Laws Degree, Strathmore
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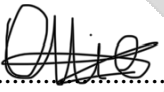
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DECLARATION

I, **KARIUKI OLIVE MURUGI**, do hereby declare that this research is my original work and that to the best of my knowledge and belief, it has not been previously, in its entirety or in part, been submitted to any other university for a degree or diploma. Other works cited or referred to are accordingly acknowledged.

Signed:

Date:30th January 2024.....



This dissertation has been submitted for examination with my approval as University Supervisor.

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Mr. Mark Mathenge

ABSTRACT

Money laundering, the process of disguising illicit proceeds as legitimate assets, remains a global challenge. This study delves into the susceptibility of Kenya's real estate sector to money laundering, despite existing regulatory frameworks. The primary objectives include assessing the degree and nature of financial crime in Kenya, scrutinizing the estate industry's role in facilitating such activities, evaluating government regulatory efforts, and proposing strategies to bolster anti-money laundering practices. In pursuit of these objectives, a doctrinal approach employing desktop research is adopted, examining legal texts and documents related to money laundering policies in the real estate industry. A documentary analysis is also employed to trace the evolution of money laundering and highlight regulatory efforts and existing gaps. Additionally, policy and institutional analyses are applied to comprehend the execution of regulations and the roles played by regulatory bodies. This research identifies critical weaknesses in Kenya's regulatory framework, including regulatory gaps between key laws, unclear compliance expectations for real estate agents, and a lack of anti-money laundering guidelines for the regulatory body. To address these issues, the study proposes key recommendations: amending legislation to address loopholes, empowering the regulatory body to enforce anti-money laundering measures, and actively collaborating with international partners such as the FATF. Implementing these measures will fortify Kenya's financial defences, safeguarding its real estate sector from further becoming a haven for laundered money.

VT OMNES VNVM SINT

LIST OF ABBREVIATIONS

Anti Money Laundering	AML
Asia/Pacific Group on Money Laundering	APG
Assets Recovery Agency	ARA
Commercial Affairs Department	CAD
Customer Due Diligence	CDD
Council for Estate Agents	CEA
Central Bank of Kenya	CBK
Corruption, Drug Trafficking, and Other Serious Crimes Act	CDSA
Directorate of Criminal Investigation	DCI
Digital Credit Providers	DCPs
Designated Non-Financial Businesses and Professions	DNFBPs
Estate Agents Registration Board of Kenya	EARB
Enhanced Due Diligence	EDD
Eastern and Southern Africa Anti-Money Laundering Group	ESAAMLG
Financial Action Task Force	FATF
Financial Intelligence Centre	FIC
Financial Intelligence Centre Act	FICA
Financial Intelligence Units	FIU
Financial Reporting Centre	FRC
Gross Domestic Product	GDP

Group of Seven	G7
Institute of Certified Public Accountants of Kenya	ICPAK
International Monetary Fund	IMF
Kenya Revenue Authority	KRA
Know Your Customer	KYC
Law Society of Kenya	LSK
Monetary Authority of Singapore	MAS
Money Laundering	ML
Organisation for Economic Co-operation and Development	OECD
Prevention of Organised Crime Act	POCA
Proceeds of Crime and Anti-Money Laundering Act	POCAMLA
Simplified Due Diligence	SDD
Suspicious Transaction Reports	STRs
Ultra-High Net Worth Individuals	UHNWI



LIST OF CASES

USA v. Alishire (2023), United States District Court District of Minnesota



LIST OF LEGAL INSTRUMENTS

Anti-Money Laundering Guidance for Legal Practitioners (2020) (Kenya)

Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill (2023)
(Kenya)

Code of Ethics & Professional Client Care for real estate agents (2010) (Singapore)

Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act (1992)
(Singapore)

Estate Agent Act (Act No. 9 of 2000) (Kenya)

Estate Agent Act (2010) (Singapore)

Estate Agency Affairs Act, (Act No 112 of 1976) (South Africa)

Financial Intelligence Act (Act No 38 of 2001) (South Africa)

Monetary Authority of Singapore Act (MAS Notice 626 of 2015) (Singapore)

Monetary Authority of Singapore Act (MAS Notice 1014 of 2015) (Singapore)

Monetary Authority of Singapore Act (MAS Notice SFA03AA-N01) (Singapore)

Proceeds of Crime and Ant-Money Laundering Act (No. 51 of 2012) (Kenya)

Prevention of Terrorism Act (Act No. 30 of 2012) (Ke

CHAPTER ONE

INTRODUCTION

1.1 Background

Money laundering (ML) is the process of converting criminal proceeds into money or other assets that appear to be legitimate.¹ This entails moving illicit funds through formal and institutional channels to conceal its source and subsequently derive benefit from the illegal funds.²

At the height of money laundering activity in 1989, the Financial Action Task Force, (hereafter FATF) an inter body, was established to globally investigate money laundering and assess the efficacy of previous preventive measures in place to curtail money laundering activities in different countries.³ In 1990, the FATF issued its first set of recommendations which have since been amended, to effectively curb money laundering threats in banking and financial institutions, having determined that these were the areas primarily affected.⁴ Kenya is subject to these recommendations as a member of the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), a group dedicated to combating money laundering through ensuring compliance and enforcement with the FATF recommendations in African countries.⁵

The Proceeds of Crime and Anti-Money Laundering Act was passed in 2009 in response to the FATF's recommendations.⁶ The purpose of the Act was to provide for the offence of money laundering and to implement measures to combat the offence, as well as to provide for the identification, tracing, freezing, seizure, and confiscation of criminal proceeds, and for connected purposes.⁷ The POCAMLA established the Financial Reporting Centre (FRC) in

¹United States Department of the Treasury Financial Crimes Enforcement Network, The FinCEN Advisory Report, 1996, 2.

² The Organization for Economic Cooperation and Development, *Illicit Financial Flows from Developing Countries*, 2014, 16.

³ – <https://www.fatf-gafi.org/about/historyofthefatf/> 1 March 2022.

⁴ The Financial Action Task Force, *International Standards on Combating Money Laundering and The Terrorism Financing & Proliferation*, 2012, 10-31.

⁵ – <https://www.fatf-gafi.org/en/countries/global-network/eastern-and-southern-africa-anti-money-laundering-group-esaamlg.html> 1 March 2022.

⁶The Financial Action Task Force, *International Standards on Combating Money Laundering and The Terrorism Financing & Proliferation*, 2012, 22-28.

⁷ *Proceeds of Crime and Anti-Money Laundering Act* (Act No. 51 of 2012).

accordance with FATF recommendations, with the primary goal of assisting in the identification of illegitimate funds, combating money laundering, and terrorism financing.⁸

Under the POCAMLA, the FRC has established reporting institutions that include financial institutions such as banks and Designated Non-Financial Businesses and Professions (DNFBPs) and Professions such as casinos (including internet casinos), real estate agents, dealers in precious stones and metals, lawyers, accountants and trust and company service providers.⁹ These institutions are required to implement anti-money laundering measures, register with the FRC and submit specified transaction reports.¹⁰ To ensure that institutions subject to regulation are carrying out their anti-money laundering obligations, reporting organisations that are a part of a regulated sector work closely with the FRC while those that are unregulated report directly to the FRC.¹¹ The Law Society of Kenya (LSK) for lawyers and the Institute of Certified Public Accountants of Kenya (ICPAK) for accountants are suitable examples of such reporting organisations that fittingly act as regulatory bodies by exercising their supervisory mandate.¹²

The real estate sector is a prevalent investment area in Kenya as it brings in a sizable amount of money to the nation's capital¹³ However, ESAAMLG has identified the real estate sector as Kenya's most vulnerable area to money laundering and has attributed this to poor regulation.¹⁴ The real estate agency has been established under the estate agents act consequently deriving its mandate from the act.¹⁵ The estate agents act provides that the functions of the regulatory body, Estate Agents Registration Board of Kenya (EARB) is that of an oversight authority with relation to the conduct and practice of real estate agents in Kenya. However, there is no mention of its capacity and mandate to undertake anti money laundering functions in the Estate Agents Act in accordance with its supervisory authority as per the FRC's regulations and in the POCAMLA.¹⁶

⁸ Section 21, *Proceeds of Crime and Anti-Money Laundering Act* (Act No. 51 of 2012).

⁹ Section 2, *Proceeds of Crime and Anti-Money Laundering Act* (Act No. 51 of 2012).

¹⁰ Financial Reporting Centre, *Guidance on Registration of Reporting Institutions with The Financial Reporting Centre*, 2021,6.

¹¹ National Risk Assessment, *The National Money Laundering and Terrorism Financing Risks Assessment Report*,2021,115.

¹² Financial Reporting Centre, *Guidance on Registration of Reporting Institutions with The Financial Reporting Centre*, 2021,12.

¹³ Kenya Mortgage Refinance Company, *Research Insights report on housing*, <https://kmrc.co.ke/wp-content/uploads/2022/07/Research-Insights-report-on-housing-June-2022_issue-1-Summary.pdf> on June 2022

¹⁴ Eastern and Southern Africa Anti-Money Laundering Group, *Mutual Evaluation Report of Kenya*,2022, 32-33.

¹⁵ Section 4, *Estate Agents Act* (Act No. No. 9 of 2000).

¹⁶ Section 4, *Estate Agents Act* (Act No. No. 9 of 2000).

Additionally, under the Estate Agents Act, registration is not contingent on a real estate agent's adherence to the FRC reporting rules.¹⁷ Furthermore, money laundering is not listed as a misconduct in the Estate Agents Act,¹⁸ neither are there penalties for money laundering for real estate agents in the act. The POCAMLA, however, imposes fines on any professional found to be violating the anti-money laundering guidelines with no backing from the EARB when it comes to the Estate Agent Act for real estate agents.¹⁹ This state of affairs is in stark contrast with the actions of other regulatory bodies who are in equal danger of money laundering,²⁰ and yet, in playing its role of self-regulation, LSK has passed anti-money laundering guidelines exclusive to legal practitioners that has provided for reporting duties.²¹ Further, anti-money laundering (AML) guidelines in relation to accountants have been provided for under the POCAMLA.²²

1.2 Problem Statement

The real estate sector in Kenya is highly prone to money laundering, despite the existence of the POCAMLA and the oversight mechanisms of the FRC. The core issue lies in the lack of enforcement of AML policies specifically targeting real estate agents, as overseen by the EARB. This gap raises concerns about the efficacy of current measures in curbing money laundering within the real estate industry.

This issue negatively impacts individuals involved in real estate transactions, potentially exposing them to illicit financial activities. Addressing this problem is crucial not only for the protection of stakeholders in the real estate industry but also for the overall credibility of Kenya's financial system. The significance of this problem is underscored by the need to align the regulatory framework with international standards, as failure to do so may not only tarnish Kenya's reputation in the global fight against financial crime but also render the real estate industry vulnerable to abuse by criminal entities seeking to legitimize illicit funds through property transactions.

¹⁷ Section 13, *Estate Agents Act* (Act No. No. 9 of 2000).

¹⁸ Section 22, *Estate Agents Act* (Act No. No. 9 of 2000).

¹⁹ Section 16, *Proceeds of Crime and Anti-Money Laundering Act* (Act No. 51 of 2012).

²⁰ Eastern and Southern Africa Anti-Money Laundering Group, *Mutual Evaluation Report of Kenya*, 2022, 39.

²¹ The law society of Kenya, *Anti-Money Laundering Guidance for Legal Practitioners*, 2020.

²²Section 48, *Proceeds of Crime and Anti-Money Laundering Act* (Act No. 51 of 2012).

1.3 Research Objectives

1. To evaluate the issue of money laundering in Kenya.
2. To examine the role of the real estate industry as a facilitator of money laundering and identify the contributing factors that lead to negative implications on the country's overall economy.
3. To assess the government's regulatory efforts in the real estate industry to prevent money laundering in Kenya, along with any gaps that have developed.
4. To assess and propose strategies for integrating anti-money laundering practices from South Africa and Singapore into Kenya's regulatory framework, with the aim of mitigating money laundering risks in the real estate industry.

1.4 Research Questions

1. What is the extent and nature of the issue of money laundering in Kenya?
2. How is the real -estate industry a facilitator of money laundering and what factors act as a catalyst leading to negative implications in the country's overall economy?
3. What initiatives have been put in place by the government to prevent money laundering in Kenya's the real estate sector, and what gaps have emerged?
4. How can anti money laundering practices in South Africa and Singapore be employed to address deficiencies in Kenya's regulatory framework and mitigate the risk of money laundering within the real estate sector?

1.5 Hypothesis

Assigning the Estate Agents Registration Board of Kenya, the responsibility of overseeing adherence to anti-money laundering guidelines and enforcing compliance with reporting obligations to the Financial Reporting Centre, will contribute to the mitigation of money laundering within the real estate industry.

1.6 Justification

The estate industry has long been known to be prone to money laundering however; it has now gradually worked its way up to being one of the most vulnerable sectors to this offence in Kenya.²³ Large quantities of money are exchanged in real estate transactions however, they are not as rigorously overseen as they are in other industries when it comes to the possibility of money laundering.²⁴ The EARB has disregarded the regulatory function assigned to it by the FRC in accordance with the POCAMLA. This lack of regulation provides a loophole that allows money launderers to operate covertly, allowing them to exploit this industry.

This study will therefore be useful to lawmakers tasked with developing and improving existing anti-money laundering laws that are particularly relevant to the real estate industry. Furthermore, this research seeks to fill the regulatory vacuum in real estate by assisting researchers and scholars who study and write on money laundering and its regulatory aspect. The FRC also stands to benefit from this research as this study can assist in enhancing existing AML policies and procedures, particularly those pertaining to reporting and regulation of real estate agents.

1.7 Theoretical framework: Public Interest Theory of Regulation

This is primarily an economic theory that provides for the implementation of policies to facilitate efficient government intervention in the market to achieve the well-being of the public.²⁵ In discussing this theory, Cecil Pigou provides that markets are often ineffective and unsuccessful because of lack of regulation. He contends that a government that contributes to preserving the highest level of social welfare, works to protect its citizens from these shortcomings through regulation²⁶ since they have adequate information and power to do so.²⁷ Therefore, this theory

²³ Rudich D, The Sentry, 'Kenya Illicit Finance Risks and Assessment,' October 2021, 7-9,24.

²⁴ Warutere P, 'Detecting and investigating money laundering in Kenya' Institute for Security Studies, 2006,4.

²⁵ Adams B and Tower G, 'Theories of Regulation: Some Reflections on the Statutory Supervision of Insurance Companies in Anglo-American Countries' 19 *The Geneva Papers on Risk and Insurance. Issues and Practice* 71,1994,163.

²⁶ Pigou CA, *The Economics of Welfare*, 4th ed, Macmillan and Co. Limited, London, 1932, 231-235.

²⁷ Hertog J, 'Review of Economic Theories Of Regulation', Tjalling C. Koopmans Research Institute, Discussion Paper Series 10-18,2010, 2—<https://www.uu.nl/sites/default/files/rebo_use_dp_2010_10-18.pdf> on 1 March 2022.

establishes that regulation is provided in response to the public's need to address ineffective and unfair market practices that are necessitated by inadequate regulation.²⁸

Posner's work supports the idea that free-floating economic markets frequently experience fragility and perform inefficiently, failing to serve the public's interests.²⁹ Inefficient running that leads to bad performance in the market is referred to as market failure,³⁰ that is attributed to the weaknesses in the bodies that facilitate regulation or the procedures that are put in place to enable regulation.³¹ Thus, the free-floating and perfunctory nature of Kenya's real estate industry renders it prone to money laundering, which results in significant losses that have an impact on the economy of the nation.³² The theory proposes that in sectors prone to significant economic losses, a higher degree of regulation leads to a decrease in the welfare losses incurred.³³

In addressing the imperfection of markets that arises when markets are left to their own devices, this theory suggests that if regulation in the real estate industry were to be implemented, the losses resulting from financial crime would be significantly reduced.³⁴ Additionally, Goldberg argues that studies have proven that the costs incurred by the government in implementing regulation of economic markets, are significantly lower than the harm that is endured in unregulated industries.³⁵ This is also supported by the idea that government regulation does not incur any monetary costs³⁶ although some scholars strongly disagree with this view given that government resources must be employed to enable regulation.³⁷ Taking the above into account, regulating the current real estate industry that is riddled with financial crime would incur costs that are insignificant compared to the losses the economy generates due to money laundering.

²⁸ Hantke DM, 'The Public Interest Theory of Regulation: Non-Existence or Misinterpretation' 15 *European Journal of Law and Economics* 1, 2003, 166.

²⁹ Posner RA, 'Theories of Economic Regulation' 5 *The Bell Journal of Economics and Management Science* 2, 1974, 336.

³⁰ Clutton BP, Massara P and Kelly J, 'Assessment of Market Failures and Rationale for Intervention' American Economic Association, 2019, 10.

³¹ Posner RA, 'Theories of Economic Regulation,' 337.

³² Rudich D, The Sentry, 'Kenya Illicit Finance Risks and Assessment,' October 2021, 11.

³³ Hertog J, 'Review of Economic Theories of Regulation,' 6.

³⁴ Hertog J, 'Review of Economic Theories of Regulation,' 7.

³⁵ Goldberg V, 'Regulation and Administered Contracts' 7 *The Bell Journal of Economics* 2, 1976, 431-433.

³⁶ Posner RA, 'Theories of Economic Regulation,' 336.

³⁷ Guasch JL and Hahn RW, 'The Costs and Benefits of Regulation: Implications for Developing Countries' 14 *The World Bank Research Observer* 1, 1999, 141-143.

In the context of this study, the EARB has the authority to regulate the real estate sector and mandate that estate agents aid in curtailing money laundering operations by submitting required reports to the Financial Reporting Centre. The EARB, however, does not exercise its functions which results into what is described above as market failure. The country suffers from economic recession brought on by the introduction of illegitimate funds into its economic system, as well as the legal consequences arising from financial crime and its impact on the legal system.³⁸ In order to counter the factors that promote money laundering, regulation should be provided by the EARB to serve the demand from the public to address these inadequacies.

1.8 Literature Review

Researchers contend that money laundering is rampant in Kenya's estate industry as a result of weak regulations in various parts of the industry.³⁹ This viewpoint is also examined in Ssekubwa's work, where he addresses this regulation in terms of the need for a regulatory framework that governs current land laws and property transactions as prescribed by the land legislation in Kenya.⁴⁰ He goes on to discuss the importance of non-financial players in property transactions and the importance of regulating this group. Further, he argues that loopholes in land legislation in Kenya as well as the failure to reconcile these laws with the POCAMLA and other anti-money laundering legislation, impair the real estate industry by rendering it susceptible to financial crime.⁴¹

1.8.1 On money laundering in the real estate sector

The ongoing academic literature shows a unanimous agreement among scholars that the estate sector is highly prone to money laundering.⁴² According to an assessment by FATF, this

³⁸ Barako D, Brown A, 'Evaluating Anti-Money Laundering Initiatives: A Country Perspective' 9 *Evaluation Journal of Australasia* 2, 2009, 17.

³⁹ Gikonyo C, 'Detection mechanisms under Kenya's anti-money laundering regime: omissions and loopholes' 21 *Journal of Money Laundering control* 1, 2019, 64-66.

⁴⁰ Ssekubwa R, 'Money Laundering and Real Estate Sector in Kenya: Towards Robust Regulation of Land laws' Unpublished LLM Thesis, Strathmore University, Nairobi, 2022, 26-29.

⁴¹ Ssekubwa R, 'Money Laundering and Real Estate Sector in Kenya: Towards Robust Regulation of Land laws' Unpublished LLM Thesis, Strathmore University, Nairobi, 2022, 76-81

⁴² Unger B and Ferwerda J, *Money Laundering in the Real Estate Sector: Suspicious Properties*, 2nd Ed, Edward Elgar Publishing, Netherlands, 2011, 21-23. See also, Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya, 2022, 32.

vulnerability primarily stems from the non-uniformity in property prices since different properties in different areas are valued and appreciate differently.⁴³ As a result, money laundering in this sector becomes difficult to detect, as the fluctuation allows for the manipulation of property prices by undervaluing or overvaluing them.⁴⁴

Schneider, in his study, attributes this vulnerability to the fact that the real estate sector not only advances money laundering, but also acts as a facilitator to other money laundering acts.⁴⁵ He employs the illustration of a house purchased with illicit funds that allows the criminal to conduct illegal business in the property, such as drug sales.⁴⁶ In this way, by acting as a conveyance, financial crime is carried out twice through the real estate sector.⁴⁷ Jojarth therefore argues that the above is the reason why individuals involved in financial crime initiate the money laundering process by buying properties as it can easily be disguised by rental income along with renovations and improvement to the property all while carrying out illegal business.⁴⁸

As established above, money laundering in the real estate industry can be easily concealed. To counter this, Unger and Ferwerda narrowed down twenty-five distinct identifications of real estate properties based on the Dutch property market, which potentially make this industry susceptible to money laundering.⁴⁹ Their research identifies that the characteristics that result in greater economic ramifications substantially stack up against those that do not. Nevertheless, their study provides that a property that exhibits more characteristics despite the kind of consequence, is more vulnerable to financial crime.⁵⁰

Furthermore, the Organization for Economic Cooperation and Development (OECD) identified features that predominantly cater to financial institutions and are to be used to determine whether

⁴³ Financial Action Task Force, Money Laundering & Terrorist Financing Through the Real Estate Sector, 29 June 2007,17,21-25.

⁴⁴ Australian Transaction Reports and Analysis Centre, Strategic Analysis Brief: Money Laundering Through Real Estate, June 2015, 8.

⁴⁵ Schneider S, 'Organized crime, money laundering, and the real estate market' 21 *Journal of Property Research* 2, 2004, 100-101.

⁴⁶ Schneider S, 'Organized crime, money laundering, and the real estate market,'102.

⁴⁷ Financial Crimes Enforcement Network, Money Laundering in The Commercial Real Estate Industry: An Assessment Based Upon Suspicious Activity Report Filing Analysis, December 2006, 12,14.

⁴⁸ Jojarth C, 'Money Laundering: Motives, Methods, Impact, and Countermeasures' in Staiano F (ed), *Transnational Organized Crime: Challenging International Law Principles on State Jurisdiction*, Edward Elgar Publishing, Northampton, 2022, 21.

⁴⁹ Unger B and Ferwerda J, Money Laundering in the Real Estate Sector: Suspicious Properties, 17-19,47-63.

⁵⁰ Unger B and Ferwerda J, Money Laundering in the Real Estate Sector: Suspicious Properties,63.

money laundering is being carried out in these institutions.⁵¹In supplementing the findings of this report, Remeur developed specific tests that are applicable to real estate, that include looking out for customers that use third parties to conceal ownership and the use of sham companies and company frameworks that allow the owner to act anonymously, as well as other tests that apply to financial institutions.⁵²

Individuals are finding it increasingly difficult to acquire property as a result of money laundering.⁵³ In Sundarakani findings, the rising property prices in Kenya make it hard for middle-income households to buy homes and afford to stay in hotels and residences built with earnings from financial crime.⁵⁴ According to the Sentry Foundation, foreigners are mostly responsible for financial crime in the real estate market, particularly in Kenya, as they attempt to conceal unexplained income from anti-money laundering regulators in their home country.⁵⁵ Kenya provides a safe haven for these individuals since despite being suspected and their properties flagged for money laundering, no penalties have followed.⁵⁶ Even when Kenya seeks to limit foreign influence in various Kenyan industries, it does so for reasons other than preventing money laundering.⁵⁷

Bak investigates the consequences of illegal financial flows from the real estate sector on the economy, focusing on the four key ways in which illicit monies are distributed. Initially, proceeds from crime or corruption are utilised to meet the necessities of the immediate family.⁵⁸Subsequently, this money is often spent on unnecessary expenditures such as high luxury items. Third, illegal cash is invested in commercial enterprises, most prominently in real estate⁵⁹ that

⁵¹ Organisation For Economic Co-Operation and Development, Report on Tax Fraud and Money Laundering Vulnerabilities Involving the Real Estate Sector, March 2008, 7-9.

⁵² Remeur C, 'Understanding money laundering through real estate transactions,' European Parliamentary Research Service , 2019, 3.

⁵³ Schneider F, 'Turnover of organized crime and money laundering: some preliminary empirical findings' 144 *Economic Policy and Public Choice Journal* 3, 2010,477.

⁵⁴ Sundarakani S, 'Money Laundering in Real Estate Sector—Effects and Implications' in Banerjee P, Kumar A, Madhukar V (eds) *Global Performance Challenges Building and Sustaining Competitiveness*, 1st ed, Excel India Publishers, New Delhi, 2016, 62-69.

⁵⁵ The Sentry, East Africa's Leverage for Peace: Target Real Estate in Kenya and Uganda Connected to South Sudan's Spoilers, June 2018, 2-4.

⁵⁶ Warutere P, 'Detecting and Investigating Money Laundering in Kenya,'3.

⁵⁷Partnership for African Social and Governance Research, *Illicit Financial Flows in Kenya: Mapping of the Literature and Synthesis of the Evidence*, August 2018,9,14-16.

⁵⁸ Bak M, 'Illicit financial flows and inequality' *Transparency International* ,2020,9.

⁵⁹ Bak M, 'Illicit financial flows and inequality,' 2020,10.

finally leads to laundered money exiting the financial system as an outflow, having a ripple effect on the economy's Gross Domestic Product (GDP).⁶⁰

1.8.2 On anti money laundering approaches in the real estate sector

The efficacy of AML rules determines expenses incurred by criminals carrying out ML. The higher the efficacy of the policies, the more expensive the activity of money laundering will be for criminals and as such, acts as a deterrence.⁶¹ Mascriando also expresses this viewpoint in his work where he claims that when policy makers acknowledge the costs of financial crime and the deficits to the country's economy, they are bound to increase regulation and the level of legal action taken which leads to a decline in the degree of ML tolerance inside a country.⁶² According to an analysis by the International Monetary Fund (IMF), legislators' acceptance has a minimal influence on AML guidelines. What considerably impacts the success of these laws' execution, however, is the country's development level.⁶³ A highly developed country is more suited and economically capable of developing and efficiently enforcing anti-money laundering standards.⁶⁴

The FATF in their recommendations set a framework to serve as AML guidelines in the real estate sector, these comprise of inclusion of financial intelligence units (FIU), reports of STRs, and customer due diligence mechanisms that require confirmation of the client's and the recipient identities, as well as monitoring their business.⁶⁵

FATF in their report, also investigated the FIU's role in enforcing anti-money laundering policies as well as their effectiveness in this operation.⁶⁶ They concluded that the key operative nature of the FIU that majors on the number of reports disclosed,⁶⁷ is not a suitable statistic since a rise in

⁶⁰ Dugato M, Favarin S, 'the Risks and Rewards of Organized Crime Investments in Real Estate' 55 *The British Journal of Criminology* 5, 2015, 948-949.

⁶¹ Ferwerda J, 'The Economics of Crime and Money Laundering: Does Anti-Money Laundering Policy Reduce Crime?' 5 *Review of Law and Economics* 2, 2009, 907-908.

⁶² Mascriando D, 'Money Laundering: The Economics of Regulation' 7 *European Journal of Law and Economics* 1, 1999, 226.

⁶³ International Monetary Fund, Anti-Money Laundering/Combating the Financing of Terrorism: The Fund's involvement in AML/CFT, June 2003, 2.

⁶⁴ Shehu A, 'Promoting financial inclusion for effective anti-money laundering and counter financing of terrorism' *Crime Law Soc Change*, 2012, 305-307.

⁶⁵ The Financial Action Task Force, International Standards on Combating Money Laundering and The Terrorism Financing & Proliferation, 2012, 11-13,26-29.

⁶⁶ Project 'ECOLEF' The Economic and Legal Effectiveness of Anti money Laundering and Combating Terrorist Financing Policy , Final report, 2013, 112-125.

⁶⁷ International Monetary Fund, Financial Intelligence Units: An Overview, 23 July 2004,59-62.

the number of reports does not always imply improved money laundering standards.⁶⁸ More commonly, it overloads the FIU with poor information, resulting in a decline in efficacy.⁶⁹ Maloney, Somerville and Unger in agreement with the above contend that regulatory responses to money laundering is the most proper way to prevent this practice and Canada's ineffectiveness in preventing and detecting this crime is attributed to the preference of FIUs over the regulatory framework.⁷⁰

1.8.3 On regulation of money laundering in the estate market

Regulation can be done on two fronts, as proposed by the FATF. They include a risk-based approach known as de-risking, which is mostly done in financial institutions, and making sure reporting requirements are met in other industries.⁷¹ De-risking requires industries and financial institutions to identify high-risk clients, find ways to mitigate the risks, and if that proves challenging, must terminate the relationship.

There is no consensus in the present academic literature about the exact features that define high risk clients, However when performing due diligence, a three-pronged test has been developed to help institutions distinguish high risk clients.⁷² They are consumers related to higher-risk nations or business sectors that are prone to money laundering, customers that have complicated beneficial ownership arrangements in real estate and those who have peculiar anonymous transactions that lack economic benefits.⁷³

To guarantee that concerned businesses can quickly identify the high risk customers and so, prevent money laundering, Johannes suggests that effective de-risking regulation should be focused on the initial phase of money laundering, the placement stage, where the illicit monies are brought into the financial system.⁷⁴ De-risking has however been criticised by a number of different academics as an ineffective regulatory strategy because, in their view, it drives high-risk clients into less regulated industries and thus does not address the issue at hand.⁷⁵

⁶⁸ Project 'ECOLEF' The Economic and Legal Effectiveness of Anti money Laundering and Combating Terrorist Financing Policy, Final report, 2013, 118-121.

⁶⁹ Takáts E, 'A Theory of "Crying Wolf": The Economics of Money Laundering Enforcement' 27 *Journal of Law, Economics, & Organization* 1, 2011, 34.

⁷⁰ Maloney M, Somerville T, Unger B, Combating Money Laundering in BC Real Estate, 31 March 2019, 2,14-16.

⁷¹ Financial Action Task Force, Drivers for "de-risking" go beyond anti-money laundering / terrorist financing, 2015, 26.

⁷² Joshi M, 'Classification of High-Risk Customers' India forensic Network, 2020, 4.

⁷³ Financial Crime Guide, A firm's guide to countering financial crime risks, Feb 2023, 14-16.

Alternatively, others argue that it prevents financial institutions from expanding because the loss of clients caused by this perceived risk stunts their expansion.⁷⁶

Muragura argues that the most effective way to stop this crime is through stringent AML regulations especially those that deal with record keeping and reporting STRs.⁷⁷ Reporting was evaluated as one of the elements in research by Subbotina aimed at determining if local AML in Russia were compatible with international standards. She discovered that reporting suspicious transaction is a suitable method for preventing money laundering in Russia.⁷⁸ Jensen and Cheong studied compliance with adoption and implementation of FATF guidelines in developing nations in Asia. The findings show that nations that achieved great strides in the fight against financial crime implemented the FATF reporting requirements.⁷⁹

1.8.4 Contribution

Scholars unanimously maintain the position that money laundering is widespread in the real estate industry. The ongoing academic literature in attempting to find out why this is the case, has done so by attributing this prevalence to the weak regulatory framework in Kenya's real estate industry. This research agrees with the above discourse however, a keener look at the specific regulatory aspect that creates this gap is yet to be adequately provided. Ssekubwa has, to some extent, explored the regulatory aspect however, he did so by looking at Kenya's current land laws, and has attributed the frequency of ML in real estate to the absence of these laws' regulation. My study would therefore be a unique contribution to the real estate sector industry as it proposes that, the EARB be mandated to be the supervisory authority that ensures compliance of the estate agents with reporting obligations and in this way, leads to a more rigorous regulatory framework in the real estate industry. Additionally, this study supplements the existing literature on real estate and

⁷⁴ Council of Europe, "De-Risking" Within Moneyval States and Territories, 15 April 2015, 5.

⁷⁵ Council of Europe, "De-Risking" Within Moneyval States and Territories, 15 April 2015, 7.

⁷⁶ Durner T, Shetret T, 'Understanding Bank De Risking and Its Effects on Financial Inclusion' Global Centre on Cooperative Security, 2015, 19.

⁷⁷ Muragura N, 'The institutional framework against money laundering and its underlying predicate crimes' 19 *Journal of Financial Regulation and Compliance* 2, 2011, 174-194.

⁷⁸ Subbotina N, 'Development of anti-money laundering regime in Russia' 11 *Journal of Money Laundering Control* 4, 2008, 358-370.

⁷⁹ Jensen T and Cheong L, 'Combating money laundering in transition countries: the inherent limitations and practical issues' 13 *Journal of Money Laundering Control* 3, 2010, 215-225.

money laundering in Kenya by offering a fresh perspective that links the regulatory gap to the absence of a compliance authority.

1.9 Methodology

The research in this study will take a doctrinal approach by employing desktop research. This approach is suitable for a study on AML policies in the estate market as it includes an examination of statutes, regulations, and legal principles in finding gaps in existing money laundering policies in the real estate industry as well as a critical review of various laws on the subject. Desktop research in this study will involve the analysis of legal texts and documents consisting of a comprehensive review of legislation such as the POCAMLA, the Estate Agents Act, and relevant subsidiary legislation. This will be carried out by accessing and analysing these legal texts, utilizing digital databases, legal repositories, and official government websites.

This study follows a deductive method as I intend to adequately verify the set hypothesis by addressing the research questions as listed in section 1.4.

To conduct the proposed research, I will employ a historical analysis to examine the development of money laundering and the elements that have contributed to its growth in chapter two. Additionally, a documentary analysis will be employed as I intend to look at documents such as the report and recommendations by the FATF as well as examining the academic literature and other reports to determine the gaps, negative repercussions of money laundering and their role in prompting the establishment of AML legislation.

In the third chapter, this research will then apply policy analysis to examine how the government has employed the existing legislation to combat this crime, as well as its execution to prevent financial crime. Further, this study will use an institutional analysis to examine the role and efforts of the FRC and other organisations designated to function as regulatory bodies.

1.10 Chapter Breakdown

1.10.1 Introduction

Chapter one will form the introductory part of the study and sets the foundation for subsequent chapters. It discusses significant parts of the study such as the background, problem statement,

research objectives, theoretical framework, and the justification of the study, methodology and approach as well as the chapter breakdown of this dissertation.

1.10.2 The Link Between the Real Estate Industry and Money Laundering: Catalysts and Economic Implications

The second chapter will examine the ML process in the context of the real estate sector. By doing so, the chapter also aims to examine the factors that contribute to this practice, as well as the resulting economic implications on the country's economy.

1.10.3 Assessing Government Regulations and Gaps in Money Laundering Prevention in Kenya's Real Estate

This chapter lays the groundwork for the subsequent chapter since it assesses the government's efforts to curtail money laundering in the estate industry. In looking at the efforts, this chapter will also look at the bodies tasked with curbing money laundering, their roles, and their efforts in curbing money laundering, as well as any gaps that are still present and overlooked by these bodies.

1.10.4 Enhancing Anti-Money Laundering Practices in Kenya's Real Estate: Insights from Singapore and South Africa

Chapter four will then focus on addressing identified gaps in Kenya's AML regime by conducting a comparative analysis with successful AML strategies employed by Singapore and South Africa. This analysis will extend to an assessment of these AML practices in Singapore and South Africa against FATF recommendations through an examination of institutional and legislative frameworks as well as pertinent legal cases.

1.10.5 Findings, Recommendations and Conclusion

Chapter five will conclude the study and will conclude by presenting the findings of the study as well as provide recommendations on how the mandated regulatory body may appropriately conduct its regulatory obligations to fight money laundering in the estate market in accordance with the Financial Reporting Centre's guidelines.

CHAPTER TWO

THE LINK BETWEEN THE REAL ESTATE INDUSTRY AND MONEY LAUNDERING: CATALYSTS AND ECONOMIC IMPLICATIONS

2.1 Introduction

The grey list created by the FATF comprises of countries identified as having deficient anti-money laundering measures, hence requiring close supervision. In 2010, Kenya found itself on the FATF's grey list however, a subsequent review of Kenya's progress by the FATF during a June 2014 meeting in Paris revealed the implementation of previously neglected legal frameworks, prompting the removal of Kenya from the list.⁸⁰ Within the same year, Knight Frank in their Wealth of Nations report, a study dedicated to reporting fast rising real estate sectors across the globe, highlighted Nairobi as the only African city among the top 25 global cities purportedly harbouring Ultra High Net Worth Individuals (UHNWI).⁸¹ Presently, data collected for the 2023 Wealth of Nations report indicate a prospective 53% surge in the global count of individuals possessing \$30 million or more in assets by 2023, with 74% of this escalation attributed to Kenya's real estate.⁸² In the conclusive 2023 Wealth of Nations report, Kenya, following South Africa, secured the second position among African nations experiencing an upswing in UHNWI numbers.⁸³

While this could be indicative of the nation's expanding economy, an advisory by The Sentry Foundation, characterized the Nairobi real estate market to be at its prime regarding money laundering activities.⁸⁴ Moreover, in 2014, the Global Financial Integrity emphasized that illicit inflows of money into Kenya constituted 8% of the nation's overall economic output⁸⁵, posing a significant risk to Kenya's position as a regional financial hub.⁸⁶ This risk was affirmed by the

⁸⁰ —< <https://www.fatf-gafi.org/en/countries/black-and-grey-lists.html>> on October 2023

⁸¹ Knight Frank, The Wealth Report, 2014, 11.

⁸² Jeremy Hurst, The Knight Frank 2014 Wealth Report released, International Realty Group, 2014, 1.

⁸³ Knight Frank, The Wealth Report, 2023, 33.

⁸⁴ The Sentry Foundation, Looted Funds Used to Buy African Real Estate, July 2020, 4.

⁸⁵ Global Financial Integrity, Illicit Financial Flows: The Most Damaging Economic Condition Facing the Developing World, September 2015, 140.

⁸⁶ —< <http://www.parliament.go.ke/node/20600>> on October 2023

National Risks Assessment Report, which employed the World Assessment Tool and categorized money laundering within the Kenya's estate industry as high-risk.⁸⁷ The increase in the presence of UHNWI in Kenya more so, the real estate industry, as outlined in various reports, can thus be seen to be linked to the prevalence of financial crime within this sector.⁸⁸

Given this context, this chapter discusses sectors within the real estate industry that function as channels for money laundering. Additionally, it closely analyses the factors contributing to an environment conducive to this practice, and the negative consequences in the country's economic landscape.

2.2 The money laundering process in the estate industry.

2.2.1 The placement stage.

Within the complex process of money laundering, there are three primary stages that make up the process with the initial phase being placement. This involves taking illegally acquired money from either another country or an illegitimate source within the same country to the financial system of the jurisdiction where the money laundering activities are conducted and thus makes it easily transferable within that country.⁸⁹ Given that the funds are integrated into the financial system, the principal actors in this stage are financial institutions which are strategically utilized by money launderers who employ the technique commonly known as 'smurfing.'⁹⁰ The Asset Recovery Agency, through the Kenyan Revenue Authority, has established a threshold of ten thousand US dollars. Crossing this threshold necessitates the mandatory declaration of currency or monetary instruments at customs.⁹¹ Smurfing has therefore emerged as a tactic employed by money launderers as it involves the subdivision of substantial sums into quantities below the stipulated limit of ten thousand US dollars, for deposit.

⁸⁷ National Risk Assessment, The National Money Laundering and Terrorism Financing Risks Assessment Report, 2021, 20.

⁸⁸ Dawson S, Migiro K, 'Nairobi throbs to the beat of dirty money' Thomson Reuters Foundation News Centre, 10 December 2013 – <https://news.trust.org/item/20131209150854-1kirf> on 29th October 2023.

⁸⁹ Dixon P, 'The Elusive Placement Stage of Money Laundering Explained' Sanctions.io, 2023, 3.

⁹⁰ Organization for Economic Cooperation and Development, Money Laundering and Terrorist Financing Awareness Handbook for Tax Examiners and Tax Auditors, 10 June 2019, 53-55

⁹¹ –< <https://kra.go.ke/helping-tax-payers/faqs/customs-and-border-control> > on October 2023

This strategy enables the introduction of funds into the jurisdiction and subsequent integration into the financial institutions without the requirement of formal declaration.⁹²

The second method of placement takes an indirect route, avoiding the introduction of cash directly into the financial system. Instead, it involves the subtle infiltration of illicit funds into the system through alternative channels, such as converting laundered money into diverse assets, often facilitated by a legal person.⁹³ Within the real estate sector, criminals exploit this stage using the indirect placement method by utilizing illicit funds to acquire or get mortgages for these properties through corporations thus obtaining assets. Subsequently, the acquired properties are sold, whether at a profit or loss, with the primary objective being the cleansing of the money rather than seeking financial gain. Through this method, the illicit funds are effectively integrated into the system while avoiding the scrutiny that would arise from direct placement of funds within the financial system.⁹⁴

Ordinarily, purchasing property in other countries purely in cash would trigger attention from regulators and thus the secondary placement stage, as discussed above in the context of the estate industry, is unique to Kenya. This is because real estate agencies are required to manage transactions over two million Kenyan shillings through banks⁹⁵ but transactions below this amount permit the unrestricted purchase of properties with cash, avoiding investigation.⁹⁶

2.2.2 The layering stage.

In the second phase known as layering, criminals aim to distance the illegally obtained funds from their original source. This involves blending illicit funds with legitimately acquired money.⁹⁷ To achieve this, they conduct a series of transactions, such as spreading the money across multiple

⁹² Organization for Economic Cooperation and Development, Money Laundering and Terrorist Financing Awareness Handbook for Tax Examiners and Tax Auditors, 10 June 2019, 53.

⁹³ Adeniyi R, Yazid M, 'Money Laundering: Analysis on The Placement Methods' 11 *International Journal of Business* 5, Economics and Law, 2016, 7.

⁹⁴ Ryder N, 'The Financial Services Authority and Money Laundering a Game of Cat and Mouse' 67 *The Cambridge Law Journal* 3, 2008, 648.

⁹⁵ Section 196, The Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill 2023

⁹⁶ Alushula P, 'State moves to relax checks on large cash transactions' *Business Daily*, July 19 2023 – <https://www.businessdailyafrica.com/bd/economy/state-moves-to-relax-checks-on-large-cash-transactions--4307970> on October 2023.

⁹⁷ Ryder N, 'The Financial Services Authority and Money Laundering a Game of Cat and Mouse' 637-640.

accounts, transferring it to offshore accounts, or transferring it for use in different jurisdictions.⁹⁸ In the Kenyan context, this layering process frequently involves the use of hawaladars informally known as hawalas, who facilitate international fund transfers. These intermediaries issue a common remittance code known to both parties involved, with the release of funds contingent upon the recipient providing the designated code.⁹⁹ This engagement with hawalas serves the dual purpose of introducing complexity into investigative efforts and disrupting the paper trail.¹⁰⁰ There is also the deliberate inclusion of legitimate third-party entities in the process hence the name ‘layering,’ as introduction of third parties to the transaction create a series of layers from the original source.¹⁰¹

2.2.3 The integration stage.

The estate market is particularly prone to money laundering operations during the integration stage. At this point, funds having been distributed across various jurisdictions and obscured through the layering process, are reintroduced into the financial system.¹⁰² The paper trail created during this process often confuses regulatory authorities, impeding their ability to keep pace with the movements of these funds.¹⁰³ Once the funds are back in the banking system, they are reallocated to the perpetrator and are frequently directed towards the acquisition of luxury assets or the establishment of seemingly legitimate businesses.¹⁰⁴ For example, a business might be set up to sell luxury watches, not necessarily for profit, but as a front to provide a plausible explanation for the source of funds if questioned.

⁹⁸ Economic Times, ‘What is ‘Money laundering?’-< <https://economictimes.indiatimes.com/definition/money-laundering>> on October 2023

⁹⁹ Passas N, ‘Hawala and Other Informal Value Transfer Systems: How to Regulate Them?’ *5 Risk Management; Special Issue: Regulation, Risk and Corporate Crime in a ‘Globalised’ Era 2*, 2003, 49-59.

¹⁰⁰ Maimbo s, ‘Challenges of Regulating and Supervising the Hawaladars of Kabul’ International Monetary Fund, 2005, 2-4.

¹⁰¹ Tookitaki, ‘Layering in Money Laundering: Unveiling the Complexity, 12 March 2021 <<https://www.tookitaki.com/compliance-hub/layering-in-money-laundering>> on October 2023.

¹⁰² Savona E and Riccardi M, ‘From Illegal Markets to Legitimate Businesses: The Portfolio of Organised Crime in Europe, Final Report of Project OCP Organised Crime Portfolio’ 2015,12-15.

¹⁰³Tookitaki, ‘Layering in Money Laundering: Unveiling the Complexity, 12 March 2021 <<https://www.tookitaki.com/compliance-hub/layering-in-money-laundering>> on October 2023.

¹⁰⁴ Tookitaki, ‘Layering in Money Laundering: Unveiling the Complexity, 12 March 2021 <<https://www.tookitaki.com/compliance-hub/layering-in-money-laundering>> on October 2023.

Similarly, the real estate sector facilitates money laundering when funds, having undergone the ‘cleaning’ process, are directed towards real estate investments thus offering an avenue for financial gain. This could involve converting funds into commercial properties for rental income or using them for residential purposes.¹⁰⁵ Additionally, criminals often prefer directing funds into residential properties by way of expansion or renovation to increase the property's value for subsequent resale at a higher price to legitimize illicit funds through these transactions that outwardly appear to be legitimate real estate dealings.¹⁰⁶ Therefore, within the context of the Kenyan real estate landscape, the residential sector, in particular, emerges as highly vulnerable to money laundering activities.¹⁰⁷

2.3 Factors that enable money laundering in the real estate sector.

The risk of money laundering is heightened in the estate market due to insufficient regulatory oversight.¹⁰⁸ This deficiency is a result of gaps in existing laws and the lack of coordination between two key statutes crucial to the industry: POCAMLA and the Estate Agents Act. The FRC, tasked with supervising reporting institutions under POCAMLA, acknowledges the EARB as the designated authority for overseeing estate agents in matters related to money laundering¹⁰⁹ and POCAMLA further confirms this by officially recognizing EARB as the supervisory body.¹¹⁰ In accordance with the FRC regulations, if there is a supervisory board that oversees professionals, it inherently bears the responsibility of meeting reporting obligations,¹¹¹ implying that EARB is mandated to be the reporting institution for real estate agents. However, upon assessment of the Estate Agents Act, which serves as the foundation for the functions of the EARB, it becomes apparent that there is a conspicuous lack of clearly defined reporting obligations.¹¹²

¹⁰⁵ Canada Working Group on Real Estate, Anti-Money Laundering in the Real Estate Sector, 9 December 2020,37.

¹⁰⁶ Canada Working Group on Real Estate, Anti-Money Laundering in the Real Estate Sector, 9 December 2020,38.

¹⁰⁷Savona E and Riccardi M, ‘From Illegal Markets to Legitimate Businesses: The Portfolio of Organised Crime in Europe, Final Report of Project OCP Organised Crime Portfolio’ 2015,12-15.

¹⁰⁸ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2021, 98-99.

¹⁰⁹ < <https://www.frc.go.ke/registration/reporting-institutions.html> > on October 2023.

¹¹⁰ First schedule, Proceeds of Crime and Anti-Money Laundering Act (Act No. 51 of 2012).

¹¹¹< <https://www.frc.go.ke/registration/reporting-institutions.html> > on October 2023.

¹¹² Mwangi J, Awuor C, ‘Estate Agents Act under Review to Lock out Bogus Property Brokers- Kaimenyi’ Ardhi, 2017—< <http://www.ardhi.go.ke/?p=290> >on October 2023.

Additionally, the Act lacks defined procedures for individual agents reporting to EARB, suggesting a potential lack of awareness regarding its powers as the supervisory authority in money laundering matters and this raises questions as to the actual execution of reporting obligations and whether they are being adequately satisfied.¹¹³ Even when its certain that reporting obligations have not been fulfilled, the EARB does not impose specific penalties on real estate agents for non-compliance with reporting obligations.¹¹⁴ This calls for a more regulatory framework to fortify efforts made to curb movement of these illicit funds within the estate market.¹¹⁵ The estate agents are not the only players in this expansive industry. Even though estate agents fall under regulation by the EARB, the FRC concedes that the broader real estate industry remains largely unregulated.¹¹⁶ This is because the industry is made up of various other participants in the real estate transactions, including brokers who collaborate closely with estate agents, property managers, home appraisers, and home inspectors. The FRC acknowledges that individuals involved in these roles are not subjected to reporting obligations under the POCAMLA and consequently, these individuals may choose not to report. While the FRC does accept reports from these individuals, there is no mandated requirement for them to submit these STRs.¹¹⁷

This situation is further complicated by the absence of a regulatory body overseeing individuals who engage in day-to-day real estate transactions posing the risk of potential money laundering. Moreover, as assessed through the World Assessment Tool, the real estate industry has been marked as highly prone to money laundering, with a potential for increased vulnerability in the future.¹¹⁸ The National Risk Assessment report attributes this heightened risk to the fact that the legal system is not keen on pursuing such cases. According to the analysis conducted, out of a

¹¹³ Mwangi J, Awuor C, 'Estate Agents Act under Review to Lock out Bogus Property Brokers- Kaimenyi' Ardhi, 2017—< <http://www.ardhi.go.ke/?p=290> >on October 2023.

¹¹⁴ Section 22, *Estate Agents Act* (Act No. No. 9 of 2000).

¹¹⁵ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 202, 98.

¹¹⁶ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2023, 143.

¹¹⁷ < <https://frc.go.ke/faq.html> > on October 2023

¹¹⁸World Bank Group, Generic National ML/TF Risk Assessment Tool, 2015, Module 7.

sample of twenty cases, thirteen were identified as involving instances of financial crime within the estate industry and from these thirteen cases, only two ended in convictions.¹¹⁹

The United States government uncovered a money laundering scheme involving the theft of COVID-19 relief funds amounting to two hundred and fifty million dollars in the case United States v. Liban Yasin Alishire¹²⁰. The illicit funds were transferred from the US to Kenya between February 2020 and February 2022 through various channels, including banks and real estate agencies. The stolen money was utilized for purchasing beach plots, luxury vehicles, and holiday homes. The investigation that was led by the US Federal Bureau of Investigation and Internal Revenue Service Criminal Investigation,¹²¹ identified forty-seven suspects involved in diverting COVID-19 relief funds from Minnesota. The funds originated from US child nutrition programs transferred to Turkey, Kenya, and Dubai. A suspect, Aimee Bock, used her organization, Feeding Our Future, to transfer thirty-two million dollars to Abdiaziz Shafii Farah, a Somali American, under the guise of providing meals to vulnerable children and used the funds to acquire properties in Nairobi.¹²²

This not only serves as a clear illustration of the shortcomings in Kenya's regulatory framework but also its inadequate consideration of cross-border crimes.¹²³ The global demand for properties in Kenya provides a ripe environment for money launderers to exploit the process in international transactions, particularly through the manipulation of currency exchange mechanisms.¹²⁴ In a scenario such as the Yasin Alishire case, individuals involved in illicit money operations, attempt to capitalize on the advantages offered by currency exchange fluctuations, and they do so by

¹¹⁹ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2023, 20.

¹²⁰ USA v. Alishire (2023), United States District Court District of Minnesota.

¹²¹ Okumu W, Dahgar M, 'Syndicates launder stolen US COVID-19 funds in Kenya' Institute for Security Studies, date—<<https://issafrica.org/iss-today/syndicates-launders-stolen-us-covid-19-funds-in-kenya#:~:text=The%20Kenyan%20Proceeds%20of%20Crime,through%20investments%20made%20between%20countries.>> on October 2023.

¹²² USA v. Alishire (2023), United States District Court District of Minnesota.

¹²³ Okumu W, Dahgar M, 'Syndicates launder stolen US COVID-19 funds in Kenya' Institute for Security Studies, date—<<https://issafrica.org/iss-today/syndicates-launders-stolen-us-covid-19-funds-in-kenya#:~:text=The%20Kenyan%20Proceeds%20of%20Crime,through%20investments%20made%20between%20countries.>> on October 2023.

¹²⁴ United Nations; Office of the Special Advisor on Africa, Intensifying the fight against corruption and money laundering in Africa, January 2022, 23-26.

investing in Kenyan real estate. A key aspect of this process involves a team effort between money launderers and fraudulent real estate agents. These partnerships are designed to organize property sales at significantly inflated prices compared to the market value.¹²⁵ The excess funds generated from these transactions are then divided between the fraudulent agent and the criminal, creating a facade of legitimacy for the illicitly obtained money.¹²⁶ Additionally, numerous players are involved in these transactions and the complex relationships that happens between money launderers and estate agents create numerous opportunities for this financial crime.¹²⁷

2.4 Negative implications of money laundering in the estate sector.

Money laundering leads to economic distortions, since excess money circulating in the financial system, causes inflation, which in turn, raises the cost of living to levels that ordinary Kenyans find challenging to afford.¹²⁸ Distorted property prices caused by the falsified prices in the value of the estate market often accord property value that is far much higher than what they would fetch in the market and this not only makes it difficult for Kenyans to afford housing but also encourages a misallocation of resources and social and economic disparity.¹²⁹ This is because investments constantly flow in and out of the real estate industry based on these distorted values, adversely affecting other sectors of the country that do not get the same cash inflow and outflow.¹³⁰ Moreover, there is a risk that when the true value of the property is realized, investors who engaged in transactions based on false values may face consequences since those who borrowed from financial institutions might find themselves owing more than the actual worth of their property.¹³¹

¹²⁵ Organization for Economic Cooperation and Development, Report on Tax Fraud and Money Laundering Vulnerabilities Involving the Real Estate Sector, March 2020, 7-10.

¹²⁶ United Nations; Office of the Special Advisor on Africa, Intensifying the fight against corruption and money laundering in Africa, January 2022, 25.

¹²⁷ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2023, 143.

¹²⁸ Dunfee T 'The Impact of Dirty Money on Global Capitalism' 17 *Business Ethics Quarterly* 4, 2007, 729-742.

¹²⁹ Martini M, 'How the Corrupt Purchase Luxury Real Estate in Key Markets', Transparency International, 2017, 15-16 on —< <https://www.jstor.org/stable/pdf/resrep20516.7.pdf> > on 20 October 2023

¹³⁰ Khoury C, Claver C, Financial Crimes Hurt Economies and Must be Better Understood and Curbed, International Monetary Fund, 7 December 2022—< <https://www.imf.org/en/Blogs/Articles/2023/12/07/financial-crimes-hurt-economies-and-must-be-better-understood-and-curbed> > on October 2023.

¹³¹ Pressman S, 'On Financial Frauds and Their Causes: Investor Overconfidence' 57 *The American Journal of Economics and Sociology* 4, 1998, 406-408.

This situation creates a challenging scenario in the financial system because it leads to an increase in non-performing loans since financial institutions will now struggle as their ability to lend is reduced, impacting economic growth.¹³² Consequently, individuals and businesses face challenges in obtaining loans for investments and business expansion, hindering overall economic development.¹³³

Following a report by the Group of Seven (G7) in September 2022, it has been highlighted Kenyan authorities, particularly the Directorate of Criminal Investigation (DCI), the Central Bank of Kenya (CBK), FRC, the Assets Recovery Agency (ARA), and the Judiciary, are not adequately addressing the issues of money laundering and terrorist financing. The report reveals that Kenya has not undertaken investigations or prosecutions of individuals, whether legal or natural, for offenses related to terrorist financing, in alignment with its threat assessment.¹³⁴ The report authored by the G7 was with the aim of safeguarding the Global Financial System¹³⁵ however, it poses a threat to Kenya's standing within this system because following that report, the FATF placed Kenya under scrutiny, warning of the possibility of being reinstated in the grey list, where their actions would be closely monitored.¹³⁶ Despite recent efforts, including the launch of an international financial centre in Nairobi, designed to attract foreign firms and enhance capital flows, Kenya's position in the global financial landscape is now at risk.¹³⁷ The new financial hub in Nairobi aims to model the city as a financial district, aligning it with established financial centres in Europe and the Middle East and this move has positioned Nairobi as a regional hub.¹³⁸ However, this recognition is now in jeopardy because the money laundering threats carry a clear reputational

¹³² Zurek M, 'Real Estate Markets and Lending: Does Local Growth Fuel Risk?' *Journal of Financial Services Research*, 2021, 29-32—< <https://link.springer.com/article/10.1007/s10693-021-00358-9> > on 21 October 2023.

¹³³ Zurek M, 'Real Estate Markets and Lending: Does Local Growth Fuel Risk?' *Journal of Financial Services Research*, 2021, 29—< <https://link.springer.com/article/10.1007/s10693-021-00358-9> > on 21 October 2023.

¹³⁴ Okumu W, Dahgar M, 'Syndicates launder stolen US COVID-19 funds in Kenya' Institute for Security Studies, date—< <https://issafrica.org/iss-today/syndicates-launder-stolen-us-covid-19-funds-in-kenya#:~:text=The%20Kenyan%20Proceeds%20of%20Crime,through%20investments%20made%20between%20countries> > on October 2023.

¹³⁵ Council on Foreign Relations, 'What Does the G7 Do?', 28 June 2023, 2.

¹³⁶ Guchu B, 'The FATF grey list: An explainer' Price Waterhouse and Coopers blog, November 2023—< <https://www.pwc.com/ke/en/blog/fatf-grey-list.html> > on November 2023.

¹³⁷ —< <http://www.parliament.go.ke/node/20600> > on October 2023

¹³⁸ Manson K, 'Nairobi the regional hub: another day, another opening' Financial Times, 4 May 2014—< <https://www.ft.com/content/3ebdeff2-2a41-3081-a85d-1c7a5ac1aee> > on October 2023.

risk for Kenya especially at a time when Kenya is striving to establish itself as a key player in international finance.¹³⁹

The impact of the risk extends beyond the country itself, reaching into the government and the regulatory authorities. Due to the perceived weaknesses in the regulatory framework within the estate market, there is a potential questioning of the government's efforts to combat financial crime and its ability to safeguard the financial system.¹⁴⁰ This doubt could cast shadows on the effectiveness of regulatory measures in place. Moreover, it also affects the estate industry directly since the confidence in these agents to conduct trustworthy transactions may be compromised, as investors may harbour doubts about the sector's credibility.¹⁴¹ The investors themselves engaging in real estate transactions could face reputational challenges because if their investments become associated with a money laundering scandal or a tainted sector, it not only jeopardizes their businesses but also raises questions about their decision-making abilities, potentially leading to financial losses.¹⁴²

Money launderers employ tactics to minimize costs and avoid losses, with one significant consequence being the potential for tax evasion.¹⁴³ They manipulate property values to interfere with the accuracy of tax assessments and this becomes problematic because governments depend on these assessments to determine property tax obligations. They are seen to engage in overvaluing properties during transactions to inflate the value of the asset however, when it comes to tax assessments, they often undervalue the same properties.¹⁴⁴ This manipulation denies the government its tax revenue and compromises on the fairness and equity of the tax system.¹⁴⁵

The consequences extend beyond lost tax revenue because industries connected with real estate, such as insurance, legal services, and financial services, also bear the burden of these

¹³⁹ AZA Finance, Nairobi's Status as Regional Hub Buoyed by UK Investment, 2020, 2.

¹⁴⁰ McDowell J, Novis G, 'Consequences of Money Laundering and Financial Crime' 6 *Economic Perspectives* 2, 2001, 6-8

¹⁴¹ Pressman S, 'On Financial Frauds and Their Causes: Investor Overconfidence,' 408.

¹⁴² Pressman S, 'On Financial Frauds and Their Causes: Investor Overconfidence,' 408.

¹⁴³ Yildiz T, 'Money Laundering and Tax Evasion report' Sanction Scanner, 17 July 2023—
<<https://sanctionsscanner.com/blog/money-laundering-and-tax-evasion-380>> on November 2023

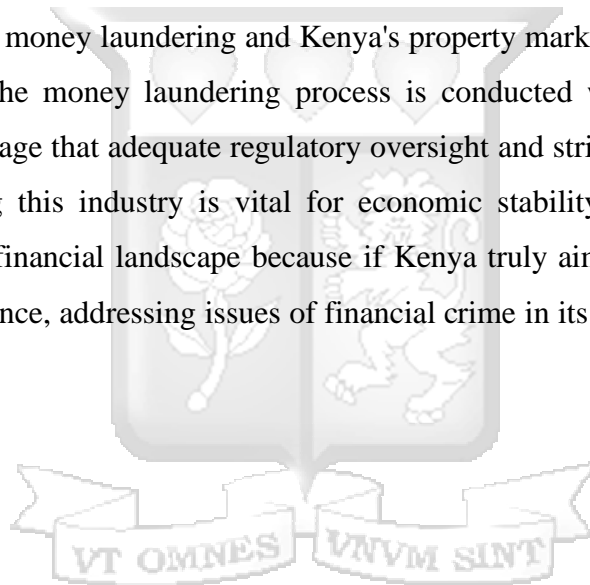
¹⁴⁴ Martini M, 'How the Corrupt Purchase Luxury Real Estate in Key Markets', Transparency International, 2017, 13
on —< <https://www.jstor.org/stable/pdf/resrep20516.7.pdf> > on 20 October 2023

¹⁴⁵ Yildiz T, 'Money Laundering and Tax Evasion report' Sanction Scanner, 17 July 2023—
<<https://sanctionsscanner.com/blog/money-laundering-and-tax-evasion-380>> on November 2023

manipulative practices. When money launderers undervalue properties, insurance premiums may be insufficient to cover actual risks.¹⁴⁶ Legal and insurance services may face challenges in accurate valuation for transactions and loans because it impedes their ability to make informed decisions and exposes them to potential losses.¹⁴⁷ For financial services in cases where money launderers secure loans, the undervaluation of properties during the money laundering process results in collateral that is far below its actual worth. This poses risks to financial services, as the collateral's lower value may not adequately cover the loan amount in the event of default leading to loss of revenue.¹⁴⁸

2.5 Conclusion

The relationship between money laundering and Kenya's property market poses many challenges. An assessment of how the money laundering process is conducted within real estate reveals vulnerabilities at every stage that adequate regulatory oversight and stringent laws could come in to address. Safeguarding this industry is vital for economic stability and upholding Kenya's reputation in the global financial landscape because if Kenya truly aims to acquire a prominent name in international finance, addressing issues of financial crime in its real estate sector ought to be the starting point.



¹⁴⁶ Martini M, 'How the Corrupt Purchase Luxury Real Estate in Key Markets', Transparency International, 2017, 17-20 on —< <https://www.jstor.org/stable/pdf/resrep20516.7.pdf> > on 20 October 2023

¹⁴⁷ Dugato M, Favarin S, 'The Risks and Rewards of Organized Crime Investments in Real Estate' 55 *The British Journal of Criminology* 5, 2015, 944,960-963.

¹⁴⁸ Khoury C, Claver C, Financial Crimes Hurt Economies and Must be Better Understood and Curbed, International Monetary Fund, 7 December 2022—< <https://www.imf.org/en/Blogs/Articles/2023/12/07/financial-crimes-hurt-economies-and-must-be-better-understood-and-curbed> > on October 2023.

CHAPTER THREE

ASSESSING GOVERNMENT REGULATIONS AND GAPS IN MONEY LAUNDERING PREVENTION IN KENYA'S REAL ESTATE

3.1 Introduction

The estate industry is a fundamental sector in Kenya's economic prosperity since it significantly contributes to the country's GDP.¹⁴⁹ In Kenya's economy, this sector is not only a symbol of the economic growth but also stands out as one of the best-performing industries, both nationally and globally.¹⁵⁰ However, this comes with a vulnerability since the nature of transactions in the estate industry render it susceptible to financial crimes, especially money laundering. This vulnerability arises from a mix of factors, including limitations in existing regulations, challenges in implementing measures, and the ever-changing nature of financial crime tactics.¹⁵¹ Together, these factors create a favourable environment for illicit funds to enter the real estate market, potentially compromising its integrity and hindering its ongoing contribution to the national economy.

Recognizing this risk, the Kenyan government has actively endeavoured to strengthen the integrity of the estate industry. The guidelines created are designed not only to protect the industry from the detrimental effects of money laundering, but also, to ensure continued economic development.¹⁵² Although the existing framework may give the impression of being comprehensive, it has faced scrutiny from various researchers, particularly concerning its implementation and therefore, there is adequate room for improvement.¹⁵³ Additionally, as these measures have been implemented, certain gaps have emerged. The failure to address these gaps has allowed them to persist as ways to carry on financial crime within the estate industry.

¹⁴⁹ Cytonn Investments, Real Estate Developers Regulatory Framework, 26 February 2023, 2.

¹⁵⁰ Knight Frank, The Wealth Report, 2014, 11.

¹⁵¹ Financial Action Task Force, Money Laundering & Terrorist Financing Through the Real Estate Sector ,29 June 2007, 18-22.

¹⁵² National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2023, 28-30.

¹⁵³ Gikonyo C, 'The Offence of Money Laundering in Kenya' 17 *The Law Society of Kenya Journal* 1, 2021, 10.

In summary, this chapter aims to provide insight into the legislative framework and interactions among various government institutions and the steps they and regulatory bodies make towards robust regulation. The objective is to enhance understanding of the dynamics within the real estate industry and through this examination, the government's efforts to protect Kenya's property market from money laundering threats. Therefore, the focus is twofold: first, to assess what regulatory measures have been put in place, and second, to identify any existing gaps that continue to expose the sector to the influence of these practices.

3.2 The Legislative and Institutional Framework

The Kenyan government, in alignment with FATF recommendations enacted POCAMLA.¹⁵⁴ The introduction of POCAMLA marked a significant milestone in Kenya's anti money laundering legislation as there was no pre-existing framework addressing these issues. This legislation serves a fundamental role in regulating and combatting money laundering and terrorism financing.¹⁵⁵ POCAMLA established the FRC, a body dedicated to receiving and monitoring reports related to suspicious transactions and its impact has been commendable on multiple fronts.¹⁵⁶ Firstly, the act's establishment of the FRC has streamlined the reporting process for designated bodies, enhancing the efficiency of addressing potential financial crimes. This measure not only strengthens Kenya's domestic efforts but also aligns with international best practices as it positioned Kenya as a team player in international prevention of financial crime.¹⁵⁷ Furthermore, the enactment of POCAMLA has boosted Kenya's standing in the global community since its existence has played a major role in Kenya's removal from the FATF grey list in 2014. By ratifying anti-money laundering treaties and establishing a dedicated legislative framework, Kenya has in this way, also demonstrated its commitment to international standards.¹⁵⁸

Domestically, the implementation of POCAMLA has significantly fortified the rule of law in Kenya. Criminals are now held accountable for their actions, and public awareness of what

¹⁵⁴ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya,2022, 13.

¹⁵⁵ < <https://www.frc.go.ke/about-frc/background.html>> on January 2020

¹⁵⁶ < <https://www.frc.go.ke/about-frc/background.html>> on January 2020

¹⁵⁷ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya,2022, 44.

¹⁵⁸ Cockayne J, Tu'emay A , Baseline Study on Anti-Money Laundering and Countering the Financing of Terrorism in the IGAD Subregion, May 2012, 25-27.

constitutes as financial crime has increased.¹⁵⁹ POCAMLA has not only provided a legal basis for accountability but has also empowered pre-existing institutions, like the FIU. Additionally, POCAMLA has addressed the previous fragmentation in regulatory systems.¹⁶⁰ It now mandates regulatory bodies overseeing various professions to detect and regulate against money laundering, thus harmonizing efforts. This expansion is evident in the first schedule, where regulatory bodies are now tasked with overseeing professionals under their purview, ensuring a unified approach between these regulatory bodies and the FRC.¹⁶¹ This legislation has not only established the FRC but has made it mandatory that reports be submitted to them, and this also extends to real estate agents who are recognized professionals under the POCAMLA.¹⁶² In recognizing the potential for money laundering in real estate transactions, the legislation has placed a lot of emphasis on financial institutions and rightfully so. This focus is strategic because researchers are of the viewpoint that money laundering often occurs during property transactions when funds are exchanged.¹⁶³ Closely monitoring transactions within the financial sector has a ripple effect that contributes to preventing dirty money operations in the property market.¹⁶⁴

3.2.1 Gaps in the legislative and institutional framework

Under the POCAMLA, specific professions and DNFBPs have been listed for regulation.¹⁶⁵ Within the estate industry, only estate agents fall under the regulatory purview of the EARB while the other parties involved in these transactions that lack a designated compliance or supervisory body are required to directly report to the FRC.¹⁶⁶ The mandate of the FRC, as outlined in the POCAMLA, encompasses conducting inspections and investigations into suspicious transactions, monitoring various industries to prevent suspicious transactions and it also serves as

¹⁵⁹ Cockayne J *et al* , Baseline Study on Anti-Money Laundering and Countering the Financing of Terrorism in the IGAD Subregion, 25.

¹⁶⁰ Central Bank of Kenya, The Integrity of our Financial System: What is at Stake? , 2021,1.

¹⁶¹ First schedule, Proceeds of Crime and Anti-Money Laundering Act (Act No. 51 of 2012).

¹⁶² Section 2, Proceeds of Crime and Anti-Money Laundering Act (Act No. 51 of 2012)

¹⁶³ Gikonyo C, 'Banks in Kenya and anti-money laundering obligations: the conflicts of interests arising' 11 *Journal of Money Laundering Control* 1, 2020, 22-25.

¹⁶⁴ Kidwai A, 'Money Laundering and the Role of Banks' 59 *Pakistan Horizon* 2, 2006, 43-47.

¹⁶⁵ Section 2, Proceeds of Crime and Anti-Money Laundering Act (Act No. 51 of 2012)

¹⁶⁶ Financial Reporting Centre, Guidance on Registration of Reporting Institutions with The Financial Reporting Centre, 2021,12.

the central authority for receiving Suspicious Transaction Reports (STRs) from both regulated entities and unregulated professions.¹⁶⁷ This situation presents two key issues.

While the FRC's role in the AML regime is well-defined, there exists a significant knowledge gap regarding its performance estimates. Granted, the nature of the FRC's work inherently limits full transparency, however the extent of this knowledge gap is too pronounced.¹⁶⁸ Additionally, limited research on the FRC's effectiveness creates a challenge, potentially demotivating reporting institutions. This is because, an unclear understanding of the efficiency and effectiveness of reporting, may make institutions disinclined to report suspicious transactions, fearing their efforts might be futile.¹⁶⁹ There is also lack of evidence that indicates whether the FRC actively monitors reporting institutions to ensure compliance with their responsibilities. This raises concerns about the quality of the reports submitted. Without proper oversight, institutions might engage in blind reporting by merely fulfilling the obligation to submit STRs without ensuring the reports are of substantive quality.¹⁷⁰

The efficiency of the FRC is also brought into question due to the substantial backlog of unattended reports. In its 2017 annual report, the FRC revealed that they had registered 289 reporting institutions.¹⁷¹ Over a four-year period from 2012 to 2016, these institutions submitted a total of 4574 reports, with 84.7% coming from financial institutions. Of the reports, only 494 reports were fully analysed, 52 were closed for lacking suspicious transactions, and 442 were shared with law enforcement with a significant portion of 4080 reports remaining unaddressed.¹⁷² Kenya has been said to be losing 40 billion annually due to money laundering and in the 494 STRs that were analysed, it was provided that they involved money amounting to 20,493,197,158. This raises

¹⁶⁷ < <https://www.frc.go.ke/about-frc/background.html> > on January 2020

¹⁶⁸Wanyela M, 'Trouble brews at Kenya's financial intelligence unit' The EastAfrican, 13 December 2014— <<https://www.theeastafrican.co.ke/tea/news/east-africa/trouble-brews-at-kenya-s-financial-intelligence-unit--1330662>> on 23 November 2023.

¹⁶⁹Sang M, 'A Critical Analysis of Kenya's (2023) Anti-Money Laundering and Counter Financing of Terrorism Regime' 10 *Journal of Conflict Management & Sustainable Development* 3, 2023, 33-36.

¹⁷⁰ Takáts E, 'A Theory of "Crying Wolf": The Economics of Money Laundering Enforcement' 27 *Journal of Law, Economics, & Organization* 1, 2011, 34.

¹⁷¹ Financial Reporting Centre, Annual Compliance Report, 2017, 18-23.

¹⁷² Financial Reporting Centre, Annual Compliance Report, 2017, 18-23.

concerns about the potential loss if only 10.8% of the reports involved such large sums of money.¹⁷³

This situation is further complicated by the FRC's expanded responsibility, now encompassing the handling of terrorism financing as mandated by the Prevention of Terrorism Act.¹⁷⁴ Although a proposal to assign quasi-judicial functions to the FRC might seem burdensome given their already extensive mandate, it is essential to give them this role to expedite the legal resolution process for STRs, which often faces delays as seen above.¹⁷⁵ Furthermore, specific sectors such as real estate agents, casinos, and dealers in precious metals lack explicit guidance on meeting their reporting obligations.¹⁷⁶ As a result, there is limited information on the compliance of these entities, and to date, no institution can be said to have faced consequences for non-compliance since the establishment of the FRC.¹⁷⁷ There also exists a challenge in determining how to strike a balance between maintaining positive client relationships and fulfilling reporting obligations. This uncertainty gives rise to concerns regarding privacy and potential data protection issues.¹⁷⁸ The issue of when and how to report suspicious transactions without negatively impacting client relationships has been a significant obstacle and this was one of the main reasons for lawyers resisting to be included as reporting institutions and despite their recent inclusion, this matter remains inadequately clarified.¹⁷⁹

Researchers have raised concerns about POCAMLA because of its focus on preventive controls while omitting procedures before and after confiscating assets or cash suspected of money laundering.¹⁸⁰ This lack of guidance creates potential vulnerabilities for corruption within the Asset Recovery Agency (ARA), especially concerning the recovery process for individuals whose

¹⁷³ Financial Reporting Centre, Annual Compliance Report, 2017, 18-23.

¹⁷⁴ Section 42, Prevention of Terrorism Act (Act No. 30 of 2012)

¹⁷⁵ Zagaris B, 'Trends in International Money Laundering from a U.S. Perspective' 35 *The International Lawyer* 2, 2001, 844-846.

¹⁷⁶ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya, 2022, 72-74.

¹⁷⁷ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya, 2022, 74.

¹⁷⁸ Millard D, 'Hung Out to Dry? Attorney Client Confidentiality and The Reporting Duties Imposed by The Financial Intelligence' *Sabinet African Journals*, 2013, 405-407 <<https://journals.co.za/doi/pdf/10.10520/EJC148924> > on 23 November 2023.

¹⁷⁹ Njaramba E, 'The conflict between anti-money laundering reporting obligations and the doctrine of confidentiality for legal practitioners in Kenya' 24 *Journal of Money Laundering Control* 3, 2020, 609-613.

¹⁸⁰ Warui B, 'Implementation and Enforcement of The Law on Money Laundering: An Analysis of Kenya's Legal and Institutional Framework.' Published LLM Thesis, University of Nairobi, Nairobi, 2009, 9, 120-122.

belongings are found not to be as a result of financial crime.¹⁸¹ Moreover, in transactions involving various industries, such as the real estate sector that incorporates banks, legal services, and insurance, there is an absence of information on who should report these transactions. This absence results in duplicated reports, contributing to a backlog in the FRC's workload.¹⁸²

Elod Takats is a proponent of the economic theory of the 'crying wolf' and he relates it to institutional reporting obligations in the prevention of money laundering.¹⁸³ He draws parallels between filing STRs and the classic tale of the boy who cried wolf, suggesting that excessive reporting diminishes the information's quality, rendering it ineffective.¹⁸⁴ While acknowledging the importance of reporting, the Kenyan government, through the KRA, has mandated individuals to declare assets, monetary instruments, or cash exceeding 10,000 US dollars when entering or leaving the country, even if there's clear evidence of its lawful source.¹⁸⁵ This frequent declaration has the effect of overreporting as advanced by Elod Takats where reporting becomes a routine function rather than a targeted effort to identify money laundering.¹⁸⁶

POCAMLA has overlooked the possibility of individuals having their own STRs, resulting in a lack of reporting procedures and, as such, there are no reporting obligations for individuals.¹⁸⁷ While this may not significantly impact individuals, it poses a greater challenge for unregulated players, especially in the real estate sector where there are several other players other than the estate agents and the parties involved in the transaction.¹⁸⁸ Currently, only financial institutions and estate agents in such a transaction are subject to regulation, leaving a gap in reporting obligations for the others. This oversight in POCAMLA allows the FRC to provide that where no reporting obligation is established, individuals or entities may choose not to report. This situation creates an environment conducive to ML in Kenya's estate sector, particularly among unregulated

¹⁸¹ Gikonyo C, 'Detection mechanisms under Kenya's anti-money laundering regime: omissions and loopholes,' 61-63.

¹⁸² Gikonyo C, 'Detection mechanisms under Kenya's anti-money laundering regime: omissions and loopholes,' 61.

¹⁸³ Takáts E, 'A Theory of "Crying Wolf": The Economics of Money Laundering Enforcement,' 34

¹⁸⁴ Takáts E, 'A Theory of "Crying Wolf": The Economics of Money Laundering Enforcement,' 34-36.

¹⁸⁵ < <https://kra.go.ke/helping-tax-payers/faqs/customs-and-border-control> > on November 2023

¹⁸⁶ Takáts E, 'A Theory of "Crying Wolf": The Economics of Money Laundering Enforcement,' 34.

¹⁸⁷ < <https://www.frc.go.ke/registration/reporting-institutions.html> > on November 2023

¹⁸⁸ Warutere P, 'Detecting and Investigating Money Laundering in Kenya' Institute for Security Studies Monograph Series, 2006, 64-66.

players.¹⁸⁹ To aggravate matters even further, the government has raised the threshold for real estate transactions that require reporting. Initially the threshold was set at transactions exceeding one million Kenyan shillings, this was later increased to two million Kenyan shillings, potentially backtracking the vigilance against money laundering in real estate transactions.¹⁹⁰

3.3 Regulatory Authorities

Several regulatory authorities, such as the LSK for lawyers, the ICPAK for accountants, and the CBK for financial regulators, have demonstrated effective oversight by establishing exclusive anti-money laundering guidelines tailored to their respective professions.¹⁹¹ This approach by LSK, CBK and ICPAK can be considered to be a recognition of the FRC's decision, to designate them as supervisory agencies for their respective professional sectors. In contrast, the Estate Agents Regulatory Board (EARB) has not exhibited a similar level of effectiveness in its regulatory role within the real estate industry. Despite the council appointed by the former Principal Secretary of the State Department for Housing and Urban Development, recommending the development of a Real Estate Developers Regulatory Board in Kenya, the plan has not been put into action. This regulatory body was proposed to oversee all participants in real estate transactions, excluding estate agents. The failure to implement this evidently beneficial initiative suggests challenges in the effectiveness of regulatory efforts within the real estate sector.¹⁹²

Unlike LSK and ICPAK, EARB lacks official AML guidelines exclusive for real estate agents. This gap in regulatory guidance raises concerns about the adequacy of oversight within the real estate sectors.¹⁹³ The relevance of the exclusive recommendations stems from their capacity to oversee the specific dangers and obstacles involved with money laundering in the specific profession. Regulatory authorities can therefore improve the efficacy of their supervision processes by customising rules to the specific industry. The lack of such specialised guidelines for estate agents creates a regulatory vacuum, especially for other parties involved in real estate transactions such as hawaladars and digital financing providers.¹⁹⁴

¹⁸⁹ < <https://www.frc.go.ke/registration/reporting-institutions.html> > on November 2023

¹⁹⁰ Section 196, The Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill 2023

¹⁹¹ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya, 2022, 33.

¹⁹² Cytonn Investments, Real Estate Developers Regulatory Framework, 26 February 2023, 2.

¹⁹³ Transparency International, A Review of AML laws in Kenya and the role of Civil Society in the Financial Action Task Force (FATF) Process, September 2022, 28-32.

The rise of digital lenders has been the saving grace for those urgently in need of financial assistance, especially for those who are unable to borrow from traditional banking services. However, this has inadvertently created challenges for real estate agents and regulatory bodies since digital lenders have become the preferred channel for money launderers seeking to conceal the origins of their funds.¹⁹⁵ Taking advantage of the easy loan obtaining processes of digital lending platforms, these individuals sidestep the formalities imposed by banks and borrow money for purchase of real estate property only to pay it back with illegitimate funds creating an illusion of legitimacy in their real estate transactions.¹⁹⁶ In response to these challenges, the government introduced the Digital Credit Providers Regulations, 2022, on March 18, 2022. The aim was to bring oversight and licensing to previously unregulated Digital Credit Providers (DCPs) under the watchful eye of the CBK.¹⁹⁷ Despite the regulatory efforts unregulated DCPs continue their operations unchecked. This regulatory gap has become an avenue for financial crime, particularly within the estate industry.¹⁹⁸

The National Risk Assessment report indicates that out of 381 operational DCPs, only 22 have been confirmed to be within the CBK's regulatory framework and the absence of penalties for non-compliance worsens the issue, permitting these entities to operate outside legal boundaries with no repercussions.¹⁹⁹ As the world of digital lending continues to change, it is important to take proactive steps to handle new risks and maintain a secure and transparent financial environment.²⁰⁰ Therefore, addressing this challenge requires effort from regulatory authorities to close existing gaps in the rules and ensure stronger enforcement. As a starting point, it is crucial to make the

¹⁹⁴Passas N, 'Hawala and Other Informal Value Transfer Systems: How to Regulate Them?' 49-51.

¹⁹⁵ Cheruiyot F, 'Money Laundering in Kenya - the Role of Digital Payments' Intasend, 21 January 2023—<
<https://intasend.com/payments/money-laundering-in-kenya-the-role-of-digital-payments/> > on 25 November 2023

¹⁹⁶ Cheruiyot F, 'Money Laundering in Kenya - the Role of Digital Payments' Intasend, 21 January 2023—<
<https://intasend.com/payments/money-laundering-in-kenya-the-role-of-digital-payments/> > on 25 November 2023

¹⁹⁷ Central Bank of Kenya, The Digital Credit Providers Regulations, 2022.

¹⁹⁸ National Risk Assessment Taskforce, Money Laundering and Terrorism Financing National Risk Assessment Report, October 2023, 144.

¹⁹⁹ Eastern and Southern Africa Anti-Money Laundering Group, Mutual Evaluation Report of Kenya, 2022, 74.

²⁰⁰ Nguyen D, Ngo T 'Digital Credit and Its Determinants: A Global Perspective' 11 *International Journal of Financial Studies* 4, 2023, 124.

penalties for not following the rules more serious and enhance our monitoring systems.²⁰¹ This is necessary not only in the operations of DCPs but also within the real estate sector and it acts as a deterrence and protects the credibility of the financial system by preventing the misuse of digital online lending platforms for illegal purposes.²⁰²

The regulatory loopholes within Kenya's AML framework as discussed above have now regrettably led to its recent re-inclusion in the grey list effective from February 23rd, 2024 as was officially communicated by the Cabinet Secretary of the Ministry of Finance.²⁰³

3.4 Conclusion

The government, via the implementation of POCAMLA, has undertaken significant initiatives to counter financial crimes. However, a closer look at the efforts taken reveals inefficiencies, transparency issues, and a backlog of unattended reports within the system. Additionally, gaps such as the oversight of unregulated players and challenges posed by digital lending platforms, persist, creating opportunities for dirty money operations. In the estate industry, the EARB, requires enhanced supervisory effectiveness, especially through the development of specialized anti-money laundering guidelines for estate agents among other efforts that have been discussed. Addressing these vulnerabilities requires not only legislative improvements, but also, collaborative efforts from government bodies, regulatory authorities, and the stakeholders in the real estate industry.

²⁰¹ Warutere P, 'Detecting and Investigating Money Laundering in Kenya' Institute of Security Studies Monograph Series, 2006, 55.

²⁰² Nguyen D, Ngo T 'Digital Credit and Its Determinants: A Global Perspective,' 12

²⁰³ Njuguna N, 'Article title' The National Treasury and economic planning, 23 February 2024 <https://www.treasury.go.ke/wp-content/uploads/2024/03/Scanb-CS2.pdf> on 29 March 2024.

CHAPTER 4

ENHANCING ANTI-MONEY LAUNDERING PRACTICES IN KENYA'S REAL ESTATE: INSIGHTS FROM SINGAPORE AND SOUTH AFRICA

4.1 Introduction

In the preceding chapter, it has been identified that Kenya's current anti-money laundering regime exhibits certain gaps. To address this, this chapter assesses countries that have successfully dealt with money laundering issues to determine what is applicable to Kenya. The focus for this comparison is on Singapore and South Africa. By examining their approaches to anti-money laundering, this study hopes to pinpoint where Kenya's system falls short and assess if adopting some of the successful elements from Singapore and South Africa could fill those gaps.

Singapore, often dubbed the 'Switzerland of Asia,' serves as the subject of this study due to its role as an international financial hub globally.²⁰³ Despite managing significant financial transactions, Singapore has been ranked by the World Bank as the second-best performing country in terms of ease of business because it has put in place a strong AML system that has shown to be quite effective.²⁰⁴ It has also been ranked third in the top performing economies²⁰⁵ and fifth in the least corrupt economies which has also been attributed to the stringent measures employed in prevention of financial crime.²⁰⁶

Equally, South Africa is included in the comparative study not merely for its global reputation as one of the countries known for implementing best practices for preventing money laundering,²⁰⁷ but also for the practical insight it can offer to Kenya. This is because as an African nation, South Africa provides a relatable example that can inspire Kenya, and other African countries, to develop

²⁰³ Lewis L and Mercedes R , 'The lure of Singapore: Chinese flock to 'Asia's Switzerland'' Financial Times, 15 January 2023 <https://www.ft.com/content/62845c24-1e45-483c-95d1-b2c5d4c07337> on 24 December 2023.

²⁰⁴ <https://data.worldbank.org/indicator/IC.BUS.EASE.XQ?locations=SG> on 24 December 2023

²⁰⁵ World Economic Forum, The Global Competitiveness, 20 October 2018,13.

²⁰⁶ Transparency International, Corruption Perceptions Index, November 2018, 2.

²⁰⁷ Financial Action Task Force, FATF (Financial Action Task Force) Countries 2022, 2022 <https://worldpopulationreview.com/country-rankings/fatf-countries> on 24 December 2023.

and implement effective anti-money laundering guidelines. The shared characteristics in institutional and legislative frameworks between South Africa and Kenya also make the practices drawn from South Africa particularly applicable to the Kenyan context.

This chapter therefore aims to conduct a comparative analysis, juxtaposing Kenya's existing AML measures, as discussed in the previous section, with the successful strategies employed by Singapore and South Africa. The objective is to gain insights from both countries on how to address money laundering challenges within Kenya's real estate sector. Furthermore, this study seeks to explore how the practices observed in Singapore and South Africa can be applied to rectify the identified gaps in Kenya's legislative and regulatory framework for preventing dirty money operations. This chapter will also examine the anti-money laundering practices in these countries in comparison to the best practices recommended by the FATF. This analysis will be done through an assessment of the legislative and institutional framework, along with a review of relevant legal cases on the same.

4.2 Assessment of Singapore's anti money laundering framework

Singapore strengthened its institutional money laundering framework upon joining the FATF in 1992. While serving as a member of FATF, Singapore assumed the presidency of the task force in 2022.²⁰⁸ Additionally, Singapore is a participant in the Asia/Pacific Group on Money Laundering (APG), a regional inter-governmental body structured similarly to FATF. APG ensures that its member countries adhere to, and implement international standards addressing money laundering, terrorist financing, and the proliferation financing of weapons of mass destruction.²⁰⁹ Within the Singapore Police, there exists the Commercial Affairs Department (CAD), tasked with investigating financial crimes.²¹⁰ This department collaborates with the Monetary Authority of Singapore (MAS), an independent body which works in conjunction with the government to investigate and deter financial crime.²¹¹

²⁰⁸ World Economic Forum, Priorities for the Financial Action Task Force under the Singapore presidency, July 2022, 1.

²⁰⁹ <https://apgml.org/about-us/page.aspx?p=91ce25ec-db8a-424c-9018-8bd1f6869162> on 24 December 2023

²¹⁰ <https://www.police.gov.sg/Who-We-Are/Organisation-Structure/Specialist-Staff-Departments/Commercial-Affairs-Department> on 24 December 2023

²¹¹ <https://www.mas.gov.sg/regulation/anti-money-laundering> on 24 December 2023

4.2.1 The institutional framework

The real estate sector in Singapore is overseen by The Council for Estate Agents (CEA) . This body derives its power from the Estate Agents Act 2010, which has a section of the act dedicated to guiding real estate agents in the prevention money laundering and financing terrorism.²¹² Furthermore, section 44E of this legislation provides for the repercussions ensuing from violations of the stipulated guidelines.²¹³ This stands in stark contrast to the Estate Agents Act in Kenya which lacks explicit reference to AML guidelines. The players involved in a real estate transaction are given the obligation to conduct Customer Due Diligence (CDD) to ensure authenticity of the money used as well as the integrity of the transactions.²¹⁴ These players have also been mandated under the Corruption, Drug Trafficking, and Other Serious Crimes Act, in their individual capacities, to file STRs after conducting CDD and a lack thereof will result to a penalty prescribed in the act.²¹⁵

4.2.2 The legal framework

The legal framework for AML in Singapore is very comprehensive because Singapore has been known to pursue a proactive approach when dealing with any warnings given. For instance, in 2011, the U.S state department gave warnings to Singapore regarding potential money laundering concerns in Singapore’s gambling industry. In response, the Singapore government gave authority to the regulating bodies to fine up to ten percent of annual casino returns.²¹⁶ The main AML regulation is the Corruption, Drug Trafficking, and Other Serious Crimes Act 1992 (CDSA) which outlines the responsibilities of government authorities and establishes AML regulations.²¹⁷ This includes reporting procedures and penalties for individuals involved in financial crime.²¹⁸

²¹² Section 44, Part 4A, *Estate Agents Act 2010* (Singapore)

²¹³ Section 44E, Part 4A, *Estate Agents Act 2010* (Singapore)

²¹⁴ Section 44B, Part 4A, *Estate Agents Act 2010* (Singapore)

²¹⁵ Section 68, Part 6B, *Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act* (Singapore)

²¹⁶ Monetary Authority of Singapore, *Singapore National Money Laundering and Terrorist Financing Risk Assessment Report*, November 2013, 69-72.

²¹⁷ Section 18, Part 3, *Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act* (Singapore)

²¹⁸ Section 68, Part 6B, *Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act* (Singapore)

In the real estate sector, stringent requirements apply to foreigners seeking property acquisition in Singapore. First, foreigners are mandated to obtain prior approval from authorities and this approval hinges on demonstrating both social and economic contributions to Singapore's economy, coupled with evidence of a five-year residency in the country.²¹⁹ This already reduces the pool of real estate available to foreigners. Moreover, even if foreigners successfully navigate these prerequisites, an Additional Buyers' Stamp Duty is imposed on sixty percent of the property's value upon acquisition.²²⁰ This does not only protect the domestic industry, but it also deters extraterritorial financial crime, an area where Kenya is primarily failing.²²¹

In tandem with these regulations, Singapore has attempted to further address cross-border criminal activities through the establishment of the Mutual Assistance in Criminal Matters Act.²²² This was necessitated by the liberation of trade and industrialization since Singapore realized the need to cooperate with other countries, more so, their trading partners, to prevent extraterritorial financial crimes.²²³ Furthermore, Singapore has designated money laundering as an extraditable crime to allow international cooperation among law enforcement agencies in other jurisdictions.²²⁴

4.2.3 Best Practices study in Singapore

This is an assessment of the 2012 FATF recommendations, which have undergone many amendments since, with the latest amendments done in November 2023. The focus will be on evaluating these recommendations alongside the FATF Risk-Based Guidance provided for the real estate field in prevention of this financial crime. Then, further compare these international standards with the AML practices implemented in Singapore, specifically in the sphere of the property market.

The lack of carrying out CDD has been seen to be a primary contributor to money laundering and as such, it forms as one of the main elements of best practices in prevention of money

²¹⁹ <https://www.sla.gov.sg/regulatory/foreign-ownership-of-property> on 24 December 2023.

²²⁰ Choong S, Yeoh L and Chew Z, 'Additional Buyer's Stamp Duty ('ABSD') Rate Essentially Doubled for Foreigners and Non-housing-developer Entities Acquiring Singapore Residential Property' Withers worldwide, 2023,1.

²²¹ Laforga B, 'Singapore Tightens Rules on Foreign Property Ownership in Latest Market Restriction' Asia Real Estate Intelligence, 2023, 2.

²²² United Nations Office on Drugs and Crime, Country Review Report of Singapore, 10 April 2015, 11-13.

²²³ United Nations Office on Drugs and Crime, Country Review Report of Singapore, 10 April 2015, 10.

²²⁴ Financial Action Task Force, Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism - Singapore, 2008, 13-15,188.

laundering.²²⁵ Recommendation 10 emphasizes the importance of CDD that is also extended to the real estate sector under Recommendation 22.²²⁶ CDD involves confirming the customer's identity, verifying the identity of those benefiting from the funds, looking at the parties' relationship and a scrutiny of the transactions to determine the integrity of these transactions.²²⁷ This is not only applicable to estate agents but to the other parties involved in estate transactions such as the financial institutions including mortgage lenders and the legal and accountant professionals facilitating this process.²²⁸

In facilitating the CDD process the FATF risk-based guidance recommends that supervisory authorities in the real estate sector establish their own tools and methods since the independence helps avoid conflicts of interest with the other institutions involved.²²⁹ The said methods should be suitable for conducting CDD and must be implemented by skilled individuals with technical knowledge of these tools and methods.²³⁰ Moreover, the guidelines advocate for the use of Simplified Due Diligence (SDD) when the money risk is determined to be minimal while the presence of a third party in the transaction calls for Enhanced Due Diligence (EDD)²³¹ since more parties involved heightens the risk associated with such transactions.²³²

The guidelines acknowledge the difficulty of carrying out CDD in acquisition of property through virtual assets since the nature of the use of this currency does not only complicate the identification of the source of funds but also but also allows for global fund transfers without the involvement of a financial intermediary.²³³ Therefore, the guidelines prescribe that in the event that the

²²⁵ Sayılmanoğlu O, 'Customer Due Diligence by Financial Institutions as a Key Prevention Instrument', Financial Crimes Investigation Board, Research paper number 22/2012, 5 <https://www.osce.org/files/f/documents/4/0/87934.pdf> on 27 December 2023.

²²⁶ Financial Action Task Force, International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation, February 2012, 14,19-21.

²²⁷ Shah P, 'A complete guide to effective customer due diligence' AML UAE, 13 September 2023 <https://amluae.com/a-complete-guide-to-effective-customer-due-diligence/> on 27 December 2023.

²²⁸ Financial Action Task Force, International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation, February 2012, 19-20.

²²⁹ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 23.

²³⁰ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 23.

²³¹ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 41-42

²³² United Nations Office on Drugs and Crime, Risk of Money Laundering through Financial Instruments, 10 February 2010, 10.

²³³ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 30.

verification of funds proves difficult, a thorough assessment of the associated risks and the implementation of effective risk mitigation systems is to be carried out.²³⁴

4.2.4 Case study

Although the principles underscoring CDD are basic and objective, the difference in how they are applied is what sets a country apart. In this regard, Singapore's implementation of CDD can be considered to be its distinguishing feature.²³⁵ The MAS issued its own AML regime known as the MAS Directions (Notices on Prevention of Money Laundering). Notice 1014 within this framework mandates institutions to exercise CDD when dealing with customers.²³⁶ Additionally, notice 626 provides that institutions are required to comply with the AML regimes through a flexible CDD system that identifies customers and allows for review of customer information.²³⁷ Furthermore, institutions are required to show MAS evidence of continued adherence to CDD measures to avoid penalties and these reports are then used as a defence if found in violation of AML guidelines.²³⁸ The practical application of CDD in Singapore is thus demonstrated through the case study below.

The Estate Agents Act 2010 has also included the code of ethics and professional client care which mandates the estate agents to conduct specific measures of due diligence while carrying out their business, and also submit STRs to the CAD.²³⁹ Section 44E further provides for the penalties associated with contravention of the listed due diligence measures.²⁴⁰ This case study handled by the Council of Estate Agencies in Singapore looks into a real estate salesperson affiliated with PropNex Realty Pte Ltd who failed to perform CDD and forged the signature on the form detailing the customer's particulars.²⁴¹

²³⁴ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 30.

²³⁵ Financial Action Task Force, Mutual Evaluation Report, September 2016, 92-98.

²³⁶ Guideline 6, Monetary Authority of Singapore Act (MAS Notice 1014 of 2015)

²³⁷ Guideline 6.24, Monetary Authority of Singapore Act (MAS Notice 626 of 2015)

²³⁸ Monetary Authority of Singapore, Enforcement Report, June 2023, 7-9,12.

²³⁹ Section 44B, Estate Agents Act (2010).

²⁴⁰ Section 44E, Estate Agents Act (2010).

²⁴¹ Khoo R, 'Real Estate Salesperson Fined and Suspended for Forgery and Failing to Perform Checks to Prevent Money Laundering and Financing of Terrorism' Council for Estate Agencies, 31 October 2023 <https://www.cea.gov.sg/news-publications/ceanergy-blog/case-studies/real-estate-salesperson-fined-and-received-5-months-suspension-for-forgery-and-failing-to-perform-the-required-due-diligence-measures-to-prevent-money-laundering-and-financing-of-terrorism> on 10 January 2024.

Ms. Geraldine Teh was approached by an entity to assist in the sale of a property and proceeded to advertise the said property for sale. Considering that the seller was a legal person, Geraldine ought to have carried out the additional CDD requirement prescribed in handling transactions associated with legal persons.²⁴² Instead, she wrote down the particulars of the owner of the entity to evade the additional measures that are to be performed for a legal entity.²⁴³ Further, she indicated “not applicable” to the question asking for verification of the buyer’s particulars and further forged the signature on the CDD form which also constitutes as an offence under section 7 of the Code of Ethics & Professional Client Care for real estate agents.²⁴⁴ Consequently, Geraldine was sentenced to a fine of nine thousand dollars and a suspension period of five months by the Council of Estate Agencies Disciplinary Committee. This case informed the amendment to the Estate Agents Act that explicitly lists real estate salespersons to be required to conduct CDD rather than merely categorizing them as ‘persons involved in estate transactions.’²⁴⁵

4.3 Assessment of South Africa anti money laundering framework

The FATF has thirty-nine member states despite their AML recommendations being used in multiple jurisdictions. This is because countries adopt these recommendations through their affiliation with organizations and bodies collaborating with the FATF to combat money laundering.²⁴⁶ Kenya, although not formally a member of the FATF, aligns itself with its recommendations by virtue of its membership in the ESAAMLG which actively strives to ensure adherence and enforcement of the FATF recommendations..²⁴⁷ South Africa, however, stands as

²⁴² Guideline 6.8, Monetary Authority of Singapore Act (MAS Notice SFA03AA-N01)

²⁴³ Khoo R, ‘Real Estate Salesperson Fined and Suspended for Forgery and Failing to Perform Checks to Prevent Money Laundering and Financing of Terrorism’ Council for Estate Agencies, 31 October 2023 <https://www.cea.gov.sg/news-publications/ceanergy-blog/case-studies/real-estate-salesperson-fined-and-received-5-months-suspension-for-forgery-and-failing-to-perform-the-required-due-diligence-measures-to-prevent-money-laundering-and-financing-of-terrorism> on 10 January 2024.

²⁴⁴ Section 7, Code of Ethics & Professional Client Care for real estate agents (2010)

²⁴⁵ Khoo R, ‘Real Estate Salesperson Fined and Suspended for Forgery and Failing to Perform Checks to Prevent Money Laundering and Financing of Terrorism’ Council for Estate Agencies, 31 October 2023 <https://www.cea.gov.sg/news-publications/ceanergy-blog/case-studies/real-estate-salesperson-fined-and-received-5-months-suspension-for-forgery-and-failing-to-perform-the-required-due-diligence-measures-to-prevent-money-laundering-and-financing-of-terrorism> on 10 January 2024.

²⁴⁶ <https://worldpopulationreview.com/country-rankings/fatf-countries> on 10 January 2024.

²⁴⁷ <https://www.fatf-gafi.org/en/countries/global-network/eastern-and-southern-africa-anti-money-laundering-group-esaamlg.html> on 10 January 2024.

the only African nation within the FATF. The country became a member in 2003 following FATF's endorsement of its efforts which included the enactment of legislation specifically aimed at preventing financial crime.²⁴⁸ To strengthen its already robust framework, South Africa is also part of the ESAAMLG which works hand in hand with the FATF.²⁴⁹

4.3.1 The institutional framework

The main institution that acts as a regulatory body is the Financial Intelligence Centre (FIC) which is governed by the Financial Intelligence Centre Act (FICA). In collaboration with other law enforcement agencies, the FIC is tasked with ensuring adherence to AML guidelines outlined in FICA by exercising its supervisory role across various industries.²⁵⁰ The estate agents in South Africa are governed by the Estate Agency Affairs Act, however, this act does not explicitly reference AML guidelines or the obligations of estate agents in complying with reporting procedures.²⁵¹ Nevertheless, FICA, in the first schedule, lists estate agents among others as accountable institutions that should report STRs to the FIC.²⁵² Other bodies other than the FIC that ensure compliance primarily in the financial sector are, South African Reserve Bank, Financial Sector Conduct Authority and National Prosecuting Authority which prosecute criminal offences including money laundering.²⁵³

4.3.2 The legal framework

South Africa was approved to join the FATF after enacting FICA and the Prevention of Organised Crime Act of 1998 (POCA). This is because by doing so, it showed commitment in the fight against money laundering and terrorism financing.²⁵⁴ The FICA mandates listed accountable institutions to report cash transactions exceeding the prescribed limit of R24,999.99 (equivalent to 1,313 US

²⁴⁸ <https://www.fatf-gafi.org/en/countries/global-network/eastern-and-southern-africa-anti-money-laundering-group-esaamlg.htm> on 10 January 2024.

²⁴⁹ <https://www.fatf-gafi.org/en/countries/global-network/eastern-and-southern-africa-anti-money-laundering-group-esaamlg.html> on January 2024.

²⁵⁰ Section 5, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁵¹ Section 1, Estate Agency Affairs Act, (Act No 112 of 1976).

²⁵² First schedule, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁵³ International Monetary Fund, Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism, 24 September 2021, 128-134.

²⁵⁴ International Monetary Fund, South Africa: Report on the Observance of Standards and Codes— FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism, April 2004, 2-4.

dollars). This limit is lower than the 10,000 US dollars limit provided for in Kenya.²⁵⁵ This lower limit ensures increased enhanced scrutiny and can arguably be one of the grounds for South Africa's recognition in the prevention of financial crime.²⁵⁶ Additionally, Section 29 of this act also mandates reporting institutions to submit STRs to the FIC.²⁵⁷ The POCA allows for regulatory authority to seize property where there is reason to believe that the asset is or forms part of criminal proceeds.

4.3.3 Best practices study in South Africa

In light of the best practices established by FATF, this study will assess South Africa's compliance with these standards. In 2023, FATF grey-listed South Africa due to non-compliance with international regulations against money laundering.²⁵⁸ However, the country has demonstrated commitment to addressing the recommended strategic actions necessary to be removed from the grey list.²⁵⁹ Furthermore, in the mutual evaluation report, South Africa had 67 recommended actions that required resolution as per the follow up mutual evaluation only eight action points were not actualized.²⁶⁰ This prompt response to FATF recommendations, including the establishment of entities like the Fusion Centre that aided in the recovery of over 1 billion in assets, and consistent reporting of progress to FATF, makes it a suitable subject for this study.²⁶¹

The 2022 amendment to FICA incorporated a risk-based approach in alignment with the recommendations, as outlined in the report 'Guidance for a Risk-Based Approach to the Real Estate Sector.'²⁶² This approach involves assessing the risk within each sector and implementing

²⁵⁵ Section 28, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁵⁶ Financial Action Task Force, FATF (Financial Action Task Force) Countries 2022, 2022 <https://worldpopulationreview.com/country-rankings/fatf-countries> on 10 January 2024.

²⁵⁷ Section 29, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁵⁸ <https://www.fatf-gafi.org/en/publications/High-risk-and-other-monitored-jurisdictions/Increased-monitoring-october2023.html#:~:text=When%20the%20FATF%20places%20a,as%20the%20%E2%80%9Cgrey%20list%E2%80%9D.> on 12 January 2024

²⁵⁹ International Finance Corporation, 'South Africa Adopts Anti-Money Laundering Measures To Exit Global Watchdog's Grey List' Name of Newspaper, 1 December 2023 <https://www.ifcreview.com/news/2023/december/africa-south-africa-adopts-anti-money-laundering-measures-to-exit-global-watchdog-s-grey-list/#:~:text=FATF%2C%20the%20global%20watchdog%20with,terrorism%20financing%20and%20proliferation%20financing> on 12 January 2024.

²⁶⁰ Financial Action Task Force, South Africa's :2nd Enhanced Follow-up Report, November 2023, 5-8.

²⁶¹ Corporate & Commercial Law Alert, Understanding South Africa's FATF grey listing, 29 March 2023, 12.

²⁶² Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022,25-27.

EDD for transactions with identified high risk, and SDD for those with minimal risk.²⁶³ This amendment goes a step further to mandate estate agents to look at the risk associated with each transaction taking into account specific circumstances rather than merely considering the monetary value involved.²⁶⁴ The amendment also introduces the Know Your Customer (KYC) which is much like the CDD provision only that this does not merely look at risks associated with the customer as CDD does but looks at the entire profile associated with a customer.²⁶⁵ This risk-based approach comprises of three essential steps: **preventing** the involvement of illicit funds in transactions, **detecting** such funds, and **reporting and recording** their use to the relevant authorities.²⁶⁶

4.4 Conclusion

This comparative study of AML practices demonstrates the strengths in the frameworks of both Singapore and South Africa as compared to Kenya. Singapore's institutional framework, and strict legal regulations accompanied by its stringent penalties contribute to its effectiveness in combating financial crime. South Africa also shows its commitment to ensure continuous improvement by its robust framework and quick responses to FATF recommendations.²⁶⁷ Kenya, like South Africa, found itself on the grey list in 2010 and exited after four years but South Africa has already demonstrated remarkable progress and is expected to be removed from the list within a year.²⁶⁸ Additionally, the lower cash transaction reporting limit in South Africa enhances regulation while Kenya moves against this enhanced regulation by increasing the already high limit.²⁶⁹ As Kenya seeks to enhance its AML regime, insights from South Africa and Singapore serve as a good place to start in this endeavour.

²⁶³ Financial Action Task Force, Risk Based Approach Guidance for the Real Estate Sector, July 2022, 41-42

²⁶⁴ Section 42, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁶⁵ Section 1, Financial Intelligence Centre Act, (Act No 38 of 2001).

²⁶⁶ International Monetary Fund, Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism, 24 September 2021, 106-120.

²⁶⁷ Financial Action Task Force, South Africa's 2nd Enhanced Follow-up Report, November 2023, 10-38.

²⁶⁸ Financial Sector Conduct Authority, Tougher Stance to Combat Money Laundering and Terrorist Financing, 24 February 2023, 1-3.

²⁶⁹ Section 196, The Anti-Money Laundering and Combating of Terrorism Financing Laws (Amendment) Bill 2023

CHAPTER FIVE

FINDINGS, RECOMMENDATIONS AND CONCLUSION

5.1 Findings

The study identifies several key findings regarding the susceptibility of Kenya's real estate industry to money laundering. Despite being a vital contributor to the country's GDP and a symbol of economic growth, the real estate industry faces certain vulnerabilities and therefore, this research has looked into the process of movement of illicit funds as carried out in Kenya's estate sector.

The placement stage is where funds enter the financial system and, in this stage, this study discusses methods like 'smurfing' and indirect placement through property acquisition, showing the need for Kenya to reevaluate transaction thresholds for properties. The study further explores the layering stage, a phase in money laundering that is characterized by efforts to distance illicit funds from their original source, often facilitated through hawalas and legitimate third-party entities. The integration stage is highlighted as the point where real estate becomes exceptionally vulnerable to financial crime. During this stage, laundered funds are reintroduced into the financial system, strategically directed towards acquiring luxury assets or invested in seemingly legitimate businesses.

The study also identifies factors enabling financial crime in the estate industry, including regulatory gaps between POCAMLA and the Estate Agents Act, a lack of oversight on various industry participants, and a legal system less inclined to pursue money laundering cases. The study also explores the negative impacts that extend to Kenya's global standing, which risk the FATF's scrutiny and reinstatement into the grey list. Additionally, the legislative and institutional framework, particularly concerning reporting obligations for specific professions and businesses, appears to have gaps. Sectors such as real estate agents lack explicit guidance on meeting reporting obligations, raising concerns about compliance and potential data protection issues. The study also highlights challenges in the oversight of the estate agents as the Estate Agents Regulatory Board lacks official anti-money laundering guidelines for them, indicating a regulatory vacuum.

Singapore has a strong focus on Customer Due Diligence and the stringent penalties for violations which contribute to its effective anti-money laundering system. South Africa's system is

characterized by a robust institutional framework led by the Financial Intelligence Centre governed by the FICA. The 2022 amendment to FICA aligns with FATF recommendations, introducing a risk-based approach that mandates estate agents to assess transaction risks individually. The lower cash transaction reporting limit in South Africa enhances regulation and scrutiny, contrasting with Kenya's decision to increase its already high limit. Kenya faces gaps in its legislative and institutional frameworks, as evidenced by the preceding chapters.

5.2 Recommendations

5.2.1 Key Legislative amendments

The Estate Agents Act should undergo amendments to explicitly incorporate anti-money laundering provisions, outlining clear responsibilities and consequences for non-compliance among estate agents. These changes aim to enhance the legislative framework, including measures such as further lowering the recently raised threshold for reporting cash transactions. Additionally, in the event that assets seized by the Asset Recovery Agency during declaration at customs and are determined to be legitimate, the legislation should be revised to explicitly specify the next course of action to ensure that they not only get to the rightful owner but are not subject to any corruption scheme. Additionally, to counteract the practice of 'smurfing,' during this declaration, where money launderers exploit the amount loophole to transfer money exceeding prescribed limit without declaration, the law should be refined. This refinement can be achieved by either setting limits on the frequency of money transfers or ensuring that the prescribed limit applies not just once but to every transaction within a defined time period.

5.2.2 Comprehensive regulatory overhaul

There is a need to expand the regulatory framework, granting increased authority to the Estate Agents Registration Board to enforce anti-money laundering measures in real estate not only to estate agents but to all who participate in real estate transactions including brokers and salespersons. The Board should also be authorized to formulate comprehensive anti-money laundering guidelines specific to estate agents. These guidelines would precisely outline key AML compliance aspects, including customer due diligence, reporting obligations, and collaboration with regulatory bodies. To ensure effective implementation of these guidelines, specialized training programs should be held for estate agents and all other concerned parties. The Financial

Reporting Centre should be amended to establish a cohesive reporting structure and stringent oversight mechanisms to ensure accountability, Additionally, an external body to be mandated to conduct assessments of reports submitted to the FRC to ensure that they are of proper standards. To expedite the resolution of money laundering cases, the Financial Reporting Centre should institute a dedicated task force with quasi-judicial functions. This is because, they not only have substantial knowledge derived from receiving reports, but also this approach will streamline the adjudication process and alleviate the backlog of pending cases.

5.2.3 International cooperation

This study has established that money laundering incidences in Kenya often involves cross-border transactions and this necessitates international cooperation. Kenya therefore should strengthen collaboration with global financial intelligence units, law enforcement agencies, and international bodies to share information and coordinate efforts. Financial crime is an extraditable offence in Kenya and therefore the country has shown intention to increase international cooperation. However, to further enhance these efforts, Kenya should actively engage with international partners, particularly by seeking membership in the FATF rather than merely considering their recommendations. This is because active participation in this task force would significantly contribute to information exchange on money laundering activities and Kenya would also benefit from intelligence-sharing agreements among different countries as established by this organization.

5.3 Conclusion

This study has conducted a deep dive into the legislative and institutional framework of Kenya in determining the reason for the prevalence of financial crime in the real estate industry. A set of specific legislation tailored to real estate agents is needed in order to ensure implementation of effective measures with regards to real estate agents and all participants involved. Additionally, the mandate of the Estate Agents Registration Board should be expanded to curb financial crime in Kenya's real estate industry by harmonizing their laws with that of the POAMLA and ensuring that reporting obligations to the FRC are met.

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