

# **Terrorist Financing**

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## **I. EXECUTIVE SUMMARY**

Terrorist finance is an area of major concern for the US Government. The events of September 11<sup>th</sup> led to an acceleration of efforts in counter-terrorism, including increased attention to issues involving terrorists' financial backing. This report seeks to describe current US efforts in terrorist financing, highlight concerns with that approach and make policy recommendations. The current approach involves a complex web of legislation, with responsibility shared between multiple agencies, each approaching the problem in a different way. We recommend improvements in inter-agency coordination through cleaner chains of command, improvements in data collection and an ongoing focus on multilateral efforts to achieve international standards for monitoring terrorist financial activities.

## **II. BACKGROUND**

By Justin Delacruz

Efforts to track terrorist financing have been an area of concern for the US government since the middle of the second Clinton administration, but the events of September 11<sup>th</sup> 2001 threw the necessity of quick action into sharp relief. Since then, the scale of government efforts has increased considerably. However, this has added further complexity to an already muddled system of oversight and responsibility, with many sites of legislative authority and multiple agencies responsible for creation, implementation and oversight of policy.

Global terrorism is currently dominated by Al-Qaeda and its disparate worldwide franchises and emulators. Osama bin Ladin is a rich financier unlike other terrorist leaders who tend to be military heroes, religious authority, or a representative of the downtrodden and disillusioned. He built al-Qaeda's financial network on a series of layers and redundancies. Its

most important source of money comes from continuous fundraising efforts. This fundraising network includes nongovernmental organizations, charities, mosques, websites, intermediaries, facilitators, banks and other financial institutions. One example of funding from mosques comes from the Islamic obligation of making regular charitable donations. *Zakat* is the religious duty for all Muslims to give at least 2.5% of their income to humanitarian causes.<sup>1</sup> Al Qaeda operates under a veil of legitimacy including businesses created by bin Laden in Sudan, as well as honey traders in Yemen that the U.S. recently identified as part of al Qaeda's financial network. It also earns money through criminal enterprises ranging from the heroin trade to smuggling, fraud, and theft.

By using the underground *hawala*, global financial banking, and Islamic banking systems, al-Qaeda moves its money. Al-Qaeda has been particularly attracted to global banks operating in under-regulated jurisdictions, places with limited bank supervision, no anti-money laundering laws, ineffective law enforcement institutions, and a culture of no-questions-asked bank secrecy. Many Islamic banks function under lax regulatory oversight for two reasons. First, they are stationed in jurisdictions without proper controls. Second, its religious nature allows Islamic banks to operate with a great deal of autonomy. The *hawala* system needs only a network of *hawaladars*, trust, and open phone lines. It is a cash business that leaves very few transaction records for investigation. Staffed primarily by family member that have been in the business for generations, it is quick, efficient, reliable, and inexpensive. This system is used by millions of law-abiding citizens, but its nature makes it susceptible to abuse by criminals and terrorists. Customers in one city hand their local *hawaladar* some money; the individual then contacts his counterpart across the world, who in turn distributes the money out of his own

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<sup>1</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 7.

resources to the intended recipient. Critical to the function of this system is the trust between the two *hawaladars* who tend to be related through familial, clan or ethnic associations. This allows them to carry each other's debts for long periods of time.<sup>2</sup>

When these modes of transporting money are not available, al-Qaeda has the option of moving money physically. The Middle East provides a perfect environment for this type of money transfer due to its weak border controls and its cash-based culture. Moreover, it moves its assets in the form of precious metals and gemstones. It uses the traditional smuggling routes and methods of drug traffickers and arms dealers.

Legislation on terrorist financing has been circulated around anti-money laundering laws. Money laundering has traditionally been known as the method of disguising "dirty" money produced by illegal activity as legitimate money through its distribution via financial institutions. Legislative action includes the Bank Secrecy Act, the International Emergency Economic Powers Act, the Money Laundering Control Act, the Annunzio-Wylie Anti-Money Laundering Act, the Money Laundering Suppression Act, the Money Laundering and Financial Crimes Strategy Act, Title III of the USA Patriot Act, the Suppression of the Financing of Terrorism Convention Implementation Act, the Intelligence Reform and Terrorism Prevention Act of 2004.

The Bank Secrecy Act concentrates on financial institutions' record-keeping in order to apprehend criminals by tracing their money trails. The International Emergency Economic Powers Act provides the President with broad powers to declare a national emergency with regard to a threat which has its source outside the United States to the national security, foreign policy, or economy of the United States. Powers include the ability to seize foreign assets under U.S. jurisdiction, to restrict any transactions in foreign exchange, to prohibit payments between

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<sup>2</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 5.

financial institutions involving foreign currency, and to prohibit the import/export of foreign currency. This act gives authority to Executive Order 13224 which empowers the US Government, through the Departments of Treasury and State, to freeze assets of designated terrorist organizations.

Money laundering is a chief concern in U.S. efforts to combat terrorist financing. Congress criminalized money laundering with the passage of the Money Laundering Control Act in 1986. The Annunzio-Wylie Anti-Money Laundering Act increased consequences for depository institutions that violate the federal anti-money laundering laws. It also authorized the Secretary of the Treasury to mandate filings of Suspicious Activity Reports and gave the Office of the Comptroller of the Currency (OCC) the power to retract charters of national banks found guilty of money laundering and cash reporting offenses. Furthermore, it gave the Federal Deposit Insurance Corporation (FDIC) the authority to terminate federal insurance for guilty state banks and savings associations. The Money Laundering Suppression Act mandated certain exemptions from reporting requirements in an effort to reduce the number of currency transaction reports filings by 30%. It also directed the Treasury Secretary to designate a single agency to receive suspicious activity reports filings.<sup>3</sup> The Money Laundering and Financial Crimes Strategy Act directed the Treasury Secretary to develop a national strategy for combating money laundering. Part of this strategy is the responsibility of the Treasury Secretary to prioritize money laundering enforcement efforts by identifying areas of the U.S. as “high-risk money laundering and related financial crimes areas” (HIFCAs).

Under Title III of the USA Patriot Act, the Treasury Secretary may require domestic financial institutions to undertake certain “special measures” if the Secretary concludes that

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<sup>3</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. (Washington, D.C.: Library of Congress, 2005). Page 5.

specific regions, financial institutions, or transactions outside of the United States are of primary money laundering concern. These special measures include obtaining information on beneficial ownership of accounts and information relating to certain payable-through and correspondent accounts. The Treasury Secretary is also empowered to prohibit or restrict the opening of these payable-through and correspondent accounts, and U.S. financial institutions are required to establish internal procedures to detect money laundered through these accounts.<sup>4</sup> Also, financial institutions and broker-dealers are prohibited from maintaining correspondent accounts for foreign “shell banks,” i.e., banks that have no physical presence in their supposed home countries. The Suppression of Financing of Terrorism Convention Implementation Act made it a crime to collect or provide funds to support terrorist activities (or to conceal such fund-raising efforts), regardless of whether the offense was committed in the United States or the accused was a United States citizen. With the passage of the Intelligence Reform and Terrorism Prevention Act of 2004, Congress authorized the appropriation of \$16.5 million for the development of FinCEN’s “BSA Direct” program, which is designed to improve the network by making it easier for law enforcement to access BSA filings and improving overall data management.<sup>5</sup>

The nation’s financial institutions, their regulators, and certain offices within the U.S. Department of the Treasury share primary responsibility for providing information on financial transactions that could help in detecting, disrupting, and preventing the use of the nation’s financial system by terrorists and terrorist organizations. Offices within the Treasury include the Office of Terrorism and Financial Intelligence that is in charge with developing and implementing strategies to counter financing and money laundering both domestically and

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<sup>4</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 6.

<sup>5</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 8.

internationally. Two offices with anti-terrorist financing responsibilities within TFI are the Office of Foreign Assets Control and the Financial Crimes Enforcement Network (FinCEN). FinCEN originated as the data-collection and analysis bureau for the BSA. It provides a government-wide, multi-source intelligence network under which it collects Suspicious Activity Reports and Currency Transaction Reports from reporting financial institutions, tabulates the data in a large database that has been maintained since 1996, and examines them to detect trends and patterns that might suggest illegal activity. It then reports what it finds back to the financial community as a whole to aid further detection of suspicious activities. The Office of Foreign Assets Control is primarily intended to administer and enforce economic sanctions against targeted foreign countries, groups, and individuals, including suspected terrorists, terrorist organizations, and narcotics traffickers.<sup>6</sup> It acts under general presidential wartime and national emergency powers as well as legislation, to prohibit financial transactions and freeze assets subject to U.S. jurisdiction. The Office of the Comptroller of the Currency is the regulator for just over 2,000 nationally chartered banks and the U.S. branches and offices of foreign banks. Along with the OCC, the Federal Reserve System supervises some international activities of national banks. It also supervises state-chartered commercial banks that are members of the system and bank and financial holding companies. The IRS collects and analyzes financial intelligence, diplomatic pressure, regulatory actions, administrative sanctions, and criminal investigations and prosecutions. Within the Department of Homeland Security, the role of the Bureau of Customs and Border Patrol lies in inspection and interdiction activities along the border and at or between ports of entry. Other agencies such as the United States Secret Service

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<sup>6</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 16.

and the Federal Bureau of Investigation have minor roles in U.S. efforts to combat terrorist financing.

## II. PROBLEMS WITH CURRENT STRATEGY

By Cameron McKenzie

Combating the flow of money into terrorist organizations is an especially problematic part of the US government's anti-terrorism strategy. The following section of this white paper identifies defects and difficulties within the current system and strategy.

### *The Scale of the Problem*

The scope and scale of money transfer in the international economy is overbearingly large. Within that system, terrorist financing is a minutely small part. The cost of financing terrorism is small, even relative to everyday business expenses. For example, the cost of carrying out a terrorist attack is estimated to be in the range of \$10,000 to \$2,000,000.<sup>7</sup> In contrast, the estimated amount of money laundered each year worldwide is between \$500 billion and \$1 trillion.<sup>8</sup> Even this amount pales in comparison with the total volume of money moved inter-jurisdictionally through ordinary financial transactions. Despite these problems, it has been possible to use financial reporting to trace back the flow of terrorist money after a terrorist event, particularly in the Madrid bombings and after September 11.<sup>9</sup> However, these case by case ex post analyses do little to prevent attacks and provide minimal data with which to evaluate the true sensitivity and specificity of the algorithms we use to identify terrorist money. As in many

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7 Maurer, Steve. *Lecture 3*. UC-Berkeley.

8 Stana, Richard M. *Investigating Money Laundering and Terrorist Financing: Federal Law Enforcement Agencies Face Continuing Coordination Challenges*. (Washington, D.C.: General Accounting Office, 2004). Page 1.

9 "The Lost Trail." *The Economist*. October 22<sup>nd</sup>, 2005. Page 15.

other areas, the lack of human intelligence makes the problem more difficult. Flows of terrorist money could be better identified through specific information from within terrorist cells rather than using ‘brute force’ algorithms and record keeping.

### *Competing Imperatives*

Competing imperatives regarding the identification and treatment of terrorist money compound the difficulties associated with formulating policy in this area and create problems within the US government's systems. On the one hand, terrorist activities require money, creating an imperative to freeze assets and dry out funding. On the other hand, the long term prevention of terrorist attacks will be achieved through better intelligence. Many argue that such intelligence can be obtained by tracing the flows of money that has been identified as terrorist money. Clearly, this logic dictates that assets are not frozen. Current stated policy favors tracing money<sup>10</sup> but that policy has not been pursued consistently. Assets have been frozen on several occasions.<sup>11</sup> It is not clear what metric, if any, is used to decide when to freeze money and when to trace.

### *Competing Agencies and Authority*

The problem of competing imperatives is compounded by the diffuse responsibility that exists within the area of terrorist financing. Multiple agencies operate under different paradigms and different sources of authority, including legislation and executive orders. As it currently stands, responsibility for creating and implementing elements of terrorist financing policy is

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10 Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page

11 Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page

shared across: the Department of Treasury; the Department of Homeland Security, including the Bureau of Immigration and Customs Enforcement and the Bureau of Customs and Border protection; the Department of Justice, including the Federal Bureau of Investigation, the US Secret Service, the Bureau of Alcohol, Tobacco and Firearms and the Drug Enforcement Agency; the Department of State; all US intelligence gathering organizations including the Central Intelligence Agency and the National Security Agency.<sup>12</sup> There is no single chain of command to evaluate issues concerning terrorist financing. Further, each agency is likely to reflexively operate according to its core competency. For example, intelligence agencies are likely to trace money and law enforcement agencies are likely to freeze assets and attempt to bring criminal charges. There is no process or structure for cross-agency decision making and in the absence of such a process decisions about tactics and strategy, such as whether to trace or freeze, the best way to monitor money flows, etc, will be done in a piecemeal manner, according to which agency first identifies terrorist moneys, rather than systematically and in keeping with a coherent national strategy.

Further, as the complex nature of the problem requires multiple competencies, information sharing and joint problem solving, the absence of a mechanism through which to achieve this is a major concern. For example, although the Department of Treasury collects large amounts of data in the form of Suspicious Activity Reports (SARs), intelligence and law enforcement agencies do not automatically gain access to such data. Instead, they must request it.<sup>13</sup> Consequently, agencies whose core competencies include refining metrics and algorithms to identify criminal and terrorist activity do not have easy access to the information which would allow them to do this.

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12 "The Lost Trail." *The Economist*. October 22<sup>nd</sup>, 2005. Page 15.

13 Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page

### *An International Problem – Cross-Jurisdictional Regulation*

The US has an interest in protecting civilians and assets outside its geographic territories from terrorist activity. Also, terrorist money which ultimately ends up within the US is likely to travel through multiple other jurisdictions beforehand. Consequently, there is a need for international cooperation and information sharing in combating terrorist finance. All the problems of inter-agency cooperation and information sharing exist also on an international scale, but with further difficulties and fewer mechanisms for resolving the problem. Firstly, the US can only change international processes and norms by exerting diplomatic pressure. Whilst it has been effective in gaining international cooperation with many allies, terrorists may simply go to jurisdictions where reforms have not been implemented. Secondly, even in states that appear to be cooperating, it can be difficult to evaluate the level of competence of agencies involved in implementing international strategies on terrorist financing. The US is trying to solve this problem through collaboration and funding<sup>14</sup> but it is difficult to evaluate the effectiveness of this strategy.

### *An International Problem – Money Laundering Jurisdictions*

The U.S. faces a specific problem in monitoring flows of money through any of several money laundering jurisdictions. Many small countries, such as the Channel Islands, Seychelles, the British Virgin Islands and the Seychelles, finance their economies by running opaque but secure financial institutions, taking advantage of wealthy companies and individuals seeking tax evasion and criminal and terrorist groups wishing to transact anonymously and without

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14 “The Lost Trail.” *The Economist*. October 22<sup>nd</sup>, 2005. Page 15.

detection. The continued existence of economies based on this process is a significant threat to any effort to track terrorist finance. However, the small scale of much terrorist financing works against terrorist groups in many of these jurisdictions, as most money laundering jurisdictions are only willing to transact with large amounts of money, often between \$1-10 million dollars.<sup>15</sup>

#### *Alternative Channels – Hawala and Suitcases*

Transactions and money movement entirely outside the normal channels for movement of money threatens the ability of the US to monitor movement of terrorist money. Hawala is a traditional system for transferring money used in much of the Muslim world. Based on reciprocal trust, it involves no engagement with the financial system as it is normally conceived in the U.S.<sup>16</sup> Thus it is virtually impossible to monitor or regulate in the absence of specific intelligence. Also falling outside financial regulatory reach, large sums of cash can be moved physically, on the person of a courier or similar. Whilst this may be detected by customs agents, this is far from guaranteed.

#### *The Reporting Burden*

Finally, there is a significant concern about the burden of regulatory compliance on financial institutions.<sup>17</sup> The cost of compliance with regulator's requests for SARs and other monitoring and security burdens becomes very large when scaled across the entire US and global financial systems. In the absence of useful metrics for effectiveness, it is difficult to evaluate whether the regulatory burden outweighs the benefit. Whatever the case, the large cost to

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15 Personal Communication, Dr Geoff Stapleton, University of Melbourne Law School.

16 "The Lost Trail." *The Economist*. October 22<sup>nd</sup>, 2005. Page 15.

17 "The Lost Trail." *The Economist*. October 22<sup>nd</sup>, 2005. Page 15.

financial institutions and the concomitant reduction in market efficiency should be taken into account when evaluating terrorist financing regulation.

#### **IV. THE DOMESTIC RESPONSE TO TERRORIST FINANCING**

By Ian Richardson

The response of the federal government to terrorist financing issues has been plagued not by a lack of congressional authority to track terrorist financing, but by a lack of a unified command structure for the enforcement of existing statutes. Although problems of federal coordination are not unique to the campaign against terrorist financing within the global war on terrorism, the campaign against terrorist financing also requires an impressive degree of coordination between the private sector and multiple federal agencies. Private sector financial institutions provide most of the intelligence used by the federal government to track terrorist finances. The two most important factors influencing the domestic response to terrorist financing are the ability of federal agencies to effectively coordinate enforcement and intelligence efforts, and the ability of the federal government to coax financial institutions into providing useful and timely information that can be analyzed and used to track terrorist finances. This paper assesses current problems with the domestic response to terrorist financing and proposes a series of general steps the federal government could take toward improving federal intelligence and enforcement capabilities.

The current structure of federal terrorist finance enforcement and intelligence efforts is extremely complex and involves not only a variety of federal agencies but multiple overlapping inter-agency working groups as well. The National Security Council (NSC) operates a Terrorist Financing Policy Coordinating Committee (PCC) which receives regular reports from the multi-

agency Foreign Terrorist Asset Targeting Group (FTATG) under the direction of the new Director of National Intelligence (DNI).<sup>18</sup> The Federal Bureau of Investigation (FBI) created a multi-agency Terrorist Financing Operations Section (TFOS) directed by an FBI section chief, and an Immigration and Customs Enforcement (ICE) deputy section chief. ICE had originally been part of the Treasury Department as the U.S. Customs Service but the creation of the Department of Homeland Security (DHS) led to the transfer of customs enforcement activities from Treasury to DHS with the move of Customs to DHS.<sup>19</sup> The Treasury Department operates a Financial Crimes Enforcement Network (FinCEN) that collects data from private sector financial institutions, and also uses information collected by the Internal Revenue Service (IRS) to identify potential terrorist activities and funds. The Treasury Office of Terrorism and Financial Intelligence (OTFI) is responsible for running FinCEN as well as the Office of Foreign Assets Control (OFAC) and the Executive Office for Asset Forfeiture (EOAF).<sup>20</sup>

The problem with the number of agencies involved in tracking terrorist financing is that they report to a multitude of different political policymakers within the executive branch. These decision makers are forced to make policy based on only the information and expertise made available to them by the agencies accountable to them. Although inter-agency working groups such as the PCC have tried to remedy the situation by bringing senior staff in from a broad range of agencies in groups such as the FTATG the lack of a clear decision maker on issues of terrorist financing and the institutional biases of the intelligence community have served to undermine its effectiveness. One of the major debates over terrorist financing is whether terrorist finances

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<sup>18</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 9.

<sup>19</sup> Stana, Richard M. *Investigating Money Laundering and Terrorist Financing: Federal Law Enforcement Agencies Face Continuing Coordination Challenges*. (Washington, D.C.: General Accounting Office, 2004). Page 4.

<sup>20</sup> Organizational Chart. Department of the Treasury. Accessed December 3, 2005.

<[http://treasury.gov/organization/secorgchart\\_7-21-05.pdf](http://treasury.gov/organization/secorgchart_7-21-05.pdf)> and Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 15-17.

should be tracked for purposes of locating terror cells and groups and physically disrupting their operations, or for the elimination of financial resources so that terrorist groups are unable to carry out operations.<sup>21</sup> While the intelligence community favors locating potential terrorist groups through the use of financial intelligence, law enforcement agencies such as the FBI would likely seek to freeze terrorist assets in order to prevent an attack from occurring. Currently, law enforcement officers can request that OFAC work with the State Department to freeze foreign assets, but there is no clear decision maker with responsibility for considering both the intelligence and law enforcement implications of asset seizure.<sup>22</sup>

Although Congress attempted to solve similar problems in the federal approach to domestic defense with the creation of the cabinet level DHS, the less than ideal results produced by this merger of several major federal agencies casts doubt on the viability of a similar proposal for the direction of federal policy on terrorist financing. Additionally, the Council on Foreign Relations recommendation that a Special Assistant to the President be given authority for organizing the federal government to deal with terrorist financing would fail to provide a real solution to existing inter-agency conflicts, it would simply add one more link in the chain of command.<sup>23</sup> To remedy inter-agency conflicts and centralize federal policy and decision making, we propose that the Treasury Department be designated as the principal federal agency in the federal strategy on terrorist financing. The Secretary of the Treasury or his designee, preferably the Undersecretary for OTFI, would have responsibility for centralizing all data available to the federal government on terrorist financing in one central location and would have final authority

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<sup>21</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 49.

<sup>22</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 39.

<sup>23</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 31.

to determine the most appropriate use of that information. Additionally, we propose that the intelligence community, the State Department, and the IRS establish on-site liaison offices within the OTFI and that the TFOS be located on-site at the offices of the OTFI and be placed under the operational direction of the Undersecretary, thereby placing the full resources of the law enforcement community at the disposal of the OTFI.

These two recommendations take advantage of the vast experience of the Treasury Department with financial matters and provide major policy players significant roles in helping Treasury formulate policy and bring their resources and information to bear on tracking terrorist financing. The experience of organizations such as the IRS in tracking money laundering activities combined with the global resources of the law enforcement and intelligence communities would significantly improve the availability of relevant information while holding agencies accountable to a single decision maker with the authority to decide when and if to seize assets or continue tracking terrorist activities.<sup>24</sup> In this organizational structure, the law enforcement and intelligence communities would be forced to share important intelligence or risk losing the favor of the decision maker responsible for deciding whether to seize terrorist assets or permit them to be tracked to their sources, thus putting an end to many of the conflicts plaguing current enforcement.

Private sector financial institutions are the primary source of intelligence on terrorist financing. Under federal law these institutions are currently responsible for collecting and reporting the vast majority of information on terrorist financing.<sup>25</sup> According to a report created by the Congressional Research Service, the Inspector General of the Department of the Treasury

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<sup>24</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 23.

<sup>25</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 14.

has concluded that the information provided by financial institutions to the government's financial crime information database, FinCEN, is frequently plagued by inaccuracies and contains less than ideal amounts of information for law enforcement and intelligence agencies to use as leads.<sup>26</sup> The FBI meanwhile, through its TFOS, has accumulated significant domestic and international contacts that provide financial data and information through alternative channels almost in real-time compared to the somewhat cumbersome FinCEN.<sup>27</sup>

Effective financial intelligence efforts require significant amounts of raw data and the ability to analyze the data effectively to detect potentially illegal activities. Unfortunately, the burdens associated with meeting the federally mandated standards for financial information collection and reporting mean that financial institutions have an incentive to pass along only a bare minimum of information in order to minimize costs. Though the Treasury Department has recently created an online secure filing system for financial institutions to make electronic suspicious activity reports (SARs), the Inspector General has determined that information is still lacking.<sup>28</sup> We recommend that the federal government partner with major financial institutions and invest in the creation of integrated reporting software. By automatically retrieving information from the databases of financial institutions the software could speed the creation of SARs, reduce the number of inaccuracies, increase the amount of information conveyed to the federal government and decrease the amount of financial institution personnel input required for their creation. Although increased efficiency in the submission of federally mandated SARs funded by the federal government would likely be sufficient to achieve financial institution

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<sup>26</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 16.

<sup>27</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 38.

<sup>28</sup> Weiss, Martin A. Congressional Research Service. *Terrorist Financing: U.S. Agency Efforts and Inter-agency Coordination*. Page 16.

cooperation, additional measures such as tax incentives and new legislation could be used to compel institutional cooperation with the federal government. However, the goal should be to increase financial institution cooperation by reducing their reporting burden instead of adding more stringent requirements.

With an increase in SARs submitted by financial institutions, the addition of TFOS and intelligence community financial information from the implementation of the preceding recommendations, new capability to analyze vast amounts of financial data would be required to create actionable financial intelligence. We recommend that the federal government contract with a private sector firm that specializes in data mining and electronic search software in order to create analysis tools capable of real-time identification and tracking of terrorist financial transactions. The evolution of commercial search and data mining capability means that automated tools created with private sector expertise could significantly improve the ability of the Treasury Department to identify and track *all kinds* of illegal financial activities, not just terrorist activity.

## **V. THE INTERNATIONAL RESPONSE TO TERRORIST FINANCING**

By Katie Veazey

Combating terrorist financing requires more than a strong domestic policy for the United States, but also requires a focused international strategy. Currently, there exists a lack of political will among U.S. allies to combat terrorist financing,<sup>29</sup> therefore, the United States needs to take an active role in organizing and designing a cooperative international strategy that nations should adopt in order to stop terrorism at its financial root.

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<sup>29</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 2.

The Treasury Department will not only head the domestic terrorist financing policy but also take on the role as the U.S. delegate for the international community. Treasury will adopt a strategy that directs the State Department to utilize the United States' power as an international leader to push the combating of terrorist financing to the forefront of the international community's agenda. Strong U.S. leadership in such delegations such as the Group of Seven (G-7) and United Nations could heavily influence the international community to expand the fight against terrorism with an increased focus on terrorist financing.<sup>30</sup> With the proper resources and teamwork, the U.S. could also push for the establishment of an international organization which specifically investigates terrorist financing and establishes mandates and sanctions for countries that do not have proper anti-money laundering policies. The United States should also continue to enforce and utilize the International Emergency Economic Powers Act and the Patriot Act which restrict or prohibit access to the U.S. financial system to state and individual foreign financial institutions that lack adequate anti-money laundering controls.<sup>31</sup> These two acts allow for The Treasury Department to have legal and economic backing by the U.S. government to carry out the fight against terrorism financing on an international scale.

Thus far, many foreign governments have welcomed and cooperated with the United State's initiative to combat terrorist financing, but a stronger set of international standards that define and establish the criterion for a secure financial system, including how governments regulate charitable organizations, are needed. It is imperative that nations such as Saudi Arabia and Pakistan build anti-money laundering regimes that are consistent with international standards, as much of al Qaeda's fundraising efforts have been particularly concentrated in

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<sup>30</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 4.

<sup>31</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 23.

nations with limited bank supervision and few or no anti-money laundering laws. A set of international banking standards would allow for the global community to be able to publicly evaluate each nation, especially those in the Middle East, on the security of their financial system, and therefore create a system in which terrorist's would have little capability to finance themselves via legal and credible financial institutions.<sup>32</sup>

In addition to creating a set of international financial standards, a multilateral approach should be used to create a system which attempts to regulate the *hawala* and charitable organizations. The hawala system and other similar alternative banking systems are almost entirely unregulated around the globe, including in the United States.<sup>33</sup> Al Qaeda, and other terrorist groups, often use this unregulated, transient, familial system to finance their organizations, as do normal citizens, so a global registry and regulatory system should be created that attempts to track and monitor the *hawala*. Along with the *hawala*, a list of reputable charitable organizations or a "white list" should be created, alongside a "black list" of charities which have or have had terrorist ties.<sup>34</sup> By creating a list of charitable organizations and credible *hawalas*, the international community would be able to more easily track and monitor terrorist's finances, while also examining the legitimacy of each organization.

The international community also must come together to combat terrorist financing by creating a system of information sharing amongst leading industrialized nations while also assisting less developed countries. Sharing of information regarding terrorist financing and other pertinent sanctions should occur between various governmental officials around the globe. Key

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<sup>32</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002).Page 24.

<sup>33</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002).Page 9.

<sup>34</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 28.

leaders from governments should meet regularly to discuss anti-terrorist financing strategies, while also working with officials in less developed countries to help develop a secure banking system. Financial aid and technological assistance should be offered by leading industrial nations to underdeveloped countries in order to promote an anti-money laundering strategy around the globe. International funding organizations, like the IMF and World Bank, should make funding contingent upon a nation's attempt to create a secure financial system.<sup>35</sup> With cooperation among governments around the world, information sharing and technical expertise would allow for more developed countries to work with less developed countries to create a much more secure global financial system than exists today, making it much more difficult for terrorist's to finance their organizations through legitimate means.

Combating terrorist financing requires more than a domestic policy in the United States, but a multilateral approach amongst leading industrial nations. The United States should use its power as a world leader to push anti-money laundering into the globe's agenda. The United Nations and the G-7 should discuss terrorist financing on a regular basis, for it is the root of terrorism. Stopping terrorism will only be possible if the globe attempts to cut off finances of leading terrorist groups. By creating a set of international banking standards, alongside a list of charitable organizations and *hawalas*, the international community will be better able to work together to track and eventually stop the financing of terrorist organizations. It is only through a multilateral approach that the United States and other countries will be able to properly attempt to stop such groups such as al Qaeda in the future.

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<sup>35</sup> Council on Foreign Relations. *Terrorist Financing: Report of an Independent Task Force Sponsored by the Council of Foreign Relations*. (New York: Council on Foreign Relations, 2002). Page 28.

## VI. CONCLUSIONS

This paper has assessed the most serious shortcomings in the United States' domestic and international strategies against terrorist financing. We have compiled eight recommendations that, if implemented in combination would greatly improve the efforts of the United States to track and seize terrorist assets, and deny terrorist organizations the capability to carry out attacks against the United States and its allies. Below is an annotated list of the recommendations proposed in the preceding paragraphs.

### *Domestic Response*

Our four recommendations to improve the domestic response to terrorist financing focus on the coordination of federal enforcement strategy and intelligence and the improvement of data collection and analysis:

- The Treasury Department should be designated the lead agency in the enforcement of terrorist financing laws and be given final authority to either track or seize terrorist assets.
- The intelligence community, IRS, and State Department should locate on-site liaison offices at the OTFI. Additionally the TFOS of the FBI should be located on-site at the offices of the OTFI and report directly to the Treasury Undersecretary in charge of OTFI.
- The federal government should partner with financial institutions to create integrated reporting software to ease the burden of federally mandated SARs.
- The federal government should contract with a commercial data mining and electronic search firm to develop automated analysis tools capable of converting raw financial data into actionable intelligence.

### *International Response*

Our international policy focuses on a multilateral approach amongst leading industrial nations, with the United States taking on the role as a leader in the fight against terrorist financing:

- The United States should spearhead the international anti-money laundering strategy; utilizing its role in the G-7 and United Nations to push other developed countries to become more involved in the tracking of terrorist financing.
- World leaders must work to create a stronger set of international standards that define and establish the criterion for a secure financial system around the globe.
- Alongside stronger international banking standards, a means of regulating the *hawala* and charitable organizations should be created, including a “white” and “black” list of charities.
- Industrialized nations should promote sharing of information regarding terrorist financing and give technical and financial assistance to underdeveloped nations who are attempting to create secure financial systems.