

## **The FATF's Nine Special Recommendations : A Too "Soft" Approach to Combating Terrorism?**

**By Michael Martuscello\***

### Introduction

“Money laundering” has traditionally referred to the deceptive practice of making criminal proceeds appear as legitimate income. Although the total amount of money that is laundered annually cannot be calculated with complete accuracy due to the clandestine and illegal nature of cleansing processes, the International Monetary Fund has estimated the sum to be somewhere between three and five percent of the world’s gross domestic product—an equivalent of between 1.75 and 2.91 trillion U.S. dollars using data from the World Bank.<sup>1</sup> Since the annual amount of money laundering indicates the prevalence of both the crime and criminals evading detecting and prosecution by law enforcement, such a significant figure is alarming, and especially so when considering that about “ten years ago, the generally accepted estimate of international money laundering was in the range of \$300-\$500 billion.”<sup>2</sup> Beyond being alarming, however, such a colossal estimate also illustrates that eradicating the practice of money laundering cannot be considered a simple task to be handled by any one nation. Indeed, given

---

\* M. Henry Martuscello II. J.D. Candidate New York Laaw School, expected May 2011. B.A. International Relations, Colgate University, 2008. Currently employed as a Senior Compliance & Legal Analyst at the NY branch Skandinaviska Enskilda Banken. I would like to thank my colleagues at SEB, August Carfano and Stephen Conwell, without whose guidance and mentoring I would never have developed an interest in AML.

<sup>1</sup> See U.S. Dept. of State, Bureau for Intl. Narcotics and L. Enforcement Affairs, *International Narcotics Control Strategy Report: Volume II Money Laundering and Financial Crimes*, 5 (2008) <http://www.state.gov/documents/organization/102588.pdf> (last accessed Dec. 6, 2010) (referring to an IMF estimate on global money laundering). See World Bank, *GDP (current US\$)*, [http://data.worldbank.org/indicator/NY.GDP.MKTP.CD?cid=GPD\\_29](http://data.worldbank.org/indicator/NY.GDP.MKTP.CD?cid=GPD_29) (last accessed Dec. 6 2010) (reporting World GDP to be \$58,228,200,000,000).

<sup>2</sup> *Id.*

that this amount is substantially greater than the budgets of most nations, the estimate indicates that effectively eliminating money laundering will require international collaboration.<sup>3</sup>

Since being founded in 1989 at a G-7 summit in Paris, the Financial Action Task Force (FATF) has led the international campaign against money laundering by identifying methods and trends of the illegal practice, developing global standards to counter them, and then ensuring that member nations implement such standards through a mutual evaluation process.<sup>4</sup> For over a decade after its conception, this inter-governmental body concentrated primarily on deterring drug trafficking and organized crime through the promotion of anti-money laundering (AML) policies designed to make it harder for launderers to hide the criminal origin of funds by increasing the transparency of the international financial system and giving countries the capacity to detect, investigate, prosecute, and punish money laundering. But after the events of September 11, 2001, widely revealed that terrorist organizations use many of the same techniques as money launderers in order to surreptitiously fund their operations, the focus of the FATF expanded specifically to include developing and promoting counter-terrorist financing (CTF) practices.

This paper explores the mission and strategy of the Financial Action Task Force as it relates to suppressing the funding of terrorism, which often, although not necessarily, involves traditional money laundering schemes. The paper centers on the FATF even though it has no actual ability to implement its recommendations or enforce its evaluations because it has still proven extremely influential with only its “soft” law techniques. The fact that “over 180

---

<sup>3</sup> See White House Office of Management and Budget, *Fiscal Year 2011 Budget of the United States Government*, Table S-1. (Budget Totals) (2010), <http://www.gpoaccess.gov/usbudget/fy11/pdf/summary.pdf> (last accessed Dec. 6, 2010) (estimating the 2011 US Government Budget to be \$2.567 trillion).

<sup>4</sup> See Financial Action Task Force (FATF), *Global Money Laundering and Terrorist Financing Threat Assessment*, 7 (Jul. 2010), <http://www.fatf-gafi.org/dataoecd/48/10/45724350.pdf> (last accessed Dec. 6, 2010) (describing the three main functions of the FATF).

jurisdictions have joined the FATF or an FATF-Style Regional Body . . . and committed at the ministerial level to implementing the FATF standards and having their AML/CTF systems assessed”<sup>5</sup> illustrates its enormous influence. Indeed, the FATF is “widely recognized by governments and international organizations as the world’s preeminent counter-laundering body, and its policies are looked to as a source of customary international law.”<sup>6</sup> The paper begins by discussing traditional money laundering in order to describe the specific threat that the FATF has long faced. Besides detailing the three-part scheme typically used to wash “dirty” money, this first section introduces specific features of the international financial system that represent vulnerabilities exploited by money launderers in order to conceal the criminal source of funds. After describing the taskforce’s original focus, the paper then goes on to explain both the direct and indirect connections between terrorist organizations and money laundering in the next section in order to demonstrate why the FATF heads the international CTF initiative. The second section recognizes not only that many terrorist organizations actively engage in traditional washing schemes to cleanse the cash derived from their own non-terror-related and profit-driven crimes, but also that less immediate links exist between terrorists and money laundering because even groups that engaged purely in terror-related acts and are fully funded by non-criminal sources, take advantage of the same features of the international system as traditional launderers in order to conceal their illegal acts and intentions. Next, the paper describes the specific actions that the FATF has taken to oppose terrorism since 9/11. Concentrating on the Nine Special Recommendations that the FATF has issued on terrorist financing, the third section outlines how

---

<sup>5</sup> *Id.*

<sup>6</sup> Allison Bachus, *From Drugs to Terrorism: The Shift in the International Fight Against Money Laundering after September 11, 2001*, 21 ARIZ. J. INT’L & COMP. L. 848, 859-60 (2004), <http://www.ajicl.org/AJICL2004/vol213/Bachus%20Note%20Final%20Revised%2011%20Nov%202004.pdf> (last accessed Dec. 6, 2010) (citing Jesse S. Morgan, Note, *Dirty Names, Dangerous Money: Alleged Unilateralism in U.S. Policy on Money Laundering*, 21 BERKELEY J. INT’L L. 771, 782 (2003)).

these “soft” laws attempt to repair weak points in the global financial system that were earlier identified as being exploited by both terrorists and money launderers. After exploring criticisms of these Special Recommendations and the 2010 threat assessment by the FATF, this section reaches the conclusion that the CTF efforts of the FATF have only had a limited effect on reducing the threat of terrorist financing. The paper’s conclusion then discusses the main limitations of the Special Recommendations and ways to improve them. In the end, the paper submits that although the FATF should be praised for seeking to establish and implement an international response to the funding of terrorism, its efforts have ultimately proven “soft” and have not significantly reduced the threat of terrorist financing because its CTF approach has been too similar to its AML program—and thus, geared too much towards solving a similar but distinct problem.

### I. “Traditional” Money Laundering

Traditionally, money laundering has been “the criminal practice of filtering ‘dirty’ money through a maze . . . of transactions, so that the funds are ‘cleaned’ to look like proceeds from legal activities.”<sup>7</sup> Such washing typically involves three stages during which illicitly obtained money is passed through legitimate people and accounts so that its criminal origin cannot be traced.

During the initial “placement” stage, money launderers convert any cash generated by crime into a monetary format that is less likely to raise suspicion of any wrongdoing when used in subsequent financial transactions. Placement occurs by depositing cash in a bank account or using it to acquire monetary instruments, like money orders or traveler’s checks, which are more

---

<sup>7</sup> Darhiana Mateo, “It’s a New World for Banks, Too,” 15-Aug *Business Law Today* 49, 49 (July/August 2006).

discrete and easier to transport and use in transactions than large amounts of physical currency.<sup>8</sup> Since individuals can seem inherently suspect when possessing large amounts of physical currency, money launderers often resort to a practice called “smurfing,” whereby “ a number of people mak[e] small deposits in a number of different depository institutions so as to avoid detection.”<sup>9</sup> They also frequently use cash to form or obtain control of front organizations, whose books can then be manipulated to show fictitious inflows of cash that can corroborate any deposits, which could otherwise be perceived as suspicious and reported to authorities.<sup>10</sup> Before converting cash into other monetary forms, launderers also often transport it across borders in order to take advantage of differences in cash declaration and reporting requirements that exist between jurisdictions. Although avoiding the unwanted attention that dealing in cash tends to attract is definitely a reason to convert it to other forms of value, the main reason that money launderers get rid of hard currency during placement is to eliminate the cash evidence that a crime has occurred. Indeed, regardless of how cash is placed into the financial system, all money launderers have the same objective during placement of destroying a direct connection between the profits and a crime.

After eliminating cash evidence of illegality, money launderers then put the funds through a “series of complex financial transactions . . . [designed] to so obscure the connection between the money and the crime that detection by law enforcement becomes impossible.”<sup>11</sup> Known as “layering,” this intermediate stage entails splitting up illicit funds into smaller amounts, commingling them with legitimate funds through multiple wire transfers to globally

---

<sup>8</sup> See S.Selena Nelson, *Regulating Money Laundering in the United States and Hong Kong: A Post 9-11 Comparison*, 6 WASH. U. GLOBAL STUD. L. REV. 723, 725 (2007).

<sup>9</sup> Paul Fagyal, *The Anti-Money Laundering Provisions of the Patriot Act: Should They Be Allowed to Sunset*, 50 ST. LOUIS U. L.J. 1361, 1365 (Summer 2006).

<sup>10</sup> See *id.* at 1366.

<sup>11</sup> Nelson, *supra* note 8.

scattered financial accounts at separate institutions, and then finally changing these mixed funds into other forms of value by buying and selling currencies, financial products, precious commodities, real estate, securities, and various other high-value items.<sup>12</sup> As funds move through multiple counterparties in different transactions, it becomes progressively harder to trace them back to a specific criminal enterprise. Since some states have stricter suspicious activity reporting requirements than others, money launderers often exploit jurisdictions with lower standards or high levels of bank secrecy in order to avoid detection.

The final “integration” stage occurs after the audit trail back to a criminal activity has been effectively concealed and involves re-introducing the funds into legitimate commerce. Money launderers can accomplish this final step by investing in clean businesses that pay out lawful returns, using front organizations to create seemingly legit profits from non-existent merchant or trade activities, or simply by reconsolidating funds that have been sufficiently layered to hide any criminal connection. The wash cycle finally is concluded when the “funds are fully assimilated into the mainstream economy and become available to the criminal for any purpose.”<sup>13</sup>

## II. The Connections Between Terrorist Financing and Money Laundering

Once one understands the connections between terrorist organizations and money laundering, it becomes clear why the FATF coordinates and leads the international response to the funding of terrorism. First and foremost, this role is suitable for the FATF because profit, not ideology, often drives terrorist organizations and thus, many are regularly involved in schemes to wash the

---

<sup>12</sup> See Fagyal, *supra* note 9, at 1367.

<sup>13</sup> Nelson, *supra* note 8, at 726.

criminal proceeds of their primary criminal operations, which do not relate to terrorism. In these cases, the FATF is fighting its “traditional” money-laundering foe.

However, the FATF appears equally suited to combat even groups which only aspire to commit terror and have no “dirty” money to cleanse, because such groups still use the same features of the international financial system that money launderers do, albeit for different purposes, in order to finance their terrorist activities in a clandestine fashion. Indeed, all terrorist organizations, regardless of their actual involvement in traditional washing schemes, are connected to money laundering by the methods that they use for moving funds around the world while remaining undetected by law enforcement. The reasons that terrorist organizations use the same techniques as money launderers ultimately relate to how they use, raise, and transfer funds. During all of these general acts, terrorist organizations must hide “financial resources and activities from the scrutiny of state authorities” and the methods that money launderers have developed to do just that come in handy.

The first general reason that terrorist organizations use laundering techniques is that, like money launderers, they deal with significant amounts of money that can easily draw unwanted attention and make the detection of illegality simple. Although funding requirements ultimately depend on the scale of a group’s activities, most terrorist organizations have two types of expenditures: those related to staging specific attacks or supplying “direct operational support,” and those related to maintaining a terrorist network or providing “broad organizational funding.”<sup>14</sup> Whereas the former category consists of the costs associated with purchasing the physical materials used in a particular strike, communicating with and within terrorist cells,

---

<sup>14</sup> Financial Action Task Force, *Terrorist Financing*, 7, (Feb. 29, 2008), <http://www.fatf-gafi.org/dataoecd/28/43/40285899.pdf> (last accessed Dec. 6, 2010) (describing the “how terrorist financing requirements fall into two general areas: (1) funding specific terrorist operations . . . and (2) broader organizational costs”) (hereinafter FATF).

providing financial assistance to affiliate groups, and paying for the planning, subsistence, training, and travel of individual operatives, the latter type includes expenses for the development of a supporting infrastructure, recruitment of new members, dissemination of propaganda, promotion of radical ideology, and financial support of charities and media outlets under terrorist control.<sup>15</sup> Recognizing that terrorist organizations have such massive funding requirements and spend money on more than just the materials used immediately in an attack (i.e. weapons, bomb-making components, surveillance equipment, and modes of transportation) is key to understanding why they behave like money launderers. Indeed, if these groups had only such minor expenses, which recent attacks have revealed to run only a few thousand dollars, then they could easily remain anonymous simply by making multiple purchases with small amounts of cash at different retail locations and would not need more complicated techniques to avoid detection.<sup>16</sup> Instead, terrorist groups find it necessary to exploit the same features of the international financial system as money launderers because their funding requirements often prove so large and diverse that disguising an audit trail would prove difficult without such techniques that allow them to spend a lot in a less conspicuous and seemingly legitimate manner.

Besides their large spending requirements, another general reason that terrorist organizations use laundering methods is because they often raise funds in a fashion that creates the need to obscure any connection to a criminal activity, whether such be a past crime or a future terrorist act. As already mentioned, many terrorist organizations fund their operations by engaging in non-terror-related crimes, such as arms trafficking, drug trafficking, extortion, fraud, kidnap-for-ransom, and racketeering, and then washing the proceeds so that they can be used as

---

<sup>15</sup> See *id.* at 7-10 (detailing what expenses fall under “direct operational support” and what ones qualify as “broader organizational support”).

<sup>16</sup> See *id.* at Table 1: The direct attack costs of a terrorist conspiracy (detailing that the average cost of 7 major terrorist attacks between 1998 and 2005 was less than \$30,000 each, with the least expensive attack costing just \$10,000).

valid funds.<sup>17</sup> However, other groups fund themselves through “black washing,” whereby they receive their support from “charities, businesses, and through self-funding by terrorists and their associates from employment, savings, and social welfare payments.”<sup>18</sup> When funding comes from such legitimate sources, terrorist organizations are not concerned with laundering it in the traditional sense of concealing its criminal origin. Rather they desire to prevent the legitimate origin of the funds from being discovered after a terrorist attack occurs in order to ensure that their benefactors both escape punishment and “can continue to provide funds to other terrorists.”<sup>19</sup>

Regardless of how they raise or spend funds, the final general reason that all terrorist organizations utilize fraudulent laundering techniques is that they want to avoid detection and conceal their true intentions for the money’s use when transferring it around the globe. The moving of terrorist-related funds often involves three methods that have traditionally been used by money launderers to layer funds: use of the formal financial system, physical cash movements, and exploitation of the international trade system.<sup>20</sup> Terrorist organizations commonly use the international financial system because of “the speed and ease with which funds can be moved . . . without detection between and within jurisdictions.”<sup>21</sup> Groups also take advantage of the international trade system since it provides the “opportunity to transfer value and goods through seemingly legitimate trade flows.”<sup>22</sup> Terrorists often use cash-intensive businesses or charities as fronts, like traditional money launderers do, in order to gain access to these two systems. Such easily manipulated entities allow them to put funds through multiple

---

<sup>17</sup> See *id.* at 15-20 (Detailing how some terrorist groups raise funds through criminal activities).

<sup>18</sup> *Id.* at 11 (Describing how some terrorist organizations raise money through diversion within legitimate charities, sham charities, legitimate businesses, and self-funding).

<sup>19</sup> Fagyal, *supra* note 9, at 1369.

<sup>20</sup> See FATF, *supra* note 14, at 21.

<sup>21</sup> *Id.*

<sup>22</sup> *Id.* at 23.

trades and financial transactions without arousing suspicions or revealing where the money is from or how it will be used. Physical cash movements allow terrorists to take advantage of jurisdictions with weak regulatory requirements and those that offer safe haven to criminals. Moreover, cash couriers allow terrorists to “move funds without encountering the AML/CFT safeguards established in financial institutions.”<sup>23</sup>

Since terrorist organizations and criminals are often the same, and even when they are not, use similar techniques in order to respectively fund their operations and to clean their “dirty” money, the expanded CTF role that the FATF has had after 9/11 not only appears appropriate, but also, seems to further its AML mission. Nonetheless, it is important to recognize that despite such similarities, which stem from the shared need to remain anonymous and evade police detection, terrorist financing is a distinct threat that does not always involve “traditional” money laundering and thus, cannot be handled in the same way as money laundering.

### III. The CFT Program of the FATF

The CTF program of the FATF has only achieved limited success because the taskforce has approached terrorist financing in very much the same fashion as it has tackled money laundering. In fact, the CTF program of the FATF consists of 9 Special Recommendations on Terrorist Financing that complement, and can only be effective in conjunction with, its previously issued 40 Recommendations on money laundering. This section of the paper begins with a brief discussion of the 40 Recommendations in order to explain their basic objectives and the reasons that they have come to be accepted as successful examples of “soft” law. Next, the section introduces 9 Special Recommendations and the specific ways that each Special Recommendation (SR) attempts to make it harder for terrorists to fund their operations. After

---

<sup>23</sup> *Id.* at 23-24.

presenting a comprehensive overview of this CFT program, the section then explores the limited success that the 9 Special Recommendations have had on suppressing the funding of terrorism by presenting the findings of the recent 2010 Global Money Laundering and Terrorist Financing Threat Assessment by the FATF. The section concludes that there are many reasons for the limited effectiveness of the CTF program of the FATF, but the most significant one is a design that too closely resembles the taskforce's AML program and does not adequately address the unique nuances of terrorist financing.

#### A. The FATF 40 Recommendations

Widely considered the “crown jewel of soft law,”<sup>24</sup> the 40 Recommendations on Money Laundering represent a “comprehensive laundry list”<sup>25</sup> of AML measures for FATF members to implement, covering the:

criminalization of laundering proceeds from serious crimes and the enactment of laws to seize and confiscate those proceeds; requirements for financial institutions to identify all clients (including beneficial owners) and to keep appropriate client records; implementation of a range of internal control measures; requirements for financial institutions to report suspicious transactions to national authorities and to have adequate systems for the control and supervision of financial institutions . . . [as well as the] entering into international treaties and passing of national legislation to provide prompt and effective co-operation.<sup>26</sup>

---

<sup>24</sup> Bachus, *supra* note 6 (citing GUY STESSENS, MONEY LAUNDERING: A NEW INTERNATIONAL LAW ENFORCEMENT MODEL 14 (Cambridge 2000)).

<sup>25</sup> Lauren Dellinger, *From Dollars to Pesos: A Comparison of the U.S. and Colombian Anti-Money Laundering Initiatives from an International Perspective*, 38 CAL. W. INT'L L.J. 419, 429 (Spring 2008) (Citing Bruce Zagaris, *Revisiting Novel Approaches to Combating the Financing of Crime: A Brave New World Revisited*, 50 VILL. L. REV. 509, 544) (breaking down 40 Recommendations into “three main categories: (1) the criminal offense of money laundering, including legislative guidelines and confiscation measures (Recommendations 1-3); (2) ‘Measures to be taken by Financial Institutions and Non-Financial Businesses and Professionals to prevent Money Laundering and Terrorist Financing’ (Recommendations 4-25); and (3) ‘Institutional and other measures necessary in systems for combating Money Laundering and Terrorist Financing,’ including international cooperation (Recommendations 26-40)”).

<sup>26</sup> Christina Jackson, *Combating the New Generation of Money Laundering: Regulations and Agencies in the Battle of Compliance, Avoidance, and Prosecution in a Post-September 11 World*, 4 J. HIGH TECH. L. 139 (2004).

The FATF has been highly effective at encouraging members to adopt these technically non-binding recommendations through “a ‘graduated approach’ beginning with the least aggressive measures and increasing in severity as a member country persists in non-compliance.”<sup>27</sup> When a member country refuses to comply, this gradual approach includes first peer-pressuring the member country to improve its AML program, followed by requiring the member to submit progress reports, then sending a formal letter or delegation to the member’s government, and finally advising financial institutions to pay particular attention to transactions involving parties domiciled in the member, or additionally suspending its membership.<sup>28</sup> Moreover, the FATF has effectively forced even non-members countries to implement AML programs by publishing a blacklist of countries that inhibit the international AML effort by having inadequate safeguards.<sup>29</sup> Accordingly, since its membership includes the world’s richest and most powerful nations, failure to comply with the “soft” law of the FATF can result in “severe trade consequences for uncooperative countries.”<sup>30</sup>

### B. 9 Special Recommendations on Terrorist Financing

---

<sup>27</sup> Bachus, *supra* note 6, at 852. *See also* at 851 (detailing how the FATF “made a deliberate choice not to cast the recommendations into the mould of a “treaty” in order to “avoid a time-consuming and extensive ratification process and to provide for flexible adaptation of the Recommendations by member countries”).

<sup>28</sup> *See id.* at 852.

<sup>29</sup> *See id.* at 848 (reporting that the “sanctions and actions threatened by the FATF persuade most NCCTs to pass the necessary laws to part ways with the ‘un savory company’ of the blacklist”); *see also* Daniel Lindner, *Money Laundering Between States: A Comparison of International Money Laundering Control Mechanisms*, 74 DEF. COUNS. J. 47, 61 (January 2007) (describing Lichtenstein promptly overhauled its AML law to become compliant, after Standard & Poor’s downgraded the nation following its addition to the FATF black list) (recalling how “due to black-listing . . . Israel enacted its AML of 2000 and its more recent amendments of 2002); *see also* Ross Delston & Stephen Walls, *Reaching Beyond Banks: How to Target Trade-Based Money Laundering and Terrorist Financing Outside the Financial Sector*, 41 CASE W. RES. J. INT’L. L. 85, 95 (2009) (detailing the success of naming and shaming countries into compliance with the taskforce’s recommendations through its Non-Cooperative Countries and Territories list); *see also* Kathleen Lacey & Barbara George, *Crackdown on Money Laundering: A Comparative Analysis of the Feasibility and Effectiveness of Domestic and Multilateral Policy Reforms*, 23 NW. J. INT’L. L. & BUS. 263, 346 (Winter 2003) (Stating that “there is a strong deterrent inherent in the negative publicity of being named as country that will not cooperate in anti-money laundering efforts” and that “the most successful method to date for reducing the use of tax havens to secretly hide illicit funds can be found in the FATF ‘name and shame’ program.

<sup>30</sup> Nelson, *supra* note 8, at 731.

The 9 Special Recommendations seek to provide a comprehensive plan for countering the funding of terrorism when implemented in conjunction with the 40 Recommendations and can be broken down into two main categories: those that establish the legal and procedural framework for detecting and punishing terrorist financing (SR's I-V) and those that are specific measures to make detecting terrorist financing more likely (SR's VI-IX).

Stressing an international duty to combat terrorism, Special Recommendation I calls for the universal adoption of the 1999 United Nations International Convention for the Suppression of the Financing of Terror and implementation of all UN resolutions "relating to the prevention and suppression of terrorist acts."<sup>31</sup> By recalling that convention, which was unanimously adopted by the UN General Assembly, SR-I rejects bank secrecy as a valid excuse for refusing to cooperate and pressures nations to "take steps to prevent and counteract the financing of terrorists, whether direct or indirect, through groups claiming to have charitable, social or cultural goals or which also engage in illicit activities such as drug trafficking or gun running."<sup>32</sup> Such steps include not only imposing criminal, civil, or administrative liability on those who fund terrorism but also identifying, freezing, and seizing funds that are allocated for terrorist activities.<sup>33</sup> By calling for the immediate implementation of all UN resolutions dealing with the funding of terrorism, and in particular Security Council Resolution 1373, which was passed in response to 9/11 and promotes international cooperation through the sharing of intelligence and lending of legal assistance to prosecute offenders, SR-I applies further pressure on nations to seek to combat terrorist financing.

---

<sup>31</sup> FATF, *IX Special Recommendations*, 2 (2010), <http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf> (last accessed Dec. 6, 2010) (hereinafter FATF, *IX*).

<sup>32</sup> United Nations, "International Legal Instruments to Counter Terrorism," <http://www.un.org/terrorism/instruments.shtml> (last accessed Dec. 6, 2010).

<sup>33</sup> *See id.*

The Special Recommendation II seeks to provide countries with “the legal capacity to prosecute and apply criminal sanctions to persons that finance terrorism,”<sup>34</sup> by obligating states both to “criminalize the financing of terrorism, terrorist acts and terrorist organizations”<sup>35</sup> and to designate terror-related offenses as “money laundering predicate offences.”<sup>36</sup> The broad definitions that the FATF supplies in its interpretive guidance for SR-II makes clear that the objective of this recommendation is to provide countries with great flexibility to prosecute any person who is somehow connected to terrorism. Moreover, by calling for any act that furthers terrorism to be a predicate offense for money laundering, the FATF pressures nations to designate terrorist-related activities as severe crimes and increases the risk for terrorist financiers, who could also be prosecuted and penalized as money launderers, as well as terrorists. SR-II is important because without terrorist financing being illegal in all countries, those who fund terrorism could utilize safe havens to avoid arrest and prosecution.<sup>37</sup>

Aiming to establish the infrastructure that is needed to punish those who are suspected or known to have connections to the funding of terrorism, Special Recommendation III requires countries to freeze the “assets of terrorists, those who finance terrorism, and terrorist organizations”<sup>38</sup> and to enact measures that allow the “competent authorities to seize and confiscate property that is the proceeds of, or used in, or intended or allocated for use in, the financing of terrorism.”<sup>39</sup> SR-III contains both a preventative measure because it denies terrorist organizations access to financial resources by freezing funds and a punitive measure in that it provides for forfeiture of assets used to help finance terrorism. The forfeiture measure is

---

<sup>34</sup> FATF, *IX*, *supra* note 31, at 4.

<sup>35</sup> *Id.* at 2.

<sup>36</sup> *Id.*

<sup>37</sup> See Charles Bowers, *Hawala, Money Laundering, and Terrorism Finance: Micro-Lending as an End to Illicit Remittance*, 37 *DENV. J. INT’L. L. & POLY* 379, 392-393 (Summer 2009) (Describing upward trend in the criminalization of terrorist financing).

<sup>38</sup> FATF, *IX*, *supra* note 31.

<sup>39</sup> *Id.*

particularly important since it represents a direct attack against the front organizations that terrorists used to appear legitimate. Indeed, if the forfeiture measures were widely applied, the incentive for legitimate companies (e.g. ethnic grocers) to allow illicit remittance operations to piggyback on their infrastructure, for example [would] substantially decrease [].<sup>40</sup>

Special Recommendation IV makes the detection of terrorist funds more probable by imposing new reporting requirements on the businesses that terrorist organizations are most likely to exploit to conceal the true intentions beyond their numerous financial transactions. SR-IV mandates that states should require financial institutions and other entities that already have AML reporting obligations to report any reasonable suspicions that “funds are linked or related to, or are to be used for terrorism”<sup>41</sup> to competent authorities. These new reporting requirements complement SR-III because alerting authorities to such suspicious activities will allow them to take appropriate preventive action to freeze suspicious funds and if necessary, punitive action to seize them. Moreover, SR-IV helps to suppress terror by getting the gatekeepers to the financial system involved in fighting terrorism. This is important because gatekeepers control the points of entry that terrorists and money launderers use to put money through transaction after transaction. Collectively, SR-III and SR-IV allows nations to take action when there is a reasonable suspicion that funds are for a terrorist purpose.

Special Recommendation V aims to make it easier to prosecute suspected terrorists and their benefactors by requiring countries to provide each other “the greatest possible measure of assistance in connection with criminal, civil enforcement, and administrative investigations,

---

<sup>40</sup> Bowers, *supra* note 37, at 393, (Arguing how “grocers who might receive a hundred dollars in ‘hush-money’ each month now have to contemplate losing their entire business, their home, their cars, their accounts, anything that the money was either spent on or commingled with”).

<sup>41</sup> FATF, *IX*, *supra* note 31.

inquiries, and proceedings relating to the financing of terrorism.”<sup>42</sup> By calling for mutual legal assistance and the sharing of information, SR-V ensures that countries will work together and cooperate in order to eradicate the mutual threat of terrorist financing. Moreover, SR-V also prevents terrorists from fleeing to a jurisdiction with more relaxed CTF laws in an attempt evade prosecution by prohibiting countries from acting as safe havens and requiring them to implement procedures for the extradition of terrorists.<sup>43</sup> Under SR-V countries must cooperate with each other to combat terrorist financing.

After providing the infrastructure for criminalizing, prosecuting, and punishing those who fund terrorism, the FATF addresses four specific things, which terrorist financiers exploit in order to avoid detection while moving funds, in its final four recommendations. Special Recommendation VI goes after the unregulated businesses that terrorist often use to transfer funds around the world by requiring states to implement measures to ensure that those who “provide a service for the transmission of money or value, including transmission through an informal money or value transfer system or network, should be licensed and registered and subject to all the FATF recommendations that apply to bank and non-bank financial institutions.”<sup>44</sup> SR-VI also recommends that countries impose penalties on those who carry out such services without a license. The aim of these requirements is “to increase the transparency of payment flows by ensuring that jurisdictions impose consistent anti-money laundering and counter-terrorist financing measures on all forms of money/value transfer systems.”<sup>45</sup>

---

<sup>42</sup> *Id.*

<sup>43</sup> See *id.* (“Countries should also take all possible measures to ensure that they do not provide safe haven for individuals charged with the financing of terrorism, terrorist acts, or terrorist organizations, and should have procedures in place to extradite, where possible, such individuals.”)

<sup>44</sup> *Id.* at 3.

<sup>45</sup> *Id.* at 13.

Special Recommendation VII increases both surveillance over and transparency of wire transfers. Representing one of most potentially potent of all of the Special Recommendations, SR-VII requires countries to force all electronic money transferors “to include accurate and meaningful originator information (name, address and account number) on fund transfers and related messages that are sent,”<sup>46</sup> which will “remain with the transfer or related message through the payment chain.”<sup>47</sup> SR-VII, also obliges “financial institutions, including money remitters, [to] conduct enhanced scrutiny of and monitor for suspicious activity funds transfers which do not contain complete originator information”<sup>48</sup> According to its guidance, SR-VII seeks to make:

“basic information on the originator of wire transfers immediately available (1) to appropriate law enforcement and/or prosecutorial authorities to assist them in detecting, investigating, prosecuting terrorists or other criminals and tracing the assets of terrorists or other criminals, (2) to financial intelligence units for analyzing suspicious or unusual activity and disseminating it as necessary, and (3) to beneficiary financial institutions to facilitate the identification and reporting of suspicious transactions.”<sup>49</sup>

Recognizing the “potential terrorist financing threat posed by small wire transfers,” the guidance maintains that countries should try “to trace all wire transfers” and to “minimize thresholds taking into account the risk of driving transactions underground.”<sup>50</sup> If broadly imposed, the measures mentioned in SR-VII would make it significantly more difficult for those who fund terrorism to move funds internationally in a non-physical way.

Showing the FATF going after an entity that terrorists commonly exploit in order to raise and move money, Special Recommendation VIII requires countries to “review the adequacy of

---

<sup>46</sup> *Id.* at 3.

<sup>47</sup> FATF, *IX*, supra note 31 at 3.

<sup>48</sup> *Id.*

<sup>49</sup> *Id.* at 16.

<sup>50</sup> *Id.*

laws and regulations that relate to entities that can be abused for the financing of terrorism.”<sup>51</sup> Since “non-profit organizations are particularly vulnerable,”<sup>52</sup> the FATF mandates that countries “ensure that they cannot be misused”<sup>53</sup> to allow terrorist groups to appear as law-abiding entities, “exploit legitimate entities as conduits for terrorist financing,”<sup>54</sup> or obscure the “clandestine diversion of funds intended for legitimate purposes.”<sup>55</sup> The guidance to SR-VIII provides a multi-tier approach for preventing the abuse of these easily manipulated entities, which includes sector outreach, supervision, and monitoring requirements as well as information gathering and international cooperation responsibilities.<sup>56</sup>

Fighting the most basic method of moving funds, Special Recommendation IX requires countries to put “measures in place to detect the physical cross-border transportation of currency and bearer negotiable instruments, including a declaration system or disclosure requirement.”<sup>57</sup> Moreover, SR-IX obliges nations to have penalties and sanctions in place for those that make false declarations, including the freezing and seizure of their funds.<sup>58</sup> This special recommendation endows nations with investigation and penalization processes that directly aim to detect suspicious activity and to deter attempts by terrorists to move money manually rather than electronically through the formal financial system.

### C. The Limits of the 9 Special Recommendations

The 9 Special Recommendations do not lack their critics. As they only represent “soft” law, it should not be surprising that many have argued that this CTF program cannot be effective

---

<sup>51</sup> *Id.* at 3.

<sup>52</sup> *Id.*

<sup>53</sup> FATF, *IX*, *supra* note 31 at 3.

<sup>54</sup> *Id.*

<sup>55</sup> *Id.*

<sup>56</sup> *See id.* at 20-24.

<sup>57</sup> *Id.* at 3.

<sup>58</sup> *See id.* at 25-27.

enough against the funding of terrorism. These critics have contended that the 9 Special Recommendations are weak because there is no way to implement them fully or uniformly across all jurisdictions. Specific criticisms have included that: SR-I incorporates UN instruments, which contain broad definitions and thus can “be gamed to the point of being rendered ineffectual;”<sup>59</sup> SR-II endows law enforcement agencies with “expanding responsibilities without commensurate increases in enforcement budgets;”<sup>60</sup> SR-III and SR-IV suffer from “qualitative enforcement issues”<sup>61</sup> respectively because frozen assets “are too often allowed to thaw and assets are all too often returned”<sup>62</sup> when a prosecution fails to occur and because different entities often have diverse reporting requirements depending on a state’s definition of a financial institution;<sup>63</sup> SR-V has not prevented the existence of safe-havens, such as Somalia or the tribal areas of Pakistan;<sup>64</sup> SR-VI and SR-VII “suffer from a simple lack of follow-through”<sup>65</sup> so that many money remitters remain unregulated and many wire transfers continue to occur without complete originator information;<sup>66</sup> SR-VIII may never be “complied with in the Middle East and in parts of Asia;”<sup>67</sup> and SR-IX has remained ineffective because currency declaration thresholds are relatively high and terrorists can circumvent these by converting cash to “more compact, and less overt, forms of value (e.g. jewelry).”<sup>68</sup>

Regardless of the validity of these criticisms, the 2010 Global Money Laundering and Terrorist Threat Assessment (GTA) by the FATF reveals that the CTF program has done little if

---

<sup>59</sup> Bowers, *supra* note 37, at 394.

<sup>60</sup> *Id.*

<sup>61</sup> *Id.*

<sup>62</sup> *Id.*

<sup>63</sup> *See id.*

<sup>64</sup> *See id.* at 394-395.

<sup>65</sup> Bowers, *supra* note 37, at 395.

<sup>66</sup> *See id.*

<sup>67</sup> *Id.* at 396 (describing how the terrorist-linked al-Rashid Trust has had its assets unfrozen by Pakistan and its organizers have been “free from arrest or prosecution”).

<sup>68</sup> *Id.*

anything to prevent terrorists from funding their operations. Identifying recent trends and methods in money laundering and terrorist financing, the GTA has reported that those who finance terrorism continue to exploit at least one of five features of the international financial system: cash and bearer-negotiable instruments; transfer of value; assets and stores of value; gatekeepers; and jurisdictional/environmental aspects.<sup>69</sup> Considering that the 40+9 Recommendations have addressed all of these features in one way or another, this revelation illustrates that the effectiveness of the FATF in addressing the funding of terrorism has been inadequate.

The threat of terrorist financing remains great. In spite of SR-IX, terrorist groups still heavily resort to physically moving cash because “as more AML/CTF controls are placed on [the] financial sector, criminals look at alternative means to move their illicit cash.”<sup>70</sup> They continue to exploit cash-intensive businesses to “direct funds to terrorist organizations/activities when the relationship between sales reported and actual sales is difficult to verify.”<sup>71</sup> Terrorist groups also still take advantage of “transfer of value” systems through banks, money-transfer/alternative-remittance businesses, the international trade system, complex legal entities, and retail payment systems, including the ATM network.<sup>72</sup> To avoid cash-reporting requirements, they have progressively taken to using “money mules,” which are third parties “recruited to receive and then send wire transfers from deposit accounts to individuals overseas, minus a certain commission payment (perhaps 5-10%).”<sup>73</sup> They have also increasingly utilized “false or stolen identities . . . to avoid being identified through application of CDD [customer due

---

<sup>69</sup> See FATF, *supra* note 4, at 10 (Recognizing that most terrorist-financing activity “must utilize at least one of five features”).

<sup>70</sup> *Id.* at 16.

<sup>71</sup> *Id.* at 21.

<sup>72</sup> See *id.* at 24.

<sup>73</sup> *Id.* at 26.

diligence] requirements or to gain access to accounts”<sup>74</sup> or to register businesses which can later be used to obscure the true beneficial owners of funds.<sup>75</sup> Recognizing that free-trade zones often have more relaxed AML/CTF programs than other jurisdictions, terrorist organizations have come to find these helpful when transferring funds through non-existent and fraudulent trading activities. The “increasing role of non-banks in offering prepaid cards, electronic purses, mobile payments, internet payment services and digital precious metals,”<sup>76</sup> especially when they are off-shore providers of such, has further made it easy for terrorists to move funds despite the attempt by SR-VII to increase the transparency and monitoring of electronic payments.

Although the incidents of money launderers using stores of value and exploiting gatekeepers “far outweigh”<sup>77</sup> those of terrorists, the GTA still recognized such features as vulnerable to being used for terrorist financing because stores of assets can enable terrorists to discretely hold funds and third-parties, such as professionals, insiders, and politically exposed persons, can allow terrorists to access the formal financial system discretely.

Lastly, the GTA reveals that terrorist organizations continue to abuse environmental/jurisdictional elements in order to carry out their operations, move funds, and evade police detection or prosecution. Since CTF standards are variable across borders, terrorists continue to take advantage of those jurisdictions with weaker regulatory and enforcement systems, such as tax havens, offshore banking centers, conflict zones, high-corruption areas, and safe havens.<sup>78</sup> By doing so, terrorist groups have been able to evade the increased transparency, customer due diligence, and suspicious activity requirements that more regulated jurisdictions have and that make them most vulnerable to being caught.

---

<sup>74</sup> *Id.* at 25.

<sup>75</sup> FATF, *supra* note 4, at 22.

<sup>76</sup> *Id.* at 34.

<sup>77</sup> *Id.* at 37.

<sup>78</sup> *See id.* at 51-52.

Based on the findings of the GTA, it seems apparent that terrorist organizations can still fund their operations with relative ease and that although the 9 Special Recommendations represent a commendable effort, their effect has been quite limited—illustrated by the fact that “most countries have been reluctant to accept the Special Recommendations in full . . . . questioning whether transparency and accountability are desirable.”<sup>79</sup>

The inability of the FATF to compel full implementation of recommendations across all jurisdictions is in great measure to blame for this lack of effectiveness because terrorists “seek out and conduct their illegal operations in countries with weak . . . regimes.”<sup>80</sup> Nonetheless, given the “soft” strategy of this CTF program, such jurisdictional variances can only be expected. Surely, mutual evaluations and a “shame” list cannot force countries to adopt “best practices.” Therefore, some areas will be easier targets for terrorist financing abuse than others that are more regulated, secure, and transparent.

However, it is equally, and perhaps more, appropriate to blame the limited effectiveness of the 9 Special Recommendations on a failure by the FATF to maintain enough of a distinction between money laundering and terrorist financing. By following an approach to CTF that very much resembled its approach to AML, the FATF failed to take fully into account that terrorists and criminal launderers do actually behave differently in important ways. There are three specific ways in which the CTF program too closely resembles the AML program and thus, is detrimentally designed.

First, the FATF put too much emphasis on preventing terrorist groups from using the formal financial system to fund their operations through Special Recommendations IV and VII, which require financial institutions to report suspicious activity possibly related to terror, to keep

---

<sup>79</sup> Nelson, *supra* note 8, at 734.

<sup>80</sup> Bachus, *supra* note 6, at 847.

complete originator information with wire transfers, and to monitor suspicious fund transfers. While suspicious activity reporting and transaction surveillance can be effective at detecting money laundering because it involves large amounts of “dirty” money with a suspect source, it is ineffective for detecting terrorist financing since this often involves small amounts of legitimate funds which do not appear suspicious by themselves. Besides the fact that it is a lot easier to prevent suspicion when funds come from a legitimate source and are in small amounts, such an emphasis on the formal financial system is also flawed because terrorists can just avoid it all together and use other less regulated means that do not leave any audit trail. Money launderers find convenience in the financial system because it allows them to transfer large amounts of cash cheaply, instantly, and globally in a way that cannot be done by any other means. Terrorist organizations, however, often have to move only small amounts of money around the globe and therefore, have many other convenient means at their disposal, especially when the funds are legitimate.

Second, the FATF has overstressed the prevention of physical cash movements with Special Recommendation IX, which requires countries to adopt declaration and detection systems. Since money launderers frequently transport large amounts of currency across borders to take advantage of jurisdictions with weaker AML regimes during placement, such a measure makes their job more difficult by increasing the risk of detection. However, for many terrorist groups, which have legitimate funds and only have to move small amounts, declaration and detection systems do little or nothing. Indeed, it is much easier to evade detection when concealing only small amounts, which often fall below the thresholds for required declaration.

Third, despite Special Recommendation VI, which requires countries to register and regulate all who provide alternative remittance services, including informal value transfer

systems, the FATF has not adequately addressed the trade system, which is increasingly being exploited by terrorist organizations to transfer funds as countries crack down on cash smuggling and limit access to financial institutions.<sup>81</sup> Money launderers also often use the trade-system but for different reasons than terrorists. For money launderers, the trade system is attractive as a means of generating seemingly legitimate funds and is commonly used during integration. Terrorist organizations often use the trade system, however, to move funds, as well as the materials that they use to carry out attacks, because it is less regulated than other methods of sending value.

In order to be more effective at combating the funding of terrorism, the FATF must revise its CTF program to adequately take into account the differences between terrorist financing and money laundering. More specifically, the FATF must recognize due diligence and suspicious activity reporting requirements while effective at deterring money launderers, do not deter terrorists, who often use and transfer legitimate funds in amounts that fall below the thresholds that are considered suspect. Also, the FATF must realize that it is easier for terrorists to smuggle cash than it is for money launderers since they frequently are dealing with relatively small amounts that fall below illegal or suspicious thresholds and are not as bulky as the massive amounts that may be generated through illegal activity in one jurisdiction and physically moved to a neighboring one. However, most importantly, the FATF must address trade-base techniques that terrorist organizations use to transfer funds and materials across the globe. Only once the FATF takes into account these three issues, can its CTF program be individually designed to fight the funding of terrorism and not simply piggyback on its AML program.

---

<sup>81</sup> See Delston & Walls, *supra* note 29, 99-100 (Detailing how the “FATF has recognized that the increasing scrutiny of the other two major avenues, financial instruments and cash smuggling, ‘may have the unintended effect of increasing the attractiveness of international trade system for money laundering and terrorist financing activities’”).

### Conclusion

The 9 Special Recommendations on terrorist financing, which are meant to complement and be implemented along with the 40 Recommendations on money laundering, appear to have been ineffectual because the FATF has not maintained enough of a separation between the two criminal practices. Despite the similarities between money laundering and terrorist financing, it is important to recognize that the two activities remain distinct. Indeed, despite the need of both money launderers and terrorists to maintain discretion and their use of similar methods to do so, funding a terrorist organization does not necessarily involve washing “dirty” revenue and instead often relies on collecting non-criminal monies through charities, legitimate businesses, or other seemingly “clean” sources.

The CTF program of the FATF closely follows its AML program by imposing by imposing due diligence, monitoring and reporting requirements on banks and other gatekeepers to the financial system. Although such measures make it harder for terrorists to move large amounts of funds through the formal financial system, they do very little to prevent them from transferring small amounts, or from using other, more convenient means of transportation that do not leave a paper trail. The currency declaration and detection system requirements that are part of the CTF program also are ineffective against terrorist financing for similar reasons. While these measures may help to deter and detect criminals who illicitly earn a lot cash in one jurisdiction and then transport it all to a neighboring one for placement, they do nothing to prevent a terrorist from importing a small amount of funds that does not have to be declared but is still enough to purchase the materials that are needed to carry out a terrorist strike. The failure of the CTF program to address trade-based techniques of transferring funds is its biggest shortcoming. Whereas combating these techniques might be less important to an AML program

because criminals mainly use them during integration, at which point the source of “dirty” money is already so well obscured that evading detection is simple, fighting such methods is imperative for a CTF program since they represent the easiest way to move “clean” money, which will ultimately be applied to a terrorist purpose, without leaving behind an audit trail.

Even though the FATF should be praised for seeking to establish and implement an international response to the funding of terrorism, its CTF program has ultimately proven “soft” and should be criticized for too closely resembling its AML program. In order to improve it, the FATF must address trade-based methods of discretely transferring funds around the globe. The FATF must make it more difficult to use such trade-based methods because its previous crackdowns on cash couriers and the formal financial system have made this area more attractive to terrorists. This attraction presents a great danger because the trade system currently lacks comprehensive regulation and a way of detecting suspicious activity. Accordingly, the FATF must address this specific weakness if its CFT efforts are to be more effective at preventing the funding of terrorism.

Here, finally, it is important to note that the FATF cannot hope to eliminate completely the threat that is terrorist financing. The incentive to do the crime cannot be fully eliminated from terrorist financing because such crime is very frequently driven by ideology and not profit. Meanwhile, the incentive to launder money can be eliminated by making the cost of doing so and risk involved high enough to negate monetary benefit. The ideological element of terrorism combined with the small direct costs of carrying out an attack makes terrorist financing a very difficult and scary subject to address. For this reason, as well as the significance that even small contributions can play in the battle against terrorism, the FATF must be praised for its attempts

to combat the terrorist financing, despite their relative ineffectiveness at preventing terrorist organizations from accessing funding.