FFI RAPPORT

FIGHTING TERRORIST FINANCE - Issues, Impacts and Challenges

HASLERUD Gjermund (HiA), TRANØY Bent Sofus (UiO)

FFI/RAPPORT-2005/02100

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FORSVARETS FORSKNINGSINSTITUTT
Norwegian Defence Research Establishment
P O Box 25, NO-2027 Kjeller, Norway

FORSVARETS FORSKNINGSINSTITUTT (FFI)
Norwegian Defence Research Establishment

UNCLASSIFIED

P O BOX 25
N0-2027 KJELLER, NORWAY

SECURITY CLASSIFICATION OF THIS PAGE
(when data entered)

REPORT DOCUMENTATION PAGE

1) PUBL/REPORT NUMBER	2) SECURITY CLASSIFICATION	3) NUMBER OF PAGES
FFI/RAPPORT-2005/02100	UNCLASSIFIED	39
1a) PROJECT REFERENCE	2a) DECLASSIFICATION/DOWNGRADING SCHEDULE	
FFI-I/888/911	-	

4) TITLE
FIGHTING TERRORIST FINANCE - Issues, Impacts and Challenges

5) NAMES OF AUTHOR(S) IN FULL (surname first)
HASLERUD Gjermund (HiA), TRANØY Bent Sofus (UiO)

6) DISTRIBUTION STATEMENT
Approved for public release. Distribution unlimited. (Offentlig tilgjengelig)

7) INDEXING TERMS

	IN ENGLISH:		IN NORWEGIAN:
a)	Terrorism	a)	Terrorisme
b)	Financing terror	b)	Terrorfinansiering
c)	Al-Qaeda	c)	Al-Qaida
d)	Security policy	d)	Sikkerhetspolitikk
e)	Islamism	e)	Islamisme

THESAURUS REFERENCE:

8) ABSTRACT
The fight against the financing of terrorism has been at the top of the anti-terrorist agenda since the attacks of 9/11. The effort has involved both strengthening existing (primarily) money laundering legislation and a new approach based on lists of designated individuals and organizations. The report is divided into four main parts, The first two sections deal with the phenomenon of terrorist finance, while the next two deal with efforts to combat it. In section two conceptual and theoretical issues are discussed. A broad definition of terrorist finance is introduced and the dynamic nature of the phenomenon is outlined. Experience and theory both underscore an expectation that as countermeasures evolve so do methods of terrorist finance. The report then maps and discusses the many mechanisms whereby terrorists fund their activities and reviews the multilevel and multilateral efforts to fight the financing of terrorism, which have been introduced since 9/11. The magnitude of these measures and the support they have received have been such that one could argue that a new international financial regulations regime has emerged. Finally, the report analyses the impact of the counter terrorist finance (CTF) regime as it stands today, both in terms of effectiveness and legitimacy. It is impossible to gauge the exact impact but Al-Qaeda appears to have suffered due to a less permissive environment. Unresolved issues tied to the adaptability of terrorist groups and the resulting need for innovation in combating terrorist financing remain. Addressing these issues, means that countermeasures have to take onboard challenges of effectiveness and legitimacy.

9) DATE	AUTHORIZED BY This page only	POSITION
2005-08-04	Jan Erik Torp	Director

ISBN 82-464-0953-0

UNCLASSIFIED

SECURITY CLASSIFICATION OF THIS PAGE
(when data entered)

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1 INTRODUCTION

Since the terrorist attacks of 11 September 2001 (9/11), the fight against terrorist financing has occupied the attention of international organizations and national governments throughout the world. Curbing terrorist finance has become a central element of the “war on terror”. The events of 9/11 ushered in a new phase in the history of regulation and controls aimed at countering abuses of the international financial system. International organizations, largely in response to US-led efforts, issued a series of measures aimed at upsetting the financial infrastructure of terrorism. The measures introduced and the support they received were of such a magnitude that some would argue a new international financial regulations regime had been kick-started.

As a result of these measures, Al-Qaeda’s current and prospective ability to raise and move funds through the international financial system has been reduced. Most likely, these efforts have had real impact on Al-Qaeda’s financial situation, and it is undoubtedly a changed, and probably also a substantially weaker organization as a result. Much of the impact has been through deterrence. Past or prospective donors are now less willing to support terrorist organizations. Two other important effects that stem from a tighter regulatory framework go together with deterrence (Biersteker and Eckert 2005). Firstly, because of freezing and seizing we can assume that the amount of funds available for terrorism has been reduced. Secondly, new measures, through facilitating the gathering of intelligence, and the possibility of tracing flows after they have occurred, have supported law enforcement investigations. Although progress has been made on several important fronts, Al-Qaeda and other terrorist organizations, as demonstrated by recent attacks, still have ready access to financial resources, terrorism and hence terrorist finance constitutes an ongoing challenge. In the aftermath of the terror attacks in London, political leaders in Europe underlined the central importance of combating terrorist financing and stressed their determination to cooperate closely in these efforts.

This report is divided into four main parts in addition to this introduction and the concluding section. Roughly speaking, the first two sections deals with the phenomenon that is terrorist finance, while the next two deal with efforts to combat it. In Section Two conceptual and theoretical issues are discussed. A broad definition of terrorist finance is introduced and the dynamic nature of the phenomenon is outlined. Section Three seeks to map and explore the problem of terrorist finance further by discussing the many mechanisms whereby terrorists fund their activities. In Section Four we review the highly charged multilevel and multilateral efforts of the international community to fight terrorism through fighting the financing of terrorism. Section Five tries to discuss the impact of the emerging counter terrorist finance (CTF) regime as it stands today, both in terms of effectiveness and legitimacy.

Most of the data underlying this report is drawn from scholarly publications, government documents, documents of intergovernmental and non-governmental organizations. In addition, interviews have been conducted with former officials at the National Security Council during the Clinton and Bush administrations; officials at the International Monetary Fund's Legal Department and the Monetary and Financial Systems Department; and officials at the United Nations Al Qaeda/Taliban Sanctions Committee (1267).

In closing this introduction, three caveats summing up the difficulty associated with trying to establish good political science analytics on the topic at hand should be noted.CC Firstly, this issue area is characterized by very fast developments (the moving target problem). Secondly, relevant activities are conducted on several levels (the problem of delineating a reasonable "dependent variable"). Thirdly, it is also a problem that we are ultimately dealing with activities that the main actors themselves do not want us to know about. Terrorists do no release financial statements. But also on "the other side" there is some reluctance. A lot of the "data" we would ideally have wanted access to, resides with law enforcement officials or even worse, intelligence agencies. The former, as a rule, and sometimes for good reasons, refuse to be very clear about what they know or how they came to know what they know.

2 CONCEPTUAL AND THEORETICAL FRAMEWORK

2.1 What is Terrorist Financing?

It is well known that the issue of defining terrorism is a contentious one, and we will not seek to contribute to that debate here. The problem does not stop there, however, because just as there are many suggestions as to how terrorism should be defined, there are also problems related to filling the concept of terrorist finance with precise content. The term terrorist financing has traditionally referred to "the act of knowingly providing something of value to persons and groups engaged in terrorist activity" (Breinholt 2003: 7). Similarly, the IMF defines terrorist financing as "the processing of property from any source (perhaps a legitimate one) to be used to finance terrorist activity that has been or will be committed" (Aninat 2002: 2).

Although this may seem straightforward, it is difficult, technically, to define "the nexus that must exist between a particular activity and terrorist activities or groups in order to attract criminal liability", and further, to decide; "how close must the causal connection be between the prohibited act and the terrorist act?" (Davis 2003: 271). Despite the difficulties, there appears to be a reasonably strong international consensus on the definition of terrorist financing. That consensus is embodied in the 1999 United Nations Convention for the Suppression of Terrorist Financing (The Convention) (Ibid). According to the Convention, terrorist financing means:

> "assets of every kind, whether tangible or intangible, movable or immovable, however acquired, and legal documents or instruments in any form, including electronic or digital, evidencing title to, or interest in, such assets, including, but not limited to, bank credits, travellers cheques, bank cheques, money orders, shares, securities, bonds, drafts, letters of credit".

Thus, any person commits an offence within the meaning of the Convention if that person by

> "any means, directly or indirectly, unlawfully and wilfully, provides or collects funds with the intention that they should be used or in the knowledge that they are to be used, in full or in part, in order to carry out: (a) An act which constitutes an offence within the scope of and as defined in one of the treaties listed in the annex; or (b) Any other act intended to cause death or serious bodily injury to a civilian, or to any other person not taking an active part in the hostilities in a situation of armed conflict, when the purpose of such act, by its nature or context, is to intimidate a population, or to compel a government or an international organization to do or abstain from doing any act".

The Convention therefore criminalizes conduct beyond money laundering. It criminalizes a wide range of activities "intended to financially support terrorist activities, regardless of whether an act of terror was ultimately committed, regardless of whether the funds in question were actually used to finance terrorist acts" (Kantor 2002: 9). Thus, the offence exists when the funds have been collected for the purpose of committing a terrorist act.

To better understand the term, and the broad approach adopted by the UN, terrorist financing can be divided into various stages, each of which may be characterized by different actors and mechanisms (Poncy 2004: 27). The first stage is the accumulation of funds. Sources may include legitimate income from legitimate businesses that are owned by or associated with terrorists or terrorist organizations, or it can include illicit proceeds from a variety of criminal activities such as "drug trafficking, kidnapping, extortion, embezzlement, or petty crime" (Ibid). Terrorists may source funds directly from sympathizing donors, or it may come from charities that, wittingly or unwittingly, generate and move funds to terrorism. Once raised, terrorist funds may be stored in a number of forms and places, including bulk cash or funds stored in more sophisticated ways in "corporate assets and currencies in bank accounts held by straw men or front companies" (Ibid).

The next stage of terrorist financing is the moving of funds to terrorist operatives and cells. Thereby, funds are moved further towards its final use in violent acts. As has been revealed by investigations, terrorists have moved funds in a variety of different ways. These include cross-border wire transfers between or among banks, wire remitters and money service businesses, charities, and movement mechanisms that exist outside the formal financial sector like informal remittance systems or via couriers, or bulk cash smuggling.

The final stage of terrorist financing is the use, which evidences its criminal nature. As defined within the Convention, the "use" covers more than a terrorist act or attack. According to the broad definition, terrorist financing supports terrorist activity. Poncy (2004: 28) illustrates this by exemplifying that the many of uses may include:

- Supporting day-to-day operations of terrorist cell, which covers everything from buying food, renting a vehicle or housing expenses
- Buying weapons or other destructive instruments
- Expenses to housing or medical treatment
- Financing terrorist training camps
- Publishing terrorist propaganda
- Recruitment of new terrorists
- Purchasing telecommunication or computer equipment
- Payments for political support or sanctuary within rogue areas or states

This contrasts with what can be described as a common but dangerous misconception regarding terrorist financing and the potential value of countering it. The relatively low cost of terrorist attacks – the end product so to speak – is misleading as an indicator of what constitutes terrorist financing. For example, the 9/11 attack is estimated to have cost around $500,000, and pre-9/11 terrorist operations are estimated to have been even less expensive, with the first World Trade bombings in 1993 estimated to cost $18,000. Also, the suicide attacks on USS Cole in Aden in 2000, because they were conducted outside the West, were probably far less expensive. Based on such estimates, there is a danger of underestimating the amount of money required to conduct a terrorist operation or support a terrorist organization. If one suffers from this misunderstanding it is easy to draw the erroneous conclusion that it is not effective to attack terrorist financing networks, because terrorist attacks cost relatively little to carry out. As we shall return to below, the low cost of "the end product" can create particular problems in detection compared to typical money laundering investigations, but this does not make the fight against terrorist finance less important.

Although, the amount of money necessary to carry out violent attacks on persons or property, for example a hijacking and suicide bombing of a bus, may not require significant funding, the amounts required to finance a terrorist organization or infrastructure are substantially larger. Stuart Levey, US Treasury's Under Secretary for Terrorism and Financial Intelligence, also points to the importance of the broader perspective. When testifying before the House Financial Services Committee at a hearing on terrorist financing, Levey emphasized that the "cost of financing terrorist activity cannot be measured by the cost of a primitive destructive act", and that the "maintenance of those terrorist networks, like Al Qaeda, which threaten our national security, is expensive, even if a particular attack does not cost much to carry out" (Levey 2004).

As defined above, and exemplified by Poncy, terrorist financing covers more than the "last step" costs of equipment and preparations for specific terrorist actions. For instance, a suicide belt is only the proximate cause of a terrorist act that cost considerably more money than the mere purchase of explosive material. The point is that "the cost of financing terrorist activity cannot be measured by the proximate cost of a destructive act" (Poncy 2004: 28). Australian

Commonwealth Director of Public Prosecutions, Damian Bugg, estimates that “Al Qaeda [only] spends about 10 percent of its income on operational costs” (quoted in Biersteker and Eckert 2005).

Terrorist financing encompasses the wide range of support that terrorist organizations require to operate effectively. Compared to the 9/11 “minor” expenses, the CIA estimates that Al-Qaeda, pre 9/11, spent $30 million annually. That included “paying for terrorist operations, maintaining terrorist training camps, paying salaries to jihadists, funding fighters in Afghanistan, and sporadically contributing to related terrorist organizations” (Roth et al 2004: 11). International terrorist groups need significant amounts of money to organize, recruit, train and equip new adherents; and otherwise support their activities.

2.2 The Evolving Nature of Terrorist Financing

When reviewing past experiences of terrorist financing, the main lesson is the following: Terrorists and terrorist organizations, and Al-Qaeda in particular, represent an evolving enemy with a significant ability to adapt to a changing environment. Therefore, the various methods for raising and moving funds tell us that “fighting yesterday’s battles” may not be sufficient.

The adaptive and inventive nature of terrorism and particularly its financing mechanisms can be analyzed from an economic perspective. Brauer (2004) illustrates this by comparing and treating terrorists and terrorist organizations as rational actors like a company or firm. In that regard the constraints imposed upon terrorists may be conceived of within the context of a “market for terror” where a game is going on between, on the one hand, the nation-states and their international organizations and, on the other hand, the “producers” of terrorism. From a terrorist perspective then, the “terrorist firm” is facing a problem of production under adverse business conditions. According to Brauer, such constraints can be separated in two categories, namely government actions that decrease terrorists’ revenues or actions that increase the costs of terrorist activities. Prior to 9/11, governments focused on the latter by introducing either passive defensive measures like passing anti-terrorist laws, or active actions like the more recent attacks on suspected terrorist facilities in Sudan, Afghanistan and elsewhere (Brauer 2004: 21). Serious efforts to intervene on the revenue side are much more recent and cover the efforts to counter terrorist financing.

From an economic perspective, either mode of government intervention can be conceived of as being equivalent to imposing a “tax” on the business of terror. As a response terrorists may change their “product mix”. For example, an unforeseen consequence of introducing metal detectors at airports, which undoubtedly increased the “cost” of terrorists conducting skyjackings, may have been an increase in embassy bombings. Similarly, enhanced embassy security may have induced terror organizations to shift toward more assassinations and terror threats (Ibid: 22). Adaptive behavior of this kind also goes for terrorist financing. “Taxes” or constraints imposed will affect the amount of funds and the financing mechanisms used. Interpol also underscores this by stating that the “frequency and seriousness of international terrorist acts are often proportionate to the financing that terrorist groups might get."[1] According to Raphaeli, "money is the engine that drives terrorist acts", and, as a consequence, funding constraints can limit the scope of attacks. (Raphaeli 2003: 60). Raphaeli demonstrates this by pointing to how funding constraints was *the* deciding factor for Al-Qaeda bombing the Egyptian Embassy instead of striking against their first choice of target, which was the American Embassy in Islamabad. In the end, the imposed "tax" on funding not only prevented them for striking at their first choice of target but also prevented strikes against both embassies. Also, in the case of the 1993 bombing of the World Trade Center, the convicted terrorists admitted that due to a shortage of funds they were unable to build as large a bomb as they had intended (Ibid).

Whenever governments or the international community impose a "tax" on terrorist financing, terrorists can be expected to take a number of "tax evasion" measures in the sense of finding new sources of revenue and new ways of moving funds (Brauer 2004: 22). Recent trends may indicate such an adaptive behavior. For example, terrorists try to mirror legitimate financing methods. This can be illustrated by the increase in revenues coming from legal, as opposed to illegal, sources, which by nature are less suspicious and more difficult to detect in advance of an attack (US Department of State 2004, Rider 2002: 18). Also, the money may be transferred in amounts below any threshold of suspicious activities. In a similar way, the recent trend of increasing use of unregulated remittance systems and cash couriers for moving funds can be explained as a way of "evading" the massive post-9/11 efforts to disrupt the financing of terrorism by regulating international finance. The decentralization in the form of self-sufficient cells, as in the case of the Madrid bombings, can also be analyzed as a "tax evasion" effort.

This rationalist model is neither intended to explain the root causes of terrorism nor why individuals or organizations finance terrorism. Instead, the model serves as an analytical tool to understand the evolving nature of the financing mechanisms, and thereby it can be used to better predict the consequences of national and international CTF-efforts. In other words, the model focuses on understanding *how* rather than *why* terrorism is financed. The National Commission on Terrorist Attacks upon the United States also implicitly supports this approach by pointing out that, because of "the complexity and variety of ways to collect and move funds, understanding and gathering intelligence on Al-Qaeda's money flows will represent an ongoing challenge for the foreseeable future" (Roth et al 2004: 19). A similar perspective is taken by the Financial Action Task Force of the G-7, stating that "as terrorists learn the methods used by law enforcement and the regulatory bodies to discover misuse, their sophistication in disguising illicit funds will increase, making detection more difficult" (FATF 2003: 6).

[1] http://www.interpol.int/Public/Terrorism/financing.asp

3 MECHANISMS USED FOR TERRORIST FINANCING

Based on the broad definition introduced above, terrorist financing involves raising funds, storing funds, moving funds and finally the using of funds. This report focuses on the mechanisms used for raising and moving of funds. Historically, variety in the funding of terrorists and terrorist activities may be traced to state entities as well as private actors. Although not completely vanished, the former seems to have diminished in significance in recent years (Bantekas 2003: 316). As a consequence, terrorist finances have to be derived from sources other than state budgets. This private terrorist money can be classified into two categories on the basis of their origin: legitimate funds and illegitimate or unlawful funds. Examples of legitimate funds are donations and money derived from charities. Unlawful funds include activities that constitute a criminal act under both national and international law. Examples of such activities may be drug trafficking, money laundering, smuggling, and illegal arms trading.

3.1 The Raising of Funds

According to Biersteker and Eckert (2005), the most important source of financial support for Al-Qaeda, at least until recently, stems directly from methods established to support the mujahadeen in the 1980s. These included charities, NGOs, mosques, web sites and direct solicitation of wealthy individuals.

A common and perhaps the most challenging type of terrorist financing, involves fund raising by seemingly legitimate charitable organizations, with the ultimate goal of supporting terrorist groups. Typically, the people who engage in this type of activity set up front organizations, most often charities, which give them the cover of legitimacy and the benefit of tax deductions to their donors.

According to Bantekas (2003: 322), the concept of “charity in the Islamic world stems from deep religious roots” and is “inseparable from the state apparatus” (Bantekas 2003: 322). As one of the five pillars of Islam, the Zakat, a “tax” on wealth, is seen as “a claim of the poor against the wealth of the rich and as a means to maintain social equilibrium among the various segments of the population” (Basile 2003: 62). The Zakat plays a particularly significant role in countries such as Saudi Arabia, which, for religious reasons, have no income tax. Individuals are expected to donate 2.5 percent of their income to charity (Greenberg et al 2002: 7). Huge amounts are involved with little knowledge of the size of the donations and how they are used. As post 9/11 investigations have indicated, some of the donations have been used to nurture religious extremism and to finance terrorist activities.

Not only may charities use their own money to finance terrorist related organizations but they may also serve as a conduit for transfer of money to finance terrorist activities far away. For example, the Philippines and Georgia branches of the International Islamic Relief Organization (HRO), which is a Saudi charity and the world’s biggest Islamic charity, were used by Al-Qaeda to fund the terrorist organizations of Abu Sayyaf (Philippines) and Ansar al-

Mujahedeen in Chechnya (Raphaeli 2003: 62). The 9/11 Commission Report also states that Al-Qaeda was funded by diversions of money raised from Islamic charities, mosques and wealthy donors primarily in the Gulf region (Roth et al 2004: 4). In the case of charities, Al-Qaeda followed two strategies. One was to infiltrate foreign branch offices of large internationally recognized charities, and take advantage of the lax oversight and ineffective financial controls, especially in remote regions of the world. When large international Gulf charities donated money to smaller foreign country charities, employees may have "shaved off" money for Al-Qaeda. The other strategy involved Al-Qaeda operatives owning and fully controlling entire charities. In the case of charities, it is extremely important to point out that not all charities finance terrorism and the vast majority of donors do not knowingly donate money for terrorist activities.

3.2 The Moving of Funds

The methods used to move money to support terrorist activities are not necessarily identical to those used for moving and laundering money for general criminal purposes. Though, in many cases, criminal organizations and terrorists employ the services of the same money professionals (including accountants and lawyers) to help move their funds.

Both terrorists and criminal groups have used and may continue to use established mechanisms in the formal financial sector, such as banks, primarily because of their international linkages. Both terrorist organizations and narcotics-trafficking groups have exploited poorly regulated banking systems and their built-in impediments to international regulatory and law enforcement cooperation, and have made use of their financial services to originate wire transfers and establish accounts that require minimal or no identification or disclosure of ownership.

In addition to the formal financial sector, terrorists also use informal methods to move their funds. One common method is smuggling cash, gems or precious metals across borders either in bulk or through the use of couriers. Likewise, terrorists rely on informal financial systems, as will be outlined below.

3.2.1 Informal Remittance Systems – Hawala

Terrorist funds are not necessarily channeled through the formal financial system. Investigations after 9/11 uncovered terrorists' use of a worldwide informal remittance system that exists outside and independently of international or national regulations.

The use of so-called "informal remittance systems"[2] by terrorist organizations, especially Al-Qaeda, was known before 9/11, and were also used prior to the 9/11 attacks (Navias 2002: 57). Al-Qaeda used hawala for various reasons. First, in the aftermath of the 1998 embassy bombings in East Africa, international efforts to regulate the formal financial system were

[2] Other terms used are 'underground banking systems', 'alternative remittance system', 'informal banking systems, 'informal money transfer systems', and 'informal funds transfer systems'.

intensified. Second, Al-Qaeda's move to Afghanistan in 1996, which had a weak and not very dependable banking system, made hawala an attractive alternative. According to the 9/11 Commission, Al-Qaeda used an established hawala network operating in Pakistan, Dubai and throughout the Middle East to transfer funds efficiently. Within this network Al-Qaeda "used about a dozen trusted hawaladers, who almost certainly knew the source and purpose of the money" (Roth et al 2004: 25). A recent report published by the Bureau for International Narcotics and Law Enforcement Affairs of the U.S. Department of State, shows that, since 9/11, informal remittance systems play an increasingly important role in the financing of terrorism (US Department of State 2004).

Traditionally, informal remittance systems have operated within cultural groups and within geographical boundaries, thus different variations have evolved in different parts of the world (Rider 2002: 28). Of the most well known are the Chinese ”chit” or ”chop” system, the Pakistan ”hundi” system, the ”black market peso exchange” of Latin America, and the Indian ”hawala” system. The hawala system has been widely used by Al-Qaeda and will be described in more detail. Hawala means "transfer" in Arabic, but in Hindi it can also be translated as ”trust”, thus referring to the personal connection and informal nature of the transactions (Schramm and Taube 2003: 407, Looney 2003: 164). As an ancient banking system, hawala is deeply rooted in the culture of many countries. Today the system is practically functioning across and independent of national borders. Being global in scope, it has become an effective way of moving money around the world beyond the regulatory oversight of both national and international bodies, not least between developed and developing countries (Basile 2004: 175, Fitzgerald 2003: 6). Actually, hawala is now mostly used for transfers across international borders, especially for migrant remittances, and "investigators believe that hawala organizations exist throughout the United States and Europe" (Looney 2003: 164). The size of hawala transactions is estimated to be $2 trillion annually, which is approximately 2 percent of total international financial transactions (Raphaeli 2003: 70). For countries like Pakistan the magnitude of transactions far exceeds 2 percent. According to estimates made by the government, the use of hawala for sending money from overseas to Pakistan more than four times exceeds the same use of formal systems, making it the country's main source of hard currency (Suther 2002). Hawala systems especially flourish in the Gulf, particularly in Dubai, which is the system handling the largest volume of transactions, but there is also a dense concentration of hawala organizations in Pakistan and India (Looney 2003: 165).

How then does the Hawala system work? A hawala transaction usually entails clients and intermediaries, or what is referred to as hawaladers, which mainly operates "undercover" out of various types of storefronts or bazaars and souks.

> "If a client wishes to transfer a certain sum of money, he meets with the local hawala intermediary in his village, city, or county and tells him the amount of the payment and where and when it has to be made. The hawala intermediary takes the sum and a small additional handling fee calculated according to the amount to be transferred and gives the client a code, for example, a simple word or a particular verse from the Koran. Then, the intermediary contacts his partner in the relevant target area and, by telephone, fax, or e-mail, tells him the

> code and the amount to be paid out. In passing on this information, the hawala intermediary in the transaction's place of origin has completed his part in it. If it has been necessary for him to keep any written record of the transaction up to this time, it can now be destroyed. The client, meanwhile, also uses the usual modern means of communication to tell the recipient the code, which can indicate where the payment will be made. The recipient then contacts the hawala intermediary in the target area (whose identity is also indicated in the code), passes on the code, and accepts payment. Once the payment has been issued, if not before, the intermediary in the target area destroys any notes or other indications of the transfer. Most hawala transactions are concluded within 24 hours leaving no bookkeeping notes or other evidence of the transfer." (Schramm and Taube 2003: 407)

In theory, no money actually has to cross the border physically, at least not when conducting the transactions. Ideally, in- and outgoing payments should balance each other naturally, and thus no money has to be moved physically, but as there is a net flow out of the Western world, the hawaladers obviously have to balance their payments. To do this they operate according to a "two-pot" system, where the balancing between them may be done less frequently and separately from specific transactions. It is this time lag between transactions and the balancing between hawaladers that makes it difficult to reveal the origin of the money.

In essence, a hawala transaction is a transfer of funds without the use of a formal financial institution such as a bank. Substantial funds can be moved within or across borders without any money being physically moved at the time of the transaction and without any wire transfers involved. As a means of transferring funds it is: simple, fast, inexpensive, reliable, and efficient. This not only makes it an attractive way of moving funds for legitimate purposes, especially in poor and isolated areas where regular financial institutions are rare or non-existent. The informal nature of the transactions, leaving no paper trails, provides a layer of anonymity that attracts terrorists and other criminals.

3.2.2 Islamic Banking

In addition to the hawala system in the Middle East, Al Qaeda also abuses the Islamic banking system (Greenberg et al 2002: 9). As the leading financial institutions of oil-rich areas, Islamic banks are the primary channel for investments and transactions into the Middle East. Therefore, the funds depart from Islamic banks that are under "loose regulatory oversight" and move to capital markets around the world, including through the third world, offshore financial centers and tax havens, and the developed world.

Al-Qaeda has used front companies to funnel its finances through this system by, for example, receiving funds in a Western Barclay's account from correspondent Islamic banks in Sudan, Dubai and the United Arab Emirates (UAE). This correspondent nature of banking allows for transfers that receive less scrutiny. Also, hawaladers associated with Al-Qaeda have taken advantage of the lax regulation and relied on banks as part of their hawala operations (Roth et al 2004: 25).

3.2.3 Offshore Financial Centres (OFCs) and Correspondent Banking

In a number of foreign jurisdictions so-called shell banks have been established to gain entry into the U.S. banking system. A shell bank has no physical presence and no affiliation with other banks. What has become evident from recent examination of the banking system is, firstly, that "many reputable financial institutions in the United States and elsewhere lack due diligence to know as much as they should about correspondent and other banks with which they do business", and, secondly, that "whatever its societal merits, secrecy facilitates tax evasion and the parking of funds obtained illegally" (Weintraub 2002: 55).

Some countries attract foreign business and wealth through certain features of their legal systems, which offer a layer of secrecy far more impenetrable than traditional rules relating to professional confidentiality. In some instances, an assurance of absolute secrecy has been marketed as a privilege that can be bought for either a relatively small fee charged for establishing a company, or for the cost of opening a bank deposit. Thus, these countries or jurisdictions often referred to as tax havens or OFCs, have become a depository for not only fugitive and flight capital, but also possibly terrorist finances (Rider 2002: 20). For example, in the case of al-Taqwa, a financial services company now designated by the US as associated with terrorists, Al-Qaeda "moved its funds through accounts in familiar havens such as Liechtenstein and the Bahamas" (Greenberg et al 2002: 9).

International capital mobility makes terrorist funds easier to transfer. Although terrorist groups like Al-Qaeda may have limited its use of banks to move money throughout the world, banks continue to play an important role as a financing mechanism. OFCs are considered by some to be a haven for terrorists who are looking for a place to anonymously store, or channel, large amounts of money. It is the tax avoidance schemes that may be misused by both criminals and terrorists. The flow of funds through OFCs, which have strict secrecy laws but otherwise lax regulations, may obscure both the origin and the destination of the money. Furthermore, some OFCs have correspondent banking relationships with many of the world's largest banks. Thereby, shell banks registered in OFCs can be established to gain entry into the international banking system (Weintraub 2002: 55).

Within the formal international financial system, "the weakest link appears to be the essentially self-regulated international network of correspondent banks" (Fitzgerald 2003: 5). Correspondent banking is when a bank provides financial services to clients of other banks, which do not have a branch in the former bank's territory. Thus, a typical "correspondent bank account involves a smaller bank entering into an agreement with a larger bank to process and complete transactions on behalf of the smaller bank's customers or the smaller bank itself" (Alexander 2002: 313). Services offered in corresponding relationships may vary from simple transfer of funds to other more sophisticated financial transactions. For example, if a "bank in Saudi Arabia had a client who wanted sterling in the UK, the Saudi bank would employ a bank in London with which it had a correspondent relationship to make sterling available in the UK" (Navias 2002: 60). This "loose" relationship among banks from all over the world have provided terrorists' access to both the North American and West European banking environment, and thus exposed the “vulnerability of Western national banking to external penetration” (Ibid). This vulnerability seems most evident when correspondent banking relationships exist between Western banks and banks domiciled in poorly regulated economies. Such arrangements between banks from different regulatory spheres “allow the transfer of both illegally and legally derived money from the unregulated to the regulated financial institutions, thus allowing funds in through the backdoor of the regulated institutions” (Nawas et al 2002: 330). This in turn makes it possible for “clean” funds to be channeled out of the backdoor as easily as illegal funds can be brought in (Ibid).

3.2.4 Couriers and Cash Smuggling

The growing supervision of bank transactions may have increased the use of couriers and cash smuggling. This method refers to “the oldest way of moving money; by physically transporting it from one place to another” (Greenberg et al 2002: 11). A courier may pick up money from a financial facilitator, e.g. a hawalader, without knowing the recipient or the purpose of the money, and bring it to its destination (Roth et al 2004: 26). A Report of an Independent Task Force, sponsored by the Council on Foreign Relations, states that cash smuggling by couriers “is rampant throughout the Middle East, abetted by weak border controls, and a cash-based culture very unlike the Western credit- and electronic-based economy” (Greenberg et al 2004). According to the 9/11 Commission Report, Al-Qaeda used couriers because they provided a secure way of moving funds (Roth et al 2004). By recruiting couriers from within Al-Qaeda, no outsiders were involved or had knowledge of the transaction. Also, bulk cash smuggling by couriers is an attractive mechanism because U.S. dollars are used as an international currency and can be converted almost everywhere without leaving a traceable paper trail. No third party such as a bank has to be involved, and, thus, no “red flags” alert bank officials of suspicious transactions. In other words, the terrorists have total control of the money.

3.2.5 Trafficking in Precious Stones and Metals

Similar to bulk cash smuggling, Al-Qaeda also moves assets in the form of precious metals and gemstones, which can be easily and virtually anonymously transferred to cash. Precious stones like diamonds are easily smuggled because of high value and light weight. The international diamond industry is fragmented in numerous small mining operations located in remote areas of Africa. These countries often have lax border controls and an ineffective rule of law. Routes to move diamonds have also been established for decades as a mechanism for tax evasion or moving stolen diamonds. Gold also represent an opportunity for moving assets, especially since the gold trade and the hawala system are almost symbiotic (Greenberg et al 2002: 11). The advantages of using gold are, firstly, that it is a “paper-less” trade, and secondly, that gold can be melted into any form and easily to smuggle across borders.

4 MULTILATERALISM, UNILATERALISM AND LEADERSHIP

4.1 Relevant International Bodies

Combating terrorist finance is obviously an international endeavour. It is in the interest of all states, and several multilateral institutions are involved. This state of affairs raises several important questions. Such as, to what degree is the work of the different bodies and states involved coordinated? Is constructive leadership provided, thereby strengthening coordination? Is there a reasonable and effective functional division of labour between bodies such as the UN, the FATF and the IMF? What are the main problems today along these dimensions? These questions will be discussed in the following section with subsections.

On the face of things, the division of labour between different multilateral bodies is the most clear-cut issue. There are three main institutional clusters involved: First and foremost the UN, with its Counter Terrorist and Taliban/Al-Qaeda sanctions Committees (known as CTC and 1267 committee respectively) in New York and the Office of Drugs and Crime (UNDOC) in Vienna. Then we have the more anonymous, but highly specialised technical bodies like the Financial Action Task Force (FATF), co-located with the OECD, but established by the then G7 in 1989 and the Egmont group of Financial Intelligence Units. Finally we have the Bretton Woods institutions: the International Monetary Fund and the World Bank in Washington DC.

4.2 The 1999 Terrorist Financing Convention

The 1999 United Nations Convention for the Suppression of Terrorist Financing was proposed 18 months before 9/11, but it received little serious attention before the attacks of 2001. The adoption of the Convention forms the cornerstone of the struggle against terrorism (Bantekas 2003: 323). It seeks to block the flow of terrorist funds without disrupting the circulation of capital across global markets. The Convention establishes three main obligations for states. First, it establishes the offence of financing of terrorism in criminal legislation. Second, it obliges states to engages in a wide range of cooperation with other states, and provide each other with legal assistance in matters relating the Convention. Third, it enacts requirements concerning the role of financial institutions in the detection and reporting of evidence of the financing of terrorism acts.

The Convention contains detailed provisions on mutual legal assistance and extradition that go much further than the nine previous anti-terrorism Conventions. One of the most significant contributions to the construction of an international regime to combat the financing of terrorism is the establishment of a detailed framework for international cooperation in this area, as represented in the Convention.

4.3 Resolution 1373

Prior to 9/11 the UN Security Council had taken concrete actions against the funding of Bin Laden and the Taliban regime in Afghanistan, through Security Council resolution 1267.

Although this action consisted of ordering the freezing of related funds, the actions were insignificant compared to those adopted in the aftermath of 9/11. Two weeks after the attacks, in an effort to assure UN support for combating terrorist financing, the Security Council unanimously adopted Resolution 1373, a binding document containing obligations that the majority of states had not been wiling to accept in the past.

Before September 2001, only four states had ratified the Convention, the Financial Action Task Force (FATF) had not explicitly addressed the issue, and only a few Western states had taken domestic measures regarding the financing of terrorism. Resolution 1373 changed this overnight. The resolution called on all member states to sign and ratify the 1999 Convention. Furthermore, it criminalized all activities falling within the ambit of terrorist financing; it obliged states to freeze all funds or financial assets of persons and entities that are directly or indirectly used to commit terrorist acts or that are owned and controlled by persons engaged in, or associated with terrorism; it obliged states to prevent their nationals (including private financial institutions) from making such funds available, in effect imposing strict client detection measures, suspicious transaction report procedures, and subordination to other intergovernmental institutions in order to receive the names of designated terrorist organizations or individuals; and it imposed substantive and procedural criminal law measures at the domestic level, including an obligation to cooperate in the acquisition of evidence for criminal proceedings.

Resolution 1373 was neither the first, nor the last, resolution to address the financing of terrorism, but arguably the most important. It was important because it characterized terrorism as a threat to international peace and security. This designation triggered the Council’s option to invoke Chapter VII of the UN Charter. This made the resolution immediately binding on all member states. To implement and monitor the terms of the resolution, the Council also decided to establish the Counter-Terrorism Committee (CTC). Member states were obliged to report to the CTC, within ninety days, on the steps they had taken to implement the resolution, thus the resolution had established a mechanism whereby states’ efforts in countering terrorist financing could be assessed.

Before UNSCR 1373 a typical member state report on the implementation of a given resolution would be minimal and “one-off”, typically indicating that the state in question was complying “with the best of our ability” (Biersteker 2005). The CTC, in contrast, empowered by mandatory reporting requirements provided explicit guidelines and thus set in motion a process of iterated reporting and much closer monitoring. In addition state’s reports are published on the web thus introducing a level of transparency that is new to multilateral processes of this type.

But the picture is not all rosy. The CTC still has several challenges to the work it is doing. Although all member states have reported at least once on the implementation of the resolutions that address terrorist financing, some reports have significant gaps. Moreover, the explicit guidelines notwithstanding, it is not always easy to establish whether what is reported in reality is a paper tiger or something that really bites. For instance, a country can describe a legal mechanism that the CTC-experts are unfamiliar with, or a state can pass the relevant laws, but there is no infrastructure to implement it. When the CTC conducted its first round of analysis of the country reports, it found that not one country was fully compliant. Thus, effective implementation has become a challenge in all UN member states. The CTC has so far neither pointed to any defaulting states, nor has the Council specified how it would react in such circumstances. One last general observation made by the CTC is that countries that have participated in the Financial Action Task Force (FATF) are on average more compliant than others.

4.4 Resolution 1377 – Technical Assistance

The problem of technical assistance is addressed in resolution 1377 of November 2001, which called upon member states to provide technical assistance to countries requesting it.
Another UN-body involved in technical assistance for counter terrorist finance purposes is the Vienna-based United Nations Office of Drugs and Crime (UNDOC). Since efforts got under way to implement the proceeds of crime provisions of the 1988 Vienna convention[3], this body has been providing technical assistance to states that have the political will but lack capacity for implementing anti-money laundering (AML)-measures. Mirroring the increased scope of the standard setting FATF's activities to include counter terrorist financing-work (CTF) (see below), the UNDOC now also focuses on both AML and CTF. As we shall see below other bodies like the FATF and the World Bank are also involved in Technical Assistance. Since 9/11, the problem has less been one of finding resources for technical assistance than the sheer complexity of coordination, matching donors, recipients and agencies in an effective way.

4.5 Resolutions 1267 and 1390 – Freezing and Listing

On January 16, 2002, the UN adopted Resolution 1390, which modifies and continues the international sanctions against the Taliban, Usama Bin Laden and Al-Qaeda established first and foremost through UNSCR 1267 of 1999. Under Resolution 1390, the Security Council again acted under authority of Chapter VII of the UN Charter. That Resolution obligates all member states to "freeze without delay the funds and other financial assets or economic resources of Usama Bin Laden, members of the Al-Qaeda organization and the Taliban and other individuals, groups, undertakings and entities associated with them" as designated on continually updated lists. This last formulation reflects that the CTC is not the only UN-body involved in CTF-work. The Al-Qaeda sanctions committee established through UNSCR 1267 (known as the 1267 committee) has taken on operational and tactical responsibility to complement the more strategic "infrastructure-oriented" work of the CTC. The 1267 committee maintains the UN's global list of individuals and entities designated as supporting or engaging in acts of terrorism.

[3] The full name of this convention is: Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.

4.6 FATF Special Recommendations on Terrorist Financing

The FATF is an intergovernmental body entrusted with the development of domestic and international policies with regard to money laundering. At an extraordinary plenary meeting in October 2001, FATF expanded its mission to encompass the issue of terrorist financing. It adopted Eight Special Recommendations, in addition to its anti-money laundering recommendations, which constitute the new international standards to prevent and combat terrorist financing. FATF called on all countries to adopt and implement the Special Recommendations in an effort to deny terrorists and their supporters, access to the international financial system. The agreement on the recommendations commit members to take immediate steps to ratify counterterrorism treaties, criminalize terrorist financing, freeze and confiscate terrorist assets, report suspicious transactions linked to terrorism, provide the widest possible range of assistance to other countries' law enforcement and regulatory authorities for terrorist investigations, impose anti-money laundering requirements on alternative remittance systems, strengthen customer identification in international and domestic wire transfers, and ensure that entities, in particular nonprofit organizations, cannot be misused to finance terrorism. The special recommendations were followed by an action plan in order to ensure effective implementation of the new standards.

4.6.1 Institutionalised knowledge sharing

An important aspect of the FATF is to provide a venue for sharing expertise and experience between law enforcement officers and financial regulators on trends in money laundering and terrorist finance. Both money laundering and the financing of terrorism are dynamic fields where new techniques or patterns can emerge in one locality and then spread to others. The bi-annual meetings of FATF always includes so-called "typologies sessions" where "field workers" from different countries learn from each other. Another arena for such sharing of information and knowledge is the so-called Egmont Group where officials from Financial Intelligence Units meet.

The Egmont Group is an international organization of FIUs from various countries around the world. As of June 2004, FIUs are established in 94 countries. The FIUs in each country receives financial information from financial institutions, analyzes and disseminates the information domestically to the relevant government authorities, and internationally to other FIUs in support of national and international law enforcement operations. The FIUs have agreed to work to eliminate impediments to information exchange; make terrorist financing a form of suspicious activity to be reported by all financial sectors to their respective FIUs; undertake joint studies in particular money laundering vulnerabilities, especially when they may have some bearing on counter-terrorism, such as hawala.

4.7 Efforts by the International Monetary Fund and the World Bank

After 9/11 the International Monetary Fund (IMF) and the World Bank entered the campaign to disrupt terrorist financing. In November 2001, the IMF's International Monetary Committee (IMFC) called on all countries to establish FIUs and to increase information exchange across borders. Also, the World Bank held a ministerial-level meeting in November 2001, and pledged to aid in capacity-building in states that are ill-equipped to regulate money-laundering or terrorist financing and who are unlikely to meet the new international standards. The IMFC then agreed to counter terrorist financing by accelerating its assessments of offshore financial centers, which were already in place, and to work more closely with FATF to develop a common methodology on these issues.

The IMF now takes a broader approach to help all member-countries identify their regulatory weaknesses in combating terrorist financing and money laundering. Consequently, the IMF's assessments of its members AML/CTF regimes are now an integrated part of their financial sector assessments, and the ongoing assessments of OFCs. The assessments are supposed to identify potential weaknesses in the AML/CFT regimes as a basis for developing corrective action (Aninat 2002: 6). The IMF, along with the World Bank, and officials from the UN and the Organization for Security and Co-operation in Europe (OSCE), then provides technical assistance in drafting the relevant legislation.

5 IMPACTS AND CHALLENGES

Since terrorist organizations do not release any financial statements, we will neither know precisely how much money is flowing to terrorists in a given year, nor will we know how much money that was intended for terrorists but that did not reach their recipients due to the CTF-efforts. We simply do not know the true extent of terrorists' financial resources.

Despite these uncertainties, success in the fight against the financing of terrorism has tended to be measured quantitatively by focusing on; how much money has been frozen or seized; how many countries are freezing assets or upgrading their laws to make it harder to move money illegally etc. Although, this may be politically satisfying in justifying the efforts, such measures can also be misleading and thus "falsely providing a sense of accomplishment when perhaps little of significance has actually been achieved" (Zagaris 2004: 147).

In an article prepared for the Journal of Money Laundering Control, a working group debates the problem of how to judge the potential impact of measures to restrict terrorist funding. To do this, they argue, one would have to know "(a) how much money the would-be terrorists need to carry out their plans (which plans of course might be a function of what funds and other instrumentalities were available); and (b) what legitimate and illegitimate means of financial support they have available at any given moment in time" (O'Brien 2003: 275). On top of that, the total stock of funds available for terrorists remains both "unknown and dynamic" (Ibid). The size will depend on the degree of support and opposition to existing terrorist movements, and the number of terrorist movements; whether established movements diminish or new ones come into existence. The total stock of funds available for terrorist use, therefore, "should not be seen as an absolute sum but as conditional upon a flexible set of factors" (Ibid).

To evaluate the efforts based on such quantified impacts is a problematic task. It is mostly based on, and giving us, inaccurate estimates. Also, for most of us, the elimination of one terrorist attack can justify enormous preventive efforts. But, regardless of how many terrorist cells or planned terrorist actions that may be disrupted; the current CTF-efforts have its limitations, and throwing estimates around cannot conceal this. Impacts tend to bring about new unexpected challenges. When some loopholes are closed, others open up.

The rest of this section will focus on this mutual relationship between impacts and challenges. The main issues that will be discussed are, firstly, the emergence of a new regulatory regime and how well this is suited to counter terrorist financing. As will be outlined, terrorist financing, with its particular attributes, seems to raise specific challenges when it comes to detection, investigation and prosecution. Secondly, what are the main impacts and challenges, both technically and politically of using the list-making strategy? And, finally, how have these CTF-efforts affected Al-Qaeda, and, furthermore, are the "tools" available robust enough to combat an adaptive enemy?

5.1 Terrorist Financing and the Money Laundering Paradigm

Measures to combat terrorist financing have been built upon the foundations of initiatives already established for the prevention of financial crime, including money laundering (Navias 2002: 62). Existing international regulatory bodies such as the FATF and the United Nations have long been involved in attempts to coordinate reactions to all forms of trans-border financial crime. In the immediate aftermath of 9/11, it thus appeared that the most effective way to combat terrorist financing was to redirect and intensify the efforts of already existing multilateral monitoring and coordinating bodies. Terrorist financing is thought to use many of the same techniques as in money laundering, and, therefore, many of the same countermeasures are similar. Furthermore, many terrorist organizations are known to finance their activities from criminal proceeds (Aninat 2002: 2). On a general level, therefore, both anti-money laundering and counter-terrorist finance efforts can benefit greatly from increased transparency and accountability in the world global financial system.

Despite these key similarities between terrorist financing and laundering of the proceeds of organized crime, there are differences that are important to be aware of. First of all, terrorists and criminals have different goals. Criminals primarily seek financial gains. The primary motivation for terrorism, however, is not financial. Instead, terrorists' financial motivations are secondary to political and ideological objectives. Second, particularly the funding sources but also the methods by which they generate and distribute funds sometimes differ from those of criminal organizations. In addition to revenues raised from criminal activities, there are three other main categories of funding that terrorist organisations avail themselves of (Navias 2002: 68-69):

- State financial sponsorship
- Donations and contributions
- Legitimate business activities

State sponsorship seems to be declining and of less relevance after the fall of the Taliban regime. What still seems to be increasingly important is the significant proportion of terrorist finances that is not derived from specific criminal activity but generated from legitimate funding sources such as charities or other forms of donations or contributions, or from legitimate businesses (Rider 2002: 18).

5.2 Reverse Money Laundering

In light of the particular attributes of terrorist financing, a key question is whether existing regulations and laws are suited as tools for combating terrorism. It can be instructive to compare money laundering with terrorist financing on a more detailed level: There are several key differences relating to size, complexity, legality (terrorist finance often "lack" a predicate offence) and urgency. Anti-money laundering legislation is based on the assumption that the funds in question are illicit (Navias 2002: 67). Actually, money laundering is a rather straightforward concept: it is the process by which proceeds from crime are disguised in order to hide their illicit origin. Before the money is reintroduced into the economy it goes through a series of dubious operations intended to give the criminals the opportunity to spend and invest it without raising suspicion. Thus, the whole process is criminal. In contrast, terrorist financing frequently involves funds that are unconnected to any illegal activity. Thus, often only the last step in the process is criminal (Reinholt 2003: 7).

In other words, while money laundering involves the process in which criminal proceeds, or dirty money, is laundered so that it appears to be legitimately derived, terrorist financing can be described as a process where money originating from legal sources, becomes dirty by virtue of its use in terrorist activity. That is why the process is often referred to as "reverse money laundering" – meaning that clean money, which may even be declared to tax authorities, becomes contaminated only after the terrorist attack.

In "reverse money laundering" neither the source nor the funds are as exposed as in traditional laundering. The financial resources allocated for terrorists' day-to-day activities, which most likely overshadow the specific cost of conducting an terrorist attack, are not as exposed to law enforcement as the financial resources of criminal groups, whose involvement in criminal activity exposes the funds connected to these illegal dealings from the moment they are derived and through the whole process of disguising the source. "Reverse money laundering" is in many ways similar to capital flight and tax evasion. The latter normally involves legitimately accumulated funds, but at the same time, there is an intention to do an illegal act like evading taxes or other forms of regulation. Likewise, as terrorist financing may be directed at future activity, the only criminal offence that has been committed when the financing takes place may be conspiracy to commit a terrorist act. This not only makes it challenging to detect, but it may also – and we shall return to this below – require a different investigative approach, which in turn also raises a difficult trade-off between concerns for due process and effectiveness.

Also, while money laundering often involves large amounts of money, terrorist acts can have devastating effects with only a small amount of money. Obviously the amount of money believed to finance a large-scale terrorist operation like the 9/11 attacks is diminutive when compared to the volumes of money in both day-to-day commercial transactions and typical money laundering operations (Aninat 2002: 2). Because of the limited amounts of funds required at the final stage of terrorist actions, and the range of legitimate sources and uses of funds, the challenge of tracking terrorist financial transactions can be bigger, or at least different, than following the money trails of "regular" criminal groups, which in and of itself is already a formidable challenge. According to Zagarias the merging of anti-money laundering and anti-terrorist financing efforts may be unsuccessful. In his words, "Since terrorist financing normally involves the disbursement and movement of small amounts of money often derived from legitimate or quasi-legitimate sources, the chances of financial institutions detecting such activities are negligible under a regulatory framework developed for larger-scale transactions" (Zagaris 2004: 156).

According to Navias (2002:69), transactions supporting terrorist actions are neither quantitatively nor "by category of the type requiring, without other indicators, additional scrutiny by those financial institutions involved in the transaction". In fact, the amounts transferred in past terrorist attacks are so small that they "barely need laundering and can easily be hidden in any financial network" (Johnson 2002: 10). Also, wire transfers of that size occur hourly and such small amounts do not even have to be wired into the country at all, because a deposit "into a foreign bank that is on the US automated teller machine (ATM) network will allow someone in the USA to withdraw whatever he needs from the foreign bank with his ATM card, just as an American tourist or business traveler uses an ATM card when he is traveling overseas" (Casella 2004: 281).

Because it is rooted in the anti-money laundering paradigm, much of the enacted legislation focuses on the past: by looking backwards to reveal the source and how it is disguised (Kochan 2003: 4). According to Johnson, this makes existing anti-money laundering legislation difficult to apply since "it is designed around money laundering having an implied or specific predicate offence" and, thus, "laws would have to be changed if laundering is to be identified prior to the money being used in a criminal act, rather than the laundering taking place after the crime has been committed" (Johnson 2003: 10).

For effective law enforcement to take place, the broad definition of terrorist financing, where providing or collecting funds with the *intention or knowledge* that they will be used in terrorist activity, represents a staggering challenge. From a legal perspective, it can be extremely difficult to prove that funds were intended specifically for terrorism. Moreover, "it is difficult to prove the intent because it is terribly hard to tell where the money ends up" and "given the difficulties in proving where the money goes – that is, in proving a link to terrorism – it is very difficult to use the new terrorism financing statutes that were enacted to help in attacking this problem" (Cassella 2003: 282).

Another problem with fighting terrorist financing with money laundering tools, is that the tools may be both slow and inefficient in preventing acts of terrorism. As Malkin and Elizur describe it, "catching a common criminal or political cleptocrat after the fact with evidence of money laundering that can be used in court is just fine; catching a terrorist after the fact can be a catastrophe, as it was on September 11th" (Malkin and Elizur 2002: 64). After the attacks had occurred, it still took several months to track the operation's estimated $500 000, and this despite the fact that the main bulk of transfers was made through U.S. channels.

There are also challenges at a more systemic level. In the last 30 years, a steady deregulation of international finance has taken place. This development was not intended for tracking terrorist assets but to support further integration of international financial markets; a benefit that increased regulation reductions (Basile 2004: 174). Thus, ideologically, there is an argument against "revolutionizing" the global financial system in order to combat terrorist financing. Assuming that market abuse whether by criminals or terrorists will never be totally removed from the global financial system, it can be argued that the "extent of regulation required to serve such a goal actually undermines the functioning of those very markets that the regulation seeks to protect" (Navias 2002: 73). For instance, international trade relies on banking ties between the Middle East and the Western banks, and, although increased regulation of correspondent banking relationships may disrupt terrorist funding, it is not necessarily feasible since it "will also significantly impact the ability of large corporations to invest in the region" (Basile 2004: 175).

In this context Basile identifies two primary reasons why the international regulatory environment is not the "silver bullet" in fighting the financing of terrorism. The first is that "the legal and regulatory structures of foreign financial markets are different and financial transfers regulations between these markets are not yet designed to identify terrorist funds." Secondly, a terrorist organization like Al-Qaeda "has a global financial system of non-U.S. based regulated and unregulated banks, including the Islamic banking system, through which it can still transfer, store, and invest its funds (Basile 2004: 174).

Frustration among law enforcement agencies is certainly shared by banks and financial institutions, which are supposed to play a vital role in the "war on terror". Also for banks, efforts to detect terrorist financing are dealt with through existing money laundering mechanisms (Fitzgerald 2003: 5). When trying to perform this task, banks run into many of the same problems as mentioned above. Since neither "reverse money laundering" nor small money transfers have the ability to raise any red flags within the existing reporting schemes, the systems have had to adapt to the new demands. But, adapting banks surveillance systems to prevent "reverse money laundering" is not an easy task. The money laundering systems that banks were using are risk-based and linked to unusual transactions or activity. Adapting these systems to intercept “reverse money laundering” will require much closer analysis of sources and destinations of funds (Kochan 2003: 4).

Banks’ main task is to identify and report on suspicious transactions, and the principal tool is the so-called suspicious activity reports (SAR). There are problems with this approach though. First, SARs are more “useful in providing a case afterward than in preventing crime beforehand” (Malkin and Elizur 2002: 62). Thus, in CTF cases, SARs have largely “failed to help police arrest terrorists” (Kochan 2003: 2). Second, as banks have become more aware of the need to report suspicious transactions, reported SARs have proliferated around the world, and, as a result, a simultaneous shortage of manpower has been uncovered. As a consequence, SARs pile up and slow down the investigative process, and on top of that, information gathering on SARs often requires cooperation between many “turf-protective agencies” (Malkin and Elizur 2002: 63). Thus, as a worst-case scenario, relevant information cannot be used preventively in case of a possible terrorist attack.

Although, on the positive side, banks have taken the new responsibility seriously by filing SARs; enhancing bank computer systems; and collecting the identity of new clients, challenges remain related to correspondent banking practices. When the names of suspected terrorists extend to accounts abroad, banks face what they call “the problem of the customer’s customer,” referring to inadequate information on the client’s identity (Ibid). But banks have cleaned up many of the loose practices and know-your-customer is becoming the new mantra in international banking (Kochan 2003: 2).

Even if an international regulatory regime will emerge and become adjusted to the new demands to combat terrorist financing, there is still the challenge of funds being generated and transferred through jurisdictions that have highly inadequate oversight. Although, terrorist finances will, arguably, meet a “wall” when trying to penetrate the USA, EU or G20 countries, loopholes may exist elsewhere. But, also in parts of the world, which currently are more vulnerable to abuse by terrorists, measures are taken to enhance the regulatory and legislative systems. According to the annual US International Narcotics Control Strategy Report (2003), the countries most vulnerable to terrorist financing, are receiving technical assistance packages to develop comprehensive anti-money laundering regimes to eliminate these vulnerabilities. Among other recent initiatives, two new FATF-style regional bodies were established in the crucial areas of the Middle East and Central Asia.

In other words, as more countries achieve a higher level of regulatory standard, one possibility is that the informal sector will gradually become marginalized and isolated from the formal sector. Thereby, as “the unregulated sector shrinks, so more financial assets and financial transactions fall under the scrutiny of the regulated sector”, and, as a consequence, those that “want to remain out of the regulated sector should find that the section of the global network in which they can easily operate without oversight is shrinking and moving money to the regulated sector is getting more difficult” (Johnson 2002: 15).

Both the FATF and the USA call for the licensing of providers of informal remittance systems. As many of those will probably seek licenses, others will go further underground and still be available for the moving of terrorist funds (Johnson 2002: 15). The balance between the formal and informal is, however, not necessarily a zero-sum game. Informal remittance systems can be seen as a market response; thus, an overly restrictive approach may not have the intended effect of minimizing such systems. Instead they might go further underground and possibly also proliferate. It is problematic to regulate a system that by definition is unregulated. To regulate it would be to change it, or to create a new and modified type of remittance system. New unregulated systems may then emerge as long as there is a difference in cost and/or availability. On the other hand, it is first and foremost the potential anonymity of the system that presents risk of terrorist financing, and not the other attributes that are so crucial to customers in poor and marginalized regions. According to a report by the FATF, a viable solution to the problems related to the informal remittance systems can only be “found in the larger context of improving basic financial services infrastructure and regulatory/oversight regimes in those countries that are the primary receiving locations” for informal remittance transactions (FATF 2003: 10). Because of the widespread use of such systems, a total crackdown of hawala organizations may not only drive them underground, it may also be neither desirable nor feasible from a socio-political perspective. As regards desirability, a hard-line approach is difficult to legitimize. The vast majority of transactions are legal, and a crackdown would have potentially devastating effects, especially on poor people in poor regions. As regards feasibility, hawala organizations are numerous and extremely powerful in the Arab and Middle Eastern region. The governments in countries where hawala flourish may have neither the capacity nor the will to enforce such regulations. Also, it could backlash against the government since it could be seen as it was “caving in to Western demands at the expense of Muslim tradition” (Looney 2003: 166). Hence, the challenges facing attempts to clamp down on hawala must be “understood in relation to the conflicting attitudes towards this particular issue which often exist between Western and non-Western mind-sets” (Nawas et al 2002: 334).

5.3 Adaptive and Resilient Al-Qaeda

A final set of factors that can frustrate efforts to curb terrorist finance is related to the adaptive behavior of terrorist organizations like Al-Qaeda. As theory would lead us to expect, Al-Qaeda and other terrorist organizations are evolving enemies that continually respond to changing conditions. This in turn has implications for the effect of both current and future CTF-efforts. According to Basile, the post-9/11 financial warfare against terrorist financing is ill-equipped to disrupt Al-Qaeda’s funding, and, as a consequence, any impact on Al-Qaeda’s ability to operate has thus so far been minimal. Basile lists three main reasons for this (Basile 2004: 169):

- First, Al-Qaeda has built a strong network of financiers and operatives who are both frugally minded and business savvy. As a result, terrorist finances are often hidden in legitimate and illegitimate businesses and disguised as commodities and cash.

- Second, Al-Qaeda has learned to effectively leverage the global financial system of capital markets. Small financial transfers, under-regulated Islamic banking networks and informal transfer systems throughout the world make it almost impossible to stop Al-Qaeda from moving money.
- Third, Al-Qaeda has built a significant base of Islamic charities in Saudi Arabia with international divisions that have not been scrutinized or controlled by the regime.

In addition to relying on innovative funding mechanisms, Al-Qaeda has adapted to the chase instigated after 9/11 by “morphing into an even looser network, devolving more initiative and resources to local operatives”, and thereby, being “better able to survive the intense worldwide surveillance of authorities” (Jenkins 2002: 12, 17). This move from a hierarchical towards a more networked type of organization has implications for both its funding structure and the mechanisms in use.

This means that terrorist cells now try to develop funding strategies in order to remain self-managed, self-sufficient, and unconnected from the sources from which the organization raises funds. And by running “its sources of funding separately from the funding needs of terrorist cells”, Al-Qaeda keeps its “financial resources as discreet as possible while allowing operational cells to deploy without ever giving away information on Al-Qaeda’s underlying network” (Basile 2004: 171). The Madrid bombings for instance were primarily financed locally. It subsisted on petty crimes on the income side while frugal living conditions helped keep expenses down.

According to Jenkins (2002), Al-Qaeda is far from quitting or gone. Instead, in adapting to the new circumstances it may “disperse, change names, merge with other entities, or be absorbed into its own successors”, and as long as “its leadership, structure, operatives, relationships, financing, and ability to mobilize resources to support further terrorist operations” is intact, it remains a continuing challenge to CTF-efforts (Jenkins 2002: 17). In another study, Hoffman shares a rather pessimistic, or realistic, view on the current CTF-efforts, and states that although some $120 million of identifiable Al-Qaeda assets have been frozen, “ample funds may still be at disposal” (Hoffman 2003: 9).

The adaptive nature of Al-Qaeda illustrated above not only indicates how the CTF-campaign has affected Al-Qaeda, but also, implicitly, points to future challenges in combating the financing of terrorism.

5.4 Lists and Legitimacy

As has been emphasized above, there are a myriad of legal and illegal terrorist financing sources as well as methods for moving funds. This in turn makes it a very difficult to determine which funds are going where, and to complicate it further, whether the “source” is wittingly or unwittingly funding terrorism. Some terrorist organizations may even generate funds for a humanitarian purpose. To trace funds from a western country through a “shadowy” Third World financial sector or through the layer of secrecy offshore, to the ultimate use in buying bombs and bullets, and to establish that the providers knew that the funds where going to terrorist activity, is an extremely complicated and difficult task.

According to Breinholt (2003: 9), this complexity led to an approach to terrorist financing enforcement that was unique to the US at first and then later increasingly adopted by other countries. In the immediate aftermath of 9/11, the international community responded to the attacks mainly through the adoption of the UN resolutions mentioned earlier. At first, resolution 1373 asked member-states to cooperate without explicitly specifying how to do this. Soon after, following a US initiative, an informal practice developed between the UN member-states where lists of individuals and organizations, suspected of having a connection to terrorists, were exchanged with the goal of freezing their assets.

This approach involves *list-making*; "an administrative procedure which results in the publication of lists of the designated groups and persons that, according to facts contained in administrative records compiled for this specific purpose, are conclusively determined to be terrorists" (Ibid). Thus, if a group or person is included on the list, it becomes a crime to engage in financial transactions with that entity, even if the transaction itself is not designed to promote terrorism. As a consequence, the list-making approach to terrorist financing effectively altered the enforcement landscape (Ibid). Instead of tracing funds to their ultimate use and proving the intention to support terrorist activity, the process chooses another operational approach. The enforcement challenge now is to establish whether persons are engaged in financial transactions with entities they knew were acting on behalf of designated terrorist entities.

In order to utilize the new international regulatory regime and actually track down the financing of terrorism, the US has continued to designate suspect people and organizations. This process still takes the shape of the US making demands and other states responding. Since 9/11 lists have been at the heart of all international measures to counter terrorist financing. US Congressman Levey (Levey 2004) gives voice to the optimistic view of what can be achieved through this method, and lists four ends:

1. Shutting down the pipeline through which designated parties raise and move money;
2. Informing third parties, who may be unwittingly financing terrorist activity, of their association with supporters of terrorism;
3. Deterring non-designated parties, who might otherwise be willing to finance terrorist activity; and
4. Forcing terrorists to use potentially more costly, less efficient and/or less reliable means of financing.

From this Levey draws the conclusion that "The benefits of designation cannot be measured simply by totaling an amount of frozen assets" before he continues in a somewhat more evocative style (Ibid.):

> Terrorist-related accounts are not pools of water awaiting discovery as much as they are rivers with funds constantly flowing in and out. By freezing accounts, we dam that river, not only

> capturing whatever assets present at that moment but, more importantly, ensuring that this individual or organization can never in the future act as a conduit of funds to terrorists. If fully implemented, a designation excommunicates supporters of terrorism from the formal financial system, incapacitating them or driving them to more expensive, more cumbersome, and riskier channels.

Officially three lists exist, one maintained by the UN, one by the US and one by the EU. In reality most of the intelligence underpinning all three originates in the US. That is, we must assume it stems from US intelligence sources. The origin is somewhat obscured by the fact that there is no obligation to provide back-up information under this system whereby individuals and organizations that are deemed to be connected to terrorist activities are identified. The UN-list, which is mainly drawn from the US-list, is then circulated, to member states, who in turn circulate it among their relevant institutions. By doing this, the UN requires member states to recognize the freeze orders of other member states, mainly the US, directed at suspected entities without providing any international guarantees that such sanctions are not being imposed in an arbitrary and capricious manner. Much dispute has arisen amongst major states with respect to whether such orders should be given mutual respect if issued without adherence to basic human rights.

In January 2002, both the Swedish and the French Governments raised the issue of whether they were obliged to recognize certain freeze orders of the US in the Security Council. Sweden and France sought to highlight the issue of the rule of law and the protections, if any, entities were entitled to, when confronted with asset freeze orders issued by foreign governments that were acting within the legal framework of the UN sanctions committee. The critique was based on what they saw as human rights and due process violations, and the UN Security Council was urged to "review its sanctions list and to establish some basic rules for enforcing anti-terrorist financial sanctions that would include specific criteria to impose sanctions, such as a direct link to Al-Q or the Taliban, and a procedure for regularly reviewing the list" (Zagaris 2004: 151). The US opposed, arguing that disclosing the requested information would threaten national security by endangering the ability to gather further intelligence (Ibid).

In addition to the European critique, a report by a group of experts working for the UN 1267 Sanctions Committee, noted that the list this committee had drawn up had lost much of its credibility and operational value (Balzaretti 2004: 16). As a result the UN is working on improving the quality of the lists it distributes, and on establishing appeal and de-listing procedures. Still, at issue are very basic factors like the spelling of names and providing better documentation for why a given individual or organization is on the list in the first place. This creates problems for both law enforcement officials and for their targets. For law enforcement agents it is difficult to prosecute and move beyond the freezing of assets on the basis of the flimsy type of "evidence" that lists constitute. For their targets it means that their funds can be frozen for long periods of time without any follow-up measures or clarifications. There is no resolution in sight, and in the meantime innocent people may well suffer from being cut off from their financial assets.

Although, at first, many entities were designated, the whole process seems to have reached a deadlock. The many challenges raised by the critique are diverse. Balzaretti sums up many of the important challenges, that “desperately” need to be addressed if the listing approach is not to lose both its function and credibility (Balzaretti 2004: 14):

1. Where do those affected by the sanctions stand with regards to fundamental human rights?
2. Questions arise regarding the criteria applied to determine whether to add a name to the list. What kind or degree of proof is needed to determine whether a person is connected to a terrorist organization?
3. Why do the member states receiving the lists have only limited access to the information on which the decision to add a name to a list is based, and why is all access denied to those persons whose names feature on a list?
4. Concerning the burden of proof, should the obligation (on proof of innocence) be placed on the persons whose names appear on a list when in many cases they have no idea on what they are being accused of?
5. Should a mechanism allow targeted people to have their case reviewed by a judicial authority, or if by an extra-judicial authority at least by an independent one both at the national and international levels?
6. Must one really accept the notion that the rights of listed people cannot be cited in opposition to a measure decided by the UN Security Council concerning peace and international security? Can the one, or, must the one, prevail over the other?
7. Concerning the appropriateness of these measures in the light of international standards of protection of human rights, must Security Council resolutions take precedence over international or regional treaties such as the UN Covenant on Civil and Political Rights of 1996 or the European Convention on Human Rights?
8. With regard to the norms carefully negotiated between States in the area of judicial assistance in criminal matters, which define the legal framework for exchanging information and adopting constraining measures including preventive blocking and confiscation, and which are taken within the context of a criminal procedure, do these norms still apply when the persons suspected of maintaining links with terrorist groups are treated as quasi-criminals?

Despite the above-mentioned questions regarding individual rights, there are some safeguards. First, before an entity is designated, a kind of consensus among the members of the Security Council is required. Second, exceptions to the freezing of accounts can be given in cases where blocking of assets has serious consequences for family members. Third, a committee and panel of experts are administering and monitoring the whole process. And, finally, if a state wants to designate a citizen of another state, the latter state can enter into negotiations with the initiating state with the aim of deleting the listed person, if it questions the listing of that individual. A problem, though, is that these safeguards are of “a political nature and do not offer sufficient guarantees of protection of the interests of the listed individuals” (Balzaretti 2004: 15).

Also the lack of a proper de-listing procedure, or process of appeal, points to a larger problem within which the list-problematique is situated. Namely that of due process concerns versus the logic of intelligence. Above we discussed the problems of effectiveness that arise when one tries to fight terrorist finance with tools designed to combat money laundering. On the flip side of that coin however, we find legitimacy problems. Due process means that law enforcement officers will work to find evidence that will stand up in a court of law, before a judge, after the event (as in the typical money laundering case). Due process means that there are fairly strict procedural demands. Terrorism on the other hand is naturally the domain of intelligence bodies because you want to interfere before an act has been committed. Most terrorist acts consist of many perfectly legal steps before the event, and information about the terrorist intent of those involved are gathered by covert methods such as the work of informers and field agents, and the use of phone and internet-taps and so on. These kinds of materials will not normally hold up as evidence before a judge. And even if the material had the potential to hold up, it will often be classified. The major challenge ahead for counter-terrorist finance work is thus arguably to balance the demands of due process with those of the logic of intelligence. This problem was not acute in the immediate aftermath of 9/11, but as time passes, the importance of the concerns listed above increases. This need to strike a balance is now becoming a concern of prime importance for specialists and practitioners of international law. Here the international legal community can probably draw lessons from procedural practices developed in order to fight (international) organized crime. One avenue probably worth pursuing is that of designating special judges to evaluate evidence gathered by intelligence techniques in anonymity. One potential candidate for taking on this work is the International Criminal Court, but here, paradoxically, US resistance to establishing this institution is a stumbling block for progress.

6 SUMMARY AND CONCLUSIONS

The fight against the financing of terror has been at the top of the anti-terrorist agenda and at or near the top of the international agenda since the attacks of 9/11. One important premise for this is the broad definition of terrorist finance that has been applied. The financing of the physical and ideological “infrastructure” of terrorism has been included in the concept of terrorist finance. If one, instead, had restricted the definition of terrorist finance to financing of the “end product”, the terrorist act itself, such a massive multilateral and multilevel effort would have made less sense. The effort has involved both strengthening existing (primarily) anti-money laundering legislation, and a new approach based on listing designated individuals and organizations. The report has identified many weaknesses of an anti-terrorist finance strategy built on strengthening anti-money laundering legislation, and that this has worked as a stimulant for the new list-based approach, but also that this approach in itself carries with it new problems, both technical and ethical.

It is impossible to gauge the exact impact of all these efforts, but what seems to be widely agreed among analysts is that Al-Qaeda has suffered financially because of the less-permissive environment. Financial contributors and mechanisms are not only constrained by international efforts to limit terrorist financing, but potential donors are most likely “deterred by threats of negative publicity, blocked investments, asset seizures, exposure to lawsuits, or merely increased scrutiny of their financial activities” (Jenkins 2002: 17). A more stringent regulatory framework has also supported law enforcement investigations, and it has therefore contributed to the relative successes we have witnessed in this field since 9/11. Thus, “greater regulatory scrutiny in financial systems around the world is further marginalizing those who would support terrorism” (Jenkins 2002: 26). Also, many key leaders and financiers have been killed or captured (Hoffman 2003: 8).

There are, however, many unresolved issues: How is Al-Qaeda responding to the new environment, and, if so, are current CTF-measures loosing some of its relevance due to the evolving nature of terrorist financing? Can we conclude that the efforts so far have resulted in more difficult, but not prohibitive conditions for the likes of Al-Qaeda, because it now has to rely more on a combination of self-sufficient cells and informal finance channels? It is probably more difficult for terrorists to invest in large-scale infrastructure projects (like training camps) and large scale attacks.

Of course these are difficult if not impossible questions to answer precisely. It can, after all, be argued that the “war on terrorist financing” is still in its infancy. On the other hand, as the war is reaching adolescence; new problems have to be addressed. The “moral capital” and general goodwill enjoyed by the US as the nation which suffered the 9/11 attacks on its territory, appears to be eroding. This is due both to “external” reasons like the war in Iraq and more importantly, due to reasons internal to the war on terrorist finance. Concerns about human rights and due process have arisen because the war on terrorist finance has created a new interface between intelligence logic and methods, diplomacy and the rule of law in all nations participating in the war on terror.

In the future then, anti-terrorist finance efforts have, much like the enemy it is fighting, to evolve. They have to evolve in a manner that takes onboard challenges both to their effectiveness and to their legitimacy.

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