

Fighting Terror with Error: Effects of Fact-free Policy Making

Nikos Passas
Northeastern University

Rationale for Financial Controls



- Reduce possible harm
- Monitor militant activities
- Reconstruct events-conspiracies
- Force tactical changes and communications – more opportunities for intelligence gathering

Synchronizing counter-terrorism and economic policy



- "We will starve terrorists of funding, turn them against each other, rout them out of their safe hiding places and bring them to justice." President George W. Bush; September 24, 2001
- AML/AC
- “...remittances...are a tremendous source of capital flowing directly into the hands of consumers and households in the developing world. We agreed to work on reducing the roadblocks for people sending money back to their families. This means identifying and removing the barriers that slow the flow of remittances, make transactions expensive or encourage money to flow through informal channels” US Treasury Secretary John Snow, February 2004, G7.

Objectives



- Crime Control
 - Transparency (operators, clients and traceability)
 - Deterrence and prevention of abuse
 - Prevent terrorist finance (asset seizures)
 - Monitor militants
- Enhance free remittance/capital flows
 - Lower cost and access to widen range of options for remittances
 - Compliance
 - Consumer protection

Risks of erroneous AML/CTF



- Driving networks/transactions underground
- Collateral damage
- Alienation of ethnic groups
- Neglect of more serious problems
- Increase of economic/other asymmetries
- More grievances = fertile ground for recruiting militants

Problem



- Overemphasis on certain financial flows at the expense of riskier ones
- Example of money transfer regulation and reliance on private sector

Comparing rates

PKR-DRH rates in various markets on 8 December, 2003 in Dubai.

PKR for 1,000 DRH

11,905 [minus fees]

12,391

12,660

Options

Draft/bank rate


Money exchange rate

Hawala rate

Comparative amounts received in Pakistan for 100 USD from Dubai

Method of remittance	Charges	Total paid	PK Rupees received
Draft (exchange house)	1.36 - 2.722	101.36 - 102.722	5901 – 5910
Draft (Bank)	2.722 - 6.80	102.722 - 106.80	5890
TT (exchange house)	9.52 - 16.33	109.52 - 116.33	5901 – 5910
TT (Bank)	12.25 - 27.22	112.25 - 127.22	5890
Western Union	9.52	109.52	5858
Hawala	NIL	100	5920

What is the cost of current regulations?



- International reg. environment
- US regulation of money transfers
 - Federal v. States regulation
 - Due process and quality of evidence (al Barakaat case)

Country	Regulatory Regime	KYC threshold	Record keeping	Filings	Fees
Canada	No registration/ no licensing	CAN\$ 3,000	5 years	STR CTR above CAN\$ 10,000	none
France	Full bank license	Comprehensive prudential regime	n/a	n/a	n/a
Hong Kong	Registration	HK\$ 20,000	6 years	STR	none
Germany	Licensing	€ 2,500	6 years	STR	€ 1,000/percentage of annual turnover – min. € 650
India	1) wire transfer services: Registration 2) other forms of remittances, incl. banking channels, under the ‘Money Transfer Service Scheme’: licensing	All transactions	10 years	STR (once FIU is set up and becomes operational)	?
Italy	Licensing	€ 12,500	10 years	STR	none
Netherlands	Licensing	All transactions	5 years	STR CTR over € 2,000	Percentage of annual turnover – min € 3,000
Spain	Licensing	All transactions	6 years	STR CTR over € 3,000	?
United Arab Emirates	1) Hawala: registration 2) Exchange Houses: licensing	1) all transactions 2) AED 2,000	1) n/a 2) all transactions over AED 2,000	1) STR 2) STR	?
United Kingdom	Registration		5 years	STR	GB£ 60 per office
USA - Federal	Registration	US\$ 3,000	5 years	SAR over US\$ 2,000 CTR over US\$ 10,000	none

Federal regime



- Registration
- Record Keeping
- Reporting Suspicious Transactions
- KYC
- AML procedures even for unregistered agents

State

- Licensing
- Bond, capitalization, net worth, fees



State	Net worth	Bond	Fee
California	min \$ 500,000 in equity	Determined by Commissioner	\$ 5,000 plus \$50 per agent
Florida	min. 100,000 plus \$ 50,000 per location in FL up to \$ 500,000 - may be waived upon request	Set by commission rule – max. \$ 250,000 – up to \$500,000 in exceptional circumstances - may be waived upon request	Appl.. \$500 plus \$50 per agent; renewal \$1000 \$50 per agent up to \$20,000
New Jersey	(1) min. \$100,000 plus \$25,000 per location or agent in NJ up to \$1,000,000. (2) \$50,000 for foreign money transmitter plus \$10,000 per location or agent up to \$400,000	(1) min \$100,000 up to \$1,000,000 (2) foreign remitters: depending on volume \$25,000-\$100,000 - commissioner may require up to \$900,000	Appl.: \$1,000 Lic.: up to \$4,000 Biannual fee \$25 per location up to \$5,000
New York	Investments equivalent to outstanding payments	Min. \$ 500,000, unless superintendent determines lower amount suffices	\$ 500 annual + \$1,000 investig.
Illinois	\$35,000-\$500,000 depending on number of locations	Min. \$100,000 or average daily outstanding for 12 months - max. \$2,000,000	\$100 appl. \$100 license \$10 per/l – ren. \$100- \$10 p/l
Pennsylvania	\$500,000	\$1,000,000	Appl. \$ 1,000, renewal \$300
Texas	\$25,000 per location up to \$1,000,000	Min. \$300,000 determined by commissioner \$ 100,000 for first location, \$ 50,000 for each additional up to \$ 400,000	Appl./lic., invest. and renewal [\$500 licensing + \$2,500 invest.]
Virginia 7/1/2005	\$100,000-1,000,000 as determined by the Commission	\$25,000-1,000,000 as determined by the Commission	License \$500, renewal \$750

Account Closings



- OCC advisory
- Examiners' practice
- Bank initiative
- 100s of legitimate accounts closed
- Underserved and undeserved: Private industry ended up deciding who would get indispensable services and who would not
- Wrong priorities anyway: formal sector/trade

Remittances and terrorist finance



- Disconnect between tons of money and lack of resources in discovered cases
- Wide range of fund raising and transfer methods used by militants
- Informal channels not the most important one
- Most 9/11 funds transferred through banks and formal remitters

Hawala and AQ



- AQ used several trusted hawaladars in S. Asia and M. East, while operating in Afghanistan
- No use for 9/11
- No cases of hawala related terrorist finance cases in US-Europe so far
- Barakaat
- Xpress route to regulation without understanding or consent

Cost of Attacks



- Madrid bombings - \$1,000 (UN: less than \$10,000)
- Bali nightclub bombings - \$20,000 (UN: less than \$50,000)
- US embassy bombings in Kenya and Tanzania – 10,000 (UN: less than \$50,000)
- Attacks in Istanbul – UN: less than \$40,000
- 9/11 attacks – \$400-500k
- UK attack - £3000 (UK Treas.)

Barakaat Case Study



- Press conferences
- World-wide closure
- Arrests
- Records seized
- Assets frozen
- No terrorism charges filed – unlicensed money transfer charges
- Names still on the lists
- Unsubstantiated allegations reiterated in FATF report 2 weeks ago



- We saw 9/11 funds flow through formal institutions – no adverse consequences against them. We saw no funds flow through Barakaat and yet we devastated the most successful business in Somalia. What message does this convey? Benign regulation pursuing transparency? Forcing banks to go overboard while MSBs go underground?
- How is the message altered or supported by subsequent actions? Answer by looking at ICE data – no independent analysis of cases and results, no transfer of cases to FBI, but WP reports that very few had anything to do with terrorism at all.

May 23, 2005 press release



- ... nationwide campaign by ICE agents against unlicensed money transmittal businesses and underground “hawalas” has resulted in the arrest of 140 individuals, 138 criminal indictments, and the seizure of more than \$25.5 million in illicit proceeds since the enactment of the USA Patriot Act, which requires such businesses to be licensed and registered.

A group of people are performing a human pyramid in a swimming pool. One person is standing on the pool floor, with others standing on their shoulders. The background shows a grassy area and trees.

**Upside-down control;
Regulatory Externalities: Overboard and Underground**

Banks, MSBs, immigrants, traders, regulators, law enforcement, the public and the international community unhappy about the current regulatory regime.

Mosquitoes, Elephants and Balanced Regulation



Fighting a war on terror and shooting ourselves in the foot



- Networks of terror v. networks against terror
- Current efforts in need of evaluation and improvement
- Away from a bulldozer approach to regulatory symmetry
- Away from embedded academics, media and single-cause NGOs
- Shift towards more balanced, consensus based, genuinely collaborative, international effort

Context of Financial Controls



- The “regulatory tsunami”: UNTOC, UNCAC, AML/CFT
- Main goal: fight serious crime
- Other goals too: security, peace, good governance, human rights, poverty, economic growth, public health, the environment
- Externalities: privatization of controls, less accountability, risk of injustice, economic disruptions
- Ignorance of externalities, persistence and thoughtless application: “regulatory fundamentalism”
- Legitimacy v. “paper compliance” and illusions of success

Recommendations



- Establish facts on informal remittance infrastructures and comparative risks
- Look carefully into trade issues
- Enforce laws in context of wider social objectives
- Smart use of technologies and human capital
- Outreach and two-way communication with stakeholders and participants in markets
- Role of private sector – proactive and innovative on what to report and how to regulate
- Through multi-agency and international efforts

Thank you so much

Nikos Passas

+1-617-373 4309

n.passas@neu.edu

nikospassas1@yahoo.com