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DRAFTING NOTES ON SPECIFIC MATTERS

Criminalizing the Financing of Terrorism

General

Authorities wishing to implement the provisions of the Convention and to respond to the requirements of the Resolution would need to consider two separate but related types of conduct regarding the financing of terrorism. One is *the financing of terrorist acts*, as defined in Article 2 of the Convention. The other is *the provision of financial support to terrorists and terrorist organizations*, as stated in paragraph 1(d) of the Resolution. While the requirements relating to these forms of conduct are similar, they are not identical, and it will be for the authorities of each country to decide in which way each type of conduct will be characterized in local law.[109] Before considering the differences between the two requirements, it should be noted that paragraph 1(b) of the Resolution requires the criminalization of the financing of terrorist acts, using language that is very close to that of the Convention. Read with paragraph 3(d), which calls upon states to become parties to the Convention "as soon as possible," paragraph 1(b) of the Resolution is a clear reference to criminalization of the financing of terrorist acts as defined in the Convention. It would follow that paragraph 1(d) requires something additional to the criminalization of terrorist acts.

While both the Convention and paragraph 1(d) of the Resolution deal with the provision of financial assistance directed towards terrorism, there are notable differences between the two. First, while the Convention clearly requires the *criminalization* of the financing of terrorist acts, paragraph 1(d) of the Resolution appears to take a different approach. Rather than requiring that countries *criminalize* the provision of funds and services to terrorists, it requires them to "prohibit their nationals and entities within their territories" from making financial assistance available to terrorists and terrorist organizations. This language appears deliberate, as it stands in contrast to the language used in paragraph 1(b) of the Resolution referred to above, which requires the *criminalization* of the financing of terrorist acts. The thrust of

[109] The FATF Special Recommendations on Terrorist Financing also appear to take the view that there are two separate types of conduct to criminalize, as SR II sets as a standard the criminalization of the financing of *terrorism, terrorist acts, and terrorist organizations.*

paragraph 1(d) is to stop the flow of funds and financial services to terrorists and terrorist organizations, whether this is accomplished through criminalization or other means.

Second, as regards the nature of such assistance, the requirement in paragraph 1(d) of the Resolution is broader than that in the Convention. The Convention criminalizes the provision of "*funds*," which it defines as the equivalent of *assets*, while the Resolution uses the broader form "funds, financial assets or economic resources or financial or other related services." Taking into account the broad definition of "funds" in the Convention, what is covered by the Resolution and not by the Convention is the provision of "*financial or related services.*"[110]

Third, the range of persons and entities that must be prevented from receiving funds or services is defined in the Resolution, but not in the Convention. In the Resolution, the list of such persons includes not only the persons who commit or attempt to commit, or facilitate or participate in acts of terrorism, but also entities owned or controlled, directly or indirectly by such persons, and entities acting on behalf or at the direction of such persons. The Convention defines only terrorist acts, not terrorists or terrorism, and, by implication, any person who commits, or may commit, an act of terrorism, would be included.

It would follow from the above that, in addition to criminalizing the financing of terrorist acts in accordance with the Convention, the Resolution requires in its paragraph 1(d) that countries prevent the flow of funds and services to terrorists and terrorist organizations. The manner in which this is to be done is left to each country. One way to accomplish this would be to provide for the freezing of the assets of the classes of persons and entities enumerated in paragraph 1(d), and to prohibit the provision of financial and other services to such persons.

In many jurisdictions, the freezing of assets and the prohibition of the provision of resources would be based on the criminalization of the conduct alleged on the part of the owners of the assets to be frozen, and who would be the intended recipients of the financial assistance.[111] In others, the provisions would rest on the establishment of lists of persons and

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[110] It is unclear what "economic resources" adds to the other terms on the list.

[111] In addition to the criminal forfeiture systems described in this paragraph, some countries, including the United States, have civil forfeiture systems in which assets can be forfeited independently of criminal proceedings. *See* Stefan D. Cassalla, "Restraint and Forfeiture of Proceeds of Crime in International Cases: Lessons Learned and Ways Forward," *Proceedings of the 2002 Commonwealth Secretariat Oxford Conference on the Changing Face of International Cooperation in Criminal Matters in the 21st Century* (Commonwealth Secretariat, 2002), p. 183.

organizations deemed to be engaging in such conduct. For example, the Barbados Anti-Terrorism Act 2002-6 criminalizes both the provision or collection of funds intended for terrorism purposes, and the provision of financial services for such purposes. The freezing and forfeiture provisions of the Act are then linked to charges under the terrorism offense as so defined.[112] In other countries, such as Canada, the freezing of assets and the prohibition of financial support are based on a list of individuals and organizations issued by the Government on the basis of information that the person or entity is engaging in a terrorist activity, independently of any indictment against such person or entity.[113] In the context of the European Union, the measures called for in paragraph 1(b) of the Resolution on criminalization have been taken by each country member of the European Union, while the measures related to the freezing of assets of terrorists and terrorist organizations have been taken at the Union level.[114]

Defining Terrorist Acts

The nine treaties listed in the Annex to the Convention did not attempt to define terrorism, but rather defined specific acts in a way that did not use the term "terrorism." The most recent of these treaties, the International Convention for the Suppression of Terrorist Bombings, uses the terms "terrorist" and "terrorism" in its title and in its preamble, and refers to resolutions of the General Assembly on terrorism, but it defines the offense of terrorist bombing without using the term. As is the case of the nine treaties listed in its Annex, the Convention does not define terrorism. Rather, it contains a definition of *terrorist acts*, which provides the basis for the definition of the financing offenses set out in the Convention.

The Resolution does not define "terrorism." It requires states to "prevent and suppress the financing of terrorist acts,"[115] and to "become parties to the [...] Convention."[116] It also requires states "to prohibit [persons] from making any funds, financial assets or economic resources [...] for the benefit

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[112] *Anti-Terrorism Act 2002-6*, Sections 4 and 8 [Barbados].

[113] *Criminal Code*, Sections 83.05 to 83.12 [Canada].

[114] Council Common Position of 27 December 2001 on the application of specific measures to combat terrorism (2001/931/CFSP), *Official Journal of the European Communities*, December 28, 2001, L 344/93, and Council Regulation (EC) No. 2580/2001 of December 27, 2001 on specific measures directed against certain persons and entities with a view to combating terrorism, *Official Journal of the European Communities,* December 28, 2001, L 244/70 [European Union].

[115] Resolution, *supra* note 5, para. 1(a).

[116] *Id.* para. 3(d).

of persons who commit or attempt to commit [...] terrorist acts [...]."[117] The absence of any indication that a wider definition is required, together with the reference to the Convention, leads to the conclusion that the Resolution does not require that states define terrorism or terrorist acts in a manner wider than the Convention.[118] Many states have used or adopted a wider definition, but this is not required by the Resolution.

FATF Special Recommendation I states that the financing of terrorism "should be criminalized on the basis of the Convention." In the following notes, the basis for the discussion of a definition of terrorist acts is the definition contained in the Convention.

Types of Terrorist Acts

Terrorist acts are defined in the Convention as (i) the terrorist acts set out in at least those of the nine international treaties listed in the Annex to the Convention to which the country is a party ("treaty offences"); and (ii) terrorist acts as defined in the generic definition set out in Article 2 (b) ("generic offences").

"Treaty offences"

Article 4, paragraph 1 (a) of the Convention refers to nine treaties, contained in the Annex to the Convention, and makes it an offense to provide or collect funds with the intention or in the knowledge that these funds will be used to carry out an offense defined in one of the listed treaties.[119] The drafters of the Convention recognized that a country may not have become party to all nine treaties listed in the Annex to the Convention at the time it became a party to the Convention. The Convention authorizes states parties to declare, at the time of becoming a party to the Convention, that a treaty to which the country is not a party will be deemed not to be included in the Annex to the Convention, such declaration ceasing to have effect at the time the country becomes a party to the treaty. Conversely, if a state party to the Convention ceases to be a party to one of the treaties, it may by declaration state that the treaty will be deemed not included in the Annex. Such declarations are optional. Countries may include the nine

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[117] Resolution, *supra* note 5, para. 1(d).

[118] Walter Gehr, a former expert of the CTC, has written that the Committee Chairman had stated that the Committee would consider as terrorist acts any act that the Committee would unanimously consider as such. Mr. Gehr added that the Committee's work proved to be concrete enough to obviate the need to resolve all issues related to the definition of terrorism. Walter Gehr, "Le Comité contre le terrorisme et la résolution 1373 (2001) du Conseil de Sécurité," *Actualité et Droit International* (January 2003), *http://www.ridi.org/adi*.

[119] The list is set out in Box 1.

treaties in their definition of "treaty offences" even if they are not parties to all of them.

In practice, some states parties have included all treaties in their definition, including those to which they were not a party. Other states parties have limited the list to the treaties to which they were a party. Among those, some have provided a mechanism under which the government may by regulation add the treaties to the list as the country becomes a party to them, without the need to amend the law. As a matter of legislative drafting, some laws refer to the treaty by name, while others extract from each treaty the offense it contains and set it out as an offense.

"Generic offences"

By contrast to the "treaty offences," which are defined in terms of conduct that is in itself "terrorist," the generic offense of financing terrorist acts relies not only on conduct, but also on intent and purpose to define terrorist acts. Under the generic definition set out in the Convention, *any act can be a terrorist act, provided it is intended to cause death or serious bodily injury to certain persons, and provided its purpose is to intimidate a population, or to compel a government or an international organization to do or to abstain from doing something.*

A number of countries have added elements to the definition that have the effect of limiting its scope, or expanding it.[120] The limiting language appears to have been motivated by a concern that the generic definition could be used in circumstances where it was not intended. Noteworthy in this respect is the qualification found in the U.K., Canadian, and Australian laws to the effect that the offense only exists "if the action is done or the threat is made with the intention of advancing a political, religious or ideological cause."[121] Another limitation takes the form of the exclusion of certain activities from the scope of "providing or collecting funds." An example of such a provision is found in the New Zealand Terrorism Suppression Act 2002, which, "to avoid doubt," expressly excludes the provision or collection of funds for the purposes of advocating democratic

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[120] In this Section, the examples of legislation provided include general anti-terrorism laws as well as laws implementing the Convention.

[121] *Suppression of the Financing of Terrorism Act 2002*, Schedule 1, Amendments to the Criminal Code act 1995, Part 5.3, Section 100.1, Definitions, paragraph *terrorist act* [Australia]; similar language is found in the *Terrorism Act 2000*, Article 1 (1)(c) [U.K.]; the *Anti-Terrorism Act*, Section 83(1)(*b*) [Canada]; and the *Terrorism Suppression Act* 2002, Section 5(2) [New Zealand].

government or the protection of human rights from the scope of the financing offense.[122]

The Convention makes it a part of the definition of the financing of terrorism that the perpetrator intended that the outcome of the act of terrorism being financed be "death or bodily injury" to civilians and noncombatants. A number of countries have defined the offense in such a way that it is applicable to cases where the intent is not necessarily to directly cause death or serious bodily injury. For example, the New Zealand Act mentioned above includes, among others, the following additions: "a serious risk to the health or safety of a population," "serious interference with, or serious disruption to, an infrastructure facility if likely to endanger human life," and "the introduction or release of a disease-bearing organism, if likely to devastate the national economy of a country."[123] Another, wider expansion is found in the Mauritius Prevention of Terrorism Act of 2002, which in addition to criminalizing the commission of acts of terrorism, criminalizes the omission of doing anything that is reasonably necessary to prevent such acts.[124]

Authorities will need to assess the advantages and disadvantages of adding language limiting or expanding the definition of terrorism for purpose of the implementation of the Convention. Local conditions and, in particular, sensitivity to basic rights considerations may suggest the addition of limiting language. However, such language may make successful prosecution of offenses more difficult. The examples of legislation given in the Appendixes are based on the Convention's requirements exclusively.

Authorities may also consider the use of a listing mechanism to facilitate the prosecution of financing of terrorism crimes. A number of states, including Canada,[125] New Zealand,[126] the United Kingdom,[127] and the United States,[128] have established mechanisms under which the names of persons or organizations suspected of engaging in terrorism (other than those listed under the authority of the Security Council) may be set out in a list issued under the authority of the executive branch. The lists are published, and

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[122] *Terrorism Suppression Act 2002*, Section 8(2) [New Zealand].

[123] *Terrorism Suppression Act 2002*, Section 5(3) [New Zealand].

[124] *Prevention of Terrorism Act of 2002*, Section 3(1) [Mauritius].

[125] *Criminal Code*, Section 83.05 [Canada].

[126] *Terrorism Suppression Act 2002*, Sections 20-24 [New Zealand].

[127] *Terrorism Act 2000*, Sections 3-13 [United Kingdom]

[128] *Immigration and Nationality Act*, 8 U.S.C. §1189 [U.S.] (applies to foreign organizations only).

knowledge that these persons and organizations are terrorists or terrorist organizations is presumed, thus easing the burden of proof of knowledge or intent in the financing of terrorism offense (such mechanisms generally also require the freezing of the assets of persons and organizations on the list and prohibit the provision of any assistance to them). While such mechanisms make the prosecution of financing of terrorism offenses easier, they must be crafted carefully to ensure that they are not abused and that persons and organizations so listed have a right to have their request to be removed from the list heard by an independent body, while taking into account the fact that the evidence used to constitute such lists is likely to be highly sensitive. As such lists are not required by the Convention or the Resolution, the examples of legislation provided in this handbook do not refer to them. Authorities interested in including such a mechanism in their legislation may consult the legislation of the countries mentioned above.

Financing of Terrorism and Money Laundering

In their responses to the United Nations questionnaire, some countries have made the point that they had implemented the provisions of the Resolution on the criminalization of the financing of terrorism by adopting money laundering legislation.[129] This would not appear to be responsive to the spirit and letter of the Resolution and the Convention. It should be borne in mind that the Convention establishes a separate, autonomous offense of financing of terrorist acts. Although both financing of terrorism and money laundering offenses are based on the common idea of attacking criminal groups through measures aimed at the financing of their activities, the two offenses are distinct. In particular, in terrorism financing, the funds used to finance terrorist acts need not be proceeds of illicit acts, and need not have been laundered. These funds may have been acquired and deposited in financial institutions legally. It is not their criminal origin that makes them "tainted," but their use, or intended use, to finance terrorist acts, or to provide support to terrorists or terrorist organizations. Thus, to rely exclusively on the offense of money laundering to criminalize terrorist financing would leave a significant gap in the legislation, as terrorist funding offenses would be established in cases where the funds intended to finance a terrorist act were of illicit origin, but the funding of terrorist acts out of legally obtained funds could not be prosecuted.

Nevertheless, the two offenses are linked inasmuch as FATF Special Recommendation II requires jurisdictions to include the financing of terrorism as a predicate offense to money laundering. Such an inclusion is

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[129] Walter Gehr, "Recurrent Issues," Briefing for the member states on 4 April 2002, UN Counter-Terrorism Committee, *http://www.un.org/docs/sc/committees/1373/rc.htm*.

automatic for countries that define predicate offenses as "all crimes" (as is required in the Strasbourg Convention)[130] or all serious crimes (as long as the terrorism financing offenses fall within the definition of "serious crimes" in the jurisdiction). In countries where predicate offenses are set out in a list, the list may need to be amended to include terrorist financing offenses.

Aiding and Abetting, and Conspiracy as Substitute Offenses

Some countries have stated that the offense of terrorist financing is included in the offense of aiding or abetting the commission of terrorist acts, or conspiracy to commit such acts.[131] However, in contrast to the notion of aiding and abetting, the Convention does not require that the terrorist act that the funds were intended to finance actually take place or even be attempted. It is sufficient that the alleged perpetrator intended that they be used to finance terrorist acts or that the person knew that they would be used for that purpose. This is made clear by paragraph 3 of Article 2, which states that: "For an act to constitute an offence set forth in [the Convention], it shall not be necessary that the funds were actually used to carry out an offence [under the Convention]." Thus the offense of financing of terrorism is separate and independent of the terrorism offenses. By contrast, in most jurisdictions, aiding and abetting offenses only occur when the principal act is committed, or at least attempted, a condition that is not included in the definition of the offense in the Convention.[132] Moreover, in most jurisdictions, aiding and abetting occurs only when the alleged perpetrator has knowledge that the principal offense is being committed or attempted, while in the case of the Convention, the link with the terrorist offense is not that it occurs or is attempted, but rather that the alleged perpetrator intends that the funds be used to commit the terrorist act (or knows that the funds will be so used).[133]

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[130] Under Article 1e of the Strasbourg Convention, "'predicate offence' means any criminal offence as a result of which proceeds were generated that may become the subject of an offence as defined in Article 6 of this Convention."

[131] Gehr, *supra* note 129.

[132] *Id.*

[133] *See, e.g.*, *Johnson v Youden*, [1950] 1 All ER 300, summarized in The Digest, Annotated British, Commonwealth and European Cases, 14(1), Criminal Law, Evidence and Procedure, London, 1993 [hereinafter "the Digest"] no. 954, at 120. Aiding and abetting may occur, however, if the alleged perpetrator knew that an illegal act (in this case, an act of terrorism) was to be committed, even if the person did not know exactly what terrorist act would actually be committed (in this case, attempting to set a public house on fire with a pipe bomb). *See*, *DPP for NI v Maxwell*, [1978] 3 All ER 1140, [1978] WLR 1350, 143 JP 63, 122 Sol. Jo 758, [1978] NI 42, sub nom *Maxwell v. DPP for NI* 68 Cr App Rep 142, HL, summarized in The Digest, no. 867, at 109.

Similar remarks may be made with respect to conspiracy. Being an independent offense, the financing of terrorism can be committed by one person acting alone, a situation that is inconsistent with a theory of conspiracy.

Attempt, Participation, Organization, Direction, and Contribution

In addition to the commission of the offenses defined in the Convention, the Convention requires the criminalization of attempts to commit these offenses.[134] The Convention requires also that the participation as an accomplice in a defined offense, the organization of such an offense, or direction of others to commit such an offense be criminalized.[135] The intentional contribution to the commission of such an offense by a group acting with a common purpose, under certain defined circumstances, is also to be criminalized.[136] Authorities will need to determine which of these requirements can be met on the basis of general criminal law principles or existing legislation, and which ones will require new offenses. Language to cover these elements is included in the examples of legislation set out in Appendixes VII and VIII.

Separately from these provisions, which are contained in Article 2, the Convention sets out in its Article 18 a requirement that states take "measures to prohibit in their territories illegal activities of persons and organizations that knowingly encourage, instigate and organize or engage in the commission of offences set forth in article 2." The exact significance of this provision is far from clear, as it contains a circular element, and because, although it appears to require the criminalization of certain acts, it is not set out in Article 2 and is not expressed in the clear "criminalization" terms of that Article. Indeed, read as a criminalization provision, it would be redundant with some of the provisions of Article 2. The circular element is that the provision appears to require the prohibition of acts that are defined as being illegal. These ambiguities are most easily resolved by considering that the word "prohibit" really means "prevent and prosecute," in which case the provision would not be considered as a "criminalization" provision, but a requirement to enforce existing laws.

Knowledge and Intent

The definition of terrorism financing in the Convention includes as mental elements that the offense be committed willfully, and with the

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[134] Convention, *supra* note 12, Art. 2, para. 4.

[135] *Id.* Art. 2, paras. 5(a) and (b).

[136] *Id.* Art. 2, para. 5(c).

intention that the funds be used to commit a terrorist act as defined in the Convention, or in the knowledge that they would be used to commit such an act.[137] The willfulness requirement appears to be a reference to the general principle of criminal law that makes criminal intent ("*mens rea*") an element of all crimes. The second element sets out knowledge and a specific form of intent as two alternative mental elements.

The Convention leaves it to each state party to define the form of intent or knowledge that would be necessary to constitute the offense, as well as the means to prove either element. The minimum requirement would consist of actual knowledge on the part of the perpetrator that the funds will be used for a terrorist act, together with the will to achieve this result. This requirement should be implemented in all states parties. However, many legal systems also admit less direct forms of intent, which, when applied to the financing of terrorism, would include cases where, for example, the perpetrator foresaw, or could have foreseen, or should have foreseen, that the terrorist act would occur as a consequence of the provision or collection of the funds, and the perpetrator provided or collected the funds anyway. Some countries have incorporated similar forms of knowledge in their legislation, while in other countries, general criminal law principles or case law may lead to similar results. One example of a specific provision is found in the Australian Criminal Code, where the financing of terrorism is defined as providing or collecting funds, and being "reckless as to whether the funds will be used to facilitate or engage in a terrorist act."[138] Another example is found in the Commonwealth Secretariat Implementation Kit for the Convention, in which the suggested definition of financing of terrorism states in part that a person provides or collects funds "with the intention that they should be used, or having reasonable grounds to believe that they are to be used" to carry out a terrorist act.[139]

Authorities may also note the impact of FATF Special Recommendations I and II and the Methodology on this issue. Special Recommendation I sets as a standard that countries "should take immediate steps to ratify and implement fully" the Convention, and Special Recommendation II sets as a

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[137] The prohibition of support of terrorists and terrorist organizations set out in paragraph 1(d) of Resolution 1373 (2001) does not refer to the mental element of the related offense, leaving it to each country to define it in accordance with its criminal law.

[138] *Criminal Code Act 1995*, Section 103.1, added to the *Criminal Code* by the *Suppression of the Financing of Terrorism Act 2002*, No. 66, 2002. A person is reckless as to a result if: "he or she is aware of a substantial risk that the result will occur; and (b) having regard to the circumstances know to him or her, it is unjustifiable to take the risk." *Criminal Code Act 1995*, Section 5.4.

[139] Commonwealth Secretariat, *Implementation Kits for the International Counter-Terrorism Convention* 293.

standard that "[e]ach country should criminalize the financing of terrorism, terrorist acts and terrorist organizations." One of the criteria for compliance with these standards is stated as follows in the Methodology: "The offences of ML and FT should apply at least to those individuals and legal entities that knowingly engage in ML or FT activity. Laws should provide that the intentional element of the offences of ML and FT may be inferred from objective factual circumstances."[140]

The first sentence of the quoted section of the Methodology is consistent with the Convention, as knowledge is required (as an alternative to intent) in the definition of the offense itself in the Convention. With respect to the second sentence of the criterion, the idea that knowledge or intent should be inferred from objective factual circumstances was already present in the FATF 40 Recommendations on Money Laundering.[141] Its origin can be found in the 1988 Vienna Convention, which states that: "Knowledge, intent or purpose required as an element of an offence set forth in paragraph 1 of this article may be inferred from objective factual circumstances."[142] There is no similar provision in the Convention. It is a matter for each jurisdiction to determine whether its general criminal law provides an equivalent standard applicable to terrorism financing offenses. If there is doubt on this point, the authorities may consider whether specific legislation is necessary to ensure that the standard as assessed under the Methodology is met.[143]

Liability of Legal Persons

Article 5 of the Convention requires states parties to take measures to enable legal entities located in their territory or organized under their laws to be held liable when a person responsible for the management or control of the entity has, in that capacity, committed an offense set forth in the Convention. Article 5 adds that such liability may be criminal, civil, or administrative. The FATF 40 Recommendations contain a similar provision with respect to money laundering,[144] but the Special Recommendations are

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[140] Methodology, *supra* note 68, Criterion I. 4.

[141] FATF Recommendation 5 states as follows: "As provided in the Vienna Convention, the offence of money laundering should apply at least to knowing money laundering activity, including the concept that knowledge may be inferred from objective factual circumstances."

[142] United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, December 19, 1988, Article 3, paragraph 3.

[143] The language used in the Methodology ("Laws should provide...") would entail that assessments based on it would look for a legislative basis for the standard.

[144] Recommendation 6 reads as follows: "Where possible, corporations themselves—not only their employees—should be subject to criminal liability."

silent on this point, except for stating that the Convention should be ratified and implemented, and for what is stated in SR VIII concerning the abuse of legal entities, and nonprofit entities in particular, for terrorism financing.

The examples of legislation set out in Appendices VII and VIII may be considered if the liability is to be criminal. Providing civil or administrative sanctions may require the amendment of other acts, such as the Companies Act or the Banking Act.

Establishing Jurisdiction over the Financing of Terrorism Offenses

Article 7 of the Convention requires each state party to take jurisdiction over the offenses set out in the Convention (i) when the offense is committed in its territory, (ii) when the offense is committed aboard a vessel carrying the flag of that state or an aircraft registered there, or (iii) when the offense is committed by a national of that state (Article 7, paragraph 1). The Convention also provides that the states parties may take jurisdiction in certain other cases (Article 7, paragraph 2). Pursuant to Article 3, the Convention does not apply to situations where the offense is committed in a single state, the alleged offender is a national of that state and is present in the territory of that state and no other state has a basis for exercising jurisdiction under the Convention. However, Article 7, paragraph 6 states that the Convention does not exclude the exercise of any criminal jurisdiction established by a state party in accordance with its domestic law, without prejudice to the norms of general international law. It follows that there is no requirement in the Convention for states parties to assume jurisdiction in such purely domestic cases, although there is no prohibition to do so in the Convention, and states would normally have jurisdiction under domestic law once the offense has been established, unless the definition of the offense excludes purely domestic situations.

States parties have implemented the jurisdictional provisions of the Convention in a number of ways. One country (Barbados) has defined the financing of terrorism offense as an act committed in or outside the country, and has provided that its courts would have jurisdiction in all cases listed in Article 7 of the Convention.[145] Thus, the offense can be prosecuted in that country even in cases where the Convention does not apply because the facts are purely domestic.

Another country (Canada) has provided that the offense is deemed to have been committed in its territory when any one of certain listed elements,

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[145] *Anti-Terrorism Act, 2002-6*, Section 12 [Barbados].

taken from the Convention, is present.[146] This type of provision responds to Article 11, paragraph 4 of the Convention, which states that, if necessary to provide a legal basis for extradition, the offenses are to be treated between the parties as if they had been committed not only in the place in which they occurred but also in the states that have established jurisdiction under Article 7.

Another country (the United States) has enacted implementing legislation limiting the jurisdiction of its courts under the Convention to the cases listed in the Convention and where the application of the Convention is not excluded by Article 3.[147] The common law examples set out in Appendix VIII contain the three variants described above, while the civil law example set out in Appendix VII follows the text of the Convention.

Procedural Matters

Article 9, paragraphs 1 and 2 of the Convention requires states parties to investigate allegations of offenses set out in the Convention and to ensure the presence of alleged offenders found on their territories for purposes of prosecution or extradition. Article 9 also requires that a person with regard to whom measures have been taken to ensure his or her presence be allowed to communicate with a representative of a state of that person's nationality. The state party must also notify other states parties that have established jurisdiction on the offense under the Convention, and indicate whether it intends to exercise jurisdiction. In some countries, implementation of these provisions of the Convention may not require new legislation. This would be the case if laws and regulations governing criminal investigations already cover the requirements of the Convention in this regard. Nevertheless, countries may find it useful to expressly implement these provisions. The examples set out in Appendices VII and VIII contain provisions implementing these requirements of the Convention.

Freezing, Seizing, and Confiscating Terrorist Assets

Requirements of the Convention, United Nations Resolutions, and the FATF Special Recommendations

The provisions of the Convention and those of the Resolution overlap in part, but each contains provisions not contained in the other. The Convention

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[146] *Criminal Code*, Section 7 (3.73) [Canada].

[147] *Suppression of the Financing of Terrorism Convention Implementation Act of 2002*, 18 U.S.C. §2339C [U.S.].

requires each state party to take appropriate measures "for the identification, detection and freezing or seizure of any funds used or allocated for the purposes of committing the offences" set out in the Convention, and "for the forfeiture of funds used or allocated for the purposes of committing [such] offences [...] and the proceeds derived from such offences."[148]

The Resolution contains the following detailed obligations for states regarding the freezing of terrorist assets:

> (c) Freeze without delay funds and other financial assets or economic resources of persons who commit, or attempt to commit, terrorist acts or participate in or facilitate the commission of terrorist acts; of entities owned or controlled directly or indirectly by such persons; and of persons and entities acting on behalf of, or at the direction of such persons and entities, including funds derived or generated from property owned or controlled directly or indirectly by such persons and associated persons and entities;

Thus the requirement of the Convention is a comprehensive one, covering identification, detection, freezing, seizure, and forfeiture of terrorist funds, while the Resolution requires only the freezing of terrorist assets. As has been discussed above, earlier resolutions of the Security Council have required states to freeze the assets of persons and organizations appearing on lists issued under the authority of the Security Council.

Special Recommendation III refers to these three elements of a country's international obligations. It sets as a standard the implementation of measures for freezing the assets of terrorists, those who finance terrorism and terrorist organizations "in accordance with United Nations resolutions," and for the seizure and confiscation of property that is the proceeds of, or used in, or intended or allocated for use in, the financing of terrorism, terrorist acts, or terrorist organizations. The *Guidance Notes* add that "with regard to freezing in the context of SR III, the term *terrorists*, *those who finance terrorism* and *terrorist organizations* refer to individuals and entities identified pursuant to S/RES/1267 (1999) and S/RES/1390 (2002), as well as to any other individuals and entities designated as such by individual national governments."[149]

Countries that are parties to the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the 1988 Vienna Convention) or the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime (the 1990 Strasbourg Convention)

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[148] Convention, *supra* note 12, Art. 8, paras. 1 and 2.

[149] *Guidance Notes*, *supra* note 66, para. 17.

may have in place freezing, seizure, and confiscation mechanisms in relation to money laundering offenses similar to those called for in the Convention with respect to terrorist funds. The 1988 Vienna Convention requires states parties to adopt measures for the confiscation of the proceeds of drug crimes and money laundering, and measures to enable their authorities to identify, trace, and freeze or seize proceeds, property, or instrumentalities of such crimes for purposes of confiscation.[150] The 1990 Strasbourg Convention contains similar provisions, which are not limited to drug crimes, and cover all crimes. In implementing these two conventions, states parties have generally provided in their criminal law mechanisms for the freezing, seizure, and confiscation of proceeds of crime. These mechanisms give competent authorities the power to seize or freeze assets on the basis of a suspicion or a belief that they are proceeds of crime, and to confiscate them (or to confiscate assets of equivalent value), usually on the basis of the conviction of a person for the related crime.

Resolutions 1267 (1999) and 1390 (2002) follow a different pattern. They require member states to seize (but not to confiscate) assets of persons and organizations that have been designated in lists issued under the authority of the Security Council. The resolutions have two novel features. First, they require that each member state freeze the assets of persons and entities independently of any suspicion or belief on the part of the member state that such persons and entities are engaging in terrorist activities. Second, the resolutions require the freezing of assets of listed persons, without providing any time frame for such freezing. The resolutions thus transform what is usually a temporary measure, intended to prevent assets from being removed from a country during an investigation or a trial, into a potentially permanent measure.

There are thus two distinct international requirements concerning the freezing, seizure, and confiscation of terrorist assets. One is the requirement to have in place a comprehensive mechanism to freeze, seize, and confiscate assets of terrorists, set out in Article 8 of the Convention and (with respect to seizure) Article 1(c) of the Resolution. In countries that already have a general legal framework for the freezing, seizure, and confiscation of criminal assets, consideration may be given to amending this framework, if necessary, to respond to the provisions of the Convention and the Resolution in this regard. The other is the requirement to seize assets of persons and entities appearing on lists issued under the authority of the Security Council (or designated as such by other states). The legislative basis for a country's

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[150] United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, Art. 5, paras. 1 and 2. The Strasbourg Convention contains similar provisions (Articles 2 and 3).

response to such lists may be established in the same legislation, or in separate legislation, as long as the legislation reflects the special characteristics of the Security Council resolutions discussed above.

Country Responses

When the first Security Council list was issued under Resolution 1267 (1999), the need to respond quickly to the requirements of the Security Council led many countries to implement the freezing requirements pursuant to existing laws and regulations, such as foreign exchange laws (France, Spain), or the legislation under which the country became a member of the United Nations (New Zealand). Such membership laws granted to the Executive the power to take necessary action to respond to decisions of the Security Council under Chapter VII of the Charter, although it was recognized in some countries that the legislation was not well suited to the novel requirements of Resolution 1267 (1999). Since then, New Zealand has enacted legislation dealing specifically with the freezing of assets of terrorists and terrorist organizations identified as such by the Security Council or otherwise suspected of being terrorists or terrorist organizations.

In Canada, regulations were issued in October 2001 under the United Nations Act, to authorize the Minister of Foreign Affairs to freeze the assets of terrorists and terrorist organizations listed as such by the Security Council. One of the features of the Canadian regulation is the fact that it authorizes a listed person to apply to the Solicitor General to be removed from the list, but leaves unstated the consequence for a successful individual of being removed from the list while still appearing on the Security Council list. Subsequently, in December 2001, Canada enacted the Anti-terrorist Act, which gives the Executive the power to list entities (but not individuals) with respect to which the Executive "is satisfied that there is reasonable grounds to believe" that the entity has knowingly carried out, or attempted, or participated in terrorist activity or has knowingly acted on behalf of, at the direction of or in association with such an entity. Assets of listed entities are frozen under the Act. Thus the Act authorizes the Executive to list entities that are not listed under the authority of the Security Council.[151] Other jurisdictions have now enacted provisions responding directly to the requirements of the Security Council Resolutions.[152] For example, the

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[151] On November 24, 2002, the U.N. Counter-Terrorism Committee adopted the view of the experts assisting the Counter-Terrorism Committee to the effect that the Resolution requires the freezing of the assets of persons or entities who engage in terrorist activities even if they are not listed by the Security Council, Letter from Jeremy Wainwright, Expert Adviser, to the Chairman of the Counter-Terrorism Committee (November 11, 2002).

[152] It may be noted that the implementation of the asset freezing provisions of the Resolution by members of the IMF results in the freezing of nonresidents' bank accounts and

(continued)

Council of the European Union issued a regulation under which the Council may issue lists of persons and entities committing, or attempting to commit, or participating in, or facilitating the commission of acts of terrorism (the text is set out in Appendix IX).[153] Similarly, in April 2002, Monaco issued a Sovereign Order requiring financial institutions to freeze the assets of persons and entities whose name is set out in lists to be issued by Ministerial Order.[154]

In designing laws to respond to their obligations under the Convention and the relevant Security Council resolutions, authorities may consider whether new legislation is needed, and if it is needed, such legislation could deal with both the requirements of the Convention and those of the Security Council resolutions. A number of questions would also need to be addressed in the design of the legislation implementing the requirements of the Convention and the Resolution. In particular, authorities would need to decide whether a listing mechanism should be adopted in this regard (in addition to the lists issued by the Security Council). It should be noted that neither the Resolution nor the Convention require the use of lists. Countries may implement the freezing requirements of the Resolution and the Convention on an individual basis, without recourse to a list.[155] Also, decisions would have to be made as to under what circumstances the freezing action could be taken, and whether (in the absence of a list) a court

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the prohibition of direct payments, including payments for current international transactions. When such freezes apply to receipts of current international transactions, including the payment of interest on the balances in the accounts, the freezes give rise to restrictions on the making of transfers for current international transactions, and, under Article VIII, Section 2(*a*) of the Articles of Agreement of the IMF, require IMF approval, even though they are imposed by IMF members pursuant to a mandatory resolution of the Security Council. The IMF has recognized, however, that it does not provide a suitable forum for the discussion the political and military considerations that lead members to establish such restrictions solely for the preservation of national or international security, and has established a procedure under which, unless the IMF informs the member within 30 days of receipt of the notice that it is not satisfied that such restrictions are proposed solely to preserve such security, the member may assume that the IMF has no objection to the imposition of the restrictions (see International Monetary Fund, Decision No. 144-(52/51) of August 14, 1952, in *Selected Decisions and Selected Documents of the International Monetary Fund*, 27th issue 474 (December 31, 2002).

[153] Council Regulation (EC) No 2580/2001 of 27 December 2001 on specific restrictive measures directed against certain persons and entities with a view to combating terrorism, *Official Journal,* L 344 , 28/12/2001 p. 0070–0075 [E.U.].

[154] Ordonnance Souveraine no 15.320 du 8 avril 2002 sur la répression du financement du terrorisme, *Journal de Monaco, Bulletin officiel de la Principauté*, no 7542, April 12, 2002 [Monaco].

[155] This is also the view expressed in a letter from Jeremy Wainwright, Expert Adviser, to the Chairman of the Counter-Terrorism Committee (November 11, 2002) and endorsed by that Committee.

order would be required before any freezing action, or whether a temporary freeze could be decided by police authorities pending a court order. The European Union Council Regulation (EC) No. 2580/2001 of December 27, 2001 (referred to above) contains a detailed set of provisions related to the listing of terrorists and terrorist entities, and the freezing of their assets. In addition, Appendixes VII and VIII provide further examples of legislation on freezing and confiscation of terrorist assets.

International Cooperation: Mutual Legal Cooperation and Extradition, Temporary Transfer of Persons in Custody, and Channels of Communications

Requirements of the Convention, the Resolution, and the FATF Special Recommendations

Generally, the Convention requires states parties to afford one another the greatest measure of mutual legal assistance in connection with criminal investigations, or criminal proceedings or extradition proceedings in respect of the offenses set out in the Convention.[156] In addition, the Convention contains special provisions concerning the temporary transfer of persons in custody, for purposes of testifying or assisting in investigations.[157]

The Resolution also requires states to afford one another mutual assistance in criminal investigations or criminal proceedings relating to the financing or support of terrorist acts.[158] Further, the Resolution requires states to find ways of exchanging information related to the actions and movement of terrorist persons and networks as well as cooperating on administrative and judicial matters.[159] The Resolution puts strong emphasis on the exchange of information as an important component in international cooperation with respect to matters related to terrorism and its financing.

Special Recommendation V establishes as a standard that countries cooperate with one another, on the basis of treaty, arrangement, or other mechanisms in criminal, civil enforcement and administrative investigations, inquiries and proceedings relating to financing of terrorism, terrorist acts, and terrorist organizations. It also requires countries to take measures to ensure that they do not provide safe havens for individuals charged with the

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[156] Convention, *supra* note 12, Art. 12, para. 1.

[157] *Id.* Art. 16.

[158] Resolution, *supra* note 5, para. 2(f).

[159] *Id.* para. 3, *passim*.

financing of terrorism, terrorist acts, or terrorist organizations, and to have procedures in place to extradite, where possible, such individuals.

The discussion that follows deals with judicial cooperation (mutual legal assistance, extradition and temporary transfers of persons in custody), and international cooperation among FIUs in dealing with financing of terrorism cases.

Extradition, Mutual Legal Assistance, and Temporary Transfer of Persons in Custody

In countries where there are general laws on mutual legal cooperation and extradition, implementation of the provisions of the Convention on these subjects may be made by amending, where necessary, the existing laws. The laws may need to be amended to ensure that their scope of application extends to the offenses and types of cooperation set out in the Convention, and that the provision of assistance in matters covered by the Convention is not denied on grounds not permitted in the Convention. The civil law provisions set out in Appendix VII follow generally the Model Legislation on Laundering, Confiscation and International Cooperation In Relation To The Proceeds Of Crime (1999), issued by the United Nations Office for Drug Control and Crime Prevention. The common law example is adapted from the Commonwealth Secretariat model provisions on extradition.

Cooperation Among FIUs

In addition to exchanges of information on terrorist financing through mutual legal assistance arrangements, countries exchange such information through arrangements among financial intelligence units (FIUs). FIUs have been established in a large number of countries as "A central national agency responsible for receiving (and, as permitted, requesting), analyzing and disseminating to the competent authorities disclosures of financial information (i) concerning suspected proceeds of crime; or (ii) required by national legislation or regulation, in order to counter money laundering."[160] While the original purposes of establishing an FIU was the detection of transactions suspected of being related to money laundering, they are now being used also to detect transactions suspected of being linked to terrorism. Thus, Special Recommendation IV sets as a standard that such transactions be reported to "competent authorities." FIUs are grouped in an informal association called the Egmont Group, which has adopted the above-mentioned definition of an FIU and uses it as a basis for deciding on the admission of new members.

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[160] Egmont Group, *Statement of Purposes of the Egmont Group of Financial Intelligence Units*, The Hague, June 13, 2001.

FIUs exchange information among themselves on the basis of the Egmont Group's *Principles for Information Exchange between Financial Intelligence Units for Money Laundering Cases*, adopted at The Hague on June 13, 2001. Up to the end of 2001, the arrangements for the exchange of information between FIUs were focused mainly on information dealing with money laundering cases. As countries enact legislation requiring the reporting of transactions suspected of being related to the financing of terrorism, FIUs will also have to exchange information among each other on terrorist financing. The Egmont Group has already taken steps to improve its information collection and sharing in respect of terrorism financing.[161] The Principles for Information Exchange state that "FIUs should be able to exchange information freely with other FIUs on the basis of reciprocity or mutual agreement..." and that such exchange should produce "any available information that may be relevant to an analysis or investigation of financial transactions and other relevant information related to money laundering and the persons or companies involved."[162] Information received by an FIU from another FIU may only be used for the purposes for which it was requested, and the receiving FIU may not transfer it, or make use of it in an administrative, investigative, prosecutorial, or judicial purpose without the consent of the FIU that provided it.[163] Such information must be subject to strict safeguards to protect its confidential character.[164]

Some FIUs have the power to exchange information with other FIUs even in the absence of an agreement with the other FIU on exchange of information (usually in the form of Memoranda of Understanding (MOU), or exchanges of letters). This is the case of FinCEN, the U.S. FIU.[165] Many FIUs have the authority to enter into information sharing agreements with other FIUs, while others can only do so after consultation with, or upon approval of, the responsible minister. In Canada, for example, agreements on exchange of information between the Canadian FIU and others may be

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[161] At a special meeting in October 2002, the Egmont Group agreed to: (i) work to eliminate impediments to information exchange; (ii) make terrorist financing a form of suspicious activity to be reported by all financial sectors to their respective FIU; (iii) undertake joint studies of particular money laundering vulnerabilities, especially when they may have some bearing on counter terrorism, such as hawala, and (iv) create sanitized cases for training purposes. *See* James S. Sloan, Director, FinCEN, Statement before the Subcommittee on Oversight and Investigations of the Committee on Financial Services, March 11, 2003.

[162] Egmont Group, *Principles for Information Exchange between Financial Intelligence Units for Money Laundering Cases*, The Hague, June 13, 2001, para. 6.

[163] *Id.* paras. 11 and 12.

[164] *Id.* para. 13.

[165] 31 U.S.C. 319, 31 U.S.C. 310, and 31 CFR §103.53 [U.S.]. FinCEN will enter into MOUs if the other FIU requires one.

entered into either by the responsible minister, or, with the consent of the responsible minister, by the FIU. The type of information that can be exchanged is enumerated in the Canadian law. In most cases, once the MOU is in place (if needed), the FIU can exchange information directly with the other FIU. In the case of Monaco, the law makes the exchange of information subject to reciprocity, and to a finding that no criminal proceedings have been instituted in Monaco on the basis of the same facts.[166]

Preventive Measures (Article 18 of the Convention and FATF SR VII)

Article 18(1)(b) of the Convention requires states parties to "cooperate in the prevention of the offences set forth in Article 2 by taking all practicable measures [...] to prevent and counter preparations in their respective territories for the commission of those offences within or outside their territories." Some of the measures set out in Article 18 are stated as obligations of each state party, while others are stated in the form of a requirement to consider their adoption.

The mandatory measures include "measures to prohibit in their territories illegal activities of persons and organizations that knowingly encourage, instigate and organize or engage in the commission of offences set forth in Article 2."[167] This requirement is discussed in Chapter 4, page 51.

The other mandatory provision in Article 18 is to require financial institutions and other professions "to utilize the most efficient measures available for the identification of their usual and occasional customers, as well as customers in whose interest accounts are opened and to pay special attention to unusual or suspicious transactions; and to report any transactions suspected of stemming from a criminal activity."[168] For this purpose, states parties are to consider the following concrete measures, which are based on the FATF Recommendations:

- Prohibiting the opening of accounts, the holders or beneficiaries of which are unidentified or unidentifiable and requiring that the identity of real owners of such accounts be verified (FATF Recommendation 10 contains a similar requirement).

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[166] Loi no 1.162 du 7 juillet 1993 relative à la participation des organismes financiers à la lutte contre le blanchiment des capitaux, amended by Loi no 1.253 du 12 juillet 2002, Article 31 [Monaco].

[167] Convention, *supra* note 12, Art. 18, para. 1(a).

[168] *Id.* Art. 18, para. 1(b).

- Verifying, when necessary, the legal existence and structure of legal entities by obtaining proof of incorporation, including the corporation's name, legal form, address, directors as well as provisions regulating the power to bind the legal entity (FATF Recommendation 10 contains a similar requirement).
- Reporting promptly to competent authorities all complex, unusual large transactions and unusual patterns of transactions, which have no apparent, economic, or obviously lawful purpose, without fear of assuming criminal or civil liability for breach of any restriction on disclosure of information if they report their suspicions in good faith (FATF Recommendations 14, 15, and 16, and Special Recommendation IV contain a similar requirement).
- Maintaining "all necessary records" on domestic and international transactions for at least five years (FATF Recommendation 12 contains a similar requirement, which specifies that the records to be kept include both customer identification records and transaction records).

For its part, FATF SR VII sets as a standard that countries ensure that financial institutions, including money remitters, include "accurate and meaningful originator information (name, address, and account number) on funds transfers and related messages that are sent," and that the information remain with the transfer or related message through the payment chain. FATF SR VII also sets as a standard that countries ensure that financial institutions, including money remitters, conduct enhanced scrutiny of and monitor for suspicious activity funds transfers that do not contain complete originator information (name, address, and account number).

If a state party has already in place an anti-money laundering law that contains provisions conforming to the FATF Recommendations, it may consider amending its law to require the reporting of suspicious transactions related to terrorism financing, as the simplest way to satisfy the requirements of the Convention and of FATF Special Recommendation IV. Amendments to the AML law could also be considered for implementing the other preventive measures set out in the Convention and in FATF SR VII. The advantage of this approach is to put together in one law all requirements related to preventive measures applicable to financial institutions and other covered entities, whether they relate to combating money laundering or the financing of terrorism. For example, Germany has adopted preventive

measures for financial institutions in a single statute which covers measures against both money laundering and terrorist financing.[169] Similarly, Monaco has amended its anti-money laundering law to extend the scope of the obligation to report suspicious transactions to include "all sums recorded in [the books of financial institutions] and all transactions relating to funds that could derive from terrorism or terrorist acts or terrorist organizations or that are intended to be used to finance them, and the evidence which provides the basis for their report."[170]

Alternative Remittance Systems (FATF SR VI)

FATF Special Recommendation VI sets the following as a standard:

> Each country should take measures to ensure that persons or legal entities, including agents, that provide a service for the transmission of money or value, including transmission through an informal money or value transfer system or network, should be licensed or registered and subject to all the FATF Recommendations that apply to banks and non-bank financial institutions. Each country should ensure that persons or legal entities that carry out this service illegally are subject to administrative, civil or criminal sanctions.

The general features of informal remittance systems are outlined in Box 4, above. Special Recommendation VI is based on the recognition that as controls over transactions of formal financial institutions have increased, launderers have tended to move funds through less supervised, unregulated channels. These systems, which are generally known as alternative remittance systems, or informal money or value transfer systems, are vulnerable to misuse for money laundering or terrorist financing purposes.

The FATF intention for SR VI is "to ensure that jurisdictions impose anti-money laundering and counter-terrorist financing measures on all forms of money/value transfer systems," including informal ones, which were not included in the scope of the FATF 40 Recommendations on money laundering. However, the FATF recognizes that the distinction between formal and informal systems is somewhat artificial.

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[169] Sections 6, 8, 11, 12, 13, and 14 of the Money Laundering Act in the version of the Act on the Improvement of the Suppression of Money Laundering and Combating the Financing of Terrorism (Money Laundering Act) of August 8, 2002 [Germany].

[170] Loi no 1.162 du 7 juillet 1993 relative à la participation des organismes financiers à la lutte contre le blanchiment des capitaux, amended by Loi no 1.253 du 12 juillet, 2002, Article 3 [Monaco].

The IMF and the World Bank have recently conducted a joint study of the types, scope, and controls exercised over informal funds transfer systems.[171] The IMF/World Bank study also contains a useful analysis of the linkages to the formal financial sectors of the *hawala* system of South Asia and their implications for fiscal, financial sector and supervisory policies of these jurisdictions. The conclusions of the study are summarized in Box 5.

Box 5. Conclusions of the IMF/World Bank *Hawala* Study

After reviewing the historical background and the operational characteristics of the *hawala* system of money remittance, its linkages with the formal financial sector, and its implications for the design of financial sector policies, the study comes to the following conclusions:

It encourages a two-pronged approach towards regulation in the context of long-term financial sector development, which includes, in countries where the *hawala* system exists alongside a well-functioning conventional banking sector, that *hawala* dealers be registered and keep adequate records in line with FATF recommendations, and that the level of transparency in these systems be improved by bringing them closer to the formal financial sector without altering their specific nature. In conflict-afflicted countries without a functioning banking system, requirements beyond basic registration may not be possible because of inadequate supervisory capacity.

Simultaneously, the regulatory response should address weaknesses that may exist in the formal sector and in particular the economic and structural weaknesses that encourage transactions outside the formal financial systems.

The study also emphasizes that prescribing regulations alone, without appropriate supervisory capacity and incentives, will not ensure compliance.

It cautions that the application of international standards needs to pay due regard to specific domestic circumstances and legal systems.

Finally, the study concludes that informal funds transfer systems cannot be completely eliminated by means of criminal proceedings and prohibition orders, and thus addressing such systems will require a broader response, including well-conceived economic policies and financial reforms, a well-developed and efficient payment system, and effective regulatory and supervisory frameworks.

Source: IMF/World Bank, *Informal Funds Transfer Systems: An Analysis of the Hawala System*, pp. 4–5.

[171] *Informal Funds Transfer Systems—An Analysis of the Hawala System*, IMF and World Bank, December 2002 (IMF/World Bank Study) (to be published in 2003).

Interpretative Note on FATF SR VI Requirements

The FATF has recently issued an Interpretative Note to define the scope of the international requirements that are envisaged in SR VI.[172] The Interpretative Note provides additional guidance on the minimum requirements for implementation of the Special Recommendation. It describes the three core elements of SR VI as follows:

- Jurisdictions should require licensing or registration of persons (natural or legal) that provide money/value transfer services, including informal systems;
- Jurisdictions should ensure that money/value transmission services, including informal systems, are subject to applicable FATF Recommendations (in particular, Recommendations 10–21 and 26–29) and the eight Special Recommendations on Terrorism Financing; and
- Jurisdictions should be able to impose sanctions on money/value transfer services, including informal systems that fail to obtain a license or register and fail to comply with relevant FATF Recommendations.

The Interpretative Note defines *money or value transfer service* as "a financial service that accepts cash, cheques, other monetary instruments or other stores of value in one location and pays a corresponding sum in cash or other form to a beneficiary in another location by means of a communication, message, transfer or through a clearing network to which the money/value transfer service belongs." Transactions performed by such services can involve one or more intermediaries and a third party for final payment. The Note adds that

> "[a] money or value transfer service may be provided by persons (natural or legal) formally through the regulated financial system or informally through non-bank financial institutions or other business entities or any other mechanism either through the regulated financial system (for example, use of bank accounts) or through a network or mechanism that operates outside the regulated system. In some jurisdictions, informal systems are frequently referred to as *alternative remittance services* or *underground (*or *parallel) banking systems*. Often these systems have ties to particular geographic regions and are therefore described using a variety of

[172] FATF, *Interpretative Note to Special Recommendation VI: Alternative Remittance*, (February 14, 2003), *http://www.fatf-gafi.org/TerFinance_en.htm*.

> specific terms. Some examples of these terms include *hawala, hundi, fei-chien,* and the *black market peso exchange*."

The Interpretative Note provides guidance on the scope of SR VI. It states that SR VI should apply to all persons (natural or legal), which conduct for or on behalf of a customer the types of activity set out in the definition. Activities described are covered if these are a primary or substantial part of the business or when such activity is undertaken on a regular or recurring basis, including as an ancillary part of a separate business enterprise.

The first issue is for each jurisdiction to identify precisely which persons or legal entities will be subject to the regulations. The Interpretative Note clarifies that jurisdictions need not impose separate licensing/registration requirements or designate another competent authority with respect to legal persons recognized as financial institutions (defined by the FATF 40 Recommendations), which carry out activities covered by SR VI, and which are already subject to the full range of applicable obligations under the FATF 40+8. As a result, the focus for the jurisdiction should be on financial sector participants that engage in the defined activities but which do not qualify as financial institutions and are not otherwise supervised.

This leads to the second issue, namely, requiring licensing or registration. The Interpretative Note states that "[j]urisdictions should designate an authority to grant licenses, and/or carry out registration and ensure that the requirement is observed." After deciding upon the definition—whether broad or narrow, the feasibility of licensing individuals or entities that are not subject to specialized licensing such as banking or wire transfer licenses must be determined.

Jurisdictions must then decide how to apply all FATF Recommendations that apply to banks and non-bank financial institutions to alternative remittance systems, including Recommendations 10–21 and 26–29, as well as the Special Recommendations on Terrorist Financing.

The third component of SR VI requires jurisdictions to assign appropriate administrative, civil, or criminal sanctions to persons or legal entities that carry out remittance services illegally. The scope of penalties for carrying out remittance services illegally can range from criminal prosecutions for engaging in transmittals outside of the established formal financial systems, to administrative or civil fines for engaging in these activities without adhering to customer due diligence, record keeping, or suspicious transaction reporting. Sanctions should be proportionate. The effectiveness of sanctions must be evaluated in light of the jurisdiction's overall system, whether based primarily on law enforcement, regulatory and supervisory oversight, or through the registration of businesses. The Interpretative Note contemplates sanctions being applicable to persons who provide money/value transfer services while failing to obtain a license or to

register, and to licensed or registered money/value transfer businesses that fail to apply the relevant FATF 40+8 Recommendations.

Jurisdiction-Specific Approaches

Some countries, for example, India and Japan, have attempted to ban alternative remittance systems altogether. The basis for such a ban in many countries is centered on the inability of authorities to obtain records or follow the flow of moving funds. The possible uses of alternative remittance systems for illegal purposes make them highly unattractive to governmental authorities in countries where a more formalized system also exists. Nevertheless, these informal systems continue to thrive in many of the countries that have attempted to ban them. One writer has stated that in India, "some estimates conclude that up to 50% of the economy uses the *hawala* system for moving funds, yet it is prohibited by law."[173] It would appear that outlawing alternative remittance systems alone has proven not to be an impediment to their continued operation.

Since SR VI was adopted, few jurisdictions have fully implemented its three components, but some progress has been made. As noted in the APG Paper, jurisdictions have approached alternative remittance systems with a combination of some obligations, for example, reporting or customer identification, registration and some obligations, and registration and full obligations. Canada and the United States have two representative approaches. Canada imposes suspicious transaction reporting, reporting on large cash transactions (above Can$10,000), and a record keeping requirement on the identity of originating customer, including the name and address of the originator for any transfer over Can$3000 to an expanded category of "money services business." The expanded category encompasses persons or entities in the business of remitting funds and does not require the physical movement of funds, thus including informal systems.[174]

The United States requires the registration of "underground banking systems" and imposes suspicious transaction reporting on them. Section 359 of the USA PATRIOT Act brings under the umbrella of the Bank Secrecy Act requirements for suspicious activity reporting, "licensed sender of money or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in

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[173] David M. Nissman, *Money Laundering,* part 1.6, Alternative Remittance Systems, *http://corpusjurispublishing.com/Articles/moneylaundering.pdf.*

[174] Section 1(2) The Proceeds of Crime (Money Laundering) and Terrorist Financial Act, February 1, 2002 [Canada].

facilitating the transfer of money domestically or internationally outside of the conventional financial institutions systems."[175] Regulations issued by U.S. financial supervisors to implement U.S. suspicious activity reporting under 31 U.S.C. §5318, are to apply equally to any other financial institutions and "to any person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system."[176] The common law legislative example set out in Appendix VIII contains a prohibition of unlicensed money transmitting businesses based on Section 373 of the USA PATRIOT Act 2001.

Nonprofit Organizations (FATF SR VIII)

In response to evidence that nonprofit organizations are sometimes used as conduits for terrorist funds, the FATF adopted Special Recommendation VIII, which reads as follows:

> Countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Non-profit organisations are particularly vulnerable, and countries should ensure that they cannot be misused:
>
> i. by terrorist organisations posing as legitimate entities;
>
> ii. to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; and
>
> iii. to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.

While the first sentence of the Recommendation is wide-ranging and would require jurisdictions to review all their laws related to legal entities to assess if any type of entity is susceptible to abuse for purposes of terrorist financing, the focus of the Recommendation is contained in the second sentence, which deals with charitable entities. In response to requests for clarification of the Recommendation, the FATF issued a note on international best practices in combating the abuse of nonprofit organizations.[177]

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[175] Section 359(a), *USA PATRIOT Act 2001*, amending 31 U.S.C. § 5312(a)(2)(R) [U.S.].

[176] Section 359(c), *USA PATRIOT Act 2001*, amending 31 U.S.C. § 5318 [U.S.].

[177] FATF Secretariat, *Combating the Abuse of Non-profit Organisations: International Best Practices*, *supra* note 87.

Best Practice Note on FATF SR VIII

The FATF Note states a number of basic principles that should guide the response to SR VIII. Among them are the following:

- The charitable sector is a vital component of the world economy and of many national economies and social systems that complements the activity of the governmental and business sectors in supplying a broad spectrum of public services and improving quality of life. The FATF wishes to safeguard and maintain the practice of charitable giving and the strong and diversified community of institutions through which it operates.
- Government oversight should be flexible, effective, and proportional to the risk of abuse. Mechanisms that reduce the compliance burden without creating loopholes for terrorist financiers should be given due consideration. Small organizations that do not raise significant amounts of money from public sources, and locally based associations or organizations whose primary function is to redistribute resources among members may not necessarily require enhanced government oversight.
- Different jurisdictions approach the regulation of nonprofit organizations from different constitutional, legal, regulatory, and institutional frameworks, and any international standards or range of models must allow for such differences, while adhering to the goals of establishing transparency and accountability in the ways in which nonprofit organizations collect and transmit funds. It is understood as well that jurisdictions may be restricted in their ability to regulate religious activity.

The FATF Note focuses on three main areas of operations and oversight of nonprofits. First, under "financial transparency," the note stresses the need for proper accounting practices, independent auditing of financial accounts, as well as the preferred use of bank accounts to channel funds. Second, under "programmatic verification," the note mentions the need to provide accurate information to potential providers of funds, the need to verify that financed projects have actually been carried out, and that the funds were in fact received and used by their intended beneficiaries. Third, under "administration," the note stresses the need for nonprofits to document their operations and to have boards of directors (or other forms of supervisory bodies) capable of proactive verification measures.

The note also mentions nonprofits' foreign operations, and government regulations. These two issues are dealt with in greater detail in the next two sections.

Best Practice for Disbursements of Funds to Foreign Recipient Organizations

When distributing funds to foreign recipient organizations, nonprofit organizations may adopt practices to ensure, to the extent possible, that such funds are not diverted to finance terrorist activities. The following paragraphs summarize the United States Department of Treasury Anti-Terrorist Financing Guidelines with respect to financing foreign recipient organizations.[178]

Nonprofit organizations should collect detailed information about a foreign recipient organization including its name in English and in the language of origin, any acronym or other names used to identify it, the address and phone number of any of its places of business, its principal purpose, including a detailed report on its projects and goals, the names and addresses of organizations to which it provides or proposes to provide funding, services, or material support, to the extent known, as applicable, copies of any public filings or releases made by it, including the most recent official registry documents, annual reports, and annual filing with the pertinent government, as applicable, and its existing sources of income, such as official grants, private endowments, and commercial activities.

In addition, nonprofit organizations may consider vetting potential foreign recipient organizations. Nonprofit organizations should be able to demonstrate that they have conducted a reasonable search of public information, including information available via the Internet, to determine whether the foreign recipient organization is or has been implicated in any questionable activity, that they verified that the foreign recipient organization does not appear on any list of the relevant national government, the United Nations, or the European Union identifying it as having links to terrorism or money laundering, that they have verified the identity of key staff at the foreign recipient including the full name of each key staff member in English, in the language of origin, and any acronym or other names used, and nationality, citizenship, current country of residence, place and date of birth of each key staff member if possible and it has run the names through public databases and compared them with the lists noted above.

Nonprofit organizations may also wish to review the financial operations of the foreign recipient organization if large amounts of aid are contemplated. Nonprofit organizations should determine the identity of the financial institutions with which the foreign recipient organization maintains

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[178] Adapted from the U.S. Department of Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S. Based Charities, pp. 4–6.

accounts. They should seek bank references and determine whether the financial institution is a shell bank, operating under an offshore license, licensed in a jurisdiction that has been determined to be noncooperative in the international fight against money laundering; or licensed in a jurisdiction that lacks adequate anti-money laundering controls and regulatory oversight. Nonprofit organizations should also require periodic reports from the foreign recipient organization on its operational activities and use of the disbursed funds and should also perform routine, on-site audits of foreign recipient organizations whenever possible, consistent with the size of the disbursement and the cost of the audit.

Oversight and Sanctions

Some jurisdictions have given their regulatory authorities the power to oversee nonprofit organizations. This is often the case where jurisdictions have conferred tax benefits on such organizations, in which case the tax authorities may exercise some oversight. In some jurisdictions, this oversight may only need to be slightly enhanced to achieve the objectives of Special Recommendation VIII. In other jurisdictions, regulatory oversight may need to be put in place.

Regulations covering the oversight and best practice requirements for nonprofit organizations should be backed up with sanctions for failure to comply. If the nonprofit is located in a jurisdiction where there are tax advantages or exemptions for nonprofit organizations, one possible sanction would be the termination of tax exempt status for breach of the best practice or due diligence provisions and the freezing of suspected funds. Other appropriate and proportional sanctions may include sanctioning of the directors of the nonprofit organization. The common law example of legislation on nonprofit entities is taken from the Commonwealth Secretariat Model Law, which is adapted from the Canadian Charities Registration (Security Information) Act. Similar provisions are provided in the civil law example.