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*in Response to Recommendation 41 of the EU Counter Terrorist Financing Strategy
presented to the European Council of December 2004 to assess*

THE EU'S EFFORTS IN THE FIGHT AGAINST TERRORIST FINANCING

IN THE CONTEXT OF THE

**FINANCIAL ACTION TASK FORCE'S
NINE SPECIAL RECOMMENDATIONS**

AND THE

EU COUNTER TERRORIST FINANCING STRATEGY

FINAL REPORT

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0 ABBREVIATIONS, SUMMARY, METHOD AND REPORT STRUCTURE

0.1 Frequently Used Abbreviations

1MLD	EU First Money Laundering Directive
2MLD	EU Second Money Laundering Directive
3MLD	EU Third Money Laundering Directive
9SR	FATF Nine Special Recommendations
AML	Anti Money Laundering
ARS	Alternative Remittance Systems
CDD	Customer Due Diligence
CFSP	Common Foreign and Security Policy
CFT	Combating the Financing of Terrorism
COTER	CFSP Terrorism Working Group
CT	Counter Terrorist/Counter Terrorism
CTC	Counter Terrorism Coordinator
CTG	Counter Terrorism Group
DNFPB	Designated Non-Financial Professional Body
EC	European Commission
EU	European Union
FATF40R	FATF Forty Recommendations on the Prevention of Money Laundering and the Financing of Terrorism
FD	Framework Decision
FI	Financial Institutions
FIN	Financial Investigator
FININT	Financial Intelligence – intelligence gathered from financial sources
FIU	FININT Unit
FSRB	FATF-Style Regional Body
HUMINT	Human intelligence (sources)
IRO	International Regional Organisation
JHA	Justice and Home Affairs
JLS	Justice, Liberty and Security
MS	Member State(s)
NPO	Not for Profit Organization
NPS	National Prosecution Service
OC	Organised Crime
PCWG	Police Chiefs' Working Group
PEP	Politically Exposed Person
SAR	Suspicious Activity Report
SitCen	Joint Situation Centre
TA	Technical Assistance
TF	Terrorist Financing
TWG/R	Terrorist Working Group
UN12ATCP	UN 12 Major Anti Terrorism Conventions and Protocols
WT(S)	Wire Transfer (Services)

0.2 Summary of Report

Method

The study team looked at AML/CFT arrangements within MS and EU institutions. The review was by means of desk research, visits and telephone interviews held with public, private and NPO sector experts and academics. The opinion of a range of other experts outside the EU was also sought. 11 MS were studied in more detail to identify patterns and trends and to check the consistency of findings.

High Level Findings

TF and ML occur in the same regulatory space, often being linked, but TF processes are less well understood. New approaches, particularly in intelligence, are constantly needed to meet known threats and to combat unknown ones, which are hard to detect by established means. Good FININT enables more informed and effective responses. However, FININT itself needs other forms of intelligence to achieve its full potential.

The UN gives individual states responsibility for implementing its instruments. Operationalisation of its high-level minimum standards occurs at regional and national level, and sometimes by economic sector. A major role in operationalising UN CFT measures in Europe is entrusted to the Financial Action Task Force and MONEYVAL. FATF has published a total of nine Special Recommendations on combating terrorist financing, and both FATF and MONEYVAL have a mandate to ensure their members, and thus all EU MS, implement them fully and effectively.

However, the FATF40R + 9SR are not treaty obligations but informal political commitments in response to political concerns. National and regional politics influence implementation and effectiveness. Research in this project suggests that, five years on from 9/11, the 9SR are still regarded as “Work in Progress”. There are issues and reservations as to their effectiveness as TF instruments. However, the FATF process overall is seen as successful and indispensable.

The EU thus has a role not just in influencing CFT process in MS, but also helping to remedy deficiencies and inconsistencies in the international acquis. The challenge is for the EU to lessen administrative and financial burdens whilst adding to public safety with regard to terrorism and crime more generally.

EU CFT Policy and the 9SR

The EU pursues four parallel CT goals - *Prevent, Protect, Pursue and Respond* - along four axes, namely *Strengthening national capabilities, Facilitating European co-operation, Developing collective capacity and Promoting international partnership*. CFT is currently part of the *Pursue* goal. The key elements of the strategy are a targeted intelligence-led approach, improved designation and listing, better tracing, ongoing monitoring, and support for Extra-Union activity.

The EU has adopted a range of measures in support of the 9SR. However, this report stresses the need for adequate resources, and EU bodies do not have the capacity to meet all the goals the EU has set itself. Importantly, there is no baseline threat analysis and there is no means of monitoring policy effectiveness in detail and proactively.

Whilst the EU can act directly under the First Pillar, under the Second and Third Pillar there are limitations. Divergent national approaches to AML/CFT on policy and operational levels

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feed back on the political level. Because the scope of AML/CFT activity is wide, it is complex enough to regulate at MS level, let alone across all MS. Complexity brings with it the constant risk of interventions compounding, not remedying, a situation. A number of respondents questioned if the role of the Counter Terrorism Coordinator, thought to have been established to address such problems, has been adequately developed. EU bodies involved at the operational level, such as Europol and SitCen, are restricted in scope of action and powers vis-à-vis MS.

MS Compliance with 9SR

Compliance with the 9SR requires good compliance with the FATF40R. Analysis of the compliance scores for 12 MS shows relatively high non-compliance re CDD, suspicious activity reporting, regulation and supervision, institutional matters and transparency. Non-compliance with the FATF40R weakens TF preventive capacity to the extent that some MS's scores on 9SR become irrelevant. Weak spots in respect of the 9SR are the freezing obligations, the reporting of suspicious TF transactions, as well as the regulation of NPOs and cash couriers. The pace of remedial action in MS is mixed, with delays caused mainly by slow political and administrative processes and problems integrating new legislation into existing laws, though delays can be for positive reasons, e.g. for consultation.

Broadly speaking, MS fall into four groups (i) those motivated to comply by the ongoing threat of terrorist attacks, (ii) those at low risk, but keen to maintain well-regulated financial and market systems, (iii) those at low risk and keen to develop their financial and market systems to attract foreign investment, and (iv) those who feel themselves to be at low risk and who need to upgrade not only AML/CFT systems, but also other necessary infrastructure. Compliance with 9SR is closely linked to the group in which each MS falls, and also to the legislative time and institutional resources available. The latter are often underestimated and under budgeted. Problems thus include not just long lead times for laws, but also getting key arrangements in pace e.g. complex IT systems and trained FINs. On the positive side, transparency engendered by FATF visits encourages compliance.

Problems with Solutions

FATF's adoption of a risk based approach has reduced regulatory burdens in some MS, but created difficulties for those public and private sector entities who lack sophistication and resources and who thus may prefer a rule based systems. Grouping factors of compliance using a standardised framework likewise confirms that MS non-compliance is rooted in deficient or complex institutional arrangements. Inter-agency coordination is a problem (and aggravated by rivalries) as are rival concerns about other threats. Co-ordination is complicated by the necessarily increased involvement of the private sector, and again by the fact that some industry associations are not as effective as others.

There is also an element of confusion regarding goals. Policy makers in some MS are not fully aware that implementing the FATF recommendations does not automatically lead to a coherent national CFT policy. Where no well-researched national policy exists, there is no rational basis for defining and ordering activities.

The 9SR themselves are comprehensive, necessary and sufficient. They increase transparency, aid investigation and support judicial action against financiers of terrorism. However, there are still problems with regard to definitions of terrorism (SRI) and asset seizure (SRIII) linked to the wording of EU regulations. Co-operation between MS (SRV) is mainly bilateral and a consensus on policy towards NPOs (SRVIII) is still to be reached. The attention given to the

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9SR may have detracted from work on “routine” AML issues that are possibly closely linked to TF.

The Intelligence-led Approach to all Economic Crime

Importantly, given the EU’s emphasis on intelligence-led approaches to TF, MS enjoy intra- and extra-EU bilateral intelligence relationships, which often predate 9/11 and cover wider issues. They outweigh global (UN, FATF) and regional (EU) relationships. Much of this work goes unseen. MS relationships with non-EU states, e.g. USA, and MENAFATF and APG states, play an important role in CFT. Primary MS intelligence cooperation is directed towards operational tasks within these established relationships, and less towards multilateral initiatives, such as typologies, where the EU could add value (e.g. by developing use of Europol and SitCen, and by encouraging more effective public private partnership).

More widely, it is not just TF measures that need to be effective but also underlying national and international criminal investigation systems. As well as high profile 9SR foreground processes (which are not in fact TF specific), less spectacular general crime reduction processes also impact on TF (e.g. tax, company and social security legislation, as well as accountancy standards in the private sector). Public and private sector antifraud measures are especially important. Data produced these and other processes can feed into wider CFT and CT intelligence systems, but to be a true force multiplier such data must be matched by the means for smart interpretation and corroboration. Otherwise collection is a waste of effort.

Updating the CFT Policy – Conclusions and Recommendations

In updating the CFT policy, priority should be given to freezing mechanisms on a national basis, more legal protection for those involved in SAR and freezing actions, more FIN training, the encouragement of cash into the formal sector, gathering more evidence on NPO risk as a basis for action and learning lessons from EU external work. The CFT policy must also consider carefully where the EU may best act itself and where it might better stimulate action by others. It should look especially to those areas where it can impact in the long term, where the value of general crime measures is high both against TF and other threats.

The Report concludes that the 9SR regime promoted by the EU is actually an OC regime, not a specific TF regime. It is based on a US threat model that does not apply in Europe (e.g. given the scale of domestic threat). The EU has a natural role helping to make the 9SR a useful tool in investigating organised crime, and the CFT policy needs to be reframed in the context of EU crime reduction policy in general.

First though, a full baseline threat analysis needs to be undertaken of threats across the EU as a whole. Thereafter, horizontal coordination must be enhanced to meet any subsequent TF threats. Once the efficiencies of the current system are exhausted there will be pressure to extend the mandate of key EU CFT arrangements. MS will face a political choice about if and how they want the process to evolve. The report sets out a possible model for a new EU horizontal coordination framework, that would enhance the role of the CTC and improve secure data sharing between MS. The report also makes a number of standalone recommendations to address the issues summarised here.

0.3 Method

The actual methodology used was in line with that set out in the bid documentation with the exception that the A2E compliance analysis framework¹ was used rather than the T11 framework. This is because A2E extends analysis to dysfunctional systems and external events and these dimensions are not covered by T11.

To comply with the tender specification for a high level analysis avoiding duplication of FATF-based mutual evaluation processes, and to inform critique of policy, the study was conducted on a causal basis i.e. once a line of analysis determine a likely problem, analysis switched to the probable cause. For example, where a low level of SARs related to TF was reported, our questions focussed more on *why* there was a low number not *what* the low number was.

Data was obtained by desk research from FATF/Moneyval and IMF reports, EU and MS official institutions and documents, as well as academic publications. Semi-structured interviews based on a questionnaire were held in person or by telephone with representatives from the public, private and NPO sectors. The countries selected for closer analysis were France, Germany, Ireland, Italy, Latvia, Malta, The Netherlands, Poland, Spain, Slovenia and United Kingdom. The selection of states was based on their size, location, length of EU membership, evaluation history, economy and history of terrorism. Where useful, reference is also made to issues and situations in other MS based on FATF/MONEYVAL reports and first-hand experience. To preserve confidentiality, responses are not attributed.

A meeting with wider range of representative of MS was held in December 2006 where the analysis, conclusions and recommendations were discussed, and certain revisions undertaken.

0.4 Report Structure

Section 1 describes the background to global CFT arrangements, issues arising from them and how they set parameters for EU action.

Section 2 describes EU CFT action, issues arising from them and how they set parameters for implementation of the FATF40R and 9SR by MS.

Section 3 reviews compliance by MS with the FATF40R and 9SR in general and with the each of the 9SR. It also reviews the effectiveness of the 9SR as a CFT instrument and the other necessary structural elements of a CFT system.

Section 4 analyses the findings in Section 3 and the intelligence dimension and their implications for updating the CFT policy

Section 5 contains the study conclusion, sets out a common model for coordination of EU crime reduction measures (operationalised for CFT) and makes a series of standalone recommendations grouped thematically.

¹ A2E and T11 are analytical frameworks for assessing potential success/failure of policy in relation to 5 risk-oriented (A2E) or eleven compliance-oriented (T11) factors. They are both logical methods of grouping those subject to rules by the risks they represent and a means of communicating compliance and risk issues.

1. BACKGROUND - GLOBAL HIGH LEVEL CFT ARRANGEMENTS

1.1 The "Financial War On Terrorism"

1.1.1 Simple Goals

The "financial war on terrorism" is a term that has been used to describe the "long term strategic blockade [of] terrorist organisations by identifying and freezing the financial assets that are their lifeblood"². This is a key part of a wider global response, including by the EU and its MS, to attacks by domestic and international terrorists that characterised the last decades of the 20th Century and reached new levels of intensity with the tragedies in the USA (2001), Spain (2004) and UK (2005).

More prosaically, combating the financing of terrorism relates to counter terrorism in much the same way as anti-money laundering relates to crime reduction. The rationale for focussing on terror funds is thus largely the same as that for targeting any other criminal funds. Terrorists and their dependents, like other criminals, cannot live or operate without financial resources. Accordingly, countermeasures in this sphere have two main aims, namely to:

- i) Prevent terrorists and those connected with them from receiving money and money substitutes in the first place, and
- ii) Enhance the speed, quality and quantity of intelligence, investigations and evidence gathering relating to terrorists who already hold funds (and so improve surveillance and/or interdiction).

1.1.2 The Same and Different: Terrorist Financing and Money Laundering

Terrorist financing and money laundering occur in the same regulatory space and are frequently linked, especially where terrorists fund their activities by means of crime. For example, a terrorist group may target a value transfer system or charity primarily to acquire funds (e.g. by getting a sympathiser to divert payments) and only incidentally to move or convert the proceeds. In such instances, the aims and means of preventing terrorist financing and money laundering are very similar.

Where terrorist financing involves the transformation of legal assets into illegal assets, the standard money laundering process is reversed. Rather than giving a legal appearance to illegal assets it involves making legal assets available for criminal purposes. The nature of money laundering - "dirty-to-clean" and "dirt-to-dirty" processes are comparatively well understood. The full nature and potential of the "clean-to-dirty" processes associated with terrorist financing are less well defined and understood, though there are similarities with fraud. The fight against terrorist financing has therefore resulted in new approaches being developed to address the gap in understanding, particularly by means of new intelligence processes. This is an ongoing task as it is necessary not only to analyse past threat patterns but also to identify and analyse new ones as they emerge

1.1.3 Elements of an effective International CFT Regime

To mitigate the first mover advantage terrorists otherwise hold, it is necessary to:

- i) Maintain effective control environments in traditional areas of crime, financial crime and money laundering and so defend against known means of asset manipulation.

² The Financial War on Terrorism- A Guide *FATF* Paris (2004)

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ii) Enhance the development and implementation of new control environments specific to terrorism. This is especially important to combat unknown forms of asset manipulation (e.g. by “budget” terrorist groups living partly in a virtual environment), which are hard to detect by established means.

As global terrorism is, by definition, an international phenomenon, these objectives must be achieved uniformly across all affected states. A level playing field is essential to ensure uniform prevention and disruption of terrorist activity, without which there is the risk of presenting a target, distorting markets and exposure to moral hazard. An effective international CFT regime is generally understood to rest on:

- A proper understanding of risks, vulnerabilities and defences
- An appropriately structured legal systems and institutions to support action against actors, activities and assets
- Preventative measures in areas at risk and mechanisms to obtain timely data from such areas
- National and international cooperation with regard to information, civil and criminal justice proceedings.

The emphasis on data, especially financial data, is essential at the high level to establish the scale of the problem and to try to assess what constitutes a proportional response. At the lower level, too, data is needed to support identification and tracking of suspicious assets or people. However, with new and fast moving forms of national and international terrorism it has become very hard to detect intentions and preparations, which impedes both operational action and useful assessment of policy proportionality³. Knowing how assets are used, and by whom, can help reveal the identity, plans and resources of terrorists and, where they exist, their networks. It enables more informed and effective decisions on how to deal with threats, individuals and assets. FININT, including TF intelligence, is important because TF either involves traditional financial crime processes that FININT experts can recognise, or there are large unknowns that they can research.

However, as will be seen, FININT itself needs other forms of intelligence to achieve its potential. A central theme of this report is how efficiently and effectively intelligence based processes contribute to the CFT effort of the EU and MS states. A key determinant of such performance is the global regulatory framework on which EU efforts are based. Key international players in this arena are the UN, the FATF, Council of Europe/MONEYVAL and the IMF.

1.2 UN Action on Terrorism and Funding of Terrorism

1.2.1 Establishing universal Standards

Whilst central to the pre-emption and investigation of terrorism, inhibiting funds flow and "following the money" are difficult to accomplish in the absence of a robust regulatory environment both within and between nations, and it has taken a relatively long time to develop a universal standard, Thirty-six years elapsed between the first of the UN anti

³ A further problem is that concepts of proportionality, and thus the outputs of analyses, differ. It would also be difficult to disaggregate CFT policy impacts from other economic crime policy impacts. This Study recommends 5.3.2 the use of structured ex ante analysis of regulation in this area to increase understanding of such issues.

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terrorism conventions in 1963, and the 1999 International Convention for the Suppression of the Financing of Terrorism.

The Convention is the result of detailed negotiations often of a technical nature. It is a key reference point for other standard setters.

Box 1: UN 1999 International Convention for the Suppression of the Financing of Terrorism

The 1999 Convention obliges member states to establish and maintain a general anti terrorist financing regime to internationally accepted minimum standards. Specifically it:

- Requires parties to take steps to prevent and counteract the financing of terrorists, whether direct or indirect, through groups claiming to have charitable, social or cultural goals or which also engage in such illicit activities as drug trafficking or gun running;
- Commits states to hold those who finance terrorism criminally, civilly or administratively liable for such acts;
- Requires the identification, freezing and seizure of funds allocated for terrorist activities, as well as the sharing of the forfeited funds with other states on a case-by-case basis. Bank secrecy is removed as a justification for refusing to co-operate¹.

The UN has reacted in response to specific threats, principally by means of Security Council resolutions. Whilst such resolutions are quicker in the making they typically result from short political, as opposed to long technical, processes. As information on threats becomes available additional resolutions are used to encompass them. UNSCRs 1267 and 1373 are key instruments in CFT policy. Both the Convention and the UNSCRs mandate action that implies the use of FININT.

Box 2: UNSCR Resolutions

UNSCR 1267 In response to *inter alia* attacks in Africa, in 1999 the UN established a Sanctions Committee on Taliban and Al Qa'eda, which publishes lists of proscribed individuals and entities, and requires assets to be seized.

UNSCR 1373 After the 2001 attacks in the United States, this instrument obliged all States to criminalise assistance for terrorist activities, deny financial support and safe haven to terrorists and share information about groups planning terrorist attacks.

UNSCR 1566 provides for the extension these measures to newly targeted terrorist groups.

1.2.2 Implementation and Monitoring

The UN helps its members to implement its measures in a number of ways. The Counter-Terrorism Committee (CTC) has published a legislative handbook covering the UN12ATC and can call on the Counter-Terrorism Committee Executive Directorate (CTED)⁴ for technical support and to facilitate external technical assistance, cooperation and co-ordination. The United Nations Office on Drugs and Crime (UNODC), which is based in the EU (Austria), also has a technical assistance role via its Terrorism Prevention Branch (TPB). The

⁴ Established under UNSCR1535

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UNODC publishes checklists for the UN12ATCP and UNSCR 1373 as well as a Guide for the Legislative Incorporation and Implementation of the Universal Instruments against Terrorism.

The UN works closely with international regional organisations, and meets annually with the EU on a technical level. In addition, the UN has direct bilateral links with EU MS, giving direct and indirect opportunities for dialogue on standards and implementation issues. Implementation of obligations by UN Members, including all EU MS, is monitored on a consensual basis by means of self-assessments and inspection visits. These country evaluations are meant to inform, maintain level playing fields and capture best practice. They rely for transparency, objectivity and fairness on a common evaluation methodology.

1.2.3 Issues relating to the UN's high-level CFT Standards

The UN gives individual states responsibility for implementing its instruments. Whilst it monitors implementation, no sanctions regime against member states operates at this level and where the CTC has attempted to pursue a critical line, it has encountered political opposition.

Whilst mandating action that implies FININT, the Convention and the key UNSCRs make no explicit mention of such intelligence in connection with CFT. It is for UN MS to decide, once they implement UN instruments, how to make them effective. The UN itself is not expected to offer TA capacity in intelligence, but to facilitate the sourcing of such help from other MS. The Convention does suggest the use of Interpol to share CFT intelligence.

Because the UN tries to secure broad agreement to its measures, it must often reconcile widely ranging national opinions, and in such cases its instruments must balance effectiveness and acceptance. This is particularly evident in the designation of terrorist groups and the definition of sanctions on terrorists. Overbroad TF instruments impact on the quantity and quality of action needed to operationalise them.

Operationalisation of the UN's high-level minimum standards occurs at regional and national level, and sometimes by economic sector. This has the advantage of leveraging the greater coherency of opinion and values as well as the higher senses of public good and utility found at these levels. However there is a trade-off, because mechanisms aimed at ensuring level playing fields in the face of different challenges and resources can be abused for national and regional political and economic advantage.

As with many regulatory processes, UN activity combines long-term general structural measures with short-term specific political initiatives. Competition can arise between the requirements of articles in conventions (which are developed through often lengthy consensus processes) and clauses of individual resolutions (which are often drafted summarily in direct response to an event). This can complicate implementation and does so in the case of the UN CFT instruments. Whilst the UN has stated that in such cases the wording of the Convention is the better wording, there is still scope for varying interpretations of high-level principles.

1.3 Detailed Global Standard Setting

1.3.1 Financial Action Task Force and the Council of Europe's MONEYVAL Processes

It was partly to tackle such issues that a major role in operationalising UN CFT measures was entrusted to Financial Action Task Force (see Box 3), whose core role is now setting and

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monitoring standards for both AML and CFT. The Council of Europe's MONEYVAL mechanism, based on a Convention between European countries, also applies FATF standards and monitors AML and CFT standards in Europe. All countries that were members of the EU before enlargement in 2002 are members of FATF, and all new members belong to MONEYVAL.

Box 3: The Financial Action Task Force

In the 1970's and 80's the UN worked not just on terrorism but also organised crime, especially drug related crime. As political consensus grew on the threat posed by money laundering to banking systems and financial institutions (as recognised in the 1988 UN Vienna (Anti Narcotics) Convention) it became clear that initial action against the finances of criminals would focus on OECD member states. At the 1989 G-7 Summit the world's leading nations established the Financial Action Task Force on Money Laundering (FATF) with the European Communities represented by the EC and the "old" 15 MS as founder members. (The "new" MS are all members of Moneyval, with some keen to be direct members of FATF). A Task Force was established to examine money-laundering patterns, review past action, and set out further measures needed to combat money laundering. In April 1990, FATF published Forty Recommendations for pursuing the fight against money laundering, which were updated in 2003 including to reflect new UN anti money laundering instruments, notably the 2000 Palermo (Organised Crime) Convention. In 2001 the FATF's mandate was extended to cover TF in which area it has now issued nine Special Recommendations.

The FATF40R and 9SR (together with their Interpretative Notes) provide detailed standards for legal systems, preventative measures by regulated sectors as well as institutional and other necessary measures based on the relevant UN AML and CFT Conventions. The aims and requirements of the 9SR are shown in Box 4.

FININT gathering capacity, coordination and exchange capacity, domestically and internationally are implicit in the FATF40R and 9SR (Recommendations 26, 31, 40 and SRV taken together). The Interpretative Note to Recommendation 40 suggests a range of options for "information" exchange, including bilateral multinational agreements, MOUs and reciprocity, as well as regional organisations and international organisations.

The CoE (via its Multidisciplinary Group on International Action against Terrorism - GMT), and later its Committee of Experts on Terrorism) has identified priorities and updated CoE CT instruments. The Council of Europe Convention for the Prevention of Terrorism (CETS No. 196) was opened for signature in May 2005 and the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism (CETS No.: 198) at the same time. The latter convention facilitates quick action to find assets and information on assets held by criminal organisations, including terrorist groups. It specifically highlights the role of FININT units in obtaining access to such information and exchanging information to speed up restraint, seizure or confiscation procedures. The CoE is also active in other areas such as cyber crime, human trafficking and, via its Greco programme, fighting corruption.

1.3.2 Implementation and Monitoring

FATF not only issues Interpretive Notes to help countries implement the FATF40R + 9SR recommendations. It also conducts typologies exercises that provides insight into global threats and responses. Since incorporating AML/CFT into its work programme in 2004 the IMF has published a reference guide on AML/CFT issues, handbooks on FIUs and on legislative drafting as well as papers on alternative remittance systems. The CoE operates a technical assistance programme aimed at improving legislation, building institutions, training practitioners providing policy advice and fostering cooperation.

Box 4: The Nine Special Recommendations

- SRI Ratification and implementation of UN instruments - notably the 1999 Convention and UNSCRs 1267 and 1373.
- SRII Criminalisation of TF and associated money laundering - to give legal means and resources to investigating, prosecuting and punishing terror finance.
- SRIII Freezing and confiscation of terrorist assets – to prevent flows and punish terrorists.
- SRIV Suspicious Transaction Reporting – to ensure the correct scope and timelines of suspicion reporting and action by those subject to a duty to report.
- SRV International Cooperation – to ensure mutual legal assistance and information exchange (civil, criminal and administrative) between countries relating to inquiries and proceedings.
- SRVI Regulation of Alternative Remittance Systems – to increase transparency and control over funds outside the conventional financial system and not subject to FATF standards.
- SRVII Standards for Wire Transfers – to make basic information available to the criminal justice system, intelligence and regulated entities.
- SRVIII Regime for NPOs – to prevent their abuse for TF purposes.
- SRIX Regime for the cross border transport of cash and negotiable securities - to stop suspicious cross border flows and enable sanctions and confiscation where indicated.

In addition to establishing international standards for AML and CFT, to ensure global action in these fields, both FATF and MONEYVAL have a mandate to ensure their members have implemented recommendations fully and effectively. This is monitored by means of peer evaluations in close cooperation with the IMF, as all evaluations of financial sector strengths and weaknesses conducted under the IMF's Financial Sector Assessment Programme (FSAP) include an assessment of the jurisdiction's AML/CFT regime. Assessments conducted by the IMF, the World Bank, FATF, and MONEYVAL use a common methodology (see 3.1.2).

Although the FATF operates a Non-Compliant Countries and Territories regime, the last country has been removed in October 2006. In 2001 FATF decided against further rounds of NCCT reviews. Whilst maintaining its readiness to apply Recommendation 21 in the future, in practice it is unlikely to do so except in exceptional circumstances. Like MONEYVAL, it must work by peer pressure.

1.3.3 Structural Problems with Standards

Practically all respondents interviewed in the course of this study were persuaded of the worthiness of the global CFT activity and value of standard setting and peer review

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mechanisms. However, a number of observations on problems inherent in current arrangements were also made. The most frequent are as follows:

- The FATF40R + 9SR are not obligations under a treaty or convention but informal political commitments in response to political concerns, especially the 9SR. Attitudes to the Recommendations vary with global and national political circumstances. They need the force of law to ensure implementation, but national and regional politics influence the speed and means of implementation, and thus effectiveness.
- Drafting of the original eight Special Recommendations took place at a time of heavy pressure to respond to the 9/11 Attacks. There was neither a comprehensive global risk analysis nor time for proper consultation. Five years later the 9SR are only just settled, or still regarded as “Work In Progress” This is especially true of SRVIII (NPOs) and SRIX (Cross-Border Cash), which give rise to complex and extensive issues.
- SRVI-IX are not special to TF and apply to financial crime generally (see Sec. 4).
- The FATF40R and 9SR are not directed at the analysis of TF in which the amount of money does not play a decisive role. Low volumes tend to remain undetected.
- The 9SR are derived from the FATF40R (with the added benefit of certain countries' experience of domestic terrorism) and rely on effective implementation of the FATF40R to be effective themselves. Countries that cannot comply with the FATF40R find it difficult to comply with the 9SR.
- There are issues relating to some of the FATF40R, which relate to past failures to consult target groups and which still cause compliance problems for businesses at national level (see also 3.4.7 for impacts of consultation on SRVIII).
- Most FATF40R are preventative. Building up AML activity based on gatekeepers' reporting obligations fosters over reliance on SARs and creates a bottle neck in the criminal justice system, symbolised by the SARs avalanche post 9/11.
- Conversely previously neglected areas of criminal justice, including non-SAR based FININT activity, are now seen as essential and the balance still has to be brought back under control.
- The standards need substantial interpretation to cope with the new forms of national and international terrorism that emerged after 9/11 in Europe, and in which native domestic elements play a much larger role.
- Despite the best efforts of many parties, including the development of training programmes typologies and indicators, there is still a lack of detailed guidance on the complex fundamental issues frequently faced by regulators and target groups encounter, and *a fortiori* on situational issues.
- The initial recommendations were originally developed by FATF members with large economies and resources. There are legacy issues, which are only now being tackled to take into account the situation of members of FSRBs who usually have fewer resource and less extensive economies, but who still must introduce a high specification system.

1.3.4 Issues with Evaluation, Overspecialisation and parallel Processes

The objectives, sophistication and results of FATF based mutual evaluation systems are well established. It has been an impressive achievement given the complexities of the issues involved and the absence of formal power. At the same time reservations were voiced about the mutual evaluation process, which directly impact on CFT effectiveness in MS:

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- A key concern was that the FATF40R and 9SR are evaluated by reference to a detailed set of 250 or so evaluation criteria, which themselves sometimes require elucidation. Where “rules give rise to rules”, evaluation processes can become over-burdensome with the risk that they become mere box ticking exercises.
- Claims of full compliance e.g. in self-assessments, made in an attempt to avoid further burdens, make the evaluation process less rather than more transparent, and adversarial rather than supportive. As interventions, evaluations risk no longer being a challenge but a chore and so may lose much of their meaning.
- Constant fine-tuning of standards by means of new rules and notes risks the whole process becoming bureaucratic and divorced from operational issues.
- The cumulative effect of pathfinder questionnaires, visits and follow-up is to engender supervision fatigue, as well as crowding out the very effort that is being evaluated.

NB: We do not attempt to solve all these problems in this report.

Moreover, whilst having many people focus on the same issues can produce useful different perspectives, we noticed it could also lead to introspection and loss of context. In particular it can lead to CFT issues being analysed in unnecessary detail in and in isolation. This entails the risk that important lessons from analogous problems (human trafficking, corruption) are crowded out for lack of time and because they belong to different processes. This raises issues of coordination at MS and institutional level.

At a higher level, taken together with action by the EU and MS analysed below, the global AML/CFT regime can be seen to consist of at least four parallel processes - UN, FATF/IMF, EU and MS - which interact in numerous ways. The same departments and agencies from Members States and IROs operate in the working groups that develop and monitor standards. Thus national specialists circulate in FATF/IMF, CoE/MONEYVAL, EU, and UN processes. Whilst they contribute to the uniformity of standards, their very efficiency is resulting in a highly specialised system and only a small number of people have a wide grasp of all issues. The system depends for its effectiveness as much on informal links between these individuals as it does on formal institutional processes.

The issues arising from UN action and detailed standard setting not only confirm the theoretical potential for the EU to contribute to the CFT process, but also help to define high level process priorities - helping to remedy deficiencies and differences in the international acquis and helping implementation in MS. The challenge is for the EU to add value by dealing with TF in such a way as to lessen the administrative and financial burdens on MS and target groups whilst adding to the public safety of EU citizens, not only with regard to terrorism but organised crime more generally.

2 EU ACTION

2.1 EU Action on CFT

2.1.1 Origins of CFT policy

EU CT activity started in bilateral dialogues between MS on criminal law issues in the context of European Political Cooperation and later CFSP. In 1975 the TREVI Group looked at terrorism, radicalism, extremism and violence on an international level, as did a working group on international terrorism in 1986. Post Maastricht, JHA subsumed some of these

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activities under the Third Pillar whilst others (notably intelligence, foreign policy and security cooperation) were developed under the Second Pillar's foreign and security policy agenda. In 1999 the Council made a Recommendation on cooperation in combating terrorist groups⁵

Key measures under the First Pillar were the First and Second Money Laundering Directives of 1991 and 2001 which imposed AML obligations on, respectively, financial institutions and DNFPBs, and mandated the establishment of FIUs in MS. The 3MLD, adopted in 2005 and due to come into force in 2007, implements the revised FATF40R and the 9SR. It is the first MLD specifically to include CFT.

The EU took wide-ranging measures against CT and CFT in the aftermath of the three large-scale terrorist attacks in the USA (2001), Spain (2004) and UK (2005). Some measures were designed to address the content of what have become the 9SRs and, within the scope of an overall Action Plan on combating terrorism, a CFT policy was developed and later updated.

Both the Action Plan and CFT policy currently operate within the overall framework of the 2005 EU Counter Terrorism Strategy. This stresses that MS have prime responsibility for CT, including CFT, and positions the EU to help MS by crosscutting contributions. The EU thus pursues the four parallel goals of the strategy - *Prevent, Protect, Pursue, and Respond* - along four axes, namely:

- *Strengthening national capabilities.* Focus: collection and analysis of information and intelligence.
- *Facilitating European cooperation.* Focus: information sharing and cooperation in criminal and civil justice systems.
- *Developing collective capacity.* Focus: making best use of EU bodies.
- *Promoting international partnership.* Strengthening cooperation in CT.

CFT is currently part of the *Pursue* goal though it has also been considered part of *Prevent*. As EU action towards each of the goals is spread across all Three Pillars and all MS, a CT coordinator has been appointed to monitor and encourage implementation of CFT measures.

2.1.2 EU CFT Strategy

As set out in 16089/04 (as updated) the key elements of the EU CFT strategy are:

- *A targeted intelligence led approach based on improved information sharing within and between government and private sector.* The strategy promoted the role of FIU-NET in promoting data sharing between competent authorities and feedback from FIUs to financial institutions (and presumably DNFPBs). It also called for a national structure for coordination and exchange of data between intelligence, law enforcement supervisors and the private sector.
- *Continual improvement to designation and listing procedures.* The strategy foresaw quicker and more accurate designation procedures focusing on NPOs, electronically delivered and monitored by the EU (including in respect of legal issues).
- *Development of tools for tracing funds, especially those held by informal banking systems and NPOs.* This was to be achieved *inter alia* by better training of financial investigators, better control of cash, wire transfers and alternative remittance systems, as well as by reducing opportunities for the abuse of NPOs.

⁵ OJ C 373 23.12.1999 p.1.

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- *Ongoing monitoring of trends and development of counter measures.* This element promoted the role of SitCen and Europol.
- *Support for Extra Union activity.* This included support for ratification of UN instruments, support for the FATF process and cooperation with global partners as well as technical assistance for key countries.

2.1.3 Current Action in Support of individual FATF Special Recommendations

The current Action Plan lists a wide range of current measures in support of the CT Strategy, which directly and indirectly support action to implement FATF 9SR. Those of particular relevance to this study include:

SRI-III All MS having ratified the 1999 Convention, the EU continues to press MS to implement legislative instruments listed in the March 2004 Declaration. MS are obliged to implement the UN list, plus names proposed and unanimously agreed by MS. Best practice advice has been made available via the web and there have been calls to MS to “top up” the EU designation mechanism to supplement possible gaps left by 2001/931/CSFP.

With regards to SRIII, key instruments are Regulations (EC) No 881/2002 (UN Al Qa’eda and Taliban list) and 2580/2001 (EU terrorism list) which are directly applicable law in all MS.

SRIV The first set of implementing measures on PEPs, simplified Customer Diligence (CDD) and “occasional” transactions (executed by non-regular customers) was adopted by a Directive 2006/70/EC on 1 August 2006 (JO L241/29 of 4.8.2006).

SRVI is implemented through the 3MLD, which requires the registration or licensing of money remitters and will be supplemented by a future Directive on payment services currently under negotiation at the Council and the European Parliament.

SRVII A Regulation on payer information sent with wire transfer of funds was adopted on 7th November 2006, setting new minimum requirements of identity information based on a \$/€ 1,000 threshold. The new regime comes into force on 1st January 2007.

SRVIII Following a EC Communication and the Council Declaration of July 2005 on preventing the misuse of NPOs by terrorists, Communication COM(2005) 620 sought greater transparency of the non-profit sector via the promotion of best practice and better cooperation, including in the exchange of financial intelligence. Five principles have been established for regulation in this sector following agreement on the FATF’s Interpretative Note on SRVIII. There has been consultation on a Framework for a Code of Conduct for NPOs to enhance transparency in the sector and research on key aspects of risk and regulation has been commissioned.

SRIX In October 2005 a new regulation was adopted providing a common system for cash controls at the external borders of the EU (26 October 2005). It supplements the 3MLD, requiring anyone entering or leaving the EU with equivalent or more than €10,000 in cash or equivalent instruments to make a written, oral or electronic declaration, with national authorities required to keep such data on file.

Other action by the EU which supports MS in achieving the CFT goals implicit in the 9SR include addressing TF issues in the European Security Strategy, tasking SitCen with threat

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assessment and risk analysis and establishing capacity in CFT, initiatives to increase the role and effectiveness of Europol and Eurojust in CT and CFT investigations, the establishment of FIU.Net and an EU FIUs platform, the promotion of Joint Investigative Teams, the Police Chiefs Working Group, and work on the European Arrest warrant. At its meeting on 1-2- June 2006 the Council also adopted a general approach on the proposal for a framework decision on the European Evidence Warrant.

The EC and Europol have initiated a project to promote the use of financial investigation as a law enforcement technique in the EU 25 through common minimum training standards. In the long term, this project can contribute to encouraging financial investigation of terrorist suspects and facilitate cooperation among FINs within the EU on TF and more generally.

In support of FATF Recommendation 31 (effective cooperation and coordination mechanisms) and the Madrid Declaration, the EC has also been looking at ways to improve national machinery for coordination and information exchange.

Finally, Council Decision of 28 November 2002 (2002/996/JHA) put in place arrangements for evaluating the legal systems and their implementation at national level in the fight against terrorism ("the Peer Evaluation"). The first evaluation exercise under the 2002 Council Decision came to an end in December 2005 and the possibility of a new round of evaluations is now under discussion.

2.2 Issues at EU Level

2.2.1 Structural Issues

The CT and CFT agenda since 9/11 has ballooned, and with it the AML and all other crime security and market agendas with a nexus to CT and CFT. At EU Level there are a large number of committees and working groups as well as myriad documents and non-documents relating to the more than 150 action points that have gone into the Action Plan. There are industry groups and think tanks tracking developments and this pattern is replicated in each MS. Trying to keep abreast of all actions and interactions in the EU is itself a challenge. The EU has undertaken peer review of CT efforts. However, it does not have the capacity or the mandate to establish an ongoing internal mechanism for periodic, structured and detailed evaluation of its own AML and CFT measures. The reports of the CTC do however fulfil a first step in this direction – an inventory of action.

The absence of structured detailed monitoring also contributes to the fact that the EU lacks a key instrument – a fully informed baseline assessment of threats and risks to the EU. Without this, there is no way to direct the efforts and set priorities, nor attribute success nor learn from failure. There are overlaps, gaps and difficulties in coordination. A proxy is available using Sitcen and the more frequent Europol Situation and Trends (TE-SAT) reports, but these rely on input from MS – the EU has no proprietary intelligence gathering capacity other than diplomatically via its delegations and representations.

The premium on coordination is further heightened by the fact that bodies in the EU that are involved with CFT are split across all three Pillars and there is a Pillar issue also in respect of MS. Whilst horizontal cooperation between pillars which has become more effective (e.g. the meetings TWG and COTER (even though TWG appears to be involved in TF only marginally) it becomes more difficult the higher (and thus the more political) the level of

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action required. By the same token, the EU, as it states in its own strategy, does not hold prime responsibility for CT and CFT issues. It only has effective direct powers in the First Pillar's communitarised areas, and in the Second and Third Pillars it relies on efforts to coordinate, harmonize and influence policies on an intergovernmental (as opposed to supranational) level⁶. Member states and their agencies are cautious in the extent to which they will allow the EU to take steps that impinge on national security issues and arrangements unless it is part of a wider political process. This is an aspect of institutional problems at EU and MS level that we review in Sections 3 & 4.

Differences in policy content are matched by differences over process. The EU that originally initiated action on AML comprised MS who were FATF members and whose approach was aimed at maintaining the integrity of the financial system, i.e. under what is now the First Pillar. Newer MS learned to tackle AML under the MONEYVAL umbrella, meaning they follow an approach that has its roots in judicial cooperation, which comes under the Third Pillar. There are divergent approaches to AML/CFT priorities on policy and in operational matters, which can feed back as particularism at the political level.

The political boundaries imposed on the EU are best illustrated by the position of the Counter Terrorism Coordinator. It would be reasonable to think that, to solve the above problems, an authority would be established to set goals, coordinate and monitor action across pillars and MS. In fact the Coordinator has neither the powers nor resources to fulfill such a role and acts instead as chronicler and *porte-parole* to his political masters. Many commentators were struck by the apparent failure to follow through the appointment of the CTC, allowing the role to achieve its presumed goals and providing the requisite organizational status, powers and resources, especially with regard to horizontal coordination. Boundaries are also apparent in the key area of data sharing and operations where even Europol, the most operational of the EU units is not only confined to information exchange and analysis but, like SitCen, is limited in its ability to receive data from, and cannot task anybody.

Where the EU is allowed to set the agenda, it faces a different set of issues. The policy makers in MS who nominally have responsibility for CFT are (for reasons as simple as job rotation) often hard pressed to keep up with what is going on in a highly complex environment. It is the experienced front line staff in intelligence and law enforcement units, as well as in organisations being used for TF purposes, which have to deal with the problem day-to-day. This is also the level at which there is practical knowledge of what needs to be done and how to do so. We noticed that effective consultation with these professionals by policy makers depends greatly on the quality of policy makers in the relevant EU and MS institutions.

This gives rise to a further problem. Because the scope of AML/CFT activity is set wide (FIs, DNFPBs, any one suspicious of TF), it is complex to make regulations at MS level, let alone across all MS where conditions can vary greatly. To do so the EU must engage in long-term structural regulation and this takes time, especially where there is political opposition. An example of this is the disinterest of a number of presidencies in regulating cash couriers (regulated in the US in the mid 1980's). The slowness of the EU in tackling issues that are important and costly to industry (such as SRVII) and the lack of associated public information and education effort was one of the most frequent criticisms of the EU encountered in this project. In the fast moving world of flexible threats including CFT, the EU is not structurally

⁶ Zimmerman

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suited to delivering responses, and risks making the situation worse when it acts faster than its ability to cover all bases and angles.

A further question is the extent to which the EU has had its hand forced in this whole area by the events in the USA. The 22-year period between 1975 (TREVI Group) and 1997 (Amsterdam) was a period of intense domestic (e.g. IRA, ETA, Red Brigade, Rote Armee Faktion) and international (e.g. PFLP) terrorist activity. There were sensational attacks and major incidents in and against MS, including Pan Am flight 103 (270 killed) and UT 772 (171 killed). Till 9/11 the EU had relatively few initiatives against terrorism in the pipeline, and the emphasis was on bilateral or multilateral cooperation between MS on single issues and cases. As we discuss in Section 4 this can be an additional source of resistance by some MS to EU initiatives. In Section 4 we also analyse how US dominance in the policy area impacts EU CFT initiatives.

3 FINDINGS ON COMPLIANCE AND EFFECTIVENESS

3.1 Compliance with FATF40R and the 9SR

As is stressed in this report, compliance with the 9SR has to be considered in connection with compliance with the FATF40R on which they are based and rely. The basis for criminalization is in most cases the same, whilst seizure, freezing and confiscation follow similar or nearly similar paths (the administrative freezing procedures for TF in some MS foresee an allied court process), as do SAR systems, arrangements for mutual assistance in the judicial field and, to a certain extent, cross-border cash control provisions. Thus compliance with the 9SR requires a high degree of compliance with the FATF40R.

3.1.1 Compliance with the 2MLD and 3MLD

Compliance with 2MLD is an issue with regard to TF to the extent that the 2MLD defined crimes (including all organised crime and most types of serious crime, including terrorism) and professions falling within the scope of AML legislation, and provided for the establishment of FIUs in MS. The FATF considers effective AML arrangements to be a basis for effective CFT arrangements and 2MLD was regarded at the time it was passed as means to “improve anti-money laundering measures generally and in particular to prevent the laundering of funds for terrorist purposes”⁷ After 9/11 decisions and regulations by EU and MS in line with the 9SR grafted CFT measures onto implementation of 2MLD (e.g. Joint Commission - Council Declaration of 13th December 2001).

The first observation is a general one: The EC operates on the basis that all MS are in, or irreversibly committed to, compliance with the 2MLD Directive. The EC checks compliance in general, principally by reference to the legal steps that have been taken by MS. It is not in a position to assess what actually occurs on the ground in each MS and this is indeed the responsibility of each MS. The EC’s decision suggests a common minimum level of compliance within the EU, though where that level lies is probably best judged from analysis, where possible, of peer review output on the FATF40R and 9SR

⁷ António Vitorino, European Commissioner for Justice and Home Affairs at the 'Justice en Mouvement' Conference Brussels, 16 September 2002

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The 3MLD replaces the 2MLD and broadly reflects the revised FATF recommendations and all nine SRs, with the exception of certain criminal justice and customs matters. In extending the scope of regulation and introducing measures to promote proportionality, it specifically addresses TF. However, the 3MLD is not due to be implemented by MS till December 2007, and again, irrespective of the nominal level of compliance, only full inspection will establish the effect on the ground. The impression gained in the course of this study was that the quality of implementation of 2LMD and preparation for 3MLD differs considerably across MS.

3.1.2 Compliance with FATF40R

The FATF and MONEYVAL mutual evaluations reports in respect of the FATF40R give a more detailed insight in the level of implementation and the problems encountered. A number of MS were evaluated in the FATF 3rd Round and a number of the new EU MS were also evaluated by MONEYVAL in the same period. The latest MS ratings for compliance with the FATF40R are given for 12 MS in Appendix 1 (see also 3.1.3).

Analysis of the figures reveals a relatively high level of non-compliance for Recommendations 6, 7 and 24 and only partial compliance for Recommendations 5, 12, 16, 32, 33. These relate to:

- *CDD* (Anonymous accounts, PEPs, CDD for FIs and CDD for DNFPBs)
- *Suspicious activity reporting* (Non financial institutions, abuse of corporate vehicles)
- *Regulation and supervision* (Specifically, casinos)
- *Institutional matters* (Ensuring effectiveness of AML and CFT through good statistics)
- *Transparency* (Beneficial ownership)

The weaknesses in compliance with customer due diligence requirements severely limit the possibility of spotting suspicious transactions. They also limit the chances of identifying particular persons involved in financial transactions and the beneficial owners of accounts or companies. This in turn limits the chances for successful analysis of transactions in criminal investigations and for intelligence work. The weaknesses in suspicious activity reporting, partially a consequence of the other weaknesses, basically have the same consequences. Difficulties persist in the area of beneficial ownership and PEPs. (NB Though arguably a corruption issue, this study makes recommendations on the PEPs regime (see 5.3.5) as it was frequently mentioned by respondents as an issue in CDD. The study does not focus in depth on beneficial ownership as a separate analysis has been commissioned by the EC.)

In short, critical weaknesses in compliance with key areas of the FATF weaken the capacity for preventive measures, intelligence analysis and investigation of TF. Recent FATF and MONEYVAL inspection data suggests that some MS still have strong deficits here to the extent that it is almost irrelevant for TF purposes (other than in terms of helping to increase financial transparency generally) how high they score on 9SR compliance.

3.1.3 Compliance with the 9SR

Appendices 1 & 2 set out the ratings given to certain MS for their compliance with FATF40R and 9SR in peer evaluation processes. Where such ratings were not available a shadow rating has been given on the basis of the content of the relevant evaluation report.

Weak spots are compliance with the freezing obligations, the reporting of suspicious TF transactions, as well as the regulation of the NPO and cash courier sectors. Progress with

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remediating deficiencies in MS appears to be mixed and occurs for a variety of reasons. Many of these reasons are structural, and delays result from the slow speed of political and administrative planning processes in MS and problems integrating new legislation into existing laws. In some cases the cause of delay is positive e.g. for consultation, but in others it is simply a case of delays.

Implementation of SRVIII is still under discussion within the EU and awaits consensus regarding the policy towards NPOs, where a number of MS have strong reservations. The final form of the EU's implementation of Recommendation IX is currently being formulated and comes into force as of June 2007. In the absence of final EU standards, MS compliance varies widely in a field that is not seen as a priority, hence the low compliance scores mentioned below.

The 2006 assessments of compliance with 9SR in EU by some MS are not better than assessments completed in 2005. This may be an indication that the pace of improvement in compliance is low, if present at all. Comparison of compliance with the 9SR and FATF40R show that the level of compliance for 9SR is lower than for FATF40R. We now analyse some of the reasons.

3.2 Reasons for Compliance Differences between Member States

3.2.1 MS Interests and Start Positions

On the basis of the present research undertaken, we found that MS have different motives for compliance with the FATF 40 and the 9SR. They also differ in regard to the sophistication and transparency of their financial and other systems. The least transparent have the longest way to go. Some still have problems with the level of compliance with the FATF 40 whilst for others it is the 9SR that give rise to problematic scores. Some score relatively low both on the FATF40 and on the Special IX. Research during this project shows that broadly speaking MS fall into four groups.

Group A: For a number of MS the main motive for compliance is the threat of terrorist attacks. These MS have had experience with terrorism, have taken a variety of measures and are still taking measures to reduce that threat. Their CFT measures are part of a wider programme aimed at preventing, limiting and investigating acts of terrorism, nationally and on a global basis. Belgium, France, Germany, Italy, The Netherlands, Spain and The United Kingdom are the main representatives of this group.

Group B: In other MS the terrorist threat is seen as mainly theoretical, and remains for some a very remote possibility. They have no recent history of terrorist attacks, no significant minorities that pose a local or international terrorist threat and no internal opposition resorting to violence. Neither have they been safe havens for terrorist groups operating abroad nor for political movements related to political violence in third countries. Although the theoretical threat is always there, the likelihood of MS in this category falling victim to terrorism is low. The interest to implement CFT measures may therefore be lower than in other MS. These countries all have comparatively well regulated and relatively transparent financial and market systems.

Group C: A number of MS that do not have a high terrorist threat level still have an explicit interest in compliance, but for a different reason. They comply willingly with the whole set of

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FATF recommendations because they want to attract foreign investment. They are thus striving for a sound and transparent financial climate, which has the approval of the FATF to create favourable conditions for such investments. Even though the NCCT has been scaled back, at almost all costs they still want to avoid the reputation damage of a negative report and the type of inconveniences experienced by Hungary in 2000 when blacklisted by FATF for short comings (notably the existence of anonymous accounts).

Most Eastern European MS belong to this group. They do their utmost to implement all recommendations. The initial position of this group was less favourable compared to the first two groups, with the average level of both economic development and the level of transparency of the financial system low. A related motive here is the reduction of economic crime, a type of crime that has accompanied the transformation from a planned economy to a market economy.

Group D: A fourth group of MS does not perceive a high terrorist threat and so does not have explicit interest in extensive countermeasures. MS in this group have mainly national level financial markets. To comply with 9SR, they must not only improve AML/CFT standards but also the other necessary structural elements on which AML/CFT standards depend, and for which there may be a low level of resources (see 3.2.3) and political support.

Using these four sets of descriptions it is possible to categorise MS along two axes, according to their initial level of compliance being low or high, and the interest they have in implementing the recommendations being low or high as well. Table 1 shows this analysis.

TABLE 1: Classification of MS by Levels of Compliance and Interest		
	Interest in introducing FATF40R and 9SR	
	High	Low
High initial level of compliance (sound financial system)	Terrorist threat countries (<i>A</i>)	Economically developed countries which want to remain transparent (<i>B</i>)
Low initial level of compliance (less transparent financial system)	Economic growth countries (<i>C</i>)	Low transparency, less concerned countries. (<i>D</i>)

3.2.2 Time

Our research also shows that compliance appears to increase but slowly over time. It takes time to create a transparent system and the associated monitoring mechanism. Above all, it takes time for laws to be changed. The 3rd MLD, which finally established the 2003 revisions to the FATF40 and the 9SR, in law in the EU, has taken over four years to reach that stage. MS also take time to draft and find legislative slots for structural AML/CFT measures. No particular pattern in delays was observed in MS other than that countries tend to work more readily where they already have equivalent or near equivalent regulations (e.g. reporting of cash and valuables on entry, WTS in Malta). They also tend to wait for final decisions on EU regulation before initiating detailed processes. There are MS who work faster and slower in all areas and AML/CFT is not particularly different. Design and implementation time is also a

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factor in the speed with which target groups can react. Systems – often complex IT systems - have to be designed, tested and installed and staff has to be trained.

3.2.3 Resources

Even when effective measures have been developed, they cannot achieve results if insufficient resources inhibit their full use. A continual complaint from public sector bodies during our interviews was the lack of resources to implement the requirements of legislation. FIUs and ML and CFT investigation teams require staff as well as training and specialised equipment for such staff. Training has to be not only initial training, but also continual training to track changes in threat and potential threat patterns. Moreover, as there are many markets and many ways of abusing markets, either financial investigators need to be trained or outside experts brought in. In practice, where there are gaps in skill and capacity, investigations are triaged and some leads abandoned because they are too complex or resource consuming to follow up. This happens in all MS, and especially in those lacking specialised investigation capacity.

Capacity problems have been, and will continue to be, brought into focus by the FATF's move towards risk-based approaches in the search for proportionality. FATF makes it quite clear that its measures are designed to minimise impact on conduct of business. However at all levels, MS, sectors and individuals, there are often problems introducing risk-based systems, leading to unintentional non-compliance because of unfamiliarity and lack of confidence. Even second tier financial players can have difficulty in this area and have to employ outside consultants to develop the necessary systems and train staff. Small and inexperienced firms with little or no idea on what is expected of them under a risk based system often much prefer a rules based system that is more onerous but offers certainty of compliance targets. It is large sophisticated firms that prefer risk based approaches because they have a better risk reward profile and it is the large firms who can lobby more effectively. Moreover, countries with banking systems that include both developed and less developed firms, and have constraints in their inspection system, may prefer a rule based approach until their financial system is fully developed, because it is easier to implement and to inspect. It is a key issue for MS as the FATF's risk based approach is central to the 3MLD

3.2.4 Non-Compliance of MS with 9SR - A2E Aspects

A2E grouping and scoring (Appendix 3) show clearly that non-compliance is rooted more in Deficient Systems (institutional arrangements/infrastructure) and External Events (potentially competing issues) than in unwillingness to act. This is discouraging because solutions to problems in these domains typically take time and money to fix, and it has been shown that time and money are scarce resources.

Most interesting is the high score in Authority, as this is an area where approaches that leverage innate belief in the rationale and goals of policy can be used to encourage spontaneous improvements in weaker areas such as dysfunctional systems. It also suggests there may be arbitrages e.g. in the form of EU activity in support of immigration problems to free resources in some MS for more effective action on the CFT front.

The scores for Controls highlight the extent to which MS respect mutual evaluation processes and suggest that they are a more effective tool than self-assessments. This is important given the low ranking of sanctions as a compliance factor.

3.2.5 Institutional Factors

Both compliance with, and effectiveness of, the 9SR were found to be affected by institutional factors. These factors play a role both at the Community level and at the level of the individual MS. Terrorism and TF are multi faceted phenomena and a wide range of different types of institutions has a multiplicity of interests and responsibilities in the field. In most MS the desired comprehensive, selective and “smart” approach is hindered by the problems created by the institutional complexity of initiatives to fight TF.

The complication is illustrated in Appendices 4A and 4B, which give a general indication of the institutional structure within countries, though it must be borne in mind that there are considerable differences in institutional arrangements between MS. When one adds the major types of activities for the various institutions (policy, coordination of action and exchange of information on the MS level and on the EU level) the degree of complexity becomes clear. The problem of managing complexity is compounded by the legal limits to the exchange of information between agencies, the secretive character of security and intelligence services, as well as competition and distrust between institutions.

Within MS, even if there is a lead department, we noted that key responsibilities for CT are shared across a number of ministries, with responsibilities for CFT issues often spread across four or five ministries and outside agencies (e.g. SROs). Coordinating mechanisms are not always comparable or continuous and often the effective coordinator is the FIU.

At MS level, CFT policies are related to broader issues, such as foreign policy in and outside the EU, international military and security issues, financial integrity issues and investment policy, criminal policy and combating organised crime. These areas often involve input for both policy formulation and execution from the private sector and NPOs. Coordination has not only to be within the public and private sectors but between sectors as well. This at least doubles the complexity of the situation. A frequent response to this problem is to create public-private cooperation mechanisms, but these bring with them their own risks of inefficiency as a result of unrepresentative composition, inexperience, and preference for form over substance in interactions.

A major problem we noted was the weakness of trade bodies both on and across MS. The financial sector, law and accounting professions have strong European associations and generally strong national associations as well. Some DNFPBs, however, have shorter traditions and less experience of cooperation on issues of common interest. Lacking adequate resources, they are not as well represented at European and sometimes even at national level as is desirable. This reduces their ability to secure legislation that is more compliance friendly (e.g. via consultation processes) and also reduces efficiency and effectiveness of collective action to address common problems (e.g. standards, training, international exchanges).

3.2.6 Confusion of Goals

Reading between the lines of some respondents’ comments, it is clear that there is an element of confusion regarding goals, which compounds an already complex situation. Specifically, some policy makers are not fully aware that implementing the FATF recommendations is not the same as developing and implementing a coherent national CFT policy, and the former does not automatically lead to the latter. Rather, unless a properly researched national policy is in place it is difficult for those preventing and investigating TF to implement FATF recommendations as intended, because they cannot target their activities. It was clear in this study that some MS have a well-researched policy but others do not. The absence of clearly

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defined risks, policy objectives, ways and means simply leaves policy makers with responsibility for an insufficiently defined and understood space with no rational basis for defining and ordering activities. They must rely on luck, experience or strategies such as simple targeting, asking colleagues in other agencies and countries or unstructured dialogue with target sectors.

3.2.7 Implications for EU Action

Identifying the structural obstacles to compliance with FATF AML and CFT standards is useful because it provides the EU with cues for targeting its actions and measuring their success. Unless action is targeted at the above obstacles it will be hard to improve MS compliance with 9SR. However, it also raises questions about the overall effectiveness of the Special Recommendations with respect to CFT and CT activity.

3.3 Effectiveness

3.3.1 Limitations on overall Effectiveness

The 9SR were designed to serve a purpose and so the question as to how the 9SR and FATF40R contribute to that purpose - combating terrorist financing - is a relevant one. For variety of reasons the question is more easily put than answered:

- The key success factors for CT and CFT have not been identified. As indicated above, EU policy regarding terrorism is based on an analysis of current and potential terrorist problems based on information obtained at second hand. This makes it difficult for policy to contain specific and realistic objectives as to how ways, means, powers and resources are to be directed. It also means that whilst processes can be monitored neither success nor failure can be identified with any useful degree of precision or attributed to specific action.
- The preventative effect of the recommendations can hardly be measured. Whilst the non-use of financial and other market systems for financing of terrorism can be established, whether it is as a result of the recommendations remains very difficult to prove.
- A “contribution” is a vague term, which does not indicate immediately and unmistakably the quality or quantity of value added in achieving a policy objective. It could cover making a small advance or a decisive one.
- Data for indicators of possible effectiveness of the 9SR are not available yet. EU regulations implementing some SRs are not yet in force, or only by some MS, whilst others have been applied only recently and implementation varies from country to country.
- Part of the scarce information on effectiveness is not openly available.

3.3.2 General expert Opinion on Adequacy of Measures

What are available, however, are the expert opinions of policymakers, specialized prosecutors and law enforcement professionals, customs, FIUs, regulators and representatives of the regulated sectors interviewed in this study. Their general opinion on the FATF40R and 9SR is unanimous: They form a comprehensive set of recommendations. No new recommendations are needed and hardly one recommendation can be done without.

According to the experts the FATF40R and 9SR recommendations contribute to the fight against TF because they have the potential to:

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- Increase the transparency of the financial system
- Increase the chances to identify originators and beneficiaries of unusual transactions.
- Help connect identified terrorists and suspects with other networks
- Bring powers of the criminal justice system into play
- Introduce sanctions for TF offences.

However, the experts also pointed out that the FATF system is like an “engine”. Whilst FININT may be the “fuel”, it is part of a wider combustion or intelligence system. The spark that makes it work comes from non-FININT processes, e.g. phone intercepts or HUMINT, which allows drilling down using a name or a transaction to produce more leads and so continue the cycle. This is a crucial high-level issue to which we return in Section 4. First we examine the effectiveness of individual special recommendations

3.4 Effectiveness of Individual Recommendations

3.4.1 SR I & SR II - Ratification and Implementation

There is no definition of implementation. With regard to the UN12ATCP some guides say it can be met by mere act of ratification. The FATF talks of implementing recommendations “fully and properly” but gives no definition. In this study we have taken implementation to mean the legal and institutional measures that are necessary to give an EU regulation effect in a MS.

Criminalization of TF as a separate crime brings the legal investigative powers and instruments of criminal law into play in the TF field. This is generally considered to be an advantage because of the concomitant ability to make arrests, seize evidence and assets and bring prosecutions based on specific activities. However, some MS – those that traditionally regulate the principle - argue that defining terrorist and TF offences may lessen effectiveness, e.g. where there is a general offence of violence against people or damage to property. It can be harder to prove terrorism as opposed to the lesser charge and even where strong cases can be brought, juries can be reluctant to convict on a charge of terrorism because of the stiffer sentences and still feel under political and public pressure to do so.

A further problem lies in the definition of terrorism. A number of MS have been criticized in FATF reports for not criminalizing individual terrorists and pairs of terrorists because they have followed the EC Framework Decision definition of terrorism, which has the effect of criminalizing a person who directs or participate in a terrorist group but not a single or pair of individuals who commit acts defined as terrorist offences in the same Decision. Art. 2 (1) of the Framework Decision also appears to preclude the designation as terrorists of larger groups who commit spontaneous acts, which would be terrorist acts had they been planned over a longer period of time. This is at variance with the FATF requirement that individuals be capable of being charged with terrorism, to cover cases like the UNA Bomber in USA. A number of MS claim that their existing laws and sanctions were / are sufficient to cope with individuals who commit terrorist-type offences, and that creating additional lesser charges of TF for such persons would be redundant.

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In practice however, criminalization has made little visible contribution to the fight against TF until now. There are only a few cases of prosecutions or convictions for TF as a separate crime⁸. The higher compliance with SR II on criminalisation terrorist financing puts the lower compliance with SR I (mainly due to slow procedures) in a somewhat better perspective as SR I also *implies* the criminalisation of TF.

3.4.2 SR III – Designation and Freezing

Freezing is to a certain extent an effective way to limit the financial resources of suspicious organizations and individuals. Its limits lie in the ease with which the formal system for the collection, movement, storage, conversion and application of assets can be circumvented. Where terrorist networks have inbuilt redundancy, other organizations or individuals can take over the financial activities of a person or organization whose assets have been frozen

Slow procedures are also a reason for low effectiveness of SR III and there is a feedback into the effectiveness of SR II by weakening the wider sanctions regime intended to prevent and punish TF. A strong aspect of freezing is the signal it gives to the organization and the financial sector and, when publicized, to the general public.

An important element of FATF SR III is that it requires terrorist funds to be frozen "immediately and without delay". It is to all intents and purposes impossible to do this if a MS does not have its own national asset freezing arrangements. If a MS relies *exclusively* on the EU Clearing House (Common Position 2001/931/CFSP) and the UN regime for the main terrorist groups then:

- It can never submit names itself because it has no proactive targeting arrangements.
- It faces considerable delay in designations being made
- It cannot take freezing action if another MS vetoes a proposal for designation submitted to the Clearing House
- Assets of 'internal' citizens are not frozen at all.

The Framework Decision on mutual recognition of orders freezing property or evidence of July 2003 (2003/577/JHA) is designed to facilitate and accelerate the execution of freezing orders between MS and requires competent judicial authorities of MS to deal directly with one another. However, its use may be problematic in countries which rely primarily on EU freezing mechanisms.

MS see EU mechanisms as important but want them to be underpinned by strong national capacity to identify and cut-off funds more quickly than the EU system allows. At the same time they want better safeguards. The absence of clear review procedures and, in the case of 'internal' citizens, the absence of the possibility to appeal against the EU listing, in combination with uncertainty about the exact grounds for listing, has led some to question the legitimacy of this instrument in the light of human right principles.

3.4.3 SR IV - Suspicious Transactions

Allowing for the fact that some parts of the financial sector and some DNFPBs are more knowledgeable about the SAR regime than others, the low level of compliance with SR IV in MS is still a concern, as the effective identification and processing of suspicious activity

⁸ NB. Not all countries have an adequate registration of court proceedings

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reports is the main instrument for the further elaboration of intelligence. Where compliance is low, the effectiveness of the system is clearly at issue. Moreover, we found that the number of suspicious transactions specifically for TF varies across MS, but is generally very limited, if present at all. It is only partly explained by e.g. differences in exemptions enjoyed by lawyers under client privilege in various MS. We develop this point in Section 4.

MS offer various reasons.

- It can be difficult to label a suspicion as “terrorist”.
- Terrorist organizations are quick learners. They have every opportunity for minimizing their use of the financial system, and leaving minimal or no footprints, e.g. dealing through supporters’ bank accounts, dealing below the €15, 000 threshold, mounting operations with a cycle time that is shorter than investigation cycle times.
- Terrorists have learned how to mount high impact terrorist operations with low resources.

A major problem in the search for terrorist organizations is the importance of small indicators in all fields, including financial transactions. The reporting thresholds for cash couriers and suspicious transactions are a problem here, as indicators below these amounts tend to be ignored and do not enter FIU or police databases. They cannot therefore be seen by analysts.

A further “complaint” from public and private sector respondents was that very few general clues for TF activity exist. A single financial transaction that raises suspicion could relate to anything. So the effectiveness of the reporting system depends heavily on the ingenuity of the analyst and on the other data he has available. The specific TF experience and quality of TF training of the analyst is critical. Thus where a well-directed and well-staffed FIU does not exist, the submission and collection of what TF SARs there are has little point.

The move towards risk-based approaches has helped to reduce divergences over which institutional form of FIU is best suited to CFT activity. This is because risk based approaches increase the ratio of suspicious to unusual transactions contained in SARs. Suspicion thresholds are thus less of an issue. The restructured FIU of The Netherlands is a hybrid police/administrative unit, which has characteristics of both forms. The basic point remains however, that whatever the form of FIU, it has to be able to obtain information (including from security services), have a strong analytical capacity and otherwise be adequately resourced and empowered to support the national prosecution service.

Without data there can be no analysis and thus the ability to obtain and store data from a wide range of sources with which to operate on TF data is critical. As stressed in this report, TF data need other data to establish lead intelligence and the other data has to be held securely and with strict conditions on its use. This is to safeguard individuals and, by extension, to encourage trust in the system and access to a wide range of data. Access to data in principle can be obtained by legislation, voluntary or commercial agreement. Use has to be strictly controlled by the NPS to ensure that opportunities for abuse are kept at the absolute minimum. This approach is sometimes called the Hour Glass model as large amounts of data are accessible but little is allowed out at any one time.

Suspicious activity can be reported on the basis of objective or subjective criteria. Objective systems have the advantage that FIUs receive large volume of data, which they can analyze, and there is (or is not!) an objective criterion, which can be inspected at the regulated entity.

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The subjective approach has the advantage of a smaller number of SARs and subsequently a greater number of hits and the use of the expertise and experience of regulated entities to decide on SARs. The advantage of the subjective systems can be realized only when there is enough trust in the financial institutions and enough expertise on ML and TF to carry out the first risk analysis.

Again we noticed that countries or sectors with limited capacity prefer a rule-based approach. Risk based approaches are beneficial to those with the ability to identify and manage risk and so reduce costs – basically large players in countries with well developed financial and professional sectors. But they are too complex for less advanced actors to develop themselves and costly to buy in. A substantial amount of investment needs to be in increasing the capacity of target groups to run risk-based systems properly. Otherwise the mountain of defensive SARs will grow further and valid suspicions risk going unreported.

3.4.4 SRV - Cooperation between Member States

Cooperation is the key word in a world as institutionally complex as the world of CT and CFT. Cooperation is a pre-condition for any attempt of effectiveness. Here a number of problems have to be faced.

Within MS cooperation in the CT and the CFT field on the political and policy level is present in a number of countries, but insufficient or totally lacking in many others. In some instances there are problems deciding on a common policy as well as setting guidelines for the cooperation between ministries and executing institutions. Where this is done the number of institutions active in the field of TF can still be too large and need to be reduced to be effective. This exacerbates another common barrier to cooperation - institutions operating in the TF field often do not want to, if they want, know how to cooperate.

On the EU level practical cooperation between MS at EU level in the field of TF is realized partially in informal ways using third parties. The Committee on the Prevention of Money Laundering and Terrorist Financing set up under Article 41 of the Directive 2005/60/EC provides a formal channel for the MS to discuss issues in relation to TF. FATF and (to a lesser extent) MONEYVAL discuss policy issues and technical cooperation, as well as being used for mutual evaluation. The Egmont Group is used for exchange of information on financial transactions and the FIU.NET offers a wider scope for obtaining, sharing and using intelligence on a wider basis, especially to FIUs with less resources or less resources in a particular area. However, FIU.NET still has to attain the breadth and depth of take-up originally foreseen, which is largely dependent on meeting its infrastructure needs (wide ranging databases, specialised typologists, trained investigators) and thus the resources at its disposal.

Eurojust and Europol, which might be considered as being in a position to further cooperation, are not used extensively in this role partly for the general reason that they are still relatively new institutions, and partly because of their functional limitations. Eurojust is not mandated, nor has it the necessary powers, to coordinate or manage investigations and prosecutions. However, MS do have an obligation to provide it with specified information and it has influence and formal production instruments at its disposal to this end. Europol has similar restrictions, and though it does store and analyse information on CT, CFT and AML issues internal evaluations have reportedly showed up shortcomings in this area. In the Section 5 we set out a framework which addresses these problems.

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In the EU's Third Pillar, the chances for cooperation are limited because of the sovereignty of MS in law enforcement. Crucially, CT and CFT investigations are basically carried out at MS or joint small scale MS level. Whilst both the PCWG (for its facilitation of informal proactive TF links in the margins) and the Joint Investigation Team system were favourably viewed by MS, sometimes very favourably, others saw their value more as being in the secondary opportunities to develop reactive bilateral dialogues. There is no fully empowered coordination mechanism for criminal intelligence on EU level. The limitations attached to the Third Pillar are illustrated in the legislative initiative of Sweden regarding the exchange of information and intelligence between law enforcement authorities of the Member States, in particular regarding serious offences including terrorist acts. It identifies in its preamble the inefficiencies created by these issues:

“Currently, effective and expeditious exchange of information and intelligence between law enforcement authorities is seriously hampered by formal procedures, administrative structures and legal obstacles laid down in Member States’ legislation; such a state of affairs is unacceptable to the citizens of the European Union which call for greater security and more efficient law enforcement while protecting human rights.”

MS can decide to investigate alone, or on bilateral or multilateral information exchange and coordination sometimes at an agency-to-agency, not MS, level. In the latter two cases information exchange or coordination can be facilitated by the systems of liaison officers at Europol and within various MS. But Europol deals mainly in data on finished cases, not running ones. Its data reliability and value can be uncertain, it is uncoded and there are language difficulties. Evaluations of CT and CFT projects it has undertaken are reported to be unencouraging. Interpol is another informal channel of information exchange but it has similar problems.

Public prosecutors have started to coordinate on a voluntary basis via Eurojust including in the field of TF and we were impressed by the range of support for this process.

3.4.5 SRVI - Alternative Remittance Systems

Interviewees confirmed that informal banking is a popular practice mainly amongst migrants and minorities and especially where their remittances play an essential role in the local and national economy of their home countries (usually outside the EU). Very often people prefer ARS to formal systems because of delivery problems in the country of destination, but they are also encouraged to do so by the high cost and slowness of formal channels and social reasons.

The effectiveness of the regulation is recognized to be dependent on the capacity of registered alternative remittance services to detect suspicious activity and make SARs, as well as on the capacity of regulated businesses and the criminal justice system to detect and punish illegal channels. On the basis of our feedback, both have to be rated as very low. Where informal systems have been licensed, e.g. by coming under FX Bureaux schemes, they often are too small to have sophisticated STR spotting capacity. There is also the problem that this sector often relies on agents to collect and pay funds, whereby such agents often have very informal arrangements. They may not be much more than specially trained messengers. They may also be (extended) family members and friends, or people standing in for them which makes registration of agents not such a simple process as it might appear.

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This increases the workload on regulators who undertake background checks, which in any case can be difficult to do on people who have commonly occurring names and come from countries with poor criminal records systems. Unravelling the deeply disguised use of formal channels to operate ARS is complex. Many countries have opted for licensing route rather than the registration route despite FATF's provision for lighter touch regimes. A probable reason is that even under a registration scheme ARS still need to be monitored for compliance and the bodies best equipped to do this are usually regulators. However, the burden of licensing again has the effect of forcing the less capable (but otherwise not necessarily criminal) operators underground.

Thus the incentive to use ARS, the clever use of formal channels and the low detection probability for cross border cash movements makes the theoretical effectiveness of this measure low, and the experience of respondents in practice bears out this prediction. The easiest part of the system is establishing penalties. However they are rarely meted out, as there are relatively few successful prosecutions for such offences, especially where there are no associated charges (e.g. money laundering)

3.4.6 SRVII - Wire Transfers

Wire transfer is an area where respondents thought regulations would be effective in meeting their objective, in this case to make information immediately available to investigators, FIU and beneficiary institutions. On analysis, it is possible to highlight certain factors, which contribute to effectiveness in this area and whose absence in other areas can cause ineffectiveness.

First, the question of wire transfers was subject to scrutiny at all levels of hierarchy and detail because wire transfers are the lifeblood of the economy. Any failure in this area would have potentially catastrophic impact on payments systems, competition and by extension stability of financial sector in very short order. Regulatory failures in areas covered by other SRs would have a slower, less visible effect on the underlying mechanisms even though the consequences might ultimately prove very serious.

Second, WTs involve banks and other financial institutions, which now have substantial experience of AML procedures, as well as better industry organizations and established consultation procedures. To the quality of process and content of regulation can be added the quality of the goal. The recommendation involves making information immediately available, not creating a system to make information available, as other recommendations do. The effectiveness of this recommendation is high as it increases the traceability of transactions and the speed of traceability. Lastly, in some countries this information is already or easily collectable and attachable, so the marginal effort is low.

Some weak spots were highlighted. Whilst the system can ensure complete and accurate information, it cannot guarantee meaningful data and a number of MS are concerned that, whilst empty or randomly filled origination fields can be spotted by automatic transfer systems, names such as Donald Duck or Mickey Mouse cannot and will be passed. Moreover, where different banks are using the same underlying data to check names, it is possible that substantially the same checks are performed at the time of the initial payment by the originating bank, by any intermediary bank and finally the beneficiary bank. Another problem area is monitoring. With banks processing millions of transactions a day and spending substantial sums on compliance systems there are issues as to how supervision should be

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exercised and how sanctions should be framed. However, these issues do not have a serious impact.

3.4.7 SRVIII - Non Profit Organizations

Depending on which definition is used there are millions or tens of millions of NPOs in the EU ranging from local self help groups and sports clubs with *de minimis* budgets to famous universities and multi-national NPOs run on commercial lines. Currently there is no EU wide assessment of the risk they pose in the TF context. Such an assessment is now being attempted but it is hampered by the relatively limited amount of information in the public domain and inability of law enforcement to add to the data set by discussing current cases other than in general terms. Some data is available (though again in generalized form) from FATF and Egmont Group by typologies and risk indicators. What wider information there is on abuse of NPOs is gathered by other intelligence means and remains classified.

The ongoing absence of a substantial and accepted corpus of empirical evidence of misuse impedes the dialogue with the third sector that the EC and some MS seek in order to develop effective policy. It also reinforces the view in many MS that, whilst present in a very limited number of cases, TF abuse of NPOs is not a prime concern, especially where NPOs are using regulated channels for their day-to-day activities. Even though the EC appears to have toned down its approach, a number of MS voiced the fear that the EU will continue to seek a robust line at the insistence of a minority of MS. This is rejected either as a matter of principle or on the basis that few SARs are made specifically for TF via NPOs, except in the high-risk high incentive group. Countries with low reporting levels say that they are confident that low reporting results from an absence of threats, not an absence of systems.

Another question is whether introducing specialist TF regimes for NPOs would be any more effective than modifying existing regimes. Of the three main objectives of SRVIII, posing as legitimate entity is seen as a form of conspiracy, whilst the use of NPOs as conduits, and for the purposes of diversion, are seen as forms of money laundering and fraud. Thus, strengthening anti fraud measures and measures to increase proportional financial oversight and reporting, whilst simultaneously including the provision of aggravated offences where terrorism is involved, was considered by many the more effective approach.

A further issue is that an effective control environment for NPOs would require a joined up system of registration, accreditation, monitoring and fiscal controls. Making this system effective on a pan-European level at the speed required for post attack investigations (let alone interdiction of imminent threats) would require the type of centralized co-operation between agencies nationally and internationally that, as explained in Section 4 currently does not exist. Nearly all MS are missing elements of such a system, and time and expense will be needed to put them in place, which again raises resources issue with respect to both individual NPOs and national level cooperation mechanisms. Moreover, underlying the whole debate is the fact that, due to cultural, legal and other contextual factors, some MS simply do not see an "effective control system" as a system that includes registration and tighter monitoring.

Finally, to be effective an NPO registration and reporting system needs to produce data that gives accurate leads to investigators. A number of interviewees highlighted that such a system might miss vital signs because of the way reporting thresholds are set, as with SARs and Cash Couriers. Conversely, it might also prejudice the operations of NPOs trying to reduce the influence of militant groups in sensitive areas merely because they were working in these sensitive areas. Militant groups would in any case likely to be subject to other official scrutiny

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by those able to obtain superior information via existing powers or covert means. A robust anti fraud (including anti tax fraud) regime would be of more general value to the NPO sector and produce better data than a TF oriented regime toned down for political reasons. The First Pillar has a role to play here by influencing tax regimes, whilst the Third Pillar can contribute under its economic and organised crime mandate.

3.4.8 SRIX - Cash Couriers

As the EU Regulation only comes into force in June 2007, not all countries regulate the import and export of cash money now and the effectiveness of the measure cannot be established yet. Once the system is in place it will be one of an increasing number of tasks being given to customs authorities and will have to compete with investigations for e.g. drugs, human trafficking, VAT fraud and CBRN threats.

Taken into account that it is legal to carry cash as such, cash controls at internal borders having been restricted by the EC Treaty, and cash being transported very easily, the effectiveness cannot be rated as high. It is rather easy to enter EU territory avoiding the official points of entry where other controls may be made, especially as a large part of the coastlines of MS are not very well patrolled. The chance of detection at busy ports of entry and exit are small, though expensive artificial technology and less expensive dog units have a positive impact on rates of detection and deterrence.

Also, the €10,000 threshold for import and export affects neither terrorism funded within the EU, nor the low cost terrorism that has developed now within EU countries. The potential for SRIX to affect international terrorist network or organizations relates to those that have higher costs.

The underlying problem is reducing the volume of cash in circulation, especially high denomination notes, when many MS still have sizeable cash economies. Tax avoidance is the major issue here, not TF, and MS have a big incentive to encourage and compel use of banking channels. This can be done indirectly and we noted the sensitivity of professional advisers to sanctions is making them take a harder line with clients on questionable invoicing and tax reduction ploys. With fewer reasonable grounds to hold and transport large cash amounts, the discovery of cash in size is more of a ground for suspicion.

3.5. Other Necessary Structural Elements

As the FATF Evaluation Methodology points out⁹, an effective AML: CFT environment requires certain other structural elements to be in place that are not covered by AML/CFT criteria. They include transparency and good governance, compliance culture, anti-corruption initiatives, reasonably (*sic*) efficient courts, high professional ethics in the criminal justice system and professions.

It was clear in our study that in some countries such elements are only gradually coming about. In a number of MS, application of the principles of transparency and good governance has a short history. Compliance cultures vary from country to country and take a long time to develop. Corruption levels vary widely across the EU. 13 of the top 25 corruption-free states are EU MS, but the other 12 are spread over places 26 – 70, by which point the integrity score

⁹ FATF Methodology for Assessing Compliance with the FATF 40 Recommendations and 9 Special Recommendations June 2006 (<http://www.fatf-gafi.org/dataoecd/45/15/34864111.pdf>)

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is one third of that of the leaders. In countries where large amounts of cash were in circulation, interviewees stated that professional integrity in DNFPBs and the criminal justice system was a problem. This ranged from colluding in false invoicing to interference with due process.

A number of states in the MS have the weakest link in the criminal justice system, especially where there are prosecutors and judges who do not have the specialist training to hear complex TF cases. Once problems with FIUs have been remedied, this soon becomes a critical and very difficult bottleneck. Despite the PHARE programme it is still a big problem in new member states.

Finally it must not be overlooked that TF is a reaction to a sudden catastrophic event that has led to the redeployment of investigators from other fields, including important aspects of AML work. This study found evidence of new threats crowding out CFT work, notably migration in Southern European MS. CFT work involves the application of scarce criminal justice resources, which are liable to be reapplied elsewhere in the case of a new threat from a different source (e.g. a flu pandemic, critical infrastructure attack). There is no guarantee that CFT activity will remain the priority it is now, even though the threat may remain constant. In this context we noted increasing concern about the resurgence of OC, which has been out of the spotlight whilst attention is focused on terrorism, despite the EU's call to look at links between CT and OC.

4 ANALYSIS – IMPLICATIONS FOR THE EU'S CFT STRATEGY

4.1 The Intelligence Based Approach

TF SARs that are not defensive reports in fact form a very small fraction of total MS SARs. Moreover, whilst MS have had numerous high profile successes in arresting terrorists, few attribute such success to TF SARs, or indeed to EU support for the 9SR. Success in CT comes mostly from two processes into which the EU has, respectively, little and no insight - intelligence and special operations. Only intelligence issues are analysed in this report.

4.1.1 Weakness of EU Intelligence Exchange and the "Elephant in the Room"

Intelligence sharing among MS on CT and CFT takes place along two axes. The first axis consists of institutional actors, namely law enforcement, internal security, foreign intelligence and policy makers. The second axis is geographical, namely i) Global, ii) Region and iii) Bilateral (including small-scale multilateral). However one of the bilateral players, the USA is so significant as to represent separate class of interaction.

This is shown diagrammatically in Table 2 (above). The intersections A1 and B1 represent the location of current research and awareness and FATF style processes. However, it is in Boxes C1-4 and for many MS D1-4 that the quality, if not the quantity, of intelligence activity take place. These bilateral relations often predate the 9/11 focus on CFT and outweigh global and regional (i.e. EU) relations. As already mentioned (Section 3) they are not restricted to sharing by intelligence agencies, but also encompass agreements between the respective law enforcement agencies. There is a necessary lack of transparency in such dealings, as bilateral links are more widely framed than TF and often based on wider bilateral political agendas and specific intelligence tasking. CFT intelligence is thus exchanged in an environment driven by other considerations than just TF.

Table 2: Locus of Intelligence Co-operation on CT and CFT

	A. Global	B. Regional (Europe)	C. Bilateral/ Small scale Multi lateral	D. Bilateral with USA
1. Law Enforcement	(Egmont) (Interpol)	FIU.NET PCWG Europol Eurojust	Egmont Interpol	FBI Academies
2. Internal Security		CTG* Club de Berne* *EU Shadow	E.G. Spain, Italy, Greece on Anarchic Terrorism	
3. Foreign Intelligence (including Military and Diplomatic intelligence)	UN	SitCen European Union Military Staff		
4. Policy Makers	FATF	CoE EU (e.g. AML Committee)	British-Irish Intergovernmental Conference	(EU-US)

For many MS the biggest and most significant bilateral relationship is the one with the USA, which is in fact the “Elephant in the Room”. The US has an outreach policy in the CT and CFT arenas, and actively engages MS on CFT policy formulation and implementation. It provides technical assistance in the form of training and equipment and it exchanges data. It is a *de facto* intelligence hub to which most MS are in some way connected. EU arrangements risk being crowded out by these relationships. Moreover, and despite safeguards, MS show reluctance to make available to an EU system data which they do not want to be shared with others. The principle of opening working files to US exchange personnel has previously caused a rift between MS at Europol.

4.1.2 Weakness of Use

In addition to the lack of transparency, a further weakness of bilateral arrangements is that it is hard to capture best practice in the field of intelligence. Two MS may have an apparently close relationship but the model of cooperation may be ineffective. It is in the provision of standardised channels and specification of forms of cooperation that opportunities exist for the EU. In this context, the wider benefits and potential of the FIU.NET do not seem to have been fully communicated or fully appreciated by some MS, some of whom still focus on the marginal cost over Egmont and bilateral links.

A similar issue is weakness of management and use of bilateral information. Because many bilateral relationships have a high personal content, relationships between individuals and teams tend to pull intelligence work in one direction and can thus defeat a higher-level strategic push. As in the law enforcement sector, rivalries between national intelligence agencies are still to be observed even where coordination and tasking mechanisms have been put in place. Often the pull is towards operations and away from the less glamorous and harder but strategically important typology work. TF intelligence analysts are in any case

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liable to be pulled of typologies work onto operations when an incident occurs. There is clearly a role here for the EU in doing such typologies work and/or mandating that it should happen and ensuring its continuity at MS level, developing Europol's activities in this field. SitCen's continuing to build its TF capacity is clearly a prerequisite, but it will also have to work hard at getting political support for access to data that will enable it to work effectively and create a valuable differentiated offering to that of the Elephant. Whilst some MS are satisfied with the range of resources and tasking open to SitCen, others are less so. This is partly explainable by differences between what can be done in theory and what can be done in practice. However, the EU needs to assure itself the capacities it believes to have in place are real and effective. Not having had access to classified material and arrangements, we are unable to comment on this.

4.1.3 Updating Intelligence Based Approach

The EU will have to do more to sell FIU.Net to MS. Egmont has been such a success because it is simply a clearing house, is bilateral and makes no pretensions to oversight. The updated policy needs to give MS incentives to use FIU.Net and show that it will not have a negative impact on the bilateral relationship they enjoy via Egmont.

There is also clearly a wide range in the of quality in public-private cooperation, which ranges from the secondment of intelligence personnel to major banks in some countries to fear and distrust of police authorities (for historical reasons) in others. These are societal issues, which need to be addressed in the wider societal context.

The pivotal role of industry associations at European and national level must be recognised by EU policy and where they do not exist, or are weak, policy must encourage their creation. Properly managed relationships between associations the EU and MS represent the most direct means of achieving welfare for both sectors via higher quality of interaction and economies of scale. There are also cost issues and policy should address how the costs of protecting society are spread equitably.

It should also be noted that the recommendations in Paras 20-24 of the CTF policy are not TF specific but would help to reduce all OC.

4.2 Crime Issues

4.2.1 Money and Assets as generalized Criminal Means

Flows, processes and structures of money and other financial assets have many forms and shapes and vary from global and regional systems to the myriad of small transactions in shops and markets. Terrorist financing hides in this complicated financial world, not in its own discrete area. To cover all possible vectors of risk, measures to fight TF, including EU CFT measures, have expanded to take this universal character into account. Most financial assets are of a general nature. By definition they can be used for a variety of legal and illegal purposes. TF is a subset of financial crime, as is money laundering and dictator funds, and financial crime is a subset of all crime.

As stated in FATF Interpretative Notes, measures needed to fight TF are to a wide extent very similar and sometimes identical to those taken to fighting financial crime more generally. The FATF40R + 9SR contain both generalised recommendations (e.g. SRVI-IX) which cover crime in general and very specific recommendations (e.g. R25) on points of procedure. They

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might well be disaggregated and recast to reflect the level at which they can be complied with and are effective in addressing, respectively, all crime, financial crime and specific forms of financial crime. Clearly the high level (and more politically loaded) recommendations have a wider potential to impact all crime. It is not just national and international financial crime, specifically TF, measures that have to be effectively implemented but also basic underlying national and international criminal investigation systems. There are thus two processes in operation:

- High profile, supposedly TF-specific foreground processes (which aren't in fact TF specific but help in crime in general).
- Less optically spectacular general crime reduction processes, which have a potentially large impact on TF, tax, company and social security legislation in the public sector and accountancy standards in the private sector which increase transparency. Probably the most important processes are antifraud measures in both the public and the private sector.

The latter case also includes certain EU FDs with a connection to TF, where there is a mixed but tentatively positive record of implementation and legislation entering force. The Action Plan¹⁰ as at May 2006 notes c.177 successful implementation outcomes out of a possible 250 (c.70%), with the Decisions on European Arrest Warrant and Joint Investigation Teams nearly universally in force. The Convention on Mutual Assistance in Criminal Matters and the FD on the execution of orders freezing property and evidence are still working their way through MS systems.

The potential of data produced by these general crime reduction measures to increase the effectiveness of the 9SR *qua* CFT measures depends greatly on how they are linked to SARs and other financial information. This requires the comprehensive, selective and smart approaches in the field of CFT to be linked systematically to over-arching criminal and CT intelligence systems. Again, the quality of non-TF specific systems has a critical role in CFT.

The more comprehensive, selective and, above all, smart the approach to terrorism, the greater the chance to detect preparations for terrorist acts, the greater as well the chance that terrorists will have more difficulties in preparing terrorist acts or even refrain from them. There are two reasons for these requirements, namely the nature of terrorism and the characteristics of financial assets, which emphasize the crucial role of "smartness".

4.2.2 Terrorism and the Need for "Smart" Intelligence Handling

As highlighted above, the EU's CT process was given added impetus by the 2001 - 2005 AQ attacks in the US, Spain, UK and elsewhere. The distinctive characteristics of Al Qa'eda terrorism require response initiatives both on a global and a regional (i.e. EU) level. These are the network of networks ("franchise") structure, the Jihad against America and its Allies, the mass casualty terrorist attacks and the no-warning suicide attacks¹. Moreover, terrorist organisations have secrecy as a common trait. A great number of strategies and tactics to remain unnoticed are known, taught and being used.

This trait and this intention to remain hidden make it very difficult to identify terrorist groups, especially small self-appointed ones. Many respondents in this study stressed that it is the smart interpretation of signals from many sources combined with the continued search for

¹⁰ 95589/06 ADD 1

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further corroboration that shapes the effectiveness of efforts, and so identifies threats and those who threaten. Without smartness, comprehensiveness is wasted effort.

Successful early detection, prevention, and investigation of terrorism are dependent on the smart combination of signals and pieces of evidence from many different sources. It is the art of sourcing and combining data and finding meaningful relationships and clues leading to individuals or groups that adds value to CFT (and by extension CT) measures. In broad terms, the complexity of the terrorist phenomenon and terrorist financing, as well as the variety of strategies and tactics used by terrorists and terrorist organisations to prevent detection and to eradicate traces require an approach to terrorism that is:

- *Comprehensive:* Relevant signals can come from a great variety of activities and sources and the approach must be capable of covering a wide variety of sources that may generate material signals in the detection of potential terrorist acts or actors. *This is the central theory behind the FATF approach.*
- *Selective:* In order to focus activities in this potential ocean of data and to reduce the workload, data must be filtered. The range of methods includes common sense and the healthy distrust/attentiveness of people, the introduction of risk based systems and comprehensive bulk data analysis techniques. Data selection can also be driven by specific suspicions. *This is also inherent in the FATF approach.*
- *Smart:* Making sense of pieces of relevant selected information from different sources involves combining various signals and to identify possible meanings and for clues as well as further information needed to check and to double check suspicions as well as to establish and test hypotheses. *This vital ingredient is implicit in, but not created by, the FATF approach.*

Almost all experts asked therefore for some form of “super clue”, approach or “angle” to help analyze the financial data and combined databases. Data search and data mining are no use if no clever and workable clues can be introduced to guide search processes. There is a strong inference that the data system is a real treasure chest but analysts have not found the key.

4.2.3 Updating Policy on Asset Freezing

Revisions to CFT policy will have to take into account that the UN and EU lists have failed to forestall the Madrid and London attacks and contributed little to pre-emptive action by MS. With designations often ex post, the value of listing lies in its strong symbolism. However as the recent action by the Bank of England shows, quick administrative action by MS also sends a powerful message and has a more immediate disruptive effect. CFT policy should make explicit the importance of national immediate freezing mechanisms.

Improving the identifying information on designation requires due diligence by trained FINs and intelligence analysts. This is another reason for policy to stress the need for appropriate training. Policy should also take into account that national asset recovery initiatives can have a long lead-time before they begin to produce results and need proper resources in this period.

Revisions should focus on making the list easier to use by providing more legal protection, guidance and, where appropriate, cost recovery out of seized funds for those who apply it. Designation errors are recruiting sergeants for terrorist groups and their remedy needs a sensitive approach.

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4.2.4 Updating Policy on Traceability and Transparency

Much of the policy relating to tracing and transparency is again “all crime”, or at least OC, policy. Making the formal banking system more attractive than ARS and encouraging cash into the formal banking sector helps to reduce crime across the board, as do measures to improve coordination and support for customs authorities at ports of control. Improved training on asset tracing supports proceeds of crime investigations across the board. Wider training of FINS also helps with spotting suspicious transactions and suspicious companies or NPOs.

In this context, interest in front organisations, NPOs and individuals in the policy has been cast too widely and needs to be reined in. The proposed threshold for getting behind the corporate veil, a top priority across all crime, has been made too lax at 25%, whilst NPOs have been faced with a regime potentially more onerous than for similar sized companies in at least some MS. The evidence to support a properly differentiated policy towards NPOs is still awaited.

Policy updates need to recognise the role tax authorities have to (and in some MS do) play in the supervision of NPOs. The involvement of tax authorities provides both a base line control where further regulation is not thought necessary and a basis on which to build more detailed regimes using other approaches. Both companies and NPOs are more often victims than perpetrators of fraud, and the fraud they are most likely to commit, if any, is tax fraud. There may be opportunities to combine training for FINs based in tax authorities with educating NPOs on how to avoid fraud. There is also a need for policy to promote the approximation of transparency and disclosure standards for companies and NPOs according to size and risk profile.

4.2.5 Updating Foreign Dimension

The CFT policy should stress the EU’s active participation in the FATF process and its commitment to sustainable streamlined processes. It should commit the EU to close links to the CoE in this area. External work on TF should reflect a shift in emphasis to OC more generally and stress that technical assistance is not a one-way process, but an opportunity to learn.

4.3. EC's Possibilities and Limitations

On the level of the European Union two questions are relevant with regard to the required comprehensiveness, the selectivity and the intelligent quality of the approach for terrorist financing:

- a. To what extent can and do EU TF institutional arrangements meet the three data requirements in 4.2.2?
- b. To what extent can and do the EU’s institutional arrangements (especially in connection with the FATF40R and 9SR) stimulate such approaches at the level of the MS?

4.3.1. EC's institutional Arrangements

The 9SR cover a number of aspects of finance and they cut through all three institutional arrangements of the EU. Appendix 5 illustrates the EC institutional arrangements and capacity to organize a comprehensive approach for an anti TF strategy as set out in the 9SR.

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Only the First Pillar has the legal power to put a comprehensive approach into practice, especially in the area of Customs and to a certain extent in the financial sector. The Second and even more the Third Pillar have very limited powers to organise a comprehensive approach.

In the Impact Assessment prepared for the Proposal for a Council Framework Decision on the exchange of information under the principle of availability, a number of current problems were highlighted, including:

- Lack of trust between law enforcement agencies
- Technological obstacles
- Legal and administrative constraints
- Organisational idiosyncrasies
- Different regimes of confidentiality and classification of information

In the case of Joint Investigation Teams, initial operations within the framework of EU police cooperation have not always led to positive outcomes, even when only a very limited number of countries participated. Causes cited were the legal limitations in some of the co-operating countries, over complex co-operation structures, institutional competition, wrong composition of the steering group, as well as distrust and loss of interest from some participantsⁱⁱ

There is limited capacity to organise a comprehensive approach within the Third Pillar because of the need for the consent of all MS. With mandates, capabilities and capacities allocated across numerous EU bodies, the need to co-ordinate activity clearly reaches across all three Pillars, but the central issue at EU level is clearly that a comprehensive approach on the EC level would require co-ordination amongst the three Pillars, to which there are practical and political obstacles.

4.3.2 Coming to Terms with legal and institutional Limitations

The limited regulatory power in the Third Pillar does not allow for fast and comprehensive lawmaking. Formalizing arrangements in the field of CT and CFT in that Pillar often requires time and compromises. While the 9SR were agreed upon very quickly, the EU regulations following from them are necessarily progressing much slower, sometimes for technical reasons, but also because of differences in situations and priorities between MS. SRVI-IX are illustrative of this. However, the long-term value of general organised crime measures, not just for TF but future unknown forms of financial crime, will be very high.

A further potential complication is that EU standards in the field of TF must be set at a level that is consistent with other obligations MS find themselves under in the same policy area. Thus EU activity must help MS fulfil their duties to UN and FATF/MONEYVAL. Again background general measures help in this respect.

Thus the relatively autonomous position of MS in the Second and Third pillars put limits to the EC's ambition to reach common goals. Even in the preparation for the implementation of the regulation for cash couriers, a First Pillar issue, no operational co-ordination by the EC is apparent as yet. Each country is preparing its own system of inspection and risk analysis.

5 CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

Para. 9 of the EU CFT strategy talks about making reporting an effective instrument. But effective for what? Certainly not the pre-emption of fast moving and rapidly evolving threats, because as we have seen, they are prevented by other means. The problem is that the FATF reporting regime, especially the 9SR regime, promoted by the EU is actually an OC regime, not a specific TF regime. This because it is based on the model adopted by the USA in reaction to the 9/11 attacks: The US saw similarities between AQ operations and OC in the USA and adapted domestic instruments developed in the fight against OC.

However, in the absence of a fuller analysis, it is not certain that the threat in the US can be compared to the threat in the EU, whose domestic terrorist groups in particular do not appear to fit into the same pattern. Where the SR9 are weak as a CFT measure is where they are not specific to TF, at least in the EU context. Therefore, they do not produce lead data, but need the spark of “clever”¹¹ intelligence based on other processes to start the CFT engine.

Where suspicious activity reporting is priceless is in completing evidence and the FATF40R and 9SR are invaluable in establishing long-term structures for investigating all organised crime. This provides a good fit with the EU, the nature of which makes it best suited to long-term high-level structural initiatives. These high level initiatives not only help against TF but a wider range of other financial and non-financial crime.

Review of the CFT policy therefore needs to reflect not only the issues raised in Section 4. It needs to be reframed in the context of EU OC reduction policy in general. As almost all the CFT measures the EU has taken to date are in fact valuable crime or financial crime measures, there is not loss.

To reframe the CFT policy however, the EU first needs to undertake a full threat analysis from its own perspective and develop a response to address TF and terrorism specifically as they occur across the EU. This should focus on threat elements that are common to all MS, and would require all MS to ensure their national threat assessments are adequate and up-to-date. The EU also needs to satisfy itself that its arrangements for preparing its own periodic and situational threat assessments provide sufficient and necessary data as and when needed.

We set out below a structure to promote horizontal coordination. Such a structure would meet calls to help the CTC and Eurojust be more effective and develop the role of Europol, FIU.NET and SitCen as mechanisms for “clever” analysis. It is a structure that creates a basis for enhanced coordination and, where agreed by MS, intervention that can be replicated to meet other threats and thus supports the creation of an integrated OC reduction framework. It also meets the criteria of the CT Strategy by strengthening first and foremost national capabilities, facilitating European cooperation and developing collective capability. These enable a crosscutting contribution to the PURSUE strand.

¹¹ Many respondents highlighted the poverty of traditional or narrow approaches to financial intelligence analysis in understanding and solving TF threats and the progress made using non-standard analytical approaches and data combinations. A term often used for this approach was the “clever” use of intelligence.

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The elements of such a system exist in most MS. However, its realisation is a matter for discussion between MS, given the likely cost benefits. The balance opinion encountered in MS was that there was potential for increased horizontal cooperation where (quite understandably) it did not prejudice effective direct links. Such an increase might be available from efficiency gains in current MS and EU cooperation arrangements. However, once they have been achieved, potential marginal efficiencies from broadening or deepening the mandate of key EU cooperation mechanisms increase.

We also set out a list of individual recommendations, which to the extent they are not integrated into this Model, should be implemented on a standalone basis.

5.2 An Extendable Model for CFT Coordination and Exchange

We suggest the following CFT Model, which could serve, *mutatis mutandis*, for countering any other form of crime (especially serious financial crime).

1. The EU would obtain an in depth review of the terrorist threats at EU level and the financial vulnerabilities of those who threaten it based on MS updated national assessments.
2. The review could be executed by a suitably vetted team under the supervision of national experts in the form of a College attached to SitCen.
3. The Counter Terrorism Coordinator would be given responsibility for ensuring horizontal cooperation between MS. He should be advised by the College on a regular basis, and in emergencies. It would be for MS to decide whether the CTC should have powers to compel cooperation and if so the limits to such powers, whilst still allowing the CTC to be fully effective in the allotted role.
4. Eurojust would form the executive arm of the enhanced CTC function. Prosecutors in Eurojust would pass on, to a dedicated EU CT prosecutor in their NPS, requests for FININT and/or the service of evidence and arrest warrants. Data would be sent to Europol or Sitcen as requested by the CTC for storage and further analysis (if needed). Again it is for MS to decide if more powers need to be given to Eurojust than it already possesses.
5. Each MS would have a Clearing House. The Clearing House would have senior representatives and staff from all relevant national agencies. The senior representatives would shape national CT policy and elect a member to the College. The staff would produce regular threat assessments. The Clearing House could be an existing body or new one; it might be wholly or in part a “virtual organisation” i.e. based on, and operating through, the resources of a range of national institutions.
6. All requests to obtain data from FIUs in other MS would pass through the Clearing House and be approved by the NPS. FIU.NET services might be recast to this end.
7. FIUs would liaise closely with the private sector. They would receive SARs from the public, private and the “third” (NPO) sector.
8. FIUs would conduct their own data analysis, and develop special teams for the “clever” analysis of data held in the FIU and other agencies. They may request data via Egmont, FIU.NET and, where necessary, the CTC.
9. The CTC and Eurojust could establish Joint Investigation Teams on an ad hoc basis, of their own initiative or at the request of a MS (subject to the approval of the CTC).

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The above Model would facilitate national and EU level coordination. Point 5 sets out the model for national coordination.

5.3 Standalone Recommendations

The following detailed recommendations could be incorporated into above Model. They are also standalone recommendations.

5.3.1 EU Policy

The EC should focus on long term, all-crime reduction measures and should avoid over-ambition on specifically TF issues. It should coordinate analysis and policy with MS.

The EU should analyse, together with those MS who are most interested, the terrorist threats within the EU and the international threat as it relates to the EU. On the basis of that analysis it should design general EU policy and propose more specific policies for adoption by individual MS. These policies should identify objectives and instruments. The analysis on which they are based should be repeated periodically and policies adjusted appropriately. Specifically a CFT policy should:

- Analyse past incidents and suspected incidents, establish successes and shortcomings, identifying where policies and practices need to be changed.
- Create a learning mechanism based on the experience of countries with a terrorist threat. The learning mechanism can be created principally for EU MS with a terrorist threat. General learning points can be distributed according to need to other MS.
- Create a group of experts from MS to advise the Council of Ministers on international terrorist threats and policies. This group would be consulted on a regular basis and in time of imminent threat or actual attack. It would contribute to the above analyses. It would also prepare a set of responses for use after any terrorist incidents, which demand an immediate political reaction on TF issues at the EU level.

5.3.2 Reduce legislative Lead Times and improve Quality of Rules

The EU should look at ways to shorten the lead-time on crime reduction legislation, and generate fewer, but more compliance-friendly rules, by:

- Developing ways to preserve priorities across presidencies.
- Reducing the production of policy papers and actions plans, and so reduce the volume of policy.
- Conduct preliminary and detailed regulatory impact analysis, as appropriate to the understanding of proportionality when dealing with asymmetric threats.
- Consulting more effectively with target groups and those implementing rules.
- Including *de minimis* provisions for minor transgression to lessen burdens of rules.

5.3.3 Monitoring

The EU should:

- Increase the EU's (Council of Ministers, DG JFS) ability to require MS to implement crime reduction measures.
- Repeat CT peer review process in a way that minimises additional burden on MS but without reliance on self-evaluation (e.g. within the course of the partnership processes mentioned below).

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- Identify a small number of key performance indicators and publish a dashboard of scores.

5.3.4 Partnership Arrangements

Countries with experience in CT and CFT should be encouraged to establish partnership arrangements (“twinning”) with one or more countries who do not, or who have fewer resources. This twinning should be based on existing bilateral relationships. The EU should cooperate with CoE in this process. Partnerships should:

- Develop links at strategic, tactical and operation level.
- Support each other in planning, training and operations, especially by informal exchanges of ideas and experience.
- Report periodically on joint activities to CTC.
- Hold meetings between partnerships to exchange experiences, review common unmet needs at partnership and at EU level and explore ways to meet them.

5.3.5 SAR System

EU should consult with MS and the private sector to:

- Boost role of national and European industry associations in AML/CFT training. *Inter alia* this should aim to achieve economies by spreading best practice and by burden sharing.
- Promote as a priority training in risk-based techniques for second tier FIs and DNFPBs.
- Establish clear rules for feedback and selective (e.g. intra-group) sharing of information.
- Review how to make the PEPs regime easier to administer
- Examine ways to avoid repetition of identical and low yield controls on wire transfers.

5.3.6 FIUs

The EU should:

- Mandate the establishment of specialised units in MS FIUs and in SitCen to develop the “clever” use of data and the generation of special insights with which to analyse FININT.
- Consider grants for under resourced FIUs, especially for training expenses.
- Promote benefits of FIUNET as an enhanced intelligence tool (whilst not undermining the efficiency of Egmont) and consider discounts to encourage take up among low volume users.

5.3.7 Financial Investigation

EU should help to improve financial investigation and analysis by:

- Developing minimum standards for training FINs.
- Promoting training for FINs in financial standards of other MS.
- Enabling greater use of joint training to foster long term links between professionals in different MS.
- Facilitating language training for FINs, prosecutors, analysts.
- Improving public records needed by FINs especially court records.
- Encouraging the further establishment of Joint Investigation Teams on an *ad hoc* basis with the close support of the PCWG.

5.3.8 Prosecutors

The EU should:

- Strengthen coordination between prosecution services in MS via Eurojust.

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- Promote awareness of legal instruments available to prosecutors.
- Create a secure CT communication system between Eurojust and prosecutors in MS.
- Ensure MS provide data in full and promptly to Eurojust.

5.3.9 *Seizure*

The EU should:

- Consider introducing a directive on immediate administrative freezing by MS to cover current gap in EU system.
- Make the electronic version of EU list legally valid.
- Allow cost recovery for banks from forfeited funds.
- Improve appeal and compensation procedures for those wrongly designated at EU and MS levels.

5.3.10 *Company Fronts and NPOs*

The EU's focus on companies and NPOs should be based on private sector principles of governance and transparency, focussing especially on fraud prevention, but not CFT as such. Such an approach will by its nature create a hostile environment for TF. Only once it is place would more specific CFT measures be worthwhile (if indeed they are needed). Specifically:

- Any framework for an NPO code should be primarily aimed at transparency and equitability.
- Work on establishing beneficial ownership of companies should be expedited
- In light of the conclusions of the UK study on BO¹², consideration should be given to:
 - Creating a duty to disclose BO of 10% or more in confidence to the FIU.
 - Creating a serious offence of failure to divulge BO with intent to commit ML/TF.

5.3.11 *NPOs*

The following principles should be observed:

- A robust anti-fraud regime would be of more general value to the NPO sector (see conclusion on p.33)
- The possible role of tax authorities e.g. in screening NPOs (new, existing) should be considered in addition to possible initiatives under the Third Pillar.
- In case of regulation, a light form of regulation (including self-regulation) should apply to NPOs under a specified turnover.
- NPOs should be encouraged to apply for ISO rating.
- Outreach/training on abuse should focus on fraud but include TF.
- Only NPOs working in certain areas should be subject to enhanced oversight.
- Oversight should be structured as much to facilitate the NPOs operations as to control.

5.3.12 *ARS Cash Couriers*

Consideration (or, where in hand, priority) should be given to:

- Developing with the private sector alternatives to ARS for remittances to under-banked areas.
- Help develop accessible formal banking systems in destination countries.
- Developing a hand book of best practice for customs officials.
- Accelerate uniform registration and reporting procedures for cross border cash.

¹² http://www.hm-treasury.gov.uk/media/DE2/7A/ownership_long.pdf

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- Establish a section in a central reporting database for recording cash smuggling incidents and updating risk indicators.
- Establish a contacts directory on the central data base updated by end users to facilitate bilateral inquiries.
- In dialogue with the private sector, study ways to reduce the use of cash.
- Develop security features in the €100, 200 and 500 notes to support detection by dog units and machines.

5.3.13 International Dimension

EU should encourage:

- FATF to reform of deficiencies highlighted in this report relating to FATF40R and 9SR, especially the burden and complexity of mutual evaluation processes.
- FATF to review of the FATF40R and 9SR, giving special attention to the distinction between measures that address OC reduction generally and those which target specific forms of crime, and to their effectiveness.
- MS to increase technical assistance to third countries and reinforce coordination e.g. through COTER.

The EU should continue to be a signatory to all CoE AML and TF conventions and ensure harmonisation of MONEYVAL and reformed FATF processes within the EU.

¹⁰ P. Wilkinson, *International terrorism, the changing threat and the EU's response*, 2005, Paris, pp. 13-14

ⁱⁱ C. Rijken, *Scientific Research JIT, Final Report*, Tilburg, pp. 39-40 December 2005,

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APPENDIX I

COMPLIANCE WITH FATF 40 RECOMENDATIONS IN 12 EU MEMBER STATES

MS REC	BE 2006 FATF	CY 2005 MV	CZ 2004 MV	DK 2006 FATF	D 2004 IMF ¹	HU 2005 MV	IR 2006 FATF	IT 2005 FATF	POR 2006 FATF	SLVE 2005 MV	SP 2006 FATF	SW 2006 FATF
1	C	LC	C	LC	C	LC	LC	C	LC	LC	LC	LC
2	C	C	C	LC	C	LC	LC	PC	LC	C	LC	LC
3	LC	C	C	LC	C	C	C	LC	LC	LC	LC	LC
4	C	C	LC	C	C	LC	C	C	C	C	C	LC
5 **	LC	PC	C	PC	LC	C	PC	PC	LC	LC	PC	PC
6 **	LC	LC	-	NC	C	LC	NC	NC	NC	NC	NC	NC
7 **	C	LC	LC	NC	C	LC	NC	NC	PC	LC	NC	NC
8	C	LC	LC	NC	C	C	PC	C	C	PC	PC	LC
9	C	C		NC	C	C	NC	PC	N/A	C	N/A	N/A
10	C	LC	LC	C	C	C	C	C	C	C	C	LC
11	C	LC	LC	NC	C	C	PC	LC	LC	LC	C	LC
12 **	PC	PC	LC	NC	C	C	PC	NC	PC	PC	PC	PC
13 **	LC	C	-	PC	LC	PC	C	PC	LC	PC	LC	PC
14	C	PC	LC	C	C	PC	C	C	C	LC	C	C
15	LC	PC	C	LC	C	C	LC	LC	LC	LC	LC	LC
16 **	LC	PC	C	PC	C	C	PC	NC	PC	PC	PC	PC
17 **	LC	PC	C	PC	C	PC	PC	PC	LC	LC	LC	LC
18	C	LC	C	PC	C	LC	PC	PC	LC	LC	C	PC
19	C	C	C	LC	C	C	C	C	C	C	PC	PC
20	C	C	C	C	C	C	C	C	C	LC	LC	C
21	C	LC	C	PC	C	C	PC	LC	LC	C	C	PC
22	LC	LC	-	LC	C	C	LC	PC	LC	PC	LC	PC
23 **	PC	LC	-	PC	C	C	LC	PC	LC	LC	PC	PC
24 **	PC	PC	-	NC	C	LC	NC	NC	PC	LC	NC	NC
25	LC	LC	-	NC	C	LC	LC	PC	PC	LC	PC	LC
26	C	C	C	LC	C	LC	LC	LC	LC	LC	LC	LC
27	C	LC	-	C	C	LC	C	C	LC	PC	LC	LC
28	C	C	NC	C	LC	LC	C	C	C	C	LC	C
29	LC	C	C	LC	C	C	LC	LC	LC	C	PC	LC
30	PC	LC	-	PC	C	C	LC	LC	LC	LC	PC	PC
31	LC	C	-	LC	LC	C	LC	LC	LC	C	LC	LC
32 **	LC	PC	LC	PC	LC	C	PC	LC	PC	LC	PC	PC
33 **	PC	LC	C	PC	C	LC	PC	C	PC	C	PC	PC
34	N/A	LC	C	PC	C	C	PC	PC	PC	N/A	N/A	N/A
35	LC	C	-	PC	C	N/A	LC	PC	C	C	LC	LC
36	LC	LC	-	LC	LC	PC	C	C	C	C	C	LC
37	LC	C	C	C	C	C	C	C	C	C	C	C
38	LC	C	C	LC	C	C	C	C	C	LC	C	LC
39	LC	C	-	LC	C	C	C	C	C	C	C	C
40	C	LC	C	C	C	C	C	C	C	LC	LC	C
41						C						

NB ONLY INCLUDES MS WITH CURRENT / RELATIVELY RECENT PUBLIC PEER RATINGS

¹ Authors' shadow ratings based on IMF Country Report No. 04/213, July 2004, Republic of Germany: Report on Observance of Standards and Codes; FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism. For rating method see footnote on next page.

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NOTES TO APPENDIX I

A. KEY

1. Legal Systems

- Scope of the criminal offence of money laundering (R. 1, R. 2)
- Provisional measures and confiscation (R. 3)

2. Measures to Be Taken By Financial Institutions and Non-Financial Businesses and Professions to Prevent Money Laundering and Terrorist Financing

- Customer due diligence and record-keeping (R. 4, R. 5, R. 6, R. 7, R. 8, R. 9, R. 10, R. 11, R. 12)
- Reporting of suspicious transactions and compliance (R. 13, R. 14, R. 15, R. 16)
- Other measures to deter money laundering and terrorist financing (R. 17, R. 18, R. 19, R. 20)
- Measures to be taken with respect to countries that do not or insufficiently comply with the FATF Recommendations (R. 21, R. 22)
- Regulation and supervision (R. 23, R. 24, R. 25)

3. Institutional and Other Measures Necessary in Systems for Combating Money Laundering and Terrorist Financing

- Competent authorities, their powers and resources (R. 26, R. 27, R. 28, R. 29, R. 30, R. 31, R. 32)
- Transparency of legal persons and arrangements (R. 33, R. 34)
- International Co-operation (R. 35)
- Mutual legal assistance and extradition (R. 36, R. 37, R. 38, R. 39)
- Other forms of co-operation (R. 40)

B. OTHER NOTES

Rating Method for Germany

Whereas other country scores are taken directly from the relevant peer evaluation report, the scores for Germany have had to be estimated by the Authors on the basis of recommendations contained in the published Germany peer evaluation report, which does not contain scores.

Germany was assessed overall as being compliant with FATF recommendations. Thus, where no action was stipulated in the evaluation in respect of an FATF recommendation, the score for that recommendation in this table has been set at 'C'. Where action was stipulated it has been set at 'LC'. Our scores may differ from the official evaluators' scores and for that reason the German scores are given in italics.

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APPENDIX 2: COMPLIANCE WITH FATF 9SR

Country Rec.	BE L 200 6	CY 2005	CZ 2004	DK 2006	D 2004 ²	HU 2005	IRE 2006	IT 2005	POR 2006	SLVA 2006	SLVE 2005	SWE 2006	SPA 2006
SRI **	LC	LC	NC	PC	LC	PC	PC	LC	PC	PC	C	LC	PC
SRII	C	PC	NC	PC	LC	PC	LC	LC	LC	NC	LC	LC	LC
SRIII**	PC	LC	NC	PC	LC	PC	PC	LC	PC	PC	LC	PC	LC
SRIV**	C	C	NC	LC	LC	NC	C	PC	LC	NC	NC	LC	LC
SRV	LC	LC	C	LC	C	C	C	C	LC	PC	C	LC	LC
SRVI	C	LC	NA	LC	C	C	PC	LC	LC	LC	NC	PC	LC
SRVII	LC	C	NR	PC	LC	C	NC	NC	NC	PC	LC	NC	LC
SRVIII**	C	PC	-	LC	C	PC	PC	C	LC	NC	PC	PC	LC
SRIX **	NC	LC	-	PC	C	PC	PC	C	LC	PC	C	NC	LC

- I. Ratification and implementation of UN instruments
- II. Criminalising the financing of terrorism and associated money laundering
- III. Freezing and confiscating terrorist assets
- IV. Reporting suspicious transactions related to terrorism
- V. International co-operation
- VI. Alternative remittance
- VII. Wire transfers
- VIII. Non-profit organisations
- IX. Cash couriers

² See Notes on Appendix 1

APPENDIX 3: A2E ANALYSIS OF COMPLIANCE WITH 9SR (1 OF 2)

DIMENSION/REASONING SCORE	1 - 5 (1 = LOW)
<p><u>AUTHORITY</u></p> <p><i>Clarity/knowledge of legal texts</i> Obligations deriving from the Special IX are well understood in governments and the wholesale and specialist sector of the finance industry, less so DNFPBs and general public. Textual differences (e.g. between (i) the CoE text of the Convention and the FATF recommendations, and (ii) the UN and EU freezing regulations) complicate the application of EU regulations in TF, The differences between the CoE convention and the EU regulation will be solved when the third directive on ML comes into force. Knowledge of 9SR is greatest amongst a small number of specialised insiders (That is a problem but does not influence the score because...)</p> <p><i>Feasibility/Overlap with Indigenous systems.</i> Those compliant with ML regulations will have overlap with CFT regulations. Some business systems (e.g. anti fraud, WTs, charity umbrella organizations) overlap CFT regulations/proposals.</p> <p><i>Legitimacy</i> Innate acceptance of the principle, if no the details of wider CFT activity. Doubts as to the goals of certain key players.</p>	<p align="center">Well Above Average (✓✓✓✓)</p>
<p><u>BEHAVIOUR</u></p> <p><i>Appreciation (Quality of Policy)</i> Initial acceptance very high. Subsequently, acceptance has differed according to recommendation, being greatest in criticism of SR VIII (non profit organisations) and SR III (freezing mechanics). With regard to international cooperation and exchange of information (SRV), acceptance differs (though to a lesser degree) between institutions both within and between countries). For the others there is a generally still a high level of acceptance.</p> <p><i>Costs</i> Costs are difficult to establish and to separate for individual SRs. Costs of compliance can be high, especially where automated systems required/need to be updated (e.g. in FIU's and for international cooperation). Up front costs attach to detection of suspicious transactions for financial institutions and introducing risk based systems. Indirect costs arise from the loss of business at the margin. Marginal cost for EU regulation and inspection are relatively low because MS have obligations via UN/FATF/Moneyval. Costs are thus mainly EU direct costs of CFT coordination measures and special initiatives by EU institutions.</p> <p><i>Benefits</i> The immediate benefits of compliance are unclear given the questionable effectiveness of the overall system. Decreased reputation risk for privates sector players Increased transparency of financial system and effectiveness of fight against TF (if none, symbolic value) Indirect benefits for governments and the EU are the easier detection and investigation of forms of financial fraud and tax offences. Both public and private sector may suffer less from other forms of financial crime.</p>	<p align="center">Above Average (✓✓-✓✓✓)</p>

APPENDIX 3: A2E ANALYSIS OF COMPLIANCE WITH 9SR (2 OF 2)

DIMENSION/REASONING	SCORE 1 - 5 (1 = LOW)
<p>CONTROLS</p> <p><u>Informal control</u> Publicity linked to the failure of a government to prevent its the abuse of a market or payment system by terrorists is a strong form of informal control. To the extent it is a non-EU control the FATF/Moneyval inspection is an informal control with a probability of 100%. The chances of informal detection feeding into the formal system are high for SR 1-3 and zero for SR 4-9 there is no formal system (though 3MLD will alter this for part of SRs 4-9).</p> <p><u>Risk of Formal Control</u> The risk of an EU inspection is low as the EC has no system of inspection for compliance with the Special IX. To the extent FATF/Moneyval is an EU control it is a formal control with 100% probability</p> <p><u>Risk of Detection.</u> Very high for non classified issues</p> <p><u>Risk of Reporting</u> The risk of being reported by FATF inspection is very high.</p> <p><u>Chance of sanction</u> Strong chance of public exposure of deficiencies</p> <p><u>Severity of sanction</u> Loss of standing in international community has high political impact in some countries but less in others. Some loss to the economy of trade and investments seeking better regulated environment.</p>	<p>Above Average</p> <p>In some MS Well Above Average</p> <p>(✓✓✓- ✓✓✓✓)</p>
<p>DEFICIENCIES (Systemic)</p> <p>Resource constraints</p> <p>Slow legislative systems</p> <p>Weak ancillary structures (criminal justice, corruption, professional ethics, CID capacity, fiscal compliance)</p> <p>Relatively weak coordination by lesser DNFPB trade bodies on the EU and national level</p> <p>Inefficient IT support for SARs</p> <p>Poor intelligence sharing capacity at national and EU level.</p>	<p>Below Average</p> <p>Locally Well Below Average (✓✓- ✓)</p>
<p>EXTERNALITIES</p> <p>Migration</p> <p>CIP</p> <p>Pandemics</p> <p>OC</p>	<p>Average</p> <p>Locally Below Average (✓✓-✓✓✓)</p>

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Appendices

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APPENDIX 4A: DIVISION OF RESPONSIBILITIES IN MEMBER STATES					
	Criminal Justice	Financial	Intelligence	Customs	Foreign Affairs
Policy and Regulation	Ministry of Justice	Ministry of Finance	Ministry of Interior Ministry of Defence	Ministry of Finance	Ministry of Foreign Affairs
Prosecution Sanctions	Public Prosecution	Public Prosecution; Ministry; Agencies	-	Sanctioning Power	MLA
Supervision & Investigation	Police; Specialized investigative units	Securities Regulator and Exchanges; Bank and Insurance Supervisors	-	Customs	MLA
Subjects	Public	Banks	Potential terrorists	Travellers	
Information & Intelligence	Police Intelligence; Financial Intelligence	FIU	Internal Security Services; Intelligence Service; Military Intelligence	FININT	

APPENDIX 4B: DIVISION OF RESPONSIBILITIES WITHIN EU						
	EC	Eurojust	Europol	Customs	Civil Intelligence	Military Intelligence
Preparing common standards	X			X		
Directing		X		X		
Coordination of action		X	x			
Exchange of information		X	X	X	X	X
Support		X	X	X	X	
Monitoring and feedback	X	X				

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APPENDIX 5: PRIME PILLAR RESPONSIBILITY AND CAPACITY WITH REGARD TO FATF 9SR			
Special Recommendation	Principal EC Pillar	Capacity within Pillar at EU level	
		Organisational	Analysis and Intelligence
SRI UN Conventions	I Market Regulation III Criminal Justice	Medium - High	Medium
SRII Criminalisation		Medium - Low	Low
SRIII Freezing & Confiscation		High (I) Low (III)	Low (I) Low (III)
SRIV Terrorism SARs		High	Low
SRV International co-operation	I Customs Customs information Banking II Military services Military police Military intelligence III Exchange of police and criminal informational and intelligence; Co-ordination of police investigation and prosecution	I High II Medium III Low	I Potentially High on Customs II Low III Low
SRVI ARS	I Market Regulation III Criminal Justice	Low	Potentially High
VII Wire Transfers		Low	Low
VIII NPOs		R&D Phase	R&D Phase
IX Cash Couriers		Low	Low