

Brzoska, Michael

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## The Role of Effectiveness and Efficiency in the European Union's Counterterrorism Policy: The Case of Terrorist Financing

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Michael Brzoska

# **The Role of Effectiveness and Efficiency in the European Union's Counterterrorism Policy: The Case of Terrorist Financing**

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For further information, please contact:

Economics of Security, c/o Department of International Economics, German Institute for Economic Research (DIW Berlin), Mohrenstr. 58, 10117 Berlin, Germany.

Tel: +49 (0)30 89 789-277

Email: [eusecon@diw.de](mailto:eusecon@diw.de)

Website: [www.economics-of-security.eu](http://www.economics-of-security.eu)

# The Role of Effectiveness and Efficiency in the European Union's Counterterrorism Policy: The Case of Terrorist Financing<sup>1</sup>

Michael Brzoska  
Institute for Peace Research and Security Policy at the University of Hamburg  
Beim Schlump 83  
20144 Hamburg  
Germany  
[www.ifsh.de](http://www.ifsh.de)  
brzoska@ifsh.de

## Abstract

European Union policy to counter terrorist financing is marked by uncertainty about causes and consequences. The paper addresses the role of evaluations of the effectiveness and efficiency of counter terrorist financing policies performed by international standard setting organizations in such a policy environment. It is found that assessments of effectiveness have shaped counter terrorist financing, but partially in a way biased towards their extension without strong evidence of their effectiveness. Assessments of the comprehensiveness of a regulatory framework and its implementation have been frequent while evaluations of the impact of activities on terrorist activities are largely lacking. As a result, there is much pressure to expand activities in the field without much knowledge about their impact. Considerations of financial and non-financial costs of counter terrorist financing measures have limited their extension, albeit again rarely based on evidence of their effectiveness. The paper's results confirm the proposition that policies in high risk fields tend to be expansive. Assessment of effectiveness and efficiency emphasizing output and outcome of measures rather than impact play an important role in shaping such expansion.

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## Introduction

The prime objective of counterterrorism policy is to prevent major terrorist attacks. In most parts of the world, including the member states of the European Union (EU), such attacks are fairly rare. If such attacks occur, however, they have major repercussions in terms of domestic, and often, international politics. Because major attacks are rare there is little evidence to go on to find the best way to counter terrorism or to establish whether certain measures are useful in preventing terrorism. The absence of a major terrorist attack is no useful indicator of the success of counterterrorism; as a result, the effectiveness of countermeasures against terrorism cannot easily be established.

Under these circumstances, the standard policy cycle of recursive correction of approaches and instruments is under duress. Standard procedures of policy correction, such as cost-benefit analysis, are difficult to apply. Furthermore, political decision-makers may be unwilling to let policies be measured by their effectiveness and efficiency. While counterterrorism policy is marked by high degrees of uncertainty about causes of terrorism and the consequences of countermeasures, at the same time, terrorism is a major concern to the general public. Policy makers thus must demonstrate activity even in the absence of evidence of the effectiveness of activities. Because they cannot use standard measures of effectiveness, instead they may prefer to base their decisions on other considerations and factors, such as path-dependent behavior, policy linkages, major events or outside pressures.

The difficulty in performing analyses of the effectiveness and efficiency of counterterrorism policy contrasts, to some extent, with the number and detail of official assessments. One field of counterterrorism policy in particular, that of counterterrorist financing, has been a frequent subject of evaluation.

In a way this is not surprising. In general, there are strong incentives to perform official policy assessments and evaluations in today's policy making world. Assessment of effectiveness and efficiency, as a core element of 'evidence-based policy', have become standard in many areas of public spending and public policy. They provide legitimacy to policies. They provide guidance for the allocation of scarce resources. They aim to save cost, to detect crucial deficiencies in policies and more generally improve policy making.

However, there are other areas of high risk/low probability policy not similarly marked by official assessments or evaluations. One such example is defense policy. While there are many studies on the effectiveness of particular weapons systems, the effectiveness of overall military postures is rarely thoroughly assessed, and if this is done it is usually with a clear political purpose<sup>2</sup>.

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<sup>2</sup> There are a good number of assessments of particular military missions, e.g. the current war in Afghanistan. However, the policies studied are not in a high risk/low probability area.

The objective of this paper is to investigate this apparent puzzle. My first question is why there is such a particular interest in officially assessing the effectiveness and efficiency of counterterrorist financing measures (CTF). The second question is whether and to what extent information coming out of official studies of the effectiveness and efficiency of CTF is shaping policy in this field and whether the costs of such measures provide a counterbalance. My empirical focus is CTF in Western Europe.

The paper concludes that assessment on effectiveness and efficiency of CTF are driven by a desire to improve the standards of control over financial transactions. Main driver is the US government, with international arrangements and institutions as important leverages to spread high standards of control. However, CTF assessments tend to have a different scope from analysis of effectiveness and efficiency in many other policy areas. Instead of assessing impacts of CTF measures, most official evaluations focus on output, on the adoption of agreed principles and best practice, and outcome, their implementation. Assessments are predominantly made against ‘best practice’ standards and regulations and not against evidence of benefits in reducing terrorist activity. They thus tend to identify implementation deficits, generally recommending remedies requiring additional CTF measures. Attempts to assess the actual effectiveness and efficiency of particular measures in reducing terrorist attacks are rare<sup>3</sup>. As a result, CTF effectiveness and efficiency assessments are biased towards the direction of expanding CTF measures.

### **Policy making under high risk of failure and great uncertainty of effectiveness**

The finding that official policy assessments are extended and brought into more and more policy fields is not new. In fact, it has been identified as a feature of modern society with its requirements for public legitimacy and bureaucratic rationality (xxx).

Policies in high risks/low probability areas are no principal exception to the trend towards evaluation. However, they provide particular environments for an ‘evidence-based’ approach to public policy. This has been analyzed in various strands of academic literature, two of which will be briefly mentioned here.

The first is the literature linking risks, uncertainty and insecurity with advances in modern society. Ulrich Beck has described a ‘second modernity’, also called ‘reflexive modernization’ increasingly threatened by its own activities. The amount and importance of information grows while society

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<sup>3</sup> This contrast, to some effect, with academic work on counterterrorism. While not a major focus in academic work on terrorism, the study of the effectiveness and efficiency of counterterrorism policies has been the topic of several dozens of academic contributions over the last few decades. See xxx and Psoiu and van Um (2011) for overviews.

monitors itself which in turn manufactures new risks. Globalization has further added to the spread and interaction of risks. Risks are increasingly incalculable while their scope for catastrophic damage grows (Beck 2006). For security policy, including counterterrorism policy, this implies that certainties evaporate and security collapses. Rationalist behavior towards risk is rendered more difficult. The scope of insurance provisions, to give an example, is reduced; the calculation of premiums unacceptable. Policy makers are put in impossible situations. They need to show activity to cope with risks that they cannot cope with.

The expansion of state activity, particularly information gathering and surveillance, also has long been an important observation in another strand of literature. For risk theorists who base their work on Foucault's analysis of technologies of power, policies to address risks are far from vain efforts to control the uncontrollable but rather are particular instruments of *gouvernementalité*, the establishment and maintenance of order through various forms of powers. The argument is that risk logics facilitate increasing control over populations and new spheres of human life (Aradau & van Munster 2007; de Goede 2008).

For the particular topic of CTF, the two approaches lead to partly overlapping but also different hypothesis. Both predict an expansion of CTF as a policy dealing with potentially high damage but low probabilities of occurrence. The risk society approach suggests that efforts to assess the effectiveness and efficiency of CTF will be frequent but not be substantial. Politicians need to demonstrate that they are grappling for control of risks, even when that is not possible. The Foucauldian approach is more compatible with the view that little effort will be made to establish effectiveness and efficiency – in contrast, they might even be seen as potentially dangerous because they interfere with the principles of precaution (Rasmussen 2006; de Goede 2008).

### **Terrorism financing**

This section is designed to give some more background on terrorism financing, addressing in particular issues related to its importance in the fight against terrorism, as well as its flexible nature.

Single attacks generally are cheap. The attackers of September 11, 2001 probably spent less than half a million US Dollars. Still, this is mentioned in the relevant literature as one of the most expensive terrorist attacks (see table 1). Much more expensive is the maintenance of a large organization committing terrorist acts or a major network of such organizations over a longer period of time (Acharya 2009). Financing needs, as well as funding activities, of those committing terrorist acts vary greatly. There is little in common between individuals or small groups of 'home grown terrorists', such as those that exploded bombs in London in July 2006, and an organization such as Hamas, which has been involved in sponsoring terrorist attacks.

Variety in the financing of terrorist acts is nothing new. However, some of the patterns of terrorist financing have changed in the last few decades, and so have some of the elements in the financial environment, in which groups committed to terrorist violence operate (Cortright and Lopez 2007; Biersteker and Eckert 2009)

The most important change has been due to the ‘transnationalization’ of a good part of terrorist activity. While not a totally new phenomenon, the operation of terrorist groups across borders as well the transnational linkage of various such groups has grown after the end of the Cold War, according to the analysis of many observers. This partial, but significant shift from predominantly national to predominantly transnational terrorism between the 1970s and 1980s to the 1990s and early years of this century has been facilitated by globalization, which allows for the easier movement of ideas, goods, and considerably less so, people. It also has connected to the rise of terrorist acts motivated by Islamic fundamentalism. Another factor has been the withdrawal of a number of governmental sponsors of national terrorist activities, such as the Libyan government.

The change is reflected in financing patterns. While up to the early 1990s, terrorist organizations were either self-financing, predominantly through illegal activities and private donations, or reliant on external sponsorship by governments. After the end of the Cold War, this last source of funding lost in importance (Giraldo and Trinkunas, 2007a, pp- 8-12). Donations and crime continued to be important sources for domestic organizations using terrorism, but at least for a number, such as the Tamil Tigers, sources of such income became more international.

Transnationalization of finance often is linked to the rise of Al-Qauida. The extension of Al-Qauida’s activities beyond Afghanistan beginning in the 1990s was clearly facilitated by a transnational financial network involving substantial amounts of funds. Even though some terrorist organizations harvested large private donations from external sponsors during the Cold War period – examples include the IRA in Northern Ireland and the Mujahideen in Afghanistan – the scope and scale of Al-Qauida’s financial activities in the 1990s were of a substantially larger scale (Wright 2006; Gunaratha 2008).

Largely because of the activities of Al-Qauida, terrorism financing moved from a side-issue to front stage in counterterrorism. Already before the September 11, 2001 attacks, a number of governments, particularly the US government, had argued for a focus on financial transactions and the freezing of assets in counterterrorism efforts. After these horrendous attacks, the US government declared the suppression of counterterrorism financing to be one of the prime instruments for stopping future terrorist attacks. A typical statement expressing the importance attached to countering terrorist financing can be found in a report of the US government outlining its policy five years after the attacks: “Before 9/11, financiers of terrorism and terrorist financing networks went untouched and



largely ignored by the international community. Today, we continue the aggressive worldwide campaign to disrupt terrorism financing, making it harder, costlier, and riskier for al-Qaida and other terrorist groups to raise and move money around the world.” (White House 2006).

### **Countering terrorism financing**

CTF measures go back in recent history at least to the 1970s. In Europe, early activity took place in the late 1970s, in order to counter national terrorist organizations active in a number of countries (Giraldo and Trinkunas 2007b).

In the US legal instruments were adopted in the early 1970s allowing the US government to stop financial transfers and seize assets, including bank accounts, related to states and organizations identified as “terrorism sponsors”. In the middle of the 1990s, this was expanded to also cover transactions and actions by individuals (Levi 2010, 652). Legal options were further expanded after the attacks against US embassies in East Africa in 1998 and the September 11, 2001 attacks to also include financial assets in foreign countries. Law enforcement agencies were given extensive rights to investigate financial transactions and banks and other financial intermediaries were requested to report suspicious activities.

With some time delay, international efforts at controlling and reducing illegal flows of money were initiated. At the UN, negotiations of a convention on terrorism financing took place in the late 1990s, resulting in the 1999 International Convention for the Suppression of the Financing of Terrorism<sup>4</sup>. Before it entered into force, it was effectually implemented by United Nations Security Council Resolution (UNSCR) 1373 in which it was decided that all States should prevent and suppress the financing of terrorism, as well as criminalize the willful provision or collection of funds for such acts (Diaz-Paniagua 2008, Talmon 2005). The Council demanded of all UN member states that they should prohibit their nationals, persons or entities in their territories from making funds, financial assets, economic resources, financial, or other related services available to persons who commit or attempt to commit, facilitate, or participate in the commission of terrorist acts.

UNSCR 1373, while largely motivated by the September 11, 2001 attacks, had a predecessor in UNSCR 1267 of 1999 as well as other activities in the UN Security Council (Messmer and Jordan 2010). This resolution demanded that all member states freeze all assets of al-Qaida and the Taliban. A sanctions committee was instituted to decide on the names of organizations and individuals whose

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<sup>4</sup> The convention was signed by 35 states in 1999. It entered into force in 2002 after the 22<sup>nd</sup> ratification and had 177 signatories by late 2010.

assets should be banned. By late-2000, the list contained almost 500 names of individuals and organizations<sup>5</sup>.

Another important negotiation track was the international cooperation to counter money laundering. A particularly important international organization in this context is the Financial Action Task Force on Money Laundering (FATF) initiated by the G-7 states in 1989<sup>6</sup>. Some discussion of adding terrorism financing to broader efforts at controlling and reducing illegal flows of money took place in the 1990s, but it took the attacks of September 11, 2001 to make it a second focus of the FATF's work, in addition to money laundering (Passas 2007).

The FATF, which as a club can only formulate "soft law", nevertheless became a powerful organization. Its standards of operation in the financial sector, expressed in a number of "recommendations", which included 8 "special recommendations" on terrorism financing, became the de facto measure of whether states implemented UNSCR 1373. This was guaranteed by the economic and political power of the 33 governments, including the G-7 states, standing behind the FATF.

The combination of UNSCR 1267, UNSCR 1363 and the FATF focus on countering terrorism financing quickly led, beginning in 2001, to the widespread introduction of legal (UNSCR) and quasi-legal (FATF) international standards and instruments to control financial transfers and assets. Much of this agenda was shaped by earlier US policies. The considerable resistance in Europe against adopting all of this agenda evaporated after September 11, 2001 (de Goede 2008).

The international, post 9/11 CTF agenda combines the asset freeze and anti-money laundering approaches. Asset freezing follows from a logic of precaution. Terrorist groups should be deprived of their means to conduct terrorist acts, based on the idea that "money is the oxygen of terrorism" (Parker and Taylor, 2010, p. 949). Assets can be frozen on the assumption of danger, without the evidentiary standards required by courts. There is no need to prove that groups or individuals have violated the law, it is enough that relevant bodies assume that they might support or perform terrorist attacks. The money laundering agenda, on the other hand, follows the two logics of crime prevention and crime detection of criminal law enforcement. Criminals are to be prevented from turning 'illegal money' – income from criminal activities – into 'legal money'. A central instrument is customer due diligence measures ("know your customer") which are to ensure that transactions are traceable, and also provide a degree of deterrence against criminals using the financial system for money laundering. Furthermore, when financial institutions suspect a client of turning illegal into legal money, they have to file a

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<sup>5</sup> <http://www.un.org/sc/committees/1267/consolidatedlist.htm>.

<sup>6</sup> The FATF had 33 members at the end of 2010. Its decisions are not binding but 130 'jurisdictions' including about 130 states had declared by the end of 2010 that they would adopt the FATF's 'recommendations' on money laundering and terrorist financing, <http://www.fatf-gafi.org>.

suspicious activity report (SAR) (Chaikin 2009). Again this measure is design to deter criminals as well as to detect cases of money laundering<sup>7</sup>.

In the wake of expanding money laundering to include CTF, prevention was extended by requiring financial institutions to file SARs when they have been informed by authorities of terrorism suspects or they suspect that a person or group is actively supporting or planning terrorist attacks<sup>8</sup>. Prevention further moves in the direction of precaution with the requirement to ensure that charities and other non-profit organizations do not provide money for terrorist activities. Further special measures on CTF were mandated by the FATF (see Table 2 for the FATF “Special Recommendations”). Of particular importance is the requirement for better customer identification in wire transfers, which include transactions hitherto performed in un-regulated ways, such as the Hawala system (De Goede 2003; Vlcek 2007). FATF rules also establish the duty to cooperate, as much as possible, with other countries on CTF.

The implementation of FATF recommendations had been a slow and painful process prior to 9/11. With the addition of CTF as major objective, they received a major push. It is questionable whether money laundering provisions in themselves would have been sufficient to expand control over financial transactions in the way it happened after 9/11. It is rather clear that law with CTF, the law enforcement approach would have remained dominant. The shift into the direction of precaution might not have occurred (Williams 2008).

One element of the stronger implementation of FATF recommendations are peer reviews of their implementation by member states and cooperating jurisdictions. The FATF claims that “the mutual evaluation process represents a central pillar of the work of the FATF.” The focus of the evaluations is stated as: “Through this process, the FATF monitors the implementation of the FATF Recommendations and assesses the effectiveness of the anti-money laundering and counter-terrorist financing systems in FATF member jurisdictions.”<sup>9</sup>

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<sup>7</sup> There is no unanimous consent that prevention of terrorist funding is the prime objective of measures in this field. Particularly among specialists one can find the view that they are more useful for criminal investigations (“follow the money trail”) than for preventing terrorist attacks. The different foci are reflected, for instance, in the institutional placements of Financial Intelligence Units (FIU). FIU are the offices, where information on suspicious activities are collected and processed. In the EU, about half of the national FIUs are placed within law enforcement structures, and the other half within institutions charged with the supervision of financial sectors. (House of Lords, 2009, p. 22).

<sup>8</sup> It has been noted that the 9/11 plotters used the financial sector to receive and transmit funds, they had ‘normal’ financial profile. It is unlikely that a SAR would have been issued in their cases, unless banks had been prewarned to look out for their names (Roth et al 2004).

<sup>9</sup> FATF website at [http://www.fatf-gafi.org/pages/0,3417,en\\_32250379\\_32236982\\_1\\_1\\_1\\_1\\_1,00.html](http://www.fatf-gafi.org/pages/0,3417,en_32250379_32236982_1_1_1_1_1,00.html)

## **CTF and the EU**

Most of the member states of the EU in 1990, including all EU members in the G-7, are also FATF members. When the FATF expanded into terrorism financing, EU member states quickly followed suite and adopted measures and regulations corresponding to the FATF recommendations. While later evaluations by FATF expert groups – such peer evaluations are part of the FATF implementation strategy – found gaps and problems in legal requirements in all member states, these were generally minor or reflected particular local issues. In general, EU member states have done what the FATF required.

Another issue is cooperation among member states. In 2001, the member states signed a Protocol to the Convention on Mutual Assistance in Criminal Matters. The Protocol, negotiated prior to September 11, 2001, but signed afterwards regulates the cooperation on issues such as the identity of holders of bank accounts, requests for details of those accounts and of banking transactions, and requests for the monitoring of banking transactions. Member states agreed that banking secrecy would not be a ground for refusing the request. While some member states quickly signed the agreement into national law, others were reluctant to do so. In 2009, five member states had not done so (House of Lords, 2009, p. 17). On 26 October 2005, three months after the terrorist attacks in London, the EU adopted a Directive on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing<sup>10</sup>. The directive largely reiterated the FATF standards, which most EU member states had already adopted unilaterally, as a EU requirement. A number of member states were slow in transposing the directive into national law and only did so after the EU Commission had instituted proceedings before the European Court of Justice.<sup>11</sup>

A particularly thorny issue is the data exchange with the US. Immediately after September 11, 2001, negotiations for an agreement on mutual legal assistance between the EU and the US were initiated which were concluded on June, 25 2003. The US insisted on additional individual agreements with all member states on implementation of the provisions of this agreement. It took nine years, until 2009, until all 27 of these bilateral agreements were concluded (House of Lords, 2009, p. 18).

## **Criteria and indicators of effectiveness**

I now turn to the question of assessments of effectiveness and efficiency in shaping CTF policy in Europe.

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<sup>10</sup> Directive [2005/60/EC](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32005L0060:EN:NOT) of the European Parliament and of the Council of 26 October 2005, see <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32005L0060:EN:NOT>

<sup>11</sup> <http://www.anti-moneylaundering.org/EuropeanChart.aspx>

Effectiveness can be measured at various levels (Brzoska 2008). In policy cycle analysis, the distinction between output, outcome and impact has proven to be useful (Easton 1965). Output refers to the broader, particularly legal, framework of shaping interventions in a policy field. Outcome addresses the question whether this framework is implemented in the way mandated. Outcome thus largely is under the control of those policy makers who want to shape a policy field. Impact, to the contrary, also depends on the behavior of those addressed by policies, including their adaption and evasion strategies and tactics. Because impact is shaped by addressees of policy measures, it can include, in addition to the intended effect, also further, non-intended consequences. These consequences may enhance the impact of a policy or policy measure but they may also counteract the intended effect, or create costs in other directions. Costs, which are not part of assessments of effectiveness, are important because policy decision-making under limited resources needs to be guided by efficiency, that is the relation between cost and benefits, with the latter being another form to measure effectiveness.

Output and outcome measures are generally seen as important preconditions for impact which is generally understood in the policy literature as the ultimate measure of effectiveness, as policies are designed to shape the real world, and not just the regulatory framework and its implementation. However, impact is difficult to assess, particularly in areas that can be classified as risk politics. Therefore a fall-back to outcome and even output assessment is often viewed as a second best-best alternative to impact assessments in policy analysis. However, output and outcome are not necessarily good indicators of impact, as, for instance the case of economic sanctions shows (Brzoska, 2009).

There have been a few attempts at assessing the impact effectiveness of CTF, predominantly the academic world (Cortright and Lopez, 2007; Biersteker and Eckert 2009; Chaikin 2009, Brzoska 2009). As mentioned, one objective difficulty is the availability of data and information (Drakos 2009). While some data, for instance on Suspicious Activity Reports (SAR) or assets frozen is publicly available at least for a number of countries, much information is either secret or difficult to assess (Levy 2010). The latter is for instance true for the importance of information on financial transactions for the prevention of terrorist plots, or the prosecution of terrorist groups. The case of the 'underwear bomber', Umar Farouk Abdulmutallab, for instance, is highlighted in a recent report by the UK Serious Organized Crime Agency (2010) as proof of the effectiveness of CTF because his past whereabouts and connections to other people could be reconstructed through financial transactions. However, it is not clear whether this information did more than lead to a more complete picture of Abdulmutallab's life history.

This example already points to another difficulty, that of establishing causality between output, outcome and impact. A major objective of CTF is to prevent terrorist attacks. In addition to the data problem – there is very little publicly available information on attacks that were planned but did not

take place – it is often difficult to assess whether or not lack of finance was a factor (Roth et al. 2004, Passas 2007, Biersteker, Romaniuk and Eckert 2008).

An alternative approach to the investigation into data and causality is to survey relevant audiences. Results are not uniform and not very reliable. In the UK, in a report funded by the City of London in 2004, the average score of responses from the wider financial community to the question of the effectiveness of money laundering activities, including CTF, was quite high (Yeandle et al 2005). On the other hand, in another survey of persons from the financial sector in Germany, Singapore and Switzerland, skepticism was high, and these activities were generally seen as ineffective (Geiger and Wuensch 2007).

### **Effectiveness assessments in official evaluations**

While maintaining the objective of reducing the incidence of terrorist attacks, official evaluations of CTF largely focus on output and outcome assessments. The focus of the work of the UN CTC as well as the peer review mechanism of the FATF and two EU-stipulated counterterrorism evaluations has been the implementation of the recommendations made by relevant international organizations, such as the UN CTC, the EU and the FATF, in particular the creation of appropriate institutional structures and the adoption of relevant legal instruments.

CTC assessments are primarily geared towards output assessments. Its task is to support countries in the implementation of UN Security Council Resolution 1363 (and the follow-up Resolution 1624) through technical assistance. The latter consists of providing best practice examples to countries, assisting with the identification of gaps in legislation and supporting the preparation of country reports.<sup>12</sup> While the UN CTC itself does not judge country reports, they can be used for comparative assessments of the implementation of the relevant resolutions. They are a means for soft pressure on countries to bring their regulations to a high standard (Cortright and Lopez 2007).

The FATF's assessment cover a wider range of issues and indicators, as the FATF judges evaluations to be one of the pillars of its activities. It particularly focuses its reports, however, on the implementation of its guidelines and recommendations on money laundering and CTFT. In addition, FATF assessments bring out 'best practice' as a standard against which particular countries activities are measured.

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<sup>12</sup> <http://www.un.org/en/sc/ctc/resources/countryreports.html>

This emphasis on promoting agreed standards is understandable for an organization whose powers are limited to mutual agreement on principles and recommendations which then have to be implemented by member states and cooperating constituencies (Hülsse and Kerwer 2007). The emphasis on standardization of measures also makes good theoretical sense as a strategy to fight transnational terrorism. Rational terrorists can choose the jurisdiction with the weakest CTF provisions to conduct their financial operations. Counterterrorism efforts are therefore most likely to have effect when addressing the ‘weakest link’ among relevant jurisdictions (Sandler 2005).

Assessments of CTF measures become problematic, however, when evaluations of the implementation of standards, based on output and outcome indicators, are not balanced by impact assessments. As indicated by the brief discussion of impact analysis of CTF, the causal link between financing and terrorist attacks, on which the arguments for the importance of CTF outcome rests, is not well established. The evidence that better CTF implementation reduces the number and/or intensity of attacks is poor (Tupman 2009; Levi 2010).

Furthermore, the emphasis on implementation of CTF standards, which are driven by US example and pressure for more control over financial transactions, tend to increase the level and intensity of CTF measures. Beyond addressing the “weakest link” FATF evaluations have found fault in all cases where assessments have been done, albeit to different degrees. But even in cases of countries with extensive CTF legislation and implementation, deficits were found and further measures recommended by FATF evaluators.

Corresponding and potentially offsetting investigations into the impact of CTF measures are largely absent from evaluations. This is not because FATF investigators are not interested in impact<sup>13</sup>. Indeed, one can frequently find examples of impact in FATF evaluations, such as the prevention of terrorist plots through following the “money chain”. However, the clear emphasis, in line with the role of standard-setter fulfilled by the FATF, is on output and outcome indicators..

The problematique of outcome measures, which are the core of FATF country reports, can be illustrated by looking at a particularly important element of CTF that is Suspicious Activity Reports (SARs). As one of the elements of CTF, institutions in the financial sector, but also other entities such as casinos, are required under FATF-inspired legislation to report customers or transactions where

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<sup>13</sup> An interesting case is the fate of the recommendation of a government advisor on the establishment of reporting instruments on the effectiveness of CTF in the UK. Sir Peter Lander recommended, that the Serious Organized Crime Agency (SOCA): “should develop and propose to participants, through the governance machinery identified earlier, a performance measurement framework for the regime as a whole”. What the SOCA adopted, is a quite different scheme, which measures success on the comprehensiveness and information value of SARs (Serious Organized Crime Agency 2010).

they suspect a link to criminal finance, including terrorism financing. The number of SARs in a particular jurisdiction is difficult to interpret (Lander 2005). There are, for instance, big differences between countries that cannot be explained by the likelihood of terrorists or terrorist organizations using the particular countries financial sectors or success or failures in the fight against terrorism (see table 3). Rather, they seem to reflect different cultures of cooperation with the government in the financial sectors of different countries, but most of all, different risk assessments by financial institutions. Furthermore, only a small share of all SARs are related to terrorism, most are based on suspicion of money laundering (see the example of Germany in Table 4).

Another often used outcome indicator of effectiveness is the amount of assets frozen under CTF legislation (CTC 2009). A major problem with this indicator is that it is highly influenced by the classification of particular groups as terrorist. Most of the changes in the amount of assets frozen under CTF legislation in the last few years have resulted from changes in the classification of organizations. Furthermore, the data is dominated by large charities, particularly those associated with Hamas and Hizbollah. Transnational terrorist organizations are not high up on the relevant lists. Still most experts believe that the share of assets frozen to overall assets owned by relevant groups is low (Napoleoni 2007, Schneider 2008, Tupman 2009).

A third indicator which is used in assessments and which comes closer to impact are convictions for violation of CTF laws. However, even here the message is not clear. The number of cases involved is very low and changes from year to year are large. For the UK for instance, there have been about 10 convictions for CTF offences (among about 100 convictions under terrorism legislation) (Sproat 2010). It is not clear whether the fairly constant number of convictions demonstrates impact of CTF, or its failure.

The EU has carried out two rounds of peer evaluation of national counter-terrorism arrangements, which included CTF policies albeit not at the level of depth that FATF peer reviewers aim for. The first evaluation was conducted in 2004/2005. Its focus was:

- the national responsibilities at the level of Government Ministries, security and
- intelligence services and law enforcement agencies, and the level of national and international coordination and cooperation, including exchange of information, in particular that relating to Islamist terrorism (Council 2005).

Recommendations aimed at improving existing and providing new instruments to law enforcement bodies, security services and other government authorities, in order to develop Member States' capabilities in line with the characteristics and significance of the threat from international terrorism. (Council 2005, p. 5).



A second round of evaluations was finalized in April 2010. It focused on preparedness and consequence management. The recommendations made in the final report (European Council 2010) aim at improving crisis and consequence management through the identification of best practices in member states as well as coordination at EU level.

While certainly useful in themselves, evaluations of the implementation of CTF principles and guidelines are no substitute for examinations of the impact on terrorism. It can be plausibly argued that a low outcome effectiveness of CTF, such as poor coordination among relevant agencies, or gaping loopholes in ‘know your customer’ provisions, could be a factor in making terrorist attacks possible, the opposite argument, however, namely that with better implementation attacks would decrease, cannot be assumed without evidence. It needs to be made via impact assessments.

Furthermore, output and outcome assessments cannot answer the question of how much of CTF is optimal, where marginal costs meet marginal returns. Among approaches to fight terrorism, they cannot establish the importance of CTF in countering terrorism. They are built on the assumption that CTF is important.

### **Cost of CTF as counterbalance?**

The argument advanced here is that the emphasis on output and outcome measures in most CTF assessments tends to lead to an expansion of CTF measures. However, the argument needs to be qualified by a brief look at potential counterbalancing forces against such expansion. The most important restriction to expansion of CTF are the costs of CTF measures. CTF has a variety of costs, among which four types have received particular attention, namely the costs to the financial sector, higher transaction costs and the – intangible – cost to data protection and civil rights.

1. No good data are available on the cost of CTF provisions for the financial sector (Yeandle et al 2005, pp. 23-35; Sathye 2008). Banks tend to claim that the costs are high (House of Lords 2009; Geiger and Wuensch 2007) but they also tend to accept without much opposition or efforts at influencing policy makers. This may have to do with distributive effects. CTF costs tend to decrease with the size of financial institutions, so that CTF regulation favors larger over smaller financial institutions. There are also some concerns with international competition. CTF costs tend to be higher in some countries, such the UK, than others, such as Switzerland (House of Lords 2009).
2. Increased transaction costs have particularly been debated with respect to traditional and wire money transfer systems such as the Hawala system. It has been claimed that the restrictions and additional information requirements put on these systems have been harmful for economic development particularly among the poorest who do not normally have access to the banking

sector (DeGoede 2003; Vlcek 2007; Warde 2007; Warde 2007). Some programs were adopted by development assistance agencies to lower transaction costs for poor people, but, information requirements have not been changed.

3. The most intense public debate is on the relationship between CTF and data protection. CTF, through SARs and the availability of private data on financial transactions and assets to public authorities in FATF-style CTF legislation, is an intrusion into privacy. In Europe, such intrusion requires a legal order, against which legal redress is possible<sup>14</sup>. The US has a different legal culture, where the data protection rights are more limited. This became a celebrated issue in the “SWIFT” affair.

In 2006 it leaked that an interbank cooperative subject to Belgian law had transferred data on financial transactions to the US government without consent of its customers. The Society of Worldwide Interbank Financial Telecommunications (SWIFT), register in La Hulpe, Belgium, daily processes an average of 12 million financial messages. The data was stored, until late 2009, in two mirror sites, one in the US and the other in Belgium. In 2002, under its Terrorist Financing Tracking Program, the US government began to issue subpoenas to SWIFT to allow the access to the data. SWIFT concurred after informing the National Bank of Belgium, which is overseeing SWIFT, but without consulting data protection authorities. The undisclosed transfer of data to the US, in the absence of the possibility legal redress, occurred in violation of Belgian and EU data protection regulations. When the information was published it led to a public outcry, reinforced by strong statements by European institutions as well as most EU member governments. There also was an uproar among companies in Europe, who had suspicions that the information was used for commercial purposes (Gonzalez et al 2008).

Council and Commission engaged in discussions with the US government which resulted in a series of changes in the data transmission. In particular, the US agreed to accept that a French Judge, Jean-Louis Broguière, would verify that data was only transmitted in legitimate cases. However, in 2009 SWIFT decided to change its architecture, and not to store EU-related data in the US any more. The US therefore requested the EU to negotiate an international agreement that would allow the US continued access to relevant data now solely stored in Europe. A first treaty, providing for transfer of almost all data to the US was rejected by the European Parliament in early 2010 (European Parliament, 2010). An amended version, valid only for an interim period until SWIFT itself could identify relevant records in its data base, entered into force in mid-2010. It also gives Europe the task of verifying whether a US request has the exclusive purpose of

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<sup>14</sup> Based on the ‘Warsaw convention’ of the Council of Europe, properly called the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism.

obtaining data necessary for the prevention, investigation, detection or prosecution of terrorism or terrorist financing (Council 2010b).

4. The preemptive nature of some of the CTF provisions is in contradiction to basic rights as enshrined in EU legislation (Bothe 2008). After initial hesitation, courts in Europe, such as the European Court of Justice in the Kadi and Al-Barakat cases are now increasingly finding it unlawful that there is no legal redress against asset freezes. The EU has responded by introducing new ways for persons affected by CTF measures to put their arguments forward. But up to now, the EU has found it more pertinent to implement the relevant UN resolutions than to follow the courts and has for instance in the Kadi case rephrased and reiterated the asset freeze (De Burca 2009).

CTF policies have been shaped by their financial and non-financial costs. Actors such as bankers, lawyers and accountants have argued against particular CTF measures. This has slowed the implementation of CTF regulations (Thony and Png, 2009). However, different from international institutions propagating CTF rules and standards, they have rarely initiated or conducted evaluations (for one such example see: xxx).

### **Effectiveness and CTF policy in Europe**

The analysis indicates that assessments of effectiveness and efficiency have shaped EU CTF policy. International organizations, in particular the FATF but also the UN CTC and the EU have used evaluations of national CTF practices to further standardize procedures and institutions.

International assessments of national CTF policies and their implementation are a core element of international CTF policy. Assessments have been plentiful but have overwhelmingly been performed with the objective to identify gaps in the implementation of laws and agreements. Yardsticks very often are 'best practices' that is particularly comprehensive and well resourced ways of implementing.

Such assessments have legitimacy and functionality. Evaluations, however, have had a particular bias towards expanding the scope and intensity of CTF regulations and implementation. They have focused on outcome and output of internationally agreed CTF policies. There has been less consideration of impact, whether measures actually reduced terrorism. Such assessments cannot substitute evaluations of the effectiveness and efficiency of CTF in terms of deterring, preventing and tracking terrorist attacks as guidepost for prioritizing policies. Rather, they carry the danger, that policies are extended beyond what can be defended on the basis of their impact and cost-benefit ratios.

Such bias towards CTF expansion is much in line with the predictions of risk politics mentioned above. In particular powerful states have a panoptical tendency to expand their activities (Levi 2010,

p. 661). Levi has rightly written that “Currently, it remains largely a matter of faith in assertions by those in authority rather than on published evidence that anti-terror financial intelligence efforts have some impact beyond the immediate operation outcomes” (Levi 2010, p. 662).

The initial push for expanding CTF in Europe, which has a longer tradition, came from the United States after 9/11. But, the EU took up this issue with verve, partly driven by terrorist acts in Europe such as the March 2004 Madrid bombings (even though financing had little role there). In fact, the EU Third Money Laundering Directory of 2005 is, in some respect, more expansive than similar regulations in other countries, including the US and Australia. For instance, lawyers for the most part do not have anti-moneylaundering responsibilities beyond base Know Your Client rules (Levi 2010, p. 655). On the other hand, privacy laws are more restrictive in Europe than the US which led to some modifications in CTF financing practices in Europe contrary to wishes of the US government. Still, the amount of data gathering and data mining in the field of CTF, often without knowledge of affected persons, are extensive (Balzacq 2008; Parker and Taylor 2010).

The paper has demonstrated that evaluations have been an important instrument in expanding CTF activities by focusing on a particular concept of effectiveness – the comprehensiveness of a CTF framework and its implementation. Such assessments, often based on best-practice models, are used to lobby and pressure governments and financial sectors into adopting and implementing broader CTF approaches.

Costs of CTF have, to some extent, counterbalanced the trend towards extension of CTF measures. However, the arguments brought forward against such extension generally are rarely based on assessments of the impacts of CTF measures. Thus despite intense debate about particular CTF measures, such as suspicious transaction reports, or data provision to the US, there is little knowledge on whether CTF measures are cost effective at the margin.

Table 1: Direct costs of terrorist attacks and source of financing

<i>Location</i>	<i>Year</i>	<i>Cost estimate</i>	<i>Financing source</i>
<i>Nairobi/ Daressalam</i>	1998	€50.000	Externally financed (Al-Quaida), transfer by courier
<i>New York, Washington</i>	(9/11) 2001	€300.000- 370.000	Externally financed (Al-Quaida), transfer by wire
<i>Bali</i>	2002	€50.000	Self and externally financed (Al-Quaida), transfer by courier
<i>Casablanca</i>	2003	€4.000	Self financed
<i>Istanbul</i>	2003	€30.000	Self financed (criminal activities)
<i>Jakarta</i>	2003	€30.000	Self financed (band robbery)
<i>Madrid</i>	(11/3) 2004	€10.000	Self financed (drug trade)
<i>London</i>	(7/7) 2005	€12.000	Self financed, credit
<i>Köln (failure)</i>	2006	€500	Self financed
<i>Istanbul</i>	2008	€10.000	Self and externally financed

Table 2: FATF Recommendations

- I. Ratification and implementation of UN instruments
- II. Criminalizing 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 organizations

Source: FATF 2008

Table 3: Suspicious activity reports (SAR), select European countries 2009

	<b>UK</b>	<b>Germany</b>	<b>Switzerland</b>	<b>Sweden</b>	<b>Spain</b>	<b>France</b>
<b>SAR</b>	240582	9046	896	9137	2904	18104

Sources: Serious Organized Crimes Agency, 2010;

<http://www.fedpol.admin.ch/content/fedpol/de/home/dokumentation/medieninformationen/2010/2010-04-08.html>, Finanspolis 2010

[http://www.sourcews.fr/lutte-anti-blanchiment-tracfin-publie\\_6c15a](http://www.sourcews.fr/lutte-anti-blanchiment-tracfin-publie_6c15a), Bundeskriminalamt 2010

Table 4: Share of suspected terrorism financing in suspicious transaction reports, Germany 2002-2009

	<b>15.08. 31.12.02</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>SAR</b>	2,271	6,602	8,062	8,241	10,051	9,080	7,349	9,046
<b>suspected “financing of terrorism”</b>	90	127	114	104	59	90	65	98

Source: Bundeskriminalamt 2010.

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