2004

Panel One: Unfunding Terror--Perspectives on UnfundingTerror: Commentary

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Panel One: Unfunding Terror—Perspectives on Unfunding Terror*

Commentary by Michael P. Malloy**

This panel is intended to examine certain U.S. and multilateral responses to the terrorist attacks against the United States on September 11, 2001 that were specifically designed to deny terrorists access to financial resources. We are concerned primarily with two types of response—the blocking of assets in which a terrorist has a direct or indirect interest[1] and prohibitions against money laundering[2]—as well as more general prohibitions against the provision of resources to terrorists.[3]

I. INTRODUCTION

The tragic events of September 11, 2001 remain difficult to comprehend at a human level, but the legal and policy effects of these events are beginning to unfold. It is already clear the sanctions program will have significant implications for economic sanctions theory and techniques, and it also raises important issues for administrative law and practice, for global technology, and for public international law and international regulation of trade and finance. By way of an introduction to the issues, I would like to focus on the implications for economic sanctions theory and on the effects on transborder banking activities.

 Portions of this essay are drawn from the author's forthcoming book, PRINCIPLES OF BANK REGULATION (Concise Hornbook Series, 2d ed., Thomson West 2003).

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1. *See, e.g.*, Exec. Order No. 13,224, §§ 1-2, 66 Fed. Reg. 49,079 (Sept. 23, 2001) (blocking property of and prohibiting transactions with terrorists or persons supporting terrorism) [hereinafter Exec. Order No. 13,224); S.C. Res. 1373, U.N. SCOR, 4385th Sess., at 1(c), U.N. Doc. S/RES/1373 (2001), *reprinted in* 40 INT'L LEGAL MAT. 1278 (2001) (mandating "freeze" without delay of funds and other financial assets or economic resources of terrorists and other participants and facilitators) (hereinafter Resolution No. 1373).

2. *See, e.g.*, Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. L. 107-56, Oct. 26, 2001, 115 Stat. 280 (codified at scattered sections of, *inter alia*, 12, 18, 31 U.S.C.) [hereinafter USA PATRIOT Act]; Resolution No. 1373, *supra* note 1, § 4 (emphasizing need to enhance coordination of efforts on national, subregional, regional and international levels against "transnational organized crime, illicit drugs, money-laundering, illegal arms-trafficking, and illegal movement of nuclear, chemical, biological and other potentially deadly materials").

3. *See, e.g.*, Exec. Order No. 13,224, *supra* note 1, § 6 (calling for bilateral and multilateral cooperation and coordination to deny financing and financial services to terrorists and terrorist organizations); Resolution No. 1373, *supra* note 1, §§ 1(a)-(b), (d), 2(c)-(e), 5 (mandating prevention and suppression of financing of terrorist acts, criminalizing willful provision or collection of funds to carry out terrorist acts, prohibiting provision of "funds, financial assets or economic resources or financial or other related services" for benefit of terrorists or persons facilitating or participating in terrorist acts; declares knowing financing of terrorist acts to be "contrary to the purposes and principles of the United Nations").

II. PRESIDENTIAL EMERGENCY AUTHORITY

The President had already taken a number of dramatic steps in response to the terrorist attack, including military activity, diplomatic overtures, and domestic political initiatives before the establishment of formal sanctions. On September 14, 2001, the President issued Presidential Proclamation No. 7463,[4] declaring a national emergency with respect to the attacks, and indicating his intention to invoke statutory authorities to activate national emergency military reserves and to recall personnel to active duty. At that stage, however, the President's action did not expand the U.S. economic sanctions that were in place since the second half of the 1990s against the assets of terrorists[5] and against the Taliban regime in Afghanistan.[6]

This situation rapidly changed. On September 23, 2001, the President issued Executive Order No. 13,224,[7] "blocking the property of, and prohibiting transactions with, persons who commit, threaten to commit, or support terrorism." Invoking such authority as the International Emergency Economic Powers Act (IEEPA),[8] section 5 of the United Nations Participation Act (UNPA),[9] and various U.N. Security Council Resolutions, the order declared a national emergency to deal with the "unusual and extraordinary threat to the national security, foreign policy, and economy of the United States," posed by the terrorist attacks.[10]

Had this been all that the preamble of the order said, it would have read like countless other executive orders declaring national emergencies issued by presidents since the IEEPA was enacted in December 1977.[11] Blocking of

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4. Declaration of National Emergency by Reason of Certain Terrorist Attacks, 66 Fed. Reg. 48,199 (Sept. 14, 2001).

5. *See, e.g.*, Exec. Order No. 12,947, 60 Fed. Reg. 5079 (Jan. 23, 1995) (prohibiting transactions with terrorists who threaten the Middle East peace process); Terrorism Sanctions Regulations, 31 C.F.R. pt. 595 (implementing Exec. Order No. 12,947). *See also* Terrorism List Government Sanctions Regulations, Foreign Terrorist Organizations Sanctions Regulations, 31 C.F.R. pt. 596 (implementing section 321 of Antiterrorism and Effective Death Penalty Act of 1996 (AEDPA), 18 U.S.C. § 2332d); Foreign Terrorist Organizations Sanctions Regulations, 31 C.F.R. pt. 597 (implementing sections 302-303 of AEDPA, 8 U.S.C. § 1189, 18 U.S.C. § 2339B). On the relationship between the successive antiterrorism sanctions programs, *see* Holy Land Found. for Relief and Dev. v. Ashcroft, 333 F.3d 156 (D.C. Cir. 2003) (upholding validity of successive designations of charitable organization and blocking of assets); Global Relief Found., Inc. v. O'Neill, 315 F.3d 748 (7th Cir. 2002) (upholding blocking of assets).

6. Exec. Order No. 13,129, 64 Fed. Reg. 36,759 (July 4, 1999) (imposing economic sanctions against Taliban).

7. Exec. Order No. 13,224, 66 Fed. Reg. 49,079.

8. IEEPA, 50 U.S.C.A. §§ 1701-1706. For discussion of the IEEPA as a statutory source of economic sanctions authority, *see* MICHAEL P. MALLOY, UNITED STATES ECONOMIC SANCTIONS: THEORY AND PRACTICE 171-86 (2001).

9. UNPA, 22 U.S.C.A. § 287(c). For discussion of UNPA as a statutory source of economic sanctions authority, *see* MALLOY, *supra* note 8, at 162-70.

10. Exec. Order No. 13,224, 66 Fed. Reg. at 49,079.

11. *See, e.g.*, 50 U.S.C.A. § 1701, *supra* note 8 (reproducing executive orders issued under IEEPA).

terrorist assets certainly resulted from the order,[12] but the order went on to find that "because of the pervasiveness and expansiveness of the financial foundation of foreign terrorists, financial sanctions may be appropriate for those foreign persons that support or otherwise associate with these foreign terrorists."[13] It also found that "a need exist[ed] for further consultation and cooperation with, and sharing of information by, United States and foreign financial institutions as an additional tool to enable the United States to combat the financing of terrorism."[14] With these two findings—and the substantive steps that the order took in response—the President' initiative was transformed into one of the most creative and savvy approaches to the use of economic sanctions in the past ten years (*i.e.*, since the original Iraq sanctions imposed by the President's father[15]), and possibly the past twenty years (*i.e.*, since the original Iran hostage sanctions of 1979-1981[16]).

III. SANCTION STRATEGY

The strategy of the new executive order is distinctive at a number of levels. The new sanctions program intimately and explicitly ties the imposition of sanctions to a broader array of foreign policy and military responses. For example, section 6 of the

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12. *See O'Neill Says $24 Million in Assets Frozen as Part of U.S. Response to Terrorist Attacks*, BNA INT'L BUS. & FIN. DAILY, Oct. 15, 2001, at d3; *Cf.* Toshio Aritake, *Japan Freezes $750,000 in Assets of Taliban, Affiliates, Ministry Says*, BNA INT'L BUS. & FIN. DAILY, Oct. 23, 2001, at d2.

13. Exec. Order No. 13,224, 66 Fed. Reg. at 49,079.

14. *Id.* In fact, cooperation swiftly emerged from close allies such as Japan (*see* Eric J. Lyman & Diana I. Gregg, *Japan Takes Steps to Find, Freeze Assets of Taliban, Osama Bin Laden, Other Groups*, BNA INT'L BUS. & FIN. DAILY, Sept. 25, 2001, at d3), the United Kingdom (*see* Patrick Tracey, *U.K. Law Boosts Crackdown on Terror Cash, Foreign Bribes*, BNA BANKING DAILY, Nov. 15, 2001, at d7), and the G-7 countries (*see* Nancy Ognanovich, *Finance Ministers Back U.S. Plan Aimed at Freezing Terrorists' Assets*, BNA INT'L BUS. & FIN. DAILY, Apr. 23, 2002, at d8). Vigorous cooperation even emerged from the European Union. *See EU Moving Against Bin Laden-Related Funds, Requests Supporting Evidence from Treasury*, BNA BANKING DAILY, Oct. 1, 2001, at d2; Arthur Rogers, *EU Asset-Freezing Plan Rushed Through European Parliament with Minimal Dissent*, BNA BANKING DAILY, Oct. 5, 2001, at d4; Joe Kirwin, *European Commission Provides Legal Basis For Freezing Suspected Terrorist Bank Assets*, BNA INT'L BUS. & FIN. DAILY, Oct. 15, 2001, at d2; Joe Kirwin, *EU Leaders Reaffirm Support For U.S., Outline Efforts to Combat Terrorism*, BNA INT'L BUS. & FIN. DAILY, Oct. 22, 2001, at d2. *But cf.* Andrew M. Ballard, *European Parliament Says EC Dragging Feet on Terrorist Asset Freezing, Laundering Bill*, BNA BANKING DAILY, Oct. 25, 2001, at d4; Nancy Ognanovich, *EU Officials Evaluating Bush Call For 50-Step Plan to Fight Terrorism*, BNA BANKING DAILY, Oct. 29, 2001, at d2. Some indications of cooperation even arose in Saudi Arabia. *See Saudi Government Joins U.S. in Freezing Terror-Linked Fund*, BNA INT'L BUS. & FIN. DAILY, Mar. 12, 2002, at d2.

15. Exec. Order No. 12,722, 55 Fed. Reg. 31,803 (Aug. 2, 1990) (imposing sanctions against Iraq and occupied Kuwait under IEEPA); Exec. Order No. 12,724, 55 Fed. Reg. 33,089 (Aug. 9, 1990) (conforming U.S. sanctions to requirements of U.N. Security Council Resolution 661; invoking IEEPA and UNPA). For discussion of U.S. and U.N. sanctions against Iraq in response to the invasion of Kuwait, *see* MALLOY, *supra* note 8, at 555-607.

16. Exec. Order No. 12,170, 44 Fed. Reg. 65,729 (Nov. 14, 1979) (blocking Iranian Government assets); Exec. Order No. 12,205, 45 Fed. Reg. 24,099 (Apr. 7, 1980) (imposing trade embargo on Iran); Exec. Order No. 12,211, 45 Fed. Reg. 26,685 (Apr. 17, 1980) (expanding sanctions against Iran). For discussion of the 1979-1981 U.S. sanctions against Iran in response to the hostage taking, *see* MALLOY, *supra* note 8, at 90-98.

order immediately triggered consultation and coordination with other countries to achieve the objectives of the order.[17] Furthermore, the order stated the declaration of the emergency (and hence the imposition of sanctions) was "in furtherance of [the] proclamation" activating the military reserves.[18] As in the case of the Iraq sanctions, therefore, the economic response was intended—but this time explicitly so—to be only one phase in what would eventually involve military or police action as well.

In addition, the Administration found a way to sidestep—or at least to blunt—the issue that is typically raised by U.S. allies and critics alike against the application of U.S. economic sanctions, namely that they are impermissibly extraterritorial in effect. The premise underlying this program is that, in response to "universal" criminal acts (terrorism, like piracy, crimes against humanity, and wars of aggression, is subject to criminal enforcement regardless of where it takes place), the President called upon other states to identify and freeze terrorist-related assets under their own authority. If a state did not take appropriate action, it may trigger the "vicarious" or "accessory" liability principle that the President has enunciated elsewhere (*e.g.*, in his speech to the joint session of Congress following the terrorist attacks). The President might sanction such states for their active or passive participation in a "universal" crime.

IV. U.N. SECURITY COUNCIL ACTION

On Friday, September 28, 2001, following fast upon the heels of these presidential actions, the U.N. Security Council unanimously adopted the U.S.-sponsored Resolution No. 1373, requiring all U.N. member states to sanction the financing, training and movement of terrorists, and requiring their cooperation in any campaign against terrorists, including military action. In effect, the resolution completely vindicates the declarations of the executive order: that terrorism was indeed an unusual and extraordinary threat; that the pervasiveness and expansiveness of the financing of terrorists made sanctions against foreign persons "support[ing] or otherwise associat[ing] with" terrorists appropriate; and that consultation and cooperation with, and sharing of information by, U.S. and foreign financial institutions was necessary to combat terrorism.

The U.N. sanctions required the immediate freezing of the financial resources of terrorists and their organizations. Once fully implemented by the member states, the U.N. sanctions also would include required efforts to prevent and suppress terrorism, prohibitions against making funds available to terrorist organizations, and the suppression of recruitment by such organizations and the elimination of their weapon supplies. In addition, the member states were required to deny safe havens to anyone who finances, plans, supports, or commits terrorist acts, or who provides safe havens to terrorists. They were also

17. Exec. Order No. 13,224, § 6, 66 Fed. Reg. at 49,081.

18. *Id.* at 49,079.

committed to providing assistance in criminal investigations of terrorism and to preventing the movement of terrorists and terrorist groups through more effective control over borders and travel documents.

However, some gray areas exist in the resolution, particularly in comparison with the immediate U.S. response. For example, section 3(d) of the order defines *terrorism* as an activity that involves a violent act or an act dangerous to human life, property, or infrastructure and *appears to be* intended to intimidate or coerce a civilian population, to influence the policy of a government by intimidation or coercion, or to affect the conduct of a government by mass destruction, assassination, kidnapping, or hostage-taking. Section 1(a)-(d) of the order describes the kinds of persons considered to be *terrorists*, and an annex to the order listed twenty-seven individuals and organizations identified by the order as terrorists or supporters of terrorism. In contrast, the U.N. resolution does not define or otherwise explain who is a terrorist. In addition, while the order invokes the necessary U.S. statutory authority—the IEEPA and the UNPA—for immediate imposition of the sanctions, the current national laws of the other 188 U.N. member states did not uniformly provide authority for implementation of the terms of the resolution. Hence, the exact contours of the multilateral response to terrorism remained relatively fuzzy for a considerable period of time, as member states took action to align their national laws with the requirements of the resolution.[19]

V. USA PATRIOT ACT

The final corner piece of the puzzle emerged on October 26, 2001, when the President signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001.[20] Usually referred to by its acronym, USA PATRIOT Act. The act is a multi-pronged legislative response to the terrorist attacks. While the USA PATRIOT Act is much broader than the anti-money laundering provisions of Title III, Title III accounts for approximately one-third of the entire text of the Act and will probably have long-term compliance implications far beyond the immediate terrorism crisis.[21] The provisions in Title III, the International Money Laundering

19. For country reports on implementation and other documentation concerning the work of the Counter-Terrorism Committee established by Resolution No. 1373, *see* http://www.un.org/docs/sc/committees/1373/top.htm.

20. USA PATRIOT Act, *supra* note 2.

21. Although the act may be terminated under the joint congressional resolution procedure in § 303, as of the beginning of fiscal year 2005, this seems an unlikely outcome in the current political climate. As yet, there has been no significant litigation concerning Title III. *See generally* L & J Crew Station, LLC v. Banco Popular de Puerto Rico, 278 F. Supp. 2d 547, 560 (D.V.I. 2003) (holding, *inter alia*, that USA PATRIOT Act did not provide basis for private cause of action on behalf of depositor); Med. Supply Chain, Inc. v. US Bancorp, NA, C F. Supp. 2d C, 2003 WL 21479192, at 6-8 (D. Kan. 2003) (holding, *inter alia*, that bank customer lacked standing to bring claim against bank holding company based upon USA PATRIOT Act, and that no private right of action existed under Act).

Abatement and Anti-Terrorist Financing Act of 2001 (IMLAAFA), most directly affect financial services firms. For example, under section 327, a financial institution's effectiveness in combating money-laundering has now become an explicit factor in considering approval of bank holding company status[22] or approval of a bank or savings association merger under the Bank Merger Act.[23]

The effects of IMLAAFA go well beyond the policing of classic money laundering transactions, and must be kept in mind even in situations where such transactions may not be apparent. In addition, IMLAAFA includes extensive amendments[24] to the Bank Secrecy Act[25] and related provisions of federal law. These are apparently intended to align reporting, disclosure, and money laundering requirements of the previous enactments to the provisions of the new act.

Under section 311,[26] the Secretary of the Treasury is authorized to designate non-U.S. jurisdictions, classes of transactions, financial institutions, or types of accounts as being of "primary money laundering concern."[27] As to any of these designated non-U.S. targets, the Secretary can require domestic financial institutions and domestic financial agencies to take at least one of the following five types of specified measures to detect and prevent money laundering: (1) recordkeeping and reporting of certain financial transactions; (2) obtaining and retaining information concerning beneficial ownership of any targeted account; (3) identifying, or obtaining identity information about, persons permitted to use, or whose transactions are routed through, certain "payable-through" accounts; (4) identifying or obtaining identity information about persons permitted to use, or whose transactions are routed through, certain correspondent accounts; and/or (5) prohibiting or conditioning the opening of certain payable-through or correspondent accounts.

Under section 312,[28] financial institutions are required to establish "appropriate, specific, and, where necessary, enhanced, due diligence policies, procedures, and controls" as to money laundering for U.S. correspondent accounts and private banking accounts of non-U.S. persons (*including* a foreign individual visiting the United States, or a U.S. representative of a non-U.S. person). Furthermore, if a foreign bank with an "offshore" banking license, or licensed by a country designated as "noncooperative" by certain intergovernmental organizations (*e.g.*, the Paris-based Financial Action Task Force on Money Laundering), requests or maintains a correspondent account with a U.S. financial institution, the latter is

22. 12 U.S.C.A. § 1842(c)(6) (West 2004).

23. *Id.* § 1828. *See, e.g.*, FDIC Statement of Policy on Bank Merger Transactions, 67 Fed. Reg. 48,178 (July 23, 2002) (amending Statement of Policy to incorporate USA PATRIOT Act requirement).

24. USA PATRIOT Act, *supra* note 2, at 351-359, 361-363, 365-366, 371-372.

25. 31 U.S.C.A. § 5311 *et seq.* (West 2004).

26. *Id.* § 5318A.

27. In this regard, *see* Treasury Department, Notice, Departmental Offices Designation of Nauru and Ukraine as Primary Money Laundering Concerns, Notice, 67 Fed. Reg. 78,859 (2002).

28. 31 U.S.C.A. § 5318(i).

required to establish additional due diligence standards. These include ascertaining the identity of each owner of the foreign bank (if the foreign bank is not publicly traded) and ascertaining the identities of other foreign banks that maintain correspondent accounts with the foreign bank, as well as related due diligence information. Finally, special due diligence requirements are imposed for "private banking accounts." These include ascertaining the nominal and beneficial owners of each account and the source of the funds deposited in such accounts, and enhanced scrutiny of accounts maintained by senior political figures, or their immediate families or close associates.

Under section 313,[29] "covered financial institutions" are prohibited from maintaining correspondent accounts for shell banks—banks with no physical presence in any country—and must take reasonable steps to ensure that correspondent accounts of foreign banks are not used to provide banking services to shell banks. A covered financial institution that maintains a correspondent account in the United States for a foreign bank must maintain records in the United States identifying the owners of the foreign bank and the name and address of any U.S. resident who is authorized to accept service of legal process from the Secretary and the Attorney General for records regarding the correspondent account.

Under section 325,[30] the Secretary is given authority to issue rules regulating the maintenance of concentration accounts[31] by financial institutions, to ensure that these accounts are not used to mask the interest of any person in the movement of funds. These regulations must, at a minimum: (1) prohibit financial institutions from allowing clients to direct funds movements in, out, or through such accounts; (2) prohibit institutions and their employees from counseling clients about such accounts; and, (3) require each institution to establish specified written procedures on documentation of transactions involving concentration accounts.

The key terms of reference under the IMLAAFA raise a variety of terminological questions that affect the scope of many of the substantive requirements imposed by the act. Many of these questions are, of course, specifically addressed by IMLAAFA itself, typically by crossreference to preexisting statutory definitions. For example, under section 318[32] the term "financial institution," used throughout IMLAAFA, is defined by reference to the term as defined in the Bank Secrecy Act (BSA).[33] There the term includes most financial entities, such as commercial banks, savings associations, credit unions (added by IMLAAFA section 321[34]),

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29. *Id.* § 5318(j).

30. *Id.* § 5318(h)(3).

31. The term "concentration account" is not defined by the IMLAAFA. Legislative history of the USA PATRIOT Act seems to suggest that concentration accounts "are used to commingle related funds temporarily in one place pending disbursement or the transfer of funds into individual client accounts." 147 Cong. Rec. S11,041 (Oct. 25, 2001) (statement of Sen. Sarbanes).

32. 18 U.S.C.A. § 1956(c)(6) (West 2004).

33. 31 U.S.C.A. § 5312(a)(2).

34. *Id.* § 5312(a)(2)(E).

broker-dealers, insurance companies, and money transmitters, among others. In addition, IMLAAFA section 318 includes U.S. branches and agencies of foreign banks in the term.

A similar—but, significantly not coterminous—concept, "covered financial institution," is key to the shell bank provisions of IMLAAFA section 313[35] and the bank records provisions of section 319.[36] For purposes of section 313, the term is defined to include only certain selected financial institutions described in the BSA.[37] These include commercial banks, savings associations and other depository institutions, branches and agencies of foreign banks, and broker-dealers registered under the Securities Exchange Act of 1934. It is not apparent that the term is so limited for purposes of the bank records provisions. Likewise, IMLAAFA incorporates the BSA definition of "financial agency." This term includes any person acting for another as a financial institution, bailee, depository trustee, or agent, or acting in a similar way relating to financial assets or gold, or a transaction involving any of these.

The breadth of coverage of the act—applying as it does not just to banks, but to a wider range of financial institutions—creates its own terminological difficulties. Certain operative terms are defined differently for different types of institutions. For example, for banks section 311[38] defines "account" as a formal banking or business relationship established to provide regular services, dealings and other financial transactions. The term expressly includes demand deposits, savings deposits and other transaction or asset accounts or extensions of credit. However, for other institutions section 311 requires the Secretary to define the term by regulation, after consultation with the appropriate federal functional regulators. In this regard, the Secretary is required to include within the definition—to the extent, if any, that the Secretary deems appropriate—arrangements similar to payable-through and correspondent accounts. The act does not reveal what sort of accounts these might be.

Similarly, section 311 defines "correspondent account" in different ways for banks and other financial institutions. For banks, the term is defined as an "account" established to receive deposits from, to make payments on behalf of, or handle other financial transactions related to, a foreign financial institution. (It is not clear from the act itself what "other" transactions are intended.) For other financial institutions, it is the Secretary's responsibility to determine the extent to which "arrangements similar to . . . correspondent accounts" are to be included within the definition. The possible discontinuity in the meaning of this term is potentially significant. For example, four key sections of the IMLAAFA—section 311 (measures against "primary money laundering" targets), section 312[39] (special

35. *Id.* § 5318(j).
36. 18 U.S.C.A. § 981(k) (West 2004).
37. 31 U.S.C.A. § 5312(a)(2)(A)-(G).
38. *Id.* § 5318(a).
39. *Id.* § 5318(i).

due diligence requirements), section 313 (foreign shell bank prohibitions) and section 319 (forfeiture of funds in U.S. interbank accounts)Ball apply to "correspondent accounts," and this fact makes the scope of the definition of the term critical to effective implementation of the IMLAAFA.

The same potential discontinuity exists for the term "payable-through account." For banks, section 311 defines the term to mean an account opened at a depository institution by a foreign financial institution, by means of which the foreign financial institution permits its customers to engage, directly or through a subaccount, in banking activities in the United States. Again, for other financial institutions, it is the Secretary's responsibility to determine the extent to which "arrangements similar to payable-through . . . accounts" are to be included within the definition.

Other provisions of the IMLAAFA raise analytical issues on their own terms. For example, section 312 creates a continuum of "enhanced," "additional," and "special" due diligence requirements that are applicable, under varied circumstances specified in the section. The "enhanced" due diligence requirements apply to financial institutions maintaining U.S. correspondent accounts and private banking accounts of non-U.S. persons. The "additional" requirements apply to accounts maintained for foreign banks with "offshore" banking licenses or licenses from countries designated as "noncooperative." The "special" requirements apply to private banking accounts. What is not clear from the text of the act is where each of these types of due diligence ends and the next begins. Nor is it clear to what extent these requirements overlap in their specifics.

Section 313 prohibits "covered financial institutions" from maintaining correspondent accounts for "shell banks"—banks with no physical presence in any country—and requires "reasonable steps" to be taken by institutions to ensure that correspondent accounts of foreign banks are not used to provide banking services to shell banks. What these steps may be, and how to assess their reasonableness, are still open questions under the IMLAAFA. Presumably, compliance issues like these may be clarified by provisions such as IMLAAFA section 314,[40] which encourages bank regulators and law enforcement agencies to share information with financial institutions.[41]

Certain provisions of the IMLAAFA necessarily require further empirical development before their practical implications will become apparent. For example, under section 311 the Treasury Secretary is authorized to designate non-U.S. jurisdictions, classes of transactions, financial institutions and types of accounts that are of "primary money laundering concern." A progressive delineation of the scope of such provisions will doubtless emerge through administrative implementation over time.

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40. Section 5311, *supra* note 25.

41. *Cf.* Financial Crimes Enforcement Network; Special Information Sharing Procedures to Deter Money Laundering and Terrorist Activity, 67 Fed. Reg. 60,579 (2002) (codified at 31 C.F.R. 103.90, 103.100, 103.110, Appendix A) (implementing USA PATRIOT Act § 314 by encouraging information sharing among financial institutions and federal government law enforcement agencies and among financial institutions).

The level of agency implementation will be significantly increasing in 2002 as proposed and final rulemaking move forward. For example, on December 28, 2001, Treasury published proposed rules[42] to implement section 313 of the IMLAAFA, among other things. The proposal establishes a new part 104 of the Treasury rules. Part 104 will eventually include other regulations implementing the IMLAAFA money laundering provisions for which the Treasury is authorized or required to issue regulations. At this point, however, most of part 104 has been reserved for future regulations.

In fact, in the three-month period ending March 7, 2002, over twenty separate regulatory issuances were published in the Federal Register that dealt with one aspect or another of USA PATRIOT Act implementation. Many of these rulemakings—as well as others that will doubtless follow in due course—will entail the commitment of additional staff, time and resources on the part of financial services firms at least for initial design and initiation of appropriate compliance programs. For example, in February 2002 the SEC published a proposed NASD rule change[43] that would establish an Anti-Money Laundering Compliance Program. In March 2002, the SEC published a proposed NYSE rule change[44] that would establish a corresponding compliance program for the exchange.

Overall, IMLAAFA compliance programs must be in place by April 24, 2002. The compliance burdens are particularly evident with respect to reporting requirements. Proposed rules[45] were published on December 31, 2001, that would require securities broker-dealers to file suspicious activity reports (SARs) with the Treasury's Financial Crimes Enforcement Network (FinCEN) if they believe a customer may be violating U.S. laws or regulations. These proposed rules would implement IMLAAFA section 356.[46] In addition, by July 23, 2002, FinCEN is to develop a secure Web site that financial institutions may use to report suspicious activities. (SARs are currently filed via paper documents.)

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42. Departmental Offices; Counter Money Laundering Requirements—Correspondent Accounts for Foreign Shell Banks; Recordkeeping and Termination of Correspondent Accounts for Foreign Banks, 66 Fed. Reg. 67,460 (Dec. 28, 2001) (to be codified at 31 C.F.R. pt. 104).

43. Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Anti-Money Laundering Compliance Programs, Release No. 34-45457, 67 Fed. Reg. 8565 (Feb. 25, 2002).

44. Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. to Adopt NYSE Rule 445, Anti-Money Laundering Compliance Program, Release No. 34-45487, 67 Fed. Reg. 10,463 (Mar. 7, 2002).

45. Financial Crimes Enforcement Network; Proposed Amendment to the Bank Secrecy Act Regulations—Requirement of Brokers or Dealers in Securities to Report Suspicious Transactions, 66 Fed. Reg. 67,670 (Dec. 28, 2001) (to be codified at 31 C.F.R. pt. 103).

46. 31 U.S.C.A. § 5318, *supra* note 25. Final rules were issued in July 2002. Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Requirement that Brokers or Dealers in Securities Report Suspicious Transactions, 67 Fed. Reg. 44,048 (2002) (codified at 31 C.F.R. 103.11, 103.19) (requiring securities broker-dealers to report suspicious transactions).

Also on December 31, 2001, an interim final rule[47] was published requiring persons in nonfinancial trades or businesses to file reports with FinCEN for transactions in which they receive more than $10,000 in coins or currency in one transaction (or two or more related transactions). The interim rule was effective January 1, 2002, but FinCEN simultaneously published identical proposed rules,[48] with written comments due March 1, 2002. (This simultaneous publication of an "interim" final rule and an identical proposed rule is an increasingly common administrative practice. It is intended to ensure that, even if there is a serious procedural objection to the interim final rule, the substance of the rule could still be preserved by making the proposed rule effective in final form.) An analogous reporting requirement has also been issued in final form by the IRS, effective December 31, 2002.[49]

This section has already highlighted certain significant terminological, analytical, and empirical issues raised by the text of the IMLAAFA.[50] To what extent do the currently available administrative issuances help us resolve these issues?

In many instances, the administrative guidance to date has simply incorporated terminological concepts established in the IMLAAFA. For example, in the December 28th proposed rule, the Treasury incorporated the statutory definition of "covered financial institution," the key to the shell bank provisions of IMLAAFA section 313 and the bank records provisions of section 319. The term is defined to include commercial banks, savings associations and other depository institutions, branches and agencies of foreign banks, and broker-dealers registered under the Securities Exchange Act of 1934.

Among other things, the proposed rule would implement IMLAAFA section 313(a), prohibiting covered financial institutions from providing correspondent accounts to foreign shell banks, and requiring such institutions to take reasonable steps to ensure that correspondent accounts provided to foreign banks are not being used indirectly to provide banking services to foreign shell banks. Under IMLAAFA section 319(b), the proposed rule would also require covered financial institutions that provide correspondent accounts to foreign banks to maintain records of ownership of such foreign banks and their U.S. agents who are designated for service of legal process for records regarding the correspondent account. Additionally, it would require termination of

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47. Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Requirement That Nonfinancial Trades or Businesses Report Certain Currency Transactions, 66 Fed. Reg. 67,680 (Dec. 31, 2001) (to be codified at 31 C.F.R. § 103.30).

48. Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Requirement That Nonfinancial Trades or Businesses Report Certain Currency Transactions, 66 Fed. Reg. 67,685 (Jan. 1, 2001) (to be codified at 31 C.F.R. § 103.30).

49. Amendment to Section 6050I Cross-referencing Section 5331 of Title 31 Relating to Reporting of Certain Currency Transactions by Nonfinancial Trades or Businesses Under the Bank Secrecy Act, 66 Fed. Reg. 67,687 (2001) (codified at 26 C.F.R. pt. 1).

50. *See, e.g.*, text and accompanying notes 28-36 (discussing terminological issues).

correspondent accounts of foreign banks that fail to turn over their account records in response to a lawful request of the Treasury Secretary or the Attorney General.

Some IMLAAFA provisions require Treasury to make some choices about the scope of terms. Thus, IMLAAFA section 311 defined "correspondent account" in different ways for banks and other financial institutions. For banks, the term is defined as an "'account' established to receive deposits from, to make payments on behalf of, or handle other financial transactions related to, a foreign financial institution." For other financial institutions, it is the Secretary's responsibility to determine the extent to which "arrangements similar to . . . correspondent accounts" are included within the definition. When it issued its Interim Guidance in November 2001,[51] the Treasury deferred the question of compliance obligations for securities brokers and dealers with respect to the BSA[52] until after consultation with the SEC. With the regulations proposed on December 28, 2001, the Treasury indicated that it would apply the BSA requirements to brokers and dealers in the same manner that they apply to other covered financial institutions. The Treasury intends to maintain parity of treatment between accounts provided to foreign banks by banks and by broker-dealers, and to treat functionally equivalent accounts—whether maintained by banks or broker-dealers—in the same manner.

Some key terms were not defined in the IMLAAFA itself, and we must look to administrative guidance in this regard. For example, the act did not define the term "foreign bank." Treasury's December 28th proposed rule would define the term to include any organization: (*i*) organized under the laws of a foreign country; (*ii*) engaging in the business of banking; (*iii*) recognized as a bank by the bank supervisory or monetary authority of the country of its organization or principal banking operations; and, (*iv*) receiving deposits in the regular course of its business. "Foreign bank" would also include a branch of a foreign bank located in a territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands. "Foreign bank" would not include an agency or branch of a foreign bank located in the United States or an insured bank organized in a territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands. (These entities are themselves "covered financial institutions" under the act.) In addition, a foreign central bank or foreign monetary authority that functions as a central bank is not a "foreign bank" for these purposes.

Other provisions of the IMLAAFA raise analytical issues on their on terms. For example, IMLAAFA section 312 creates a continuum of "enhanced," "additional," and "special" due diligence requirements that are applicable, under varied circumstances specified in the section. The act does not elaborate on the content of these due diligence obligations; nor is it clear to what extent these

51. Departmental Offices; Interim Guidance Concerning Compliance by Covered U.S. Financial Institutions with New Statutory Anti-Money Laundering Requirements Regarding Correspondent Accounts Established or Maintained for Foreign Banking Institutions, Notice, 66 Fed. Reg. 59,342 (2001).

52. 31 U.S.C.A. § 5318(j)-(k).

requirements might overlap. By April 2002, rules to implement IMLAAFA section 312 should be proposed to address due diligence requirements for financial institutions administering, maintaining, or managing private banks accounts or correspondent accounts covered by the act. Final rules are required to become effective by July 2002.

IMLAAFA section 313(a) prohibited covered financial institutions from maintaining correspondent accounts for "shell banks," and required the taking of "reasonable steps" by institutions to ensure that correspondent accounts of foreign banks are not used to provide banking services to shell banks. The Treasury rules proposed on December 28, 2001 would implement section 313. The rules codify, with some modifications, the Treasury's November interim guidance on the subject. The proposed rules still would not prescribe what constitutes "reasonable steps" under 31 U.S.C. section 5318(j), but it does provide a safe harbor if a covered financial institution uses model certifications in appendices to the proposed rule.[53]

Administrative efforts are still at a relatively early implementation stage, and it will be a while before empirical developments, like the Treasury designations of non-U.S. jurisdictions, classes of transactions, financial institutions and types of accounts that are of "primary money laundering concern" under IMLAAFA section 311, are fully in place. We have begun to see more designations of foreign terrorist organizations[54] pursuant to USA PATRIOT Act section 411(c),[55] but these efforts are only of indirect interest to financial services firms.

Some of these empirical concerns should be eased as interaction between the Treasury and other interested administrative agencies on the one hand and regulated financial services firms on the other continue over time. For example, an interim final rule[56] was published by FinCEN on March 4, 2002, to implement the IMLAAFA section 314 information sharing procedures. The interim rule was effective immediately, but FinCEN simultaneously published an identical proposed rule,[57] with written comments due by April 3, 2002. Such procedures should promote cooperation among financial institutions, regulators, and law enforcement entities in identifying persons who may be involved in terrorism or money laundering.

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53. Appendix A, Appendix B, set forth in Departmental Offices; Counter Money Laundering Requirements—Correspondent Accounts for Foreign Shell Banks; Record Keeping and Termination of Correspondent Accounts for Foreign Banks, 66 Fed. Reg. 67,460 (Dec. 28, 2001) (to be codified at 31 C.F.R. pt. 104).

54. *See, e.g.*, Designation of 39 "Terrorist Organizations" under the PATRIOT Act", Notice, 66 Fed. Reg. 63,620 (2001); Office of the Coordinator for Counter Terrorism' Designation of Foreign Terrorist Organizations, 66 Fed. Reg. 66,492 (2001) (codified at 31 C.F.R. pt. 103).

55. 8 U.S.C.A. § 1189(a) (2004).

56. Financial Crimes Enforcement Network; Special Information Sharing Procedures to Deter Money Laundering and Terrorist Activity, 67 Fed. Reg. 9874 (2002) (codified at 31 C.F.R. pt. 103).

57. Financial Crimes Enforcement Network; Special Information Sharing Procedures to Deter Money Laundering and Terrorist Activity, 67 Fed. Reg. 9879 (Mar. 4, 2002) (to be codified at 31 C.F.R. pt. 103).

VI. Other Implications for Transborder Banking

Whatever the uncertainties about the full legal expanse of the multilateral response to the terrorist attacks, a number of features are clear even now. The implications for transborder banking are obviously serious.

Section 1 of Executive Order No. 13,224 blocks "all property and interests in property" of persons targeted by the order if the property is in the United States or later comes within the United States, or within the possession or control of a U.S. person (which is defined to include a foreign branch of a U.S.-based bank). Presumably, blocked assets would include such items as bank accounts, assets held in trust, and funds in the course of transaction through the banking system. Section 2(a) goes on to prohibit any "transaction or dealing" in blocked assets by any U.S. person or any person within the United States. The blocking applies even if a preexisting contract with respect to the property or transaction requires the U.S. party to perform, and even if the property or transaction was covered by a preexisting license or permit from the U.S. Government.

At first glance, this might seem to be a relatively discrete group of potential bank clients and customers. If so, compliance with the sanctions as applied to transborder banking would be easily sustainable. However, the reach of the order is potentially much broader, and markedly more dynamic. As a result, transborder banking is likely to be burdened by considerable compliance and agency costs. This will have implications for the global technology on which international banking relies.

For example, under section 1(d) of the order, targeted persons include those determined by the Treasury Secretary (in consultation with the Secretary of State, the Secretary of Homeland Defense, and the Attorney General) to be assisting in, sponsoring, or providing financial, material, or technological support for, or financial or other services to or in support of, terrorism or persons listed in the annex or otherwise determined to be subject to the order. Persons may also be blocked if the Secretary determines that they are "otherwise associated with" persons listed or determined to be subject to the order. Taken as an objective test, these provisions dramatically widen the scope of the blocking to include a broad range of *financial intermediaries and other international middlemen—perhaps even banks themselves*. However, for this class of potentially blockable persons, section 5 of the order authorizes the Treasury Secretary to take steps in his discretion short of a complete blocking. This could mean, for example, selective blocking of accounts; reversal of transactions, restrictions on operations, and the like. The history of U.S. blocking programs is replete with such examples.

Equally significant in terms of the effects of the blocking on transborder banking are the provisions of section 1(c) of the order. Targeted persons will also include persons determined by the Secretary of the Treasury (in consultation with the Secretary of State, the Secretary of Homeland Security, and the Attorney General) to be *owned or controlled by*, or *to act for or on behalf of*, any other targeted person. In many, if not most situations, this provision will make it very

difficult for a bank to preplan and monitor compliance with the sanctions, absent prior notice from Treasury.

Prior notice may well be absent, however. Section 10 of the order eliminates the necessity of prior notice of any "listing or determination made" pursuant to the order, at least as to any person who has "a constitutional presence in the United States." The reason for this provision is the President's finding that prior notice to targeted persons might make application of these sanctions "ineffectual," in light of "the ability to transfer funds or assets instantaneously" in the international financial system.

Perhaps even more ominous in terms of compliance burdens and potential liability are the provisions of section 2(b) and (c) of the order. Notwithstanding any preexisting contract or any preexisting license or permit, section 2(b) prohibits any transaction by a U.S. person or within the United States that *evades or avoids*, or *has the purpose of evading or avoiding*, or attempts to violate, any of the prohibitions of the order. Section 2(c) prohibits any conspiracy formed to violate any of the prohibitions of the order. Conspiracy theory has long been a fruitful device in federal enforcement, and there is considerable case law and commentary on the subject. However, what constitutes "avoidance"—as opposed to intentional evasion—of federal prohibitions remains something of a mystery, and hence a dangerous source of potential difficulty for banks operating in the international market. Of course, a bank might be able to show that its involvement in a particular transaction was not initiated with the *purpose* of avoiding the prohibition, yet it might still find itself, objectively speaking, involved in a transaction that in fact *avoided* the prohibitions. This might well be an independent basis for enforcement action against the bank.

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