

NORTHERN ILLINOIS UNIVERSITY

U.S.-Swiss Relations:

**Is the United States fighting terrorist financing operations in
Switzerland to the extent of its power?**

University Honors Program

In Partial Fulfillment of the

Requirements of the Baccalaureate Degree

With University Honors

Department of

Political Science

By

Kathryn M. Green

DeKalb, Illinois

May 2011

University Honors Program

Capstone Approval Page

Capstone Title: (print or type):

U.S. - Swiss Relations:
Is the United States fighting terrorist financing
operations in Switzerland to the extent of its
power?

Student Name (print or type):

Kathryn M. Green

Faculty Supervisor (print or type):

Dr. Daniel Kempton

Faculty Approval Signature:



Department of (print or type):

Political Science

Date of Approval (print or type):

13 May 2011

HONORS THESIS ABSTRACT
THESIS SUBMISSION FORM

AUTHOR: Kathryn M. Green

THESIS TITLE: U.S.- Swiss Relations: Is the United States fighting
terrorist financing operations in Switzerland to the
extent of its power?
ADVISOR: Dr. Daniel Kempton
ADVISOR'S DEPT: Political Science

DISCIPLINE: Political Science

YEAR: 2011

PAGE LENGTH: 15

BIBLIOGRAPHY: pages 19-20

ILLUSTRATED: no

PUBLISHED (YES OR NO): no

LIST PUBLICATION:

COPIES AVAILABLE (HARD COPY, MICROFILM, DISKETTE): hard copy

ABSTRACT (100 - 200 WORDS): see page 1

US-Swiss Relations:
**Is the United States fighting terrorist financing operations in Switzerland to
the extent of its power?**

Kathryn Green
Department of Political Science
Northern Illinois University

Abstract

Switzerland has long been notorious for its acceptance of large, sometimes nefarious banking clients. However, in a world increasingly plagued by multi-millionaire terrorist organizations, that target large numbers of innocent civilians, Switzerland's guaranteed banking secrecy is increasingly called into question. Terrorist financing is one area in which relatively little progress has been made since the September 11 attacks. Terrorist financial networks continue to thrive, funding acts of violence. In the Patriot Act, the United States gave itself increased abilities to follow these financial transactions overseas. Yet it still does not make full use of these new powers. This study examines the funding structure of terrorist organizations. It then assesses the abilities of the United States to neutralize these financial assets. Finally the author assesses whether the United States is utilizing these tools to engage its ally Switzerland in substantially limiting or eliminating terrorist financial action within its borders.

Introduction

Terrorism funds include: *“assets of every kind, whether tangible or intangible, movable or immovable, however acquired, and legal documents or instruments in any form, including electronic or digital, evidencing title to, or interest in, such assets, including by not limited to, bank credits, travelers cheques, bank cheques, money order, shares, securities, bonds, drafts, letters of credit.”*-*The International Convention for the Suppression of Financing of Terrorism*¹

The financing of terrorism was an international concern long before the September 11 attacks. However, the passage of the *Uniting and Strengthening America by Providing Appropriate Tools Required to Interrupt and Obstruct Terrorism Act* (USA PATRIOT Act, hereafter the Patriot Act) brought the discussion of financial regulations to suppress the financing of terrorists and terrorist acts into a sharper light. This paper ascertains how such legislation has impacted the international banking community with a focus on the Swiss banking system.

Tracking the funds that provide terrorists with the ability to carry out their violent acts is plagued by opaqueness, uncertainty, and a web of unconnected transactions. Terrorists who are able to raise funds, “often commingle legitimate with illegitimate sources of funding, the individual parts of the mix becoming not only untraceable to their source, but virtually indistinguishable from each other.”² This variety of methods makes it increasingly difficult for authorities both inside and outside of the United States to track, or follow funds as they move; trace, to follow the path after the funds have moved; and seize funds. The Patriot Act is intended to create an environment of amplified diligence in the controllable portions of the financing network, namely the institutionalized banking system inside the United States and abroad.

Methods and Means: How Terrorists are Funded

In order to understand the exact nature of the problem that the Patriot Act hopes to control, it is necessary to understand how terrorists raise their funds. Fundraising is accomplished in myriad ways, complicated by Islamic religious principles like Zakat. Zakat is one of the five pillars of Islam. It requires adult Muslims of a certain wealth to donate a portion of their income to the less privileged. This amount is carefully calculated according to the Quran.³ Since most faithful Muslims donate to charities, this presents a problem. Charities may funnel this money to violent groups and individuals. In fact, “not only may charitable organizations use their own money to finance terrorist related activities, but they may also serve as a conduit for the transfer of money to finance terrorist activities far afield.”⁴ These organizations can appear quite legitimate on the outset,⁵ and may, in fact be funding actual charitable works as well. In such cases, a certain percentage of funds may be siphoned off the top, causing the majority of raised money to be fulfilling the stated purpose of the charity, while only a small portion may be funding illicit activities.⁶

Another system of terrorism financing is the hawala system. An informal banking system used by Muslims to transfer money without going through formal institutions,⁷ hawala means change or transform. Money is transferred via bills of exchange or promissory notes and hawala functions primarily as a structure for remittances⁸ dependant on close knit, familial networks.⁹ The hawala is by no means the only one of its kind; similar systems also exist in South Asia and China.¹⁰ Today, “the primary users of the hawala system are emigrants in Europe, the Persian Gulf, and North America.”¹¹ The Muslim banking system is especially useful for terrorists because it leaves little trail for authorities to follow,¹² because no money actually moves and the system works incredibly quickly.

Hawala can be used to launder money in three ways: placement; layering; and integration.¹³ Placement solves the problem of large cash transfers. In many countries, reporting requirements will draw attention to such large transfers. Hawala effectively removes this problem, by facilitating such large cash transfers. Layering involves the movement of illicit funds from one account to another until the funds appear legitimate. Such transfers may raise suspicion in a well regulated banking system. The deregulated hawala allows this process to proceed without fear of detection. Integration occurs when terrorist, “invests the money in his legitimate assets, consumes it for pleasure, or reinvests it in illegal activities.”¹⁴ Hawala allows the funds to be easily converted from illicit funds to seemingly legitimate funds, allowing them to be reinvested.¹⁵

Despite the lack of a paper trail, governments still try to regulate hawala. However, “the International Monetary Fund makes the point...that attempts to tightly regulate an informal financial system such as the hawala may not only change the very characteristics of the business that has popularized it—but also may place an additional administrative burden on financial

sector regulations.¹⁶” The United States cannot control what happens inside much of the Muslim world. If the United States sought to decrease use of the hawala system, it would need to make the institutionalized banking system more competitive through decreasing service speed and removing restrictions on the foreign exchange regime.

Terrorists also use feeder accounts, under names of organizations, charities, or businesses and organizational accounts, under the names of anonymous or know trustworthy individuals. These accounts are used to hide where money trails.

Another major method by which terrorists hide money is in commodities. Use of items with physical value, like diamond, gold, and other gems, allows for easy smuggling across borders. This began in late 1998, when the United States froze assets of al Qaeda and the Taliban after the U.S. embassy bombings in Kenya and Tanzania. The frozen assets caused al Qaeda to diversify, in a sense, in order to make up for such financial vulnerabilities. Terrorists may also counterfeit items, using profits to fund terror. In a similar plan, terrorists also use profits from tax evasion through smuggling goods like cigarettes across U.S. state lines. In addition to the above, terrorists can also utilize Islamic banks, diplomatic channels, and personal couriers.¹⁷

The vast range of methods used to transfer money raised and used for terrorist operations means that governments like the United States face serious difficulty in shutting off the funding valve. Rather, the focus must be on putting as many roadblocks as possible in order to make funding terrorists more difficult. The area of money laundering is the area wherein most focus is generally placed.

History of Money Laundering Legislation in the United States

According to the Financial Action Task Force, money laundering is, “the processing of...criminal proceeds to disguise their illegal origin.¹⁸” Most of the original legislation passed in response to the problem of money laundering was intended to combat the problem of national criminal issues.¹⁹ The first law passed was the *Bank Security Act* (BSA) in 1970, also known as the *Currency and Foreign Transactions Reporting Act*.²⁰ However, this has proven difficult and can lead to over-reporting due to the strict liability laws surrounding this type of reporting. Additionally, this law only required reports of cash deposits of over \$10,000. This led to a phenomenon called “smurffing” in which criminals broke up their money into smaller deposits. The regulation then was changed.²¹ The new rules required bankers to determine suspicious activities that must be reported, defined as transfers of monetary instruments (cash, either foreign or domestic, and other monetary items like travelers checks) over \$5,000 in a single transaction.²²

However, these laws and regulations do not apply to the entire financial industry; they only cover transactions by banks: “for instance, Western Union was required to report all

transactions over \$3,000, but unlike banks, was not required to maintain records and tracking data.²³ Further complicating the issue was the backlash against the laws based on the argument of invasion of privacy. The U.S. Supreme Court determined that the BSA was constitutional. Yet, the backlash became the impetus for the *Right to Financial Privacy Act of 1978*.²⁴

The Right to Financial Privacy Act of 1978 specifically stated all the procedures the government and courts must follow when requesting financial information. Such requests could only be made through search warrants, judicial subpoena, or formal written request and the customer in question must be notified. Only in certain specified cases is delay of customer notice permissible. In each case, the customer in question is allowed to challenge the request. In any obtainment of information, the possessor may not turn it over to another agency, except for certain cases and if any transfer occurs, the customer must be notified. The only areas where these stipulations do not apply to requests from government authorities “authorized to conduct foreign counter- or foreign positive-intelligence activities,” or the secret service. In such a case, the customer must not be notified. However, the government is required to tabulate all the instances in which this section is used.²⁵

The next salient act passed was *The Money Laundering Control Act of 1986*. This act increased the definitional strength originally provided in the *Bank Secrecy Act of 1970*. Of particular interest is the section that deals with extraterritorial reaches, in the cases where the act is committed by a U.S. citizen, a non-citizen within the United States, or the value of the action exceeds \$10,000. This act amended the *Right to Financial Privacy Act of 1978* by protecting financial institutions from being liable to the customer when providing information. The only other point of note within the bill is the plan specified in Section 1363 for the creation of an informational exchange system with foreign governments in the attempt to better share information about suspected criminal activities. It further required that a study concerning “money laundering through foreign branches of domestic financial institutions.”²⁶

The subject of money laundering was again addressed in legislation through the *Money Laundering Prosecution Improvements Act of 1988*. This act sought to tighten the regulations surrounding money transfers and reporting procedures. It also amended the *Bank Secrecy Act*, strengthening the penalties faced by financial institutions that fail to report suspicious activity.^{*27}

In the 1990s, two additional laws were passed. The *Annunzio-Wylie Anti-Money Laundering Act* was passed in 1992. Its primary purpose was to strengthen anti-money laundering laws already in place. This law also clarified the role of nonbank financial institutions. The majority of the law dealt with enforcement and punishment of those tried for money laundering, specifically referring to the role of the institution (see Subtitle A: Termination

* By this time, the Bank Secrecy Act had been codified. In the 1988 act, it refers to the United States Code section derived from the Bank Secrecy Act.

of Charters, Insurance, and Offices; Subtitle C: Money Laundering Enforcement Improvements).²⁸

Two years later, another anti-money laundering bill was passed. *The Money Laundering Suppression Act of 1994* was intended to clarify reporting activities of financial institutions. The majority of the legislation focuses on the reporting process, with provisions to institute additional training and to raise the financial institution's liability for not reporting suspicious activities. In particular the law required all states to develop "uniform laws for licensing and regulating businesses which provide check cashing, currency exchange, or money transmitting or remittance services...[and/or] are not depository institutions."²⁹ The legislation then provided a model statute. In addition to requiring increased reporting and uniform laws between all states, this law also augmented the existing penalties for money laundering.³⁰

The original intent of the Bank Secrecy Act, and subsequent bills was to slow the domestic criminal usage of money laundering. This can be inferred based both on the historical context, wherein terrorism was not at the forefront of the United State's security concerns, and based on the text of the legislation itself. Most of these bills focus primarily on domestic financial institutions and customers. When foreign institutions or actions are mentioned at all it is usually as an afterthought at the end of the bill. As can be seen from the title of the bills, there was also a great deal of pull between the need for regulation and reporting to the proper authorities by the banks, and the customer's right to financial privacy. In the end, regulation and reporting clearly won out, as regulations and penalties for underreporting grew increasingly harsher as the years progressed.

In response to the increasing regulations in the late 1990s, a proposal called, "Know Your Customers" was presented by a number of U.S. banks. At the time, the components of the proposal were not accepted. They subsequently have been incorporated into the measures described in the Patriot Act. Before 2001, "banks were required to know their customer in one of three specific situations: (1) to verify and record the name and address of the individual presenting a transaction when a CTR filing was required; (2) when customers purchased certain monetary instruments, such as cashier's checks and money orders; and (3) in certain wire transfers."³¹ With the passage of the Patriot Act, the variety of applicable situations was greatly expanded and enhanced.

The USA PATRIOT Act: Changes in Legislation regarding Terrorist Financing

The Patriot Act was passed in the emotionally charged atmosphere immediately following the 9/11 terrorist attacks against the United States. As a whole the Patriot Act was both comforting and terrifying, providing the U.S. government with the powers and abilities it needed to track down and halt terrorists while concurrently walking the edge of infringing upon the cherished rights of the American public.

In the area of terrorist financing, the Patriot Act expanded anti-money laundering laws to cover more than banks³² (the primary focus of previous legislation). As a result, the same stipulations apply to broker-dealers and investment companies. While the intention of the Patriot Act was to improve the anti-money laundering laws, the increased paperwork required may cause it to become less effective.³³

Even more troubling than extra paperwork is the idea that financial tools provided by the Patriot Act may not prove effective in the long term. A major problem with the Patriot Act is that through its legislation on terrorism financing, it contains legislation that, while not directly creating laws for foreign or international financial institutions, does create stipulations that would make it difficult for said banks to work with U.S. banks, particularly in correspondent accounts. Such stipulations may cause foreign banks to try side-stepping the Patriot Act regulations, or banks may simply sever ties with U.S. banks. If such severance were to occur, it would be similar to “cutting off financial ties with a country.”³⁴

As the Patriot Act provides new legislation (as opposed to amending old legislation) on this issue, it is necessary to observe how court cases of money laundering involving this type of financial information sharing were treated. Historically, U.S. courts required parties to produce foreign documentation even if it violated that nation’s bank secrecy laws. This sense of international authority did not last, most likely due to refusal or inability to produce such documentation. Today, U.S. courts must consider the following:

“the importance to the investigation or litigation of the documents or other information requested; the degree of specificity of the request; whether the information originated in the USA; the availability of alternative means of securing the information; the extent to which non-compliance with the request would undermine the important interests of the USA, or compliance with the request would undermine important interests of the state where the information is located.”³⁵

After these precedents were set, two additional preconditions were also established: “personal jurisdiction over that person or company, and their control over the documents.”³⁶

Within the Patriot Act, there are five sections that address the concept of U.S. extraterritoriality in legislation: sections 311, 312, 313, 317, and 319. The first three sections deal with regulations on domestic institutions, the last two deal more directly with foreign institutions.³⁷

Section 311, "Special Measures for Jurisdictions, Financial Institutions, or International Transactions of Primary Money Laundering Concern," deals with measures that may be enacted by the Secretary of the Treasury (Secretary) against suspect institutions, accounts, or individuals. It begins by detailing specifics from previous anti-money laundering laws (see above for a full summary) and goes on to specify how the Secretary should determine if such special measures should be put in place by looking at the following items: "(1) is any other nation already pursuing this measure; (2) will these measures cause economic disadvantages in competition to the party in question; (3) what extent the measure(s) would have on the business transactions of the party in question; (4) the affect on the national security of the United States."³⁸ An explanation on how to qualify these measures follows. Anyone dealing in international banking may be subject to reports, special records, etc. Additionally, it may be necessary to inform the Secretary with whom you (as the institution) are working, their legal status, and the type of transaction being done. This is especially important for U.S. firms working with foreign individuals or representatives of foreign individuals.

The types of accounts that are most likely to see these special measures are payable-through accounts, and correspondent accounts. If the account is already active (in operation at the time the Patriot Act was passed), the necessity of treating foreign customers with the same standards as national customers in the context of knowing vital information about them, is emphasized. For those looking to open an account, if the Secretary finds the account suspicious, the U.S. firm may not be able to open the account. However, in order to be fair, the Secretary must consult with the Secretary of State and the Attorney General before making such a ruling. When observing "suspicious" firms, accounts, or individuals, the secretary must take the following into consideration: "evidence of criminal or terrorist business transactions; the offer of secrecy by foreign institutions; the quality of the administration and how well the administration deals with money laundering; the volume of the transactions in respect to the economy; if the territorial area is known for money laundering; if the United States has a mutual legal assistance treaty, and how well the area has dealt with U.S. law enforcement in the past; and the amount of corruption."³⁹

Despite the numerous factors of which the Secretary must be aware, the definitions of many items are quite broad, leaving generous room for interpretation. Further, it is quite clear that the bill singles out foreign customers and institutions for special consideration. Most likely this was due to the lack of prior legislation specifically regarding foreign sources of money laundering.

Section 312, "Special Due Diligence for Correspondent Accounts and Private Banking Accounts," emphasizes the idea of due diligence in activities. Accounts in the United States for a non-United States person, a visiting foreigner, or a representative of a non-United State person are required to act with due diligence, in order to ascertain if the account(s) are being used for

illicit purposes. In dealing specifically with banks possessing correspondent accounts that are “non-cooperative” with international anti-money laundering regulations or have been designated by the Secretary as warranting special measures shall be subject to requirements including identification of the account holder, and “enhanced scrutiny” under the due diligence measures described above.

Due diligence further requires minimum standards for private banks when the account holder is a non-United States person, including, knowing the identity of the depositor and beneficiary; enhanced scrutiny for accounts held by foreign senior politicians or their immediate family members/associates to prevent foreign corruption.⁴⁰ Once again, this section is especially heavy handed towards non-United States citizens and foreign institutions. All are subject to additional scrutiny, checks, and regulations.

Section 313, “Prohibition of United States Correspondent Accounts with Foreign Shell Banks,” begins by discussing correspondence accounts.⁴¹ A correspondence account in this context is, “any account established for a foreign financial institution to receive deposits from, or to make payments or other disbursements on behalf of, the foreign financial institutions, or to handle other financial transactions related to such foreign financial institution.⁴²” This section stipulates that any correspondent account where one side is located in the United States must have a physical location for the corresponding side. The Act goes further, stating that no United States correspondent account shared with a foreign bank should be connected, even indirectly with a bank that has no physical presence.⁴³ In short, all accounts managed partially in the United States must have a similarly managed and regulated institution in order for the two to be connected via a correspondent account.

The above three sections of the Patriot Act are all domestically focused with some affects extending to foreign account holders or institutions. It is clear that while the United States cannot enact legislation on foreign individuals or institutions, it is willing to create stipulations that make it difficult for such individuals or institutions to interact with U.S. institutions. Clearly, none of the stipulations are overtly open to objection: knowing one’s customers is simply a good business policy if the institution is interested in protecting its international reputation. However, the Patriot Act in creating difficulties for terrorists attempting to raise funds in the United States also makes it significantly more difficult for foreign individuals and institutions to bank in the United States. Further, the vagueness of the wording within the bill leaves the Secretary of the Treasury with a great deal of discretion in determining what constitutes a suspicious transaction or customer, again making it difficult for legitimate businesses and individuals to operate in the U.S. financial market. On whole, the restrictions can be considered both comprehensive and reasonable given the political climate during the aftermath of the September 11.

Section 317, "Long Arm Jurisdiction Over Foreign Money Launderers," gives district courts jurisdiction of "any foreign person, including any financial institution authorized under the laws of a foreign country," that the United States has an interest in either the case or the assets. The U.S. courts may seize what assets they find necessary and may appoint a Federal Receiver to carry out the task.

Section 319, "Forfeiture of Funds in United States Interbank Accounts," is equally as forceful as section 317. If money is deposited into a foreign account in a foreign bank that has an interbank account with the United States, the United States assumes the funds are in the interbank account. Then United States can pursue legal action against the foreign institution and the funds. The U.S. Attorney General can halt this process when he sees conflict between the national laws of the foreign state and U.S. laws *if* such conflict causes liability.

After seizure, there is, "no requirement for [the U.S.] government to trace funds." In short, the government does not have to prove a connection between the seized funds and the funds deposited into the foreign bank. The owner of the funds is allowed to contest the seizure. In some cases, this owner may be defined as the foreign bank. This is the case if: (1) the bank was practicing the wrongdoing; (2) the foreign bank had, "discharged all or part of its obligation to the prior owner of the funds."⁴⁴

In collecting information about the funds, the Secretary or the Attorney General can subpoena information on correspondence accounts if one base of the account is in a foreign state as long as the other is in the United States. Further, a bank representative may be asked to appear if he is in the United States. If he is abroad, he still may be asked to appear if the foreign state is under any mutual assistance treaty or other similar agreement. Any foreign bank with a correspondence account in the United States must maintain records as though it was a U.S. institution.

The most potent portion of this section is the one on termination requirements. U.S. banks are required to terminate an account within ten days of a request made by the Secretary or Attorney General. These requests are made when the foreign bank has failed to: (1) comply with a subpoena; (2) "initiate proceedings in a United States court contesting such summons or subpoena."⁴⁵ In cases of termination, U.S. banks are not liable "to any person in any court or arbitration proceeding."⁴⁶

These last two sections are particularly forceful in the dealings of the U.S. government towards foreign institutions. In such cases, the United States is expanding its definition of territorial jurisdiction, especially evident in the seizure stipulations under section 319. The question becomes: will other states be willing to conduct business with such a tightly regulated and broad reaching state and what happens if foreign states do not comply? Some scholars assert

that in the end, “the USA may face the choice between cutting off access to the international financial system and permitting access to a system that does not conform to its policies.⁴⁷”

The Swiss Banking System

Switzerland is a prime case to study because of the notoriety surrounding its banking system. The Swiss banking system is the largest sector of the Swiss economy. In 2000, Swiss banks employed over 116,000 people and accounted for 10.5% of GDP.⁴⁸ The Swiss banking system holds over \$1.2 trillion in cross border assets and the system is based on universal banking.

There are two major banks that dominate the Swiss banking industry: UBS AG and Credit Suisse Group. Under these banks are twenty-four Cantonal, or state banks that are, “semi-governmental organizations that focus business activities on deposits and lending⁴⁹.” Beneath Cantonal banks are regional banks who, “limit activities to particular regions of Switzerland, thus building a competitive advantage by responding to local circumstances and regional business cycles.⁵⁰” At an even smaller level are Raiffeisen banks, or, “local rural credit cooperatives that raise funds locally and lend to members in their region.⁵¹”

But it is the last bank classification of private banks that causes the most sensation. Private banks are, “individually owned or owned in partnership...known for discretely managing the financial affairs of the world’s wealthy and...do not openly offer to accept savings deposits.⁵²” In the popular media, Swiss banks are often portrayed in this light, and are further given the reputation of catering to unsavory characters. For example, the criminals chased by the popular book and film character, James Bond, generally stash their cash in a Swiss bank account, with only a number and passcode, rather than a name, attached. This portrayal gives the impression to the public at large that Swiss banks are engaged in an unsavory business and commonly deal with criminals.

However, such an opaque, corrupt system is not necessarily an accurate portrayal of the Swiss system. One of the most prominent aspects giving the Swiss banking system its poor reputation is the numbered account. Yet, the numbered account is actually not anonymous: “Today, when opening numbered accounts, depositors must provide the bank with the same information as when opening regular accounts.⁵³” The difference between a regular account and a numbered account is that for a number account the attached name is restricted to a certain number of senior bank officials. In fact, some European states have more lax and secretive laws than Switzerland.

Yet, unlike the United States, in Switzerland the right to privacy extends to banking information. “A breach of banking confidentiality is a criminal offence, punishable by up to six months imprisonment and/or up to CHF 50,000 in fines.⁵⁴” This confidentiality can be lifted in cases of “serious criminal legal proceedings and most civil litigation cases.⁵⁵” Additionally,

secrecy is lifted for other states when certain conditions are met: the investigation is pertaining to an act also a criminal offense in Switzerland; the provided information will not be used for any other purpose than the stated purpose; the government requesting the information agrees to reciprocate if asked; and the “punishment” is comparable to the Swiss “punishment.”⁵⁶ Terrorism against the United States would ostensibly meet these criteria with the possible exception of the ‘punishment.’[†]

In fact, the success of Swiss banking is predicated on “the trust and reliability that have been established over generations of service.”⁵⁷ As a result, Switzerland cannot afford to let a “few bad apples” spoil its system for its numerous clients.⁵⁸ It can be presumed that such assiduousness also stems from the desire to avoid negative publicity. The Swiss have two major laws pertaining to money laundering: the Due Diligence Agreement (DDA) and the Swiss Federal Money Laundering Act of 1998.⁵⁹

Under the Money Laundering Act, Switzerland defined financial intermediary as any person, “who professionally accepts, keeps on deposit or helps invest or transfer assets belonging to third parties.”⁶⁰ In applying the law, financial intermediaries are required to: know the client’s identity; the beneficial owner; and form written documentation about the background of the client and the client’s funds.

Switzerland defines terrorist financing as: “the financing of a violent crime in order to intimidate a population or to compel a government or an international organization to do or abstain from doing any act.”⁶¹ Switzerland does not black list any clients because it does not want international pressure on the creation of a list. Switzerland has created a fine line in its laws between failing to report suspicious activity and reporting unnecessarily. In Switzerland, the Swiss Money Laundering and Control Authority does provide a list of suspected terrorists that actually comes directly from the U.S. government watch list. Thus it should be emphasized that terrorists generally avoid the Swiss banking system as a platform.⁶²

Did the United States affect the way the Swiss banking system operates?

Contrary to popular opinion, the Swiss banking system is highly committed to anti-money laundering efforts and has been for quite some time. According to the Swiss Bankers Association website, “By international comparison, Switzerland’s anti-money laundering measures have a very long history.”⁶³ Independent of the government, Swiss Banks have developed their own due diligence codes of conduct dating back as far as 1977. These codes are written and agreed upon by Swiss banks, and are submitted to their oversight body, the Swiss Financial Market Supervisory Authority (FINMA), which is given the power to impose sanctions on banks for infringement upon the codes.⁶⁴

[†] Considering the United States would consider terrorism a capital offense, punishable by the death penalty; in Switzerland, as in most other developed states, the death penalty is not practiced.

As Swiss Banks have actively practiced anti-money laundering techniques for many years, it is difficult to determine what affect the Patriot Act had on Swiss behavior. The Swiss Money Laundering Act has been in force since 1998, three years prior to the passage of the Patriot Act. Further, when observing the guidelines passed since 2001, the number of guidelines passed by the Swiss Bankers Association did not appreciably increase immediately following the passage of the Patriot Act, or even in the year or two after that. In fact, there exists a gap from 2001 to 2004 in passage of new regulations.⁶⁵ Under FINMA, there appears to have been even less in the period following the passage of the Patriot Act—only one new ordinance passed in 2010.⁶⁶

In 2008, the Swiss Bankers Association came out with a press release describing its new due diligence agreement. The agreement took into account the FATF revised recommendations, particularly the nine related to the financing of terrorism. These recommendations were integrated into the agreement, which is revised every five years.⁶⁷

The newest form of the Swiss due diligence agreement expanded the requirements of identification of customers and, “lays down the obligations on banks with regard to client identification and establishment of the identity of beneficial owner assets.⁶⁸” The process described states that identification must be verified when opening accounts, entering into fiduciary transactions, renting safe deposit boxes, management of third party assets, and transactions involving over CHF 25,000. It specifies exactly how to establish identity with both individuals and corporations. The language is simple, but direct and very specific. The document attempts to cover various contingencies that may be encountered when dealing with the administration of financial business. There is an auditing component to the agreement, conducted with external auditors. Any problems are to be reported to the supervisory body under the Swiss Banking federal commission. Any discrepancies between this agreement and practice can end in a fine.⁶⁹ The agreement “also takes a systematic risk-based approach, giving banks greater freedom in their decision making.⁷⁰”

On the whole, the Swiss agreement is more comprehensive than the Patriot Act in its descriptions and instructions on identifying and dealing with such administrative matters. Such inclusiveness is particularly telling when one considers that the Swiss use U.S. definitions and lists of suspected terrorists in their system. The difference appears when one looks to the reporting aspects. This document does not specify reporting requirements for the government, though this is because the document is not a legally binding document under the Swiss government’s auspices.⁷¹

Based on the above evidence, it seems fair to state that the Patriot Act had little impact on the Swiss banking operations or their regulatory bodies. This is most likely due to the fact that

Switzerland and the Swiss banking system already had a comprehensive and enforced legal system at work against money laundering. Any of the legislation passed by the United States would not have greatly impacted the Swiss banking system because the system “has set up what is probably the world’s most comprehensive and effective mechanism for dealing with money from criminal sources.”⁷²

Policy Recommendations

U.S. legislation has had minimal to no direct impact on the Swiss banking system in its fight against terrorism. This stems from the fact that Switzerland already had a comprehensive system in place to prevent money laundering and terrorist financing. Thus, the United States should not be looking to legislate and enforce its codes in other states, particularly post-industrial states, like Switzerland. Rather, it would behoove the United States to determine what has made an impact and continue to work through those channels.

If United States legislation did not have a direct impact on the Swiss banking system, FATF, an international organization, did. This bears the question: why? Further, why did the Swiss Bankers Association wait until 2008 to implement recommendations first established in 2001?

To begin to answer these questions, it is important to recognize that the Swiss Bankers Association agreement under consideration is only reviewed every five years. Yet, it would have been possible for the Swiss Bankers Association to employ the recommendations when the agreement was revised in 2003. Because the association waited an additional five years to implement the recommendations suggests that there must have been a change in how the recommendations were published or how the FATF was perceived or both, between 2003 and 2008.

These conclusions give the United States two areas on which to work. First, the United States should ascertain why Swiss corporations chose the FATF recommendations to implement. Second, the United States should determine the change that persuaded the Swiss to integrate the recommendation in 2008 as opposed to 2003. Only then can the United States begin to alter its own policies to better accomplish its overall security goal of halting terrorist financing.

To begin, it is important to determine why the Swiss chose to implement the FATF recommendations. FATF is an inter-governmental organization established in 1989. Its current mission is “the development and promotion of policies, both at national and international levels to combat money laundering and terrorist financing.”⁷³ The FATF has “34 member jurisdictions” including the United States and Switzerland, “2 regional organizations” and 23 observers.⁷⁴ That FATF is an intergovernmental organization must make it more appealing to Switzerland than

being manipulated by another country's laws and regulations. This is most likely why the Swiss Bankers Association eventually adopted its recommendations.

Another likely reason the Swiss Bankers Association embraced the FATF recommendations is the simplicity and directness with which the FATF expressed its recommendations. The nine recommendations published by the FATF were special recommendations on terrorist financing. The first recommendation proposed the "ratification and implementation of UN instruments," particularly the 1999 United National International Convention for the Suppression of Financing Terrorism. Second, the FATF recommended that states, "criminaliz[e] the financing of terrorism and associated money laundering." Third, states were advised to "freez[e] and confiscate[e] terrorist assets." Fourth, "reporting suspicious transactions related to terrorism" was proposed. Fifth, states were encouraged to participate in, "international cooperation" through treaties or other formal agreements, established for the purposes of information exchange. States were also advised to avoid providing safe havens to those who finance terrorism. The sixth recommendation addressed "alternative remittance." States should register all those who deal with financial movements via FATF registration suggestions and prosecute anyone that attempts to participate in the market without proper registration. Seventh, the FATF proposed that "wire transfers" have identification attached to them, with such information remaining attached through all stages of multiple transfers. Eighth, legal "non-profit organizations" deserve protection. Finally, the FATF recommended that states should be vigilant regarding the physical movement of cash by "cash couriers."⁷⁵

Such straight forward and broad recommendations and language made it easy to incorporate the FATF recommendations into an already existing document. Attempting to pass U.S. legislation that would make it difficult for foreign corporations to financially interact with the United States has clearly proven ineffective. And, given the current economic recession, the United States can ill-afford to lose business in any of its major sectors, and this includes the financial sector.

The United States will need to find other ways to prevent the financing of terrorism. The United States cannot take complete control of an intergovernmental organization; it can find ways to better work through such an organization. One such way would be through existing national organizations such as the Financial Crimes Enforcement Network (FinCEN). FinCEN was established in 1990, "to provide a government-wide multiscore financial intelligence and analysis network."⁷⁶ In 1994, this agency took over regulatory responsibilities regarding the Bank Secrecy Act. It was again given even more responsibilities under the Patriot Act.⁷⁷ While FinCEN does affiliate with the FATF, as well as other international organizations, the United States should work on strengthening its appeal and applicability worldwide.

One way the United States has attempted to work through FinCEN already is via the Egmont Group. Originally founded in 1995, the Egmont Group was designed to serve as a communication network to combat money laundering and terrorist financing. This organization is made up of financial intelligence units, or small national agencies that work within their home states. Today, the group has approximately 120 members.⁷⁸

The United States should work on better synergizing its efforts bringing together its national organizations and the international organizations in which it is involved, and putting forward a cohesive set of goals. These should be structured along the lines of the FATF which appears to be the most successful organization at this time. Further, the United States should promote policies that can be easily adapted to existing institutions, documents, and agreements of individual countries, as the Swiss were able to do with the FATF recommendations.

Additionally, the United States should identify ways to further strengthen the existing organizations such that they are better able to perform their intended function. For example, the FATF has an excellent report with its members, but it lacks any sort of enforcement mechanisms if its members choose not to abide by its recommendations. Therefore, it would behoove the United States, working in conjunction with other member states to strengthen the FATF and better promote enforcement.

Conclusion

Due to its large market share and importance in the Swiss economy, it is not surprising that Switzerland was ahead of the curve when it comes to anti-money laundering actions. In fact, one might conclude that despite Switzerland's sometimes poor reputation, the United States probably could learn a thing or two from the Swiss system. Switzerland's apparent disregard for direct U.S. policy calls into question of the true influence and power of the United States. If the United States assumed that it could pressure another developed state into immediate action by threatening to close off significant aspects of the U.S. economy, it appears sadly mistaken. It should not be concluded that the United States lacks the ability to sway another state in a given direction. Rather, that the United States cannot or should not depend solely on its economic power to do so.

Despite the apparent lack of direct U.S. influence on the banking system, the Swiss have indirectly implemented several U.S. backed policies, as evidenced by the inclusion of the FATF regulations. Given such action, it would be illuminating to further examine the factors explaining the success of indirect policy methods over direct policy methods in the prevention of terrorist financing. Findings in such a study may suggest a more comprehensive understanding of how the United States can best exert its influence given its current characteristics.

Notes

- ¹ General Assembly of the United Nations. "International Convention for the Suppression of the Financing of Terrorism." New York: un.org, 9 December 1999
- ² Raphaeli, Nimrod. "Financing of Terrorism: Sources, Methods, and Channels." Terrorism and Political Violence (2010): 59-82.
- ³ Burr, J. Millard and Robert O. Collins. Alms for Jihad. Cambridge: Cambridge University Press, 2006.
- ⁴ Raphaeli, 2010
- ⁵ *ibid*
- ⁶ Basil, Mark. "Going to the Source: Why Al Qaeda's Financial Network is Likely to Withstand the Current War on Terrorist Financing". "Howard, Russel D., Reid L. Sawyer and Natasha E. Bajema. Terrorism and Counterterrorism: Understanding the New Security Environment. New York: McGraw Hill, 2009. 530-547.
- ⁷ Raphaeli, 2010
- ⁸ Burr and Collins, 2006
- ⁹ Weiss, Martin A. Terrorist Financing: The 9/11 Commission Recommendation. Washington D.C.: The Library of Congress: Congressional Research Service, 2005.
- ¹⁰ Burr and Collins, 2006
- ¹¹ *ibid*
- ¹² Raphaeli, 2010
- ¹³ Burr and Collins, 2006
- ¹⁴ *ibid*
- ¹⁵ *ibid*
- ¹⁶ Raphaeli, 2010
- ¹⁷ *ibid*
- ¹⁸ Financial Action Task Force. FATF GAFI. 2 April 2011 <www.farf-gafi.org>.
- ¹⁹ Gouvin, Eric J. "Bringing Out the Big Guns: The USA PATRIOT Act, Money Laundering and the War on Terrorism." Baylor Law Review (2003): 955-990.
- ²⁰ The Currency and Foreign Transactions Reporting Act of 1970, Pub. L. no. 91-508, 84 Stat 1118 (1970). Print.
- ²¹ Gouvin, 2003
- ²² The Currency and Foreign Transactions Reporting Act of 1970, Pub. L. no. 91-508, 84 Stat 1118 (1970). Print.
- ²³ Gouvin, 2003
- ²⁴ *ibid*
- ²⁵ The Right to Financial Privacy Act of 1978, Pub. L. no. 95-630, 92 Stat 3697 (1978). Print.
- ²⁶ Money Laundering Control Act of 1986, Pub. L. no. 90-570, 100 Stat. 3207-18 (1986). Print.
- ²⁷ Money Laundering Prosecution Improvements Act of 1988, Pub. L. no 100-690, 102 Stat 4355 (1988). Print.
- ²⁸ The Annunzio-Wylie Anti-Money Laundering Act, Pub. L. no. 102-550, 106 Stat 4044 (1992). Print.
- ²⁹ The Money Laundering Suppression Act of 1994, Pub. L. no. 103-325, 108 Stat 2243 (1994). Print.

-
- ³⁰ *ibid*
- ³¹ Gouvin, 2003
- ³² *ibid*
- ³³ *ibid*
- ³⁴ Preston, Ethan. "The USA PATRIOT Act: New Adventure in American Extraterritoriality." Journal of Financial Crime (2002): 104-116.
- ³⁵ *ibid*
- ³⁶ *ibid*
- ³⁷ *ibid*
- ³⁸ *ibid*
- ³⁹ The USA PATRIOT Act, Pub. L. no. 107-56, 115 Stat 296 (2001). Print.
- ⁴⁰ *ibid*
- ⁴¹ *ibid*
- ⁴² Financial Crimes Enforcement Network. FinCEN. 14 April 2001 <www.fincen.gov>
- ⁴³ The USA PATRIOT Act, Pub. L. no. 107-56, 115 Stat 296 (2001). Print.
- ⁴⁴ *ibid*
- ⁴⁵ *ibid*
- ⁴⁶ *ibid*
- ⁴⁷ Preston, 2002
- ⁴⁸ Peppas, Spero C. "Swiss Banking Confidentiality: Perception vs Reality." Management Research News (2004): 14-33.
- ⁴⁹ *ibid*
- ⁵⁰ *ibid*
- ⁵¹ *ibid*
- ⁵² *ibid*
- ⁵³ *ibid*
- ⁵⁴ *ibid*
- ⁵⁵ *ibid*
- ⁵⁶ *ibid*
- ⁵⁷ Delco, Fabio and Nadja Marugg. March 2004. IFLR The Global Practice Service. 15 February 2011 <www.iflr.com>.
- ⁵⁸ *ibid*
- ⁵⁹ Peppas, 2004
- ⁶⁰ Swiss Bankers Association. Swiss Banking. 2011. 8 April 2011 <www.swissbanking.org>.
- ⁶¹ *ibid*
- ⁶² Delco and Marugg, 2004
- ⁶³ Swiss Bankers Association, 2011
- ⁶⁴ *ibid*
- ⁶⁵ *ibid*
- ⁶⁶ FINMA. finma. 2011. 8 April 2011 <www.finma.ch>.
- ⁶⁷ Swiss Bankers Association, 2008
- ⁶⁸ *ibid*
- ⁶⁹ "Agreement on the Swiss banks' code of conduct with regard to the exercise of due diligence (CDB 2008)." 7 August 2008. 14 April 2011 <www.swissbanking.org/en/20080410-vsbcwe.pdf>

⁷⁰ Swiss Bankers Association, 2008

⁷¹ Agreement on the Swiss banks' code of conduct with regard to the exercise of due diligence (CDB 2008)," 2008

⁷² Swiss Bankers Association, 2011

⁷³ Financial Action Task Force, 2011

⁷⁴ *ibid*

⁷⁵ Financial Action Task Force. February 2008. FATF-GAFI. 14 April 2011 <www.fatf-gafi.org/dataoecd/8/17/3849466.pdf>

⁷⁶ Financial Action Task Force, 2011

⁷⁷ Financial Crimes Enforcement Network, 2011

⁷⁸ *Ibid*

Bibliography

Burr, J. Millard and Robert O. Collins. Alms for Jihad. Cambridge: Cambridge University Press, 2006.

Delco, Fabio and Nadja Marugg. March 2004. IFLR The Global Practice Service. 15 February 2011 <www.iflr.com>.

Financial Action Task Force. February 2008. FATF-GAFI. 14 April 2011 <www.fatf-gafi.org/dataoecd/8/17/3849466.pdf>.

—. FATF GAFI. 2 April 2011 <www.farf-gafi.org>.

Financial Crimes Enforcement Network. FinCEN. 14 April 2011 <www.fincen.gov>.

FINMA. finma. 2011. 8 April 2011 <www.finma.ch>.

General Assembly of the United Nations. "International Convention for the Suppression of the Financing of Terrorism." New York: un.org, 9 December 1999.

Gouvin, Eric J. "Bringing Out the Big Guns: The USA PATRIOT Act, Money Laundering and the War on Terrorism." Baylor Law Review (2003): 955-990.

Money Laundering Control Act of 1986, Pub. L. no. 90-570, 100 Stat. 3207-18 (1986). Print.

Money Laundering Prosecution Improvements Act of 1988, Pub. L. no 100-690, 102 Stat 4355 (1988). Print.

Peppas, Spero C. "Swiss Banking Confidentiality: Perception vs Reality." Management Research News (2004): 14-33.

Preston, Ethan. "The USA PATRIOT Act: New Adventure in American Extraterritoriality." Journal of Financial Crime (2002): 104-116.

Raphaeli, Nimrod. "Financing of Terrorism: Sources, Methods, and Channels." Terrorism and Political Violence (2010): 59-82.

Swiss Bankers Association. April 10 2008. SwissBanking. 14 April 2011 <www.swissbanking.org/en/medienmitteilung-080410-vsbs.pdf>.

—. Swiss Banking. 2011. 8 April 2011 <www.swissbanking.org>.

The Annunzio-Wylie Anti-Money Laundering Act, Pub. L. no. 102-550, 106 Stat 4044 (1992). Print.

The Currency and Foreign Transactions Reporting Act of 1970, Pub. L. no. 91-508, 84 Stat 1118 (1970). Print.

The Money Laundering Suppression Act of 1994, Pub. L. no. 103-325, 108 Stat 2243 (1994). Print.

The Right to Financial Privacy Act of 1978, Pub. L. no. 95-630, 92 Stat 3697 (1978). Print.

The USA PATRIOT Act, Pub. L. no. 107-56, 115 Stat 296 (2001). Print.

Weiss, Martin A. Terrorist Financing: The 9/11 Commission Recommendation. Washington D.C.: The Library of Congress: Congressional Research Service, 2005.