

**Testimony of
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“Terrorist Financing: A Progress Report on Implementation of the USA PATRIOT Act”

**Financial Services Committee
United States House of Representatives
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Chairman Oxley, Congressman LaFalce, and distinguished members of the Committee, thank you for inviting me to testify about the implementation of the USA PATRIOT Act. In many ways, the PATRIOT Act and the regulations that we have promulgated to implement it are central to the war on terrorism. I applaud the Committee for its work in passing the Act. I look forward to continuing to work with the Committee as we further implement the Act.

Before reviewing the work we have done to implement the Act, I wish to update the Committee on the progress we are making on the financial front of the war on terrorism. Along with my testimony, I am submitting a document entitled, “Contributions by the Department of the Treasury to the Financial War on Terrorism.” This document is available on our website at <http://www.treas.gov/press/releases/reports/2002910184556291211.pdf>.

The President has emphasized that the financial front of the war on terror is critically important to America’s success in fighting terrorism. The President has directed the Secretary of the Treasury and the Department, in coordination with other departments of the federal government and with other nations, to fight this front. As Deputy Secretary of the Treasury, I ensure that the Secretary’s initiatives are implemented across all the components of the Department. I also help lead National Security Council deputies committee meetings in setting strategic priorities for the financial front. Our Under Secretary for Enforcement, Jimmy Gurulé,

leads our enforcement bureaus including the United States Customs Service, the United States Secret Service, the Financial Crimes Enforcement Network (FinCEN), and the Office of Foreign Assets Control (OFAC) as in fighting terrorist financing. In addition, Under Secretary Gurulé oversees a particularly important Treasury initiative, Operation Green Quest – an interagency task force that draws upon expertise in the Customs Service, the United States Secret Service, the IRS Criminal Investigations Division, the Department of Justice, the FBI, and other agencies to investigate terrorist financing. Our Under Secretary for International Affairs, John Taylor, works, along with the State Department and the Department of Justice, to build and maintain the international coalition against terrorist financing. Our Under Secretary for Domestic Finance, Peter Fisher, works to help implement the USA PATRIOT Act, and to help protect our nation’s critical financial infrastructure. And, of course, we have many, many employees who are working hard and, in some cases, putting their lives at risk to fight the financing of terror. In all of these efforts, we work closely with the State Department, the Department of Justice, and other departments. This is a team effort and our success depends on it.

ACHIEVEMENTS IN FINANCIAL ASPECTS OF U.S. ANTI-TERRORISM INITIATIVES

Our goal is straightforward. We seek to prevent terrorist attacks by: (1) disrupting terrorist finances; and (2) following financial trails to disrupt terrorists themselves.

Our first actions after the tragedy of September 11 were to identify known terrorists and terrorist entities, freeze their assets in the US, and work with our allies to extend those freezes world wide. Since September 11th, the United States and other countries have frozen more than \$112 million in terrorist-related assets. More importantly, the actual amount of money blocked understates the full effect of the blocking action in that our blocking actions have effectively cut

the flow of terrorist money through funding pipelines. For example, we disrupted Al-Barakaat's worldwide network that, by some estimates, was channeling \$15 to \$20 million dollars a year to al Qaida. As another example, we froze the assets of the Holy Land Foundation for Relief and Development, which, as the principal U.S. fundraiser for Hamas, raised over \$13 million in 2000. Where warranted, we have also unblocked funds. \$350 million in Afghan government assets that were frozen in connection with the Taliban sanctions, mostly before September 11, have now been unfrozen for use by the legitimate Afghanistan government.

We have obtained strong international cooperation in this effort. All but a small handful of countries have pledged support for our efforts, over 160 countries have blocking orders in force, hundreds of accounts worth more than \$70 million have been blocked abroad, and foreign law enforcement agencies have acted swiftly to shut down terrorist financing networks. The United States has often led these efforts, but there have also been important independent and shared initiatives. To cite just three examples: on March 11, 2002, the United States and Saudi Arabia jointly referred to the U.N. Sanctions Committee two branches of a charity; on April 19, 2002, the G7 jointly designated nine individuals and one entity; and, on September 6, 2002, the United States and Saudi Arabia jointly referred to the U.N. Sanctions Committee Wa'el Hamza Julaidan, an associate of Usama bin Laden and a supporter of al Qaida terror. These efforts have been bolstered by actions from the European Union, which has issued three lists of designated terrorists and terrorist groups for blocking.

In addition to these efforts, we work with countries daily to get more information about their efforts and to ensure that their cooperation is as deep as it is broad. In many cases, we provide technical assistance to countries to help them develop the legal and enforcement infrastructure they need to find and freeze terrorist assets.

We have also had success pursuing international cooperation through multilateral forums including the U.N., the G7, the G20, the Financial Action Task Force (FATF), the Egmont Group, and the international financial institutions. In particular, Treasury continues to play a strong leadership role in FATF, a 31-member organization dedicated to the international fight against money laundering. In late October 2001, the United States hosted an Extraordinary FATF Plenary session, at which FATF adopted eight Special Recommendations on Terrorist Financing. These recommendations quickly became the international standard on how countries can take steps to avoid having their financial systems abused by terrorist financiers. Many non-FATF members have committed to implement these recommendations, as well. Over 80 non-FATF members have already submitted reports to FATF assessing their compliance with these recommendations. We are continuing our work within FATF to ensure that member countries fully implement the recommendations.

We are cleaning up the financial environment generally. Hardly a week passes without news that a foreign government or bank has taken an important new step to crack down on money laundering or terrorist financing. For example, according to foreign press accounts, Thailand recently announced plans “to reduce the minimum value of transactions subject to scrutiny” by its anti-money laundering office. As another example, the foreign press recently reported that Qatar National Bank provided its entire staff with a four-day course on fighting money laundering and terrorist financing. There are scores of similar examples involving countries around the globe.

Governments are also taking steps to prevent charities from being abused by terrorists. In the United States, we have designated or blocked the assets of several U.S. and foreign charities including the Holy Land Foundation, the Afghan Support Committee, and the Pakistan and

Afghan offices of the Revival of Islamic Heritage Society. We have also blocked the financial accounts of the Benevolence International Foundation and the Global Relief Foundation pending on-going investigation of these organizations. Kuwait and Saudi Arabia have each reportedly established new supervisory authorities to better regulate charities. This work is very important. Charity is an important component of many religions, including Islam, and few acts are as reprehensible as misusing charities for terrorist purposes. We seek to ensure a regulatory climate in which donors can give to charities without fear that their donations will be misused to support terrorism.

In addition to preventing terrorists from abusing our formal financial systems, governments are taking important steps to prevent terrorists from abusing informal financial systems, including hawala (a centuries-old, trust-based method of moving money that generates little paper trail). FATF's Eight Special Recommendations require member countries to impose anti-money laundering rules on informal financial systems, including hawala dealers. As of December 31, 2001, the United States required money service businesses to register, maintain certain records, and report suspicious activity. In May 2002, the United Arab Emirates hosted an international conference where several countries agreed to improve the regulation of hawalas by, among other things, implementing the FATF Recommendations against hawalas and designating a supervising authority to enforce the rules.

These efforts are paying off. We know that al Qaida and other terrorist organizations are suffering financially as a result of our actions. We also know that potential donors are being deterred from giving money to organizations where they suspect that the money might wind up in the hands of terrorists.

Under leadership from the President, the Congress, and this Committee, we are making it increasingly difficult for terrorists to use the mainstream financial system. As a result, we believe that terrorists increasingly will attempt to finance their operations by smuggling bulk cash or other instruments. But smuggling is costly. It takes time. It is uncertain. Smuggling exposes the cash or other instruments to possible detection and seizure by the authorities. Indeed, since September 11, our Customs Service has seized over \$9 million in cash being smuggled out of the United States to Middle Eastern destinations or with some other Middle Eastern connection. By making bulk cash smuggling a crime, the USA PATRIOT Act helped make these increased seizures possible.

Smuggling also exposes couriers to possible capture. This summer, Customs, United States Secret Service, and FBI agents apprehended and subsequently indicted Jordanian-born Omar Shishani in Detroit for smuggling \$12 million in forged cashier's checks into the United States. The detention and arrest of Shishani are highly significant as they resulted from the Customs Service's cross-indexing of various databases, including information obtained by the U.S. military in Afghanistan. That information was entered into Customs' "watch list," which, when cross-checked against inbound flight manifests, identified Shishani.

While we have had important successes, I must tell you that we have much to do. Although we believe we have had a considerable impact on al Qaida's finances, we also believe that al Qaida's financial needs are greatly reduced. They no longer bear the expenses of supporting the Taliban government or of running training camps, for example. As I have cautioned before, we have no reason to believe that al Qaida does not have the financing it needs to conduct additional attacks.

Implementation of the USA PATRIOT Act

I wish to turn now to an update on Treasury's implementation of the money laundering and anti-terrorism provisions of Title III of the USA PATRIOT Act. We have devoted ourselves at the highest levels of Treasury to carrying out the tasks that this Committee and Congress have placed on our shoulders to improve and fortify our anti-money laundering and anti-terrorist financing regime. The provisions of the Act, and now our regulations, take aim at areas in which our financial services sector may be vulnerable to abuse. As the principal architect of these new regulations, Treasury is mindful of the need to craft rules that achieve the goals of the Act without unduly burdening legitimate business activities or our citizens' privacy.

Any discussion of Treasury's implementation of the USA PATRIOT Act would be incomplete without recognition of the assistance provided by the Federal banking agencies, the Securities and Exchange Commission, the Commodity Futures Trading Commission, and the Department of Justice. These agencies have lent their time and expertise for the common goal of protecting our financial system through intelligent regulations. Active participation by the financial services industry that will operate under our regulations, has also been essential.

Our major accomplishments over the past eleven months include:

- Together with the Federal functional regulators, issuing customer identification and verification regulations.
- Developing a proposed rule to that seeks to minimize risks presented by correspondent banking and private banking accounts.
- Expanding our basic anti-money laundering program requirement to the major financial services sectors, including insurance and unregistered investment companies, such as hedge funds.
- Developing rules to permit and facilitate the sharing of information between law enforcement and financial institutions, as well as among financial institutions themselves.

Of course, each of these accomplishments emanated from the very legislation that this Committee was instrumental in drafting.

1. Ensuring Appropriate Customer Identification and Verification of Identification.

In July, Treasury and the Federal functional regulators, jointly issued proposed rules requiring certain financial institutions to develop identification and verification procedures that enable them to form a reasonable belief as to the identity of the customer. The proposed rules apply to banking institutions, securities brokers and dealers, mutual funds, futures commission merchants, and futures introducing brokers. Just as this Committee envisioned, the proposed rules seek to make mandatory what many financial institutions are already doing—obtaining basic identifying information from customers at the time of account opening. However, the rules also maintain sufficient flexibility so as to accommodate advancing technology and the wide range of channels through which financial services are offered by these institutions, including opening accounts via the Internet. Obtaining certain information is mandatory, but the manner in which that information is obtained and verified is appropriately left to the discretion and judgment of each particular financial institution. We are continuing our work on drafting similar regulations for the remaining types of financial institutions that maintain accounts for customers.

From the outset, we recognized the potential benefits to a financial institution's identification program if it were able to reliably confirm that the customer's name matched the social security number provided at the time of account opening. The most reliable source for this information is, of course, the Social Security Administration. This spring, we reached an agreement in principle with the Social Security Administration to permit financial institutions to verify with the Social Security Administration the authenticity of the social security numbers provided by account holders. We are continuing to work out the logistical details and hope to

have this service available in the near future. However, I caution that verifying the authenticity of a social security number does not ensure that the person who provided the information is in fact that person.

2. Eliminating Risks Associated with Correspondent Banking Activities of Foreign Banks and other Foreign Financial Institutions.

Several important provisions of the USA PATRIOT Act took aim at systematically eliminating the risks that can exist when U.S. financial institutions offer correspondent accounts to foreign banks and other foreign financial institutions. Given their breadth and international focus, these provisions are some of the more significant ones in the Act.

One month after the Act became law, we issued interim guidance to financial institutions describing how they were to comply with two key provisions —the prohibition on maintaining correspondent accounts for foreign shell banks (section 313) as well as the recordkeeping provisions for foreign banks having correspondent accounts (section 319(b)). A proposed rule followed shortly thereafter. Having thoroughly reviewed public comments received and analyzed the issues presented, this week we issued a final rule implementing both provisions.

In the final rule, we have defined “correspondent account” to reflect the objectives of different provisions of the Act, as well as comments received from the private sector. With respect to the shell bank prohibition, for example, we have construed the term “correspondent account” broadly to reflect the intent of Congress to cut off unregulated “brass plate banks” from the U.S. financial system. Similarly, we determined that a broad definition of “correspondent account” was appropriate for the recordkeeping provisions of section 319(b). These recordkeeping provisions apply to correspondent accounts maintained by any foreign bank, regardless of the jurisdiction in which the foreign bank is licensed. Obtaining the basic information required by this section from all foreign banks, namely, the names of the owners of

the foreign bank and the name of a U.S. agent for service of process, serves a valuable law enforcement purpose and will assist U.S. banks and securities brokers with their anti-money laundering efforts. Further, section 319(b) also contains an important provision authorizing both the Secretary of the Treasury and the Attorney General to serve administrative subpoenas on any foreign banks with correspondent accounts in the United States. Any limitation on the definition of a correspondent account in this section would unduly limit this subpoena power.

Treasury has also issued a proposed rule that aggressively implements section 312 of the Act, a provision that takes aim at a wide array of money laundering risks associated with correspondent accounts maintained for foreign financial institutions in the United States. Additionally, both the statute and Treasury's proposed rule seek to curb potential abuses in connection with private banking accounts for foreign persons by requiring due diligence, including obtaining information on the true ownership and source of funds placed in such accounts. Recent events have demonstrated the risks posed by well-intentioned financial service professionals seeking to court and maintain wealthy foreign clients. This rule is designed to minimize those risks. Treasury's rule also includes important safeguards to prevent the proceeds of foreign official corruption from finding a home in the U.S. financial system.

After issuing this proposed rule, Treasury received extensive comments from the affected industries. While many of the issues raised will take time to analyze, the statute became effective on July 23. Accordingly, on that date we issued an interim rule that effectively tolled the application of this provision pending our issuance of a final rule for most financial institutions. However, because of the importance of this provision in protecting the financial system, we required certain financial institutions, such as banks and securities and futures

brokers, to begin conducting the type of due diligence that will eventually be incorporated into the final rule.

3. Expanding the Anti-Money Laundering Regime to All Facets of the U.S. Financial System.

A basic tenet of our anti-money laundering regime is that tainted funds will follow the path of least resistance to enter the legitimate financial system. Therefore, a comprehensive approach to minimizing money laundering and terrorist financing risks within the United States necessarily involves extending controls to the full range of financial services industries that may be susceptible to abuse. Section 352 of the Act embodies this approach by directing Treasury to expand the basic anti-money laundering program requirement to all financial institutions presenting risks of money laundering by virtue of the products or services offered. The challenge is to take the broad statutory mandate and translate that into rules applicable to each of the diverse industries defined as financial institutions under the Bank Secrecy Act.

In April, Treasury, with the assistance of the SEC, the CFTC, their respective self-regulatory organizations, and the banking regulators, issued regulations requiring firms in the major financial sectors to establish an anti-money laundering program. In addition to the banks, which already had an anti-money laundering program requirement, we covered securities brokers and dealers, futures commission merchants and introducing brokers, mutual funds, money services businesses, and operators of credit card systems. Separate rules applicable to each financial industry were drafted to ensure that the programs would be appropriately tailored to the risks posed by their operations. With the pledge that we would work diligently to complete our task, the Secretary exercised his discretion and allocated additional time for us to study the remaining industry sectors and craft regulations.

Since that time, we have regarded the business operations of the remaining financial industries in order to take banking oriented regulations and modify them to apply to these other industries. Members of the remaining financial industries have never been subject to comprehensive federal regulation of their relationships with customers, let alone anti-money laundering regulation. Additionally, the remaining categories of financial industries encompass a broad range of businesses, from sole proprietorships to large corporations, further complicating the process of drafting a regulation that does not impose an unreasonable regulatory burden. Following months of meetings with industry groups and representatives, we have virtually completed our research and are working now on the task of drafting the regulations.

This week we issued proposed rules that would require firms in certain segments of the insurance industry and certain investment companies (namely, those not registered with the Securities and Exchange Commission) to establish anti-money laundering programs. These two rules reflect the complexities of our task. For the insurance industry, after tapping the expertise of the state insurance regulators and both domestic and international law enforcement officials, we tailored the rule to those areas of the industry where the products offered are susceptible to money laundering abuse and instances of money laundering have been documented. This is primarily the life and annuity products. Also, while the insurance agent must play a vital role in any comprehensive anti-money laundering program, we expressly left the obligation on the insurance company to set up and assure implementation of the program. Upon the establishment of an effective program, the insurance company can delegate responsibilities to the agents as appropriate. With respect to investment companies, such as hedge funds, that are not registered with the SEC, with the expert guidance and assistance of the SEC and the CFTC, we specifically targeted collective investment vehicles with characteristics that make them susceptible to money

laundering. Those vehicles investing in securities, commodity futures, or real estates fall within the rule. Furthermore, to facilitate effective regulation, we are proposing to require investment companies covered by the rule to file a notice with FinCEN identifying themselves, their principal investments, and contact information. Such a notice is crucial given that many such vehicles often have offshore operations despite their marketing to U.S. investors.

Another important component of an effective anti-money laundering regime is ensuring that financial institutions report suspicious activity to FinCEN promptly. With the able assistance of the SEC and the Federal Reserve, we have successfully completed a final suspicious activity reporting rule for securities brokers and dealers, ensuring that firms in this critical financial sector has a mechanism in place for reporting suspicious activities. Similarly, we are working with the CFTC to complete a proposed rule that would require the futures industry to file suspicious activity reports, and we are working with the SEC on a rule requiring mutual funds to file suspicious activity reports. And, although not required by the Act, this week we issued a final rule requiring casinos to file suspicious activity reports. Beyond these financial institutions, we are considering whether reporting obligations should be imposed on additional financial sectors such as the insurance industry. As we gain more experience with the various financial sectors, we will be able to make an informed judgment as to the efficacy of imposing reporting requirements.

4. Facilitating the Sharing of Critical Information Relating to Money Laundering and Terrorist Financing.

Early in the implementation process, I emphasized that one of the principles that guides Treasury's implementation of Title III is honoring a central purpose of the Act to enhance coordination and information flow. To that end, this week we have issued a final rule pursuant to section 314(a) seeking to establish FinCEN as an information conduit between law

enforcement and financial institutions to facilitate the sharing and dissemination of information relating to suspected terrorists and money launderers. The system builds upon FinCEN's ongoing relationships with law enforcement, the regulators, and the financial community. We have also pledged to work going forward to provide the financial sector with additional information, such as typologies of money laundering or terrorist financing schemes and updates on the latest criminal trends.

Since March of this year, Treasury has authorized certain financial institutions to share information among themselves concerning those suspected of terrorism or money laundering pursuant to section 314(b) of the Act. Our final rule issued this week retains the central features of the prior rule, but we have expanded the scope of financial institutions eligible to share information under this provision. Also, as required by the statute, financial institutions must provide FinCEN with a yearly notice that they will be taking advantage of this provision to share information.

Further facilitating the sharing of information is FinCEN's establishment of a highly secure network to permit, among other things, the filing of required Bank Secrecy Act reports via the Internet. This system will instantaneously place important reports into the databases used by law enforcement. FinCEN has completed a successful beta test in which twenty major financial institutions volunteered to file their BSA reports using this system. Beginning October 1, once minor adjustments to the system are made, FinCEN will begin offering this optional filing method to financial institutions generally.

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In summary, we have made substantial progress in implementing the USA PATRIOT Act. The Act is making a difference. Just yesterday, USA Today reported the results of a survey

of over 2,000 financial professionals. 69% of them agreed that the PATRIOT Act will prevent terrorist access to the U.S. financial system. They are right. We believe that the Act is making it increasingly difficult for terrorists to use the U.S. financial system. We are disrupting their ability to plan, operate, and execute attacks. And we are forcing them to resort to methods, such as bulk cash smuggling, that expose them to a greater risk of detection and capture.

Of course, we still have much more work to do. We will continue our efforts with the same intensity that has characterized the first eleven months. Yet as we complete our tasks in the months ahead of preparing final rules implementing these important provisions, I firmly believe that our job will have just begun. Time and experience will allow reasoned reflection on the decisions we are making today. It is incumbent upon Treasury to make adjustments to these rules when it is necessary to ensure that they continue to achieve our goals.

To that end, I am pleased to announce the creation of a new task force within Treasury, the Treasury USA PATRIOT Act Task Force. The specific mandate the task force will be to work with other financial regulators, the regulated community, law enforcement, and consumers to improve the regulations that we have already implemented. As we learn more about what works in the war on terrorist financing, we can find ways to calibrate our existing regulations both to better disrupt terrorist financing and to do so in a way that imposes the least cost on the regulated community. We look forward to working with the Committee on this project as well.