

Stopping the Islamic Terrorist Financing Machine

Written by Peter Lesniak

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Since the events of 9/11, when governments realized that money is the fuel that keeps the terror threat burning, Money Laundering (ML) and Terrorist Financing (TF) has become a matter of great concern for Western governments, who are responsible for preventing acts of terrorism.

Nonetheless, it is extremely difficult to conduct robust, falsifiable, and in-depth research on these issues mainly because most of the data is highly classified, and thus, not open for public inspection. Also, as Levi (2010:662) rightly states, there is very little official desire to inform the public about results, especially when they prove to be very modest. This, he argues, presents particular problems for researchers. Napoleoni (2010) also acknowledges that paramilitarism and terrorism as an economic phenomenon is little studied, as well as the methods by which organizations fund themselves.

Actually, it was the removal of economic barriers from international financial markets in the 1990s that gave rise to the process of merging the terrorist financial system with illegal and criminal economies. This fusion, as Napoleoni argues (2010:65), triggered the creation of the international illegal economic system, which has a GDP of \$1,500 billion, exceeding the GDP of the UK, and of which \$500 billion springs from terrorist organizations.

While much has been written on the issues of TF, most of such literature is based on particular case studies, or on national, private, and international initiatives undertaken against it (Freeman, 2011). While this is certainly a valuable tool that brings much insight into particular cases and organizations, it barely addresses the problem of the Western incapacity and lack of effectiveness in some areas of TF and ML. This work will attempt to fill this gap.

1.1. COSTS OF TERRORIST ATTACKS

Among many, there are two particularly opposing arguments in today's literature that deal with the direct and indirect costs of terror attacks. On the one hand, we have scholars and journalists who say that terrorism does not need money to terrorize and that the direct costs of conducting operations are very low, therefore, neither perceive that as a problem, or it is made hardly influential in dealing with the issue of fighting terrorism. Politis (2003) argues that one of the reasons behind the common conception that terrorism does not need money to terrorize lies in the stereotypic thinking of the attacks from the 1970s, where small groups were not as organized and used smaller measures to achieve equally big aims. To show approximate costs, I summarize literature from across the spectrum to compare estimates for major terror operations over the last 20 years:

- The 1993 World Trade Center attack was estimated at about \$19,000 (Freeman, 2011).
- The September 11 Commission estimated the cost of carrying out the 1998 U.S. embassy bombings was only \$10,000 (Hett, 2008).
- The al Qaeda-funded 2002 bombing in Bali estimates are from \$20,000 (Hett, 2008; Freeman, 2011) to \$50,000 (FATF, 2008).
- The USS Cole bombing: between \$5,000 and \$10,000 (Politis, 2003; FATF, 2008).

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- The September 11 attacks were relatively inexpensive, estimated to be between \$400,000 and \$500,000 (Politis, 2003; Hett, 2008; Levi, 2010; Freeman, 2011; House of Lords Report, 2009).
- The 2003 Jakarta JW Marriot Hotel bombing: \$30,000 (FATF, 2008).
- The 2004 Madrid train bombings: estimates vary from as little as \$10,000, (Barett, 2009; Freeman, 2011, FATF, 2008) up to \$70,000 (Hett, 2008).
- The 2005 London bombings are estimated to have cost as little as \$15,600 (Hett, 2008; Barett, 2009; Levi, 2010, FATF, 2008).

This shows that the costs of terrorist operations can be relatively low for “strategic” level attacks.

On the other hand, scholars have looked more broadly at this issue and have provided arguments from across the economic spectrum and broader framework of terrorist activity. They differentiate between the demands of direct costs, and the needs of broader requirements. In their view, to terrorize is not only to organize attacks, but also to maintain the whole structural network with all its needs and expenses. The dark side of globalization is that it has allowed terrorist groups to grow and spread, but they need substantial finances to maintain their effectiveness. The main indirect costs include recruitment, maintaining training camps, housing and food, equipment, security, forged identities, money to maintain the families of dead supporters, travel documents, intelligence gathering, contacting and directing operatives and groups, and propaganda materials or bribes, among others.

Taking into account that many groups span across many continents, their budgets are subsequently increasing. The total cost of maintaining the global Islamist terror network is estimated to be in the billions of dollars (Politis, 2003). According to Bin Laden himself, al Zarqawi's operations only in 2004 cost \$10.4 million per year (MEMRI 837) and al Qaeda's annual budget was estimated to be \$30 million to maintain its activities (House of Lords Report, 2009). Freeman (2011:463) identifies that at its peak in the 1990s, “the Kurdish Workers Party (PKK) was thought to have an annual budget of \$86 million, Hezbollah's budget is between \$100 million and \$200 million per year, and may range as high as \$400 million, the Afghan Taliban raises somewhere between \$240 million and \$360 million per year, and all the different insurgent groups in Iraq collectively raised between \$70 million and \$200 million per year.”

As much as we would like to believe in the first argument, terror financing and money laundering is a global issue that needs a global response. The business of money laundering is perceived as the world's third largest industry, right after the oil trade and foreign exchange, which in economic terms means around 2-5 percent of the world's GDP. Just within the UK, the underground economy accounts for up to £15 billion a year (Robinson, 1995; House of Lords Report, 2009). Over \$130 million in assets has been blocked across the world since 9/11, with more than \$34 million in the United States (Levi, 2010:654; Tupman 2009). As the global terror market accounts for billions rather than millions, the amount of dollars blocked and confiscated is not relatively big, and that shows a great inefficiency in dealing with this issue.

1.2. A NEEDLE IN A HAYSTACK: WHY FOCUS ON ISLAMIC TERRORISM?

It was not until 9/11 that American and international security agencies and, indeed, Western governments, realized that financing is a great threat to their security, especially when it comes to Islamic terrorism which has proven it goes to great lengths to achieve its aims. It was not until the symbol of the great Western economy was shattered to pieces by two commercial airplanes that statesman realized the potential threat that originates from the Middle East and the radicalization of Muslim communities around the world.

The very nature of this threat, based on religious, financial, and political measures, has made governments reconsider and adapt their approach to security and terrorism. With this realization, came the difficulty of dealing with the vast and complex issue of financial terrorism. It proves to be particularly difficult when it comes to Islamic terrorism, with its highly complex means, measures, resources, both informal (charities) and formal (Zakat) systems of financing, but also religious and socio-political safeguards. By this, I mean the difficulty of dealing with a state-

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sponsor of terror, which is harder to detect, not to mention control. Further problems are created when dealing with Informal Fund Transfer (AFT) systems like Hawala (a traditional Islamic system based on trust), where funds can be easily used for legal (legitimate remittances, humanitarian reasons, and emergency aid) as well as illegal (ML, TF, tax evasion, etc.) means, with no clear-cut system of control.

Another particular difficulty in dealing with Islamic terrorism is not only the source of funding, but also the means of channeling the money, which in this case, benefits from the distinctive methods of the Islamic banking financial system. Some of the most distinctive characteristics of such a system are its weak financial oversight, lack of supervision, religious character, and it having been built entirely on bank secrecy, and, therefore, it has a great degree of autonomy from international checks and balances. What is more interesting though, is how Islam has taken great interest in the condition of market and financial institutions, with Islamic law prescribing various rules and measures to influence this industry to great lengths.

I will further analyze all of the above, and more, to increase the understanding of the difficulties in dealing with Islamic terrorism and its financing methods. This will help in constructing the final hypothesis, which showcases Western inefficiency in dealing with the financing of Islamic terrorism.

SECTION 2– METHODS OF FINANCING AND RESPONSES

As mentioned above, there has not been much research done on the issue of identifying the most profitable and reliable sources of terrorist funding. The complexity and variety of ways to gather and move funds in a worldwide financial system makes gathering data on financial flows a difficult task for the foreseeable future. As such, for the purpose of this research, the strength of the main Independent Variables (the ways of gathering and transferring funds) have been assessed by looking at the international responses to them, as well as the capacity in which the undertaken initiatives (private, national, and international) have been able to deal with them and prevent or limit their use. The strongest IVs, in such a case, would be the ones that are the hardest to limit, or initiatives that have been undertaken that have not been dealt with. First, this section will consider some of the commonly used sources of Terrorist Funding and then present measures taken against it.

2.1 TERRORIST FINANCING MEASURES

2.1.1. LEGITIMATE BUSINESSES

Legal businesses are a common source of funds for terrorist groups and can range from small businesses, like fisheries and farms, to large companies and investment corporations. The FATF report (2008) points out that this is particularly the case in regions where starting a business does not require substantial investment, and where the relation between sales reported and actual sales is difficult to verify because of inefficiency or a low level of financial regulation in the region. Southeast Asia was one such region; its rapid economic expansion in the 1990s provided a business-friendly environment and encouraged the establishment of companies and firms, but the formal financial regulatory system was not developed for years after the expansion. Al Qaeda was quick to capitalize on this situation, especially in Malaysia, which also later became an international centre for Islamic banking, and established many formal revenue-generating companies, many of which are still functioning today (Abuza, 2003). It has also been noted that al Qaeda has established many formal businesses across the Middle East. Its companies in Khartoum included a holding and construction company, investment companies, transportation business, and agro-business (Weichardt 2006:307). Other companies in the Sudan include Blessed Fruits (exporting fruits and vegetables), Al Hijra Construction (road building), International al-Ikhals (manufacturing sweetmeats), and others.

2.1.2. FORMAL FINANCIAL SECTOR

The formal banking sector still serves as one of the main ways to move funds across the globe. The reliability and speed allows groups to move assets quickly and effectively. To ease the process, terrorist groups employ and recruit,

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either people that know about and work within the financial sector, or train their own members in the mechanisms of the international banking system to avoid detection while transferring funds. That way, al Qaeda was easily able to move hundreds of thousands of dollars across the globe by keeping the transactions under the £10,000 detection threshold. Additionally, access to this sector is easy and transfers can be made over the phone, internet, or by using third-party links, such as lawyers or accountants. Wire transfers involving cash in the formal banking sector turned out to be a primary technique to move terrorist funds in the study conducted by FATF in 2009 (FATF 2010:24).

2.1.3. CREDIT CARD FRAUD AND PRE-PAID CARDS

One of the easiest ways to generate money for terrorist groups is through the misuse of credit cards. Mainly because the data that needs to be acquired for this purpose is easily accessible, such as a card holder's name, billing address, phone number, and expiration dates. One of the main sources of funding for the attacks in Bali was the selling goods acquired through stolen credit cards (Abuza 2003). The proliferation of internet transfers increased the capacity to move large sums of money from country to country without it being subjected to formal financial regulations. Raymon (2008:13) points out that terrorist organizations use all sorts of measures including debit cards, other stored value cards, online value transfer systems, online value storage systems, pre-paid cards, credit cards, and charge cards. This allows the movement of funds through networks without necessarily using banks. Al Qaeda's European financial hub, which relies on credit-card fraud, is estimated to generate around \$ 1 million per month, all of which is shipped to the Middle East and Pakistan (Rohan Gunaratna, 2003:87).

2.1.4. DRUG TRAFFICKING

Money generated from selling drugs has been an increasing source of revenue for terrorist organizations since the decline of state-sponsorship after the Cold War. Moreover, globalization of the financial markets and the increasing opportunities for trade have allowed terrorist groups rapid expansion in this market and, subsequently, for generating larger sums of money. Hezbollah, for instance, is reported to have a strong operational base in South America where it exports drugs, arms, and stolen goods. Al Qaeda has also established business relations in South America with groups like FARC and the National Liberation Army of Columbia (Politis 2003:267 and Weichardt 2006:306). Another centre for the drug trafficking business is Southeast Asia. In a report conducted in 2003, the Thai government announced that around \$3.3 billion is laundered annually in drug money through financial institutions and that almost 40 percent of Thailand's GDP is unregulated and untaxed, a majority of which benefits terrorist and crime groups (Abuza 2003:187). Nonetheless, the most important and most resourceful region for generating drug-money is Afghanistan, where the Taliban regime continues to support al Qaeda through taxes on opium production (estimated to constitute from 70 to 90 percent of the world supply) and trafficking (Weichardt 2006:307).

2.1.5. OTHER SOURCES

Apart from the few main funding sources outlined above, there are plenty of other ways to gather funds. Still, the simplest method of avoiding formal regulations is either by the transfer of hard cash, or transforming money into valuable commodities like gold, diamonds, and other stones to avoid the audit trail. Jama'at al Islamiyah in Malaysia is mainly funded through cash couriers sponsored by al Qaeda. As Abuza (2003:179) reported, the organization has received about Rpl. 35 billion from al Qaeda since 1996. Hezbollah has also raised millions of dollars over the years by buying commodities for lower prices and selling them in places with different tax rates (Freeman 2011). Another profitable way of gathering funds is by extorting taxes. The Pakistani Taliban produces a list of various fees for different activities and companies, which have to give additional tax to the Taliban regime. The PLO is reported to have extorted up to \$10 million per year from airlines and around \$220 million from OPEC (Freeman, 2011:466).

2.2 RESPONSES

2.2.1. INTERNATIONAL RESPONSES

One of the biggest and most effective bodies that deal with AML/TF measures is the Financial Action Task Force (FATF). The FATF is an inter-governmental body created in 1989 by the G7 countries. Since its establishment, it has

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expanded and now includes over 30 countries from across the globe. It is the main body that creates and regulates AML/TF measures by producing legislative recommendations for member-states. In 2003, the FATF issued forty recommendations for AML/TF, and as a result of which the Non-Cooperative Countries and Territories List (NCCT) was established. The NCCT identifies countries that fail to meet FATF regulations. So far, it has been effective in pressuring countries to impose stricter financial regulations, and since 2003, 23 countries have adopted its recommendations (Hett 2008:30).

Before the 9/11 attacks, little attention was paid by the international community to the issue of terrorist financing. The UN International Convention for the Suppression of the Financing of Terrorism was adopted in 1999, but only 4 states ratified it by 2001. One month after the attacks, the CTF was added to the FATF mandate, which produced nine special recommendations on this topic (House of Lords, 2009:13):

1. Ratification and implementation of the 1999 United Nations Convention for the Suppression of the Financing of Terrorism and relevant UN Security Council Resolutions;
2. Criminalizing the financing of terrorism, terrorist acts and terrorist organizations;
3. Freezing and confiscating terrorist assets;
4. Reporting suspicious transactions related to terrorism;
5. Providing the widest possible assistance to other countries' law enforcement and regulatory authorities for terrorist financing investigations;
6. Imposing anti-money laundering requirements on alternative remittance systems;
7. Strengthening customer identification measures in international and domestic wire transfers;
8. Ensuring that entities, in particular non-profit organizations, cannot be misused to finance terrorism; and
9. Putting in place measures to detect physical cash movements.

FATF provisions set global standards in dealing with the dangers of ML/TF, especially with those mentioned in Section 2.1., and have a record of success in identifying patterns of terrorist financing, as well as detecting cash movements and illicit businesses.

The UN Convention against Transnational Organized Crime, adopted on November 15, 2000, is the main international instrument in the fight against transnational organized crime. It has now been ratified by the great majority of UN members, and requires them to criminalize and to institute measures to counter TF, and to adopt measures for the confiscation of the "proceeds of crime." Additionally, UN Resolution 1267 (1999) set up a Sanctions Committee of the Security Council to "freeze funds owned by or used for the benefit of the Taliban. Resolution 1333 (2000) strengthened the sanctions of the earlier Resolution, providing that States are to freeze funds and other financial assets of Osama bin Laden and individuals and entities associated with him as designated by the Sanctions Committee, including those of Al-Qaida" (House of Lords, 2009:18). In addition, Resolution 1373, passed in 2001, recognized the need for states to complement international initiatives by taking additional measures to prevent financing and the preparation of any acts of terror. These included: freezing financial assets or economic resources, prohibiting their nationals from making funds for the benefit of persons who commit or attempt to commit terrorist acts, and criminalizing terrorist financing and adopting measures requiring licensing and registration of private financial service providers. Also, in compliance with this provision, the UK has listed over 50 people on the sanction list (House of Commons: Terrorist Asset Freezing, 2010). Additionally, the UN passed the International Convention for the Suppression of the Financing of Terrorism, which imposed "know your customer" procedures, obliged participating countries to criminalize the provision or collection of funds for terrorist activity, and implemented SARs[1] requirements (Raphaelli, 2003:35).

The Council on Foreign Relations Independent Task Force on Terrorist Financing has also pointed out a number of initiatives that have been undertaken over the past years with regard to AML/TF measures (CFR Report, 2004:10):

- The G8 established a Counter-Terrorism Action Group (CTAG).
- The UN's al-Qaeda and Taliban Sanctions Committee has expanded the list of terrorist entities against which all states are required to restrict financing.

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- In collaboration with the FATF, the International Monetary Fund (IMF) and World Bank have assessed forty-one countries' compliance with anti-money laundering and countering terrorist financing (AML/CTF) standards in a pilot program.
- Cooperation on terrorist financing has become a permanent part of the agendas of regional organizations such as the EU, Asia-Pacific Economic Cooperation (APEC), the Association of Southeast Asian Nations (ASEAN), the Gulf Cooperation Council (GCC), the Organization of American States (OAS), the Organization for Security and Cooperation in Europe (OSCE), and the African Union.

2.2.2. EUROPEAN MEASURES

Three major initiatives have been undertaken at the European level: (1) the third money laundering Directive was adopted in 2005 which deals with terrorist financing – declaring the financing of terrorist activities a criminal offence and introducing additional requirements; (2) the Protocol to the Convention on Mutual Assistance in Criminal Matters, adopted in 2001, deals with requests for information on the identity of the holders of bank accounts, requests for details of those accounts and of banking transactions, and requests for the monitoring of banking transactions; and (3) the Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism—the Warsaw Convention, which serves as the first comprehensive international treaty covering both the prevention and control of money laundering and the financing of terrorism (House of Lords Report, 2009:17).

On May 10, 2010, the European Parliament adopted a decision authorizing the Commission to establish the Terrorist Financing Tracking Programme (TFTP) jointly with the US Government (Council of European Union – File 2010/0177, 2010). The purpose of this programme is to make available to the US Treasury Department financial messaging data stored in the EU. To date, the TFTP has generated a substantial amount of intelligence which has benefited both parties in effectively fighting against TF.

2.2.3. US

Efforts undertaken by the US government under the International Economic Powers Act include intelligence activities, enforcement efforts, as well as the designation of terrorists or terrorist organizations and individuals. The passing of the US Patriot Act (Uniting and Strengthening America by Providing Tools Required to Intercept and Obstruct Terrorism Act) gave the government new laws to restrict access to the US financial system for states and individual foreign financial institutions that lack adequate anti-money laundering controls. (Raphaelli 2003:34). Many investigations undertaken by US law enforcement resulted in prosecutions for internet-related activities with regard to terrorism financing (including al-Hussayen and Babar), the broader targeting of money remitters without appropriate AML/TF compliance systems, and the closing of many websites that were related to terrorism financing (Jacobson 2010:8). Another example of an effective AML/TF measure involves the US Currency Transaction Reporting (CTR) requirement under the BSA (Bank Secrecy Act). As Forman reports (2006:116), “the CTR requirement has forced criminal organizations to attempt to avoid filings, which actually results in behavior patterns and schemes that can be readily detected. The avoidance of CTR filing is an easily detectable indicator of criminal activity that has been successfully detected and used by law enforcement in thousands of cases.” Additionally, when President Bush signed Executive Order 12334, and invoked the International Emergency Economic Powers Act (IEEPA), a large amount of funds in U.S. banks with suspicious links to terrorists were frozen and many transactions were stopped (Basile 2004).

Another successful initiative has been undertaken by US Immigration and Customs Enforcement (ICE) in the form of “Operation Cornerstone,” which aims to target the means by which terrorists gather their funds by working with financial, trade, manufacturing, and transportation sectors across the globe. Through this initiative, Cornerstone is working closely with the private sector in detecting counterfeit merchandise, import-export crime, human trafficking, as well as cash and drug smuggling. As a result, ICE managed to identify and dismantle numerous networks operating in the US, UK, Spain, and other European countries, which were responsible for gathering and storing funds for TF purposes (Forman, 2006:17).

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In particular, in response to digital currencies and internet transfers used for TF purposes, various regulations were put in place in the belief that the private sector, as opposed to the government or formal banking system, is better equipped to recognize the patterns and indicators of terrorism financing. As such, if it is assumed that a digital currency provider is a financial institution, many regulations under the Bank Secrecy Act are imposed on such an industry, including obligations for the financial reporting of common transaction patterns, maintaining transaction records, and information regarding account holders and their accounts. Such regulations also require filing SARs to the Treasury Department for any transaction involving more than \$2,000. Also, all digital currency providers now have to register with the Financial Crimes Enforcement Network (FinCEN), along with the list of their agents and employees, and must renew their registration every two years. Under those regulations, over 40 incidents of digital money transfers used for TF have been detected (Hett 2008:16).

2.2.4. The UK

In particular, in response to the threat posed by pre-paid card providers and credit-card fraud, FIUs (Financial Intelligence Units)[2] have been established. Following FATF recommendations for establishing cooperation between the FIU and counter-terrorist agencies, intelligence organizations, the law enforcement sector, and the formal banking sector, the case-studies in the UK show that: (1) joint investigations resulted in identifying methodologies used by the suspects and effectively stopped identity theft, credit card fraud, and mortgage fraud; (2) it was possible to identify terrorist financing activity even though it was not possible for banks themselves to link the suspicious activity to terrorism; (3) joint efforts provided valuable information that was used in identifying additional accounts and individuals linked to terrorist financing cases under investigation, which gave the law-enforcement agency a broad network of individuals included in terrorist financing initiatives; (4) financial information acquired after the suicide attacks in London was helpful in identifying valuable information including vehicle hire, accommodation, procurement, and overseas travel, which then led to identifying certain members of the group and their affiliates; and (5) the financial trail was used to identify attack indicators, and by extensive investigation, the FIU and law enforcement established the travel patterns of individuals, small items sent to the same country by international courier over many months, as well as multiple transactions to accounts controlled by an associate. (FATF 2008:30-37). Many similar results have been seen in other countries.

The UK government is also creating a cyber-coordination unit located in Whitehall that will lead actions against ML and TF across the Internet (Williams, 2009). In addition, the Anti-Terrorism, Crime and Security Act was passed in 2001, which allows for measures to “cut off terrorist funding, facilitate sharing of information between law enforcement agencies and public authorities, increase investigative powers and to provide for new offences in relation to the duty to disclose information or suspicion of terrorist financing” (Leong 2007:143). In 2005, the Serious Organized Crime and Police Act was passed, part of which establishes the Serious Organized Crime Agency (SOCA), a public body reporting on activities connected with serious organized crime at all levels. According to the Act, SOCA takes over responsibility for the Financial Intelligence Unit (FIU) and controls the database of suspicious activity reports (SARs). In the same manner, the FSA (Financial Services Authority) has been given powers to deter criminals from using financial systems (including the power of criminal prosecution for breaching the ML/TF regulations), and has itself made some regulatory rules and recommendations (Leong 2007).

To date, measures introduced in the UK have led to the conviction of over 200 people over TF-related issues, and police and intelligence agencies across the country have disrupted over a dozen attempted terrorist plots using the financial trail and implementation of other AML/TF measures (Home Office, 2010).

SECTION 3– MAIN INDEPENDENT VARIABLES: THE METHODS THE WEST CANNOT DEFEAT

While dealing with financing terrorism, it is important to take into consideration not only the methods that deal with gathering funds, but also the methods that are used to transfer money to different locations. This section will look closely at two main ways of funds gathering, which are state funding, and charities and NPOs. Moreover, the two main ways of moving funds across the globe, those being the Islamic banking and taxation system, and Hawala – the traditional Islamic remittance system – will also be discussed.

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3.1. STATE FUNDING

State sponsorship substantially declined after the Cold War but still continues to be one of the primary sources of funding for terrorist groups across the world, especially Islamic ones. Today, apart from the formal US State Department list of State Sponsors of Terror (SST), we can identify a few more countries that are not compliant with international AML/TF measures and that have been known to sponsor terror groups, particularly Saudi Arabia. For now, let us focus on those listed as SST in the Middle East and North Africa. The current list contains four countries including Syria, Cuba, Iran, and Sudan, as of August 27, 2011 (US State Department, 2011).

Iran is probably one of the most prominent sponsors of international terrorism. Apart from setting up training camps, Iran funded Hezbollah by providing them with money and resources for attacks and operations. It has been reported (Freeman 2011:456) that Iran is currently providing Hezbollah with an estimated \$100 million per year, which accounts for about 50% of its overall funds. Additionally, according to the US State Department's report (2011: ch.2, para.34), Iran continues to fund, train, and provide weaponry to Shia extremists in Iraq to fight against US and coalition forces. Iran also fails to comply with FATF standards such as the establishment of Financial Intelligence Units, freezing or blocking accounts at banks and non-financial institutions connected to TF, criminalizing TF, and requiring financial institutions to provide SARs. Likewise, Syria's al-Assad regime is also providing weaponry, money, and shelter for Hezbollah and other terrorist groups in its territory, including the Palestinian Islamic Jihad (Freeman, 2011). Syria also provides arms smuggling routes for Hezbollah, from Iran to Lebanon (US State Department, 2011). Sudan is one of the most popular shelter-states for terrorist organizations. Al Qaeda, the Egyptian Islamic Jihad, the Palestinian Islamic Jihad, Jama'at al Islamiyah, and Hamas are all known to have bases and receive technical support from Sudan (Politis 2003:262).

Saudi Arabia is a subject of investigation for almost every international body dealing with terrorist funding, particularly with its links to al Qaeda financing through charities. The Saudi government is involved with financing numerous groups operating across the Middle East, but also in initiatives that broaden the Islamic Jihad on its own territory. In 2000 alone, Saudi subsidies to various Islamist groups amounted to \$500 million, some of which was spent on developing *ulemas* and *madrassas* (radical Islamic religious schools) in the country (Politis 2003:260). Internationally, the Saudi government is exploiting diplomatic channels to sponsor individuals and groups overseas. As Raphaeli (2003:72) reports:

"in December, 2002, it was revealed that Princess Haifa al-Faisal, the daughter of the late King Faisal and the wife of the Saudi Ambassador to the United States, had paid a monthly stipend of \$2,000 to the allegedly needy Saudi family of Omar al-Bayyuni between December 1999 and May 2002 through Mrs Osama Basnan in Santiago, California. Part of this stipend found its way to two of the terrorists who participated in the 9/11 attack on the Twin Towers in New York."

Even though the Saudi government is a formal ally to the United States, it has not implemented AML/TF laws and regulations, and did not cooperate with Western governments requesting information on the status of their implementation. Moreover, since the 9/11 attacks, not a single Saudi donor of funds to terrorist groups has been publicly punished and key financiers (Yasin al-Qadi – designated global terrorist, Wa'el Julaidan – supporter of al Qaeda, as well as Khalid bin Mahfouz, Saleh Abdullah Kamel (Bisard, 2002:11), and many more) remain free. The assessment conducted by the Council on Foreign Relations groups Saudi Arabia with Egypt, Pakistan, and other Gulf states as "source and transit countries," which means that terrorist financing originates in these countries, and that donations from other countries pass through them (CRF Report, 2004:8). Finally, UNSC Resolution 1373, dealing with monitoring and sanctioning terrorist assets, has not been implemented in Saudi Arabia.

Ironically, even the EU has been funding Fatah's terrorist salaries through aid and money that was formally given to pay for administrative issues for the Palestinian Authority. According to Politis (2003:265), "the documents showed that about \$640,000 to \$1 million has been used for this purpose." Moreover, the Pakistani Inter-Services Intelligence agency (ISI) is the main source of Taliban funds, as well as other smaller organizations fighting for the control of Kashmir in Pakistan (Freeman, 2011:465).

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3.2. ISLAMIC BANKING SYSTEM AND TAXATION MECHANISMS

To understand the Islamic banking system and its taxation mechanisms, it is crucial to know that social justice, equality, compassion, and maintaining social equilibrium are the core values promoted by Islam and, since in many countries the financial system is intertwined with the religious and legal system, philanthropy and charity play a crucial role in Muslim societies. Under Sharia'h law, there is no separation between business and religion. As it will be demonstrated, because philanthropic and charitable sectors are an integral part of the economy and are politically institutionalized in the system under Sharia'h, this creates space for the abuse of those sectors by fundamentalists and terrorists.

3.2.1 ZAKAT

Since the Qur'an is considered the ultimate source of knowledge about human life, it emphasizes compassion, social justice and, most importantly, wealth distribution. As such, one of Islam's five pillars of faith is the collection and distribution of Zakat, which obliges Muslims to give 2.5% of their annual income to those in need. Zakat has been described as the "cornerstone of the financial structure in an Islamic State" (Bisard 2002:12). It was estimated (Crimm 2008, 587) that the amount of money distributed through Zakat exceeded \$200 billion per year across the globe and around \$10 billion in Saudi Arabia alone. Under the Qur'an, Zakat should be destined for the poor, but because of the very character of Islamic financial transactions, the nature of the collection and distribution of Zakat is interpreted in various different ways. Thus, many Islamic scholars justify the use of Zakat funds for Jihad and some of the donations have been used to spread religious extremism or have been used to finance terrorism.

Under Islamic law, the intention and motives behind financial contracts are an essential consideration and affect the validity of the transaction. The formality of a legal act can be the same, but the end result depends on the intention (Sanusi 2008:251). In other words, the transaction of funds originating from Zakat, if considered by a religious scholar as, for example, the payment for religious efforts, or 'Jihad' for martyrs (warriors of freedom), the intentions are good, and so is the transaction. The issue of motive and intent is critical in legal contracts under Islamic law.

Even more, monitoring Zakat donations is almost impossible as most countries with Islamic banking systems lack effective legal and auditing instruments to control the flow of charitable donations, thus, turning it into an illegal money-laundering machine. Following this loophole, bin Laden utilized extensively the confusion between religion and finance, and relied on Zakat donations to fund al Qaeda activities (Bisard, 2002:12). This scheme is utilized by many terrorist groups across the Muslim world. The way in which Zakat is used as a source of funding through charities will be showcased later.

3.2.2. ISLAMIC BANKING SYSTEM

Due to the globalization of financial markets, macroeconomic reforms, the liberalization of capital movements, and the global integration of financial systems over the past twenty years, there has been growth in global Islamic finance mechanisms. Some sources say that funds under Islamic financial institutions are growing at an annual rate of up to 20% per year with the total value of Islamic funds management adding up to over \$200 billion (Zaher and Hassan, 2001:54). The Islamic banking system is very different from the Western one, particularly in the sense that, due to the fact that it is controlled by religious law, it forbids profit-making on interest-based mechanisms (used in all Western banking systems), which is considered illegal under Sharia'h law. As such, Islamic banking is based on a PLS-system (Profit-Loss Sharing), and is currently integrated into over 60 countries and over 250 Islamic financial institutions throughout the world, as it provides for "cohesion between social classes because financing is equally available to anyone with a productive idea" (Zaher and Hassan, 2001:160). Under the PLS, and because Islamic banks are religiously forbidden to pay interest to their investors, banks operate by sharing profits or projects, participating in investments, and earning fees for banking services. Along with the growth of Islamic banking, the system became irreversibly linked to capital markets across the world and serves as a primary channel for investments and transactions into the oil-rich Middle Eastern regions. This allows terrorist groups to use front companies to channel money through its system.

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Al Qaeda has been reported to use this advantage extensively. Basile (2004:175) observes that “the Advice and Reformation Committee, a presumed front for al Qaeda, received funds in a Barclay’s account from correspondent Islamic banks in Sudan, Dubai, and the UAE. The funds in the Barclay’s account were then forwarded to operational cells in Western Europe by the signatory on the account, a presumed Al Qaeda associate.” To the advantage of terrorist groups, such transfers are not subjected to the usual scrutiny of Western financial systems. Most importantly, measures taken to curb such transfers are very likely to impact the ability of large corporations to invest in the region and, therefore, are unlikely to be implemented (Basile 2004). Al Qaeda not only used this system, but also invested in its own banking structures to help redistribute funds. Bin Laden, in partnership with several Saudi and Gulf Islamic banks was reported to have founded a banking institution in Sudan called the “Al Shamal Islamic Bank,” which provided funding for his operations (Bisard 2002:12). Dar al-Maal al-Islami (DMI) is one of the institutions created in early 1980s by Saudi Arabia with the aims of spreading Saudi financial influence in the Arab world and, most importantly, supporting the radical Islamic cause. Growing over the years, DMI is currently one of the central bodies for financing international Islam, sponsoring and supporting institutions like the Islamic Investment Company of the Gulf, the Faisal Islamic Bank of Bahrain, and Faisal Finance, some of which were reported to accumulate and distribute funds used for terror purposes (Raphaelli 2003:71). In short, Islamic banking systems acted and continue to act as facilitators and transfer mechanisms for terrorist organizations.

3.3.HAWALA – ALTERNATIVE REMITTANCE SYSTEM OF CHOICE

Hawala is one of several Alternative Remittance Systems (ARS) used by terrorist groups, primarily for financial transfers across the globe. Hawala can be found as an Islamic legal concept as early as the year 1327 (Schramm and Taube, 2003). Therefore, it is an eight-century-old traditional Islamic institution that was developed due to the lack of formal financial mechanisms, is based on trust, and is embedded in the religious and social dynamics of Islamic communities. This particular system offers many benefits for organizations and individuals that want to move funds quickly, efficiently, and without leaving a trace. Hawala, like Islamic banking systems, is controlled by Sharia’h law, but unlike in the formal sector, no money is wired, no names are taken, no account numbers used, and no records kept. Schramm and Taube (2003:407) do a great job in explaining the particularities in the functioning of the Hawala system:

“If a client wishes to transfer a certain sum of money, he meets with the local Hawala intermediary in his village, and tells him the amount of the payment and where and when it has to be made. The Hawala intermediary takes the sum and a small additional handling fee and gives the client a code, a simple word or a particular verse from the Koran. Then, the intermediary contacts his partner in the relevant target area and tells him the code and the amount to be paid out. In passing on this information, the Hawala intermediary in the transaction’s place of origin has completed his part in it. If it has been necessary for him to keep any written record of the transaction up to this time, it can now be destroyed. The client, meanwhile, tells the recipient the code. The recipient contacts the Hawala intermediary in the target area, passes on the code, and accepts payment. Once the payment has been issued, if not before, the intermediary in the target area destroys any notes or other indications of the transfer.”

Schramm and Taube 2003:414

First, the characteristics of this system will be considered, and then the importance and global reach in regard to moving terrorist funds will be presented. Hawala proves to be a particularly cheap method of moving funds across the border, with commissions of only around 2% (Abuza 2003:183) (with average bank fees of up to 15 %), Hawala presents itself as a great money-saver which is of great importance while transferring large amounts of money. Also, it offers transactions in a very short period of time, with most transfers made within 24 hours. Moreover, and most importantly, Hawala leaves no record and no track of the transactions. The efficiency of the system can be seen in the amount of funds transferred throughout the world.

Since Hawala is beyond all of the classical instruments of monetary policy, and functions below legal and financial radars, it is almost impossible to account for and control its transactions. In Pakistan, only around 20% of the money that is being remitted to the country annually arrives through the formal banking system. The rest is transferred through Hawaladars. In the same manner, Hawala is used extensively in Southeast Asia. For example, over \$6 billion (Abuza 2003:185) is remitted annually to the Philippines using the system because of the weak banking sector and

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no regulatory framework. More importantly, research shows (Abuza 2003, Raphaeli 2003, Basile 2004) that when measures are being taken to stop currency flows and regulatory standards are imposed, remittances through ARS become increasingly popular, as the new regulatory framework drives brokers underground, making monitoring and regulations even more difficult. Between 2001 and 2005, around \$30 billion was moved through Hawala across the Middle East (Spiegel-Online, 2001). Globally, the numbers vary from \$200 billion (Intern.de, 2001) to about \$2 trillion (Raphaeli, 2003:70) per year, which moves without any regulatory standards.

Even measures imposed in accordance with FATF standards have proven insufficient in regulating this financial system. Hawala keeps functioning as probably one of the most efficient and un-traceable systems ever found, posing a great risk for western countries when used for financing terrorist acts.

3.4. CHARITIES AND NON-PROFIT ORGANIZATIONS

Probably the biggest sectors that generate, as well as move funds, for terrorist-related purposes are charities and non-profit organizations. They are used particularly because they possess characteristics/vulnerabilities that make them very attractive for the illicit generation of funds. Not only can they generate funds from across the world, but can also operate in a global manner, establishing branches and sending representatives to different countries. Moreover, charities enjoy public trust and are subjected to lighter scrutiny by financial authorities.

As mentioned before, Islamic charities, apart from direct investors and donors, membership fees, subscriptions, and events, are generating funds for themselves using public support in the form of Zakat – the obligatory Muslim tax. This mechanism makes charities a very stable and reliable source of income. There are many ways in which funds can be generated and moved through charities and NPOs. For example, al Qaeda has been generating a large part of its income by inserting its chief operatives in top positions in many Islamic charities operating across Southeast Asia, the Middle East, as well as the US. (Raphaeli 2003:68). Alternatively, organizations like Hamas and Hezbollah include charities in their organizational structure, therefore creating a solid base of funding (Hardouin, 2009). Two years after the 9/11 attacks, there were around 300 Saudi charities established in Saudi Arabia and the Gulf region with an annual income estimated between \$3 and \$4 billion (Bisard, 2002:26). Other research (Abuza 2003:173) shows that of those 300 charities, 20 were established by Saudi Intelligence to fund the Afghan Mujahadeen, and sent around \$6 billion a year to Islamic causes abroad, and around \$1.6 million per day is donated by Saudi donors alone. Following this path, the Afghan Taliban has been receiving money from charities located across the Middle East in sums estimated from \$150 million to \$200 million per year (Freeman, 2011:470). It has also been estimated that up to 20% of Islamic charity funds in Indonesia and about 50% in the Philippines are directed toward terrorist groups (Abuza 2003:173).

The main charities involved in financing terror causes across the world include the Al-Haramain Islamic Foundation and the Global Relief Foundation (associated with al Qaeda and the Benevolence International Foundation (Al-Bir Society)), which provide money for Chechen groups. Also, the International Islamic Relief Organization (IIRO) (founded by Usama bin Laden's brother-in-law) or Holy Land Foundation for Relief and Development, and the Quranic Literacy Institute, financially support Hamas (Bisard, 2002:27; Freeman, 2011:471). Usually, the way in which terrorist groups receive funding from charities is very simple. Basile (2004:174) provides a clear example of funds channeled to al Qaeda using the case against Ennam Arnaout, and his Benevolence International Foundation:

“Funds would be allocated, and accounted for, by the charity for community development and charitable activities. Once the full amount was pulled out for the charitable project, a small percentage (around 10%) of the cash was skimmed off the top and physically passed to an Al Qaeda operative who deposited this clean money into Al Qaeda accounts in the Middle East or dispersed it to operational cells in other parts where Al Qaeda operates.”

Most importantly, however, unlike the charities established in the West, those in Asia and the Middle East are almost completely unregulated and allow for the transferring of large sums of money across continents without being scrutinized. This is not to say that charities and NPOs in the West are not subjected to this problem. In fact, it is the opposite; let us consider one of the many examples from the West.

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Viva Palestina

Viva Palestina (VP) is an organization, established by George Galloway, the former British MP for Bethnal Green and Bow, which claims to be a non-profit organization that delivers humanitarian aid for people suffering in Palestine. A sister-branch was established in the US, called the "Viva Palestina US" (VPUS). Galloway's organization led three convoys to Gaza in 2009 and also organized a flotilla to Gaza in 2010. The operations of VP and VPUS have been proven to provide material and financial resources to Hamas, whose representatives are also sitting on VP's executive board in the US. The report conducted by the Investigative Project on Terrorism (an American research group recognized as the world's most comprehensive data center on radical Islamic terrorist groups) has established that Galloway's campaign is "more about supporting and legitimizing Hamas than it is about providing aid to the needy. [...] They treat Hamas leaders as the legitimate representatives of the Palestinian people and provide both material and moral support to the terrorist organization" (IPT: VP Report 2009:3). Due to the fact that VP lacks formal non-profit status, all funds collected by VP and VPUS are handled by IFCO (Interreligious Foundation for Community Organizations), whose tax exempt forms for 2005 and 2007 show subsequent contributions for \$805,544 and \$742,812 (IPT: VP Report, 2009: 6). Gaza convoys organized by VP on route to Gaza have made several stops in Turkey, Syria, and Jordan, where the group received greetings from members of Hamas and the Muslim Brotherhood. In February 2009, a few members of the convoy were arrested in the UK under allegations of smuggling large amounts of money to Syria. During the third convoy, Galloway's group clashed with the Egyptian police while trying to enter Gaza. One guard was shot dead by a Hamas member. When the convoy arrived in Gaza, VP's members handed over keys to the trucks to Ahmed al Kurd, a Hamas leader who was previously designated by the US Treasury Department as a terrorist (Frenkel 2010). Whether the money has been distributed to the Palestinian people is still not known.

Viva Palestina, which is still functioning, represents only one example of sham charities and NPOs established and operating in the West. Other institutions found guilty of supporting terror and moving funds include: The Council on American-Islamic Relations (CAIR) (America's largest Islamic organization), the Islamic Society of North America, the Global Relief Foundation, the Islamic Association of Palestine, Khalifah Ramadan, and many more. Clearly, even where judicial and formal monetary policies put restrictions on charities and NPOs in the West, many of them easily find ways to gather and move funds in support of terrorist organizations by adapting to, and abusing, democratic procedures and by using public figures.

SECTION 4 – DEFINING CAUSAL MECHANISM: WHAT WENT WRONG? INEFFICIENCY AND LACK OF COOPERATION

The amount of AML/TF legislations passed all over the world since 9/11 has been enormous. Clunan (2006) argues that the ultimate effectiveness depends on a state's redefinition of its national interest to include such measures, and also understanding the theme of collective responsibility.

The main concern for the US government is the lack of coordination and integrated strategy with which to deliver AML and CTF training and assistance to vulnerable countries. The biggest problem we can observe is the internal malfunction of the US political system when it comes to dealing with a coordinated strategy. First, as the Government Accountability Office reports (GAO 2005), the Treasury does not accept the State's Department leadership of the Terrorist Financing Working Group's (TFWG), which is supposed to deliver training and technical assistance for countries abroad. The two departments also disagree on the procedures of implementation and delivery of AML/CTF measures. This internal dispute results in ineffective implementation and delivery of AML and CTF measures to many countries. Second, the US government has been missing a "clear presentation and objective assessment" (2005:2) of its resources and, as such, has not been able to allocate appropriate measures where needed. Finally, since the FATF measures consist only of a general framework, the government is missing a clear system of assessing and measuring the performance of AML/CTF implementations. Similar internal bureaucratic disagreements have also been observed between the US Customs Service and the FBI Terrorist Financing Operations Section, and a few other agencies. In the same manner, the enforcement of AML legislation in France has been limited by the internal

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dispute between Tracfin (French Financial Intelligence Unit) and the French government (Favarel-Garrigues et.al., 2011). As a result, decision-makers are not aware of the full range of measures at their disposal and the general effort is constrained by a lack of effective leadership and implementation.

Internationally, in terms of the implementation of regulations, there are two fundamental problems. First is the fact that many states are missing an institutional capacity, as well as political interest in enforcing important AML and CTF measures because of, as Clunan argues, competing interests of those in power and those outside of government (2006:574). Also, there is a basic problem in assessing risks in accordance with such measures. Lopez identified a problem with SARs that occurs globally. The inefficiency of reporting and detecting illicit funding does not come from a lack of regulations, but from a lack of institutional capacity. SARs are useless if staff are not properly trained to detect them and are provided with the appropriate tools to analyze them (2006:54). It has also been the case that most of the states rely on legislations and freezing terrorist assets allocated in formal financial institutions with hardly any, or none, measures taken against moving funds through alternative remittance systems or NPOs. Lastly, probably the biggest institutional issue, as argued by McDonagh (2008), is the fact that most of the international AML/CTF legislations, given their complexity and pace, and arising from vast changes, are extremely hard to implement.

When the US government introduced the Patriot Act in October 2001, this legislation imposed a variety of obligations on the formal banking system and financial institutions, including additional reporting requirements, stricter customer identification measures, a prohibition on US banks maintaining accounts with offshore banks and, most importantly, it allowed for monitoring every transaction in the world conducted in US dollars. As a result the US ceased to be the center of international money laundering, which seemed to be the desired effect. Nonetheless, as the flow of illegal funds declined, the global turnover of US currency decreased. At the same time, due to the fact that US financial institutions could not conduct business with tax havens and offshore banks, and it could penalize Western banking institutions for not reporting transactions in US dollars, big international banks started to encourage their customers to avoid making transactions and transfers in US currency (Napoleoni, 2010). As a result, not only did the weakened dollar cause harm to the US economy, but the legislation failed to secure the stability and security of international financial markets with regard to ML and TF and, in turn, allowed terrorist organizations to shift their financial center to European and Asian markets.

The US case suggests that a successful strategy will be much harder to develop and sustain than anyone expected. Effective reporting and implementation of measures has to start with re-designing a state's economic, social, as well as political systems, in both public and private domains, in order to adopt a comprehensive international and national legal framework that deals with the threat of terror financing. As Clunan argues, building this institutional capacity is a pre-requisite for effective action (2006:569). This, unfortunately, is missing from Western governments so far. As the case of the Patriot Act shows, the benefits of implementing measures that constrain financial institutions in the US have proven to be counter-productive in the sense that they weakened the US economy and only moved terrorist financing centers to other parts of the world. This case is of particular importance to other Western states because they are now more hesitant to implement similar legislation, presenting the international community with the typical Collective Action Problem. Therefore, as we have seen, states are likely to adopt international regulations, but are hesitant to enforce the changes or, as in the case of US, agencies are likely to pursue their own interests at the expense of the collective effort.

4.2. LOSING THE ULTIMATE BATTLE

Most importantly, however, it is not only the case of lack of effectiveness with Western governments in dealing with terrorist financing, but the very fact that while trying to curb it, governments have also lost public support and, thus, lost their legitimacy. In dealing with this issue, it is useful to adapt the Hobbesian concept of the Leviathan. We can argue that states have, to a certain extent, always limited the liberty of their citizens who, in turn, accepted such limitations for their protection. If we apply to this concept the legislative measures taken by the government, we can see that security comes at a double cost. As Vleck (2008:22) rightly points out, "first when the citizen exchanges liberties for increased security and second when the citizen accepts the obligation to contribute to the maintenance of the security of the state." The government's attempt to monitor, and in many ways limit, many aspects of our lives

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(extended surveillance, monitoring banking transactions, or keeping transaction records and personal details) in pursuit of terrorists can result in losing support and creates popular discontent within a democratic society. The case that proves the point was presented to the public by the American Civil Liberties Union in reference to legislative measures introduced in the US after the 9/11 attacks. The ACLU Report (2009) observes that the US Treasury has unchecked powers to designate organizations as terrorist-related and, to freeze funds, make arrests, and delegitimize institutions. "Today, the Terrorism financing laws are overly broad and lack procedural safeguards that would protect American charities against government mistake and abuse. The terrorism financing laws and the government's interpretation of them raise serious constitutional and human rights concerns. The counterterrorism legal framework is inherently vulnerable to mistake and abuse" (2009:9).

This global fight against terrorist financing presents many states with a very difficult liberty versus security dilemma. More importantly, one of the least desired, long-term effects of introducing strict regulations, closing legitimate charities, NPOs, limiting options for remittances sent to less developed countries, and virtually curbing the philanthropic initiatives across the globe, can result in deteriorating conditions in these countries. Lack of funding will result in greater economic deprivation (Crimm, 2008) and lack of welfare support, which will strengthen anti-government sentiments, ultimately providing a breeding space for terrorist organizations.

As it was shown, a lack of international, as well as national, cooperation between agencies, ignorance in dealing with the most sophisticated methods of fund-gathering and fund-moving measures, and the implementation of contradictory policies have resulted in a system in which the West cannot find a comprehensive strategy to curb the financing of Islamic terrorism.

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[1] SAR – Suspicious Activity Report is a report made by formal financial institution regarding potentially suspicious financial operations, which is forwarded to FIU (Financial Intelligence Unit) for further investigation

[2] Financial Intelligence Units – national centers for the receiving (and, as permitted, requesting), analysis and dissemination of STR [Suspicious Transaction Reports] and other information regarding potential money laundering

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or terrorist financing (FATF 2008)

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