



The EU and Counterterrorism Financing

Right Diagnosis, Wrong Patient?

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About Project CRAFT

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On 20 July 2021, the European Commission presented what it calls an ‘ambitious package of legislative proposals to strengthen the EU’s anti-money laundering and counterterrorism financing (AML/CTF) rules’.¹ Presented as an important overhaul of the existing EU AML/CTF framework, the package consists of four new legislative proposals: the establishment of an EU AML Authority (AMLA),² a Sixth AML Directive (6AMLD),³ a Regulation on AML/CTF⁴ and a Regulation on information accompanying transfers of funds and certain crypto assets.⁵ Together the last three proposals lay the foundations of an EU Single Rulebook on AML/CTF.

The impetus for this renewed urgency to combat money laundering and terrorism financing at the EU level was a series of money-laundering scandals involving major European banks, including ABLV, Danske Bank, Swedbank, Deutsche Bank, ING Bank and Pilatus Bank. After a first evaluation in the form of a ‘Post Mortem report’ (24 June 2019),⁶ an Action Plan (7 May 2020)⁷ and Council conclusions on AML/CTF (5 November 2020)⁸ were drafted and led ultimately to the four legal proposals mentioned above.

While the failure to comply with AML regulations is at the origins of the legislative package, the European Commission also stresses its relevance to CTF. It states that ‘[t]he aim of this package is to improve the detection of suspicious transactions and activities, and to close loopholes used by criminals to launder illicit proceeds or finance terrorist activities through the financial system and that the

measures will greatly enhance the existing EU framework by taking into account new and emerging challenges linked to technological innovation ... and the global nature of terrorist organisations’.⁹

This paper briefly examines the four legislative proposals with a focus on CTF,¹⁰ and asks if these proposals will enhance the EU’s effectiveness in this area. The paper argues that the measures might be the right response with regard to the failures identified after the various AML compliance-related scandals but seem to be a mismatch when it comes to improving CTF effectiveness and responding to the latest terrorism financing threats. Next, the paper makes a new diagnosis on which a policy enhancing CTF effectiveness should be based. Finally, recommendations are made for improving CTF effectiveness.

The EU AML/CTF Package

AMLA

The establishment of the AMLA has been hailed as the ‘centrepiece’ of the proposed legislative package.¹¹ This new authority should become operative in early 2024 and will have both supervisory powers and serve as a financial intelligence unit (FIU) support and coordination mechanism. The creation of the AMLA aims to resolve some of the key failings of the AML framework regarding supervision. These failings include, among others, the

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1. European Commission, ‘Beating Financial Crime: Commission Overhauls Anti-Money Laundering and Countering the Financing of Terrorism Rules’, press release, 20 July 2021.
 2. European Commission, ‘Proposal for a Regulation Establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and Amending Regulations (EU) No. 1093/2010, (EU) 1094/2010, (EU) 1095/2010’, 20 July 2021.
 3. European Commission, ‘Proposal for a Directive on the Mechanisms to Be Put in Place by the Member States for the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing and Repealing Directive (EU) 2015/849’, 20 July 2021.
 4. European Commission, ‘Proposal for a Regulation on the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing’, 20 July 2021.
 5. European Commission, ‘Proposal for a Regulation on Information Accompanying Transfers of Funds and Certain Crypto-Assets (Recast)’, 20 July 2021.
 6. European Commission, ‘Report on the Assessment of Recent Alleged Money Laundering Cases Involving EU Credit Institutions’, 24 June 2019.
 7. European Commission, ‘Communication on an Action Plan for a Comprehensive Union Policy on Preventing Money Laundering and Terrorist Financing’, 7 May 2020.
 8. Council of the EU, ‘Council Conclusions on Anti-Money Laundering and Countering the Financing of Terrorism’, 5 November 2020.
 9. European Commission, ‘Beating Financial Crime’.
 10. Due to their size and nature the proposals cannot be discussed exhaustively within the format of this paper. The author has chosen to focus on some key aspects potentially relevant to CTF.
 11. European Commission, ‘Proposal for a Regulation Establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and Amending Regulations (EU) No. 1093/2010, (EU) 1094/2010, (EU) 1095/2010’, p. 4.

lack of supervision of the group-wide AML/CTF policies of obliged entities that have a cross-border presence.¹² It also includes the lack of common supervisory standards, risk-assessment methodologies and monitoring and coordination of supervisors responsible for non-financial entities.¹³

Regarding law enforcement, one of the identified loopholes consists of the absence of joint analysis of cross-border money-laundering and terrorism-financing cases due to the lack of common tools and resources. The role of the AMLA would be to enhance cooperation and coordination among national FIUs and help them to improve their analytical capacity around cross-border illicit flows and facilitate information exchange.¹⁴

In general terms, high-quality supervision throughout the EU is important to signal the societal importance of fighting financial crime and to put pressure on obliged entities to take AML/CTF compliance seriously. By closing some of the identified loopholes regarding supervision – for example, the harmonisation of supervisory standards and methods at a higher level or the improvement of expertise levels within supervisory authorities – there may be a positive impact on the effectiveness of CTF, albeit indirect and impossible to quantify.

However, in recent years, terrorist attacks and plots in Europe have been mostly small scale, carried out by lone actors or small cells, financed with cash from illegal sources or through legal transactions so mundane that they did not raise suspicion. The challenge to effective CTF is for obliged entities to preventatively detect terrorist plots at all. Many terrorist plots remain undetected even when banks and other obliged entities would be fully AML compliant with strong supervision. Therefore, the supervisory issues that the AMLA is set to solve, and even the quality of supervision itself, seem to be less relevant for preventing this type of terrorism and its financing.¹⁵

The second aspect of the AMLA concerns increased cooperation between FIUs. The proposal suggests that the AMLA will be providing a stable hosting to the secure FIU communication network, FIU.net, which is now temporarily hosted by Europol, and the AML/CTF database, currently managed by the European Banking Authority. It also states that the AMLA ‘shall play a significant role in the conduct of joint analyses by FIUs, i.e. in the identification of relevant cases and the development of appropriate methods for the joint analyses of cross-border cases ... It shall promote expert knowledge on detection, analysis, and dissemination methods of suspicious transactions, provide specialised training and assistance to FIUs and prepare and coordinate threat assessments’.¹⁶ While the proposed FIU coordination and support mechanism may produce overlap with existing structures and initiatives – for example, those carried out within Europol or the Egmont Group – the proposed mechanism can potentially increase the effectiveness of the EU’s CTF efforts.

The lack of trust and willingness of law enforcement agencies to cooperate and exchange data on a national and international level, and the legal restrictions on doing so have been a common thread in post-terrorist attack evaluations.¹⁷ The past two decades have shown improvements both with regard to information sharing within FIUs and with the development of public-private partnerships to combat terrorism financing in which FIUs are involved. One of the operational successes in this field has, for example, been the ISIL project that was carried out in 2013–16 by several members of the Egmont Group of FIUs. In this project the finances of the Islamic State and foreign terrorist fighters were analysed through spontaneous multilateral information disclosure between the participants instead of bilateral information exchange. This project has generated new red flags with regard to terrorism financing and has led to the prosecution of alleged terrorists.¹⁸ As rightly identified by the European Commission, effective FIU

12. European Commission, ‘Report on the Assessment of Recent Alleged Money Laundering Cases Involving EU Credit Institutions’, pp. 21–22.

13. European Commission, ‘Proposal for a Regulation Establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and Amending Regulations (EU) No. 1093/2010, (EU) 1094/2010, (EU) 1095/2010’.

14. *Ibid.*

15. On the difference between being compliant with AML/CTF regulations and being effective against terrorism financing, see Mara Wesseling, ‘The European Fight against Terrorism Financing’, 2013, PhD thesis, University of Amsterdam.

16. European Commission, ‘Proposal for a Regulation Establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and Amending Regulations (EU) No. 1093/2010, (EU) 1094/2010, (EU) 1095/2010’, p. 12.

17. See, among others, US Government, ‘The 9/11 Commission Report: Final Report of the National Commission on Terrorist Attacks Upon the United States (9/11 Report)’, 2004.

18. Mara Wesseling and Marieke de Goede, ‘Beleid Bestrijding Terrorismedinanciering, Effectiviteit en Effecten [‘CTF Policies: Effectiveness and Effects’], University of Amsterdam, December 2018.

coordination and support depends in part on further streamlining certain practical issues.

However, to successfully make joint analyses and generate typologies and red flags, the nature of the terrorist threat is also important. One of the factors that made cooperation within the ISIL project successful was the scale and shape of the threat. It was possible to detect patterns because numerous foreign fighters were travelling to a specific region and made similar expenses and transactions.¹⁹ Moreover, there was a commonly felt urgency and agreement on the importance of the potential threat to all of the countries participating in the project. It remains to be seen how much FIU.net and joint analyses can contribute to threats from 'hard-to-detect' lone actors or small-scale plots.

The Sixth AMLD

The proposed 6AMLD and the two Regulations aim to harmonise AML/CTF rules across the EU. Since the 9/11 attacks, the EU AML Directive has become the core piece of legislation to translate the Financial Action Task Force's (FATF) international guidelines on AML/CTF into the European legislative framework. The Directive defines the principal elements of the EU's AML/CTF policy. In brief, the obligation for regulated entities such as banks to know their customers and monitor their transactions and to report suspicious transactions to a national FIU. In the proposal for 6AMLD parts of the current fourth and fifth AML/CTF Directives will become directly applicable rules in the form of the above-mentioned regulations. The purpose of the 6AMLD will be to regulate the organisation of the institutional AML/CTF system at national level, leaving the member states some flexibility.²⁰

The 6AMLD's new provisions on FIUs could have a positive impact on the effectiveness of combating certain types of terrorism financing. As specified in the proposal, FIUs play an important role in identifying the financial operations of terrorist networks and in detecting their financial backers.²¹ One of the failures in the current AML

framework concerns the uncertainty some FIUs experience with regard to the data that they are allowed to share with other FIUs and on which legal basis. One of the reasons for this uncertainty is the difference in legal setup and status between the FIUs in the EU. The proposed 6AMLD aims to clarify the powers of and practical cooperation between FIUs. This is partly done by suggesting a minimum (yet to be defined) set of data that FIUs should have swift access to and be able to exchange without impediments with their counterparts from other member states.

Although it is difficult to quantify how the proposed harmonisation and an improvement of data exchange between FIUs will have an impact on the effectiveness of the EU's fight against terrorism financing, post-attack evaluations throughout the 20-year War on Terror have shown repeatedly that barriers to cooperation between agencies were one of the main failures in detecting and preventing larger terrorist attacks.²² Therefore, any initiative to further lift barriers to cooperation may have positive effects on CTF.

Regulation on AML/CTF

The Regulation on AML/CTF proposes more precise and directly applicable AML rules compared to those in the current AML Directive.²³ The European Commission suggest a clarification and a more detailed definition of customer due diligence (CDD), ultimate beneficial ownership (UBO) and suspicious transaction reporting standards. It also proposes to update and broaden the range of obliged entities falling under the scope of the regulation. Furthermore, the Regulation would put an end to anonymous accounts and would set an EU-wide limit of €10,000 on large cash payments.

From a CTF perspective these measures are not expected to greatly enhance the EU's effectiveness in this area. The curb on anonymity and the clarification of CDD and UBO requirements could raise a barrier to terrorism financing as it becomes more difficult to hide one's identity when

19. On the notion of lone actors and the fact that they often operate alone but are radicalised and find support in larger communities, see Matthew Levitt, 'The Lone-Wolf Terrorist Is a Misnomer', *Morning Call*, 22 September 2016; Boaz Ganor, 'Understanding the Motivations of "Lone Wolf" Terrorists: The "Bathtub" Model', *Perspectives on Terrorism* (Vol. 15, No. 2, April 2021), pp. 23–32.

20. European Commission, 'Proposal for a Directive on the Mechanisms to Be Put in Place by the Member States for the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing and Repealing Directive (EU) 2015/849'.

21. *Ibid.*, p. 21.

22. See, for example, US Government, 'The 9/11 Commission Report'.

23. European Commission, 'Proposal for a Regulation on the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing'.

holding an account or making transactions. However, many terrorists who carried out attacks in Europe in recent years have been ‘hiding in plain sight’ and had not been hiding their finances at all. For instance, the perpetrators of the Charlie Hebdo attacks held bank accounts with high street banks for their savings and obtained credit. Likewise, the perpetrator of the Manchester Arena attack held a regular bank account.²⁴ They were difficult to detect as their financial behaviour did not attract suspicion.

Likewise, there have been cases of terrorism financing through crowdfunding (Islamist movements and extreme right-wing groups).²⁵ The inclusion of those crowdfunding service providers which fall outside the EU Crowdfunding Regulation as regulated entities would indeed target the part of the market where the risk is most likely to be and could therefore have some modest effect on fighting terrorism financing.²⁶ Yet, the significance of the use of crowdfunding platforms for the financing of terrorism appears to be rather small so far. In addition, what the proposed Regulation would require from these platforms is to identify their customers and monitor their transactions and these do not necessarily raise suspicion as one of the fundamental challenges of detecting terrorism financing is the identification of terrorists and their sources of finance ahead of their actions.

With regard to large cash payments, it is interesting to recall that the Commission has already proposed a limit in 2015.²⁷ Based on a study it then commissioned, it decided ‘not to proceed with a restriction on cash payment to combat terrorist financing, due to its limited impact on terrorist financing’.²⁸ While an EU-wide limit on cash payments might have an impact on money laundering as it makes the laundering of big sums through one transaction

harder, the recent terrorist attacks carried out in Europe were low budget (almost all were carried out with less than €10,000)²⁹ and were not financed through large-scale money laundering. Therefore, the study’s conclusions are still relevant.

Regulation on the Traceability of Crypto Assets

The proposed Regulation on the traceability of crypto assets revises the 2015 Regulation on Transfers of Funds (Regulation 2015/847/EU) with the aim of harmonising the CDD obligations for cross-border wire transfers and crypto asset transfers. This includes a standardised set of information of the originator of a transaction and on the beneficiary. The new obligations for Crypto Asset Service Providers imply a full application of the ‘regular’ EU AML/CTF rules to the crypto sector.

However, despite the initial hype surrounding the potential of crypto assets for terrorism financing, there was for a while ‘little current evidence of the adoption of cryptocurrencies by terrorist organizations or the motivation to do so’.³⁰ More recently there are, however, some examples of Islamist groups fundraising via cryptocurrencies³¹ and extreme right-wing groups also seem to have a particular interest in this currency for ideological reasons and to circumvent banning by the formal banking and payment industry.³² The use of cryptocurrency for international fundraising for terrorism purposes can be attractive and so limiting the anonymity of crypto assets could curb their use for terrorism financing.

24. Ecorys, CEPS, ‘Study on an EU Initiative for a Restriction on Payments in Cash: Final Report’, 15 December 2017.

25. A recent example of Islamist crowdfunding is related to Islamic State detainees in Syria. See Audrey Alexander, ‘Cash Camps: Financing Detainee Activities in Al-Hol and Roj Camps’, *CTC Sentinel*, 29 September 2021. For examples of crowdfunding by extreme right-wing groups, see FATE, ‘Ethnically or Racially Motivated Terrorism Financing’, June 2021, p. 9.

26. See, for example, Stephen Reimer and Matthew Redhead, ‘Following the Crowd: Clarifying Terrorism Financing Risk in European Crowdfunding’, CRAFT Research Briefing No. 7, RUSI, 2021, pp. 4–5.

27. Ecorys, CEPS, ‘Study on an EU Initiative for a Restriction on Payments in Cash: Final Report’.

28. *Ibid.*

29. *Ibid.*

30. Cynthia Dion-Schwarz, David Manheim and Patrick Johnston, *Terrorist Use of Cryptocurrencies, Technical and Organizational Barriers and Future Threats* (Santa Monica, CA: RAND, 2019), p. xi. See also, Tom Keatinge, David Carlisle and Florence Keen, ‘Virtual Currencies and Terrorism Financing: Assessing the Risk and Evaluating the Responses’, European Parliament, May 2018; Jessica Davis, *Illicit Money: Financing Terrorism in the Twenty-First Century* (Boulder, CO: Lynne Rienner, 2021).

31. For examples of the use of cryptocurrencies for terrorism fundraising, see Chainalysis Insights, ‘Chainalysis in Action: Department of Justice Announces Takedown of Two Terrorism Financing Campaigns with Help from Blockchain Analysis’, 13 August 2021; *The Guardian*, ‘Virginia Teenager Pleads Guilty over Facilitating Bitcoin Funds to Aid Isis’, 11 June 2015.

32. See, for example, Erika Kinetz and Lori Hinnant, ‘How the Far Right Embraces Crypto to Move Millions and Fund Hate’, *Bloomberg*, 28 September 2021.

Towards a New Diagnosis

Taken together, the expected impact of the legislative package on the effectiveness of terrorism financing is at odds with the announcements on an ambitious AML/CTF package from the European Commission. What transpires from the brief analysis above – despite not being exhaustive – is that some elements of the package may have a positive impact on CTF under certain circumstances. However, there are more structural characteristics that impact the effectiveness of CTF that the package does not address.

In fact, the proposed package closely responds to the diagnosis made in the post-mortem report and the further objectives set out by the European Commission.³³ While the diagnosis might be right for these purposes, CTF must be seen as a different ‘patient’ all together.

A Bad Combination?

After 9/11, the fight against terrorism financing was grafted on a set of pre-existing measures to combat money laundering. While there were several reasons to do so at that time, it is often an uneasy combination. In fact, the motivation behind the two types of financial crime (profit as a means or as an end goal) as well as the practices (how is money obtained) are often different – though overlap in the form of a ‘crime–terror nexus’ does exist. However, putting AML and CTF under the same policy umbrella may make sense to combat money laundering but has no or limited impact on fighting terrorism financing. It is fair to say that the FATF has also defined separate intermediate and immediate outcomes for CTF and some countries have decided to make separate national risk assessments for AML and CTF (for example, Belgium, Israel, the Netherlands, Russia, Serbia and Singapore). Given the emphasis on solving AML-related failings in the current legislative package, the EU’s communications and actions would gain in clarity and better manage expectations if the two issues were treated separately.

A CTF Specific Post-Mortem Report?

Whereas the existing post-mortem report provides an interesting analysis into the gaps and loopholes identified after the various AML scandals, a similar overview and analysis of the current internal and external terrorism threat in the EU and a corresponding action plan is lacking. There is of course Europol’s annual Terrorism Situation and Trend Report which provides a statistical and thematic update on the terrorism threat in the EU. However, this document does not have the intention to give a roadmap on legislative initiatives that could improve effectiveness. Likewise, the EU’s Security Strategy briefly touches on the issue of terrorism financing, but no clear link is made between this document and the present AML/CTF legislative package.³⁴

The terrorist threat has changed significantly since the wave of major terrorist attacks that took place in the EU between 2013 and 2018. The demise of the Islamic State ‘caliphate’ and the growth of its franchises in Africa, the Taliban’s control of Afghanistan and the rise of right-wing terrorism throughout the West have implications for terrorism financing. To increase the effectiveness of CTF measures, the new threats and their geographies need to be analysed and an evaluation is needed on how the current proposed framework corresponds to the exact threat.

Is Consistency the New Effectiveness?

It is interesting to note a linguistic shift in the AML/CTF package from long-standing debates on the effectiveness of the AML framework to one of harmonisation and consistency. The post-mortem report and the EU’s following action plan identified the need to improve on the lack of or divergent implementation of AML rules as central objective of the EU legislative package. As such the AMLA aims to create a single supervisory framework to avoid inconsistent application of AML/CTF rules by different member states’ supervisors. The 6AMLD and the two regulations aim to provide more detail on key concepts of the AML rules to increase harmonisation.

33. These are: closing loopholes and fixing failures that became apparent through money-laundering scandals; responding to the latest technological developments such as virtual currencies; more integrated financial flows in the European Single Market; and to ease up daily compliance processes for regulated entities. See European Commission, ‘Beating Financial Crime: Commission Overhauls Anti-Money Laundering and Countering the Financing of Terrorism Rules’.

34. European Commission, ‘Communication from the Commission on the EU Security Union Strategy’, 24 June 2020.

There is a greater emphasis on creating ‘a much more consistent framework’³⁵ and harmonisation in the four proposals and accompanying communications than on the effectiveness of it in combating money laundering and terrorism financing. This redefines which issue needs to be solved and what counts as success or progress in this new context. A policy can be very consistent but nevertheless ineffective. The lack of effectiveness of the CTF framework is less of a regulatory consistency problem than a result of the nature of terrorism financing. The main challenges to CTF effectiveness are to preventatively detect terrorist plots by finding the needle in the haystack of financial data, the low amounts of money usually involved, and self-funding through mundane legal transactions or illegal cash. Finding relevant indicators to measure the effectiveness of CTF measures has proven difficult³⁶ but focusing on consistency instead of effectiveness is not the solution.

and private stakeholders but avoid ‘tick the box’ formats. In any case, effectiveness (and effects) are more than a matter of harmonisation and consistency.

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Recommendations

The legislative package is now being discussed by the European Parliament and Council and is generally considered non-controversial. Its main focus is on ‘closing the door on money laundering’³⁷ and responding to the failings identified after the string of money-laundering scandals involving major European institutions. From the perspective of effective CTF, this paper has shown that the package falls short. To present an equally ambitious package with regard to increasing the effectiveness of CTF this paper recommends:

1. Adopting a differentiated treatment of CTF and AML at the EU level to avoid the mismatch between the proposed policies and the current terrorism financing threat. This should lead to more targeted policies and legislative proposals for CTF.
2. Getting the diagnosis right through a specific evaluation of the current terrorism-financing threat and how the identified threat matches AML/CTF existing measures.
3. In the private sector efforts are already being undertaken to further these discussions, and a renewed focus on the effectiveness of the fight against terrorism financing is essential. ‘Measuring’ the effectiveness of CTF measures comes with many methodological challenges and other imperfections. One way forward may be to differentiate effectiveness goals and expectations for all of the public

35. European Commission, ‘Beating Financial Crime’.

36. Wesseling and de Goede, ‘Beleid Bestrijding Terrorismefinanciering, Effectiviteit en Effecten’ [‘CTF Policies: Effectiveness and Effects’].

37. European Commission, ‘Beating Financial Crime’.