

- The extent to which the action or the timing of the action would have a significant adverse systemic impact on the international payment, clearance, and settlement system, or on legitimate business activities involving the particular jurisdiction, institution, or class of transactions; and

- The effect of the action on United States national security and foreign policy.

In addition to (1) the consultations for the designation of a primary money laundering concern, and (2) the consultations with the larger group of agencies for determining which of the special measures to impose, the Secretary, in determining specifically whether to impose the fifth special measure, must consult with the Secretary of State, the Attorney General, and the Chairman of Board of Governors of the Federal Reserve.

Last, the Secretary, in determining whether to apply one or more special measures only to a foreign institution(s), transaction(s), class(es) of transactions, or type(s) of account(s) within a particular jurisdiction—as opposed to applying the special measure more generally to the foreign jurisdiction itself—must consult with the Secretary of State and the Attorney General, and shall take into consideration the following “institutional factors”:

- The extent to which such financial institution(s), transaction(s), class(es) of transactions, or type(s) of account(s) are used to facilitate or promote money laundering in or through the jurisdiction;

- The extent to which such institutions, transaction(s), class(es) of transaction(s), or type(s) of account(s) are used for legitimate business purposes in the jurisdiction; and

- The extent to which such action is sufficient to ensure, with respect to transactions involving the jurisdiction and institutions operating in the jurisdiction, that the purposes of the BSA continue to be fulfilled, and to guard against international money laundering and other financial crimes.

#### *D. Procedures for Imposing Special Measures*

Pursuant to section 5318A, any of the first four “special measures” can be imposed by order, regulation, or as otherwise “permitted by law.” If an order is issued, it can remain in effect for 120 days, unless authorized by a regulation promulgated before the end of the 120-day period. The fifth “special measure” can only be imposed through the issuance of a regulation.

## **II. Nauru**

### *A. Background*

Nauru is a small island of approximately 10 square miles that has a population of only approximately 12,000 people. At one point in time, the island had one of the highest per capita incomes in the developing world due to the mining and export of phosphates, a funding source expected to be completely depleted within five to ten years. As a result of the phosphate mining, the central part of the island, once thriving with vegetation and wildlife, has become uninhabitable and only the perimeter of the island remains available for habitation. This perimeter itself is vulnerable to storms and the movement of the ocean.

Although Nauru at one point in time was relatively wealthy, most of the funds emanating from the phosphate mining and originally contained in the country’s trust funds have been depleted through waste, poor investments, and fraud. As a result, the country has been borrowing heavily to finance fiscal deficits. Currently, the basic infrastructure of the island is so poor that electric, water, and phone service is available only on a limited and sporadic basis.

### *B. Offshore Shell Banks in Nauru*

In an effort to raise funds, the island has resorted to the selling of passports (or “economic citizenships”) to non-resident foreigners, and, of greater concern, the selling of offshore banking licenses. Nauru is notorious for permitting the establishment of offshore shell banks with no physical presence in Nauru or in any other country. The evidence indicates that the entities that obtain these offshore banking licenses are subject to cursory and wholly inadequate review by the country’s officials, lack any credible on-going supervision, and maintain no banking records that Nauru or any other jurisdiction can review. In addition, one of the common requirements imposed by Nauru on these offshore banks is that they not engage in economic transactions involving either the currency of Nauru (currently the Australian dollar) or its citizens or residents. Consequently, these offshore shell banks have no apparent legitimate connection with the economy or business activity of Nauru. Indeed, only one bank appears to be physically located in Nauru, the “Bank of Nauru.” It is a local community bank that also serves as the Central Bank.

In 2000, FinCEN reported that 400 offshore banks had been granted

licenses by Nauru.<sup>3</sup> It has been verified by on-site reports that a 1,000 square foot wooden structure is “home” to these banks that have no physical or legal residence anywhere in the world. The United States Government has been able to verify the names of 161 of the institutions licensed by Nauru.<sup>4</sup> These are institutions for which the limited information available indicates that there is a strong likelihood that they are shell banks that are not subject to effective banking supervision.

### *C. FATF Designation*

As a consequence of the current practices of Nauru, the Financial Action Task Force on Money Laundering (FATF) placed Nauru on the “Non-Cooperative Countries and Territories” (NCCT) list in June 2000 for maintaining an inadequate anti-money laundering regime. According to FATF, Nauru’s anti-money laundering weaknesses included, but were not limited to, the following: money laundering was not a criminal offense; offshore banks licensed by Nauru were not required to maintain customer identification or transaction records; Nauruan financial institutions were under no obligation to report suspicious transactions; and Nauru maintained strong bank secrecy laws. In July 2000, FinCEN issued an advisory to U.S. financial institutions, warning them to give enhanced scrutiny to all financial transactions originating in or routed to or through Nauru, or involving entities organized or domiciled, or persons maintaining accounts, in Nauru. In addition, the Office of the Comptroller of the Currency has issued 15 Alerts concerning offshore shell banks located in Nauru that were potentially attempting to engage in the business of banking in the United States without authority.

In June of 2001, FATF determined that Nauru had made insufficient progress towards remedying deficiencies in its anti-money laundering regime and warned Nauru that FATF would impose countermeasures by September 30, 2001, if Nauru failed to address these deficiencies.

On August 28, 2001, Nauru passed the Anti-Money Laundering Act of 2001 (the AML Act). On September 7, 2001, however, FATF indicated that the AML Act was not consistent with international standards because it did not apply to the numerous offshore

<sup>3</sup> FinCEN Advisory Issue 21 (July 2000).

<sup>4</sup> A list of these institutions was presented as Appendix A to the December 20, 2002, designation of Nauru as a jurisdiction of primary money laundering concern.