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COUNTERFEIT U.S. CURRENCY ABROAD

Observations on Counterfeiting and U.S. Deterrence Efforts

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Counterfeit U.S. Currency Abroad: Observations on Counterfeiting and U.S. Deterrence Efforts

SUMMARY OF STATEMENT BY JAYETTA Z. HECKER, ASSOCIATE DIRECTOR, INTERNATIONAL RELATIONS AND TRADE ISSUES

U.S. currency has become a vulnerable target for international counterfeiting because it is widely used abroad and currently lacks updated security features. GAO's testimony focuses on the diverse nature and the unknown extent of counterfeiting abroad, as well as the recent U.S. efforts to deter this activity.

U.S. law enforcement officials say that counterfeiters range from office workers to organized crime and terrorist groups and that the equipment used for counterfeiting U.S. currency includes both simple photocopiers and sophisticated offset presses. Moreover, counterfeit currency varies significantly in quality. Of increasing concern is a very high-quality family of counterfeits commonly known as the "Superdollar." According to reports by the House Republican Task Force on Terrorism and Unconventional Warfare, the Superdollar is printed in the Middle East on "high-tech state-owned presses with paper only acquired by governments." However, the Secret Service says that the task force has provided little evidence to support its allegations.

Counterfeiting is a criminal activity. Thus, it is impossible to determine the actual extent of this activity abroad. Both Treasury and Secret Service officials agreed that counterfeiting of U.S. currency is a threat to be taken seriously but said that it is not now at a level that poses an economic threat to the U.S. monetary system. Treasury Department and Secret Service officials use counterfeit-detection data from the Secret Service to help assess the extent of counterfeiting. According to the Secret Service, it supplemented these data with intelligence information and field experience and concluded that counterfeiting of U.S. currency abroad has been increasing. Our analysis of detection data raised questions about their usefulness for illustrating either actual counterfeiting activity or recent growth in such activity.

Foreign law enforcement and financial organization officials we interviewed in seven European countries varied in their degree of concern over the counterfeiting of U.S. currency. Foreign law enforcement officials tended to be more concerned about the counterfeiting of U.S. currency than were foreign financial organization officials.

The United States is increasing its deterrence efforts. It is redesigning U.S. currency to incorporate more security features; bolstering exchanges of

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information abroad, including providing more counterfeit-detection training; attempting to increase the Secret Service presence abroad (although the Secret Service has encountered difficulty in obtaining approval); and trying to stop production and distribution of counterfeit currency, including the Superdollar, using special task forces and diplomatic efforts.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss our observations on the counterfeiting of U.S. currency abroad and recent U.S. efforts to combat this activity. In light of the impending release of the new U.S. currency design and media reports concerning high-quality counterfeits, much public attention has recently focused on the vulnerability of our currency. Our currency has become a target of counterfeiters because of its increasing international use and outdated security features.

My testimony today will discuss the diverse nature and unknown extent of counterfeiting abroad, as well as the recent efforts of the United States to deter this activity. These efforts include (1) redesigning the currency, (2) exchanging more information with foreign law enforcement agencies and financial organizations, (3) attempting to increase the Secret Service presence abroad, and (4) attempting to stop production and distribution of an extremely high-quality counterfeit commonly known as the "Superdollar."

My remarks today are based on the work that we performed for Representative John Spratt, Jr., over the past year and a half on the counterfeiting of U.S. currency abroad. This work is more comprehensively summarized in our report entitled Counterfeit U.S. Currency Abroad: Issues and U.S. Deterrence Efforts (GAO/GGD-96-11), which was released by Representative Spratt today. In doing our work, we obtained views and material from (1) U.S. government agencies in the United States and abroad, including the Treasury Department, the Secret Service, the Bureau of Engraving and Printing, the Federal Reserve, and the State Department; (2) foreign law enforcement and financial organization officials in England, France, Italy, Germany, Hungary, Poland, and Switzerland; (3) Interpol (the international police organization) officials in the United States and abroad; and (4) individuals researching the Superdollar case, including the author of the House Republican Task Force on Terrorism and Unconventional Warfare reports¹ on the Superdollar.

Please note that our work was limited by a number of factors related to national security and investigative concerns. All of my remarks today are based on our report, which was cleared as unclassified through a security

¹The House Republican Research Committee, Iran, Syria and the Trail of Counterfeit Dollars (Washington, D.C.: July 1, 1992); and Update: Iran, Syria and the Trail of the Counterfeit Money (Washington, D.C.: July 13, 1994).

classification review by the appropriate U.S. agencies, including the Treasury and the Secret Service.

Background

The U.S. currency,² reportedly the most widely held in the world, is susceptible to counterfeiting. High foreign inflation rates and the relative stability of the dollar have contributed to the increasing use of U.S. currency outside the United States. Of the \$380 billion of U.S. currency in circulation, the Federal Reserve estimates that over 60 percent may be held outside the United States. The widespread use of U.S. currency abroad, together with the outdated security features of the currency, makes it a vulnerable target for international counterfeiting. Excluding two changes introduced in 1990,³ the overt security features of the currency have not substantially changed since 1929. This situation has resulted in the U.S. dollar's becoming increasingly vulnerable to counterfeiting.

Widespread counterfeiting of U.S. currency could undermine confidence in the currency and, if done on a large enough scale, could even have a negative effect on the U.S. economy. The United States benefits from the international use of its currency. When U.S. currency remains in circulation, it essentially represents an interest-free loan to the U.S. government. The Federal Reserve has estimated that the existence of U.S. currency held abroad reduces the need of the government to borrow by approximately \$10 billion a year.

The Treasury, including the Secret Service and the Bureau of Engraving and Printing, and the Federal Reserve have primary responsibilities for addressing the counterfeiting of U.S. currency. The Secretary of the Treasury is responsible for issuing and protecting U.S. currency. The Secret Service conducts investigations of counterfeiting activities and provides counterfeit-detection training. The Secret Service is also the U.S. agency responsible for anticounterfeiting efforts abroad. The Bureau of Engraving and Printing designs and prints U.S. currency and incorporates security features into the currency. The Federal Reserve's role is to distribute and ensure the physical integrity, including the authenticity, of U.S. currency.

²In this statement, "U.S. currency" refers to U.S. Federal Reserve notes and does not include coined money.

³In 1990, the Treasury added a security thread and microprinting to U.S. currency.

Nature of Counterfeiting of U.S. Currency Is Diverse

A diverse group of perpetrators uses a variety of methods to counterfeit U.S. currency. And, although counterfeiting is carried out primarily for economic gain, it is sometimes linked with other more nefarious criminal endeavors, such as drug trafficking, arms dealing, and alleged terrorist activities.

According to law enforcement officials, counterfeiters run the gamut from office workers to organized crime and terrorist groups, and the equipment used for counterfeiting U.S. currency ranges from photocopiers to sophisticated offset presses. Moreover, the quality of counterfeit notes varies significantly. Even those notes made using the same method vary according to the sophistication of the perpetrator and the type of equipment used. Of increasing concern is the fact that certain foreign counterfeiters are becoming extremely sophisticated and are now producing very high-quality counterfeit notes that are more difficult to detect than any previous counterfeits.

The highest-quality family of counterfeits known today is commonly referred to as the Superdollar.⁴ While many allegations have been made about the Superdollar, little evidence in support of these allegations has been made public. In the Middle East, a group, allegedly a foreign government, is said to be sponsoring production of the Superdollar. According to reports by the House Republican Task Force on Terrorism and Unconventional Warfare, the Superdollar is printed in the Middle East on “high-tech state-owned presses with paper only acquired by governments.” Also according to the task force, the Superdollar is “designed for direct infiltration into the U.S. banking system and has become a major instrument in facilitating the flow of militarily useful nuclear materials and equipment and various weapons systems.”⁵ A few of the foreign law enforcement and financial institution officials we spoke with believed the Superdollar was being circulated through various terrorist organizations around the world. This belief was primarily based on reports of detections involving individuals with links to terrorist organizations.

However, according to the Secret Service, the task force has provided almost no evidence to support its allegations. According to the Treasury, no evidence exists to show that the Superdollar is printed with paper

⁴The note is also known as the “Supernote” or the “Superbill” and is referred to as the “C-14342 Family” by the Secret Service.

⁵The House Republican Research Committee, Iran, Syria and the Trail of Counterfeit Dollars; and Update: Iran, Syria and the Trail of the Counterfeit Money.

acquired only by governments and that it is designed for direct infiltration into the U.S. banking system. The Treasury also maintained that support for the remaining allegations concerning the Superdollar was inconclusive. Furthermore, although the task force reported that between \$100 million and billions of Superdollars are in circulation, the report provided no evidence to support these allegations. Since the Superdollar's initial detection in fiscal year 1990, Superdollar detections have represented a small portion of total counterfeit currency detections, according to the Treasury and Secret Service.

While high-quality counterfeit notes, such as the Superdollar, have received the most attention from the media, Treasury officials told us that their biggest concern was the rapid advances in photographic and printing devices. According to a 1993 National Research Council report requested by the Treasury, the counterfeiting problem will increase as these technologies improve and are made more accessible to the public. The Treasury has planned to combat such counterfeiting through changes to the U.S. currency design, expected to be introduced in March 1996.

Extent of the Problem Could Not Be Determined, and Foreign Views Were Inconclusive

The criminal nature of the activity precludes determination of the actual extent to which U.S. currency is being counterfeited abroad. The best data available to reflect actual counterfeiting are Secret Service counterfeit-detection data.⁶ Using these data, Treasury officials concluded that counterfeiting of U.S. currency was economically insignificant. Secret Service officials told us that they supplemented the counterfeit-detection data that they gathered with intelligence information and field experience and that these data demonstrated an increase in counterfeiting activity abroad. However, our analysis of the same counterfeit-detection data proved inconclusive. Secret Service data have limitations and thus provide only a limited measure of the extent of counterfeiting activities. Foreign officials' views about the seriousness of the problem of counterfeit U.S. currency were mixed.

⁶Interpol data, the only other international compilation of counterfeit-currency statistics, were less reliable due to the limited amount of reporting by foreign countries. According to Interpol officials, reporting to Interpol was inconsistent and mostly limited to European nations.

Treasury Said the Level of Counterfeiting Was Economically Insignificant; Secret Service Said Activity Abroad Was Increasing

On the basis of the number of Secret Service counterfeit detections, Treasury officials concluded that counterfeiting of U.S. currency was economically insignificant and thus did not pose a threat to the U.S. monetary system. According to Secret Service and Treasury officials, detected counterfeits represented a minuscule portion of U.S. currency in circulation. Secret Service and Federal Reserve data showed that, in fiscal year 1994, of the \$380 billion in circulation, \$208.7 million had been detected as counterfeit notes. This figure represented less than one one-thousandth of the currency in circulation. However, while Treasury and Secret Service officials agreed that, overall, counterfeiting was not economically significant, they considered any counterfeiting to be a serious problem.

The Secret Service used counterfeit-detection data, supplemented with intelligence information and field experience, to report that counterfeiting of U.S. currency abroad was increasing.⁷ In one analysis, it reported that the amount of counterfeit currency detected abroad increased 300 percent, from \$30 million in fiscal year 1992 to \$121 million in fiscal year 1993, thereby surpassing domestic detections in the same period.

The Secret Service has also reported that, in recent years, a larger dollar amount of the notes detected in circulation domestically has been produced outside the United States. Since 1991, the dollar amount of counterfeit U.S. notes detected while in circulation and produced abroad has exceeded the dollar amount of those produced domestically. In fiscal year 1994, these foreign-produced notes represented approximately 66 percent of total counterfeits detected in circulation domestically.

The Actual Extent of Counterfeiting Abroad Could Not Be Determined

The true dimensions of the problem of counterfeiting of U.S. currency abroad could not be determined. The Treasury and the Secret Service use Secret Service counterfeit-detection data to reflect the actual extent of counterfeiting. However, although these data are the best available, they have limitations. Specifically, they are incomplete and present only a partial picture of counterfeiting. If these limitations are not disclosed, the result may be misleading conclusions.

⁷It employed two counterfeit-detection data measures to illustrate the extent of counterfeiting abroad: (1) counterfeit detections abroad and (2) domestic detections of counterfeits that were produced abroad. Counterfeits detected abroad are categorized as "appearing abroad," while counterfeits detected domestically are divided into two separate categories. Domestic detections of counterfeits not yet in circulation are called "seizures"; counterfeits detected while in circulation are called "passes."

First of all, the actual extent of counterfeiting could not be measured, primarily because of the criminal nature of this activity. Secret Service data record only those detections that are reported to the Secret Service; they do not measure actual counterfeiting. As a result, the data provide no information about the number of counterfeiters operating in any given year or the size and scope of their operations. More importantly, these data could not be used to estimate the volume of counterfeit currency in circulation at any point in time. In the case of counterfeit currency appearing abroad, reasons for this include the following: (1) the data do not distinguish between how much counterfeit currency was seized and how much was passed into circulation; (2) the data could not provide information about how long passed counterfeits remained in circulation before detection; and (3) most critically, the data provide no indication of how much counterfeit currency was passed into circulation and not detected.

Second, counterfeit detection data may in part only reflect where the Secret Service focuses its efforts. Use of these data thus may not identify all countries with major counterfeiting activity, but simply countries where agents focused their data collection efforts. For example, in fiscal year 1994, almost 50 percent of detections abroad occurred in the six countries where the Secret Service was permanently located. In other countries, counterfeit-detection statistics tend to be more inconsistent.

Third, detection data for high-quality notes may be underreported. The Secret Service has said that, because so few Superdollars have been detected, this indicates that there are not many in circulation. However, according to the House Republican Task Force on Terrorism and Unconventional Warfare reports, the majority of Superdollars are circulating outside the formal banking system and therefore would not be reported to the Treasury if detected. Also, as we discovered on our overseas visits, many foreign law enforcement and financial organization officials had inconsistent and incomplete information on how to detect the Superdollar. Thus, financial institutions abroad may be recirculating the Superdollars.

Fourth, reported increases in counterfeiting abroad, as supported by Secret Service detection data, may be based on a number of factors other than increased counterfeiting activity. For example, in 1993, the Secret Service changed its reporting practices abroad to be more proactive in collecting counterfeit-detection data. Instead of relying solely on reports from foreign officials, agents abroad began to follow up on Interpol

reports and intelligence information in order to collect additional data. Also, according to Treasury officials, foreign law enforcement officials have improved their ability to detect counterfeit U.S. currency and report it to the Secret Service. Furthermore, the increase in domestic detections of counterfeits produced abroad is also subject to interpretation. For example, rather than foreign-produced notes increasing, it is possible that the Secret Service's ability to determine the source of counterfeit currency has simply improved over time.

Fifth and finally, counterfeit-detection data fluctuate over time, and one large seizure can skew the data, particularly for detections abroad. For example, according to the Secret Service, several large seizures accounted for the jump from \$14 million in counterfeit detections abroad in fiscal year 1988 to \$88 million in fiscal year 1989. The following year, the data indicated a significant drop in detections. For detections outside the United States, the Secret Service has relied heavily on information provided by foreign law enforcement organizations, and has obtained little information from financial organizations.

Officials Said Secret Service Field Experience and Intelligence Information Supplemented Detection Data

According to Secret Service officials, they supplemented their counterfeiting detection data with knowledge their agents gained through field experience and the sharing of intelligence information. Some of this information was not available or was considered too sensitive for an unclassified report. Our work did yield some information on the unclassified activities. For example, the Secret Service told us that it was conducting vault inspections during its joint international study team visits with Treasury and Federal Reserve officials. According to a Secret Service agent who performs the vault inspections, they include the checking of all U.S. currency in the vault for counterfeits. According to Federal Reserve and Secret Service officials, vault inspections had been conducted in only one of the six locations the Secret Service visited during the time of our review. Secret Service officials told us that the inspections had been conducted only in Argentina and were discontinued because of the limited results obtained there. The officials told us that the inspections might be reinstated in other countries if it was decided that the effort was warranted.

Foreign Views on the Extent of Counterfeiting Abroad Were Mixed

Overseas law enforcement and financial organization officials' views on the extent of the problem of counterfeit U.S. currency varied. Foreign law enforcement officials tended to be more concerned about counterfeit U.S.

currency than foreign financial organization officials. Financial organization officials we met with said that they had experienced minimal chargebacks,⁸ and most expressed confidence in the ability of their tellers to detect counterfeits. Furthermore, we heard few reports from foreign financial organization and foreign law enforcement officials about U.S. currency not being accepted overseas because of concerns about counterfeiting.

Most foreign law enforcement officials we spoke with believed that the counterfeiting of U.S. currency was a problem, but their opinions on the severity of the problem differed. Swiss, Italian, and Hungarian law enforcement officials said that it was a very serious problem. French and English law enforcement officials said that the problem fluctuated in seriousness over time. And German, French, and Polish officials said that the counterfeiting of U.S. currency was not as serious a problem as the counterfeiting of their own currencies. Some of these law enforcement officials expressed concern over increases in counterfeiting in Eastern Europe and the former Soviet Union. Some also expressed particular worry about their ability, and the ability of financial organizations in their countries, to detect the Superdollar.

Conversely, most foreign financial organization officials we spoke with were not concerned about the counterfeiting of U.S. currency. Of the 34 organizations we visited in 7 countries, officials from 1 Swiss and 1 French banking association and 2 Hungarian banks viewed the counterfeiting of U.S. currency as a current or increasing problem. According to other foreign financial organization officials, they were not concerned about U.S. counterfeiting activity because it did not have a negative impact on their business. For example, none of the 16 financial organization officials with whom we discussed chargebacks told us that they had received substantial chargebacks due to counterfeit notes that they had failed to detect. In addition, some of these officials cited other types of financial fraud and the counterfeiting of their own currency as more significant concerns. For example, officials from one French banking association were more concerned with credit card fraud, and officials from two financial organizations in Germany and one financial organization in France said counterfeiting of their country's currency was a greater problem.

⁸A chargeback occurs when the Federal Reserve or a bank detects a counterfeit note in a deposit and charges the customer's account for the value of the counterfeit.

Furthermore, foreign financial organization officials we spoke with were confident about their tellers' ability to detect counterfeits and, in some countries, tellers were held personally accountable for not detecting counterfeits.⁹ In most of the countries we visited, detection of counterfeit U.S. currency relied on the touch and sight of tellers, some of whom were aided by magnifying glasses or other simple detection devices, such as counterfeit detection pens.¹⁰ Other counterfeit-detection devices used abroad, like ultraviolet lights, did not work effectively on U.S. currency. While foreign financial organizations appeared confident of their tellers' ability to detect counterfeits, some of these organizations had incomplete information on how to detect counterfeit U.S. currency, particularly the Superdollar.

Finally, foreign financial organization and law enforcement officials provided a few isolated cases in which U.S. currency was not accepted abroad. For example, when it first learned about the Superdollar, one U.S. financial organization in Switzerland initially stopped accepting U.S. \$100 notes, although it later resumed accepting the U.S. notes from its regular customers. Also, Swiss police and Hungarian central bank and French clearing house officials reported that some exchange houses and other banks were not accepting \$100 notes. We were unable to confirm these reports. However, a State Department official commented that, because drug transactions tended to involve \$100 notes, some foreigners were reluctant to accept this denomination, not because of counterfeiting concerns, but rather because of the notes' potential link to money laundering.

Additional U.S. Counterfeit Currency Deterrence Efforts

The U.S. government, primarily through the Treasury Department and its Secret Service and the Federal Reserve, has been increasing its counterfeiting deterrence efforts. These efforts include redesigning U.S. currency; increasing exchanges of information abroad; attempting to increase the Secret Service presence abroad; and attempting to stop production and distribution of counterfeit currency, including the Superdollar.

⁹For example, in Hungary tellers were charged for every counterfeit note they accepted that the bank later detected.

¹⁰Counterfeit-detection pens are filled with a chemical that, when applied to currency, turns gold if the currency's paper contains certain characteristics of genuine paper and turns black if those characteristics are not present.

Treasury Department to Introduce Currency Redesign

To combat counterfeiting both domestically and abroad, the Treasury is redesigning U.S. currency to incorporate more security features intended to combat rapid advances in reprographic technology. This change, the most significant in over 50 years, is long overdue, according to some U.S. and foreign officials. The redesigned currency is planned for introduction in 1996 starting with changes to the \$100 note, with lower denominations to follow at 9- to 12-month intervals. According to Treasury officials, the currency redesign will be an ongoing process, because no security features are counterfeit-proof over time. These officials also said that the old currency would not be recalled and would retain its full value. Moreover, the Treasury is leading a worldwide publicity campaign to facilitate introduction of the redesigned currency, ensure awareness and use of the overt security features, and assure the public that the old currency will still be accepted in full. Through this campaign, the Federal Reserve hopes to encourage the public to turn in old currency for the redesigned notes.

Secret Service Sharing More Information Abroad

In addition, the Secret Service, through its team visits abroad in company with Treasury Department and Federal Reserve officials, has gathered further information on counterfeiting and provided counterfeit-detection training. As of May 1995, the team had met with law enforcement and financial organization officials in Buenos Aires, Argentina; Minsk, Belarus; London, England; Zurich, Switzerland; Hong Kong; and Singapore. According to Secret Service officials, their visits were successful because they were able to develop better contacts, obtain further information about foreign financial institutions' practices, learn more about tellers' ability to detect counterfeits, and provide counterfeit-detection training seminars for both law enforcement and financial organization officials. Since May 1995, the team has taken initial trips to Moscow, St. Petersburg, and Novgorod (Russia); Ankara and Istanbul, Turkey; Cairo, Egypt; Bahrain; Abu Dhabi; Dubai; and Riyadh, Saudi Arabia.

Secret Service Increasing Its Presence Abroad

Further, the Secret Service has been attempting to increase its presence abroad, although it has encountered difficulties in obtaining approval. The Secret Service has over 2,000 agents stationed in the United States, but it has fewer than 20 permanent positions abroad. The Secret Service first requested additional staff in February 1994 for permanent posting abroad beginning in fiscal year 1996. However, due to uncertainties about the funding of the positions and to other priorities within the Treasury Department, as of June 21, 1995, the Secret Service had secured approval for only 6 of 28 requested positions abroad. After our discussions with the

Secret Service, the Treasury, and State, on July 21, 1995, the Treasury approved the remainder of the positions and sent them to the State Department for approval. As of November 30, 1995, the respective State Department chiefs of mission had approved only 13 of the 28 positions, and only 1 agent had reported to his post abroad.

U.S. Efforts to Eradicate the Superdollar

The U.S. government has undertaken special efforts to eradicate the highest-quality counterfeit note—the Superdollar. These efforts include an interagency task force led by the Secret Service, an overseas Secret Service task force, and diplomatic efforts between senior policy level officials of the involved countries. Due to the sensitivity and ongoing nature of this investigation, we were made generally aware of these efforts but were not given specific information.

In a February 1994 Secret Service request to the Treasury for funding under the 1994 Crime bill, the Secret Service stated that, for the past 4 years, it had spearheaded a multiagency effort to suppress the most technically sophisticated note detected in the history of that agency. According to the request, this initiative has prompted an unprecedented forensic effort, utilizing the resources of the Secret Service, other government offices, and several national laboratories.

The efforts of senior policy level officials in the U.S. government involve ongoing diplomatic contacts concerning the Superdollar with Middle Eastern government officials, according to a State Department official. This official said that, in May 1995, our government asked these foreign governments to provide a show of good faith in improving relations by locating the printing plants and perpetrators involved in producing the Superdollar. He added that these efforts did not specifically implicate these governments in the production of the Superdollar, but that, at a minimum, they were believed to be tolerating this illegal activity within their borders.

U.S. and Interpol officials we interviewed stated that final resolution of cases similar to that of the Superdollar, should such cases occur, were beyond the purview of law enforcement and would require diplomatic solutions. According to U.S. and Interpol officials, jurisdictional constraints may prevent law enforcement agencies from dealing effectively with cases of foreign-condoned or -sponsored counterfeiting of U.S. currency. In such cases, the Secret Service would only be able to identify and assist in suppressing the distribution of the counterfeit notes.

In countries where the United States has no diplomatic relations, U.S. law enforcement has no leverage to help deter counterfeiting. U.S. and Interpol officials agreed that the decision on how to suppress a foreign government-condoned or government-sponsored counterfeiting plant would need to be made at a senior U.S. government level.

Mr. Chairman, this concludes my prepared statement. I would be pleased to answer any questions you or the Subcommittee may have.

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