

# CTN Electronic Journal

## Preventing the Abuse of Non-Profit Organizations for Terrorist Financing

June 2011

“OSCE participating States (should) ensure that legitimate activities of non-profit organizations and charities are not restricted and that they cannot be misused by terrorist organizations (...)”

OSCE Permanent Council Decision No. 617 (2004) *on Further Measures to Suppress Terrorist Financing*

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## Editorial

While a devastating terrorist attack can be planned and executed at a relatively low cost, the broader organizational requirements of maintaining a terrorist network can demand significant financial resources. To meet their funding requirements, terrorist groups rely on a variety of financial sources, both legitimate and criminal. One of these channels involves the abuse of non-profit organizations (NPOs), which FATF Special Recommendation (SR) VIII identifies as “particularly vulnerable” to terrorist abuse.

This issue of the CTN Electronic Journal aims to provide a multi-faceted overview of key issues linked to the abuse of NPOs for terrorist financing. A variety of authors have contributed their expertise on this issue in order to shed light on a complex and challenging aspect of counter-terrorism.

Preventing and identifying the abuse of non-profit organizations is an important component of the global struggle to halt terrorist financing. In recent years, a number of cases have been reported in which NPOs were misused, sometimes with the knowledge of their leadership, to provide a cover for terrorist financing. Although this is only one of many channels used by terrorist financiers, the abuse of NPOs merits particular attention. The threat of terrorist abuse is detrimental to legitimate NGOs and undermines charitable giving by fomenting doubt in potential donors and damaging trust between state authorities and civil society.

As in many other areas, one of the key challenges in curbing terrorist financing involves striking an appropriate balance between effective oversight and the protection of fundamental rights and freedoms. On the one hand, sustaining confidence in the integrity of the non-profit sector requires the activities of NPOs to be transparent and accountable. On the other hand, oversight and enforcement measures should not unduly restrict freedom of association or discourage legitimate charitable activities.

Terrorist financing poses a security threat both transnational and multi-dimensional in nature. Interdicting terrorist financing is vital to disrupt terrorist operations and minimize the threat of attacks and following the trail of terrorist financing is often a crucial element in the successful investigation and prosecution of terrorist cases. When confronting this challenge, governments should pay careful attention to protecting and promoting fundamental human rights, specifically freedom of association. They should also take into account the economic and financial interests of business and civil society stakeholders.

Given its co-operative and comprehensive approach to security, the OSCE is particularly well-suited to assist its participating States in tackling this challenging issue. With the Bucharest Plan of Action for Combating Terrorism (MC(9)DEC/1) adopted 10 years ago, OSCE participating States pledged to take action to prevent and suppress the financing of terrorism within the framework of the United Nations Convention on the Suppression of the Financing of Terrorism and United Nations Security Council Resolution (UNSCR) 1373 (2001), while also bearing in mind UNSCR 1267 (1999).

Recognizing that terrorist financing often moves through the same channels as money laundering, participating States also pledged to strengthen their ability to suppress money laundering and terrorist financing by taking steps towards the quick implementation of the FATF 40 Recommendations against money laundering and IX Special Recommendations on combating terrorist financing.

With regard to preventing the abuse of NPOs for terrorist financing, participating States specifically decided with OSCE Permanent Council Decision (PC.DEC) 617 (2004) on *Further Measures to Suppress Terrorist Financing*, in line with the FATF SR VIII, that they “should review the adequacy of their laws and regulations that relate to entities, in particular non-profit organizations and charities that can be abused for the financing of terrorism”. They also committed “to ensure that legitimate activities of non-profit organisations and charities are not restricted and that they cannot be misused by terrorist organizations posing as legitimate entities, exploited as conduits for terrorist financing, or for concealing the clandestine diversion of funds intended for legitimate purposes to terrorist organisations”.

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Furthermore, PC.DEC/617 recommends that participating States guide themselves by the FATF International Best Practices on combating the abuse of non-profit organizations and tasked the OSCE Secretariat and OSCE Office for Democratic Institutions and Human Rights (ODIHR) to promote these best practices.

In support of the implementation of these commitments, the Office of the Co-ordinator of OSCE Economic and Environmental Activities (OCEEA) has conducted a range of activities to help combat money laundering and the financing of terrorism. At the request of OSCE participating States, these activities aim to assess national legislation, provide advice on improving legal frameworks and build national capacity, particularly within and between national institutions such as financial intelligence units (FIUs).

The OSCE Action against Terrorism Unit (ATU) for its part has been promoting through political conferences and expert workshops the development of public-private partnerships in countering the financing of terrorism, in particular in support of the implementation of the FATF 40+9 recommendations, in line with OSCE Ministerial Council Decision No. 5/07 on *Public Private Partnerships in Countering Terrorism*.

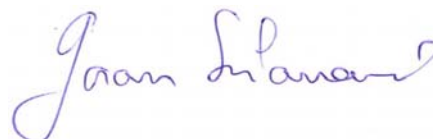
Most notably, the ATU and the OCEEA jointly organized in September 2009, in co-operation with the United States and the Charity Commission for England and Wales, a Public-Private Expert Workshop on Preventing the Abuse of Non-Profit Organizations for Terrorist Financing. This workshop addressed topics such as adequate government regulation and effective enforcement actions as well as self-regulation and good governance capacity building in the non-profit sector. The proceedings emphasized that there remain significant compliance issues across the OSCE area with respect to FATF SR VIII, notably in terms of risk assessment, inadequate oversight of the non-profit sector, and lack of outreach and awareness raising efforts by state authorities.

This issue of the CTN Electronic Journal aims to further facilitate the exchange of information and encourage reflection with regards to the abuse of NPOs for terrorist financing. OSCE participating States, international bodies and civil society stakeholders have been invited to share their views in the spirit of multi-stakeholder dialogue and co-operation. We are delighted that an unprecedented number of them replied to our call.

We hope that you will enjoy this issue of the CTN Electronic Journal.



Raphael F. Perl  
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Environmental Activities



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### The abuse of non-profit organizations for terrorist financing: The Belgian regulation and oversight of the non-profit sector

*Belgian Financial Intelligence Processing Unit (CTIF-CIF)*

#### Introduction

Even though non-profit organizations (NPOs) play a vital role in the world economy and in many national economies and social systems by providing comfort and hopes to those in need around the world, experience in fighting terrorist financing unfortunately demonstrated that terrorists and terrorist organizations exploit the NPO sector to raise and move funds, provide logistical support, encourage terrorist recruitment or otherwise support terrorist organisations and operations.

NPOs feature a number of vulnerabilities that terrorist organisations can use:

- NPOs enjoy public trust.
- NPOs have access to considerable sources of funds.
- NPOs are often cash-intensive.
- Some NPOs have a global presence that provides a framework for national and international operations and financial transactions, often within or near areas that are most exposed to terrorist activity.
- NPOs may often be subject to little or no governmental oversight (registration, record keeping, reporting and monitoring, check of background of beneficial owners, employees, management).
- Governmental bodies may have insufficient resources to effectively oversee the sector.
- NPOs may have limited resources or capacity to withstand demanding regulatory requirements.

The aim of this document is to provide an overview of CTIF-CFI's experience on the use of NPOs for terrorist financing purposes as well Belgium's implementation of Special Recommendation VIII.

#### The functioning of the Belgian financial intelligence unit CTIF-CFI

##### **Mission**

CTIF-CFI is the disclosure receiving agency responsible for combating money laundering and terrorist financing, established by the Law of 11 January 1993 and has been operational since 1 December 1993. It is an autonomous and independent public administrative authority, supervised by the Minister of Justice and by the Minister of Finance. Its mission is to receive and analyse all suspicious transactions and facts reported by the institutions and persons subject to the disclosure obligation.

CTIF-CFI operates as a filter between these subjects and the judicial authorities. Upon identifying serious indications of terrorist financing or money laundering, which are restricted to the predicate offences enumerated in the Law of 11 January 1993, it reports the case to the Public or Federal Public Prosecutor.

##### **Reporting of suspicious transactions**

Whenever a financial institution knows or has reason to suspect that a transaction or fact is related to money laundering or terrorist financing, the compliance officer must inform CTIF-CFI before executing the transaction and indicate, if possible, the deadline for completing the transaction.

If unable to inform CTIF-CFI prior to completion of the transaction because of its very nature (e.g. immediate money changing) or because delaying the execution of the transaction is likely to prevent prosecution of the beneficiaries of the suspected money laundering or terrorist financing, the compliance officer of the financial institution must inform CTIF-CFI immediately afterwards, stating the reason of the report 'a posteriori'.

In order to safeguard the integrity of the related money or property for seizure by the judicial authorities, CTIF-CFI has the authority to block the disclosed transaction before the deadline indicated by the reporting institution. This opposition freezes the transaction for a maximum period of 2 working days.

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#### **Analytical process**

When CTIF-CFI is informed of a suspicious transaction, it is empowered to demand and receive any information it deems useful in order to accomplish its mission, from:

- the disclosing institution;
- all other financial institutions and persons subject to the Law;
- all police agencies;
- the judicial authorities;
- all administrative services of the State;
- the supervisory, regulatory or disciplinary authorities;
- the European Commission’s Anti-fraud Co-ordination Unit (OLAF).

The strict confidentiality to which CTIF-CFI is subject does not apply to the exchange of information with foreign counterpart agencies, on the condition that similar secrecy obligations apply. This exchange is possible on the basis of international treaties of which Belgium is signatory or on the basis of reciprocity. It is the policy of CTIF-CFI to lay down the rules of co-operation based on reciprocity in a memorandum of understanding or by way of exchange of letters.

According to the Belgian anti-money laundering Law any request from a counterpart unit on specific cases is considered equal to a disclosure of a suspicious transaction, which enables CTIF-CFI to use its investigative prerogatives upon receipt of such foreign request.

After analysing all data and finding serious indications of money laundering or terrorist financing, CTIF-CFI will submit the information, along with appropriate justifications, to the Public or Federal Public Prosecutor for further investigation and prosecution.

#### **CTIF-CFI’s role in combating terrorist financing**

Following the terrorist attacks of 11 September 2001 it was necessary to include terrorist financing. The detection of terrorist financing led the FATF to set up recommendations in this regard. The Belgian Law of 12 January 2004 amended the Belgian AML system established by the Law of 11 January 1993 in order to extend it to terrorist financing. Preventive detection of the latter has been a new priority for CTIF-CFI ever since.

Because of this new dimension, within the legal standards of each department, CTIF-CFI set up partnerships with other competent authorities such as the office of the Federal Public Prosecutor, the financial department of the offices of the Public Prosecutor, the federal judicial police and the State Security Department. The aim is to create synergy and to optimise the cooperation and possibilities for CTIF-CFI to obtain necessary and relevant information from each department in this regard.

CTIF-CFI regularly analyses the files reported for terrorist financing in order to identify typologies and indicators. This information is forwarded to the disclosing entities to help them identify suspicious transactions that could be related to terrorist financing.

#### **CTIF-CFI’s experience regarding the abuse of non-profit organizations for terrorist financing**

A study conducted by CTIF-CFI on financial crime in the NPO sector and abuse of NPOs for financial crime purposes, including terrorist financing, demonstrated that NPOs are used for terrorist financing purposes in various ways.

#### **Collected amounts**

According to CTIF-CFI’s experience, NPOs are used to collect funds from donations. Amounts collected are generally small (between 25 and 250 EUR per transaction). However, if the number of transactions carried out by each donator is limited to one single operation, the number of donators is as high as several dozen. The total amount of the funds collected from donations, therefore, is by no means negligible. These transactions are then followed by cash withdrawals or fund transfers abroad. They are therefore considerably higher than those that come from individual donations, amounting to as much as several hundred thousand EUR.

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#### ***Real estate investments***

CTIF-CFI's experience has shown that NPOs are used to purchase property with the aim of providing logistical support to terrorist organizations. One case disclosed by CTIF-CFI involved an NPO holding a bank account on which several large amounts of cash had been deposited, probably from donations. The money was used to issue cheques to the account of a notary as an advance to purchase property.

#### ***NPO as a cover***

NPOs serve as a cover for other NPOs with terrorist financing activities. One case reported by CTIF-CFI involved many small transfers and cash deposits from donations made on the bank account of charitable organisation A. Substantial transfers were subsequently made in favour of charitable organization B. Charitable organization B was the parent company of charitable organization A and was suspected of having links with a terrorist network. The humanitarian activities were used as a cover for financial transactions linked to terrorist activities.

#### ***Infiltration***

Persons who have links with terrorist groups may infiltrate NPOs and use these organizations to collect funds, part of which will not be used for charitable purposes but will be used to finance terrorist activities. One case reported by CTIF-CFI involved a group of charitable organizations with humanitarian purposes. A bank disclosed suspicious financial transactions (numerous small transfers and deposits that could originate from donations by private individuals) on the bank accounts of these organizations. The funds were then sent to the personal bank account of one of the NPO's managers and withdrawn in cash. One of the NPOs was known to be linked to a terrorist group.

#### ***Use of third parties or front companies***

NPOs use bank accounts of third parties or front companies to collect donations and finance terrorist activities. One reported case regarded suspicious (abnormal) transfers and deposits on the bank account in Belgium of an individual receiving only a small income through social benefits. One of the transfers had been made by the founder of a NPO established in Belgium. This person had links with a terrorist group. Another disclosed case concerned suspicious transactions (many cash deposits) on the bank account of company X, which was not an NPO. According to the balance sheet the company had no activity at all. Individual A, who had power of attorney on company X's bank account was the manager of a NPO known to be linked to a terrorist group.

### **FATF Special Recommendation VIII**

FATF Special Recommendation VIII, related to NPOs, requires that:

- Countries review the adequacy of laws and regulations relating to “entities” that can be abused for terrorist financing,
- Countries implement measures to ensure that (legitimate) NPOs cannot be misused by terrorist organizations.

The objective of Special Recommendation VIII is to ensure that NPOs are not misused by terrorist organizations: to pose as legitimate entities, to exploit legitimate entities as conduits to finance terrorists, to divert funds intended for legitimate purposes to terrorism purposes.

The approach adopted by the FATF to achieve this objective is based on the following principles:

- Given the sector's important social and economic role it is important to preserve the integrity of NPOs. The fight against the use of the non-profit sector by terrorist organizations is important not only to combat terrorist financing but also because the use of the NPO sector by terrorist financiers will undermine donor confidence.
- Past and ongoing abuse of the NPO sector by terrorist organizations demonstrates the need for protective measures. Measures should be taken to protect the sector against such abuse and to identify and take effective action against those NPOs that either are exploited or actively support terrorists or terrorist organizations.

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- Measures should aim to prevent and prosecute terrorist financing and terrorism support. When an NPO is suspected or implicated in terrorist financing activities or other forms of terrorism support actions taken by countries must be to investigate and halt such terrorist financing or support eventually using freezing measures.
- Measures adopted by countries should not disrupt or discourage legitimate charitable activities but should promote transparency, integrity and public confidence in the management and functioning of NPOs to ensure a greater confidence in the sector, across donors and the general public (charitable funds reach intended legitimated purposes).
- Cooperative relationships should be developed amongst the public, private and NPO sector to raise awareness and foster capabilities to combat terrorism abuse of NPOs (develop academic research and information sharing within the NPO sector to address terrorist financing related issues).
- The approach taken in dealing with the terrorist threat to the NPO sector should be targeted and flexible to adapt to the diversity of NPOs within individual national sectors and to evolve over time to face the changing nature of the terrorist financing threat.

### The implementation of Special Recommendation VIII

The FATF recommends the following approach for the implementation of Special Recommendation VIII:

- *Countries should encourage or undertake outreach programmes to raise awareness in the NPO sector about the vulnerabilities of NPOs to terrorist abuse and terrorist financing risks, and the measures that NPOs can take to protect themselves against such abuse. Countries should work with the NPO sector to develop and refine best practices to address terrorist financing risks and vulnerabilities and thus protect the sector from terrorist abuse.*

CTIF–CFI’s website contains various examples, both national as well as international, of misuse of NPOs for terrorist financing purposes. CTIF–CFI’s website also includes different FATF reports on the risks and vulnerabilities of terrorist financing that the NPO sector could be confronted with. Its annual report, which is widely published, is also a useful tool for raising the sector’s awareness. This information allows NPOs to become more aware of the risks of misuse they face. Because of this awareness raising the financial sector is also in a better position to detect transactions by NPOs that may be linked to terrorism or terrorist financing.

- Countries should promote transparency, confidence in the administration and management of all NPOs. *NPOs should maintain information on: (1) the purpose and objectives of their stated activities; and (2) the identity of the person(s) who own, control or direct their activities, including senior officers, board members and trustees. This information should be publicly available either directly from the NPO or through appropriate authorities.*

Belgian law stipulates that NPOs and foundations must have very detailed articles of association, including the last names, first names, address, date and place of birth of each founder or, in case of a legal person, the registered name, legal form and address of the registered office, the precise description of the aim(s) for establishing the association, the rules governing the appointment, termination of duties and removal from office of directors. These documents and information must be deposited at the Commercial Court registry in the court district where the NPO has its registered office. Anyone may inspect these documents and information free of charge at the Commercial Court registry.

NPOs wanting to benefit from the tax exemption scheme for their donors must register with the Ministry of Finance.

- *NPOs should issue annual financial statements with a detailed breakdown of income and expenditures.*

In Belgium all NPOs must keep accounts. Large and very large NPOs as well as foundations are subject to the same accounting rules as commercial companies. Small NPOs only have to submit



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simplified accounting. Large and very large NPOs must deposit their annual financial statements with the Belgian National Bank just like commercial companies do. Small NPOs must establish their annual financial statements according to a simplified procedure and deposit them with the Commercial Court registry, where they are added to their file.

- *Countries should also take steps to have an effective supervision or monitoring of NPOs which account for (1) a significant portion of the financial resources under control of the sector; and (2) a substantial share of the sector's international activities.*

NPOs should be licensed or registered. This information should be available to the competent authorities.

NPOs should have appropriate controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose and objectives of the NPO's stated activities.

NPOs should maintain, for a period of at least five years, and make available to appropriate authorities, records of domestic and international transactions that are sufficiently detailed to verify that funds have been spent in a manner consistent with the purpose and objectives of the organization.

First of all, in Belgium the large and very large NPOs must have their financial situation, annual financial statements, and compliance with the law and the articles of association of the transactions in the annual financial statements checked by one or more auditors (company auditors).

NPOs domiciled in Belgium are subject to tax on legal persons. Therefore, even if they do not engage in profit-making activities, they must make an annual tax return with an overview of their receipts and expenditure and are subject to an in-depth audit at least once every six years.

The tax authorities are very mindful of the problem of “false NPOs” – i.e. those that carry out profitable activities under the cover of an NPO.

As part of the detecting “false NPOs”, the articles of association, the activities actually carried out and the accounting records held by the NPO are closely examined. An audit is made of the transactions carried out by the NPO, its income, the nature of its customers, its personnel and its assets used.

Consequently, the tax audits carried out on NPOs are likely to lead to the detection of money laundering and/or terrorist financing mainly through revealing the real business of the NPO and by tracing its commercial and financial accounts. When evidence of money laundering and/or terrorist financing is discovered during the audits and checks carried out by the tax authorities, it may report the facts to the Public Prosecutor's Office.

- *Competent authorities (law enforcement, FIUs, tax authorities) must be able to gather information on NPOs of concern and investigate activities of NPOs suspected of links with terrorist organizations.*

Countries should ensure that full access to information on the administration and management of a particular NPO (including financial and programmatic information) may be obtained during the course of an investigation.

In Belgium NPOs must deposit their articles of association, the instruments relating to the appointment or resignation of directors, persons entrusted with the day-to-day management, persons authorised to represent the association at the Commercial Court registry in the court district where the NPO has its registered office. This file also contains a copy of the annual financial statements of the NPO. Any person may inspect the documents that any NPO has filed free of charge. The competent authorities (including the FIU) can obtain a copy of the documents in the file of an NPO free of charge.

- *Countries should have investigative expertise and capability to examine those NPOs suspected of either being exploited by or actively supporting terrorist activity or terrorist organizations. Countries should ensure effective cooperation, coordination and information sharing to the extent possible among all levels of appropriate authorities or organizations that hold relevant information on NPOs.*

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In Belgium the judicial authorities (mainly the Federal Public Prosecutor's Office with respect to terrorism and terrorist financing), the police services, the intelligence and security services and the FIU have investigative powers and sufficient material and human resources to examine and conduct the necessary investigations into NPOs that could be exploited or support terrorist activities.

For instance, they have access to the information on a particular NPO at the Commercial Court registry, to the financial information through court orders from banks or through FIU cooperation.

The Belgian anti-money laundering law allows cooperation between the police/judicial authorities and the FIU for investigations, especially in case of suspicions of terrorism with regard to an NPO.

- *Countries should establish appropriate mechanisms to ensure that when there are suspicions or reasonable grounds to suspect that a particular NPO: (1) is a front for fundraising by a terrorist organization; (2) is being exploited as a conduit for terrorist financing, including for the purpose of escaping asset freezing measures; or (3) is concealing or obscuring the clandestine diversion of funds intended for legitimate purposes, but redirected for the benefit of terrorists or terrorist organizations, this information is promptly shared with all relevant competent authorities in order to take preventative or investigative action.*

In Belgium an association may be declared unlawful if the articles of association do not contain the information referred to above or if one of the aims for establishing the NPO breaches the law or public order.

At the request of a member, any interested third party or the Public Prosecutor's Office, the court may order the dissolution of the NPO that does not fulfil its obligations, uses its assets or revenue for aims other than those of its establishment or seriously infringes the articles of the association or breaches the law or public order.

Transparency measures have also been introduced for NPOs established under foreign law wishing to open a centre of operations in Belgium. At the request of the Public Prosecutor's Office or any interested party, the court may order the closure of any centre of business seriously infringing the articles of the association in question or breaching the law or public order.

- *Countries should identify appropriate points of contact and procedures to respond to international requests for information regarding particular NPOs suspected of terrorist financing or other forms of terrorist support.*

As to international cooperation, the judicial authorities as well as the FIU have appropriate channels for exchanging information on NPOs suspected of being linked to terrorist organizations.

## Conclusion

According to CTIF-CFI's experience, the legal sources of terrorist financing mainly regard the illegitimate use of non-profit organizations. These are primarily organizations established in Belgium holding accounts on which funds are raised, often donations, for terrorist activities. The financial transactions mostly consist of cash deposits corresponding to the donations, followed by cash withdrawals or transfers abroad.

It seems that a relatively large number of files reported by CTIF-CFI in connection with terrorism regard NPOs. The total amount of funds collected in the form of donations by each of the charitable organizations featuring in CTIF-CFI's files remains relatively small. Indeed these funds appear not to exceed several hundred thousand EUR, which are entirely or partly used to finance terrorist activities. However, as far as several of these organizations have international branches, the total amount of funds collected by all the organizations can be relatively substantial.

Special Recommendation VIII and its implementation by countries is therefore of great importance.

In addition it seems likely that terrorist organizations have different sources of financing, since they do not limit themselves to licit sources of financing. This trend is to be monitored closely and reflects the importance of the implementation of all other FATF Special Recommendations.

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OSCE Permanent Council Decision No. 617 (2004) *on Further Measures to Suppress Terrorist Financing*

## Preventing the abuse of non-profit organizations for terrorist financing: Canada’s regulatory regime

*Canada Revenue Agency, Charities Directorate*

### Background

There are over 85,000 registered charities in Canada, mostly run by volunteers and with low revenues. They touch all aspects of society – including education, health, faith, human rights, social justice, environment, arts and culture, community amenities and recreation. Of course, the vast majority strive to comply with legislative and regulatory rules.

Charities play a vital role in achieving goals that Canadians value highly, both at home and abroad. Recognizing this, and to encourage Canadians to support charitable activity, the *Income Tax Act (the ITA)* gives significant tax privileges to charities and donors. To maintain public confidence in these incentives, the Government of Canada and charities need to protect the charitable sector from abuse, including the exploitation of charitable resources to support terrorism and other non-charitable purposes and activities. But the very factors that promote Canadians' high respect for charities can also make them vulnerable to exploitation by terrorist supporters. Charities bring people together for a common purpose and collective action. Some have a global presence, often in conflict zones or in places with little infrastructure, and frequently move money, people, and goods to and from these areas. Where there are no banks, charities may have to deal in cash or use alternative remittance systems. All this may unintentionally provide a network, and a cloak of legitimacy, for activities that support terrorism.

In testimony before the Air India Commission of Inquiry into the Bombing of Air India Flight 182, Royal Canadian Mounted Police (RCMP) officials reported that they generally see the involvement of one or more charities and related non-profit organizations (NPOs) in major terrorism investigations, and that these organizations play a significant role not only as vehicles for fundraising but in providing other means of cover and support for the activities of terrorist groups. Analysis by the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) tabled at the Inquiry shows that charities and NPOs have figured in over one-third of disclosures related to suspected terrorist financing.

### Legal Framework

Constitutionally, the regulation of charities falls within provincial jurisdiction. The federal role is limited to the regulation of charities for purposes of the ITA. Canada has had a tax incentive for charitable giving since the 1930's, and from 1967 charities have been required to register with the Canada Revenue Agency (CRA) to qualify for the special tax privileges associated with that incentive. In 2008, 5.9 million Canadians declared financial or in-kind charitable donations of \$8.8 billion. This indirect tax assistance to registered charities amounts to around \$3.7 billion in foregone revenue for federal and provincial governments. The privilege of being able to offer donors a tax credit or deduction to reduce tax otherwise payable gives the Government of Canada both a direct regulatory interest, as well as a stewardship responsibility, in providing an increased measure of confidence to Canadians that their generosity is well-founded.

The Charities Directorate of the CRA is the Government of Canada's centre of expertise on charities. The Directorate administers and enforces the ITA rules relating to registered charities by ensuring that organizations that do not comply with the applicable rules are not granted or allowed to maintain registered charitable status.

Canada has followed FATF advice and has taken a targeted approach in dealing with the terrorist threat to the non-profit sector. Registered charities represent a significant portion of the financial resources of the non-profit sector, accounting for approximately 68% of all revenues and 95% of all donations. In addi-

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tion, they account for a substantial share of the sector’s foreign activities: 75% of international organizations in Canada are registered charities. The Charities Directorate role relates only to registered charities, not to other NPOs (there are around 80,000 additional NPO corporations operating in Canada). Registered charities must be non-profit, but not all NPOs are eligible for registration as charities. While neither registered charities nor NPOs pay tax on income, only registered charities can issue official donation receipts for income tax purposes. CRA data show that the highest terrorist financing risk is associated with organizations which in Canada fall within the registered charity segment of the non-profit sector. The rest of that sector, like registered charities, remains subject to the full range of Canada’s anti-terrorism legislation; and the reporting obligations of banks and designated non-banking financial organizations apply to the financial dealings of charities and NPOs just as to any other undertaking.

The ITA requirements for charities are a mix of tax policy considerations and statutory expressions of common law principles relating to charitable trusts. Certain fundamental requirements – such as non-profit provisions and the requirement that charities not operate for a mix of charitable and non-charitable objectives – derive from common law principles relating to charities. The common law also sets out the four ‘heads’ of charity – over centuries, the courts have decided that unless an organization is created, and operated, for one or more of the relief of poverty, the advancement of education, the advancement of religion, or other purposes beneficial to the community that are recognized as charitable, it cannot be considered, legally, as a charity. The ITA also imposes residency requirements, an annual expenditure test, the obligation to file annual returns and to keep adequate books and records to verify donations and the use of resources (not having sufficient books and records in Canada to substantiate that the requirements for registration have been met is, in itself, reason to revoke an organization’s registration), and a prohibition against making resources available to organizations that are not “qualified donees” – primarily, other Canadian registered charities. As well, the organization’s purposes and activities must comply with Canadian law and public policy.

### The Charities Anti-Terrorism Program

To effectively identify and manage the risk of terrorist involvement in charities, the program must integrate information from a variety of sources. As noted in the Air India Report [1]:

“The CRA receives intelligence reports from, and has liaison arrangements with, both the [Royal Canadian Mounted Police] RCMP and the [Canadian Security Intelligence Service] CSIS. The Charities Directorate also has its own pool of information. In particular, the CRA has considerable investigative powers under the ITA. As well, the CRA actively monitors the media and the Internet and it reviews case law, academic papers and texts....[r]esources are devoted to the collection and analysis of program-derived and publicly available information specifically related to the use of social, community, religious and humanitarian organizations to provide cover and legitimacy for international terrorism.”

All this information is used to assess risk in both application screening and post-registration proactive monitoring, in cooperation with CSIS, RCMP and FINTRAC.

In reviewing new applications and existing registered charities, the CRA requests information from the RCMP and CSIS when there are concerns an organization may be connected to terrorism. Where publicly available information combined with information an organization is required to provide to the CRA is sufficient to make the case that an organization is not exclusively dedicated to charitable purposes, the CRA will – and does - use the regular procedures under the ITA to deny charitable status, or to support a range of sanctions up to and including the revocation of registration.

The ITA provides CRA a range of intermediate sanctions against registered charities that are non-compliant. These include financial penalties and/or the temporary suspension of certain privileges such as the ability to issue tax receipts. The scope of activities that can be subject to sanctions range from, but are not limited to, certain business activities, unjustly enriching principals of the organization, gifting resources to non-eligible recipients and furnishing false statements with respect to tax receipts. The se-



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verity of the penalty increases with subsequent infractions and may ultimately lead to revocation.

About 2,000 charities have their registrations revoked each year. These are mostly organizations that have ceased operations or have failed to file annual returns. CRA conducts comprehensive field audits of about 800 registered charities each year. About 40 charities a year lose their registration as a result of serious noncompliance issues, including dubious fund-raising schemes, political activities, lack of proper books and records, and improper personal benefit. In addition, registered charities that have failed to demonstrate sufficient control over their foreign operations have been revoked.

The regular ITA powers have been used to revoke the registration of three charities in the last year on grounds that included their links to terrorism, (the following details are quoted from the CRA's publicly-accessible letters to the organizations concerned):

- in July 2010, the Tamil (Sri Lanka) Refugee-Aid Society of Ottawa was removed from the register on the grounds, among others, that it had “provided funding to non-qualified donees outside Canada...[t]his funding included \$713,000 provided to an organization which, on the basis of publicly available information.....the CRA believes was operating as part of the support network for the Liberation Tigers of Tamil Eelam (the LTTE), a listed entity under the *United Nations Suppression of Terrorism Regulations* and the *Criminal Code of Canada*”;
- in March 2011, the World Islamic Call Society (Canada) was revoked for a range of non-compliance reasons, including that “....the Society acts at the direction of, and receives all of its funding from, the Libyan-based World Islamic Call Society (WICS-Libya), an organization founded by Muammar al-Qaddafi (Gadhafi) in 1972 whose objects and activities are not confined to the advancement of religion as that term is understood under Canadian law.....the Society's operations consisted primarily of acting at the direction and on behalf of WICS-Libya to transfer funds through Canada to specific groups and individuals.....some of these groups and individuals are alleged to have been involved in terrorism ..... an affidavit and the Plea Agreement filed in the successful U.S. conviction of Abdurahman Muhammad Alamoudi in 2004 on charges of willfully attempting to violate U.S. economic sanctions against Libya imposed because of Libya's involvement in terrorist bombings and the downing of Pan Am Flight 103 over Lockerbie, Scotland, attest to the use of the WICS-Libya's network to move funds on behalf of the Libyan government in violation of the sanctions against Libya.....it is clear from the Alamoudi plea agreement that .....the purposes in which WICS-Libya is concerned, and which in turn direct the purpose and operation of the Society, extend to political causes and goals that cannot be reconciled with the concept of charity under Canadian law ”; and
- in April 2011, the International Relief Fund for the Afflicted and Needy (Canada), whose privilege of issuing tax receipts to donors had been suspended for the previous year, lost its registration on the grounds, among others that “ ...[o]ur analysis of the audit information has led the CRA to believe that IRFAN-Canada provides support to Hamas, a listed terrorist organization. Our findings indicate that IRFAN-Canada provided over \$14.6 million in resources to operating partners that were run by officials of Hamas, openly supported and provided funding to Hamas, or have been listed by various jurisdictions because of their support for Hamas or other terrorist entities.”

However, as a prudent reserve power, the *Charities Registration (Security of Information) Act* (the CRSIA) provides a different process for use if it is necessary to rely on classified information to substantiate an organization's ties to terrorism. Parliament enacted the CRSIA as part of the *Anti-Terrorism Act 2001*, to “demonstrate Canada's commitment to participating in concerted international efforts to deny support to those who engage in terrorist activities; to protect the integrity of the registration system for charities under the *Income Tax Act*, and to maintain the confidence of Canadian taxpayers that the benefits of charitable registration are made available only to organizations that operate exclusively for charitable purposes”. Under CRSIA, the Ministers of Public Safety and National Revenue may certify that there are reasonable grounds to believe that an applicant or registered charity has, is or will provide resources

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to support terrorism. The test is tied to the definitions of a listed entity and terrorist activity in the *Criminal Code*. There is no requirement to link particular charitable resources to specific acts of terrorism. It is an objective test; the criminal standard of mens rea (“guilty mind”) does not apply. The grounds on which a certificate are to be based refer specifically to the use of an organization’s “resources”, which in the context of the charity provisions under the ITA is interpreted as including financial, human, and physical resources. If the certificate is upheld in the Federal Court, it is grounds for immediate denial of a request for, or revocation of, charitable registration. This is a civil procedure, not criminal; action is taken against organizations, not individuals; civil law standards apply. A successful CRSIA action can result only in the refusal or removal of registered charity status, which is not in any sense a right but a privilege in the form of a tax benefit, and not in any action against a person.

The CRSIA provides the legislative framework for CRA to use security and intelligence information in deciding if an organization qualifies for registration, or continued registration, as a charity. It provides a means by which sensitive security information can be used in determining an organization’s eligibility for registration, and yet be protected from disclosure. It gives the CRA new grounds for refusing or revoking charitable status - related explicitly to support for terrorism.

### Information sharing

Privacy considerations and maintaining the confidence of Canadians that their personal information is secure dictate that information provided to the CRA by taxpayers can only be disclosed under specific exceptions to the general prohibition on releasing it. Given the considerable value of the tax privileges that are available to registered charities, the need for transparency and accountability means that much of the information charities provide is subject to such exceptions and is thus publicly accessible. Where there are reasonable grounds to suspect that information held by the CRA might be relevant to the investigation of a terrorism offence under the *Criminal Code* or to threats to the security of Canada, the ITA permits the CRA to share other, broader but tightly defined information with the RCMP, CSIS and FINTRAC, who are then permitted to use the information for their own purposes. These special provisions relate to both registered charities and organizations that have applied for registration – information about applicant organizations is not shareable in other situations. Additionally, the CRA can share any taxpayer information with other government departments and agencies for the purpose of enforcing the ITA and CRSIA, although in these circumstances, there are prohibitions on its further use by them.

### Outreach

The Government of Canada is very conscious of the need to strike a balance between a firm stand against the abuse of charities for terrorism purposes, and the need not to disrupt or discourage legitimate charitable activities. The Charities Directorate takes a holistic approach to its outreach both to the sector and to the public, in order to promote transparency generally and engender greater confidence in the sector, across the donor community and with the general public that charitable funds and services reach the intended, legitimate, beneficiaries. Great efforts are made to develop a co-operative relationship with the sector to this end.

The CRA publishes a wide range of guidance for registered charities on a range of legal and operational matters, supplemented with webinars and in-person information sessions around the country. Issues addressed include carrying out activities outside Canada, and on conducting activities directed at upholding human rights. Specifically in relation to the vulnerability of the sector to terrorist abuse, Charities in the International Context provides background information on the international and domestic legal regime <http://www.cra-arc.gc.ca/chrts-gvng/chrts/ntrntnl-eng.html> . The Terrorism Checklist provides a ready reference for charities on some basic precautions they can take to protect against this and other forms of abuse, as part of good management practice <http://www.cra-arc.gc.ca/chrts-gvng/chrts/chcklsts/vtb-eng.html> .

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The CRA also administers a contribution program, the Charities Partnership and Outreach Program, to provide funding to registered charities and non-profit organizations in Canada to develop and deliver innovative education and training on compliance for registered charities. The overall objective is to increase compliance by the charitable sector with relevant parts of the *Income Tax Act*, including by improving the sector's own capacity to develop and deliver sustainable compliance-based education programs. In 2009-2010, a successful project under the program focused on increasing the sector's capacity to avoid involvement in terrorism. The materials developed can be accessed via <http://www.capacitybuilders.ca/clip/clip-resources.php>

The sector has a number of “umbrella organizations” that provide guidance and varying degrees of oversight. The Canadian Council of Christian Charities offers its members a certification program, under which participating charities can display a special “seal of approval”. Certification requires that the member organization has an independent board, audited financial statements, and that it has adopted the Council's “Code of Ethical Fundraising and Financial Accountability”. Similarly, the Canadian Centre for Philanthropy encourages its members to adopt its “Ethical Fundraising and Financial Accountability Code”. The 500 charities that have adopted this Code are committed to responsibly managing the funds that they receive and reporting their financial affairs accurately and comprehensively. The Association of Fundraising Professionals also encourages its members to adopt a code of ethics, a donor's bill of rights and put in place a mechanism to register complaints. Imagine Canada is launching a Standards Program in 2011 that offers a Canada-wide set of shared standards for charities and nonprofits wishing to enhance their effectiveness in the fundamentals of governance, paid-staff management, financial accountability, fundraising, and volunteer involvement. The Program includes a voluntary accreditation program for organizations wishing to publicly demonstrate they have successfully met the standards through a third-party peer review process. A variety of resources will be publicly available to give all organizations the opportunity to strengthen their capacity in each area of the standards regardless of their intention to participate in the accreditation process. Other charitable organizations with chapters or branches in Canada also play an important role in ensuring that high standards of accountability are observed by their affiliates.

## Conclusion

The Government of Canada has made it very clear that it will not tolerate the abuse of the registration system for charities to provide any means of support to terrorism, and that the tax advantages of charitable registration should not be extended to an organization where its resources may, directly or indirectly, provide any means of support for, or benefit to, any organization engaged in terrorism. In delivering this outcome, the CRA works with the sector to ensure that there is a good level of awareness of the risk and of its obligations; and takes a proportionate and risk-based approach to ensuring that areas of greatest vulnerability receive the greatest scrutiny.

## End Note

[1] Report of the Commission of Inquiry into the Investigation of the Bombing of Air India Flight 182, Volume 5, p 222.

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## Non-profit Organizations and their relationship with terrorist financing

*Kyrgyzstan, State Committee of National Security*

Research and analysis on the issue of abuse of non-profit organizations (NPOs) for financing of terrorism show that the diversion of even a very small amount of money can pose a potentially serious problem of terrorist financing activities. Despite the fact that in most countries regulatory measures and oversight are applied to NPOs in order to reduce the risk of their abuse to finance terrorism, the need for developing additional measures and strengthening mechanisms to detect abuses in this area is still relevant.

The abuse of non-profit and non-governmental organizations in complex terrorist financing schemes is a growing concern to the international community today. This is connected primarily with absolute, as one would think, incompatibility of noble, human rights functions which NGOs and NPOs undertake in their founding document. Difficulties in detecting terrorist financing through abuse of NPOs are related to their social status. It is widely acknowledged that NPOs play a crucial role in social and financial sectors of society, and it is obvious that no one puts this fact into question. Nevertheless, the amount of cash and other assets involved in the charitable sector means as such that diversion of even a very small proportion of these funds to support terrorism would constitute a serious problem. Therefore, the international community should pay attention to the problem of lack of information on the risks faced by the NPO sector, in terms of its possible abuse by terrorists.

Many NPOs are particularly vulnerable to abuses associated with financing of terrorism. NPOs are trusted by society and have access to significant sources of funds and often have relatively high cash turnover. In addition, some of them have an extensive network of offices in many countries, which provide a basis for domestic and international financial transactions, often in areas that are most vulnerable in terms of abuse to finance terrorist activities. Finally, depending on the country of residence and legal form, the activities of NPOs are often not regulated sufficiently or not regulated at all, or there are no set requirements as for establishing NPOs (for example, requirements on the amount of capital, there are no checks of persons who are the founders and employees of NPOs, etc).

Examples studied by analysts from financial intelligence units (FIU) show that NPOs can be abused for terrorist financing in a variety of ways:

- First of all, NPOs are often used by terrorists to collect money. For example, assets of large NPOs were frozen at one point on the basis of the UN Security Council Resolution 1373 (2001);
- Often, NPOs are recognized as charitable organizations and are exempt from taxes;
- Some NPOs use rather aggressive methods of fund-raising, sometimes trying to get donations from the general public, and in some cases focusing on specific target groups, particularly within certain ethnic or religious communities.

For example, an organization officially registered as a children's charity has used videos depicting the actions of religious "freedom fighters" in various countries, while showing videos of inhuman treatment of the followers of this religion. The videos called for donations to a specific mailbox number to help in this "struggle". There is no doubt that these videos were widely distributed by religious organizations throughout the region. The same mailbox number has frequently appeared in publications with articles of known extremists.

Experts note the importance of informal cash collection in many ethnic or religious communities and the difficulties to implement proper control over these funds. It is likely that a large portion of these funds may be used for completely legitimate charitable purposes; however, the risk of possible abuse is also obvious.



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Collecting cash can also contribute to laundering the proceeds from criminal activities carried out by terrorist groups, and injecting them into the “legal financial system”. These funds could possibly be presented as legitimate collections of cash for charitable purposes by NPOs, while in fact, being a form of money laundering. These funds can be used in the future to fulfill terrorist purposes.

NPOs can also be abused by terrorists to move money. In this case, they use the fact that financial transactions to transfer funds from one region to another (often to foreign countries) are considered as normal operations of foundations and charities. In some cases, the legal form and official purpose of NPOs are specially selected in order to avoid regulation and control (for example, cultural associations, created in some countries by local religious communities). There are examples where within a particular ethnic community a network of related foundations is organized, which are officially registered in various countries and then used for illicit money transfers. It is difficult to assert that these schemes are directly related to the financing of terrorism, but such a structure is of interest because of its unusual characteristics and vulnerabilities to abuse. Often, such examples show that so-called “alternative money remitters” use bank accounts of NPOs to accumulate cash and perform mutual settlements with their foreign counterparts. In some cases, these transactions are considered by the competent authorities as suspicious because of an apparent discrepancy between the movements of funds and the living conditions of a particular community, which provides the financial support to NPOs involved.

**The following example clearly shows how NPOs can be abused to transfer money to individuals suspected of involvement in terrorism:**

A FIU in the country “A” received updated information on the consolidated list of individuals and entities prepared by the UN Security Council. One organization operated under different variants of the same name in several countries. It was characterized as a tax exempt NPO, the official purpose of which was to implement humanitarian aid projects all around the world. Among the many addresses of this organization designated by the UN, some were located in the country “A”. The FIU received a report of suspicious transactions regarding the NPO, which was on the list of addresses named in the UN list. The notification included bank accounts and names of three individuals who owned a controlling block of shares of the branch of the NPO located in the country “A”. One of these individuals (Mr. “X”) lived at the address specified in the UN list, and two other individuals had addresses in two different countries. The notifications included detailed information on a significant number of fund transfers sent from related locations to the branches of the above mentioned charitable organization, and to Mr. “X”. The investigation carried out by the FIU showed that Mr. “X” was associated with these organizations, as well as four other international NPOs.

**The following is another example showing that the leadership of an NPO abuses the organization to finance terrorism:**

A certain NPO was registered in the country “X” as a charitable organization and exempt from taxes. The official purpose of the activities of this NPO is implementation of projects to provide humanitarian assistance. The NPO was registered in the country “X”, but actually carried out its activities in different countries, using changed names. Financial and business documents were seized at the headquarters of the NPO and homes of the Chief Executive Officer of this NPO, and a member of its Board of Directors. On the same day an order was issued in the country “X” instructing to freeze the assets of the NPO for further investigation, which eventually proved the abuse of the NPO to support terrorism. 11 months later, in accordance with UN Security Council resolutions, country “X” sent information on the NPO to the UN for its inclusion in the lists of organizations linked to terrorist activities. In the country “X” the Chief Executive Officer of the NPO was convicted for fraud and for participating in organized criminal activity associated with transferring charitable contributions in excess of 315,000 USD in favor of terrorist organizations. Evidence was obtained prior to the trial that the NPO provided, both directly and indirectly, support to terrorist organizations.

**In general, the typology of financing of terrorism includes the following implementation phases:**

1. A foreign foundation accumulating funds in religious communities based in Western countries, as well as countries of the Arab world sends the funds to NPOs for supporting co-religionists, including those abroad.

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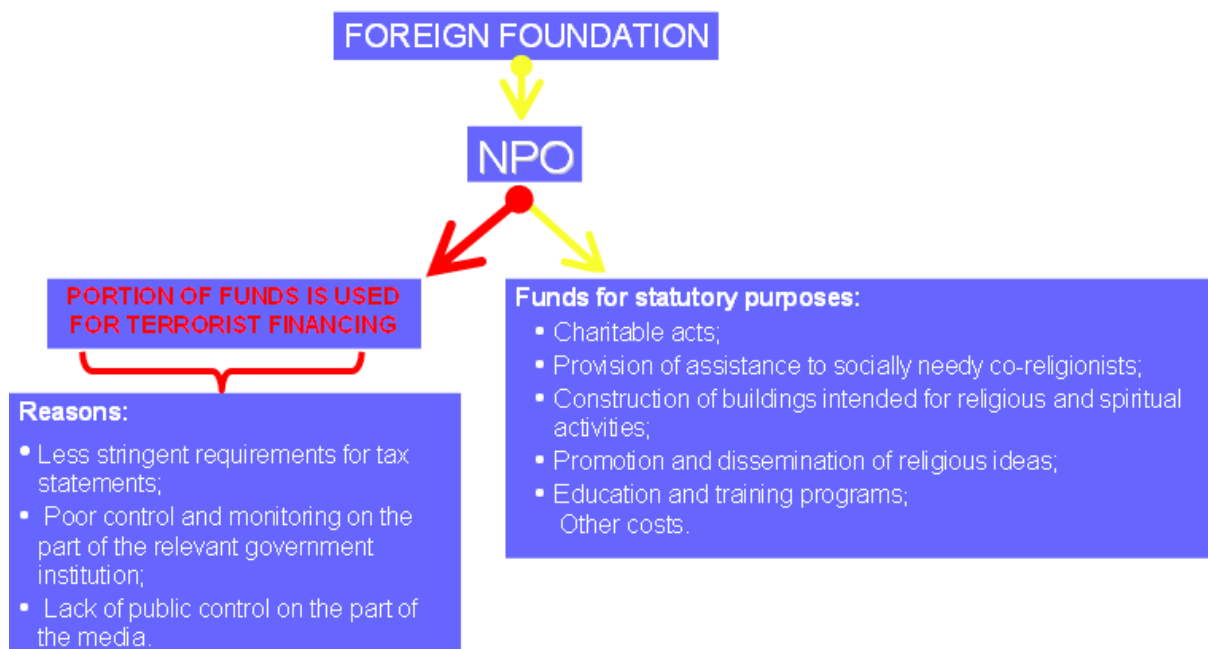
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2. NPOs recipients of assistance from external donors should direct these funds, according to their statutory purposes, to:
  - charitable acts;
  - provision of assistance to socially needy co-religionists;
  - construction of buildings intended for religious and spiritual activities;
  - promotion and dissemination of religious ideas;
  - educational and training programs;
  - other costs.
3. Funds are transferred from abroad into the bank accounts of these NPOs or in cash.
4. Currently, the less stringent requirements for tax statements of NPOs in new democratic government entities as well as the liberal regime of control over their activities by state authorities and the public, make the sector vulnerable to abuse for terrorist financing and laundering of proceeds of crime. For example, foreign aid can be diverted towards non-statutory objectives, including financing of terrorism.

#### Typical Pattern of Using NPOs to Finance Terrorism



Given the above mentioned typologies one can conclude that an intelligence based method is most likely to be successful in detecting possible links between NPOs and terrorist financing schemes. This method consists in uncovering linkages with other NPOs, or contacts with people already suspected of involvement in terrorist operations or terrorist financing. In some cases, biographical data of directors or managers of NPOs may already point to connections with criminal activities, including extremist or terrorist activities. In other cases it is possible to establish links with known terrorist organizations or with other organizations included in the lists of individuals or entities involved in terrorist activities, which are maintained by the United Nations or some countries. The vigilance of the broader society with regard to possible involvement of NPOs in questionable activities may also contribute to identifying potential abuse.

Reports by financial institutions about suspicious or unusual transactions, and their subsequent analysis by the FIU or law enforcement agencies, also play an important role in identifying specific instances of abuse, involving NPOs, by persons suspected of terrorism. In some countries, reports on suspicious transactions related to unusual activity of NPOs often lead to the initiation of an investigation; in other cases, notifications and analysis by the FIU contribute to the further developing ongoing investigations.

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## The role of the NGO sector monitoring for preventing the terrorism financing risks: the Latvian experience

*Latvia, State Revenue Service*

The non-governmental sector (according to the Special Recommendation of the Council of Europe – the non-profit organisations) in Latvia is a union of civil society organisations and informal groups, which co-exists with the governmental and commercial sectors. Non-governmental organisations are acting in the interests of society and its groups, and their actions are not aimed to gain profit.

Usually, non-governmental organisations in Latvia are established to support a specific need of the society which is not getting enough attention from either the state or municipality, or private entrepreneurs. Non-governmental organisations provide an opportunity for people to enhance their quality of life, as well as to express their professional qualities and form their personalities. For youth non-governmental organisations are offering an opportunity to get the first job experience in different volunteer work programmes.

According to the European Convention for Protection of Human Rights and Fundamental Freedoms the term “non-governmental organisation” is broader than the traditional notion of non-governmental organisation, which is commonly used in Latvia. Pursuant to the European Convention of Human Rights, this group of entities involves all unions to which the often used label “non-governmental organisation” may be referred. Namely, different public organisations and unions, public foundations, clubs, trade unions, etc. Political parties are non-governmental organisations as well, even if under national laws they are governed by the provisions of the public law.

Although the trade unions, open society foundations, political parties, unions of the political parties, corporations (professional associations) all are active in Latvia, when a reference to the non-governmental organisations is made, usually only associations and foundations are implied.

Association is a voluntary union of individuals, aimed to achieve the goal, which specified in its articles of association. Therefore, it is an organisation, which joins individuals on the membership basis. At the same time, foundation is an aggregate of property that has been separated for the achievement of a goal specified by its founder. There are no members in the foundation. It may have one or more founders, whose status remains unchanged for the rest of their lives. Besides, neither the former, nor the latter are aiming to gain profit.

Apart of the general legal acts and internal normative acts the legal activities of non-governmental organisations depending on their type are also governed by:

- the Law on Associations and Foundations;
- the Law on Entering into Force of the Law on Associations and Foundations;
- the Law on Public Benefit Organisations (providing that the status of the public benefit organisation has been granted).

Other organisations in Latvia, having similar aims with non-governmental organisations, are religious organisations, trade unions, professional organisations and foundations, governed by other laws.

Every resident of Latvia has a right to join religious organisations thus manifesting the freedom of thought, conscience and religion, which involves the right to freely express their opinion towards religion, to manifest individually or together with others any religion or not to manifest any of them, perform religious rites, freely change their religion or other faith, as well as express their religious conviction in accordance with the relevant provisions of law.

Religious organisations are congregations, religious unions (churches) and dioceses. The activities of religious organisations are governed by the Law on Religious Organisations.

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In Latvia, associations and foundations, religious organisations and institutions thereof are registered by the state registry institution – the Register of Enterprises of the Republic of Latvia (hereinafter – the RE). The RE is overseen by the Ministry of Justice of the Republic of Latvia. Thus, the RE performs the registration of specified entities in order to establish their legal status and to ensure the public accessibility of the information prescribed by the law.

In accordance with law everyone is entitled to receive from the RE the information concerning entities registered therein - merchants, representations of foreign merchants and organisations, co-operative societies, European economic interest groups, European commercial companies, European co-operative societies, political parties and associations thereof, administrators, insolvent entities, associations and foundations, religious organisations and institutions thereof, trade unions, mass media. The database is being updated on an ongoing basis, not once per year, month or day. Every time, when availing himself of the RE information, one can be sure that the received data formally are not out of date.

Before commencing their activities in Latvia associations and foundations shall lodge an application with the Registry of Associations and Foundations of the RE, while religious organisations upon commencing their activity shall lodge an application with the Registry of Religious Organisations and Institutions of the RE.

Information regarding associations and foundations shall be entered into the Registry of Associations and Foundations of the RE, specifying the name of association or foundation, its legal address, information on responsible persons, aims of association or foundation, the period of activity providing that association or foundation is established for a limited period of time. In the case of prohibition of the activity, insolvency, liquidation or reorganisation of association or foundation, the respective data are entered in the Registry of Associations and Foundations as well.

Religious organisations and institutions thereof are registered by the Registry of Religious Organisations and Institutions of the RE. In addition to the data, which must be specified when registering association or foundation, information on the legal status of the religious organisation (congregation, religious union (church), dioceses, educational institution for clergy training, monastery, mission, etc.) must be provided.

Prior to the registration of a religious organisation or institution thereof, the RE shall request an opinion from the Ministry of Justice regarding the conformity of the aims and tasks indicated in the articles of association (constitution, statute) of the religious organisation or institution thereof with the law, as well as whether the activities (teachings) of the religious organisation may endanger human rights, the democratic structure of the State, public safety, welfare and morals.

Taking into account the afore-mentioned, it can be concluded that society is granted a possibility to get acquainted with the actual and historical information concerning associations, foundations and religious organisations, which is available in the Registry of Associations and Foundations and the Registry of Religious Organisations and Institutions of the RE.

When registering associations, foundations and religious organisations in the RE, information concerning personal data, registered domicile of the founders of organisation shall be provided and must be confirmed by the signature of these persons. The articles of association (constitution, statute), clearly defining the aim for the establishment of organisation, shall be provided as well.

The requirements to provide upon registration detailed information on founders and aims of association, foundation or religious organisation are essential, since they are also mentioned in the Special Recommendation of the Council of Europe concerning prevention of the terrorism financing risks by means of non-governmental organisations.

According to the information provided by the Lursoft database (Latvian IT company, which provides to its clients access to different registries, including public state registries via Internet connection) as on May 12, 2011, there have been registered:

- 12,865 associations;
- 926 foundations.



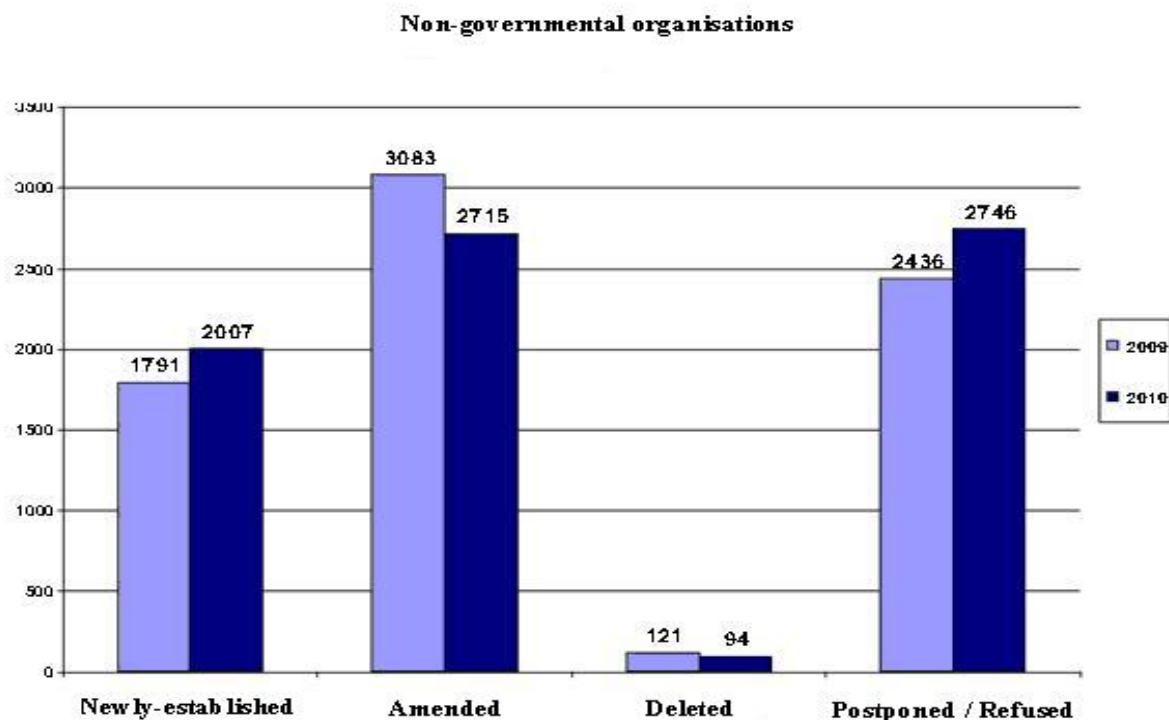
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At the same time, on May 12, 2011, there were registered 1,200 religious organisations.

The following chart provides comparative information concerning non-governmental organisations (excluding religious organisations), which were registered, deleted from the registry, whose registered data were amended or to whom registration was refused in 2009 and 2010.



Although these data contain also the information concerning other non-governmental organisations - trade unions, open society foundations, political parties, corporations (professional association), etc., their number is comparatively low (approximately 5%) from all associations and foundations registered in the RE.

Pursuant to the Latvian law associations, foundations and religious organisations shall organise their accounting to reflect all commercial transactions, as well as all facts or events, which cause changes in the state of the property of the undertaking. Therefore, all requirements set out by the relevant accounting laws concerning organisation and preservation of the source documents, accounting registers, inventory lists, annual account balance sheets and the annexes thereof, accounting organisation documents (chart of accounts, codes, etc.) are binding for all associations, foundations and religious organisations. It is the executive institution of association, foundation or religious organisation which is responsible for organising accountancy therein, which in its turn avails itself of the services of experts – professional accountants. The recording of donations or gifts in the said organisations is important, since it ensures all monetary donations or gifts received in cash or to the bank account, as well as all donations or gifts in a form of movable or immovable property during the accounting year. Therefore, all assets received by associations, foundations and religious organisations shall be reflected in their accounting and supported by the source documents. Such accounting practice facilitates the control over disposed assets for the organisations themselves, as well as for the monitoring institutions.

Every year association, foundation and religious organisation shall prepare the annual account balance sheet. The annual account balance sheet shall provide actual and clear representation of the assets of organisation, their source and financial situation, as well as commercial transactions, incomes and expenditures within the accounting year. In the case of associations, foundations and religious

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organisations their annual account balance sheet shall consist of a balance sheet, profit and loss statement, gift and donation statement and report or annex thereof.

One of the elements of the annual account balance sheet of the associations, foundations and religious organisations is the gift and donation statement, which shall indicate all gifts and donations, received within the accounting year, as well as to provide information about the grantors and contributors. Thus, the tax administration (hereinafter – the SRS) is able to obtain information on every grantor, which in its turn allows to verify whether the grantor's income level corresponds to the donation, and accordingly to evaluate the legality of the asset source.

As of 2010, the associations, foundations and religious organisations shall submit their annual account balance sheets to the SRS only. Previously the annual account balance sheets had to be submitted both to the RE and the SRS. It is possible to submit the annual account balance sheets electronically by means of the SRS Electronic Declaration System, thus ensuring the accuracy of submitted data, since the automatic verification of submitted documents performed by the Electronic Declaration System diminishes the possibility of typewriting and calculation mistakes.

Pursuant to the Latvian law, the SRS shall electronically transmit for the publication to the RE those annual account balance sheets, which have been submitted electronically, or the electronic copies thereof, if the respective documents have been submitted in the paper form (including those, which were received by the SRS since February 24, 2010).

Thus, the information, which has been reflected in the annual account balance sheets of associations, foundations and religious organisations is publicly available for society, since their annual account balance sheets, which have been electronically submitted to the RE, are publicly available for all concerned persons. At the same time, if the annual account balance sheet has not been submitted within the specified period of time, the responsible officials of the organisation may be called to administrative liability and punished pursuant to the Code on the Administrative Offences, i.e. the court may issue a warning or apply a fine not exceeding LVL 300 (EUR 426.86).

If, upon the examination of information contained in the annual account balance sheet, the SRS discovers any suspicious transactions within the period of review on behalf of association, foundation or religious organisation – credits or loans of significant amount of money - or information concerning the source and use of the said assets is not sufficient enough, the SRS within its scope of competence shall conduct additional examination.

Since Latvian associations, foundations and religious organisations shall organise their accounting pursuant to the relevant accounting laws, the requirements concerning preservation of source documents are binding for them as well. According to the said requirements, all source documents, accounting registers, inventory lists, annual account balance sheets, accounting organisation documents (chart of accounts, codes etc.) shall be systemically organised and preserved in the archive of the entity (the archival period shall be no less than 5 years and no longer than 75 years depending on the type of the document).

The annual account balance sheets of associations, foundations and religious organisations shall be preserved in their archives till their reorganisation or termination of their activity. Afterwards they shall be sent to the state archives.

Therefore, even in the case of changes within the membership or executive composition of association, foundation and religious organisation, the new members will be able to acquaint themselves with the information provided in the previous annual account balance sheets of the organisation.

It must be noted that pursuant to the law, Latvian associations, foundations and religious organisations shall declare all transactions in cash exceeding LVL 3,000 (EUR 4,269), as well as all transactions in cash exceeding LVL 10,000 (EUR 14,229) are restricted.

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Thus, it limits the possibility to commit fraudulent transactions and evade payment of taxes, as well as denies the possibility to legalise illegally obtained assets, including so called “envelope wages”.

In addition, the legislative amendments are being drafted, which envisage significant restrictions for legal entities concerning transactions in cash. Pursuant to the said amendments only transactions in cash not exceeding LVL 3,000 (EUR 4,269) will be allowed and the threshold for mandatory declarations of transactions in cash will be lowered to LVL 1,000 (EUR 1,423).

As a significant change in the area of monitoring of associations, foundations and religious organisations must be noted that on October 1, 2004, the Law on Public Benefit Organisations entered into force, which promotes the public benefit activities of the associations, foundations and religious organisations. Pursuant to the said law, the public benefit activity is an activity, which provides a significant benefit to society or a part thereof, especially, if it is directed towards charitable activities, protection of human rights and civil rights, development of civil society, promotion of education, science, culture and health, disease prophylaxis, support for sports, environmental protection, provision of assistance in cases of catastrophes and emergency situations, and raising the social welfare of society, especially for low-income and socially disadvantaged groups of persons. The Law on Public Benefit Organisations also defines the procedure for granting and withdrawal of the public benefit status.

Pursuant to the Law on Public Benefit Organisations, public benefit organisations are entitled to receive tax alleviations specified by relevant laws; persons donating to a public benefit organisation are entitled to receive tax alleviations specified by relevant laws as well.

In addition, it is prohibited for a public benefit organisation to split its property or financial assets among founders, members of board or other executive institutions and their relatives, as well as to use it in a manner, which provides direct or indirect benefit; thus the received property and financial assets shall be used only in accordance with aims established in the articles of associations, constitution or statute.

The afore-mentioned encourages the associations, foundations and religious organisations to receive the status of public benefit organisation, while individuals are willing to provide donations. This ensures the transparency of relevant financial transactions, as well as the use of donations for the aims of public significance.

The following table provides information concerning those public benefit organisations, who have received the status of the public benefit organisation, to whom the status was refused or whose status was revoked during the period from 2005 till 2010.

	2005	2006	2007	2008	2009	2010
Organisations, which have received the status of the public benefit organisation	608	294	170	234	192	268
Organisations, the public benefit organisation status of which was revoked	0	30	52	64	48	41
Organisations, to which have been denied a public benefit organisation status	22	10	11	11	29	22

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As of 2010, the granting of the status of public benefit organisation, supervision of the public benefit organisations, keeping of the Registry of Public Benefit Organisations, as well as ensuring the proper functioning of the Public Benefit Commission has been taken over from the Ministry of Finances by the SRS. These changes were necessary since granting and withdrawal of the public benefit status is related to tax administration, which is within the scope of the competence of the SRS, not to the planning and organisation of tax policy, which is within the scope of the competence of the Ministry of Finances.

The SRS has access to wider information, which is necessary for a more effective administration of the activities of public benefit organisations. In addition, by overtaking these functions a more effective decision making process has been achieved in respect of granting the status of public benefit organisation and supervision thereof, since it is not necessary to request documentation from other institution, and the function of supervision over public benefit organisations is not duplicated.

The Public Benefit Commission (hereinafter – the Commission) is involved in the proceedings, by which the status of public benefit organisation is granted. The Commission is a collegial consultative institution, which issues advisory opinions to the SRS regarding the conformity of associations, foundations or religious organisations to the essence of the public benefit organisations, as well as whether their property and financial assets are disposed pursuant to the law. Each year the Commission, which consists of six appointed state officials and six representatives of non-governmental organisations, examines, evaluates and approves the annual account balance sheets and activity reports from the previous period of review, including the detailed disposition of gifts and donations. Upon examination of received reports (annual account balance sheets, performed public benefit activity reports from the previous period of review, detailed dispositions of gifts and donations, information on tax payments), the Commission evaluates the conformity of the public benefit organisation to the essence of public benefit activity. If the Commission has reasonable doubts concerning conformity of disposition of gifts and donations received by the public benefit organisation to the law, the SRS within its scope of competence shall conduct respective examination to verify whether the registration of received donations and disposition thereof has been conducted pursuant to the requirements of relevant laws and informs the Commission on the results thereof. The decision of the Commission is of recommendatory nature.

The SRS is one of the institutions exercising monitoring and control over the subjects of the Law on the Prevention of Money Laundering and Terrorism Financing. Information provided by the Office for Prevention of Laundering of Proceeds Derived from Criminal Activity regarding the persons suspected of involvement in terrorist activities is regularly published on the SRS intranet and, in the case of necessity, it is possible to examine, whether the donator has been included in the provided information.

It must be noted that upon the results of the SRS tax control measures, there has been no case when a donator to associations, foundations or political organisations (parties) was also included in the information provided by the Office for Prevention of Laundering of Proceeds Derived from Criminal Activity concerning persons suspected of involvement in terrorist activities.



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## The abuse of non-profit organizations to finance terrorism

*Romanian Intelligence Service*

### The situation in Romania

In Romania, the cases of suspicion of terrorism financing were exceptions. There is no network operating in our country that is designed to obtain, raise, or send funds abroad to the benefit of terrorist entities.

With regards to the engagement of non-governmental organizations (NGOs) in financing terrorism, or the potential connection between NGOs and terrorism, we note that, to date, NGOs in Romania have not been engaged in supporting terrorist organizations.

Generally, however, we can consider a number of aspects which provide an overall image of the interaction of the NGOs in Romania with terrorist activities:

- Individuals within NGOs involved in activities from which terrorist elements or entities benefit financially may be implicated in the transaction process without knowing the purpose, connections, or final destination of the transaction in question.
- Even in cases where terrorist entities exploit opportunities to access the physical infrastructure (premises, locations used for meeting), human asset (membership), or online presence (website, forums) of existing NGOs, this fact alone does not certify a concrete link between the NGO and the beneficiary terrorist entity.
- NGO's in Romania avoid being associated in any way with terrorist activity because this association would endanger their position and status in our country.

### The international situation

#### *Ways of raising funds through NGOs*

International terrorist groups need funds to attract, support and keep their followers, as well as to ensure the loyalty of other groups sharing the same objectives.

#### Sources of financing

International investigations of individuals suspected of terrorism demonstrate their engagement in money transfer operations through alternative systems that are available globally.

Such systems do not require opening a bank account, as they are based on compensation. Furthermore, they frequently use methods involving transfers to multiple locations, which makes it difficult for authorities to trace the funds and their destination.

In brief, the funding of terrorist activity may be achieved from **government sources** (state-sponsored terrorism) or from **private sources** (such as natural or legal persons, charities, and non-governmental organizations). [1]

Terrorist financiers can exploit certain financial channels in vulnerable domains, such as charities and NGOs, since these entities have a structure that is designed to ensure anonymity. Most of the time, donors do not know the final beneficiaries of their donations.

#### Funding methods through NGOs

- A - **multi-jurisdictional structures** of entities and corporative trusts;
- B - **non-financial mediators / professionals**;
- C - **cover entities** (natural and legal persons, including companies). [2]

After examining terrorist-related financial activity, experts at the Financial Action Task Force (FATF)

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concluded that, in order to launder money, terrorists and support organizations generally use the same methods as criminal groups. Funds can be generated by legal or criminal activities; in the latter case, terrorism can be funded with “black money” which undergoes money laundering.

The terrorist financing cases we identified demonstrated exploitation of the following methods:

- **Large cash deposits** (sometimes made by third parties) into the accounts of non profit organizations [3]. The deposits are mostly made as donations, following the actions carried out on behalf of charities.
- **Large number of deposits** into personal accounts [4]. For such deposits, a frequent practice is **cash smuggling**, both through couriers and cash cargos. Methods include the use of structured deposits into or withdrawals from bank accounts, the acquisition of various types of monetary instruments (traveler’s checks, bank checks, money orders), debit or credit cards, wire transfers and SWIFT transfers.[5]

In both cases, there are factors that prevent the detection and tracing of the destination of the funds in question, as it is difficult to associate a specific financial transaction to a terrorist activity.

#### ***Factors favoring the extension of the financial networks of terrorist entities, through NGOs***

Charities have a number of features that may be exploited by terrorist entities in order to fund their activities.

Due to the nature of their activities, such organizations enjoy the public’s trust and have access to considerable sources of finance. Their activity frequently entails the handling, almost exclusively, of cash money, and they usually have branches in many states, thus facilitating a number of international transactions.

Moreover, they are not subject to the strict rules that are applicable to business organizations with regards to the records of funds and financial operations.

The exploitation of the NGOs for terrorist purposes is also favored by the fact that conducting charitable activities can be considered a religious duty. Islam in particular has been exploited by terrorists who use deviant interpretations of religious dogmas to justify indiscriminate violence.

With regard to terrorism exploiting Islamic dogmas, the **following factors** have contributed to blurring the picture, making it difficult for donors, state authorities and the public at large to distinguish between legitimate religious endeavors and terrorist activities:

- The **existence of (intentional) ideological and terminological confusion** between the declared objectives of Jihadist organizations (the re-establishment of the Caliphate, an Islamic transnational form of government) and of some Islamic NGOs (e.g. the establishment of a “universal Islam” – in the case of the Federation of Islamic Organizations of Europe - FIOE)[6];
- **The setting up of NGOs by people with radical Islamic views**, in conflict areas marked by extremist violence;
- **The involvement of some Islamic countries** in setting up and financing charitable organizations, in order to use them for their own **political purposes**.
- **The establishment of charity organizations** in Western countries **by members of the immigrant communities**, some of them sharing Islamist radical views.
- **Terrorist organizations themselves can carry out charitable actions** to mobilize social support.

#### ***Current trends***

New trends within international terrorism have emerged since the beginning of the global economic crisis. These trends have mainly been directed towards increased cooperation with transnational organized

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#### ***The main challenges in the implementation of SR VIII***

The main challenges in implementing SR VIII are related to the efficiency of the methods used by the terrorism financing networks.

There have been instances of terrorists abusing traditional religious financial networks. Examples include abuses of “**the Islamic banking system**”, which provides loans without real guarantees, in exchange of some investments in the bank capital. This procedure is known as “loan back”.

Some Islamic banking institutions operate on the basis of the Zakat system. After the initial transaction has concluded, the percentage representing the Zakat no longer appears in financial documents. As a result, this money leaves no trail and could be used for financing Islamist terrorist groups.

Terrorists also resort to the **international banking system**, using a method called “**smurfing**”. This method involves opening accounts in which small sums of money are deposited in order to avoid verification and arousing the suspicion of authorities. [8]

“**Hawala**” represents another financing and money transfer system. It is an **informal system**, operating on the basis of trust among the business partners.

To a lesser extent, the Al-Qaeda network uses **offshore** companies to cover financial operations, due to the fact that law enforcement agencies have only a few instruments with which to verify these companies.

By means of certain **cover building and real-estate companies**, terrorist organizations conducted illegal operations, such as weapons trafficking and electronic card fraud and document forgery, including cards and identity papers for stolen vehicles.

Some companies are used as umbrella organizations for facilitating Al-Qaeda operations in Europe, using false contracts signed by businessmen linked to the network.

To an even lesser extent, casinos were also used to perform suspicious financial transactions for terrorist financing. [9]

#### **End Notes**

[1] <http://cccec.gov.md/.../RAPORT%202009.08B2C7AE64AA43C98A8417D9EA95C263.pdf>

[2] <http://www.fintrac.gc.ca/publications/typologies/2009-05-01-eng.asp>

[3] <http://www.fintrac.gc.ca/publications/typologies/2009-05-01-eng.asp>

[4] <http://www.fintrac.gc.ca/publications/typologies/2009-05-01-eng.asp>

[5] [http://www.inm-lex.ro/fisiere/pag\\_34/det\\_415/1380.doc](http://www.inm-lex.ro/fisiere/pag_34/det_415/1380.doc)

[6] <http://www.nefafoundation.org/miscellaneous/FeaturedDocs/nefafioreport1008.pdf>

[8] <http://www.investigativeproject.org/documents/testimony/22.pdf>

[9] <http://www.fintrac.gc.ca/publications/typologies/2009-05-01-eng.asp>

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## The supervision of foundations in Switzerland

*Nicole Anthonioz, Foundations Supervising Authority, Swiss Federal Department of Home Affairs*

### Legal form

Swiss law provides specific legal form for non-profit organizations. In practice, foundations and associations are the most commonly used legal vehicles.

Associations, the primary function of which is to facilitate collective activities mainly in favour to their members, are not submitted to an enhanced public supervision, especially since their activities are on the whole limited to Swiss territory.

Foundations, on the other hand, come under state supervision by virtue of Articles 80 to 89 of the Swiss Civil Code (CC). Primary responsibility for supervising foundations operating nationally or internationally rests with the Federal Government (Federal Department of Home Affairs), though a significant number of foundations whose operations are restricted to the territory of a particular canton come under the supervision of the cantons. As at 31 December 2010, the Federal Government had assumed responsibility for supervising 3,432 foundations (with national and international remits).

### Supervision (84 CC)

Before placing a foundation under supervision, the supervisory authority checks the source of the initial capital and makes sure that the members of its board are entered in the relevant Commercial Register.

It is the duty of the supervisory authority to ensure that the assets are effectively used for the purpose stated in the foundation's statutes (Art. 84 CC).

With this in mind, each year the foundation is required to provide the supervisory authority with various documents, in particular a report of its activities, the annual accounts, the report of an approved firm of auditors, and the minutes of the board meeting approving the annual accounts.

After examining all these documents, if it has any doubts regarding the sources or the beneficiaries of donations, the supervisory authority will ask the foundation for additional information and supporting documentation.

The supervisory authority can apply a whole range of sanctions: a call to order (the mildest measure), directives, execution by substitution (acting instead of the board), reporting to the law enforcement authorities (and freezing of bank accounts), removal of the foundation bodies, or even the dissolution of the foundation.

The federal supervisory authority also acts as a complaints body if appeals or complaints are made to it by third parties regarding the legality of a foundation's operations or the conduct of its statutory bodies.

Finally, since 1 January 2008, a foundation's auditors are obliged to provide directly the supervisory authority with a copy of their audit report and of all important communications between them and the foundation (Art. 83c CC). This enables the supervisory authority to react more quickly in problematic situations.

### Other means of (indirect) supervision

#### **Commercial Register**

All foundations must be entered in the relevant Commercial Register ([www.zefix.ch](http://www.zefix.ch)).

Since 1 January 2008, moreover, all members of the board – and not just persons with signatory rights – must be likewise registered. This enhances transparency where the composition of the statutory bodies is concerned.



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#### ***Financial establishments***

When a foundation is set up, and subsequently when donations are received or paid out, the vast majority of financial transactions pass through a bank account. The application of banking regulation provisions, the rules for identifying clients (know your customer), the record keeping, etc., if needed STRs (suspicion transaction reporting) is therefore another important factor in monitoring the financing of foundations.

#### ***Tax authorities***

When examining an application for tax exemption, the tax authority will also carry out a check on a foundation's financial circumstances and ensure that the conditions required for tax exemption, from which the charitable sector may benefit, are effectively met. If there is any doubt, the tax exemption will not be granted.

In cases where a non-profit organization has been misused for the purposes of funding terrorism, the tax authority can report the suspicions to the law enforcement agencies.

#### ***Law enforcement agencies***

As part of their functions, law enforcement agencies ensure that the charitable sector is not being used for illegal purposes. The measures they can take include freezing bank accounts, conducting criminal investigations and imposing sentences.

#### ***Private watchdogs***

An important supervisory function is also performed by private watchdogs. The most important of these, in Switzerland, is the ZEWO Foundation ([www.zewo.ch](http://www.zewo.ch)), which has introduced a quality label attesting that donations collected by state-approved organizations are used in a targeted, effective and cost-efficient way. It guarantees the integrity of such organizations with regard to their fund-raising and internal and external communication, and transparency in the conduct of their activities and accounting. Approximately 500 of Switzerland's most important charitable organizations are accredited by ZEWO. The ZEWO Foundation is a founding member of the International Committee on Fund-raising Organizations (ICFO). It also maintains close contact with organizations all round the world which perform similar functions in their own countries.

Other groupings, such as SwissFoundations, promote and support transparency and professionalism in the voluntary sector. In 2005, SwissFoundations published the Swiss Foundation Code, a detailed guide to assist foundations in their work.

### **Risks and challenges associated with the financing of terrorism and regulatory issues**

- Abuse of the legitimacy accorded by foundation status
- Ensuring that the initial capital and the subsequent donations are legitimate
- Diversion of activities from the stated purpose

#### ***Foundation status***

When a foundation is constituted, if there are suspicions regarding the identity of the founders, the supervisory authority may request that an investigation be conducted. The supervisory authority also occasionally receives denunciations from private individuals arising from an entry in the Commercial Register. The supervisory authority may at any time take the decision to suspend all of a foundation's activities or dissolve it. If a foundation is no longer entered in the Commercial Register, it no longer has any legitimacy.

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#### ***Financial flows controls***

Assets pass usually through financial institutions when the initial capital and subsequent donations are paid in, in the course of a foundation's operational activity, and in the event of its dissolution.

The financial intermediaries have then to perform the due-diligence required by the Federal Law of 10 October 1997 concerning efforts to combat money-laundering and the financing of terrorism in the financial sector (Federal Act on Combating Money Laundering – LBA/GwG), including for example reporting STRs if necessary.

#### ***Diversion of activities from the stated purpose***

The danger of the purpose of a foundation being diverted is limited by examination of its annual reports by the supervisory authority, the external monitoring of projects put in place by some foundations. In practice, denunciations made to the supervisory authority by third parties are an important factor. In addition, we request sometimes our embassies to make some controls.

#### ***Actual cases***

The supervisory authority is aware of some cases in which terrorist groups extorted money from nationals who had sought refuge in Switzerland, then used the money to buy weapons. Criminal proceedings are undertaken and the bank accounts frozen.

In another case, the suspicious origin of a foundation's funds led to it being reported to the law enforcement agencies, its activities being suspended, and the foundation itself dissolved.

## **Conclusion**

For several years, the Swiss authorities have been taking steps to make people more aware of the risks to which the sector is exposed, and to improve the transparency of non-profit organizations. In particular, in line with the recommendations of the FATF, Switzerland has introduced measures to improve its existing arrangements, including revising the Federal Law concerning efforts to combat money-laundering and the financing of terrorism in the financial sector (Federal Act on Combating Money Laundering – LBA/GwG), and strengthening due-diligence obligations and financial market structures.

Also of significance is the high level of cooperation between the various tax authorities and law enforcement agencies, at both federal and cantonal levels.

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### The United Kingdom’s approach to dealing with concerns about the terrorist abuse of charities

*Michelle Russell, Head of Compliance at the Charity Commission for England and Wales, responsible for the implementation of the Commission’s Counter Terrorism Strategy and all the Commission’s investigations and other work dealing with allegations of terrorist abuse of charities.*

Terrorism is a serious and continuing threat to societies across the world. Terrorists look to every part of society and across international boundaries in their search for vulnerable organisations or situations which they can exploit for their own ends. As one vulnerable area is secured against exploitation terrorists are quick to seek other routes and methods.

Sadly, charities are no exception. It is well debated internationally that non-governmental organisations (NGOs), charities and the not for profit sector are vulnerable to abuse for terrorist purposes. It is recognized that governments must therefore ensure their sector is as well protected as possible. It is essential that they do enough to both prevent and disrupt terrorist abuse and take effective action when incidents of abuse occur. Like many of its partners in Europe and elsewhere, the United Kingdom (UK) government is clear that the abuse of charities for terrorist purposes is completely unacceptable.

At the same time, it is also recognised internationally, including by the Financial Action Task Force (FATF), that charities make a vital contribution to society. They are a crucial manifestation of citizens’ rights to freedom of association. Governments should therefore ensure the steps they take to combat terrorist abuse do not disrupt or discourage legitimate charitable activities. Rather, they should promote transparency in the charity sector and engender confidence among the donor community and the general public that charitable funds reach the intended, legitimate beneficiaries. It is therefore important for governments to ensure that the legal framework and their approach to NGO regulation enable charities to flourish and carry out their vital legitimate work.

#### The UK Legal Framework

The UK’s legislative framework for preventing and pursuing terrorists and those supporting terrorist organisations is quite sophisticated. We have a legislative framework within criminal law dealing specifically with terrorism [1]. In addition, some terrorist related activities may be dealt with under separate pieces of criminal legislation, for example that dealing with fraud, theft, public order, drugs, forgery or counterfeiting. Incidents of such abuse involving a charity or those responsible for managing charities - known as “charity trustees” in the UK - would be dealt with under those regimes. In that sense, the charity sector is dealt with no differently to other sectors of the economy or society.

In addition, the UK’s financial sanctions regime more particularly helps to suppress the financing of terrorism. The UK’s Foreign and Commonwealth Office (FCO) is responsible for overall policy on international sanctions including the scope and content of international sanction regimes. HM Treasury, meanwhile, is responsible for the implementation and administration of international financial sanctions in the UK, for domestic designation [2] and for licensing exemptions to financial sanctions. This is dealt with by a dedicated Asset Freezing Unit within the Treasury, which publishes a consolidated list of asset freeze targets designated by the United Nations, European Union and UK under legislation relating to current financial sanctions regimes on its website [\[LINK\]](#).

These criminal and financial sanctions regimes are supplemented by the more general charity law framework [3] and regulatory remit of the Charity Commission, the regulator of charities subject to the jurisdiction of England and Wales [4]. Criminal and financial sanctions regimes generally look at past or present conduct and events. The Commission, however, can step in to resolve the underlying problems that helped make the charity vulnerable to such criminality and to ensure by the use of regulatory powers if necessary, that the charity’s other assets are redirected and only used for legitimate charitable activities.

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The police and law enforcement agencies will always have primacy in investigating and prosecuting any suspected terrorist activity under criminal law, whether that is attack planning, financing or other support. More specifically, the UK's general approach to dealing with the risk of abuse of charities for terrorist purposes is to target those responsible for that abuse– the terrorists and their supporters– without, if possible, disrupting any legitimate charitable activity. Where possible, this includes targeting regulatory action against those individuals and restoring a legitimate or disrupted charity to the control of responsible individuals who will run it lawfully and properly.

### Charities' Vulnerability to Abuse

In England and Wales there are over 180,000 registered charities [5]. The number of incidents and allegations about charities' involvement or connection with terrorism, directly or indirectly, is small in number compared to the size of the sector [6]. However, terrorist abuse is not acceptable, in the same way that fraud, corruption or the theft of charitable funds is not acceptable. A single event or allegation has the potential to do serious damage to both that charity and levels of public trust and confidence in the wider charitable sector.

It can be charities' strengths that make them so vulnerable to abuse. The good reputation of charities, the fact that they are so highly valued in society and enjoy high levels of public trust, their international reach – including their ability to reach hard to access or vulnerable communities – and the complex and frequent nature of their financial transactions and humanitarian activities, can provide an opening for terrorists and cover for illegal activity. While the risk of terrorist abuse may increase if a charity works in politically unstable or high risk regions, problems can occur even within relatively well regulated environments, such as that found within the UK, especially given the diverse nature of the charitable sector.

Charities can be abused in a variety of ways, including through the exploitation or misuse of a charity's funding, assets, name or status or through the establishment of a sham charity. Abuse may also include inappropriate expressions of support for a proscribed organisation by a trustee or others closely involved in a charity. Terrorism risks may arise when funds are raised and donations received or where grant funding is disbursed and in the provision of services and other charitable activity. The risks take a number of forms, including operational, financial, reputational and external, as well as compliance with the law and regulations.

#### ***Types of Abuse***

Charity funding – Funds may be raised in the name of a charity or for charitable purposes, which are then used by the fundraisers for supporting terrorist purposes, with or without the knowledge of the charity. Where a charity's funds are being moved from one place to another they could be diverted before reaching their intended recipients. This risk is increased if the charity's financial controls are weak.

Use of charity assets – Charity vehicles might be used to transport people, cash, weapons or terrorist propaganda, or charity premises used to store them or arrange distribution. Individuals supporting terrorist activity may claim to work for a charity and trade on its good name and legitimacy in order to gain access to a region or community.

Use of a charity's name and status – Terrorist activities may be hidden by or take place alongside additional, and otherwise legitimate, charitable activities. A charity may give financial or other support to an organisation or partner that provides legitimate aid and relief. However, that organisation or partner may also support or carry out terrorist activities.

Abuse from within a charity – Those within a charity may abuse their position within the charity to divert funds and use the name of charity itself for illegal purposes.

Sham charities – Terrorists may try to set up an organisation as a sham, promoted as charitable but whose sole purpose is really to raise funds or use its facilities or name to promote or coordinate inappropriate and unlawful activities.



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### The Challenge for Governments: stopping abuse but allowing humanitarian aid to get through to where it is needed

Greater awareness has been achieved internationally through FATF Special Recommendation VIII: Non-Profit Organisations but the implementation of this in each country is not consistent and there are practical challenges for some countries in doing so. One key challenge is how do we ensure that we as government take robust and necessary steps to stop terrorism and protect the charitable sector from such abuse but do not stop legitimate aid and charitable activity and do not penalise the very people in society they are providing crucial help to.

Charitable donors are entitled to have confidence that their money is going to the intended cause and destination. But over regulating and restricting the operations of charities is not the solution. Putting obstacles in the criminals' way by seizing funds and closing down charities is one option, some would say robust and fail safe, but we know criminals find other ways around obstacles - they open up new organisations to take over or, even worse, their activities go under ground into unregulated sectors.

Finding an approach that works for the sector, the government and the public and that strikes this balance is possible. It is possible to take action and disrupt and stifle terrorist abuse whilst neither over regulating the sector, nor preventing freedom of association, nor suppressing good works.

### The UK Regulatory Approach – the Charity Regulator's role

In 2003 the UK published its national strategy for dealing with terrorism, which is embodied in the work of every government department and agency that deals with terrorism issues. It is called CONTEST ([LINK](#)) and has four key strands:

<b>PURSUE</b>	to stop terrorist attacks
<b>PREVENT</b>	to stop people becoming terrorists or supporting violent extremism
<b>PROTECT</b>	to strengthen our protection against terrorist attack
<b>PREPARE</b>	where an attack cannot be stopped, to mitigate its impact

It is regularly refreshed and, over recent months the PREVENT strand has been formally reviewed, the results of which will soon be on the Home Office's website.

In addition, following the UK government's more detailed review in 2007 of the vulnerability of the UK charity sector to terrorist abuse, the **Charity Commission developed and published its own Counter-Terrorism Strategy** which set the regulator's approach for tackling the threat of terrorist abuse to the charitable sector with four aims:

<u>Awareness</u>	raising awareness in the sector to build on charities' existing safeguards
<u>Oversight</u>	proactive monitoring of the sector, analysing trends and profiling risks and vulnerabilities
<u>Co-operation</u>	strengthening partnerships with government regulators and enforcement agencies
<u>Intervention</u>	dealing effectively and robustly when abuse, or the risk of abuse, is apparent

This strategy was developed in line with wider national and international developments, taking on board the FATF recommendations in SR VIII, which specifically tasks member countries with reviewing their domestic laws and regulations relating to non-profit organisations. It also proposes that countries ensure these organisations cannot be misused by:

- terrorist organisations posing as legitimate entities;
- exploitation of legitimate entities as channels for terrorist financing; and
- diversion of funds intended for legitimate purposes to terrorist organisations.

It is important to point out, however, that while the Commission pays particular attention to preventing and dealing with issues relating to terrorism, this work and the way in which we tackle the risk of terrorist abuse in charities, falls squarely within the Commission's overall approach to regulation. We are uniquely

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placed to deal with all kinds of abuse of charities where it does occur, collaborating with other regulators, law enforcement agencies and other government departments, and supporting trustees to protect their charities. This three way partnership between us as regulator, other government agencies and the charity sector itself is vital. Crucially in our view, effective regulation involves putting a strong emphasis on giving support and guidance to charities to prevent problems and abuse occurring in the first place as well as ensuring we act swiftly and effectively when there is evidence or serious suspicions of terrorist abuse or support involving charities.

If there are any concerns that a charity is being, or has been, abused for terrorist purposes, three key principles underpin the Commission’s handling of the concerns:

- we will not register an organisation that has support of terrorism explicitly *or implicitly* as one of its purposes;
- the use of a charity’s assets for support of terrorist activity is not a proper use of those assets; and
- links between a charity and terrorist activity corrode public confidence in the integrity of charity.

### Proportionality

The Commission applies a risk-based and proportionate approach to regulation. We have developed a risk and proportionality framework for our compliance work so when we do intervene and take action, we do so in a targeted way that represents a proportionate response to the seriousness of the issue. We also take into account the impact of not taking action.

What is clear is that all charity trustees need to be vigilant about the potential risks from terrorism. However, because of the enormous diversity of the sector, the risks will be different from charity to charity. What an individual charity will need to do to protect itself from harm will therefore vary. For large numbers of charities there may be few risks. Other charities may experience much higher risks, whether working solely in the UK or operating internationally when carrying out their activities themselves or in partnership with others, and depending on the particular type of work they engage in. Charities and NGOs often face great challenges when working in regions where terrorist are known to operate and where they may have control over areas in which there are people in dire humanitarian need. This is why a risk-based, proportionate and targeted approach is so important; “one size fits all” will not work.

Proportionality does not mean taking a soft handed approach to dealing with well-supported suspicions of abuse or non compliance. However, it does mean focusing regulatory action where it can make a difference and putting more responsibility on the trustees of charities to ensure they protect their charity from harm in the first place.

### What role do charities themselves have to play in preventing abuse?

It is important to take targeted and swift executive action in dealing with abuse when it takes place. Equally important is to prevent abuse happening in the first place and ensuring that the sector do enough themselves to safeguard charities from this.

The Commission’s experience, from dealing with incidents of suspected and actual abuse, is that charities and NGOs that are transparent about what they do and who with, and which have strong governance and financial management arrangements in place will be better protected against all abuse, not just from terrorists and their supporters. This includes implementing good general risk management policies and procedures and having meaningful and effective oversight of their activities. It is in the sector’s own interest that they do this themselves and that we encourage and support them in doing so.

One of our key messages is that it is not the regulator’s job to safeguard all 180,000 charities from abuse; it is responsibility of those charities’ trustees as part of their existing legal duties. In order to discharge their legal duties and responsibilities under charity law, trustees must take appropriate steps to prevent abuse of their charity. Charity trustees must ensure they adequately assess the nature and extent of the risk of their charity coming into close contact with terrorist organisations. The greater the risk, the more charity trustees need to do.

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The Commission expects trustees to be vigilant to ensure that a charity’s premises, assets, staff, volunteers or other resources cannot be used for activities that may, or appear to, support or condone terrorist activities. In addition, they should ensure that proper and adequate procedures are put in place and properly implemented to prevent terrorist organisations taking advantage of a charity’s status, reputation, facilities or assets. It sounds simple, but trustees must also ensure that they report a belief or suspicion of abuse and must act responsibly themselves when dealing with concerns raised. They cannot just dismiss those concerns or not take them seriously.

To help trustees understand their legal duties and to give them some practical advice and tools to put in place measures to protect their charities, the Commission has produced a toolkit of guidance and advice. One important feature of this toolkit, is that we worked not just with other government agencies, but also with the sector itself to include case studies and practical tools some charities already use. The toolkit has been published on our website so any charity can access it. It has four chapters, dealing with:

- Charities and terrorism ([LINK](#))
- Due diligence, monitoring and verification of the end use of funds ([LINK](#))
- Fraud and financial crime ([LINK](#))
- Holding, transferring and receiving funds safely

The proportionality aspect referred to above also applies to the more detailed requirements for trustees. For example, charity trustees in the UK are required to act in the best interests of the charity and must use charity funds only for legitimate purposes. In practice, this includes carrying out proper due diligence checks, and monitoring and verifying the end use of funds. The detail of the checks and due diligence required in each case and for different charities will depend on the extent of the risks evident in the circumstances. The level of checks and necessary procedures will be affected by the nature of the activities they carry out and area in which they operate. Proportionality does not mean that trustees can choose which duties to comply with – they must comply with them all. But they can apply a risk based approach to deciding what action is reasonable or proportionate to take to ensure they do comply.

### Summary

Hopefully, all of the international community would agree that the abuse of charities for terrorist purposes is completely unacceptable. Our experience suggests that it is vital that the government, the regulator, if there is one, and the sector itself work together in partnership to ensure that charities are robustly protected from the abuse in the first place but also so the legal and regulatory framework allows the important work of charities and support they provide to legitimate beneficiaries to continue.

Money underpins all terrorist activity, without it there can be no training, recruitment, facilitation or support for terrorist groups. The disruption of terrorist financing activity is a key element of the UK Government’s overall fight against terrorism, involving close working across government between the intelligence and law enforcement agencies and the financial sector. Charities and voluntary organisations themselves play an important role in ensuring that the funds they collect are not diverted to terrorist organisations. This is not an easy role but one that it crucially important and which national governments and international communities must help them with.

### End Notes

- [1] Including the Terrorism Act 2000, the Anti-Terrorism, Crime and Security Act 2001, the Prevention of Terrorism Act 2005, the Terrorism Act 2006 and the Counter-Terrorism Act 2008
- [2] under the Terrorist Asset-Freezing (Temporary Provisions) Act 2010
- [3] Charities Acts 1992, 1993 and 2006 as well as common law duties and responsibilities which apply to trustees of charities
- [4] Similar regulatory bodies now exist in Scotland (Office of the Scottish Charity Regulator) and for Northern Ireland (The Charity Commission for Northern Ireland)
- [5] As part of a proportionate regime, not all charities must be registered under law, although many choose to do so voluntarily anyway. Charities registered in England and Wales can be seen in a public Register of Charities on the Commission’s [website](#)
- [6] *Review of Safeguards to Protect the Charitable Sector, England and Wales, From Terrorist Abuse* Home Office and HM Treasury 2007. See also the Commission’s reporting of its terrorism work in publications *Charities Back on Track 2009 and 2010*

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## Introduction to the NGO Sector and Regulation Review Tool Designed by the International Programme of the Charity Commission for England and Wales

### What is the NGO Sector and Regulation Review Tool?

Recent years have seen unprecedented interest in the issue of NGO legislation and regulation. There are many reasons: the unprecedented growth of the global NGO sector; the increasing sophistication of the sector; the growth of multi-national NGOs; a more complex relationship with government as partner, service provider, critic and rival; and a focus on the sector as a potential weak-spot in global anti money laundering and counter terrorist financing efforts, as illustrated by Special Recommendation VIII of the Financial Action Task Force (FATF SRVIII).

These factors put pressure on both governments and NGOs to identify the risks to the NGO sector. The NGO Sector and Regulation Review Tool (the ‘Tool’) has been designed to help identify the risks that affect the sector in a particular country and assess how effective the regulatory framework is in mitigating that risk.

### Why is effective regulation important?

While both title and meaning differ in many parts of the world, many people understand the NGO sector to be one that exists for the benefit of others; a sector driven not just by the desire to increase profits, but to improve life for ordinary people.

However, this is just the first of numerous benefits that NGOs bring. Studies of the global NGO sector show that a vibrant sector has significant economic and political value to a country. A strong, well regulated NGO sector provides a most important and complimentary role alongside government in achieving development goals and improving the lives of ordinary people.

Furthermore, the NGO sector is governed by civil norms which drive their desire to help society – respect, reciprocity, tolerance, inclusion. These norms and values increase the likelihood of open discourse, citizen engagement and informed dialogue within society. NGOs therefore provide the best possible forum for identifying, expressing and defusing some of the most destructive forces within society.

Effective regulation is crucial to maximising the positive contribution that NGOs make. Effective regulation is enabling, providing space for the sector and allowing it to work at maximum potential. It creates a healthy, accountable and independent NGO sector with an agreed set of norms and behaviours. It formalises the relationship between Government, society and the NGO sector giving each a clear set of rules and increased information about the other. In establishing a level playing field, NGOs have a far clearer idea of the space they have to work in, meaning they can seize opportunities in all areas, maximise their potential and the contribution they have to improving society. As a consequence, well regulated NGOs benefit from improved governance and confidence in their sector.

In contrast, poor regulation restricts the NGO sector’s potential. Regulation that does not allow NGOs to work flexibly and respond rapidly to situations may stop vital work - NGOs often provide crucial assistance to people in very challenging situations. Most importantly, where countries have burdensome and/or unclear rules for NGOs, it is far more likely that charitable money will be driven underground and given to unknown and unseen organisations. In other words, introducing measures which overly restrict NGO activities is counter-productive to increasing transparency and accountability.

### How does the Tool work?

The Tool takes a systematic approach that comprises four parts.

**Part One: Sector Survey** profiles the sector and the risks that affect it. It provides a framework for



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identifying and recording the key information on the NGO sector. It also identifies areas where no information is available and further work may be needed. The information gathered helps inform the subsequent assessment and review process.

**Part Two: Assessment of the Regulatory Framework** is an assessment of the effectiveness of the current regulatory framework. It breaks down regulation into eighteen areas. Indicators are given for each objective to help identify them. The objectives are then tested against seven key standards of effective regulation.

**Part Three: Analysis and Recommendations** prompts consideration of the broad strategic issues which may be impacting upon the effectiveness of the sector and the regulatory framework. It then asks the LAT to make recommendations for improvements.

**Part Four: Final Report** completes the assessment by reporting key information, including summaries of the survey and assessment, recommendations for the future and an executive summary.

The Tool has been designed to be applicable in any country, regardless of size, legal system or level of development. However, different countries and different assessors will use the Tool in different ways. For this reason it is not intended that the Tool should be used to compare one country's results with another. Instead, the aim of the Tool is to provide countries which want to assess their NGO sector with the framework and methodology to do so.

A further outcome of the assessment exercise is the prompting of debate about the role and nature of the sector and the risks it faces, and the highlighting of key issues and some potential solutions, which can then be taken forward to inform future actions to improve the strength of the sector within the local context.

### Who implements the Tool?

The Tool is implemented by a Local Assessment Team (LAT). This body will have responsibility for ensuring that the Tool is effectively implemented and that, as far as possible, the recommendations which arise from its findings are brought to the attention of national level policy and law makers.

The LAT is made up of equal numbers of government and NGO representatives. Government representatives should represent the key agencies responsible for NGO regulation. NGO representatives should represent the main different types of NGO within that country's sector.

The constitution of the LAT is the single most important factor in the successful implementation of the Tool.

The intention is that the Tool can be independently implemented by the LAT. However, in most cases prior specialist training or external assistance from experienced assessors will help improve the quality of the result. This support can be provided by trained implementers recommended by the tool designers.

### Will implementing this Tool ensure compliance with FATF Special Recommendation VIII?

The FATF Special Recommendations apply to all governments that are members of the Financial Action Task Force (FATF) or FATF-Style Regional Bodies (FSRBs). Special Recommendation VIII and the associated Best Practices Paper and Interpretative Note require governments to:

- review the adequacy of laws and regulations in relation to NGOs;
- know the characteristics of their NGO sector;
- implement measures to prevent:
  - terrorist organisations posing as NGOs;
  - escape from asset freezing measures; and
  - NGO funds being diverted to terrorist organisations.

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This Tool deals with many of the recommendations and requirements of FATF Special Recommendation VIII. However, it has not been designed for the specific purpose of ensuring compliance with that recommendation. Whilst this Tool may assist in this process, government agencies responsible for ensuring compliance with SRVIII should refer directly to FATF or the relevant FSRB.

#### Who produced the Tool?

The NGO Assessment Tool has been designed by the International Programme of the Charity Commission for England and Wales. The Charity Commission was founded in 1853 and is the independent government regulator of NGOs ('charities') in England and Wales. The International Programme was established in 2004 to help create a healthy, accountable and independent NGO sector in countries worldwide through the development of effective and locally relevant regulation.

This Tool was developed with the assistance of an advisory group made up of expert representatives from the NGO, government, donor and inter-governmental communities. Financial support for the Tool was received from the UK Foreign and Commonwealth Office, the International Monetary Fund and the World Bank.

#### Is the NGO Sector Assessment Tool free to use?

The Tool is the copyrighted property of the International Programme of the Charity Commission for England and Wales. The Charity Commission does not charge for the use of the Tool. If you wish to use the Tool in your country, please contact the International Programme via the website ([www.NGOregnet.org](http://www.NGOregnet.org)).

Please note that the Charity Commission retains the right to restrict or withdraw the use of the Tool for any reason.

#### What restrictions are there on the use of the Tool or the results of an assessment?

As stated above, the Tool is the copyrighted property of the International Programme of the Charity Commission for England and Wales. Whilst the Charity Commission does not charge for the use of the Tool, it can only be used with the written permission of the Charity Commission and the Commission retains the right to restrict or withdraw the use of the Tool at any time or for any reason.

Whilst the format of the Tool remains the property of the Charity Commission, the results are the property of the LAT and the agencies that constitute it. The LAT has the exclusive right to decide on the distribution or publication of the final report. If publishing, the copyright of the Charity Commission over the Tool must be recognised and the Tool should not be presented in a way that is out of context or misleading. It also a condition of use that the Charity Commission is provided with a copy of the full final report. This will be provided in confidence and will not be shared with any person outside of the International Programme of the Charity Commission except with express permission.

#### How much will it cost to implement the Tool? How long will it take?

In short, it will vary. Key variables are the size of the country, the costs in that country, the complexity of the regulatory framework, the size of the NGO sector, the availability and accuracy of information and the degree of accuracy required.

Pilots of the tool to date suggest that for large countries, a full assessment requires the support of two-three full-time staff employed for six-twelve months. Less detailed assessment and/or smaller countries will require considerably less resources.

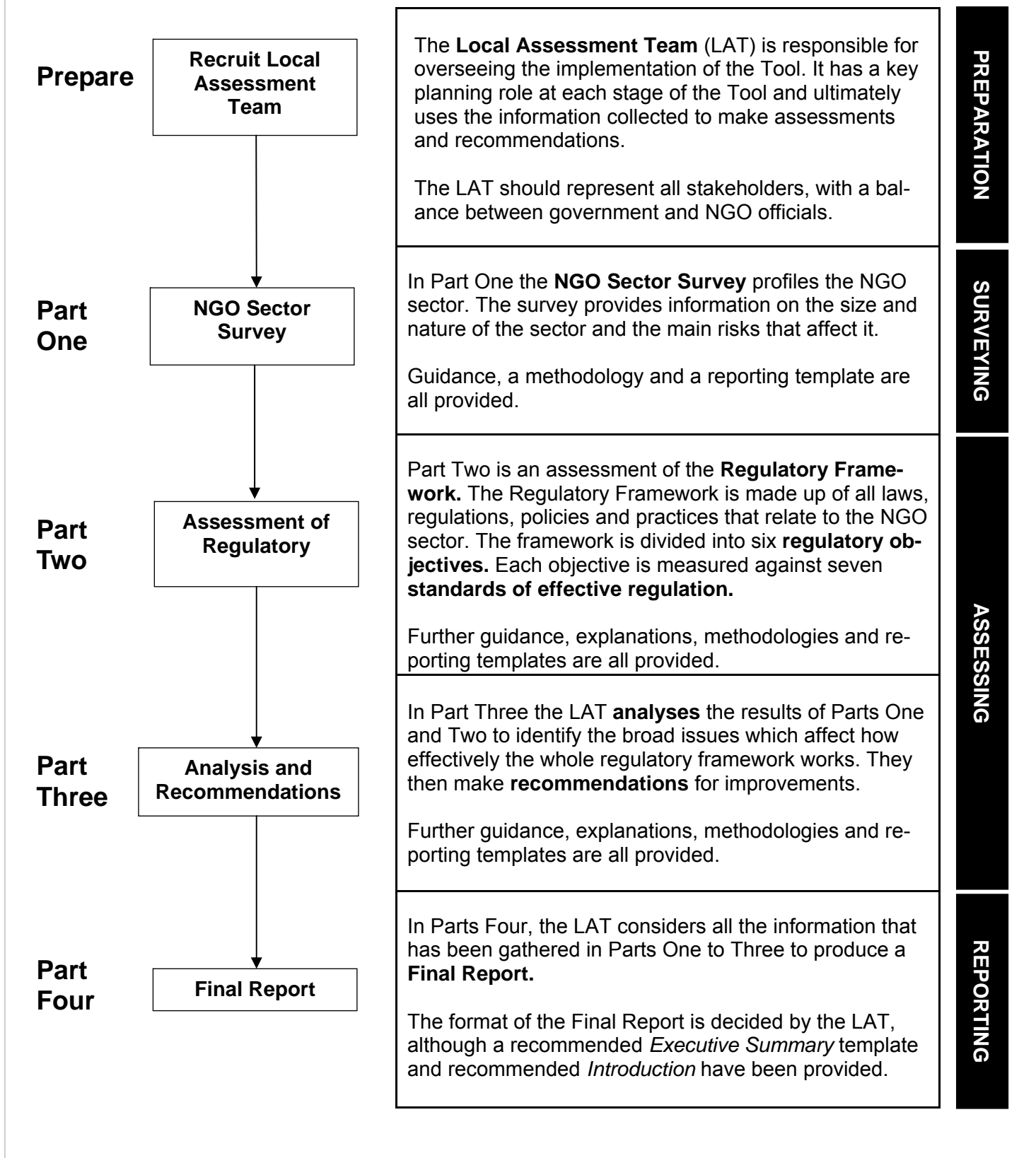
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### NGO Sector Assessment Tool Flow Chart



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### Methodology - How to Use the Tool

This document provides you with all the information and materials you need to implement the Tool in your country.

There are five sections to this document, one for each part of the Tool and one for General Information. There is a standard format to each section as follows.

1. **Introduction:** An overview of the aims of that part of the Tool.
2. **Flowchart:** A diagram illustrating how that part of the Tool is implemented.
3. **Methodology:** Detailed notes on implementation.
4. **Glossary:** Definitions of key terms are provided (General Introduction and Part Two only)
5. **Materials:** The materials and information you will need for implementing the Tool (not including General Introduction).

A banner at the top of each page provides a quick indicator to which section of the document you are in.

Each Part of the Tool is designed to be implemented separately, and each section of this document is a stand-alone guide to the implementation of that Part.

The materials in this document are for reference purposes and cannot be adapted or written on. Adaptable materials designed for use in implementing the Tool are available separately in the *Working Documents* file.

### Glossary - Definition of NGO

**For the purposes of this Tool, an NGO is...**

- an organisation;
- non-governmental, autonomous and self-governing;
- freely formed and run by a group of people;
- for a purpose which benefits a section of society;
- is not a political party; and
- does not distribute its profit to the members / directors / fiduciaries.

**An organisation.** It has a degree of formality which indicates an organisational structure and an identified common goal. Formal does not necessarily imply a legal structure, but does exclude more ad hoc or disorganised groups. It is different from an appeal which tends to be set up to finance a short term goal and then disbanded.

**Non-governmental, autonomous and self-governing.** It is self governing and independent. It is not a part of or controlled by government or any other agency which is not itself an NGO.

**Freely formed and run by a group of people.** It consists of more than one person, and the NGO is established voluntarily. Forced establishment or membership undermines its independence and autonomy.

**For a purpose which benefits a section of society.** An NGO's purpose should benefit the public. Benefits may be restricted to some part of society where it forms a recognisable sub-section (e.g. a particular age group, ethnic or religious group, residents of a particular area, or those with a particular need). Access to benefits may be limited to members where membership is freely open to all within a particular group as defined above.

**Is not a political party.** Whilst political parties may not be part of government, it is usually their aim to become part of government and as a result that cannot be considered NGOs for these purposes. This does not disqualify NGOs that engage in some limited political activity or campaigning that is linked to their public benefit purposes.

**Does not distribute its profit to the members / directors / fiduciaries.** NGOs can make money through fundraising, donations or even trading. What is important is how these funds are distributed. They should not be used for the private benefit of those who control the funds. Instead, all funds should be used solely for the purposes for which the NGO was established.



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## Implementation of the NGO Sector and Regulation Review Tool in the Philippines: a case study

*Phil Cooper, Regional Manager, International Programme, Charity Commission for England and Wales*

In 2007 the government of the Philippines agreed to pilot the use of the tool and this process was completed in 2008. It should be noted that the Philippines were happy to resource the requirements of the tool and to ensure that it was completed fully with full co-operation from both government and the sector. The costs were also partly met by the International Monetary Fund (IMF) who saw this as an important development in the delivery of compliance to Financial Action Task Force (FATF) Special Recommendation VIII.

### Initiation

Following discussions held at the fringes of the Asia Pacific Group Plenary meeting held in Manila in 2006 it was agreed that the government of the Philippines would work with the Charity Commission International Programme (CCIP) to assess the effectiveness of NGO regulation in the context of SRVIII and to see what further work might be needed to continue to improve the regulatory framework.

Pursuant to the recommendation of the Philippine delegation, in January 2007, SEC Chairperson Fe B. Barin agreed to convene a Technical Working Group (TWG) to formulate Terms of Reference seeking technical assistance from the Charity Commission (CC) for the conduct of an NGO Sector Assessment. The CC agreed to provide technical assistance and conceptualized the Tool that was used in this project. The Tool was developed with the assistance of an advisory group made up of expert representatives from the NGO sector, government, donor and inter-governmental communities. Funding was provided by the IMF and the Foreign and Commonwealth Office (the foreign affairs ministry in the UK government).

The Charity Commission entered into an agreement with the Caucus of Development NGO Networks (CODE-NGO) in September 2007, for the latter to be its partner in undertaking the project to pilot test and evaluate the Tool. CODE-NGO was chosen by the CC because as stated in the Tool, *“NGOs have greater access to other NGOs than governments. They have a much wider reach – geographically, their networks meet many different levels from the very local to the international, and with many different kinds of people. The NGO sector will therefore have a different way of engaging with society to that of the regulator and therefore they will have access to different information than government and access to a much wider network of NGOs.”*

Thereafter, the Local Advisory Committee (LAC) was created to help CODE-NGO in the assessment and Tool evaluation process. The representatives from the government were chosen and invited by the Charity Commission based on their participation at the Regional Conferences in Antipolo (February 2006), Hong Kong (September 2006), the special workshop held at Pasig City (July 2008), as well as their membership in the Technical Working Group that formulated the terms of reference for technical assistance. The representatives from the NGO sector were chosen and invited by CODE-NGO based on their experience and active involvement in NGO affairs and activities. A Project Management Team acted as the Secretariat, gathered and analyzed data on NGOs from government agencies and NGO databases and from secondary sources, as well as existing laws and regulations on NGOs, and drafted the reports.

### Funding

Full implementation of the tool is a resource-intensive process requiring amongst other things:

- A project manager or co-ordinator
- People to sit on the Local Advisory Committee and the funding to attend meetings and arrange evaluation events etc
- Funding for visits to regulators and other bodies

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- Costs to develop the report
- Meetings to agree report contents
- Evaluation events etc

In addition, the government has to agree that government offices will co-operate and contribute in a timely manner to the review and other agencies such as NGOs also have to agree to contribute. It is often the case that further costs would be incurred to deliver all these elements.

In the case of the Philippines review, the government of the Philippines fully supported the review and provided local resources as required. This was essential for the success of the review and such commitment is an absolute requirement if the tool is to be used successfully.

Additional funds and support came from the IMF, the International Programme of the Charity Commission and the UK Foreign Office.

### The four stages of the review using the tool

#### Part One: Sector Survey

Part One is a desk-based survey of the NGO sector to gather information on the size and nature of the NGO sector and the major risks that affect it, or are perceived to affect it. It provides a framework for identifying and recording the key information on the NGO sector. It also identifies areas where no information is available or is outdated and helps establish where further work may be needed.

There are four stages to Part One:	<b>Scope</b>	<b>Activities</b>
1	Survey Scope or Scope of the Study	The Local Advisory Committee agrees on the scope of the survey or study and determines what organizations within the country fall within the definition of NGO.
2	Resource Management	The LAC develops a plan for implementing the Sector Survey/Study plan. The plan includes the allocation of resources, methods for obtaining information, a timetable and review and oversight procedures.
3	Research	Research begins to obtain information on the profile of the sector and the major risks that affect it. The information that needs to be collected is set out in the Sector Survey Questions. The results from the survey are entered into the Sector Survey spreadsheet.
4	Report	The results are presented to the Local Advisory Committee. The LAC considers the results and notes any caveats, concerns or comments. The LAC completes the Sector Survey Summary Report.

The desk-based survey included data on the following:

- number and income of NGOs, including overseas income; risk/ abuse profile including vulnerabilities and nature, purpose, causes and perception of abuse (first priority according to the Charity Commission tool);
- profile of NGOs by size, legal type, activity, donors and funders, income types, beneficiary and expenditures (second priority);

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The desk-based survey was undertaken by the project manager, Randy Tuaño, and the project research assistant, Josephine Tria, who collated several books and journals and statistical information available from the regulatory agencies and other publications to complete this step of the report. A survey was also undertaken for a small sample of SEC registered organizations. It had envisioned that the information collected will be of interest to a wide range of stakeholders. As well as being of general interest, it would provide specific information which should help policy makers when considering laws and regulations for the NGO sector.

In order to make allowances for capacity and capability in conducting the desk-based survey, the information collated by the profile is divided into a hierarchy of three different priority levels. Priority one data (number and total income, including those from overseas) is the most important information to be gathered, and up to 75% of resources should be allocated to obtaining this information to a good degree of confidence. Priority two information includes data on NGO activities, beneficiaries, sources of income and expenditures. The least essential information is priority three, and not every country will gather this information. However, during the collation of the data, all data containing all three levels of confidence were included in this Report.

In order to make a judgment on each source of information and how this might impact the result, the sources were classified into primary and secondary, whether the information is based on fact or anecdote or whether it is verified.

#### ***Part Two: Assessment of the Regulatory Framework***

Part Two assesses the effectiveness of the regulation framework and describes the totality of laws, regulations, systems, processes and activities which are designed to regulate the NGO sector.

The Local Advisory Committee members took turns in interviewing government and non-government informants. More than 35 persons were interviewed from 20 government agencies and NGO organizations in Metro Manila, Cebu and Davao. Of the government agencies, four were the primary registration authorities for NGOs: the Securities and Exchange Commission (SEC), the Cooperative Development Authority (CDA), the Housing and Land Use Regulatory Board (HLURB) and the Department of Labor and Employment (DOLE). The other government agencies were the secondary registration, licensing or accreditation authorities for NGOs: the Department of Social Welfare and Development (DSWD), the Department of Health (DOH) and the Insurance Commission (IC). An NGO certification body, the Philippine Council for NGO Certification (PCNC), was also briefly reviewed.

Charity Commission representatives, Ben Evans and Sarah Jane Digby, arrived from London to join the LAC members in conducting the interviews in Metro Manila, Cebu and Davao and observed the assessment process, which was undertaken for a period of two weeks, from January 14 to 25, 2008 although several interviews were also undertaken outside of these dates.

There are four effectiveness assessment ratings coded according to color: Effective (Green), Mostly Effective (Yellow), partially Effective (Orange) and Not Effective (Red). These were utilized in the assessment of whether the Philippine government in general was able to achieve the regulatory objectives set in the manual.

#### ***Part Three: Strategic Issues***

Strategic issues are the broad issues which impact on the effectiveness of the regulatory framework. Part Three takes these issues one level higher and encourages discussion and brainstorming at a more strategic level.

The results of Parts 1 and 2 were collated and discussed in full during a workshop conducted in Tagaytay City on January 24 and 25, 2008, which finalized the assessments of individual regulatory agencies including the four primary NGO registration agencies (the SEC, the Cooperative Development Authority, Bureau of Labor Relations, and the Housing and Land Use Regulatory Board) and three secondary

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registration agencies (the Department of Social Welfare and Development, the Insurance Commission and the Department of Health).

The assessment of the NGO regulatory environment was undertaken in a collective way among government and NGO representatives of the Local Advisory Committee. Key strategic risks in the regulatory environment and their root causes were also identified, and a preliminary assessment of the regulatory tool was undertaken.

Two Local Advisory Committee meetings on February 15 and 29, 2008, were undertaken after the Tagaytay workshop. During these meetings, the LAC identified key regulatory issues were finalized and then prioritized. A probability score (high, medium, low) was assigned to each of the issues. The issues were then plotted against a risk matrix. The second of the two meetings focused on finalizing the strategies to mitigate the risks.

Although not a requirement under the Tool, the Local Advisory Committee decided to hold a workshop to validate the results and findings of the assessments. The validation workshop was conducted on March 28, 2008, in Pasig City, with around thirty participants coming from both government and non-profit organization sectors. The results of the workshop validated the assessments of specific regulatory agencies made by the LAC, and the list of risks and vulnerabilities and the interventions to reduce the impacts of these risks were also developed by the LAC in consultation with the workshop participants.

#### **Part Four: The Final Report**

Part Four is the Final Report. The Final Report is the ultimate outcome of the Assessment. It summarizes the results from Parts One, Two and Three and identifies the main features of the sector, the main risks and recommends priority steps for the future. The Local Advisory Committee undertook meetings in April and then in July, 2008, to finalize the report.

#### **Effectiveness in the Philippines**

The present regulatory framework in terms of registration and licensing NGOs is very effective; and the rules are clear to most organizations. However, there is some debate on the effectiveness of rules in the areas of protecting non-profits and mitigating risks; government and non-government organization representatives in the Local Advisory Committee disagree based on their differing perspectives on the clarity of the guidelines issued by the government and the mandate and capacity of the government regulators.

#### **Lessons learnt**

The Charity Commission International Programme team were very pleased with the effective way which the government of the Philippines adopted and ran with the tool, and concluded that it had been thoroughly used and that the final report was clear and delivered the expected benefits in terms of an assessment of the scope and nature of the NGO sector and the effectiveness or otherwise of the current systems of NGO regulation. There were seven key issues that would be useful for future implementation of the tool:

1. The importance of senior government commitment to the process from day 1
2. Adequate funding to be in place for all aspects of the review
3. Having a project manager to oversee the process
4. Meeting stakeholders early in the process to explain what was going to happen and when so that they can prepare
5. Driving the process forward to meet deadlines and not allowing the review to be bogged down by small issues
6. Ensuring that each stage and process has an owner who will take responsibility for that role
7. Delivering an outcome that is positive and that can actually be implemented in the country.



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## U.S. Government Efforts to Protect and Promote Charitable Giving

*United States Departments of Treasury and State*

The spirit of giving unites people of all backgrounds, from every religious tradition and every ethnic heritage. The beneficial work of charities to communities around the world can be seen every day. From providing humanitarian assistance to areas afflicted by disaster and conflict, to increasing access to education and medical services, charities fulfill a critical role to society. Charities in the United States serve their local communities as well as populations overseas, including those living in disaster areas and conflict zones.

Charitable giving and voluntarism have a long tradition in the United States, and our country is a global leader in charitable donations year after year. In recent years the American people have donated more than \$300 billion annually to charitable causes around the world, such as those affected by the 2004 tsunami in Indonesia and Southeast Asia, the 2010 earthquake in Haiti, and the 2011 tsunami in Japan. The U.S. Government values and encourages charitable giving, both at home and abroad.

At the same time, the U.S. Government seeks to protect charities from abuse, including the very real threat of exploitation by terrorist organizations. It is well documented that terrorist organizations, such as al Qaida, the Taliban, Hamas, and Hizballah, divert charitable and developmental funds, use charitable organizations to cultivate support for their organizations, and shield their activities from official and public scrutiny. Often, donors to these charitable organizations are unaware that their funds are being used for nefarious purposes.

The U.S. Government has taken a number of actions over the past decade to identify and disrupt attempts by terrorist organizations to exploit the charitable sector. Unfortunately, such efforts have at times had a chilling effect on legitimate, well-intentioned donor activity, particularly in Muslim communities. The U.S. Government is committed to working with these communities to mitigate such unintended consequences and better protect the charitable sector from terrorist abuse.

In his 2009 speech in Cairo, President Obama stated that “in the United States, rules on charitable giving have made it harder for Muslims to fulfill their religious obligation. That’s why I’m committed to working with American Muslims to ensure that they can fulfill zakat.” The President’s commitment has been honored through numerous outreach efforts with the charitable sector and Muslim American communities over the last few years. Such outreach is one part of a comprehensive counter-terrorist financing strategy to diminish the capacity of terrorist organizations and their support networks.

The U.S. Government’s strategy to protect the charitable sector from terrorist abuse closely follows the internationally-agreed framework provided by the Financial Action Task Force (FATF) Special Recommendation VIII. This multi-pronged government approach to countering the specific terrorist threat to the charitable sector includes the need for: (i) oversight; (ii) investigations and enforcement actions; (iii) outreach and guidance; and (iv) international cooperation.

### Nature of the Threat Posed by Terrorist Organizations

A variety of characteristics make the charitable sector particularly vulnerable to abuse and attractive to those who seek to support terrorist activity. Charities often focus their relief efforts on areas of conflict – areas where humanitarian aid is urgently needed, where oversight is limited, and where terrorist groups may be active and may even control territory. In addition, charities often deal in cash and may have access to considerable funding sources, including from donors who are unaware of or unlikely to question potential links to terrorism.

Moreover, many charities have a global presence that can facilitate the movement of funds and material across borders via international branches. Although the resources necessary to support any given terrorist attack may be relatively small, the amount needed to support the ongoing efforts of a transnational

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terrorist organization, such as al Qaida, the Taliban, Hamas or Hizballah, is significant. Charities can provide a veil of legitimacy for the movement of substantial amounts of funds, personnel, military supplies, and other resources by terrorist groups and their associates, often with minimal government supervision.

One of the greatest challenges is that, by providing funds or otherwise legitimate social services to vulnerable populations, terrorist groups and their supporters can use charitable institutions to radicalize communities and build local support for violent causes. Charities established or controlled by terrorist groups fund the operation of schools, religious institutions and hospitals that may create fertile recruitment grounds or generate dependency among vulnerable populations for essential services. Local support for these essential services, often provided in places where governments have difficulty supplying competitive alternatives, makes it politically difficult for local governments to take action against these organizations.

For all of these reasons, legitimate charities are vulnerable to abuse through exploitation by terrorist groups and their associates, and apparently well-intentioned groups may be used as cover for nefarious activity. For example, United Nations (UN)-designated terrorist group Lashkar e Tayyiba (LeT) has established numerous charitable fronts to mask the organization's activities, including Jamaat ud Dawa, Idara Khidmat-e Khalq, and Falah-e Insaniat Foundation. LeT has used these cover names to raise funds, evade sanctions, and operate hundreds of schools and health clinics to recruit members to the organization. LeT's efforts were particularly visible following the 2005 earthquake in South Asia and the 2010 flooding in Pakistan. LeT's charitable fronts are clear examples of charities that provide social services to communities in Pakistan, while at the same time serving as key components of the overall terrorist mission of LeT.

There have been many other examples around the world of charities that have been integral components of terrorist networks. Examples include: the Revival of the Islamic Heritage Society (RIHS) and the Al Haramain Islamic Foundation (AHF), both of which were designated for sanctions by the U.S. and have multiple branches listed by the UN for having provided financial and material support to al Qaida and other designated terrorists and terrorist organizations; the Union of Good, which was designated by the U.S. for providing support to Hamas; the Martyrs Foundation, which was designated by the U.S. for providing support to Hizballah; and Tamils Rehabilitation Organization (TRO), which was designated by the U.S. for providing support to the Liberation Tigers of Tamil Eelam (LTTE).

### Threat to U.S. Charities and Donors

There have been several examples of terrorist organizations and their support networks raising funds through charities in the United States. The extent of the terrorist financing risk for U.S.-based charities varies dramatically depending on the operations and activities of the charity. As of 2010, there were over 1.8 million charities operating in the United States, the overwhelming majority of which face little or no terrorist financing risk. However, for those U.S.-based charities operating abroad, particularly in high-risk areas where terrorist groups are most active, the risks can be significant. Terrorist groups and their supporters continue to attempt to infiltrate the charitable sector and exploit charitable funds and operations to support their activities.

Such abuse and exploitation have become far more difficult over the past several years through the collective efforts of the U.S. law enforcement and counter-terrorism community, including sanctions designations of charities associated with terrorist organizations. To date, the United States has designated eight U.S.-based charities and approximately 60 global charities. The Holy Land Foundation for Relief and Development (HLF), for example, was a large U.S. charity that was designated almost ten years ago for providing millions of dollars of material and logistical support to Hamas.

Not surprisingly, designated charities include organizations engaged in legitimate humanitarian activity – even as they support terrorism. In such instances, the provision of charitable services cannot excuse the charity's support for terrorism. Rather, sanctions and enforcement actions against such charities serve to protect the public by identifying those organizations that support terrorist groups or activities,

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thereby preventing such organizations from preying on well-intentioned donors. It is important to emphasize that there have been no U.S. Government sanctions designations to date based solely on good-faith donations.

### **U.S. Strategy to Counter Terrorist Abuse of Non-Profit Organizations (NPOs)**

In working to fulfill its international obligations, the comprehensive U.S. strategy to counter this threat consists of the following objectives:

1. Enhancing the transparency of the charitable sector through coordinated oversight;
2. Protecting the integrity of the charitable sector through investigations, designations, and targeted enforcement actions against specific terrorist financing threats within the sector;
3. Raising awareness of the risk of terrorist abuse of the charitable sector and engaging in direct and sustained outreach to the charitable sector to provide guidance on how to mitigate this risk; and
4. Pursuing multilateral efforts by engaging foreign partners in protecting the charitable sector from terrorist abuse.

Each element of this strategy is briefly discussed in turn below.

#### ***Enhancing transparency of the charitable sector***

Strengthening the transparency of the charitable sector counters terrorist abuse by allowing charitable organizations, donors, and government authorities to better understand, oversee and detect such activity. In the U.S., the charitable sector is subject to three levels of oversight: (i) the federal government; (ii) state authorities; and (iii) the private sector.

At the federal level, the primary vehicle for oversight of charities is the federal tax system, administered by the Internal Revenue Service through the provision of tax-exempt status for non-profit organizations.

Additionally, most U.S. states have agencies with oversight responsibilities over charities raising money in that state, no matter where the charities are domiciled. Finally, a key element of the U.S. system is the self-regulation performed by private sector bodies. However, it is important to recognize that regulation or oversight are not sufficient to protect the sector; all of the terrorist threats in the U.S. charitable sector have been identified and addressed using investigations and sanctions or enforcement actions, which are critical elements of charitable sector protection.

#### ***Conducting investigations and targeted enforcement actions***

Many government agencies are involved in protecting the integrity of the charitable sector. The U.S. Departments of the Treasury and State work with the Federal Bureau of Investigation, the Department of Justice and other agencies to investigate and combat cases of terrorist financing in the charitable sector through targeted regulatory and law enforcement investigations, information sharing, terrorist financing sanctions designations, and criminal prosecutions.

The application of sanctions designations is one of the primary actions used by the U.S. Government to protect the integrity of the charitable sector. A sanctions designation deprives the subject of access to the funds required to pay for infrastructure, travel and other logistics, supplies and weaponry, and for the day-to-day sustenance of terrorist groups. Designations are designed to be preventive – to freeze assets when there is a reasonable basis to believe that the entity or individual is engaged in terrorist activity or supporting a designated terrorist or terrorist group. In addition, a key objective and significant benefit of a designation is the notice it provides to the charitable sector, the donor community and the general public.

#### ***Conducting outreach, providing guidance and strengthening partnership***

One of the U.S. Government’s most important missions is to identify, disrupt, and dismantle illicit financial networks that support terrorists, organized criminals, weapons of mass destruction proliferators, and other national security threats. To the extent that the charitable sector is exploited to provide support to

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terrorist activity, our challenge is clear: to close the avenue of material support to terrorist activities while at the same time supporting and, indeed, encouraging legitimate and well-intentioned donor activity.

As already noted, necessary enforcement actions may, in some cases, create an unintended chilling effect on charitable giving, particularly within Muslim communities. This is especially true with respect to charitable interests in servicing vulnerable and needy populations overseas in areas where terrorist organizations are most active. Overcoming these challenges requires strong partnership and a shared commitment among the security, humanitarian, and development communities. This realization, together with the underlying need to protect charities from terrorist abuse, frames the U.S. Government’s efforts to (1) conduct outreach, (2) issue guidance, and (3) develop a greater partnership with the charitable sector.

#### **Outreach**

It is important to highlight the significant role that community organizations play in supporting government efforts to tackle abuse of the charitable sector, especially from those communities that terrorists are most seeking to exploit. The U.S. Government frequently meets and collaborates with specific communities and organizations, such as the Arab and Muslim American communities, as well as representatives from the broader charitable sector.

U.S. Government outreach efforts focus on fostering greater understanding of the terrorist threats we face and the actions we are taking to combat these threats. Another important part of the outreach message is that the public and private sectors should work together to promote safe charitable activity and to protect the sector from terrorist exploitation. Such collaboration is needed not only to develop effective and practical safeguards, but also to identify and develop ways in which charities can safely assist populations in high risk areas regions.

#### **Guidance**

To reinforce our outreach efforts, the Department of the Treasury has developed and issued extensive guidance to charities seeking to protect themselves from terrorist abuse, including Treasury’s Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities (Guidelines). The Guidelines do not create any new legal requirements. Rather, they are intended to provide guidance on fundamental principles of good charitable practice; governance, accountability and transparency; financial accountability and transparency; programmatic verification; and anti-terrorist financing best practices.

The Guidelines are risk-based, reflecting Treasury’s recognition that a “one-size-fits-all” approach is untenable and inappropriate due to the diversity of the charitable sector. The Guidelines also acknowledge that certain exigent circumstances (such as catastrophic disasters) may make application of best practices difficult. Moreover, the Guidelines are not an exhaustive or exclusive set of best practices, and Treasury recognizes that many charities, through their extensive experience and expertise in delivering international aid, have already developed effective internal controls and practices that lessen the risk of terrorist financing or abuse.

Treasury’s most recent guidance was issued in June 2010 – a set of answers to frequently asked questions (FAQs) by the charitable sector and donors. This FAQ document provides important public material on U.S. sanctions authorities, terrorist threats within the charitable sector, and best practices for mitigating such risks. The U.S. Government also maintains a number of publicly available Web sites and resources, including a comprehensive list of designated foreign terrorist organizations and their support networks, typologies of terrorist behavior, a public “hotline,” and a Web page devoted to terrorist financing issues that impact charities [[LINK](#)].

#### **Partnership**

The final component of the U.S. Government’s engagement with the charitable sector focuses on the importance of both promoting and protecting charitable assistance in high risk regions. Neither the government nor the charitable sector, acting alone, can adequately address this challenge.



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Over the past decade, the U.S. Government has worked diligently – within the government, with key stakeholders in the charitable sector, and with Arab and Muslim communities in particular – to explore how best to achieve our common aims. These discussions have focused on the development of alternative relief mechanisms, intended to provide safe and effective ways for individuals to contribute assistance into critical regions where aid is desperately needed, but where terrorist organizations largely control relief and distribution networks.

The concept of alternative relief mechanisms is compelling. But it also extraordinarily difficult to put into practice and will require a strong partnership among elements of the national security, development, and charitable communities. One example of such a mechanism was a pilot project to establish an alternative relief mechanism for the Palestinian Territories. Launched in August 2008, the American Charities for Palestine (ACP) raises funds from U.S. donors for health and education projects in the Palestinian Territories. The funds are delivered through channels approved by the U.S. Agency for International Development, in consultation with U.S. counter-terrorism authorities. While there is still more work to be done in developing additional mechanisms, the ACP represents one model for our continued work.

#### ***Pursuing multilateral efforts***

There is more global awareness of terrorist exploitation of the charitable sector than ever before, and greater efforts have been made to prevent such abuse. Many countries are increasingly using financial, economic, and law enforcement powers to identify, investigate, designate, and prosecute charities and charity officials engaged in supporting terrorist groups. Many countries are also working with their development agencies and the broader charitable community to protect social and charitable services, especially in regions at high risk of terrorist abuse.

#### **Addressing Challenges Together**

The threat of terrorist abuse of charities is clearly a global challenge – one that requires the understanding, cooperation and collaboration among many partners. The U.S. Government has made substantial progress in forging and strengthening partnerships among various agencies, governments and communities. But much work still needs be done. The U.S. Government will continue to work domestically and internationally to help promote charitable giving and protect it from terrorist abuse. The expertise, input, and resources of government and the charitable sector are required to advance these shared goals. It is only through these collaborative efforts that we can succeed collectively.

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## Fighting financing of terrorism through the abuse of non profit organizations, FATF Special Recommendation VIII

*Council of Europe, Secretariat of the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL)*

The objective of MONEYVAL is to ensure that its member states have in place effective systems to counter money laundering and terrorist financing and comply with the relevant international standards in these fields. The main standards subject to MONEYVAL evaluation are the 40 recommendations of the FATF and the 9 Special Recommendations on Financing of Terrorism and Terrorist Acts. MONEYVAL is responsible for the evaluation of the anti-money laundering measures and measures to counter the financing of terrorism (AML/CFT) in Council of Europe member States which are not members of the Financial Action Task Force (FATF).

The ratings given in the third round reports for each individual Recommendation (including SRVIII) range from Compliant (C), Largely Compliant (LC), Partially Compliant (PC) and Non Compliant (NC). The present analysis of Special Recommendation VIII is based on all third round mutual evaluation reports, each of which followed the global template for AML/CFT assessment, agreed by the FATF and FATF style regional bodies (such as MONEYVAL) and financial institutions in 2004. The article describes the level of compliance with FATF Special Recommendation VIII, best practices identified in two countries with high ratings for SRVIII and difficulties frequently encountered in meeting all required criteria of the standard. It is based upon the recently published Horizontal Review of the third round of MONEYVAL evaluations [\[LINK\]](#).

### Non-profit organisations, a MONEYVAL countries overview

In most MONEYVAL countries, the non-profit sector largely comprises civil associations, foundations, endowments and charities. The sector was generally regulated by specific legislation that had typically been enacted for a considerable time, usually focusing on formal registration requirements.

The standard relating to the prevention of the misuse of non-profit organisations (NPOs) for financing of terrorism purposes is set out in FATF Special Recommendation VIII:

Countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Non-profit organisations are particularly vulnerable, and countries should ensure that they cannot be misused:

- by terrorist organisations posing as legitimate entities;
- to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; and
- to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.

It is first noted that NPO sector is large and diverse and plays a vital role in the world economy, in many national economies and social systems. The efforts of the sector complement the activity of the governmental and business sectors in providing essential services, comfort and hope to those in need around the world. The ongoing international campaign against terrorist financing has unfortunately demonstrated however that terrorists and terrorist organisations can and do exploit the NPO sector to raise and move funds, provide logistical support, encourage terrorist recruitment or otherwise support terrorist organisations and operations. This misuse not only facilitates terrorist activity but also undermines donor confidence and jeopardises the very integrity of NPOs. Therefore, protecting the NPO sector from terrorist abuse is both a critical component of the global fight against terrorism and a necessary step to preserve the integrity of NPOs.

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The main problem the MONEYVAL evaluators encountered in almost every country was the lack of sector specific reviews undertaken first, to assess the adequacy of domestic laws and regulations that relate to NPOs and second, to gain an adequate overview of the NPO sector for the purpose of identifying those organisations that are or may be at risk of being misused for terrorist financing. In a large majority of MONEYVAL countries some of the relevant registering authorities also appeared not to have any real awareness of the importance of the terrorist financing issue.

Most countries were therefore unable to demonstrate that any formal and targeted assessment of the adequacy of their NPO specific legislation had taken place.

### Non-profit organisations and the financing of terrorism risks

It is recognised that implementation of Special Recommendation VIII is far from easy for national authorities. Many authorities, rightly or wrongly, indicated that as they did not consider their country to be a TF risk, they had not yet given full attention to this Special Recommendation.

It was far from clear in many countries that the authorities nationally responsible for NPO oversight had a complete picture of the whole sector, particularly those that controlled the majority of the financial resources of the sector or which were barely involved in international transactions. Thus, it was not always clear that they had identified which were the potentially risky NPOs in FT terms. On the more positive side though, it was frequently apparent that law enforcement were aware of any potential risk at a national level in this sector and were able to take action where necessary through criminal, or in some cases, civil process.

SRVIII was one of the lowest rated Recommendations with 27 countries (93,1%) in the lower range, of which 12 (41,3%) were found “Non compliant”.

Few countries had fully established appropriate measures to ensure that funds or other assets collected by or transferred through NPOs were not diverted to support the activities of terrorists or terrorist organisations. Deficiencies in this area were detected in many countries, regardless of their overall preparedness in AML/CFT matters. The only country found “Compliant” in the 3rd round mutual evaluation was Latvia, which had comparatively recently adopted modern and comprehensive legislation governing the NPO area and a monitoring regime.

The only “Largely compliant” country was Israel, where very positive steps had been taken in line with the majority of the essential criteria under this Special Recommendation (particularly in terms of ongoing monitoring of sector vulnerabilities) though the NPO legislation had not yet been formally reviewed and an outreach programme to the sector had yet to be commenced.

National authorities of almost every lower rated country failed to perform either a periodic or any review of the NPO sector with the objective of assessing its exposure to the threat of terrorist financing. This was despite the sources of information available which could have provided a basis for such reviews: the existing structures of reporting and supervision within the NPO sector (typically performed by a ministry or other governmental body responsible for the area to which the main activity of a particular NPO belongs); or, if applicable, the annual audits or other financial information the NPOs submit to the domestic tax authority (usually when applying for exemption from taxation). There were some signs of ad hoc reviews. For example, Cyprus took some action after 11 September 2001 in checking NPOs with significant participation of foreign individuals.

The apparently low level of governmental terrorist financing awareness resulted in generally insufficient, if any, outreach to the NPO sector.

As a result, the reports show only sporadic awareness-raising in this field. A notable example, again, was Latvia, where an extensive public awareness campaign had been conducted “to inform NPOs of their obligation to register and educate the public of its responsibility to know who they are donating money to and what those funds are being used for”.

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Examination of the third round reports shows that obligatory licensing and registration, had already been part of the ordinary procedure for establishing NPOs in most MONEYVAL countries but for purposes other than the fight against terrorist financing. Likewise, the requirement of financial transparency had been part of the ordinary regime in a number of countries for many years, but also for other, typically tax related purposes. Nonetheless, this means that there is, in most countries, a legislative foundation to build on when developing compliance with SR VIII. The third round Horizontal Review notes “whether and how these opportunities are leveraged for CFT purposes will need to be tested and verified in the next evaluation round”.

### Best practices in preventing and countering financing of terrorism through NPOs

#### Latvia

##### The need for registration

In Latvia a Law on Associations and Foundations was introduced which, among other things, required all nonprofit organizations (NPO) to register with the associations and foundations registrar. Registration is required whether or not the organization receives outside funding. Annual reports on NPO activities are required to be filed. Religious organizations are separately recorded by the Agency of Religious Issues.

##### Internal control

A variety of laws and regulations impose internal control requirements on NPOs. The Law on Accounting extends to associations and foundations, to political organizations and their associations, and to religious organizations. In Latvia, accounts must reflect all economic transactions and the status of property. The Associations and Foundations Law requires that income of an association or foundation may only be utilized for the achievement of goals specified in the articles of association.

Likewise, the Public Benefit Organization Law requires that associations and foundations, religious organizations and public benefit organizations should utilize their donations according to the goals stated in the articles of the organization, constitution or regulations. The associations and foundations are required to submit to a State agency annual reports of donations and gifts. Using a wide range of information systems, the above mentioned agency monitors the financial assets of NPOs, as well as donations to NPOs, both for tax compliance and, in cases of suspicion of ML or FT, informs the FIU.

In addition to registration information, financial data on NPOs could be generated by:

- NPO reporting of charitable donations;
- taxpayers claims for charitable deductions on tax filings;
- applications from NPOs to be eligible to receive tax deductible charitable contributions;
- information on payment of social contributions by NPOs;
- a review of all donations above a certain threshold.

Based on extensive consultations with the FIU, analytical systems originally developed for tax needs are also used to identify suspicious transactions. In 2005 a new Order on was issued (“Order on how the tax administration units forward information to the Financial Intelligence Unit”) which details procedures for co-operation between the State Revenue Service and the FIU. The order defines indicators that could give evidence about the legalization, or attempts to legalize, illegal proceeds, the actions to be taken by an official who detects suspicious transactions or transactions related to the financing of terrorism, as well as the appointment of persons responsible for the exchange of information with the FIU. Indications of criminal activity are referred to the police and suspicious transactions are reported to the Control Service.

##### The need for awareness

In addition the monitoring carried out by the Latvian Ministry of Finance, an extensive public awareness campaign has been conducted to inform NPOs of their obligation to register and to educate the public of its responsibility to know who they are donating money to and what those funds are being used for. Under Latvian law, donors have the right to receive such information from the NPOs they support.



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#### ***The Israeli experience***

The two principal types of non-profit bodies in Israel are the amutot (associations) and public welfare/benefit corporations which national authorities supervise and perform ongoing risk assessments.

The Law of Non-Profit Organisations requires all associations to submit to the Registrar of Non-Profit Organisations annually various documents, including financial statements and protocols. These documents are open to the perusal of the public in the offices of the Registrar. In the event that an association does not submit these documents it is not entitled to receive a certificate of proper management and therefore can not receive governmental funding or funding by those bodies which require presentation of the certificate.

#### The need for monitoring

The law also confers upon the Registrar of Non-Profit Organisations powers to oversee the associations, including powers to demand clarification in respect of financial statements, to investigate, to administratively remove the registration of the associations and to submit court applications to liquidate those which violate the law.

In accordance with current practice approximately 700 in-depth checks are carried out annually on Israeli associations. The checks are carried out mainly on those which have high annual incomes.

In the context of the amendment of the Public Welfare Corporations Law, additional rules for non-profit organisations were implemented, such as the obligation to submit, in addition to a financial statement, a verbal report which shall include information regarding service providers to associations, transactions with relatives, changes in geographic location, etc.

According to the Law of Non-Profit Organisations, NPOs are under a statutory obligation to submit financial information to the Registrar on a yearly basis. Furthermore, the Registrar of Non-Profit Organisations conducts in-depth accounting checks regarding hundreds of NPOs every year.

#### The need for transparency

In Israel, the associations must submit updates regarding executive board members, protocols of meetings, financial statements, etc. This information is placed on files, which are open to the general public.

The Registrar's inspection files are available to law enforcement conducting investigations with regard to money laundering or financing of terrorism. Law enforcement agencies may receive, upon request, any relevant information held by the Registrar.

#### The need for risk assessment

In addition, the Registrar's office employs a lawyer who specialises in those NPOs which are connected to high risk sectors. He works in full coordination with the security authorities where information appears to him to be of a suspicious nature - for reasons such as the particular entities involved in the NPO, the nature of its activity, or as a result of previous information (which may in part be received from the security services).

#### The need for reporting

When it appears that an NPO is carrying on activity which is likely to involve a danger to public security, or when it appears that there are people involved in an association's activity who are likely to constitute a danger to the public, information is transferred to the law enforcement authorities. Information is also disseminated from the Registrar's office to the FIU upon suspicion of money laundering or financing of terrorism.

The law of Non-Profit Organisations obliges the NPOs to report in their annual financial statements the names of the donors who provided to an NPO sums above a threshold. The Registrar may exempt

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NPOs from the duty to publicise donor's names in financial statements in special circumstances, but in any case this information is held at the Registrar's office and is available to law enforcement. More in depth inspections and verification of submitted data regarding the identities of donors is carried out once every several years in the framework of in-depth accounting inspections.

#### The need for sanctions

There exist a number of sanctions which can be imposed upon non-profit organisations for not submitting documents to the Registrar of Non-Profit Organisations in accordance with the law. The Registrar of Non-Profit Organisations issues annual certificates of proper management to most active associations. An association cannot receive a certificate if it has not submitted for the relevant year the documents required by law. Recently, the Registrar of Non-Profit Organisations has begun to impose the sanction of administrative fines on associations which have not submitted documents in accordance with the law. The fines are levied in accordance with the law which established administrative fines, and in accordance with regulations. In other cases, when an association does not submit documents and there is an indication that it possesses property, the Registrar of Non-Profit Organisations can engage in legal proceedings and move the court to liquidate it.

#### The need for cooperation

In Israel, arrangements for domestic co-ordination, co-operation and information sharing in this area have been developed between the supervisors, the tax authorities, the Police, the Security Services and FIU on a case by case basis. There are also written procedures between some of these bodies (including memoranda of understanding).

## Conclusions

It is clear that the NPOs may be vulnerable to abuse by terrorists for a variety of reasons: they enjoy the public trust; they have access to considerable sources of funds; they are often cash-intensive; they may have a global presence which provides a framework for national and international operations and financial transactions etc

Depending on the legal form of the NPO and the country, NPOs may often be subject to little or no governmental oversight, or few formalities may be required for their creation. Terrorist organisations have taken advantage of these characteristics of NPOs to infiltrate the sector and misuse NPO funds and operations to cover for or support terrorist activity.

The experience of MONEYVAL third round mutual evaluations report shows that a series of key elements could lead to an enhanced protection system against abuse of the NPO sector:

- Licensing/registration
- Controls and monitoring
- Sanctions for non compliance
- Public awareness
- Increasing transparency
- National risk assessment
- Systems in place for efficient reporting
- Cooperation between public agencies and private sector

It is also necessary that all stakeholders understand that preventive measures should be adopted by countries in order to protect the NPO sector from terrorist abuse and that they should not disrupt or discourage legitimate charitable activities. They should promote transparency and engender greater confidence in the sector across the donor community and the general public that charitable funds and services will and do reach intended legitimate beneficiaries.

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## NPOs and Terrorism in Latin America and the Caribbean: Legal Framework, Red Flags and Case Studies

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### Introduction: legal framework and main characteristics of NPOs in the region

When we refer to terrorism financing, we refer to the way in which terrorists sustain themselves, their operations and their day to day, economically, through monetary and financial instruments of any kind. In the legal sphere, the international community arrived at a consensus around the definition of the crime of terrorism financing through article 2 of the International Convention for the Suppression of the Financing of Terrorism (1999) [\[LINK\]](#). Additionally, this Convention, in article 5, obliges State Parties to adopt all necessary measures to hold liable—in a criminal, civil or administrative way—any legal entity located in its territory or organized under its laws that commits an offense set forth in article 2.

Non-Profit Organizations (NPOs), according to the definition of the Financial Action Task Force (FATF) are “a legal entity or organization that primarily engages in raising or disbursing funds for purposes such as charitable, religious, cultural, educational, social or fraternal purposes, or for the carrying out of other types of “good works.” [\[LINK\]](#) Therefore, NPOs fall under the scope of article 5 of the 1999 Convention.

Despite the preventive legal measures put in place by the international community, the tragic attacks of September 11, 2001 served as a wake-up call in the fight against the financing of terrorism. Particularly, NPOs and other charitable institutions, as sources of funding, were shaken to their core: It is believed that 9/11 attacks and the cells that participated were mainly financed through the *Zakat* or *Zadakat*—a charitable legal institution through which Muslims are required to pay 10% of their business earnings and savings—in amounts estimated at 300 to 500 million dollars in a period of ten years.[1]

Undoubtedly, NPOs are a very attractive option for terrorists to fund their activities. These organizations, particularly charities, have the public’s trust, they are a growing sector worldwide both economically and politically, they have access to considerable and diverse sources of funding, they circulate large amounts of cash, they usually operate both at the national and international levels, they frequently have offices close to deprived or socially marginalized areas—where criminals feel more comfortable operating. Often, NPOs are not subject to as strict regulation and are easy to set up as they are seen to conduct beneficial social work with resources outside the reach of governments. Therefore, in developing countries of the Latin America and Caribbean region, as in other developing countries, the risks associated with NPOs’ characteristics tend to increase.

As a consequence of 9/11, the United Nations Security Council decided to take a step forward and adopt—under chapter VII of the Charter—resolution 1373 of September 28, 2001 [2]. The resolution begins its operative section—which shows the importance of the topic—emphasizing the need to prevent and suppress the financing of terrorism, criminalizing it (reproducing almost the same formula of article 2 of the 1999 Convention), freezing without delay funds and related assets related to terrorism, and taking measures against the people and *entities* that participate in the financing plot.

Coincidentally, on September 11, 2001, the Ministers of Foreign Affairs of the Americas were meeting to adopt the Inter-American Democratic Charter, and did not hesitate to condemn the attacks and initiate the steps to adopt specific Inter-American measures against terrorism. On June 3, 2002, all Member States of the Organization of American States (OAS) adopted the Inter-American Convention against Terrorism in Barbados [\[LINK\]](#). The Inter-American legislator understood the importance not only of

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creating a comprehensive and complementary regional framework to the universal one—especially through article 2, which specifically refers to it—but also of establishing sound counter-terrorism financing obligations for State Parties. The first operational section of the Convention, articles 4 to 6, deals with measures to prevent, combat and eradicate the financing of terrorism, seize and confiscate funds and assets, and establish terrorism financing as a predicate offense to money laundering—a measure that was innovative for an international counter-terrorism treaty as it was not part of the 1999 Convention. Article 4.1.a specifically obliges Parties to institute or develop a “*comprehensive regulatory and supervisory regime for banks, other financial institutions, and other entities [stress is ours, as it includes NPOs] deemed particularly susceptible to being used for the financing of terrorist activities.*”

Since 2002, 25 OAS Member States out of 35 have ratified the Inter-American Convention against Terrorism. Although its implementation is still under way and has been uneven, there are good examples in the region of national counter-terrorism financing legislation that has been drafted, sometimes with the support of the CICTE Secretariat and other technical assistance providers—partners such as the United Nations Office on Drugs and Crime (UNODC) and the Financial Actions Task Force of South America (GAFISUD)—, in full accordance with the universal and regional legal framework and other international standards, specially FATF’s 9 Special Recommendations, adopted in October 2001 and updated in October 2004 [[LINK](#)]. It is worth mentioning, as models in different topics and aspects, counter-terrorism financing legislation from Colombia, Costa Rica, Honduras, Peru, and Uruguay, among others.

In regard to NPO’s, Panama has developed over the past years a good legislative model by which only legal persons with ministerial authorization—i.e. license—can lawfully collect funds and economic resources for religious, charitable or cultural purposes. Additionally, there are specific requirements that must be met by associations in order to be recognized as legal persons and proceed to open accounts. Such legal persons are monitored and their transactions analysed by the Financial Intelligence Unit (UAF, by its initials in Spanish). Furthermore, article 3 of Act 50 (July 2, 2003), states that “*Non profit associations shall have an obligation to keep track of any funds that they receive, generate or transfer.*” To that end, they must keep a detailed record of financial operations or transactions and donations, verifying the origin and nature thereof [3]. Finally, Executive Order No. 524, issued on 31 October 2005 pursuant to article 3 of Act No. 50 of 2 July 2003, regulates recognition of legal status of private non-profit organizations and foundations. [4]

### Typologies and red flags

A “typology” could be defined in the anti-money laundering and counter-terrorism financing (AML/CFT) context as the method or technique that criminal and terrorist organizations use to confer an appearance of legality to the money used to finance their activities. Among other things, typologies are used to identify the modus operandi and criminal patterns of these organizations, which in turn allow us to conduct sound analytical investigations and build the capacities to fight terrorism financing.

Hence, the use of typologies creates a virtuous cycle that analysts use to examine a case or to illustrate it as a way to improve overall understanding of how the criminal scheme may be operating. This virtuous cycle comes to an end when the investigator realizes that the typology used by the criminal organization cannot be associated to an already known one, or when the case presents variations from the typology that has been used as guidance—making it necessary to modify it or to create a new one. There are not many terrorism financing typologies per se, as there are few successfully prosecuted and well documented cases. However, typologies linked to money laundering can usually also be applied to terrorism financing due to certain similarities between the two crimes, especially in regard to how assets or financial instruments are transferred, transported or converted into other assets as in the “placement” phase in the money laundering cycle.

In regard to NPOs, identified typologies have traditionally been linked to the way in which shell—or front—companies operate when laundering assets. This comparison is useful to draw similarities on how they



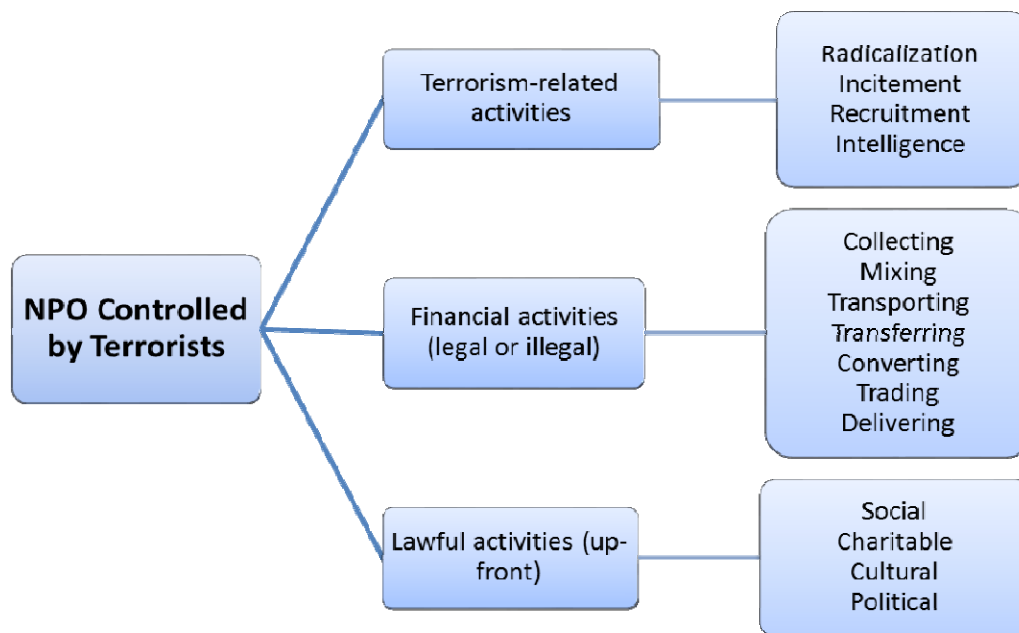
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constitute themselves, but is worthless when examining their transactional behavior or how they pursue their corporate purpose, as they are radically different. For instance, some of the better known cases of NPOs used by terrorists [\[LINK\]](#) show that these organizations not only help them raise, place and change the nature of funds to finance their activities, but also allow terrorists to meet their radicalization, recruitment and incitement goals—something quite unique that sets these typologies apart from the already existing ones.



For each of the financial services mentioned in the diagram, the terrorist organization can conform to complementary typologies to take advantage of the vulnerabilities of the system (normative as well as those inherent to financial products), according to variables of the environment such as the financial products used, the availability of front companies and supporting networks, or the place in which they will be used.

The complexity of the operations associated with NPOs related to terrorist organizations (taking into account their clandestine nature), results in one operation with various typologies, depending on the needs of the organization and the available resources. This complexity makes their detection more difficult and increases the relevance of exhaustively documenting its activities and swiftly addressing red flags (warning signs) that allow us to identify them.

Some of the typologies that could be linked to NPOs are the simulation and structuring of donations (“smurfing”), originated locally or abroad; the development of operations of foreign exchange arbitration mixing legal and illegal assets; open smuggling operations carried out by terrorist organizations taking advantage of mobility corridors used by them or criminal partner organizations; cross border bulk currency smuggling [5]—including cash and new payment methods such as pre-paid value cards; and the use of other illegal methods such as extortion or kidnapping [6], in order to facilitate or generate their financing.

How can we develop a preventive system to disrupt these terrorism financing schemes? A first step would entail developing an early-warning system for suspicious NPOs, which would in turn depend on identifying red flags. Red flags are particular behaviors and atypical situations that present themselves in transactions of clients or users of obligated entities that could be linked to illegal activities. Thus, red flags facilitate the identification of operations potentially associated with the financing of terrorism by linking them to previously mentioned typologies.

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Like typologies, these warning signs are compiled based on the analysis of cases that have been previously investigated and/or prosecuted. However, their usefulness truly depends on the expertise and knowledge that investigators and analysts must have to identify them when confronted by a specific case—for instance, in reports sent by obligated entities related to operations potentially associated with the financing of terrorism.

Red flags related to NPOs include:

- NPOs whose corporate purpose does not pertain to the place in which it carries out its activities;
- NPOs that despite being tax exempt do not take advantage of that benefit;
- The transfer of money between local and foreign NPOs that because of the quantity, destination, or corporate purpose do not fit the characteristics of the NPO from which it came;
- NPOs that suddenly show a significant increase in volume or amount of incomes;
- NPOs that after remaining financially inactive for some time make transactions for sums significantly higher than usual;
- NPOs that keep their financial products funded for very long periods of time;
- Financial products under the name of the NPO that present a high volume of cash transactions;
- NPOs that despite developing projects for high sums of money do not have either the employees or the capacity to execute those projects;
- NPOs that open financial projects with hardly verifiable personal and/or commercial references, or whose partners or legal representatives are never in the country;
- NPOs which use a name that suggests a relationship with another recognized NPO or is similar to another NPO in order to deceive potential donors or clients;
- NPOs that often make changes in its shareholders, legal representatives, and/or administrators;
- NPO employees or executives that claim to work for the organization but do not have legal permits to work in that country;
- NPOs that are lawfully constituted but manage its financial resources through the personal bank accounts of its executives or employees, thus avoiding opening financial products on behalf of the NPO as such.

From the financial intelligence analysis point of view, investigators should carefully handle any information linking NPOs to terrorist organizations, as some red flags could also point to a money laundering scheme deprived of any terrorist component. Consequently, law enforcement agencies and investigators play a crucial role in linking money laundering schemes to terrorist organizations or plots, and analysts and investigators can only put the pieces together and build a case that can successfully be prosecuted if information is exchanged at both the strategic and operational levels.

Nevertheless, NPOs represent an investigative challenge. This complexity calls for an integrated approach that requires efficient public-private partnerships as a component of any preventive system. In this regard, it is worth praising the European Commission’s current effort in drafting voluntary guidelines to establish an auto-regulatory NPO regime that aims to address risks related to the financing of terrorism by increasing information and transparency [7]. It seems to us that this model should be followed closely and, based on its results, even adapted and exported to the Latin American and Caribbean region.

### Case studies

Once the legal context and main characteristics of terrorist-controlled NPOs have been laid out, it seems important to assess what has been the practical impact of the theoretical instruments developed in the last twenty years. To this end, we will chronologically present two case studies with NPO implications, linked to terrorist groups in Latin America. The first case refers to the use of educational organizations

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by the Peruvian terrorist group Shining Path (*Sendero Luminoso*) in the 1990s [8], and the second one involves a Spanish-based NPO, headed by an alleged member of the terrorist group Revolutionary Armed Forces of Colombia (FARC by its acronym in Spanish), which has been under investigation for the last couple of years [9].

1) Albeit “Cesar Vallejo” and “ADUNI” were preparatory academies officially aimed at helping students pass pre-college tests, both academies were used in the 1980s and 1990s by Shining Path to finance its activities, to serve as logistical centers for the terrorist organization, and to incite, recruit and radicalize young individuals.

As the evidence proved during the prosecution of the case, the heads of both academies, Luís Manrique Lumba, Alfonso Joel Ascencio Borja and Luís Alberto Aguirre Gómez, gave Shining Path’s directorate cash and other financial instruments through different intermediaries. The three of them were aware of Shining Path’s structure and aims, they were aware that the money given was being used to finance Shining Path’s activities, and one of them was a member of the organization and even held a face-to-face meeting with Mr. Abimael Guzmán, leader of the terrorist group.

This behavior would clearly fall under article 2 of the 1999 Terrorist Financing Convention, as they were “directly or indirectly, unlawfully and willfully” providing and collecting funds with the intention or knowledge that they will be used to carry out terrorist offenses. As the academies were legal entities, the scope of application of the international legal regime would have also reached the entities as such under article 5 of the 1999 Convention, and article 4.1.a. of the 2002 Inter-American Convention against Terrorism. Unfortunately, both legal instruments did not exist when the offenses were committed. Therefore, the offenders were prosecuted according to legislation in force in Peru at the time of the commission of the offense. For this same reason, the legal entities as such were neither prosecuted nor sanctioned criminally, civilly, or administratively, and are still today functioning—without any known links to Shining Path or its members, though.

Should a similar case occur today in a country in which international legal standards have been implemented, prosecutors would find it much easier to find support in a variety of legal tools to bring to justice not only the persons responsible for the management or control of the entity—probably under harsher penalties—but also the legal entity as such.

Finally, it is worth stressing that although these academies were not, strictly speaking, NPOs, the case is very relevant for our purposes as it follows typologies characteristic of NPOs—e.g. the educational purpose of the institution to cover terrorist objectives such as radicalizing, indoctrinating, inciting and recruiting students. Additionally, certain characteristic red flags mentioned earlier could have been identified in the NPO’s financial information: financial products funded for very long periods of time; high volume of cash transactions; and not having either the employees or the capacity to execute its corporate purpose.

2) In 2008 an NPO called “Redvivar”—headed by an alleged member of political wing of the Marxist Terrorist Guerrilla FARC, Jaime Cedano Roldán—was granted 81,378 euros to conduct a development project in Puerto Brasil, a rural area in Colombia. The Foundation that granted this funding—which came in turn from a Fund of the municipality of Sevilla, Spain—was “DeSevilla”, a local political Foundation headed by Antonio Torrijos, a member of Spain’s communist leaning party Izquierda Unida.

In this case, in addition to a typology commonly used by terrorist-controlled NPOs [10]—i.e. a request for funding to undertake a development project—there are a number of red flags that should have been addressed: the head of the NPO had been one of the heads of the extinct “Union Patriótica”, a political wing of FARC; the development project was vaguely described and its objectives were not clearly defined; the authorities of the beneficiary area of the project, Puerto Brasil, Viotá, Cundinamarca, Colombia, were not aware of the project; the proposed development projects were not in line with usual economic activities in the region—i.e. mostly seasonal and weekend tourism; and finally, as of October 2010, no spending details or invoices had been provided by Redvivar or DeSevilla.

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Although the case is still under investigation, it should be made clear that, contrary to the Peruvian academies case, nowadays analysts, investigators and prosecutors have a larger number of tools to effectively address alleged criminal activity. In addition to the international legal instruments in place and their applicable provisions, Colombia and Spain are two of the countries with the most developed counter-terrorism and counter-terrorism financing legislation in the world. Moreover, Colombia and Spain effectively cooperate and exchange information with one another [11], which are certainly key aspects to ensure a successful investigation and prosecution of any terrorism financing case.

### **Conclusion: some recommendations to strengthen a preventive approach**

As the legal framework and the analysis of cases show, the Latin America and Caribbean region has developed different tools to prevent terrorists from using NPOs to fund their activities and to serve as recruitment and indoctrination entities. There has been significant progress in this area.

Although this preventive system has been positively developed, several challenges remain. For one, from the legal perspective, many countries in the region still have to adopt as national legislation, and develop through different regulations, the tools that the international framework offers. Furthermore, full implementation of available tools will also require—to ensure maximum effectiveness—strengthening international cooperation and enhancing, both from a quantitative and qualitative perspective, the exchange of information among all stakeholders from the private and public sectors, as well as from the national and international level. This cooperation is paramount to the swift detection, investigation and successful prosecution of individuals and NPOs linked to terrorist organizations.

The provision of any kind of material support to these criminals should be strongly discouraged, regardless of any charitable or social purpose the terrorist-controlled NPO may have, through sound and tailored legal regimes, comprehensive and sustained capacity-building programs for public and private sector officials, and constant exchange of information and cooperation with international partners.

Until that holistic framework is fully achieved, other preventive measures should be immediately implemented as a first step. The lack of legislation related to NPO supervision in most countries of the Latin American and Caribbean regions should be temporarily addressed by the public sector through the adoption of relevant international best practices and standards—e.g. through operational manuals, guidelines or regulations. Along the same lines, NPOs should implement self-regulating mechanisms aimed at increased transparency of their activities, thus building public confidence. Finally, financial institutions should implement specific procedures when doing business with NPOs—knowing their clients (legal representatives, stakeholders, and even donors) through reinforced due diligence procedures; creating risk-profiles and risk-managing NPOs financial portfolios as they do with Politically Exposed Persons (PEPs) [12]; familiarizing themselves with typologies and red flags related to NPOs; improving reporting mechanisms to relevant authorities,

Most economies of the Latin American and Caribbean regions are expected to grow at an average projected real GDP of above 4%, and many of them of above 6% [13]. Should the growth be sustained and political stability ensured, significant growth of the middle class will most likely ensue in the middle to long run. In turn this will strengthen civil society, increasing the number of organizations, foundations and associations in the region [14], and their financial resources. Latin American and Caribbean countries must be ready to benefit from these expected increases, but also remain vigilant and prepared to address its challenges. We must not allow terrorists to use NPOs for their purposes. Let's get ready before it is too late.

#### **End Notes:**

[1] Practical Guide to the Prevention, Detection and Suppression of Terrorist Financing; Inter-American Committee against Terrorism, Organization of American States; ed. 2006-2007; p. 147

[2] “(d) Prohibit their nationals or any persons and entities within their territories from making any funds, financial assets or economic resources or financial or other related services available, directly or indirectly, for the benefit of



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persons who commit or attempt to commit or facilitate or participate in the commission of terrorist acts, of entities owned or controlled, directly or indirectly, by such persons and of persons and entities acting on behalf of or at the direction of such persons;” S/RES/1373 of September 28, 2001 [\[LINK\]](#). In relation to the fight against the financing of terrorism it is also worth mentioning the S/RES/1267 (1999) regarding al-Qaeda and the Taliban.

- [3] Republic of Panama, Act 50 of 2 July 2003, Official Diary of the State n. 24.838, which legislates on and criminalizes terrorist and terrorist financing offenses modifying Title II, Book II of the Criminal Code. Art. 3 stipulates: “Non-profit organizations shall have the obligation to keep records of the funds they receive, generate or transfer. To that end, they shall keep detailed log of all financial operations and transactions and of donations, substantiating their origin or nature.
- [4] Executive Order No. 524 issued on 31 October 2005 pursuant to article 3 of Act No. 50 of 2 July 2003 regulates recognition of the legal status of private non-profit organizations and foundations. This Executive Order empowers the Ministry of Interior and Justice to recognize or deny recognition of the legal status and oversee the operations of private non-profit organizations and foundations; churches, congregations and other religious communities or organizations; federations and any other organization not concerned with sports, agriculture, cooperatives or labour matters. It also authorizes the creation of an office under the Ministry of the Interior and Justice for the purpose of keeping records of the activities of non-profit organizations and foundations.
- [5] In the Latin America and Caribbean region, it is interesting to study how criminal networks operate smuggling money and goods, especially at the US-Mexico border. A remarkable study on this topic has been co-authored by the U.S. Immigration and Customs Enforcement (Department of Homeland Security/ICE) and the Mexican government (Secretaría de Hacienda y Crédito Público, SHCP) [\[LINK\]](#).
- [6] Daniel Benjamin, Co-ordinator for Counter-Terrorism at the U.S. State Department recently noted in an interview with the Financial Times that “al-Qaeda groups were increasingly financing themselves through kidnappings, with terrorist organisations netting more than \$100m from ransoms in recent years.” Financial Times, May 9, 2011, available at: <http://www.ft.com/cms/s/0/e064f490-7a65-11e0-af64-00144feabdc0.html?ftcamp=rss#axzz1LyuyYrzw>
- [7] Cf. “EU prepares voluntary anti-terrorist financing guidelines for non-profit organizations” (10/06/2010) <http://www.efc.be/EUAdvocacy/Pages/Transparencyandaccountability.aspx> ; and DISCUSSION PAPER 3rd conference on “Enhancing Transparency and Accountability of the Non-Profit Sector” on 2 July 2010 in Brussels. Voluntary Guidelines for EU based non-profit organizations [\[LINK\]](#).
- [8] The authors would like to thank Peruvian Senior Prosecutor Ms. Luz del Carmen Ibáñez, who provided us with the details of the case. Prosecutor Ibáñez was one of the main prosecutors in the “Mega-Process” conducted against Abimael Guzmán and the leaders of Shining Path (Exped. 560-2005 and subsequent).
- [9] Sources: ABC newspaper (04/03/2009) [http://www.abc.es/hemeroteca/historico-04-03-2010/abc/Internacional/el-ayuntamiento-de-sevilla-subvenciona-a-un-terrorista-de-las-farc\\_1134220875651.html](http://www.abc.es/hemeroteca/historico-04-03-2010/abc/Internacional/el-ayuntamiento-de-sevilla-subvenciona-a-un-terrorista-de-las-farc_1134220875651.html); El Mundo newspaper (18/03/2009) [http://www.elmundo.es/elmundo/2009/03/18/andalucia\\_sevilla/1237363677.html](http://www.elmundo.es/elmundo/2009/03/18/andalucia_sevilla/1237363677.html); ABC newspaper (06/07/2009) <http://www.abcdesevilla.es/20090706/sevilla-sevilla/redvivir-presenta-ahora-proyecto-20090706.html>; ABC newspaper (11/10/2010) <http://www.abcdesevilla.es/20101011/sevilla/exige-aclare-destino-dinero-20101011.html>.
- [10] For instance, Hamas social and community assistance projects.
- [11] Particularly some investigations about the FARC-ETA connections in Spain and Colombia.
- [12] For PEPs see FAFT definition [\[LINK\]](#): ““Politically Exposed Persons” (PEPs) are individuals who are or have been entrusted with prominent public functions in a foreign country, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, important political party officials. Business relationships with family members or close associates of PEPs involve reputational risks similar to those with PEPs themselves. The definition is not intended to cover middle ranking or more junior individuals in the foregoing categories.”
- [13] See International Monetary Fund, April 2011, World Economic Outlook. Latin America and the Caribbean: Average Projected Real GDP Growth during 2011-12 (percent) [\[LINK\]](#).
- [14] Although precise data is difficult to obtain, according to the World Association of Non-Governmental Organizations (WANGO, [www.wango.org](http://www.wango.org)), there are currently around 1360 NGOs in the Latin-America and Caribbean region.

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## Respecting freedom of association while countering terrorism

*Organization for Security and Co-operation in Europe, Office for Democratic Institutions and Human Rights*

### Context

The international community is in agreement that the protection and promotion of human rights is essential to the success of any counter-terrorism strategy. The OSCE Charter on Preventing and Combating Terrorism and the United Nations Global Counter-Terrorism Strategy have emphasized two points: counter-terrorism measures must respect human rights and; protecting and promoting human rights is essential to reducing conditions which may engender support for terrorism and/or terrorist recruitment. A number of studies have confirmed a correlation between poor human rights protection and terrorism.

The OSCE regards human rights as an integral element of security and considers that combating and ultimately overcoming terrorism will not succeed if the means to do so are not in conformity with human rights standards. In this perspective, the Office for Democratic Institutions and Human Rights (ODIHR), which is the OSCE Institution assisting OSCE participating States in implementing their human dimension commitments, takes a principled but practical approach to supporting the participating States in their efforts to develop effective human-rights compliant counter-terrorism legislation, policies and practices.

Yet countering terrorism while upholding human rights is easier stated than put into practice. As recent years have demonstrated, counter-terrorism policy makers have been, perhaps understandably, tempted to focus on security measures but neglected the task of developing a comprehensive, human-rights compliant approach.

In this context, freedom of association that is guaranteed under a number of international instruments, such as the International Covenant and Civil and Political Rights (ICCPR); the United Nations Declaration on Human Rights Defenders and OSCE commitments may at times have been jeopardized. Far from being a hindrance to countering terrorism, respecting freedom of association is a tool to achieve security. Government authorities should acknowledge that Non Governmental Organizations (NGOs) are generally recognised as making an essential contribution to the development and realisation of democracy and human rights. The significance of involving civil society in a comprehensive and multidimensional response to the threat of terrorism has been stressed by various international documents and NGOs have an important and meaningful role to play in preventing terrorism and addressing its root causes.

This contribution aims to highlight OSCE commitments on freedom of association and challenges faced by States and NGOs as a result of countering terrorism, in particular when it comes to its financing.

### The right to freedom of association in practice

An association is a voluntary grouping of people for a common goal. Freedom of association enables citizens to join together without interference by the state in order to achieve various ends.

Freedom of association is a fundamental right and not something that must be granted by the government to individuals. Requirements to register or obtain a license for the association are compatible with human rights standards as long as these schemes do not impair the activities of the association.

The scope of freedom of association includes:

- Right to have a multitude of NGOs working in the same field: Freedom of association encompasses the right to set up an organisation in an area of activity, even if other organisations

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doing similar work already exist.

- Freedom from direction by public authorities applies to the decision to establish an NGO, the choice of its objectives, the way it is managed and the focus of its activities.
- Presumption of legality: The fundamental principle for policy makers and legislators to be respected, when developing legislation that may impact on freedom of association, is that NGOs should enjoy the presumption that any activity is lawful in the absence of the contrary evidence.

Therefore,

- NGOs should conform to democratic principles. They should not seek changes through violence and should not resort to unlawful means;
- NGOs should not be banned for pursuing unpopular causes or causes which oppose state policies as long as their actions are peaceful and lawful.

### Restrictions to freedom of association

The right to freedom of association may be subjected to interference in order to protect important state's interests, such as national security and the rights of others. For example, one person's right to association may conflict with the state's interest in protecting national security by preventing terrorist financing.

However, grounds for restriction cannot be interpreted loosely. States are required to strike a permissible balance between competing interests and any interference with the right to freedom of association must satisfy several tests:

- Legality: there must be a sufficiently precise legal basis for the interference which contains a measure of protection against arbitrariness;
- Necessity: the interference should correspond to a “pressing social need” and, in particular, that it is proportionate to the legitimate aim pursued. The legitimate aims are included in the provisions of the European Convention for the Protection of Human Rights and Fundamental Freedoms (i.e. national security, public safety, protection of the rights of others).
- Proportionality: The European Court of Human Rights usually asks three questions in this regard:
  1. whether the measure is “suitable” or appropriate to the legitimate aim being pursued;
  2. whether there are less restrictive ways of achieving the same purpose; and
  3. whether the cost to the right is justified by the benefits to the pressing social need.
- Non-discrimination: finally any interference must not be discriminatory.

To address the legitimate concern of terrorist financing, States have introduced lists proscribing/sanctioning terrorist organization or individuals in order to curtail and/or control the financing of terrorism such as the Consolidated List of proscribed organisations maintained by the 1267 Sanctions Committee established pursuant a United Nations Security Council Resolution. Once an organisation is included on the Consolidated list, all United Nations member States are obliged to freeze its assets, among other sanctions. Such listing has an impact on fundamental freedoms, including freedom of association:

- Listing has consequences for “members” of organizations, but it is not always evident who is or is not a “member” of an organization or who is involved or not in terrorism;
- In addition, listing makes it a crime to provide funds to a listed organization. Many NGOs have complained that the listing regime has had a chilling effect on charitable donations, especially to Muslim charities. Certain governments have sought to alleviate this problem through the creation of lists of “approved” organizations, but these efforts have also been criticized as interfering with the freedom of association;
- Listing and freezing of assets in the absence of a possibility to challenge the decision may violate freedom of association and due process.

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### Access to funding

Access to funding is an inherent element of the right to freedom of association. Without funding, an organization would not be able to operate and pursue its objectives. However, the possibility for NGOs to collect funds is not absolute and may be subject to regulation, with a view to protect the targeted audience.

The United Nations Declaration on Human Rights Defenders stipulates that NGOs can solicit, receive and utilise resources for the express purpose of promoting human rights through peaceful means. The Council of Europe Fundamental Principles recall exactly the same principles, and the United Nations Human Rights Committee indicates that control of funding would have to be consistent with article 22 of the ICCPR.

The Special Recommendation VIII on International Best Practices on Combating the Abuse of Non-Profit Organizations developed by the Financial Action Task Force of the Organization for Economic Cooperation and Development (OECD) reiterates the following fundamental principles that are covered by article 22 of the ICCPR and the Council of Europe standards:

- Legitimate activities of NGOs are not restricted; and
- Government oversight should be flexible, effective and proportionate to the risk of abuse.

### Transparency, Accountability and Self-regulation

NGOs can be subjected to various obligations to ensure the transparency of their activities, which may also be supervised by one or more relevant public authorities. However, such obligations should only apply to NGOs receiving some form of state's support. Furthermore, supervision should be based on the presumption that the activities of such organizations are lawful and that self-regulation is prioritized. Accountability and transparency can be tempered by other obligations relating to respect for privacy and confidentiality. When in exceptional cases, the general interest may justify having access to private/confidential information and therefore interfering into the internal affairs of an NGO, the principle of proportionality should come into play.

To address abuse of NGOs by terrorist organizations, NGOs have been developing over the years some accountability mechanisms as a means to retain public trust and credibility such as:

- NGOs are accountable to their members. In this regard, one accountability mechanism is to submit annual reports on accounts and activities;
- NGOs are also accountable to state institutions in case they benefit from public support or preferential tax treatment; and
- NGOs are accountable to donors to whom they have to provide reports regarding their spending.

### Conclusion

Terrorist financing represents a challenge for states' security and stability. Therefore, states have a legitimate interest in regulating NGOs in order to guarantee respect for the rights of third parties. International human rights standards provide all the necessary elements for regulating NGOs.

Such regulation of NGOs is certainly a means to prevent the abuse of NGOs for illegitimate purposes, such as terrorist financing. Cooperation between state authorities and NGOs is also key to ensure that the legislative framework put in place serves its purpose: allowing NGOs to fulfil their objectives and the state to protect the interests of others. In this regard, involving NGOs in the process of public policy formulation can certainly enhance the implementation of the legislation. Most importantly, the guiding principle the authorities should abide by when regulating the activities of NGOs is the following: failing proof to the contrary, NGOs' activities are lawful. In case limitations are imposed, they must be consistent with the principle of proportionality.



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Protecting freedom of association and countering terrorist threats are not conflicting goals but complementary and mutually reinforcing. The valuable role and expertise of civil society in addressing conditions conducive to the spread of terrorism and countering terrorism cannot be overemphasized. In the OSCE framework, the 2002 Charter on Preventing and Combating Terrorism recognised that it was vital to engage civil society in finding common political settlement for conflicts and to promote human rights and tolerance as an essential element in the prevention of terrorism and violent extremism. States should not miss the opportunity to enhance their cooperation with civil society when countering terrorism and thus, to foster freedom of association.

#### End Notes

- [1] Article 22 of the ICCPR is the main binding instrument, ICCPR is ratified by most states and reads as follows: “1. Everyone shall have the right to freedom of association with others, including the right to form and join trade unions for the protection of his interests. 2. No restrictions may be placed on the exercise of this right other than those which are prescribed by law and which are necessary in a democratic society in the interests of national security or public safety, public order (ordre public), the protection of public health or morals or the protection of the rights and freedoms of others. [...]”
- [2] The UN Declaration on Human Rights Defenders includes into freedom of association: (I) the right to form, (II) the right to join, and (III) the right to participate in associations.
- [3] 1990 Copenhagen Document: “(9.3) - the right of association will be guaranteed [...]”; (10) [...] the participating States express their commitment to “[...] (10.3) - ensure that individuals are permitted to exercise the right to association, including the right to form, join and participate effectively in non-governmental organizations which seek the promotion and protection of human rights and fundamental freedoms, including trade unions and human rights monitoring groups; [...]”
- [4] The UN Global Counter-Terrorism Strategy on 8 September 2006, affirmed the determination of Member States to “further encourage non-governmental organizations and civil society to engage, as appropriate, on how to enhance efforts to implement the Strategy.” The 2002 OSCE Charter on Preventing and Combating Terrorism, recognised that it was vital to engage civil society in finding common political settlement for conflicts and to promote human rights and tolerance as an essential element in the prevention of terrorism and violent extremism
- [5] Fundamental Principles on the Status of Non-Governmental Organisations in Europe of the Council of Europe: Paragraph 50 of Recommendation CM/Rec(2007)14 of the Committee of Ministers to member states provides: “NGOs should be free to solicit and receive funding - cash or in-kind donations - not only from public bodies in their own state but also from institutional or individual donors, another state or multilateral agencies, subject only to the laws generally applicable to customs, foreign exchange and money laundering and those on the funding of elections and political parties.”
- [6] Human Rights Committee, Concluding Observations on Egypt, CCPR/CO/76/EGY, 28 Nov 2002
- [7] Financial Action Task Force of the Organization for Economic Cooperation and Development (OECD), International Best Practices on Combating the Abuse of Non-Profit Organizations – Special Recommendation VIII: stresses that “government oversight should be flexible, effective, and proportionate to the risk of abuse. Mechanisms that reduce the compliance burden without creating loopholes for terrorist financiers should be given due consideration. Small organizations that do not raise significant amounts of money from public sources, and locally based associations or organizations whose primary function is to redistribute resources among members may not necessarily require enhanced government oversight.”
- [8] See Paragraphs 62 to 72 of the Council of Europe’s Recommendation CM/Rec(2007)14 on the legal status of NGOs in Europe.
- [9] OSCE Charter on Preventing and Combating Terrorism, MC(10).JOUR/2, 7 December 2002, Annex 1, Para. 20. The 2001 Bishkek Programme of Action on Strengthening Comprehensive Efforts to Counter Terrorism also stressed the importance of promoting active civil society engagement in the fight against terrorism.

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## Good governance and AML/CFT compliance in the non profit sector in the United Kingdom and beyond

*Trevor Barratt, Chief Risk Officer, Charities Aid Foundation (CAF)*

In the United Kingdom (UK) not for profit sector, fighting financial crime is regrettably an every day occurrence. Whilst some attempts are clearly amateurish others are highly sophisticated and clearly linked to organised crime, or financing of terrorism and all financial institutions have had to organically grow the defences which are in place to combat these attempts.

It is troubling to realise that organisations solely dedicated to support civil society is targeted the same as firms in the private sector, as criminals and terrorists look for opportunities to achieve their personal aims or make personal gain. Because of this the sector has looked to develop and maintain comparable systems and processes to protect its clients, staff, as well as its own reputation from all aspects of financial crime.

UK based not for profit organisations adhere to the requirements of the UK regime, although many have offices and subsidiaries throughout the world which brings with it an international complexity. As many of these organisations operate in multiple jurisdictions it is necessary to ensure that local laws and regulations are captured, but fundamentally as the UK's Joint Money Laundering Steering Group (JMLSG) guidance is based on FATF recommendations, the base requirements are generic and can be adopted across all jurisdictions, albeit flexed to take account of local requirements.

This article gives an insight in to the practical approach adopted by one particular not for profit organisation, as it continually enhances its fighting financial crime regime.

As with so much, what differentiates a good business from an average business comes down to culture and leadership. The promotion and good governance of anti money laundering and combating financial terrorism is no different. Within the firm a specialist team supports the business in ensuring it adheres to the requirements of sanction regimes and the various fighting financial crime regulations and laws.

Ownership, leadership and accountability starts at Board level, who have signed-off a detailed policy which covers:

1. why fighting financial crime is important and considers the financial impacts, regulatory requirements, personal responsibility and reputational impacts;
2. principles by which the organisation operate, including:
  - adoption of all necessary and appropriate external standards into a Fighting Financial Crime (FFC) framework;
  - monitoring of external pronouncements to ensure continued adherence to requirements to ensure the comprehensiveness of the framework and keep it aligned to regulatory developments and initiatives;
  - agreed processes/practices which are assessed on an ongoing basis to ensure they are compliant and that the controls continue to apply;
  - practices and processes being monitored to ensure adherence using a risk based approach, with oversight being proportionately applied; and
  - change management, ensuring new activities are in line with the organisation's risk appetite and risk maps.

Any changes to the FFC framework/architecture require discussion with the Executive Committee (Ex Com) and Audit, Risk and Compliance Committee (ARCC);

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3. periodic reporting to provide the Ex Com and ARCC and through these committees the Board, thereby ensuring compliance to the policy. Delegation of an over-riding control from the Board to the Money Laundering Reporting Officer so that no person may amend, change, implement or disapply the agreed procedures/controls and practices without the specific written consent of the Money Laundering Reporting Officer (MLRO); and
4. the Board and through delegation of their authority the ARCC and ExCom to provide ongoing leadership and direction with regard to fighting financial crime.

### Legislative and Regulatory Framework

The organisation considers the fighting financial crime arrangements under the following headings:-

- Anti-Money Laundering;
- Combating Terrorist Financing;
- Anti-Bribery and Anti-Corruption;
- Anti-Fraud;
- Whistleblowing; and
- Information Security, Privacy, Data Protection and Identity Theft.

External materials were drawn upon to formulate an appropriate and proportionate statement of ‘requirements’ applicable in fighting financial crime. These external materials include regulatory pronouncements and material from amongst others Financial Action Task Force (FATF), Joint Money Laundering Steering Group (JMLSG), WorldCheck, Transparency International, Serious Organised Crime Agency (SOCA), British Banking Association (BBA), Legislation, Ministry of Justice, Financial Services Authority (FSA) and the National Fraud Authority.

The external materials used also provide a rationale as to why the business practices were necessarily undertaken and help ensure that redundant practices were identified and removed where appropriate.

The materials utilised in this part provide an audit trail leading from those materials to the manuals provided to the business.

### External Monitoring

Resource is utilised to ensure the ongoing comprehensiveness of the FFC control framework/architecture and keep it aligned with current regulatory developments/initiatives. This list includes material provided from Complinet, Regulators, SOCA, HM Treasury, FATF, JMLSG, WorldCheck, Law Enforcement, and the Information Commissioner amongst other sources.

### Ongoing Assessment of Agreed Processes/Practices

Any process maps prepared by the business are assessed for FFC compliance and evidenced as such. Arrangements are established on an ongoing basis to ensure that any new or amended processes/practices are similarly assessed as to their adequacy for FFC. The policy is to match the manual against business processes to streamline, validate and document continuing business processes, and disapply those processes identified as no longer serving any useful purpose.

### Internal Monitoring via Risk Based Methodology

Processes, practices and client facing activity are monitored on an ongoing basis via a risk based methodology.

Ownership of financial crime risks and responsibility for mitigation of those financial crime risks operate at the point where the risks reside (often at the point of interaction with the ‘clientele.’), i.e. the business. A core part of the FFC policy is:

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1. to confirm ownership for FFC;
2. to support the business in managing and mitigating their risks of financial crime; and
3. to require the business to evidence their discharge of FFC responsibilities.

Separate to the business evidencing their discharge of FFC responsibilities (and the oversight and control exercised by senior management over that discharge), independent monitoring processes are undertaken by the Anti-Money Laundering and Risk and Compliance functions to provide additional assurance to the Ex Com and ARCC regarding FFC.

To ensure compliance, the Risk and Compliance Team, independent of the FFC team, undertake regular (monthly) testing across the business to ensure adherence to requirements. This testing has been adapted to be business specific and focuses on higher risk areas where enhanced due diligence is expected.

### Change Management

Change management seeks to ensure that any new FFC activity is undertaken, as agreed, in accordance with the risk appetite and the risk maps.

The Executive Committee and ARCC delegate authority to the MLRO so that ad-hoc improvements to FFC arrangements can be made without prior referral, particularly:-

- to close perceived weaknesses in the control framework;
- to recognise & mitigate perceived risks (or changes in perceived risks);
- to recognise changes in best practice; or
- to implement changes necessary as a consequence of changes in legal and regulatory obligations.

The ARCC/ExCom have delegated the capacity to make such necessary changes to the MLRO on the understanding that any material change to the FFC framework and practices is subsequently reported in accordance with the agreed reporting mechanisms.

### Arrangements for Ongoing Leadership & Direction on FFC

To provide the necessary leadership the Ex Com and ARCC, in conjunction with the Chief Risk Officer, have deliberated carefully upon the question as to what are the most appropriate and proportionate FFC arrangements. To provide appropriate leadership and set an appropriate ‘culture’ the Ex Com and ARCC adopted the FFC Principles and policies and recommended that the Board approved the Policy, which after challenge they duly did. The point regarding challenge is a key aspect of a Board’s role and something that allows the members to discharge their duties effectively.

### Periodic Reporting

The Board sign-off the policy annually and then require a quarterly report that is submitted to the ARCC, which amongst other topics updates on:

- adherence to policy;
- client and transaction screening;
- system matters, including enhancements or system failures;
- FFC Training;
- numbers of suspicious activity reports submitted by the business and onward to relevant agencies;
- any changes to risk profiles for screening.

This is a very comprehensive approach but what really counts is the culture this engenders throughout senior management who witness the engagement the Board members demonstrate.

### Fighting Financial Crime in practice

At the business level, the organisation has a FFC manual, which is based on recommendations of the UK’s Joint Money Laundering Steering Group (JMLSG), an industry body most of which is approved by



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Her Majesty's Treasury (HMT) and recognised by the UK's regulatory authority (Financial Services Authority). Due to the diversity of business units within the organisation, work has been undertaken to 'localise' the manual requirements to ensure they are both specific and relevant for each area. This has largely been achieved through process maps, which are agreed with the business area thereby capturing the specific nuances and requiring sign-off by the FFC Team and the respective business unit senior management team. This approach, whilst initially time consuming, has seen significant business buy-in and acceptance of the requirements.

Key reoccurring themes within the JMLSG documents are 'risk based' and 'proportionality' and the organisation has endeavoured to capture these within the architecture of the approach adopted. As always this brings with it some element of subjectivity which in turn brings differing views, but the level of Board and Executive support has allowed these issues to be pragmatically approached and acceptable processes and procedures to be agreed by the business and the risk teams.

The implementation of enhanced processes and procedures has brought with it a sizable business cost in terms of additional resource and significantly enhanced business practices particularly around Know Your Customer (KYC) requirements, which has seen a significant increase in the level of required documentation and information collection to allow acceptance of new accounts under the increasingly challenging legislative and regulatory requirements.

Whilst the processes for new clients can be adopted and applied relatively quickly, the 'back fill' exercise to ensure adequate KYC acceptance for existing clients is not something that can be completed in a short timeframe to bring all records to the revised standards. The organisation has agreed with its Board a timeframe for completion and has then prioritised using a risk based approach which considers such things as country risk, customer risk, product risk and transaction risk. 'Trigger' events have been identified and agreed, which when they occur, initiate the process.

### Training

As with all organisations regular and ongoing training for staff is undertaken, starting at the induction of new entrants and using a computer based method of videos, screen based information and Q&A's resulting in a final test. This is supplemented by bespoke training which is relevant to specific teams and different levels of management.

### In Summary

So what are the key challenges? Well the significant cost that organisations are burdened with to ensure they continue to effectively manage the fight against financial crime. This manifests itself due to the increasing needs of system enhancements which are required for screening to look for unusual client behaviour or transactional trends which raise alerts. Additional people costs are also an unavoidable consequence of meeting the obligations in the fight against financial crime. These cover everything from enhanced checking during the account opening/relationship commencement stage through to on-going monitoring.

To conclude, the vast majority of institutions and individuals that the not for profit organisation and its subsidiaries interact with do an enormous amount of good work for society's benefit, having a positive impact throughout the world. But, as with all organisations, it recognises the realities of the world in which we live today and has built its processes to mitigate the behaviour of a few; this in turn creates an increased financial burden which has to be balanced against the goal of passing on to the not for profit sector the maximum value possible. Through increasing the understanding of the sector of the requirements and benefits of adopting a fit and proportionate fighting financial crime regime, we can all work together to minimise the success that the few have on society and limit the enormous damage they do.

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## A take on transparency and accountability in the foundation sector

*Emmanuelle Faure, European Affairs Senior Officer, European Foundation Centre (EFC) AISBL*

In the 1990's and early 2000's foundation networks started developing self-regulation initiatives at national and European levels as a means to enhance foundations' governance, develop a mutually beneficial relationship with partners, funders and beneficiaries, forge a more professional sector and support the sharing of good practice and learning. They also aimed at maintaining public trust in the sector while protecting the (operational/political) space in which it operates. To date, over 20 foundation self-regulation schemes can be found at the regional and national levels, and one at European level.

Self-regulation schemes developed by foundations and their networks are not meant to replace legislation, even if their starting point is compliance with the laws of democratic societies and with international conventions, but rather to complement it. The main goals of these initiatives are to improve accountability, advance transparency and promote effectiveness.

These objectives were at the core of the European Foundation Centre (EFC)'s approach to self-regulation, with a focus on core values such as acting in the public benefit, respecting the donors' intentions, securing independence and ensuring the effective use of resources and obligations to multiple stakeholders.

The EFC, the principal European-level umbrella organisation for public benefit foundations, was set up in Brussels in 1989 to promote the work of foundations, improve their operating environment and professional capacity and advance the public good in Europe and beyond through cooperation with a range of partners. Today the Centre gathers some 230 individual foundations from over 30 countries across Europe and beyond, and hosts the secretariat of the network of national associations of foundations from 22 European countries (DAFNE) set up in 2006, representing c. 6,000 foundations.

The Centre is firmly committed to the transparency and accountability of foundations in Europe, as illustrated by its work on EFC standards since 1993. However, the EFC wants to ensure that transparency and accountability measures taken at national and European levels do not hamper the work and development of the sector.

EFC's approach to self-regulation has been threefold: The Centre started by devising a general framework for transparency and good practice through a first code of conduct adopted in 1994 which has been revised twice since then. A second step has been to step up the accountability of foundations in their international work. Finally, in 2009 the Centre partnered with the Donors and Foundations Networks in Europe (DAFNE) to review the state of play of foundations' self-regulation schemes in Europe, take stock of developments and practices, assess challenges in the field, and make recommendations to improve the current frameworks where necessary.

### An embracing framework

The EFC Principles of Good Practice (PGP), revised in 2006, represent a shared vision of good practices and a recommendation to reinforce good practice, openness and transparency in the European foundation community. As such, they are intended to be of application both within the European Union and in the context of the wider Europe, and refer to both the national and international dimensions of a foundation's work.

The foundation sector encompasses a variety of organisations with diverse structures, sizes, cultures, policies and concerns, as well as various activities and procedures. Every foundation in Europe is encouraged to respect the EFC PGP and to use them as guidelines when (re)shaping their formal or informal ways of working. EFC members must adhere to the Principles when joining the Centre. In

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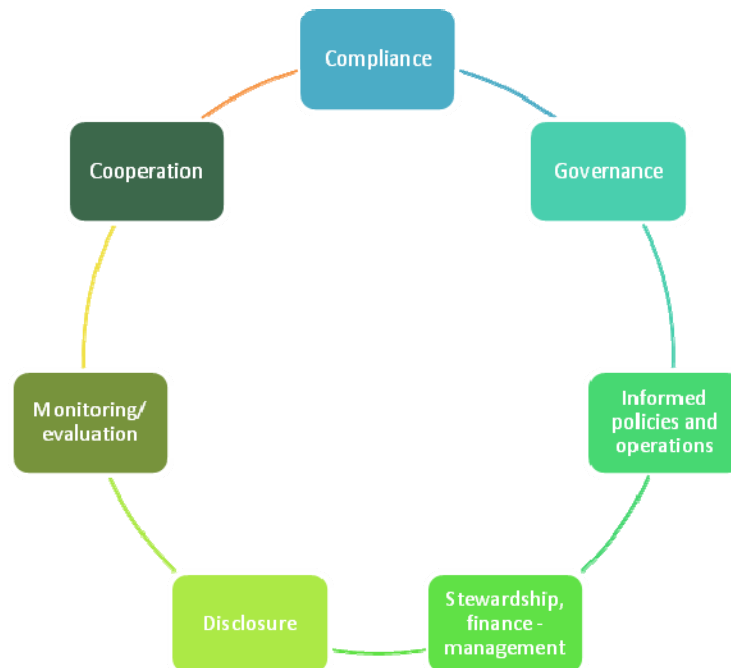
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parallel, the EFC has developed a misconduct and sanction policy which addresses potential cases of breaches of the Principles.

The EFC code consists of a concise set of 7 principles of good practice as shown below:

### EFC 7 Principles of Good Practice



**Figure 1: EFC 7 principles of good practice**

All 7 principles are further defined through concrete illustrative practice options and recommendations. Implementation of the Principles is ensured through the EFC's capacity building and peer learning programme targeted at foundation staff, executives and boards. As of 2011, this work will further benefit from online and in-print resources, toolkits and benchmarks for the professionalisation of foundation practitioners within the framework of GrantCraft, a collaborative partnership between the EFC and the US Foundation Center.

### Stepping up foundations' accountability at the international level

Promoting the accountability of foundations in their international work has been a key priority of the EFC membership. By accountability, we mean a commitment to uphold a foundation's core mission, serve the public good, engage and inform stakeholders, and assure positive impact. In 2005, the Centre joined forces with the Council of Foundations - its peer organisation in the US and concerned international stakeholder - to develop a set of stewardship principles and guidelines for accountable international grantmaking and operating activities that are relevant to their respective memberships as well as the broader international donor community.

The Principles of Accountability for International Philanthropy are voluntary and aspirational, complementing the EFC's "Code". They aim to guide foundations in their cross-border work and cover the following areas: integrity, understanding, respect; responsiveness; fairness; cooperation and collaboration; and effectiveness. They also include a set of good practice options which illustrate the steps and approaches to implement the principles, and a resources section covering leading institutions, studies and tools addressing this topic.

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#### 2009 EFC - DAFNE joint initiative on accountability and transparency

In 2009, the EFC and DAFNE launched a new collaborative project to map and analyse the regulatory frameworks for and use of self regulation mechanisms by foundations in Europe and other DAFNE member countries (30 countries in total are looked at: EU 27, plus Switzerland, Turkey and Ukraine).

The project, which will be completed by the end of 2011, will enable the identification and documentation of practices in different countries and in a cross-border context as well as ensuring cross-fertilisation of knowledge, sharing best practices and developing genuine European benchmarks for foundations active both at national and international level. In addition to the published study, the project will deliver opportunities for discussion of and peer learning based on the results of the analysis, including the possibility of developing grant risk management guidelines for foundations to help public benefit foundations deter and detect external grant fraud.

EFC’s work and experience in the field have found that all self-regulation systems reflect a specific context, and hence need to be updated as the context changes. Their success comes from the high degree of buy-in from their concerned constituencies. The challenges in the implementation of a Code/self-regulation mechanism is not so much (as one would think) how to monitor compliance but the capacity and the resources to develop the various appropriate tools that can help the organisations and their staff to comply with the codes. In this sense the responsibility of umbrella organisations and networks is not to turn into watchdog or rating agencies, this is not their role; they should be facilitators, and benchmark developers. Furthermore, compliance costs (monitoring, certification, disclosure) should not be underestimated. Compliance requirements and practices should be proportionate to the size, activities and “risk-appetite” of the organisations concerned.

Under no circumstances should compliance requirements set out by regulations or even self-regulation provisions discourage innovation (or risk-taking) by foundations, nor should it overcome foundations’ effectiveness, or their capacity to effectively fulfil their public benefit mission.

In this context the EFC has expressed growing concerns over the past years about the impact of security and counter-terrorism policies on the activities of the sector and its grantees.

The EFC had welcomed the five principles to prevent criminal abuse of NPOs by the EU Ministers of Justice at their December 2005 meeting, as a good basis for cooperation between the EC, the Member States and the NPO sector to promote transparency and accountability. The EFC agrees with the paramount importance of safeguarding the integrity of the non-profit sector from external abuse and influence, the value of dialogue between Member States, the non-profit sector and other relevant stakeholders, the need for Member States to develop their knowledge of their non-profit sectors continually, and not least that the risks of terrorist financing are managed best where there are effective, proportionate measures for supervision. Indeed, foundation boards, staff and volunteers are best placed to design policies and practices that prevent, address and expose malpractices.

The Centre’s main worry is the potential development of a ‘one size fits all’ approach and harmful regulations, which would overburden the sector and hamper the international work of foundations and their grantees, including important mediation and post conflict resolution work.

This will be at the core of the discussions at the EFC Annual General Assembly (AGA) and Conference in Belfast in 2012 which will gather some 600 foundation leaders to examine the contribution of foundations to social justice, peace and human rights.



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### Preventing abuse of the NPO Sector for terrorist financing

*Haroun Atallah, Director of Finance and Services, Islamic Relief*

The extension of FATF rules to cover Counter Terrorism Financing (CTF) was the obvious available mechanism after September 11. Financial institutions and regulators had become accustomed to rules developed to combat money laundering of ill gotten funds. Regulators and financial institutions as well as Non Profit Organisations (NPOs) are still figuring out how to protect the sector without harming the good work it does. Some charities especially Muslim lead ones were adversely affected with dependant beneficiaries paying the price.

The role of financial institutions is central in anti money laundering or counter terror financing operations. It was not expected to be the only player but in some cases they became the most influential. Special recommendation 8 that deals with NPOs presented governments, NPOs and financial institutions with new challenges. This short article will explore some of the challenges created for each of three in turn.

#### Governments

To deal with the requirement to maintain a register of all NPOs in their country, governments resorted to available structures. For example in some countries ministries for social welfare kept a register and in others revenue authorities did the same. The approach to registration and regulation of NPOs varied greatly. In fact the definition of NPOs is so broad that many countries have multiple registers with different government departments. Some NPOs could be registered with local authorities while others are registered on a national register. Some charities are registered with specialist departments like education, health or social welfare.

As a result, some countries have been struggling to introduce regulations/laws for the NPO sector. Alternate state arms have been offering competing views and in the absence of a consensus, the *status quo* (with no empowered regulator) is allowed to carry on. For some countries the tax authorities represented the best source of information as tax concessions required submission of annual returns by qualifying organisations. However, not all organisations qualified for tax concessions and there are some countries that have a limited tax system. In certain cases records of the governance structures and financial dealings of NPOs were not submitted to any regulators let alone maintained on a register. Where the *status quo* approach was taken financial intelligence units (FIUs) and compliance units in banks became the supreme powers. The narrow space offered to NPO's gave reassurance to the governments that all is well. When these states were given low scores by the FATF mutual evaluation they became incensed. The reality is they have not reached the standards. However the objective of stopping terror financing, in their view, has been achieved.

Governments have struggled with this challenge as changes were required in regards to legislation, roles of departments and even the creation of a new department in some cases. The sheer volume of organisations that were required to register suddenly caused an administrative challenge that many countries struggled with. A regulator from a country that introduced compulsory registration of all NPOs lamented the amount of work that had to be carried out and the fact that it left his department unable to focus on high risk organisations.

To make matters more difficult, many NPOs work across borders. This required governments to make a distinction between the requirements for organisations that operated exclusively in a country and international organisations that have a local branch. The absence of proportionate regulation leads to excessive methods that stifle NPO efforts. Governments needed to meet the SR 8 requirement of creating a single point of contact for information but the departments that specialise in analysing information are many. FIUs took the lead in the investigation of financial transactions.

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Financial transactions within international NPOs are often not understood well when looked at in isolation from the work that they do. It is knowledge of the sector that is often required to raise the alarm. The best source of information on abuse in the sector will come from people that work in the organisations or from members of the public that come in contact with an NPO. The public would not have direct access to an FIU. A dedicated regulator is necessary for fulfilling this role. They are needed to sieve through information to distinguish false allegations from merited claims. Regulators have a responsibility to protect the sector from abuse as well as protect the sector from false accusations. FIUs and security forces are not mandated or set up to do the latter.

### Non-profit organisations

NPOs faced many challenges to ensure compliance with all the new regulations. International NPOs (that operate across jurisdictions) have the difficult task of complying with regulations in multiple jurisdictions that each feels responsible for the activities of the NPO. This created a legal and structural challenge that many NPOs continue to suffer from.

International NPOs found themselves having to establish a local board that is answerable to the local governments. For this reason, NPOs resorted to complicated contractual arrangements to maintain the right of ensuring observance of agreed standards and to meet their responsibility for oversight. International NPOs are often given licences to work for a few years with stringent rules attached to renewal of registration. Organisations would be threatened with withdrawal of their licence if they engaged in advocacy or campaigning on issues that the governments deem unacceptable. This may include the rights of street children or other disadvantaged groups in society. Imagine a school or health centre that needs to await renewal of registration before renewing staff contracts and then telling students or patients that they might have to close down.

With conflicts raging in many parts of the world, some saw the accusation of terrorist links as just an reason to curtail or close down charities activities, often without due process. Charities became vulnerable to accusations of terrorism links with vast resources invested in defending the organisation's reputation. New definitions of terrorism links, lists of proscribed individuals and entities and court cases in different parts of the world gave lawyers a field day. Excessive amounts of resources (especially in the case of leading Muslim charities) are being diverted from the beneficiaries to defend the charities' name and reputation as well as meet new standards.

While speaking on this topic at an international conference held in Canada I asked the audience (that represented some 20-30 organisations mainly from North America) if they were aware of the necessity to screen partners. And if they actually carried it out. Only 3 had heard of screening and only put this into practice. Although this is anecdotal rather than based on scientific evidence it is nevertheless indicative of the lack of awareness in the sector in some quarters.

The 'Know your Customer' principle in banking was carried over to charities to become known as 'Know your Beneficiary' (KYB) in SR8. International aid organisations give help on the basis of need. NPOs working in conflict zones are put at risk by expecting them to start asking people for extensive personal information. How can a charity work in developing countries, failed states or conflict zones where a regulator does not exist? How can a charity go into an area hit by a disaster and start saving lives immediately if they have not been registered in that country previously? How will they open bank accounts and move funds around quickly?

The reality of work in international aid at the moment is that organisations are gathering far more information than they have ever done. They must now screen names of organisations, individuals and suppliers at substantial cost and despite this they are more vulnerable than ever to being tripped up by regulators. NPOs need to apply proportionality to the work they do (as do regulators and financial institutions). It is not possible to ask every individual beneficiary or donor for their ID, whereas it is possible to ask for details on organisations they partner with and carrying out background checks on

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large benefactors. NPOs have collected information about their partners' capacity and track record for a long time. This is an effective way for identifying fake organizations (that is often overlooked). Screening is not the only effective tool.

### Financial institutions

In cases where countries did not already have a regulator the governments resorted to financial institutions to ensure funds are not channeled to terrorist activities. Financial institutions were expected to play a policing role on all financial transactions with the warning of heavy penalties if they failed. To make matters more complicated, financial institutions had to defend themselves against legal action brought by the victims of terrorism. Not only were they expected to have identified proscribed persons and organisations, they were also expected to have foreseen potential problem customers.

All financial institutions involved in a financial transaction have equal responsibility for carrying out checks without relying on checks carried out by other institutions (reputable or not). This led banks to adopt a zero tolerance approach. This resulted in transfers from some countries being stopped unless they came from a handful of government-linked organisations. The work of NPOs was effectively nationalised. This had a major impact on beneficiaries that relied on charitable contributions from these countries.

The official avenues created to harvest charitable contributions lacked the credibility of independent organisations rendering amounts collected a fraction of potential contributions. The only assumption one could make (in societies where such contributions represent a religious obligation) is that non-charitable avenues are being used to transfer funds.

The risks made banks turn down business because related risk assessments made the business not worth the trouble. This only led to people carrying out charitable activities through personal accounts.

The responsibility placed on banks in the financial chain of a transaction resulted in correspondent banks that relied on screening lists more than first-hand knowledge of parties to a transaction. This resulted in them holding up transactions based on name similarities. This in turn resulted in harm to beneficiaries and damage to the reputation of NPOs.

A few real life examples may illustrate the challenges we face:

1. ECHO funds an agency to deal with a humanitarian disaster. The organisation purchases supplies and pays the supplier. The supplier does not get their money and after chasing the money they are told that the money needs to be cleared by OFAC due to name similarities. Clearance takes months and the work is delayed. Refugees are left without timely help. The organisation's reputation is tarnished.
2. A transfer is made by a financial institution in one country to 'organisation A' in Britain. The bank refuses to complete the transfer and after the donor enquires they are told the charity is listed. After enquiring with the bank they realise that the list they referred to was that of politically exposed persons. The list had a negative story published in a media source about the 'organisation A' making it a potential risk. The incident cast a doubt on the organisation. 'Organisation A' is left to wonder how many donors are deterred from making a donation.
3. A transfer is made from Britain to a field office in a developing country. The bankers in Britain and the recipient country have full details about the organisation, including a letter from OFAC to say it is not listed. The funds are stopped by the correspondent bank in the middle that has no access to information yet has the responsibility for screening to the same level as the other two banks. (This last scenario happens on a weekly basis). It takes up to a month to clear the funds affecting beneficiaries, staff and the organisation.

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4. Funds transferred by the UN to ‘organisation A’ are held up by a financial institution in the middle of the transaction that is neither the banker for the UN or ‘organisation A’. They refund the money back to the UN after pocketing charges.

### Recommendations

**Governments** are recommended to set up an agency that has specific responsibility for the regulation and monitoring of the NPO sector. Cumulative experience and specialism will allow agency staff to see risk signals better, communicate with the public more effectively and set up relevant joined up regulation that protects the public and the sector.

**The NPO sector** needs to respond as one entity in introducing self-regulation and standards that assure confidence in the sector. The importance of transparency and accountability cannot be over emphasised. Improving governance and sharing lessons learnt with the sector is important to raise the standards across the board. Greater transparency is needed in the process of proscribing to allow organisations to challenge assumptions that are made.

**Financial institutions** should not have equal responsibility for transactions handled. The remitter and recipient banks are adequate for scrutiny of the parties to a transaction as they have access to accurate information. It serves no purpose to stop all transactions based on risk assessment. Banking federations need to open a dialogue with regulators to ensure customers have a positive experience and that fear of litigation does not drive decision making. Financial institutions should not be allowed to impose additional charges for investigating transactions. The costs should be distributed over all transactions to eliminate profiteering from investigations.



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## Transparency and Accountability of Civil Society in the Context of Terrorism

*Hon. Rollin van Broekhoven, President, International Committee on Fundraising Organizations (ICFO)*  
*Adri Kemps, ICFO Secretary General and Executive Director of Centraal Bureau Fondsenwerving (CBF)*

### Background

As stated in the September 2002 issue of International Journal of Not-For-Profit Law, in an article titled, *Charities and Terrorism: The Charity Commission Response*: “It is difficult to imagine an issue that could undermine public faith in charity more than the suspicion of terrorist links.”

The issue was brought to our attention in ICFO in December 2001, following the Al-Qaeda attacks on the World Trade Center in New York and the Pentagon in Washington. The Bush Administration, as part of its War on Terrorism, declared legal and financial war on groups believed to have aided and supported sponsors of terrorism. These initially included Islamic groups that reportedly raised funds that helped militants in the Palestinian territories, Iraq, Afghanistan, and other conflict areas in the Middle East.

Then, the European Commission held a conference in mid-February 2009 addressing the European Center for Not-For Profit Law (ECNL) study on ‘*Recent Public and Self-Regulatory Initiatives Improving Transparency and Accountability of Non-Profit Organizations in the European Union*’. The focus of this meeting at the EU headquarters in Brussels was to encourage discussions on the outcome of this study, its recommendations, and possible follow-up.

Much of the agenda discussion during this conference arose out of the recommendations of the Financial Action Task Force on Money Laundering (FATF), and specifically, out of Special Recommendation VIII (SR8). Broadly stated, the FATF in SR8 recognized that non-profit organizations are particularly vulnerable to being abused for the financing of terrorism. Whether or not this is true in much of the developed world may be subject to debate. Nevertheless, countries were encouraged to review the adequacy of their laws and regulations to ensure that the sector was not misused by terrorist organizations posing as; (1) legitimate non-profit organizations; (2) by legitimate organizations that were exploited as conduits for terrorist financing; or (3) were used for concealing and obscuring the clandestine diversion of funds that were donated for legitimate purposes to terrorist activities. A document, dated 11 October 2002, entitled ‘*Combating the Abuse of Non-Profit Organisations*’, provided detailed recommendations or best practices for addressing SR8.

In January 2009, the European Court of Justice issued its decision in *Hein Persche v. Finanzamt Lüdenscheid*, addressing the tax deductibility of a gift-in-kind given by a taxpayer in one country to a charity located in another country. Briefly, the Court ruled that legislation of a Member State which precluded the deduction for tax purposes of gifts to bodies established and recognized as charitable in another Member State violated Article 56 EC. This limited the free movement of capital, which Articles 56 to 60 EC addressed. This rule applied to claimed donations without regard to whether they were financial transactions or gifts-in-kind. Although this decision was unrelated to any potential financing of terrorism, we believe that achieving the objectives of SR8 becomes more complicated when countries are not in a position to evaluate the legitimacy of charitable organizations in other Member States or determine whether the funds contributed for legitimate purposes are diverted to terrorist activities.

### Know Your Donor; Know Your Beneficiary

A number of examples have been provided to illustrate the reason for SR8 and the problem. The 11 October 2002 document detailing best practices stated the problem as follows:

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Unfortunately, numerous instances have come to light in which the mechanism of charitable fundraising – *i.e.*, the collection of resources from donors and its redistribution for charitable purposes – has been used to provide a cover for the financing of terror. In certain cases, the organisation itself was a mere sham that existed simply to funnel money to terrorists. However, often the abuse of nonprofit organisations occurred without the knowledge of donors, or even of members of the management and staff of the organisation itself, due to malfeasance by employees and/or managers diverting funding on their own. Besides financial support, some non-profit organisations have also provided cover and logistical support for the movement of terrorists and illicit arms. Some examples of these kinds of activities were presented in the 2001-2002 FATF Report on Money Laundering Typologies; others are presented in the annex to this paper.

Here is the situation: There is a relief and development charity based in Europe or North America. The charity is recognized as a tax exempt organization under the laws of the relevant country in which it is located, and may or may not be monitored by an independent, or self-regulatory, non-governmental monitoring or accrediting body, such as those which are members of ICFO. Through its child sponsorship funding and other fundraising efforts, it supports a group of orphanage homes in the Gaza Strip. These homes may be owned and operated by that charity, or a consortium of similar cooperating charities licensed in Palestine.

While the United States, Canada, the European Union, and other countries characterize Hamas as a terrorist organization, the United Nations, Russia, and other countries do not. Nevertheless, Hamas, in addition to governing the Gaza Strip, may be responsible for operating these orphanages and may even take over ownership of the properties. Much of the funding as a result of individual donations is directed to the humanitarian causes for which it is raised in North America and Europe. However, as money is fungible, some of it may end up in the hands of Hamas and be used for the purchase of weapons and munitions, communications equipment, medicine, visas and so on. These appropriations could subsequently be utilized when fighting UN police forces, Israeli forces, and other allied groups.

Or, for another example, during the 2010 summer floods in Pakistan, relief aid flowed to NGOs involved in alleviating the devastation of the flooding. Demands for food, water purification tablets, shelter, medicine, hygiene kits, and medical teams to help save the lives of flood victims poured into government offices and NGOs. Requests for aid also addressed the added need for transportation of these supplies and medical teams by raft, boat, or donkey. While militant groups in Pakistan previously had limited success in providing aid to refugees, the flood disaster, as well as anger and mistrust of the Pakistani government, had certainly given militant groups offering services and disaster relief some credibility. Jamaat-ud-Dawa (JuD), under the name of Falah-e-Insaniyat Foundation Pakistan, had set up approximately 29 relief camps in a number of flooded areas. According to one report by the *Times of India*, JuD had set up camps in its own name until police started demanding extortion money. JuD claimed to have provided food to 50,000 flood survivors in all four provinces every day and was in the process of reaching out to 100,000 survivors. Additionally, it claimed to be distributing packets of food, hygiene items, and other items to 8,000 families.

There are a number of issues in these examples with respect to transparency and accountability in the charity sector in connection with SR8. One is simply the question of whether the charities in question are in compliance with national laws. In the case of the European and US charities providing aid to the Gaza Strip, most of them were completely legitimate and operating in full compliance and respect to their fundraising and humanitarian activities. Moreover, many were accountable to the public regarding their operations, to ensure they function in accordance with the laws of the US or of a European country in which they were located. Many countries require that domestic charities legally control and operate the

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foreign entity to which it channels funds. In the United States, the tax authorities will disallow a tax deduction for contributions to domestic charities if the domestic charities are mere conduits for funds to foreign organizations. In Europe, a different result would probably be obtained as a result of the European Court of Justice Decision in *Hein Persche v. Finanzamt Lüdenscheid*.

The situation with respect to the disaster aid in Pakistan might be different, although there was no indication that JuD was operating outside the limits of Pakistani law. However, there were reports in the international press that JuD was involved in the attacks in Mumbai, India, and was a front for a terrorist organization, *Lashkar-e-Taiba*. As a result, there may have been questions about the ultimate use of funds donated.

Secondly, there is simply the question of standards and monitoring to be performed on charities, and whether such monitoring is to be done by government agencies or some form of independent or self-regulation monitoring regime. In the case of government monitoring, what sort of sanctions should be applied; criminal, civil, or some other form of sanction? Prosecution is challenging in these cases because even if intelligence shows signs of terrorism support, it is difficult, if not impossible in many cases, to obtain the unambiguous evidence that is admissible in court proceedings to prove that the money ended up in the hands of terrorists overseas and that the charity knew that to be the case, or understood its probability. This is often further complicated by the security classification of the intelligence gathering methods.

So, what is the solution? We are not persuaded that reliance on governmental regulation and charity monitoring are always the answer. Indeed, it is in the context of increased cross-border fundraising that independent self-regulation and charity monitoring mechanisms may actually foster, from a national perspective, an international response to money laundering and terrorist financing and the misuse of funds donated by individuals to charities that is better than a response by individual states through active regulation and monitoring of the sector.

ICFO, as an international umbrella body of national monitoring organizations, has led coordinated efforts to contribute to the cause of transparency and accountability on billions of funds raised from private donors and spent for the public benefit. It is, we believe, noteworthy that the FATF in its Special Recommendation VIII specifically recommended that the third sector, or NGO sector, take action on Anti-Money Laundering/Counter-Terrorism Financing (AML/CTF). ICFO is building a network on the concept of donor's trust instead of promoting specific measures on AML/CFT. The question naturally arises as to what ICFO and its members are doing in this regard, and how they are doing it.

Most members of the ICFO use the model of awarding seals to trusted charities as a component of accreditation schemes. This can be referred to as innovative oversight in addition to legislation or obligatory measures on AML/CFT. ICFO takes an alternative way of oversight based on independently articulated standards and assessments to protect donors trust. The effectiveness of this model is that it relies, in part, on existing structures. These include existing laws and regulations, auditing services, and the availability of news media. The authors argue that the concept of “know your donors and know your beneficiaries” can be of added value to good governance by charities and will help NGOs strengthen trust in public fundraising as long as the concept is not used by authorities to take control over the NGOs and their policies to pursue their objectives.

### Civil Society and AML/CFT

Historically, the concept of civil society can pose a bit of a problem with respect to addressing AML/CFT and government or state regulation and monitoring. Civil society has been generally understood as being historically one of the three legs of a democratic and open society. As such, civil society is understood to refer to the un-coerced collective action around shared interests, purposes, and values. Its institutional forms are distinct from the state, family, and market. Therefore, the sector is set apart from government

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and the market, and does not distribute profits. It is self-governing, and is a mediating organization, or group of organizations, voluntary in nature, between the state and individuals.

The problem occurs when much of the activity of the civil society organization (CSO), such as a charitable organization, is funded by government largesse, meeting a need which the government deems to be important, and perhaps even part of the government's own sense of governmental responsibility. The work of the charitable organization is accordingly regulated by the government because of the nexus between government funding and the activities of the charity. It is clear, it seems to us, that if funds from the state treasury are to be used to accomplish some public or humanitarian purpose, which the government asserts to be part of its responsibility to be a good steward of the money entrusted to it through taxes, the government acts appropriately in requiring the CSO to account for the expenditure and use of that money. Such accounting would naturally cover some form of regulation and reporting, through audits and the submission of information concerning the work of that charity.

However, it would seem that some form of legislative or regulatory regime would also be proper in the case of the government's obligations with respect to the flow of funds through NGOs on the same basis as its obligations to protect its citizens and satisfy its obligations under the FATF SPECIAL RECOMMENDATIONS ON TERRORIST FINANCING. For example, Special Recommendation No. I provided that countries were responsible for implementing UN resolutions regarding the prevention and suppression of financing of terrorist acts, including UN Security Council Resolution 1373. Similarly, Recommendations II, III, IV addressed the criminalization of terrorist financing and associated money laundering, freezing of terrorists' assets, and the reporting of suspicious transactions relating to the financing of terrorism. Recommendations V, VI, and VII addressed the requirement for international cooperation between nations, and the regulation of the transfer of funds, including wire transfers. All of these seem appropriate functions of government, both with respect to AML/CFT, as well as to the prevention of fraud on the private donor sector. While none of these recommendations specifically addressed the regulation of non-profit organizations, the actual handling of monies was implicated, and to that extent, had relevance to the activities of non-profit organizations.

We have seen no evidence that a regulatory scheme imposed by the government, instead of regulation schemes of independent watchdogs, increased the level of transparency and accountability of NGOs. and that to the extent it did, that it increased the level of trust between donor and NGO, thereby increasing the level of giving. The charitable impulses of the giving public are based on more than simply whether the civil society sector is regulated by the government, and whether the monitoring by the government both ensured compliance with the regulations, and was consistent with the freedom and effectiveness of organizations to fully serve their role in civil society. We sometimes forget that giving to charity is more than simply a financial transaction.

### **Informed Trust as Basis for Credibility of Charitable Work**

A national registration system for non-governmental charitable organizations is widely required by law in countries around the world, particularly where there is some tax exemption to the organization or tax consequences applicable to the donor. In most countries, this registration requirement insures that the non-governmental charitable entity is established for a public benefit purpose and is in compliance with minimal legal requirements for registration. True standards of accountability and ethics and monitoring standards are seldom associated with the requirement.

The issue of establishing standards promoting transparency and integrity and monitoring non-governmental charitable organizations through an accreditation process is a different matter. For example, the ICFO standards cover five key areas of the activities of international NGOs, or not-for-profit, public benefit, private organizations. These include membership and responsibility of the governing body, fulfilment of public benefit goals, fiscal control and management, fundraising practices, and provision of public information, such as disclosure of audited financial statements. Important to the satisfaction of



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these standards is the goal of ensuring that the public, donors and recipients of the public benefits, have ready access to sufficient and adequate information to enable them to make informed decisions about the organization, their relationship to the organization, and the accountability of funds raised by the organization. Standards, without monitoring, provide little assurance to the donor regarding the transparency, integrity, and governance of charities and other public benefit non-governmental entities.

However, it is equally important that the monitoring body, responsible for setting standards and monitoring charities to insure their compliance with those standards, have insight into the charity sector and the trust of the organizations which are to be subject to the standards and monitoring. Implicit in this model is the idea of a relationship between the NPO and the monitoring organization based on the establishment of standards of accountability and monitoring to ensure compliance with those standards. This requires maintaining currency with fundraising techniques and activities, particularly in a fast moving technological age, worldwide monitoring practices, and the free exchange of information with other monitoring or accrediting bodies external to a particular country.

Governmental versus non-governmental monitoring is a matter of considerable interest to the ICFO, and has been the subject of frequent debate in many countries, particularly those with an active charity sector. Much of the public benefit work around the world is done by charities, the Church, or religious communities. As the readers may well appreciate, non-governmental organizations have become an important social counterpart of the economic and political forces in society. Private donations are widely regarded as an important factor for the independence of the charity sector.

One concern is that this independence could be compromised when there is substantial funding by the government, particularly when those funds are targeted to government objectives. While it is important to protect the rights of donors, donors are also generally assumed to be aware that they are not always adequately protected by the state from fraudulent fundraising appeals, and indeed, that they are ultimately responsible for their contributions to the charitable causes. This is why private and semi-private monitoring and advisory boards, such as various forms of self-regulation and accreditation bodies, have been established in many countries, including those countries represented by the ICFO. These monitoring and accrediting non-governmental bodies are building bridges of trust between reliable NGOs and the donor public.

One of our concerns is that a statutory regulatory scheme, with governmental monitoring, together with the potential reporting of suspected fraud or similar irregularities to police, and the denial of registrations or criminal prosecution, tend to increase the administrative costs. Specifically, such schemes generally require accounting and legal services beyond those normally required for the responsible administration of the charity. The experience in the United States, and no doubt in many countries, suggests that, as a result of governmental regulatory requirements and governmental monitoring, there is an increased requirement for additional accounting and legal services beyond that normally required to meet the general transparency, integrity, and other operational interests of the charity, to insure that all the requirements of such laws are met.

There is also experience and some data that tend to support the conclusion that such requirements do little to assure the public that the finances and operations of the charity are in accordance with the requirements of such laws. This is particularly true since many donors do not understand the requirements of the law, and give to those charities with which they are familiar and which perform public benefit services they support and for which they have personal commitment. While many large charities can bear these added costs with little effect to their administrative cost ratios to total donated funds, most smaller charities cannot continue to operate and perform the public benefit functions for which they were established, with the added burden of governmental regulation and monitoring, plus the costs of the accounting and legal services that would not otherwise be warranted.

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## Conclusion

Traditional independent monitoring by an independent organization or self-regulation scheme to promote trust of donors has been focused on good governance of NPOs and their policies on fundraising and the transparent reporting of the income and spending of the funds. The question is how we in the general public and donor pool are to have some sense that particular NPOs are well-governed and whether their policies and practices on the raising of funds and the use and disbursement of funds are disclosed to the public and to donors on request. In other words, is it possible to improve trust between donors and the NPO sector, and is it possible to formulate clearly understood standards applicable to good governance, transparency and accountability, and to specific techniques of fundraising? And if so, is it possible to monitor the activities of NPOs against such standards to enhance the level of trust between donor and NPO? We think so.

Standards promoted by the ICFO and its members can help charities protect themselves from becoming involved in fraud, money laundering or the financing of illegal activities. The bridges of trust will be stronger if the charities are willing to submit to accreditation schemes and be monitored by independent or self-regulatory monitoring bodies, such as the members of the ICFO.

In these days of globalization, extended social media, and increased cross-border fundraising within the European Union, bridges of trust can be eroded by permitting “open areas” without national monitoring systems in the European Union. Independent monitoring should honour the national laws, history, values, traditions, and circumstances, but will be more effective when charities based in one of the countries of the European Union, will be in all cases subject to standards of substantial monitoring procedures.

Civil engagement, supported by donations for public benefit purposes, can flourish and strengthen open societies as long as trust between charity and donor, and the donor public, is maintained. In the new era of upcoming social media, personal connections and relationships are often replaced by Internet connections. It will be a challenge for charities to make use, for example, of new platforms of social networks to keep donors and beneficiaries recognised as persons with real identities and not with faked identities. Charities who know their donors and beneficiaries will be able to build and strengthen relationships in a changing world.

The authors recommend that countries that do not have self-initiated models that include standards and methods of monitoring for promoting transparency and accountability, consider adopting such models, such as those employed by the members of the ICFO, to strengthen donor trust in civil society and reduce the probability of the misuse of funds.

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### Strengthening NGO credibility and effectiveness compliance systems in civil society self-regulation

*Michael Hammer , Executive Director, and Christian Laybourn, Researcher, One World Trust*

Over the past decades civil society organisations (CSOs), and in particular non-governmental organisations (NGOs) [1], have seen a significant change in their role and influence in society and politics. NGOs are now major providers of essential services, influential advocates for marginalised groups and knowledgeable advisors on public policy. As such, they have become important players in national and international governance. However, with this newfound influence has come greater scrutiny of CSO activities. Worldwide, CSOs are facing growing pressure to be more accountable. The motivations for these calls are however to be differentiated. In many cases governments, donors and the public ask NGOs to be more accountable out of a genuine interest in ensuring effectiveness and to some degree competitiveness in the use of public funds. In other cases pressures are driven by security concerns about the funding of illegal and criminal activities, and fraud prevention. Finally, the accountability discourse is used by some government actors to justify asserting control over civil society, and limiting the space in which civil society organisations can operate, where their advocacy or democratisation work runs counter to government interests.

Independent of the motives, in all cases accountability pressures focus on a whole range of elements including openness about funding sources; transparent accounting to show that funds are used for the purposes they are raised for and remain traceable in complex and cascading partner relationships, coherence of use of funds with the value framework of the organisation, and fulfilment of public benefit claims the organisations make. Increasingly NGOs are also asked to provide evidence of impact, be more open about failures and problems, demonstrate with whom they work and on what basis, which groups they represent and how.

While some NGOs are responding to these challenges, and the different motives that drive them by developing individual, organisational responses such as learning and accountability frameworks, others are coming together at national, regional and international levels to develop common norms and standards and encourage best practice. These range from codes of conduct/ ethics to certification schemes, self-assessment templates, information services to working groups and awards schemes. Sector level forms of cooperation and self-regulation are becoming an important means for CSOs to build public trust in the sector, prevent overly restrictive government legislation, and support the sharing of good practice and learning [2].

Research conducted by the One World Trust on issues of NGO accountability and self-regulation since 2005 shows that self-regulation amongst civil society organisations is more widespread than has previously been thought with over 365 initiatives currently in existence or development worldwide. The survey results, published in 2008 in form of a global database of CSO self-regulation initiatives [[LINK](#)], shows that in all regions of the world CSOs are coming together at sector and subsector level to define common standards and principles in a bid to encourage learning, protect the sector's political space and build public and donor trust.

Yet while the emergence of initiatives such as codes of conducts and certification schemes is a positive development, the development of a set of common principles or framework alone is rarely enough to change the practices of organisations or provide a credible signal of quality. Mechanisms also need to be developed that provide monitoring and, where necessary, enforcement of the standards. In other words, a system for compliance is needed.

Problematically however, our global survey shows that less than half of all of the CSO self-regulation initiatives (47%) that currently exist worldwide have any element of a compliance system, and among the

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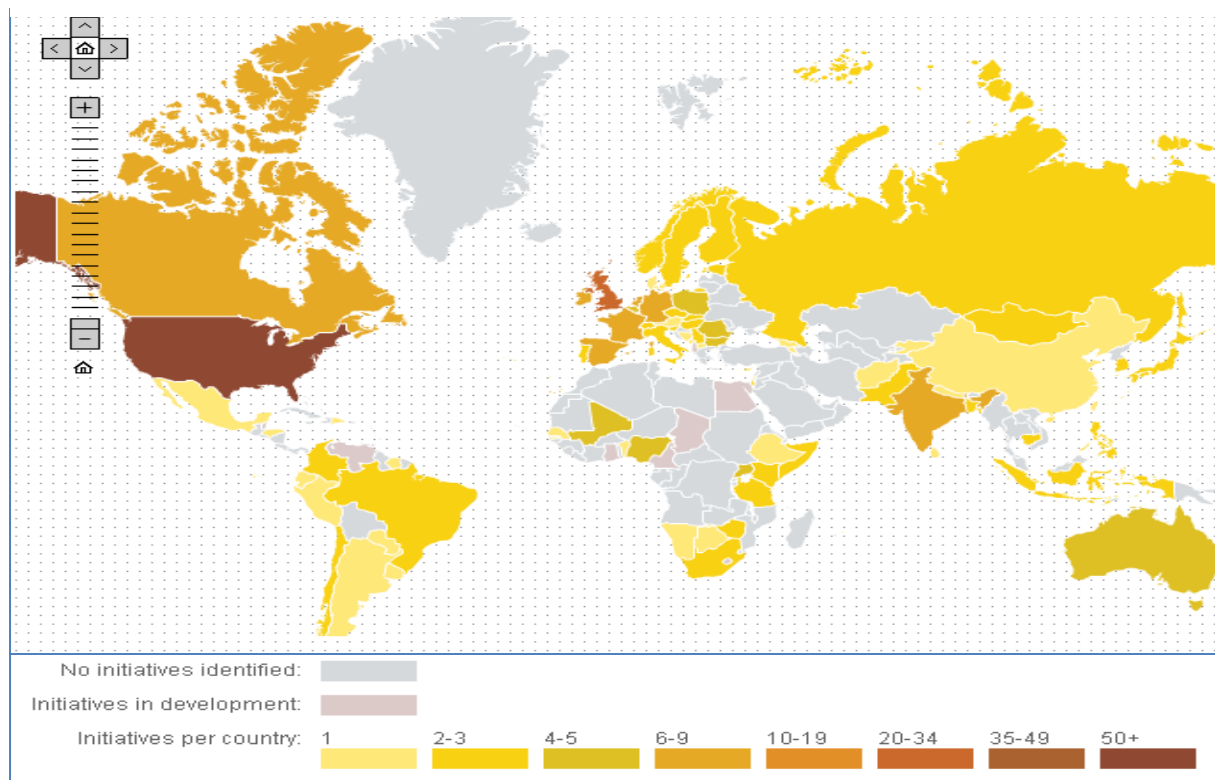
most common form of self-regulation (codes of conduct) this percentage drops to 27%. We argue that this raises important questions about the effectiveness and credibility of many CSO self-regulation initiatives.

While developing a set of common principles is an important contribution to debate and practice on development effectiveness, to ensure they impact upon practice, incentives need to be created to encourage their uptake and adoption. In the absence of these the process runs the risk of producing inspiring words which have very little effect on how CSOs actually operate.

### Challenges associated with self-regulation

The emergence of self-regulation initiatives within civil society is certainly a positive development, yet it does not automatically guarantee the sector’s credibility or accountability. Self-regulation faces two main challenges.

**Figure 1: Geographical distribution of CSO self-regulation initiatives worldwide**



- The first is that it is by definition voluntary. Unlike state regulation organisations can choose whether or not to engage with a self-regulation initiative. Therefore, unless an initiative has wide support within a sector, its overall reach and impact may be limited. There are of course reputational incentives to engagement; being a member of a code of conduct for example, can provide a signal of quality to donors and help an organisation stand out in a crowded and competitive sector. Likewise, some donors require engagement with self-regulation initiatives in order to access funding. In general however, in the absence of donors mandating membership, the ability of organisations to opt in or out of self-regulation can present a barrier to it raising standards across an entire sector.
- The second challenge is that in order to provide an effective signal of quality, a self-regulation initiative needs to ensure that members comply with its provisions. Without this, organisations may join which are of poor quality and that undermine an initiative’s credibility. Economic Club Theory



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explains that voluntary associations and their rules are effective when club benefits are sufficient to justify the cost of membership: with self-regulatory initiatives ‘club benefits’ are in the form of a recognizable indicator of quality, or ‘brand’ which separates members from non-members (Gugerty and Prakash 2008). However, in *The Logic of Collective Action* (1965) Mancur Olson argues that club members have perverse incentives to shirk their responsibility to uphold club standards and are prone to free-riding (receiving club benefits, without paying the costs). This can in turn undermine the credibility of the club and decrease the benefits experienced by all other club members. Both Olson (1965) and Harding (1968) argue that in order to prevent free-riding a club must put up barriers to poor-performers becoming members (in King and Lennox, 2000) and that monitoring and sanctioning mechanisms are an important means of achieving this.

### Self-regulation, compliance systems and effectiveness

While there are few studies available on self-regulation in the NGO sector, the literature that does exist suggests compliance systems are key to ensuring the effectiveness of SRIs. Beckkers (2003) for example found that the *Centraal Bureau Fondsenwerving* in the Netherlands - a certification initiative that provides NGOs with a seal of approval if they comply with standards of good governance and financial management - improved the level of public trust in the organisations which possessed it. The author suggests that the awarding of a seal by an independent body was a majority factor in this as it strengthened the perceived credibility of the initiative. Dale (2005) in his review of 22 NGO self-regulation initiatives, found that the single most important factor in creating an effective initiative is the enforceability of sanctions, followed by the ability to remove accreditation, particularly if accreditation is required for an organisation to access funding. Similarly, Gugerty (2009) in her study of 32 non-profit self-regulation initiatives from around the world, found that key factors in determining an initiative’s ability to provide a credible ‘signal of quality’ to stakeholders such as donors were whether it has a certification process and would publicly disclose findings from its assessments. Similar conclusions are reached by the literature analysing self-regulation of the corporate sector (explored for instance by Lennox and Nash (2003); Rivera, de Leon and Koerber (2006) and King and Lennox (2000) [3].

Research into self-regulation across different sectors therefore seems to point to the same conclusions: providing a reliable and credible signal of quality is contingent on an initiative ensuring members meet its standards, and excluding those that seek to enjoy the benefits of membership without investing the necessary resources, and that key to this is having in place a system of monitoring and sanctioning compliance.

### What is a compliance system?

A compliance system is the set of mechanisms, processes and procedures that support the implementation of a self-regulation initiative standards and/or principles and protects its overall credibility. It is made up of two components: a proactive or reactive monitoring function and a sanctioning mechanism (see Table 1: Components of a compliance system). In practice it is only codes of conduct and certification schemes that can include compliance mechanisms. Self-assessment templates, working groups, information providers, or awards schemes do not by nature necessarily aspire to work with compliance systems.

Proactive monitoring involves organisations actively monitoring and reporting on their compliance with principles or standards, for instance by means of self-assessment, peer assessment, or assessment by an independent third-party.

A reactive approach to monitoring involves the initiative investigating a member when it has been alerted to a case of potential non-compliance through a complaints procedure.

To strengthen their compliance systems, some initiatives use both proactive and reactive monitoring.

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**Table 1: Components of a compliance system**

Monitoring function			Sanctioning mechanism
Approach	Method of assessment	Source of assessment data	
Proactive monitoring	Self-assessment	Desk based	Recommendations for corrective action made, but kept confidential
	Peer assessment	Interviews / surveys / field visits	Recommendation for corrective action made and disclosed publicly
	Third party assessment	Both	Financial penalty imposed
Reactive monitoring	Complaints procedure	Depends on nature of complaint	Membership suspension / expulsion
			Expulsion publicised

### Sanctioning mechanisms

While monitoring mechanisms are important in supporting the implementation of self-regulation, they are unlikely to guarantee compliance on their own. The reality is that not all members of an initiative will be equally committed to its implementation. Some organisations will be happy receiving the reputational benefits of participating without committing the necessary resources to ensuring compliance. In order to tackle this problem, and in turn protect the credibility of an initiative, a number of self-regulatory schemes have developed mechanisms for sanctioning non-compliance.

Table 1 outlines the five main types of sanctioning mechanism; each puts a progressively higher penalty on the organisation for non-compliance. In many initiatives these represent different steps in an escalation process where sanctions are progressively increased if a member proves unresponsive.

The softest form of sanctioning is simply a recommendation for corrective action by the body administering the self-regulation initiative, and issuing a member with recommendations for improvement. In most cases the recommendations made by the body administering an initiative to the member organisations are kept confidential, but there are cases where they are publicly disclosed. Another type of enforcement mechanism involves imposing financial penalties in cases where a member is failing to implement principles. The strongest form of sanctioning is suspension of membership, followed by expulsion. In initiatives that use such a mechanism, a member may have its membership suspended until it addresses areas of non-compliance. After a set period of time however, if an organization remains unresponsive, membership will be revoked. The rigour can also be increased by publicising the use of sanctions against the non-compliant member.

### Compliance systems for CSO self-regulation: current patterns

Out of the 365 self-regulation initiatives in the One World Trust database a total of 263 initiatives falls within the categories of codes of conduct or certification schemes, which were identified as suitable for analysis with regards to compliance systems. Of these, however only 123 (47%) do in fact have some component of a compliance system as set out above.

#### Codes of Conduct

The most salient finding from the research is that while code of conducts are by far the most common form of self-regulation, only 41 out of the 149 identified (27.5%) have elements of a compliance system.

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This means that the overwhelming majority (72.5%) have no way of monitoring or enforcing adherence to the standards and principles they set. This raises significant questions about the effectiveness of many of the existing codes in improving practice amongst CSOs and providing a credible signal of quality to stakeholder such as donors and the public.

Among the codes of conduct with a compliance system, complaints procedures are the most common monitoring mechanism, used by 37 initiatives. Self-assessment is the next most common, used by 15 initiatives, followed by independent, third-party auditing (5 initiatives) and peer assessment (2 initiatives).

Significantly, most codes of conduct have no sanctioning mechanisms (113). This means that in the majority of cases there are no provisions for punishing members that persistently fail to comply with a code's principles. Again, this points towards a serious deficiency in the compliance systems of most codes of conduct.

The majority of codes that have a compliance system use a combination of monitoring and sanctioning mechanisms. One of the most common arrangements is to have a complaints procedure alongside a mechanism for expelling members (used in 17 codes of conduct). For example, with the Fundraising Standards Board Self-Regulatory Scheme in the UK, the body administering the initiative investigates complaints against its members that are raised by external stakeholders, and works with the NGO in question to resolve the dispute. If the complaint is upheld by the FRSB, the Board may demand an apology from the charity, and that the offending fundraising material or strategy is withdrawn. In extreme cases, where these demands are not met, the FRSB reserves the right to suspend the charity's membership. The other most common arrangement is where an organisation assesses themselves against the code of conduct, but a complaints procedure is also used to monitor compliance (also used by 17 codes of conduct). The Slovenska Filantropija (Slovenian Philanthropy) Code of Conduct for Organized Voluntary Work is one such example. To monitor compliance members self-assess themselves against the code, however, if anyone feels that a member organisation is not complying with the principles, they can raise their concerns with the Slovenska Filantropija complaints board.

#### **Certification Schemes**

Given the nature of certification schemes, it is unsurprising that all of the 82 initiatives identified through our research have elements of a compliance system. In contrast with codes of conduct, the most common form of monitoring mechanism for certification schemes is third party monitoring: 60 initiatives (74%) use third party monitoring, either by itself, or in combination with other monitoring mechanisms (see below). Only 6 certification schemes (7%) just require organisations to conduct a self-assessment of their compliance and only one relies exclusively on a complaints procedure to monitor its signatories' performance.

More than half of the certification schemes analysed (47) threaten non-compliant members with sanctions, such as suspension or expulsion, although only nine (11%) reserve the right to publicize the suspension. In terms of sanctioning mechanisms, all certification schemes have a de facto means of penalizing members that fail to comply with its standards, as they can refuse to renew an organisations certification once it expires. However, our research shows that 35 certification schemes (43%) have no mechanisms in place to impose sanctions, if bad practise occurs during the certified period.

Among certification schemes, the most common means of ensuring compliance is the use of just third-party monitoring (in 23 certification schemes, or 28%). For example, The Co-operation Committee for Cambodia offers certification against its Code of Ethical Principles and Minimum Standards for NGOs in Cambodia. NGOs submit documentation to the CCC, and undergo a field visit when applying for the certificate. Certification is valid for three years: applicants that do not meet the standards go through a capacity building programme, and can then apply again. The next most common arrangement involves the use of third party monitoring alongside a complaints handling system and the threat of sanctions (22 cases, or 27%). One such example is the Investing in Volunteers Standard in the U.K. This is a certified

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standard for organisations which involve volunteers in their work, and covers all areas of volunteer involvement, from selection and equal opportunities to training and support. The certification process begins with the organisation conducting a self-assessment of their performance, which is then verified by an external third-party assessor. A complaints board reviews any complaints against certified members. If an organisation is deemed to not be meeting the standards, they are given recommendations for improvement, which must be fulfilled within a specific timescale, or else certification is removed.

### Benefits and challenges of different compliance systems

While we have argued that compliance systems are key to strengthening the credibility and ensuring the effectiveness of self-regulation initiatives, the institutional design of a code of conduct or certification scheme needs to be understood within the context in which it is developed.

**Table 2: Benefits and challenges of different monitoring and sanctioning mechanisms**

	Type	Benefits	Challenges
<b>Monitoring mechanisms</b>	Self-assessment	<ul style="list-style-type: none"> <li>• Encourages ownership of the assessment process</li> <li>• Less costly than peer and third party assessments.</li> </ul>	<ul style="list-style-type: none"> <li>• Ensuring that organisations are truthful about themselves</li> <li>• Integrity of assessment may be questioned by external stakeholders</li> </ul>
	Peer-assessment	<ul style="list-style-type: none"> <li>• More independent process than self-assessment</li> <li>• Encourages organisations to share their experiences and learning with each other</li> </ul>	<ul style="list-style-type: none"> <li>• Members may be reluctant to criticise their peers</li> <li>• Assessing organisations need to be willing to commit the necessary time and resources</li> <li>• Requires strong foundation of trust between organisations.</li> <li>• Assessment is only meaningful between similar organisations</li> </ul>
	Third-party assessment	<ul style="list-style-type: none"> <li>• Greater credibility from an independent assessment</li> <li>• External assessment can identify issues that are difficult for those internal to an organisation to see</li> </ul>	<ul style="list-style-type: none"> <li>• The process of assessment can be costly</li> <li>• Being granted a certificate can lull an organisation into a false sense of security</li> </ul>
	Complaints procedure	<ul style="list-style-type: none"> <li>• Relatively low cost to set up and run</li> </ul>	<ul style="list-style-type: none"> <li>• Only reveals cases of non-compliance when reported</li> <li>• Public/stakeholders need to be aware of complaints procedure</li> </ul>
<b>Sanctioning mechanisms</b>	Confidential recommendations	<ul style="list-style-type: none"> <li>• Allows member to rectify mistakes, build on learning process</li> </ul>	<ul style="list-style-type: none"> <li>• Members may ignore recommendations</li> </ul>
	Recommendations made and disclosed publicly	<ul style="list-style-type: none"> <li>• Encourages members to act on recommendations by creating public pressure</li> </ul>	<ul style="list-style-type: none"> <li>• May undermine public confidence in the sector</li> </ul>
	Financial penalty	<ul style="list-style-type: none"> <li>• Acts as a strong deterrent to non-compliance</li> </ul>	<ul style="list-style-type: none"> <li>• Will only be effective if penalty cost exceeds benefits of free-riding</li> </ul>
	Membership suspension / expulsion	<ul style="list-style-type: none"> <li>• Acts as a deterrent to free riding</li> <li>• Removes poor performing members</li> </ul>	<ul style="list-style-type: none"> <li>• Seen as too extreme by member organisations</li> </ul>
	Expulsion publicised	<ul style="list-style-type: none"> <li>• Demonstrates stringency of the initiative to the public</li> </ul>	<ul style="list-style-type: none"> <li>• May undermine public confidence in the sector</li> </ul>



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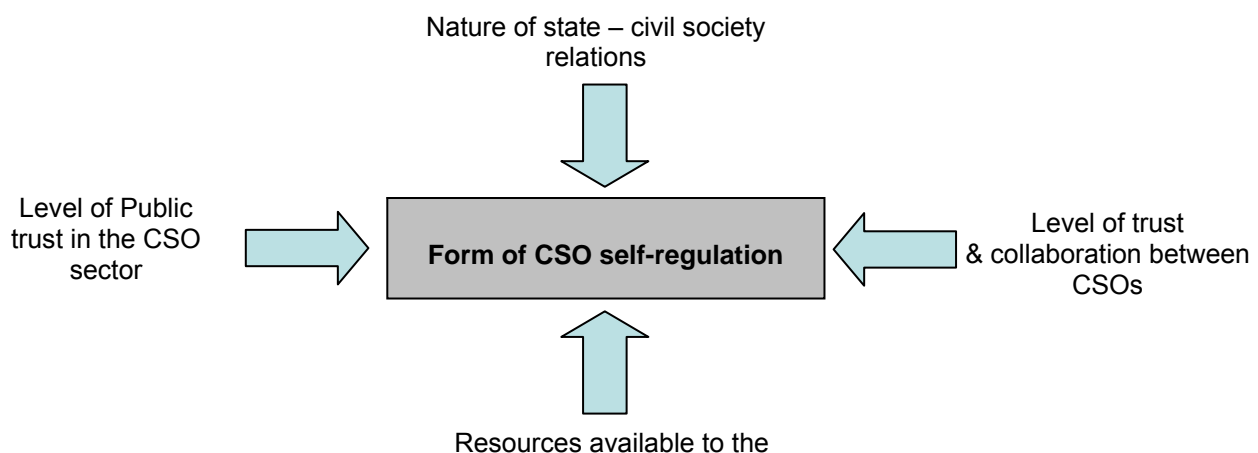
June 2011

**“OSCE participating States (should) ensure that legitimate activities of non-profit organizations and charities are not restricted and that they cannot be misused by terrorist organizations (...)”**  
**OSCE Permanent Council Decision No. 617 (2004) on Further Measures to Suppress Terrorist Financing**

An initiative must weigh up the relative benefits and challenges of including various compliance mechanisms in light of a number of factors, such as the resources that are available to develop and administer a self-regulation initiative and the level of coordination and collaboration within the CSO sector.

For example, while an external observer may see the absence of a monitoring mechanism for a code of conduct in country X as evidence that it is ineffective, the sector may have until recently been highly fragmented; the development of the code may therefore be seen as a major accomplishment, and members may be very committed to implementing its provisions. This is not to say that in the future monitoring mechanisms should not be developed, but at this moment and time relying on a commitment from signatories might be the most appropriate approach for improving performance. As the principles become more widely understood and accepted, monitoring and enforcement mechanisms can be developed. The following section therefore, offers an analysis of the benefits and challenges associated with different monitoring and sanctioning mechanisms. A summary of this discussion can be found in Table 2.

**Figure 2: Key factors shaping a compliance system**



### Key factors shaping a compliance system

Reflecting on these findings, four key factors can be identified that shape and influence the design of a compliance system: available resources, the nature of the relationship between civil society and the state, public trust in the sector, and trust and collaboration within the sector (see Figure 2: Key factors shaping a compliance system). As an organisation seeks to design a new code of conduct or certification scheme, or revise and improve an existing one, these can provide a useful framework for deciding which approach to take.

- **Available resources:** The more components a compliance system consists of, the more expensive it will be to administer. Mechanisms such as third-party assessment are costly to implement. Certification schemes usually require prospective organizations to pay an application fee to cover the audit process. Even self-assessment based initiatives, although in relative terms less expensive, if done well, still require organizations to make staff and financial resources available to review and collect internal data. Such costs can create barriers, both for the bodies developing compliance mechanisms, and for prospective organisations, if they have to bear the cost of monitoring. The form a compliance system takes will be shaped both by the resources that the organisation(s) initiating the scheme have at their disposal and the resources of potential participating agencies.
- **State – civil society relations:** The political context also shapes the form a compliance system takes. In some countries civil society organizations have developed self-regulation in reaction to threats or actions by the government to introduce restrictive legislation. In particular in very hostile

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environments, where accountability arguments are used to limit NGO activity and participation in governance processes any initiative that is developed by the sector has to be seen as credible in the eyes of the government or it will not have its desired impact. It therefore has to provide a strong signal that state regulation is not necessary and that the sector is self-policing. In such circumstances developing strong compliance mechanisms may be a political necessity, but can also carry risks of instrumentalisation. In other contexts where the relationship between civil society and the state is more amicable, the incentives offered by government for the sector to self-regulate can shape the nature of the compliance system in direction of a weaker form. In a number of countries, the government makes access to funding or other benefits contingent on compliance with a particular set of standards developed by the sector: in these contexts strong third party certification schemes emerge. This is because in delegating state authority to a non-profit entity, or providing them with tax payers money, the governments wants reassurance that standards are being met.

- **Public trust in the sector:** Securing public trust is another factor which shapes an initiative’s approach to compliance. If the public’s trust in the sector is low, for example because of instances of fraud in fundraising and abuse of funds for bogus causes, self-regulation must be seen to provide a level of rigor that ensures basic standards are met. In contexts where there is a deficit of public trust in the sector, a code of conduct with no form of compliance system will not be enough. Studies of the impact of certification schemes including fundraising quality seals (Beckers (2003)), have found that certified charities were felt to be more trustworthy by members of the public, and also received higher levels of donations.
- **Trust and collaboration within the CSO sector:** Self-regulation can also be shaped by the level of trust and collaboration that exists between CSOs themselves. Monitoring mechanisms require member organisations to willingly open themselves up to outside scrutiny, be this from the body administering the initiative, a peer organisation or a third party actor. Doing so requires that organisations trust the process and those involved. In an environment where there is strong competition between NGOs for funding exposing an organisation’s weaknesses publicly, or even to a peer agency, could be used against it. Co-ordination within the sector can also be important. A CSO umbrella group/ association which has legitimacy within the sector can play a valuable role coordinating and leading the process of developing a self-regulation initiative. In the absence of such a body, efforts at developing self-regulation may become fragmented.

## Conclusions

The paper has outlined the different approaches that exist to monitor and enforce compliance with the principles and standards set by CSO self-regulation initiatives and the benefits and challenges associated with these. It has shown that, problematically, less than half of all of the initiatives (47%) that currently exist worldwide have any element of a compliance system, and among the most common form of self-regulation – codes of conduct - this percentage drops to 27%.

The existing research on self-regulation both from the NGO and the corporate sectors points to a strong link between the existence of compliance systems and the effectiveness of self-regulation. The findings of our research therefore raise some significant questions about the ability of many existing CSO self-regulation initiatives to improve practice with the sector or help build trust with the public and donors.

Designing a code through a highly consultative process will certainly help in encouraging its adoption, yet it is thus rarely enough: incentives and sometimes sanctions are also needed and sufficient thought and resources need to be invested to identify what needs to happen after a set of principles, standards or frameworks are developed. For as our research and that of others has indicated, without systems for monitoring and enforcing compliance, self-regulation initiatives are unlikely to meaningfully influence an organisation’s behaviours and practices.

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The review of existing self-regulation initiatives that include elements of compliance systems shows that there are lots of options out there that can serve as a basis to develop relevant initiatives in an appropriate way. Yet making sound judgments about the design is critical when considering the context of political governance and formal regulatory environment in which self-regulation is happening. Not in all cases the strongest compliance systems will be the best, and civil society should avoid handing ownership of self-regulation initiatives to governments and donors to avoid risks of self-regulation initiatives becoming, intentionally or unintentionally tools that can be used to exercise politically motivated normative control over organisations. The challenge is in finding the approach that is best suited to the context and that allows the initiative to meet the demands of different stakeholders while retaining ownership within civil society.

CSO self-regulation is a rapidly developing field: the Open Forum on CSO Effectiveness has defined common principles of effectiveness and quality for CSOs worldwide, a growing number of initiatives are in development at both the national and international level, and a number of donors are funding CSO self-regulation initiatives as part of their efforts to build capacity and support an enabling environment for civil society to operate. Self-regulation, when supported by appropriate monitoring and sanctioning methods, can be a powerful tool for improving CSO accountability and effectiveness while enabling civil society to develop and become a recognised and legitimate partner in governance.

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#### End Notes

- [1] In difference to the wider group of CSOs we define NGOs as legally, economically and organizationally more developed entities, which often operate on a registered basis, have staff, and work either at national or international level.
- [2] For more information on the drivers and benefits of self-regulation see Warren, S & Lloyd, R. (2009)
- [3] For discussion of the literature on corporate self-regulation please see Lloyd, R., Calvo, V. and Laybourn, C.

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## Thinking outside the (tick)box: a wider look at Non-Profit Organizations and Counter Terrorism

*James Shaw-Hamilton, Director, The Humanitarian Forum*

The 2010 floods in Pakistan illustrate some of the problems that we, as the international community, need to tackle. Listed terrorist organizations took credit for being the first on the scene – just as they did after the Kashmir earthquake in 2005 – and in other cases where international non-profit organisations (NPOs) cannot provide an immediate response to intense development or humanitarian need, local NPOs do not have the capacity to do so and Governments or other providers do not have the skills.

Are we shooting ourselves in the foot? Can policies which target the financing of terrorism (CFT) through NPOs undermine broader counter-terrorism (CT) goals? [1] There are large demands for aid, terrorist organizations ready to take the credit for aid delivery – and human and political consequences to the way that CFT rules are implemented. Supporting the development of a stronger, more transparent and accountable NPO sector is essential in the broader context of countering terrorism. Looking at NPOs and accountability through a CFT lens ignores reality: we cannot change demand for aid, nor the urge to give charity. Poor CFT regulation or implementation can hamper the activities of NPOs, in particular humanitarian NPOs, and create a vacuum in which terrorist and violent extremist groups can take credit for relief activities. Governments should take a balanced approach in regulating NPOs, and enter into consultation and partnership with a growing sector. The NPO sector itself should share good practice and agree on standards.

The timing is crucial. In the first months of 2011, the popular uprisings in many countries in the Middle East and North Africa create a new opportunity to re-look at the relationship between the Government and civil society there. This relationship is vital in all countries.

### Recognising contradictory pressures

International CFT standards [2] apply in all countries, but it is left to each Government to decide how to implement them. It is vital that CFT is implemented in a way that does not disrupt development and humanitarian aid, otherwise CFT may well undermine CT.

The need for social welfare and international aid are perhaps greater than ever, while there are fewer available resources. In 2010, there were 373 natural disasters, killing over 296,800 people, affecting nearly 208 million others and costing nearly US\$110 billion [3]. The UN Office for the Coordination of Humanitarian Affairs (OCHA) refers to the “increasing vulnerability of populations and the growing magnitude of emergencies”[4] while the UN Secretary General refers to the “unacceptably slow” improvements in the lives of the poor [5].

The international community and western Governments cannot tackle this alone. All Governments are facing declining tax receipts and, therefore, budgets for essential social services. At the same time, development expenditure is often increasing due to changes in exchange rates, increased unemployment and rising food prices. At the same time, expectations on Governments are growing, with the Millennium Development Goals coming to an “end” in 2015 and because of international obligations of aid effectiveness. G8 Governments should also be applauded for continuing to stand by their commitment to spend 0.7% GDP on aid by 2015 – but this is not enough globally. Governments are realizing this, and there is an increasing reliance on other service providers and co-financers:

- Governments and international NPOs in “new” donor countries such as China, Saudi Arabia and the United Arab Emirates.
- Domestic NPOs in traditional donor countries, and many recipient countries.
- International NPOs registered in the west.

NPOs are an important means to deliver aid. Both beneficiaries and donors seem to prefer to give to or-



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ganizations that share their values, and predominantly prefer to give to culturally similar organizations [6].

Several studies demonstrate the importance of NPOs to areas at the heart of the UN Strategy, such as good governance, democracy, and the significant share they have in many countries' economies [7]. However, the size of the sector is very small in many places. Often, this is for structural reasons that Governments and others could change, such as the legal environment.

The imbalance between demand for aid and supply by NPOs allows listed terrorist organisations to fill the gap. If money is not spent, there is a lingering resentment by survivors against the Government or the international community, either for failing to help them and/or putting its attention to counter-terrorism rather than humanitarian relief. There is also a social welfare vacuum for terrorist organisations to fill: these “hidden” costs give an opportunity to terrorist organisations to increase their legitimacy. A US Treasury report into the 2005 Kashmir earthquake [8] said that terrorist organisations were sometimes the first on the scene, remained prominent throughout the emergency and seem to have been effective in their delivery of aid. It also reports a survivor saying that, if the terrorist organisation hadn't helped her, she would have died.

An analysis of CFT alone does not take this broader cost into account. Thus, it may be a CFT success that some countries do not allow public fundraising by NPOs or the transfer of funds by them overseas, but one must also look at other costs.

This brings us to the ways CFT rules are implemented. Many Governments do not have the tools to balance the contradictory pressures of providing basic human needs and of dealing with terrorism. The FATF Special Recommendation VIII talks about the need to regulate NPOs while its Interpretive Note suggests some ways to regulate NPOs from a CFT perspective. The UN Global Counter-Terrorism Strategy (2008) takes a more nuanced approach, placing CT within an understanding of peace promotion, security, sustainable development, human rights and rule of law [9]. There are few guidelines on how to work with NPOs.

In different countries, over-implementation of CFT happens in a number of ways:

- Governments apply bad rules, whether from lack of imagination or as an excuse to undermine civil society [10].
- CFT rules which are designed for a situation where a terrorist organisation controls the whole territory will have unintended consequences in territories where terrorist organisations coexist with legitimate NPOs.
- Governments apply rules “out of context”. The FATF and others have been very successful in getting global adoption of CFT rules, but circumstances differ greatly between countries.
- Other organisations are discouraged from dealing with NPOs, due to administrative costs and fear of litigation. In the absence of positive statements from Governments, risk-averse intermediaries are left with negative messages about CFT risk and unclear rules. It is not surprising – but it is unacceptable – that some private banks have told this author that they will not accept a client's instructions to transfer money to an Islamic NPO, whether or not that NPO appears on a list of terrorist organizations [11].
- NPOs themselves are becoming more risk-adverse, both about the countries they work in and the kind of work they do (eg peace-building is becoming increasingly hard).

### Counting the costs

There are costs to CTMs, but not all of these are considered or understood by Governments:

#### **Transaction costs**

- Stopped aid to beneficiaries.
- Delayed aid to beneficiaries.

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- Increased administrative costs reduce the amount of aid.

#### ***Collateral costs, or the foreseeable side effects of direct costs***

- Abandoned beneficiaries may become more susceptible to extremism.
- NPOs change the kind of work they do. This will have a direct impact on Governments’ ability to work more in “fragile states”.
- Aid which cannot be given to NPOs is driven underground.
- Terrorist organisations gain legitimacy.
- Aid is seen as increasingly politicized.
- Perhaps this is also the reason for increased insecurity of humanitarian workers.

#### ***Opportunity costs, or potential that is not met***

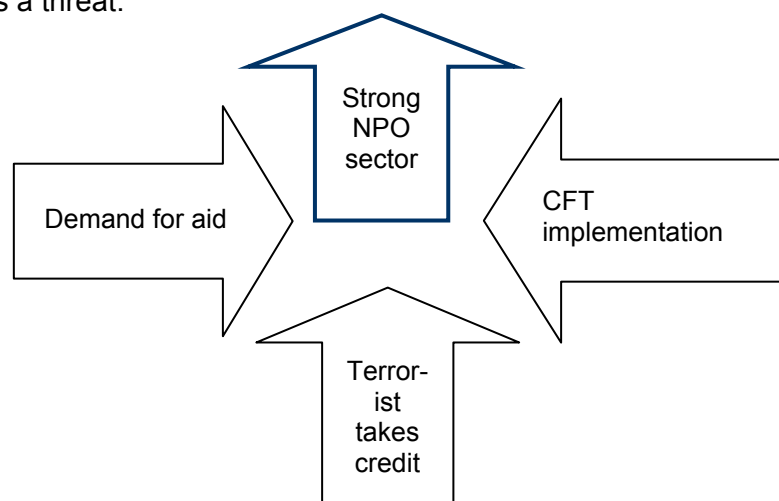
- Work is not done in the vital areas described in the UN Strategy – and in the regions that need it most.
- Charitable giving is untapped because Governments do not encourage private giving – and several discourage it.
- Aid cannot demonstrate that there is no Islamophobia.

These costs are hard to quantify. But we can say that it is not enough to look only at the risk of money being misused (which is also hard to quantify). We need to ask what is the impact of aid money not being spent at all.

### **A solution**

There are vast opportunities to counter the terrorists’ message – if aid can be delivered by legitimate NPOs. Beneficiaries do not choose aid from listed terrorist organizations, but are obliged to accept it if there is no sufficient alternative. At the same time, all but a small minority of donors would prefer to give in genuine ways: this well-meaning, but constrained, majority of donors needs to be enabled to do so.

This note suggests some ways to implement the ideas in the UN Strategy and to deal with competing demands. The solution is to increase aid. NPOs should be seen as an opportunity (and the sector made larger) rather than as a threat.



A larger, enabled sector will minimise the space within which terrorist organisations’ social activities thrive. This can happen by:

- Increasing the amount of giving that goes through NPOs, particularly amongst “non-traditional” donors. At the moment, much aid goes through unaccountable routes: only 1% of Kuwaiti charitable giving may go through NPOs.

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- Increasing the capacity of NPOs to deliver it, both in donor countries (including the Gulf) and recipient countries. This is partly about increasing the efficiency, accountability and transparency of existing NPOs. It is also about scale: there is 1 NPO per 42,000 people in Saudi Arabia, while there is 1 NPO per 200 people in the USA.
- Decreasing unaccountable and non-transparent aid through balanced regulation.

A number of things can be done to put this into effect, and this article concludes with recommendations to Governments and NPOs.

#### **Governments in both donor and recipient countries need to:**

- Encourage accountable charitable giving. This involves giving comfort to donors about the value of NPOs (and countering the weight of negative stories in recent years and the fear of criminalisation) and encouraging the creation of a philanthropic sector through a favourable tax environment for donors, endowments and NPOs.
- Create an enabling environment which helps the NPO sector to grow and operate independently. This includes making it easy to register NPOs, raise and transfer money, and work with volunteers. It also includes encouraging NPO alliances, networks and think tanks to grow, and funding them. As part of this, there needs to be a collaborative working relationship, where the Government involves the NPO sector on the development of social policy.
- Have a holistic approach to CFT and CT, both at a policy level and at an operational (departmental) one. This includes the Government giving comfort to banks and donors.
- Look at accountability more broadly. There are many reasons to be accountable, but too often NPOs go through the motions because of fear or routine. Positive reasons must be supported, such as quality, efficiency and use of money. The least helpful reasons for organisations to be accountable are for fear or routine, because this turns accountability into a box-ticking exercise. Accountability is a complex area, since it is worth thinking about why accountability is needed, what accountability should about and how it can be achieved. It is also worth bearing in mind that regulatory systems are poor at prediction, but can be very good at dealing with allegations of misuse. Therefore, the regulators need to rely on other people to strengthen accountability and to deal with non-serious issues. A number of other stakeholders already do this: the NPO's Board and staff, its funders and beneficiaries, and the media and wider NPO sector.
- Working with the NPO sector, research information gaps such as the amount of charitable giving and spending by region, including the proportion of this that goes through registered NPOs, and the quality of accountability (beyond regulation).
- Take a balanced approach to laws and regulation, so that these both protect the sector from misuse and promote it. As part of this, consider aspects of laws such as material support (the definition, a humanitarian exception to it and/or a good faith defence). The role of regulation should be to help NPOs to identify and manage risks, allowing them to operate in even the most unstable parts of the world even though (because ?) areas of humanitarian need so often overlap with concerns about terrorist organisations. The Charity Commission model may provide an answer[12].
- Fund NPOs, particularly those from another faith community and region. For example, it would have a big impact if a western Government funded a Muslim NPO from the Gulf or if a Muslim-majority country funded a Christian NPO.
- Advocate for these issues to other Governments and at multilateral institutions.
- Reward NPOs for quality.

#### **The NPO sector should:**

- Develop and share best practice.

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- Develop standards for financial management and “know your partner”.
- Agree joint understanding of accountability and transparency. A working group made up of practitioners from the east and west, together with expert advisers, can compare the key elements of accountability for western and Muslim NPOs, describe the overlaps and develop ways to embed better accountability.
- Create a robust Code of Quality. This needs to cover financial management and choice of partners, and have assessment/accreditation by a third party. This could also look beyond accountability to efficiency.

#### **Individual NPOs should:**

- Have a strong vision, strategy, and internal governance.
- Engage with the Government.
- Have transparent and accountable financial accounts, work and plans. As part of this, accounts should be externally audited and made available.
- Support national NPO networks.
- Evaluate projects, so that they are better at explaining and quantifying the impact of their work.

#### **End Notes**

The Humanitarian Forum is a global network of key humanitarian and development organizations from Muslim donor and recipient countries, the West and the multilateral system. We improve the effectiveness and efficiency of aid by addressing identified gaps between humanitarian communities through training, dialogue and cooperation, working internationally and in partner countries like Yemen.

- [1] Parts of this note draw on the ideas in James Shaw-Hamilton, “Recognising the umma in humanitarianism”, in Jon Alterman and Karin von Hippel, *Understanding Islamic Charities* (Washington DC: CSIS, 2007).
- [2] FATF Special Recommendation VIII [\[LINK\]](#) requires countries to review the adequacy of their laws and regulations to ensure that NPOs cannot be misused by terrorist organizations posing as legitimate entities, exploiting legitimate entities as conduits for terrorist financing, or wanting to conceal or obscure the clandestine diversion of funds.
- [3] 2010 Disasters in Numbers, Centre for Research on the Epidemiology of Disasters [\[LINK\]](#)
- [4] UN OCHA Plan 2011 [\[LINK\]](#).
- [5] UN Millennium Development Goals Report 2010 [\[LINK\]](#). This situation seems to affect Muslims or Muslim-majority countries disproportionately, through measures such as the proportion of people living in absolute poverty, the proportion of refugees and IDPs, and the amount of humanitarian aid received by Muslim countries. Bruno de Cordier “The ‘Humanitarian Frontline’, Development and Relief, and Religion”, *Third World Quarterly*, 30:4.
- [6] See for example, Jonathan Benthall in *Religion and Humanitarianism*, a conference organised by the Geneva Graduate Institute of International and Development Studies, October 2009. [\[LINK\]](#)
- [7] See James Shaw-Hamilton, “Recognising the umma in humanitarianism”, in Jon Alterman and Karin von Hippel, *Understanding Islamic Charities* (Washington DC: CSIS, 2007).
- [8] *Typologies and Open Source Reporting on Terrorist Abuse of Charitable Operations in Post-Earthquake Pakistan and India*, U.S. Department of the Treasury, 2006, [\[LINK\]](#)
- [9] A/Res/60/288, section I. These ideas are not new, since human security has long been understood to go beyond physical security. Human security was defined by the UNDP’s then Special Adviser Dr Mahbub ul Haq as economic, food, health, environment, personal, community and political securities (*Assessing Human Security in the Western Balkans*, CSIS-EKEM, [\[LINK\]](#)).
- [10] Doug Rutzen and Cathy Shea, “The Associational Counter-Revolution,” *Alliance* 11, no. 3 (September 2006).
- [11] Conversation with author, Geneva, May 2005.
- [12] *The Financial Challenge to Crime and Terrorism* (London: HM Treasury, 2007), pp 51, 52, [\[LINK\]](#). See [www.charitycommission.gov.uk/](http://www.charitycommission.gov.uk/) for additional information about the Charity Commission.



