PAVED WITH GOOD INTENTIONS

The Unintended Consequences of Terrorist Financing Controls on NPOs

What if controls for combating the financing of terrorism (CFT) also caused more suffering, and even death, in conflict zones because humanitarian aid could not be delivered in time? What if tight CFT controls resulted in fewer African girls going to school? What if, perversely, obstacles within the formal financial sector incentivised NPOs to use less transparent payment methods in order to get their money to where it is needed?

These are not hypothetical scenarios. For many years, efforts to comply with AML/CFT legislation have resulted in the undue targeting and de-risking of NPOs, with sometimes dire consequences. This is especially true for smaller NPOs and NPOs delivering humanitarian aid to conflict areas or high-risk countries.[II]

Over the past years, awareness of the de-risking issues faced by NPOs has grown both within the FATF as well as amongst public and private stakeholders across the compliance sector.

In consultation with the NPO sector, the wording of the FATF's Recommendation 8 – which identified NPOs as being "particularly vulnerable to terrorist abuse" – has been modified to emphasise that the focus should be on the relatively small number of NPOs that may actually be at risk.[III] Moreover, as of 2021, the FATF has commenced an investigation into the unintended consequences of its AML/CFT framework, including its impact on the work of NPOs. Similar attempts have also been made by some financial institutions seeking to address the indiscriminate de-risking of NPOs.

Despite this increased attention however, de-risking of NPOs remains a live issue. Many banks and financial service providers have taken an overly simplistic approach to the risk profiling of NPOs, placing them all in a high-risk category. Attempts to classify NPOs have often lacked nuance, and have failed to significantly improve the situation.

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Too often, NPOs are faced with a myriad of obstacles in obtaining access to bank accounts and carrying out transactions, making their daily work (almost) impossible. If any advice is forthcoming at all, it may be to game the system. In order to avoid raising alerts, NPOs hear that they should redefine the purpose of their charity as aid for schools 'in Africa', rather than in Uganda, or avoid explicit reference to 'Gaza' in wire transfers to projects in the Palestinian Authority.[IV]

The delays, denial of services and contrived 'workarounds' to the system are unsatisfactory. This White Paper explores, in brief compass, how a better understanding of the risks posed by NPOs, together with more nuanced risk assessments, can avoid unnecessary de-risking under Recommendation 8.

NPO DE-RISKING IN PRACTICE: WHAT IT MEANS, WHY IT MATTERS, AND WHY THE PROBLEM PERSISTS

The de-risking problems faced by NPOs are threefold. A first hurdle is the difficulty, especially for smaller NPOs, in opening bank accounts. This may be because banks consider them to be too risky from the outset, or because the aspiring client is unable to produce sufficiently detailed information throughout the due diligence process. The latter may be a result of lack of staffing within smaller NPOs, or of unclear or excessive demands from the bank –or both. Second, once they are clients, NPOs are confronted with blocked or delayed transfers. This often happens in relation to transfers to high-risk countries, which can trigger internal payment screening tools and/or necessitate a separate due diligence process being carried out by correspondent banks processing such transactions. Finally, NPOs are faced with sudden closures of their accounts, often without prior notice or explanation, or with the vague reasoning that their profile does not match the institution's risk appetite.[V]

The de-risking of NPOs is problematic as it undercuts a range of other important societal objectives. As summarized by the Global NPO Coalition on FATF, "the consequences of bank de-risking are undermining other policy goals and concerns such as those of economic development, the rollout of the UN Sustainable Development Goals, human rights protection, the creation of an enabling environment for civil society and last, but not least, the financial inclusion of the world's marginalised."[VI] The difficulties NPOs face in accessing financial services may even be counterproductive in the fight against terrorism, given that the work some charities do in improving educational and work opportunities may indeed contribute to lowered instances of crime and radicalisation.

However, at the micro-level, various reasons may explain why de-risking of NPOs occurs. One such reason stems from unfamiliarity. NPOs are not always fully aware of the AML/CFT framework with which banks must comply, nor with the bank's due diligence processes and the way in which they like to see their questions answered. Banks may also find themselves on unfamiliar terrain, with some financial institutions having highlighted that they have difficulty understanding the way in which NPOs work. To them, varying amounts of money raised via diverse (international) donors, coupled with often one-off project-based expenditures, seem random and difficult to follow. In other cases, the set-up of the NPO appears very complex, involving trustees, multiple areas of activities and global money flows.[VII]

Another reason for the reluctance to service NPOs is that, from the bank's perspective, they are generally low-profit customers yet high-cost in terms of compliance, and moreover give rise to reputational risk. For instance, one major Dutch bank has recently announced that it will temporarily stop opening new accounts for NPOs as these require additional compliance staff. It will also more than double the monthly fees for existing NPO accounts to reflect additional compliance resources that these entities demand.[VIII]

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GETTING RISK RIGHT

In response to the challenges NPOs face, various initiatives have been undertaken (see endnote)[IX]. As rightly pointed out by the FATF, the root cause of NPO de-risking lies in the non-implementation, or the incorrect implementation, of the FATF's risk-based approach.[X] There are at least three ways in which better risk assessments could immediately improve financial access for NPOs.

First, part of the problem can be attributed to the initial targeting of NPOs as high risk by the FATF itself and the lack of nuanced risk-scoring on the national level. The FATF's own assessment into Recommendation 8 states that "most countries are not yet conducting adequate risk assessments of their NPO sector, and fewer are conducting risk-based outreach and monitoring"[XI]. This observation can be confirmed by comparing the risk scoring of NPOs in various national risk assessments and the evidence provided (or lack thereof) to justify the score. Better national risk assessments on NPOs would also provide guidance to the private sector on producing their own tailored, realistic assessments of actual risks posed by NPOs.

Second, financial institutions need to revise their own approach to risk profiling in order to prevent unnecessary de-risking of NPOs. To help focus their resources on only those NPOs deemed to pose actual risk, and to make an informed risk analysis thereafter, financial institutions can undertake an assessment of their existing clients and create "whitelists" of trusted NPOs based on, for example, long-term business relationships; certification status; government endorsement; and transparency of legal/corporate structure, amongst other things. When designing an internal NPO-specific risk matrix, it is important that the tool reflects the fact that, amongst the thousands of NPOs operational within a country, only a handful (at most) might turn out to be potentially problematic.

Third, existing information can be better exploited through research and tech-based efficiency gains. While only a very small fraction of NPOs has been involved in terrorism financing (whether consciously or otherwise), we can collect, analyse and compare those known cases to improve our knowledge and potentially identify trends or patterns. Although the discussion is often limited, Europol's TE-SAT report, reports by the FATF and certain NRAs do provide examples of the misuse of NPOs by terrorists. Contrasting the lessons learned from these cases with the customer base of a financial institution may help to further narrow the focus on potentially high-risk NPOs.

Ultimately, it must be recalled that financial integrity cannot be achieved without financial inclusion. Widespread de-risking of NPOs is not conducive to the fight against terrorism financing and can in fact frustrate CFT objectives (as well as the critical work of NPOs themselves). Effective adherence to FATF's Recommendation 8 demands greater nuance and critical engagement with the risks actually posed by individual NPOs. It is a systemic issue that must be addressed at the intergovernmental level, at the national level, and indeed within the private sector, by the gatekeepers themselves. By getting risk right, we can improve CFT compliance without compromising the social and economic progress advanced by NPOs.

FATF RECOMMENDATION 8 ON NON-PROFIT ORGANIZATIONS

Countries should review the adequacy of laws and regulations that relate to NPOs which the country has identified as being vulnerable to terrorist financing abuse.

Countries should apply focused and proportionate measures, in line with the risk-based approach, to such non-profit organisations to protect them from terrorist financing abuse, including:

(a) by terrorist organisations posing as legitimate entities;

(b) by exploiting legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset-freezing measures; and

(c) by concealing or obscuring the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.

[I] This paper has benefitted from the comments and suggestions from several Acuminor colleagues, notably Stephanie, Rob, Ellinor and Andrea.

[II] European Center for Non-Profit Law & Human Security Collective (2018) Understanding the Drivers of De-risking and the Impact on Civil Society Organizations, available at: NEW HSC/ECNL RESEARCH REPORT: Understanding the Drivers of 'De-risking' and the Impact on Civil Society Organizations | Global NPO Coalition on FATF (fatfplatform.org)

[III] FATF (2015) Public Consultation on the Revision of the Interpretive Note to Recommendation 8 (Non-profit organisations), available at: Documents - Financial Action Task Force (FATF) (fatf-gafi.org)

[IV] Evidence collected by the author during workshops and private conversations.

[V] Global NPO coalition on FATF (2022) De-risking & Financial Access, available at: De-risking & Financial Access | Global NPO Coalition on FATF (fatfplatform.org)

[VI] Global NPO Coalition on FATF (2022) De-risking and Financial Access, available on: De-risking & Financial Access | Global NPO Coalition on FATF (fatfplatform.org)

[VII] European Banking Authority (2022) EBA Opinion and annexed report on de-risking, p. 23, published on 5 January 2022, available on: EBA Opinion and annexed report on de-risking.pdf (europa.eu)

[VIII] Nu.nl (2022) Goede doelen kunnen geen rekening openen bij ING door personeelstekort (Charities can't open accounts at ING because of staff shortages), published on: 19 August 2022, available at: Goede doelen kunnen geen rekening openen bij ING door personeelstekort | NU - Het laatste nieuws het eerst op NU.nl.

[IX] In the UK, the Netherlands and several countries of the Western Balkans multi-stakeholder dialogues have been created to increase familiarity between NPOs and the financial sector. These dialogues have also included professional and international organizations and national government bodies. One of the outcomes of such a dialogue has been to streamline the expectations of the financial sector when NPOs want to open a bank account. Other initiatives include events from NPO umbrella organisations to inform the sector how to navigate the opening and maintaining of bank accounts. Some banks have also created specific processes to help NPOs and facilitate their needs.

[X] FATF (2021) High-Level Synopsis of the Unintended Consequences of the FATF Standards, p. 4, published on: 27 October 2021, available on: Unintended-Consequences.pdf (fatf-gafi.org).

[XI] Idem, p. 4. Some notable exceptions of countries who did make a sector specific NPO risk assessment are: the UK, Jersey, Mauritius, Tunesia, the Western Balkans and Turkey.

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