

# De-Risking 101: Nonprofit Organizations Seeking Financial Access

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# Derisking

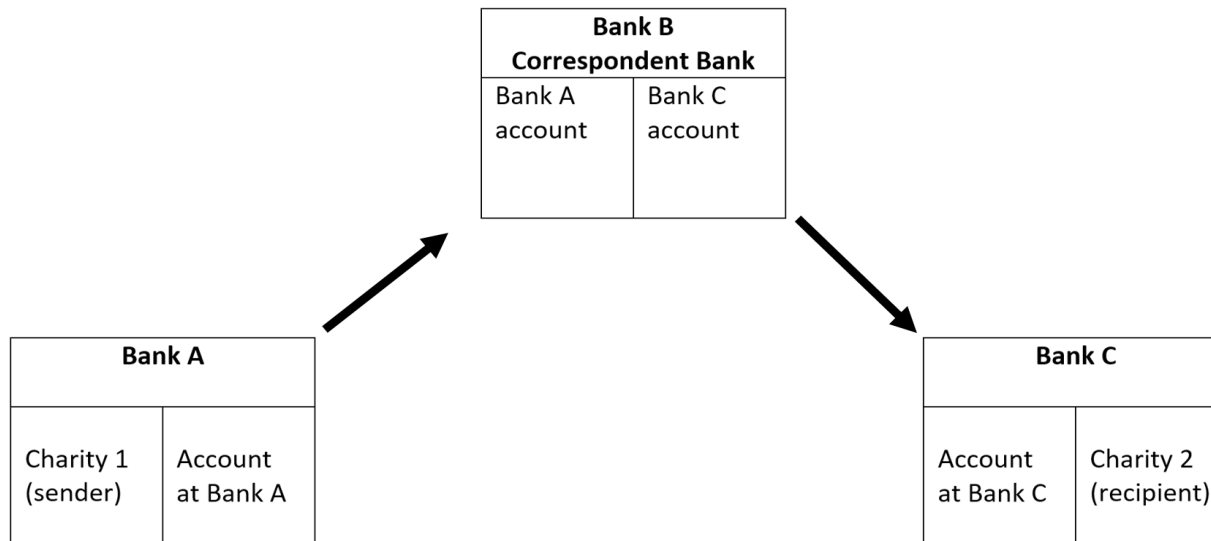
- Financial institutions terminating or restricting business relationships to avoid, rather than manage, risk
- An established trend with complex drivers – banks' concern for running afoul of regulatory requirements/expectations

- Financial institutions are concerned about record penalties and settlements, compliance uncertainty, and excessive regulatory scrutiny. This has shifted their risk-reward calculus away from banking NPOs.
- De-risking of nonprofit organizations coincides with an unprecedented need in regions of conflict, humanitarian crises, and natural disasters.

# Correspondent Banking

The provision of an account, and related services, by one bank “the correspondent bank” to another financial institution “the respondent bank”, including affiliates, used for the execution of third-party payments and trade finance, and other services

## Basic Process for Cross-Border Financial Transfers



# International Framework for Counter-Terrorism Financing: United Nations

After 9/11, the UN Security Council quickly passed Resolution 1373 urging member states to criminalize terrorist financing, prevent and suppress terrorist financing, and freeze assets associated with terrorist financing.

# International Framework for Counter-Terrorism Financing:

## Financial Action Task Force

Established by G-7 in 1989. The global standard-setting body for anti-money laundering (AML) and counter-terrorism financing (CFT) standards:

- 198 countries have committed to implement the standards
- 9 special recommendations on CFT (issued 2001-04): Recommendation 8 on nonprofit organizations: *until last year*, stated that NPOs were “particularly vulnerable” to terrorist abuse

- The Interpretive Note to Recommendation 8 tried to provide nuance, stating, “measures adopted by countries to protect the NPO sector from terrorist abuse should not disrupt or discourage legitimate charitable activities.” However, overall perception in the Recommendation was pervasive.
- June 2016: “particularly vulnerable” language was removed from Recommendation 8, but the perception remains.

# FATF: Why Does It Matter?

- Countries implement CFT laws and policies based on FATF recommendations and guidance.
- R1: National Risk Assessment (NRA)  
*Countries should identify, assess, and understand the money laundering and terrorist financing risks for the country... (FATF Methodology, 2016)* Countries are required to get input from nonprofits when developing the NRA
- R8: Identifying NPOs at risk  
*...identify the features and types of NPOs which by virtue of their activities or characteristics, are likely to be at risk of terrorist financing abuse. (FATF Methodology, 2016)*
- FATF standards and a country's NRA forms the foundation for the country's CFT laws.



# EU Supranational Risk Assessment: June 2017

- NPOs represent significant threat *when they are misused*; vulnerability of NPOs to misuse is significant
- NPOs *may be exposed to risk* of being misused for terrorist financing purposes
- Controls appear in place when dealing with transfer of funds within EU – *transfer outside EU more vulnerable*
- NPO Risk Scenarios:
  - Establishment of NPOs to fundraise for TF
  - Abuse of NPOs
    - Complicit NPOs supporting terrorist groups
    - Legitimate NPOs exploited by “outsiders”
    - Legitimate NPOs exploited by “insiders”

## EU SNRA (cont.)

- Recognizes concern about de-risking; this should be kept in mind when developing policy
- Does NOT suggest EU regulation of NPOs, but Member States should ensure appropriate NPO coverage in their national RAs.
- Calls on EC to organize multi-stakeholder exchanges and to provide more guidance/training for NPOs that receive EU funding

# UK National Risk Assessment: Oct. 2017

- Moves assessment of risk of abuse of NPOs from medium-high (2015) to **low**
- Risk concentrated in charities working internationally
- Most linked to terrorist financing are victims of internal abuse by employees/volunteers/trustees, looting in country, or linked to aid convoys
- De-risking may push charities out of intensely regulated areas into higher-risk transaction methods including cash or MSBs.

# US National Risk Assessment: Sept. 2015

- Abuse of the charitable sector tends to involve individual fundraisers claiming a charitable purpose but “*outside of any charitable organization recognized by the U.S. government.*”
- Charities operating overseas, “particularly in high-risk areas where terrorist groups are most active,” can face significant risk.
- Treasury did not conduct public outreach to solicit input or comments. The 61-page document is based solely on government sources.

# EU Counter-terrorism Financing Laws and Regulations

## 4<sup>th</sup> Anti-Money Laundering Directive

- Focus on transparency, beneficial ownership, and enhanced customer due diligence
- Enhanced risk-based approach, including requiring evidence-based measures
- NPOs: *could be* subject to directive if they fulfill certain requirements
- Trusts and other similar legal entities: subject only if they generate tax consequences
- Unclear how this will evolve at the national level

# UK Counter-terrorism Financing Laws and Regulations

- Sanctions regime – operated by Office of Financial Sanctions Implementation (OFSI, created in 2016)
- Proceeds of Crime Act 2002 (POCA)  
Terrorism Act (TACT)
- Terrorist Asset-Freezing etc. Act 2010
- The Money Laundering, Terrorist Financing and Transfer of Funds Regulation 2017

Reminder: Until Brexit negotiations are concluded, the UK remains a full member of the EU and all the rights and obligations of EU membership remain in force.

# U.S. Counter-terrorism Financing Laws and Regulations

- Bank Secrecy Act – requires financial institutions to report suspicious activity
- Sanctions regime (against countries, individuals and non-state armed groups) – implemented and enforced by the U.S. Treasury’s Office of Foreign Assets Control (OFAC)
- Executive Order 13224 – authorizes US Treasury to designate foreign and domestic individuals and organizations as terrorist entities; prohibits interactions with these entities.
- Prohibition on material support of terrorism

# Extraterritorial Jurisdiction and Enforcement

The extraterritorial reach of OFAC impacts both U.S. and international banking. Most transactions in U.S. dollars are within OFAC's jurisdiction because they pass through the U.S., even if both sender and recipient are located outside the US.



*“Simply put, the blizzard of counter-terrorism legislation that has been produced by governments and multilateral organisations since 9/11, particularly as it regards financing and material support, is leading banks to operate with increasing conservatism. This is restricting financial access for clients deemed ‘outside [the] risk appetite’ of the banking sector. Many of those excluded from the system are NGOs, primarily those operating internationally and across borders in ‘high risk’ jurisdictions.”*

- Tom Keatinge in the report *Uncharitable Behavior*

# **Humanitarian Action and Non-state Armed Groups: The Impact of Banking Restrictions on UK NGOs**

**By Tom Keatinge and Florence Keen**  
Published April 2017 by Chatham House



# Report: Qualitative Data

NPOs are experiencing:

- Increased documentation requests
- Increased costs
- Delays of wire transfers
- Account closures

# Three Hundred UK Charities Hit by Global Crackdown on Illegal Funds



REUTERS

July 27, 2017

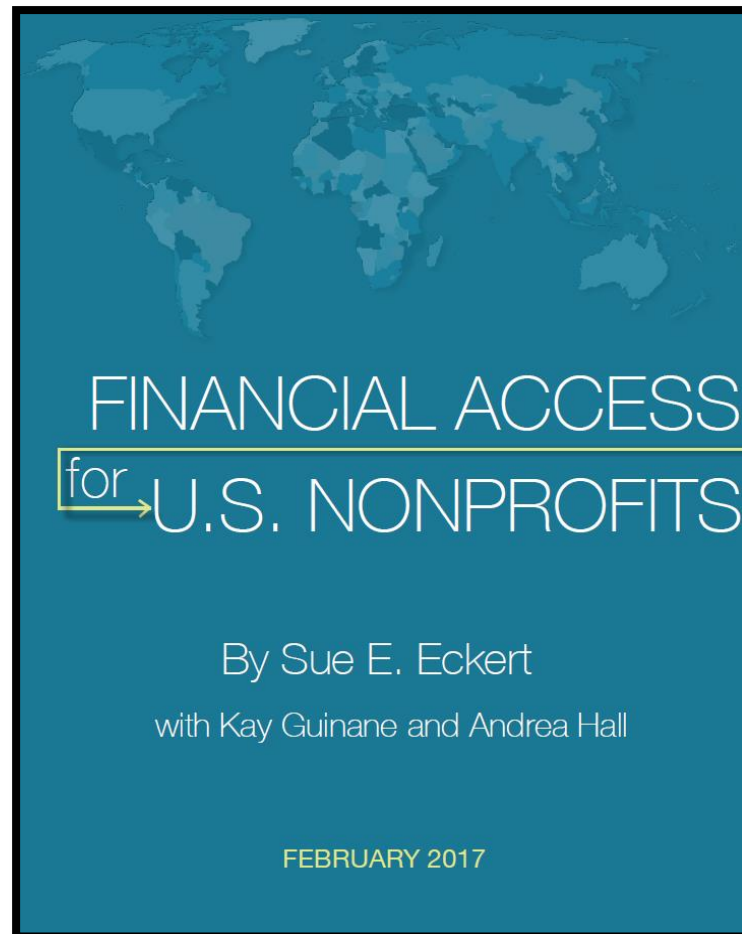
- 300 UK charities' bank accounts closed in last 2 years
- Operations disrupted at 1,000s more due to delayed wire transfers
- Charities experience disruption on daily or weekly basis
- 1 small charity shut down due to inability to open a bank account
- HSBC and Co-Operative Bank closed the most accounts

[www.reuters.com/article/us-banks-charities/three-hundred-uk-charities-hit-by-global-crackdown-on-illegal-funds-idUSKBN1AC0FH](http://www.reuters.com/article/us-banks-charities/three-hundred-uk-charities-hit-by-global-crackdown-on-illegal-funds-idUSKBN1AC0FH)

# Financial Access for U.S. Nonprofits

By Sue Eckert with Kay Guinane and Andrea Hall

Published February 7, 2017 by Charity & Security Network



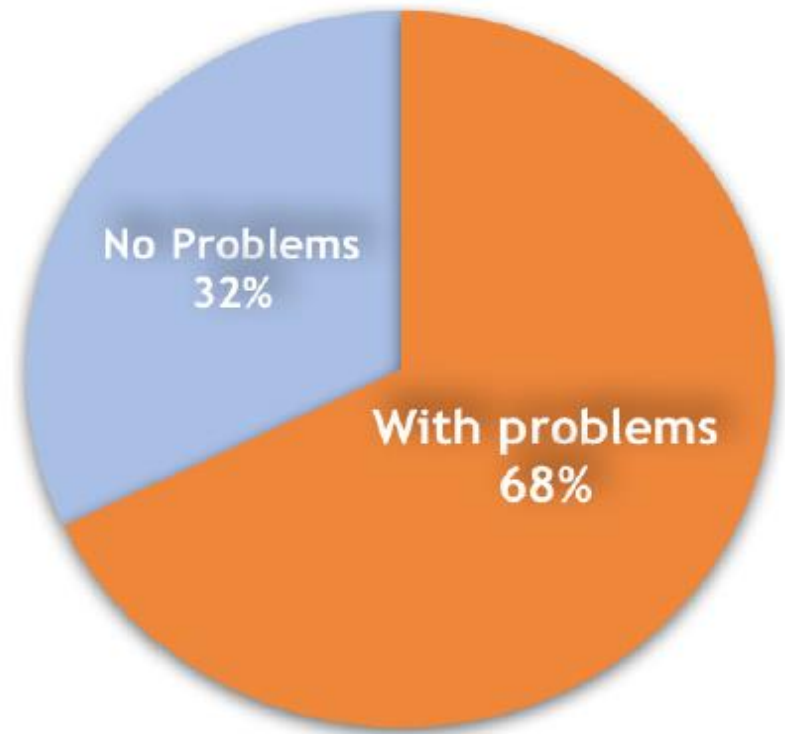
# Methodology

**Quantitative:** Random sample survey drawn from universe of 8,665 US-based NPOs (IRS filings). Telephone interviews with financial officers/executives of 305 NPOs (response rate of 38%; findings valid within 5.4% margin of error)

**Qualitative:** Data derived through focus groups, roundtables, and interviews with various stakeholders in government, the financial sector, former regulators and nonprofit leaders

# Scope of NPO Financial Access Problems

A significant proportion (2/3) of NPOs that conduct international work are experiencing obstacles in accessing financial services.



# Frequency of Financial Access Problems

Frequency of financial access problems	Total organizations (percent)	Total organizations likely impacted
Constant	5.4	468
Regular	9.7	841
Occasional	31.2	2,703
Rare	21.5	1,863
Never	32.2	2,790
<b>TOTAL</b>	<b>100.0</b>	<b>8,665</b>

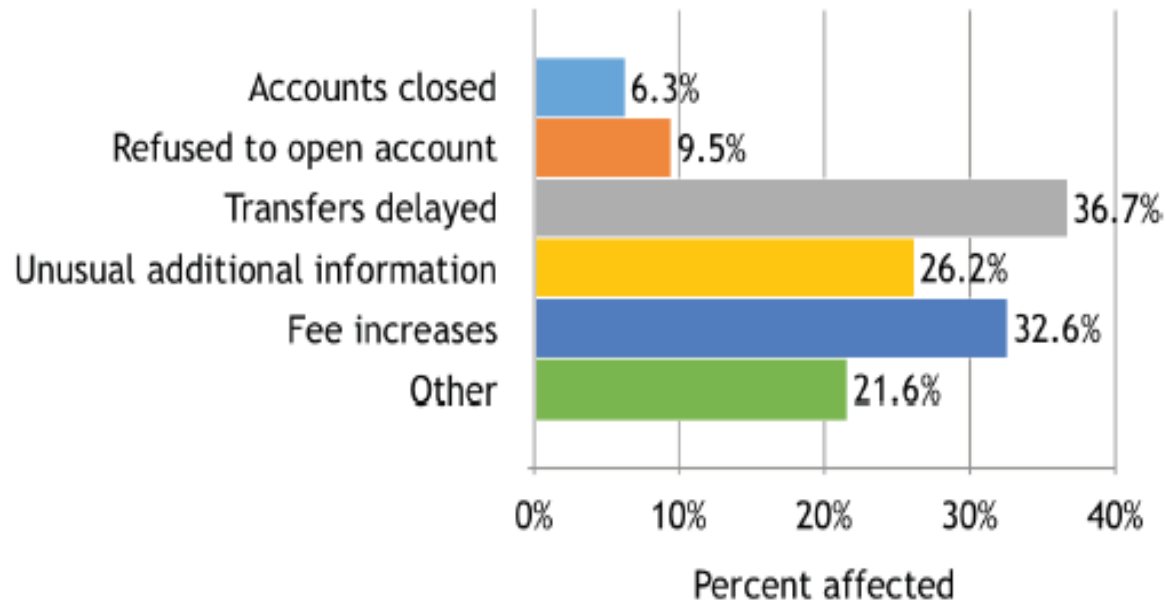
Over 15% of NPOs encounter these financial problems constantly or regularly, with another 31% reporting occasional problems.



# Types of Financial Access Problems

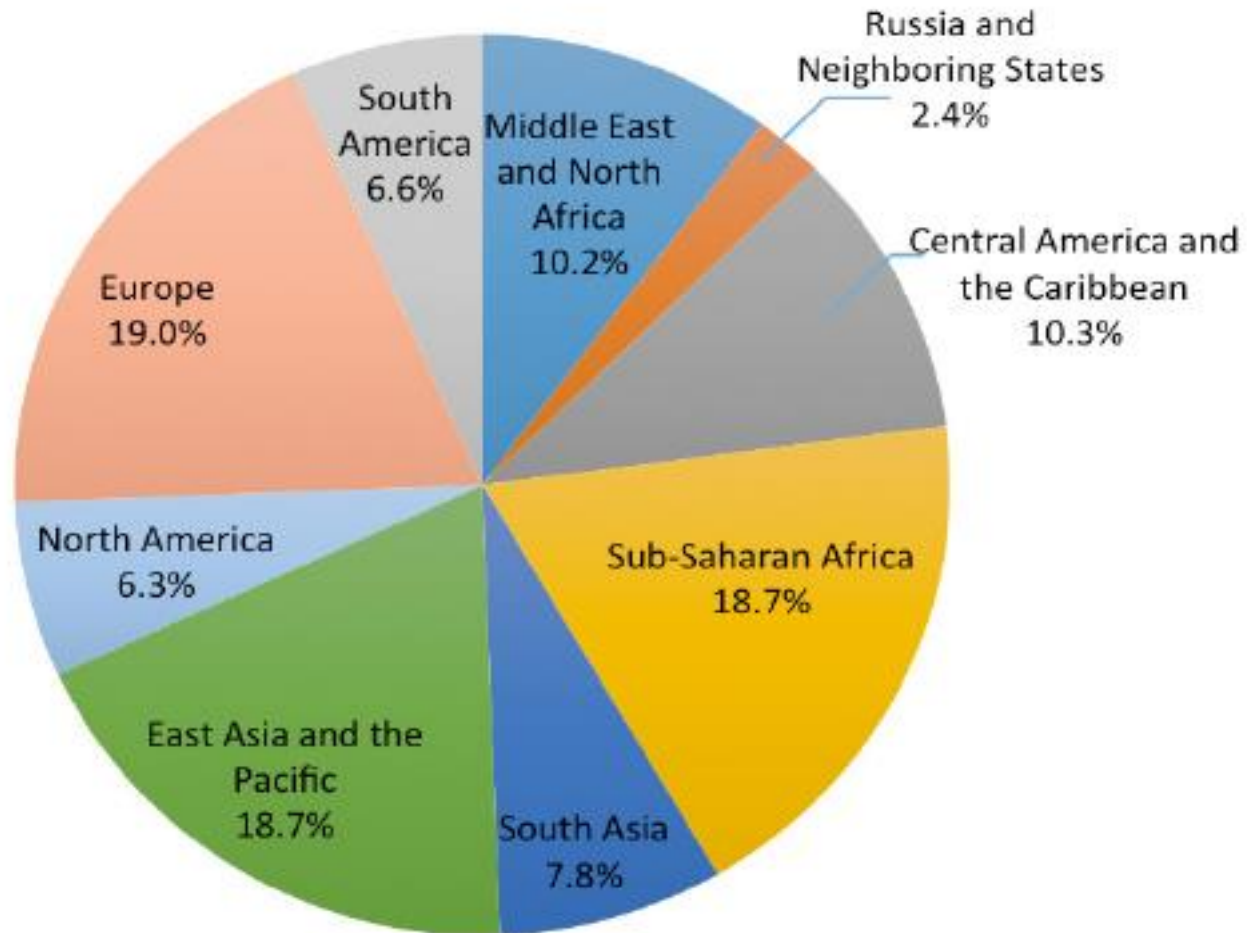
The two most common problems encountered by NPOs are delayed wire transfers and increased fees. Although account closures are less common than transfer delays, they can have an extraordinary impact.

***Prevalence of Financial Access Problems\****



\*Percentages do not total 100% because survey respondents were allowed to give more than one response.

# Destinations of Delayed Wire Transfers



# Strategies NPOs Use to Address Problems

NPOs utilize a variety of strategies to cope with financial access problems, some of which put the safety of their staff and the integrity of the financial system at risk. Of significant concern is the data indicating that 42% of NPOs resort to carrying or sending cash when traditional banking channels become unavailable.

## *Strategies Used to Address Problems\**

<b>Strategies</b>	<b>Percent of NPOs Utilizing</b>
Carry cash	41.7
Cancel the program	3.4
Find another financial institution	36.5
Use money remitter (Western Union or similar)	29.4
Performed a transaction successfully later	67.2
Other	24.9

\*Percentages do not total 100% because survey respondents were allowed to give more than one response.

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