



FINANCIAL ACCESS

for → U.S. NONPROFITS

By Sue E. Eckert

with Kay Guinane and Andrea Hall

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ABOUT THE CHARITY AND SECURITY NETWORK

The Charity & Security Network is a resource center for nonprofit organizations to promote and protect their ability to carry out effective programs that promote peace and human rights, aid civilians in areas of disaster and armed conflict and build democratic governance.

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List of Acronyms

AAPOR	American Association of Public Opinion Research
ABA	American Bankers Association
ACAMS	Association of Certified Anti-Money Laundering Specialists
AML	anti-money laundering
AML/CFT	anti-money laundering/countering the financing of terrorism
BBA	British Bankers' Association
BSA	Bank Secrecy Act
C&SN	Charity & Security Network
CB	correspondent banking
CFT	countering the financing of terrorism
CGD	Center for Global Development
CTITF	Counter-Terrorism Implementation Task Force
EO	Executive Order
EIN	employee identification numbers
FATF	Financial Action Task Force
FATF R8	FATF Recommendation 8
FBI	Federal Bureau of Investigation
FDIC	Federal Deposit Insurance Corporation
FFIEC	Federal Financial Institutions Examination Council
FI	financial institution
FinCEN	Financial Crimes Enforcement Network
FSB	Financial Stability Board
G-20	Group of Twenty
GMU	George Mason University
IMF	International Monetary Fund
IRS	Internal Revenue Service
ISIL	Islamic State of Iraq and the Levant
KYC	know your customer
KYCC	know your customer's customer
MENA	Middle East & North Africa
ML/TF	money laundering and terrorist financing
MSB	money service business
MTO	money transfer operator
NGO	non-governmental organization
NPO	nonprofit organization
NTEE	National Taxonomy of Exempt Entities
OCC	Office of the Comptroller of the Currency
OFAC	Office of Foreign Assets Control
P/CVE	preventing/countering violent extremism
PEP	politically exposed persons
PVO	private voluntary organization
RBA	risk-based approach
SAR	suspicious activity report
SDG	sustainable development goal
SDN	specially designated nationals
SWIFT	Society for Worldwide Interbank Financial Telecommunications
TF	terrorist financing
UN	United Nations
USAID	United States Agency for International Development
USG	U.S. government

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EXECUTIVE SUMMARY

In response to the September 11, 2001 attacks on the United States, the regime to deny terrorists and criminals access to the global financial system has significantly expanded. Financial institutions (FIs), the lynchpin of the system, are required to employ a “risk-based approach” to assess their money laundering and terrorist financing (ML/TF) vulnerabilities, know their customers, and implement compliance programs to manage and mitigate situations of higher risk.

Over time, a number of factors, including anti-money laundering (AML) and countering the financing of terrorism (CFT) regulatory obligations and oversight of FIs, have led to the phenomenon of “derisking.” This refers to the trend of financial institutions terminating or restricting business relationships to avoid rather than manage risk. The most frequently mentioned driver of derisking, as cited by FIs, is the concern for running afoul of regulatory requirements.

There are costly consequences of derisking for a variety of sectors, including nonprofit organizations (NPOs). In particular, examples have come to light of lifesaving assistance stymied as a result of charities’ inability to transfer funds to foreign countries, including humanitarian disasters in Syria, Somalia and other conflict areas. Banks under pressure to comply with AML/CFT regulatory expectations and sanctions have delayed or denied financial transfers and closed accounts, complicating efforts by charities and humanitarian groups trying to deliver aid.

Until now, there have been no data indicating the scope and type of difficulties U.S. NPOs might be experiencing. This research initiative, commissioned by the Charity & Security Network and supported by the Bill and Melinda Gates Foundation, was undertaken to develop empirical data to inform the policy discussions concerning derisking and financial access.

With this report, *the question as to whether financial access is a problem for NPOs has now been answered: it definitively is.* Years of anecdotal evidence reported by NPOs regarding difficulties with financial services are now confirmed through a random sample survey of U.S. nonprofits, using Internal Revenue Service data on public charities that do international work (NPOs).

Survey Results Show There is a Systemic Problem

This report presents empirical data from the random sample survey undertaken for this study. The findings are valid within a 5.4% margin of error. The results paint a picture of significant problems, affecting many kinds of NPOs operating in all parts of the globe. Highlights of the survey findings are below:

Characteristics of U.S. NPOs Working Internationally

- There are 8,665 U.S. NPOs operating abroad (based on IRS data).
- They work in a range of sectors, including education, development/poverty reduction, humanitarian relief, public health, medical services, human rights/democracy building and peace operations/peace building, among others.
- 45% of all U.S. NPOs engage in humanitarian relief work.
- Most NPOs are relatively small (median revenues of \$1.5 million and expenditures of \$1 million), but almost half of them (48%) are large enough to operate a branch or field office abroad.

Financial Access Problems

- 2/3 of U.S.-based NPOs working internationally experience banking problems.
- The most common problems include: delays of wire transfers (37%), unusual documentation requests (26%), and increased fees (33%). Account closures represent 6% and refusal to open accounts 10%.
- 15% encounter these problems constantly or regularly.
- The prevalence and types of problems vary by program area, with NPOs working in peace operations/peacebuilding, public health, development/poverty reduction, human rights/democracy building, and humanitarian relief reporting the greatest difficulties.
- Transfers to all parts of the globe are impacted; the problem is not limited to conflict zones or fragile and failing states.
- NPOs with 500 or fewer staff are more likely to encounter delayed wire transfers, fee increases, and account closures. Most significantly, smaller organizations are almost twice as likely to receive unusual additional documentation requests. The smallest NPOs (those with 10 or fewer employees) are having the most trouble opening accounts.
- NPOs, categorically treated as high-risk, are sometimes forced to move money through less transparent, traceable, and safe channels as a result of delays in wire transfers and requests for additional documentation.

The scope of the problem, which affects 2/3 of U.S. NPOs and programs in all parts of the world, constitutes a serious and systemic challenge for the continued delivery of vital humanitarian and development assistance – a core component of American foreign and security policies. As a result, financial access for NPOs must be recognized as a barrier that needs to be addressed on par with correspondent (intermediary) banking and money service businesses (MSBs). It is time to move beyond discussions of whether there is a problem, arguments over definitions, and the finger-pointing that have characterized the issue to date. Now is the time to seek solutions.

As NPOs' ability to access the financial system has been hampered, the level of humanitarian need worldwide has reached all-time highs. Refugees fleeing war, climate disasters and political repression have generated the largest number of displaced people since World War II, making the programs U.S. NPOs operate in other countries more important in saving lives and preventing the further erosion of democracy and human rights.

The Drivers of Narrowing Financial Access for NPOs Are Complex

There is no simple or singular reason for derisking generally or of NPOs specifically, and this study does not contend that all decisions by FIs to terminate NPO accounts or delay wire transfers are attributable exclusively to AML/CFT concerns. However, interviews for this report, as well as regular surveying of the financial industry, consistently demonstrate that FIs' compliance-related concerns and regulatory expectations are among the most significant reasons for derisking. A multiplicity of factors has indeed created a "perfect storm" resulting in serious unintended consequences which limit financial access for NPOs.

For many FIs, decisions to withdraw or decline to provide financial services involve customers perceived to be higher-risk, such as NPOs, and higher-risk jurisdictions (often the countries where humanitarian assistance and development NPOs work). Routine second-guessing of FIs' decisions and treatment of certain clients as categorically high risk by bank examiners require FIs to undertake extensive and expensive steps to mitigate those risks, tipping the risk-reward scale toward exiting such relationships. Despite reassuring statements from government officials, FIs perceive a clear disconnect between what policy officials say and what happens at the individual bank examination level.

Action Is Needed

To effectively address the problems of derisking/financial access, all stakeholders must work together in a concerted effort. Solutions will only be found if the problem is approached as a shared responsibility. Policymakers' characterizations of these issues as solely "commercial decisions" ignores reality and is a recipe for continued derisking and all of its consequences.

There has been little recognition by U.S. officials that financial access is a problem for NPOs, in contrast to the public acknowledgement of derisking in the context of correspondent banking and MSBs. U.S. policymakers and regulators appear reluctant to take NPOs' concerns seriously or to address these issues. Skepticism, along with long-held attitudes that the NPO sector is high-risk, pervades many discussions, from the policy levels down to individual bank examiners. FIs are likewise reluctant to devote resources to address issues regulators do not treat as a priority.

The result is a clear lack of leadership and accountability on derisking issues, as noted in previous reports. Government points to the private sector, banks point at regulators, and NPOs are frustrated and left without financial services. A recent dialogue initiated by the World Bank and Association of Certified Anti-Money Laundering Specialists (ACAMS) shows promise in bringing stakeholders together.

All parties would benefit from solutions to these financial access issues, but the associated cost makes it unlikely that any individual group can or will undertake them alone. The ideal solution is therefore, collective action, the cost of which is shared. Leadership from policymakers and regulators is necessary, starting with acknowledgment of the seriousness of the issue, and moving to action to clarify regulatory expectations and articulate a coherent policy.

Inaction is Costly

Importantly, the human costs of NPOs' financial access difficulties and continued inaction must be recognized. When programs are delayed or cancelled because of the inability to transfer funds, peace is not brokered, children are not schooled, staff is not paid, hospitals lose power, the needs of refugees are not met and in the worst cases, people die. Maintaining current policies in the face of evidence of the negative humanitarian consequences is not only harmful but inconsistent with American values.

There are multiple interests at stake in the derisking crisis. In this context, broader foreign policy and security concerns appear to be underappreciated. The goals of financial inclusion and financial integrity have been characterized as incompatible, but both can be achieved. Ironically, current policy has created consequences that increase the risk of illicit finance. Because these problems are not being effectively managed, U.S. policy objectives of development, humanitarian assistance, and even countering terrorism and violent extremism are negatively impacted.

Protection of the global financial system from abuse by criminal and terrorist organizations has been and will continue to be an essential element of U.S. national security policy. A key component of multilateral counterterrorism/countering violent extremism (P/CVE) initiatives is the ability of civil society organizations to engage and support local populations where terrorism takes root. NPOs play a vital role in this effort.

The U.S. government process to address financial access issues, however, remains heavily weighted to illicit finance concerns, with the range of other agencies and interests not playing a commensurate role. Ultimately, even AML/CFT objectives are not promoted when financial access of NPOs is restricted. Excessive regulatory expectations and enforcement are pushing more money into opaque channels where it is more likely to fall into the wrong hands. Fear of compliance failures results in a vacuum that is likely to be filled by less transparent and accountable financial institutions, undermining the integrity of the global financial system and U.S. security.

Recommendations

There are several promising avenues for stakeholders to explore. The recommendations and options discussed in this report should be viewed as the starting point in a process that moves toward solutions and in no way do they exclude additional ideas that emerge from further consideration of the problem. However, in order to be effective, solutions must meet these basic criteria:

- Address the drivers of narrowing financial access for NPOs
- Adapt to all sizes of NPOs and FIs
- Improve the implementation of the risk-based approach to AML/CFT programs
- Avoid anything that would make compliance more complex and burdensome

This report recommends the following:

Launch a Solutions-Oriented Multi-Stakeholder Dialogue

There is an urgent need for all stakeholders to collaboratively review the existing illicit finance system and the policies designed to prevent it, and work to address the serious and systemic problems hindering financial access for U.S. nonprofits. For that reason, this report's top recommendation is for a multi-stakeholder dialogue to work towards solutions to NPO financial access problems.

Update the Bank Examination Manual and Bank Examiner Training

As enforcers of the Bank Secrecy Act with the ability to impose civil fines, Federal Bank Examiners are key to regulatory oversight and significantly influence FI behavior. As this report reveals, their work is often intrusive, second-guessing FIs' due diligence procedures and applying pressure that increases compliance costs and discourages FIs from serving their NPO customers. In addition, regulatory oversight often varies by examiner and the inconsistency adds to FI uncertainty. As suggested by multiple FIs interviewed for this report, a program is needed to re-train examiners to bring them up to date on the risk-based and proportionate framework, to create consistency between FI examinations, and to emphasize that NPOs are not by definition high-risk customers.

The NPO section of the Bank Examination Manual has not been updated to reflect the June 2016 changes in the Financial Action Task Force's Recommendation 8. A collaborative effort between FIs, NPOs and the Federal Financial Institution Examination Council is needed to remove outdated language concerning risk assessment of NPOs. The resulting revision should guide FIs through a proportionate risk-based approach.

Create an NPO Repository/Utility to Streamline FI Customer Due Diligence

Technology-based solutions that enable effective and proportionate FI compliance, often referred to as “utilities,” can tackle much of the paperwork and oversight that results in rising compliance costs and hence, restricted financial access for NPOs. These utilities can eliminate much of the burdensome and duplicative documentation requests cited by numerous focus group participants. One proposal calls for a repository created specifically for NPO financial access purposes that would set out customized criteria that allow all types of organizations—large and small, established and new, secular and religious—to be included. FIs could then use the repository to collect information for their customer due diligence, obtaining it quickly and inexpensively. Using existing models as a guide, a team of lawyers and financial industry experts would evaluate the information submitted by NPOs.

Create a Special Banking Channel for Humanitarian Crises

As discussed in Chapter 7 of this report, the most profound and perhaps devastating impact of NPOs' financial access problems is the loss of humanitarian programming. When the international financial system is not able to meet the needs of NPO customers doing humanitarian work, new and special procedures to facilitate the transfer of funds overseas may be needed. Given the dire humanitarian need in places like Syria, it is even more important that fund transfers are timely and that NPOs have access to bank accounts. Although special procedures would not address the systemic problem revealed by this study, they could alleviate some of the most dangerous and serious impacts.

Institute Safe Harbor Protections

The World Bank/ACAMs dialogue suggested the creation of safe-harbor provisions, whereby FIs that bank NPOs in good faith and meet certain criteria would be held harmless if funds inadvertently ended up in the wrong hands. Adopting a safe harbor would give U.S. banks confidence that they can do business with higher-risk customers and regions provided they maintain rigorous risk-mitigation controls that are recognized by regulators. Investment in consistent and effective due diligence procedures would lessen the threat of prosecution or regulatory enforcement, or at a minimum, cap penalties at nominal amounts. This approach could be highly effective in expanding financial access for NPOs.

Improve Implementation of the Risk-based Approach

FATF has updated its risk-based approach to make it proportionate and ensure that it does not negatively impact the work of legitimate NPOs. This framework is focused on effectiveness, and is relatively new. In particular, the notion of residual risk acceptance, inherent in the risk-based approach, is not always reflected in current rules or enforcement policies. As the FATF noted in its 2016 mutual evaluation of the U.S., terrorist financing and sanctions violations “are strict liability offenses.” There is an inherent tension between strict liability and a risk-based approach that appears to contribute to narrowing financial access for NPOs. Steps to improve implementation of the risk-based approach include:

- Counter the outdated portrayal of NPOs as “particularly vulnerable” to terrorist abuse by incorporating the FATF’s revised Recommendation 8’s risk-based, proportionate approach into relevant rules and guidance, such as the Bank Examination Manual.
- Develop clear guidance and standards to reduce guesswork and compliance costs so that they outline what information is required to ensure legal compliance by both banks and NPOs.
- Promote transparency, information sharing and proportionality to recalibrate risk perception so that fear of harsh penalties for inadvertent violations does not drive FI risk assessment. Give credit for measures taken in good faith.
- Create incentives to encourage appropriate risk management so that FIs will not avoid NPOs as customers.

Explore Alternatives to the Formal Banking System

In cases where formal financial transfers remain problematic, U.S. and international organizations could identify appropriate informal payment channels that NPOs can utilize to help lessen reliance on carrying cash. Alternative methods of moving funds, such as Bitcoin and other virtual currencies, mobile money, and new electronic payment systems, should be explored.

Impractical Options

The findings in this report are likely to generate other ideas for increasing financial access for nonprofits that merit further consideration. At the same time, however, some ideas have been proposed which, upon examination, were found to be unworkable for a variety of reasons. Others have been attempted without success. This report suggests that government sponsored “white lists” of approved NPOs, appeals to FI social responsibility programs, or NPO-focused efforts to build relationships with local bank managers are either unlikely to effectively address the NPOs’ financial access difficulties or have the potential to create additional problems.

Additional Research

While this report provides important new information on the impact the global trend of bank “derisking” has on the nonprofit sector, suggestions for additional research on questions raised by this report are provided.

Concluding Thoughts

A new way of looking at financial access is necessary to confront the growing crisis of financial access for NPOs. It is not a choice between financial integrity and financial inclusion; indeed they are complementary, not contradictory goals. As U.S. Treasury Secretary Jack Lew noted, these efforts should not be antithetical, "This is not a conflict of interest, it is a need to bring together two parallel interests." The convergence of interests of all stakeholders—U.S. policymakers and regulators, financial institutions, and nonprofits—in finding solutions to the financial access problems NPOs are encountering, provides the basis for a win-win proposition.

INTRODUCTION

On September 8, 2000, the United Nations (UN) General Assembly adopted the Millennium Declaration, heralding the critical role of non-governmental organizations (NGOs) and civil society and broadening the definition of security beyond protection from external invasion to the quality of life, political freedom, education and human rights.¹ But one year later, the situation changed dramatically—a “zeitgeist,” as some called it.² Following the 9/11 terrorist attacks, civil society organizations generally, and nonprofits in particular, were swept up in a new focus on counterterrorism. Harnessing new authorities and programs, CFT moved center-stage in the Bush Administration’s “Global War on Terrorism.”

Utilizing the U.S.’s influence in the global financial system, the Administration took an aggressive stance to stem the flow of money, calling it the “life-blood of terrorism—to terrorist groups.”³ Charitable organizations were considered vulnerable to terrorist abuse, and several were investigated, had their assets frozen and were shut down. In the years since, both experience and better data have led to a more-targeted approach. FIs and NPOs are expected to employ a “risk-based approach” (RBA) to their compliance programs, whereby they assess their ML/TF vulnerabilities and implement risk management and mitigation procedures in situations of higher risk.

Over time, a number of factors, including AML and CFT regulatory obligations on FIs, have led to the phenomenon of derisking. This refers to the trend of financial institutions terminating or restricting business relationships to avoid rather than manage risk.⁴ The most frequently mentioned driver of derisking cited by FIs is the concern for running afoul of regulatory requirements and expectations.⁵ Established through the FATF recommendations, and implemented by national measures, AML/CFT requirements compel FIs to track money flows and “know their customers”

1 United Nations General Assembly, United Nations Millennium Declaration, para. 30, UN Doc. A/55/L.2, September 8, 2000, <http://www.un.org/millennium/declaration/ares552e.htm>.

2 Douglas Rutzen, “Aid Barriers and the Rise of Philanthropic Protectionism,” *International Journal of Not-for-Profit Law*, (vol. 17, no. 1), March 2015, <http://www.icnl.org/research/journal/vol17ss1/Rutzen.pdf>.

3 “President Freezes Terrorists’ Assets: Remarks by the President, Secretary of the Treasury O’Neill and Secretary of State Powell on Executive Order,” September 24, 2001, <https://georgewbush-whitehouse.archives.gov/news/releases/2001/09/20010924-4.html>.

4 There are varying distinctions in the definition of derisking. As defined by the FATF, derisking is the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk in line with the FATF’s risk-based approach. The U.S. government defines derisking as “instances in which a financial institution seeks to avoid perceived regulatory risk by indiscriminately terminating, restricting, or denying services to broad classes of clients, without case-by-case analysis or consideration of mitigation options.” Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference, November 16, 2015, <https://www.treasury.gov/press-center/press-releases/Pages/jl0275.aspx>.

5 “Banks have raised concerns about (1) the cost of complying with AML/CFT regulations, (2) uncertainty about supervisors’ expectations regarding what is appropriate due diligence, and (3) the nature of the enforcement and/or supervisory response if they get it wrong.” Remarks by Under Secretary Nathan Sheets at the Center for Global Development, November 12, 2015, <https://www.treasury.gov/press-center/press-releases/Pages/jl0264.aspx>.

so as to provide information useful to law enforcement in detecting and prosecuting illicit finance. There is widespread recognition of the importance of AML/CFT efforts as an essential component of U.S. security, and broad support for effective measures to prevent the use of the financial system for criminal purposes. Until recently, however, the unintended consequences of these policies, including derisking, have not been well appreciated.

Recognition of the phenomenon of derisking has grown significantly in the past few years and has been featured prominently in speeches at the 2016 UN General Assembly, reports by development agencies such as the World Bank, guidance and work plans of international financial and security bodies such as the Group of Twenty (G-20), Financial Stability Board (FSB), and FATF, statements by members of Congress concerned about local populations, and policy pronouncements by the U.S. government (USG).⁶ Although disagreement persists about the appropriateness and even the definition of the term, derisking is now a well-documented occurrence.

Most often, derisking is discussed in terms of a decrease in correspondent banking (CB) relationships and the debanking of Money Service Businesses (MSBs),⁷ leaving financial institutions, businesses, nonprofit organizations and individuals without access to essential financial services. Recent studies by the World Bank and other organizations confirm a significant decline in correspondent banking and an increased trend of account closures for MSBs.⁸ The consequences of these trends are critical to many countries, indeed for entire regions of the world dependent on correspondent banks and remittance services for their economic survival.

In 2015, the USG and the FATF began recognizing and addressing some of these concerns. Largely absent from the policy discussions to date, however, is the impact of the derisking trend on NPOs, especially humanitarian and development groups working in conflict areas around the globe. Reports in November 2015 by the Center for Global Development (CGD)⁹ and by Oxfam and the Global Center on Cooperative Security¹⁰ highlighted the unintentional but costly consequences of derisking for a variety of sectors, including NPOs. In particular, examples have come to light of critical humanitarian assistance stymied as a result of charities' inability to transfer funds to foreign countries such as Syria, Somalia and other conflict areas, as well as support for millions of refugees in Europe. Banks under pressure to comply with AML/CFT requirements and sanctions

6 See Bibliography in Appendix A for recent reports and statements on derisking.

7 Money Service Businesses are non-bank institutions providing check cashing, money orders, travelers' checks, money transfers and foreign currency exchange services. Money transfer operators (MTOs) are a subset of MSBs providing international remittance transfers. See Box on MSBs in Chapter 3.

8 Nearly half of financial institutions surveyed and 75% of large international banks indicated a decline in correspondent banking relationships. See *Withdrawal from Correspondent Banking: Where, Why, and What to Do About It*, The World Bank, November 2015, <http://documents.worldbank.org/curated/en/113021467990964789/pdf/101098-revised-PUBLIC-CBR-Report-November-2015.pdf>; *Report on the G-20 Survey on De-risking Activities in the Remittance Market*, The World Bank, October 2015, <http://documents.worldbank.org/curated/en/679881467993185572/pdf/101071-WP-PUBLIC-GPFI-DWG-Remittances-De-risking-Report-2015-Final-2.pdf>.

9 *Unintended Consequences of Anti-Money Laundering Policies for Poor Countries*, Center for Global Development ("CGD Study"), November 9, 2015, <http://www.cgdev.org/publication/unintended-consequences-anti-money-laundering-policies-poor-countries>.

10 Tracey Durner and Liat Shetret, *Understanding Bank De-risking and Its Effects on Financial Inclusion*, Oxfam and Global Center on Cooperative Security ("Oxfam/GCCS Study"), November 2015, <http://www.globalcenter.org/publications/understanding-bank-de-risking-and-its-effects-on-financial-inclusion-2/>.

have delayed or denied financial transfers, complicating efforts by charities and humanitarian groups trying to deliver aid. A recent report prepared for the UN, *Study on Humanitarian Impact of Syria-Related Unilateral Restrictive Measures*,¹¹ documented the “chilling effect” of the private sector’s reluctance to support humanitarian activity. This reluctance, particularly on the part of banks, was fueled in part by a fear of fines stemming from inadvertent regulatory violations.

These complications occur at a time when the need for life-saving relief efforts in regions of conflict, protracted humanitarian crises and emergencies, compounded by severe access challenges, is greater than ever before. In 2015, international humanitarian assistance rose to an historic high of \$28 billion, with many countries surpassing their own records for giving.¹² But despite this overall rise in international assistance, funding was not sufficient to meet growing needs; the UN reported an unprecedented shortfall of 45% (\$9 billion) in unmet needs.¹³ As of 2017, emergencies in Syria, Yemen, South Sudan, Iraq and Sudan, as well as long-term crises in Somalia and Pakistan, are still not being adequately addressed. Indeed, the very countries in most dire need of significant support are among those in which NPOs are having difficulties transferring funds.

To date, there have been no data available concerning NPOs and their problems accessing banking services, save for an informal indicative survey in 2014 of UK charities.¹⁴ The CGD report recommended a number of steps to develop data, including a representative survey to provide an unbiased determination of the extent and nature of derisking of NPOs. At the same time, senior U.S. Treasury Department officials have called for more data “to continue to improve our understanding of the scope, nature, and drivers of the [derisking] problem through better data collection.”¹⁵ Meetings with Administration officials and Congressional staff alike all echoed the need for sound analytical data going beyond anecdotal examples.

Largely in response to the dearth of data concerning NPOs and the problems they face in obtaining financial services, the Charity & Security Network (C&SN), with funding from the Bill and Melinda Gates Foundation, commissioned this report in late 2015. C&SN is a resource center for NPOs to collectively promote human security and protect their ability to fulfill their missions.

The purpose of this initiative has to been to understand financial access issues encountered by the nonprofit sector as charities attempt to carry out their important work abroad. Moving beyond anecdotes, the study set out to gather empirical data as to the scope and nature of NPOs’

11 Justine Walker, *Study on Humanitarian Impact of Syria-Related Unilateral Restrictive Measures: National Agenda for the Future of Syria*, May 16, 2016, <https://assets.documentcloud.org/documents/3115191/Hum-Impact-of-Syria-Related-Res-Eco-Measures-26.pdf>.

12 Development Initiatives, *Global Humanitarian Assistance Report of 2016*, <http://www.globalhumanitarianassistance.org/wp-content/uploads/2016/07/GHA-report-2016-full-report.pdf>.

13 Ibid.

14 “Charity Finance Group, *Briefing: Impact of banks’ de-risking on Not for Profit Organisations*,” March 2015, http://www.cfg.org.uk/Policy/~/_media/Files/Policy/Banking/Briefing%20%20Impact%20of%20banks%20derisking%20activities%20on%20charities%20%20March%202015.pdf.

15 Remarks by Under Secretary Nathan Sheets at The Center for Global Development. November 12, 2015, <https://www.treasury.gov/press-center/press-releases/Pages/jl0264.aspx>, and Szubin Remarks, November 16, 2015.

difficulties accessing financial services. Questions explored the prevalence of financial access problems, specific obstacles charities encounter in transferring funds, the geographic destinations most problematic (e.g., limited to higher-risk countries with ongoing conflict or globally) and strategies NPOs employ when formal banking channels are not available to support programs. The study focused specifically on U.S.-based nonprofits working internationally even though problems have been noted in the U.K., Australia and elsewhere. As such, the report is a starting point in understanding barriers nonprofits face; going forward, additional data should be gathered on comparable problems in other countries to expand knowledge of the scope of the challenges. At this time of transition in the Executive Branch and Congress, the report provides important new data to inform the policy discussions going forward.

Organization of the Report

This report is organized into four sections.

Section One summarizes the methodology used in the research for this report, which includes extensive interviews, focus group discussions and a random sample survey of U.S. nonprofit organizations. It also includes background chapters to establish the context within which both FIs and NPOs operate and describe the derisking phenomenon.

Section Two provides a summary of the data and analysis from the quantitative portion of the study, a random sample survey of American nonprofits.

Section Three contains the results of discussions with U.S. policy and regulatory officials, financial institutions, and NPOs. It was through these sessions that examples of NPOs' financial access difficulties, including the impact on the delivery of humanitarian aid, were discussed.

Incorporating both the qualitative and quantitative data, **Section Four** contains observations on the information gathered, summarizing what we now know concerning financial access for NPOs. The concluding chapter proposes a range of options and recommendations to address these problems and create a more sustainable collaborative process among stakeholders going forward. It also lays out an agenda for future research and policy discussions more broadly.

Special Notes

The following notations are provided to clarify the terminology and focus of this report.

First, with regard to terminology, the report generally refers to the collective problems experienced by NPOs as “access to financial services” rather than derisking. Financial access is a more appropriate characterization because the difficulties charities encounter are much broader than merely restricting or terminating accounts or failing to take on NPOs as clients. They also include delays in processing transfers, requests for additional information and other complicating actions. However, because derisking has become a common catch-all term, it is unavoidable in discussing the issues addressed in this report, especially in the context of previous reports and public characterizations.

Second, this report is focused solely on NPOs. Problems with correspondent banking relationships and MSBs have received significant attention in policy discussions and multilateral fora and have been highlighted in other studies. Difficulties in the correspondent banking and MSB sectors undoubtedly contribute to the current problems NPOs are experiencing. A reduction in correspondent banking relationships makes it more difficult for charities to move money internationally, and MSBs have become an alternative to the formal financial sector. However, the unique obstacles faced by NPOs in accessing financial services remain the exclusive focus of this report.

Third, for purposes of this report, NPOs are defined according to the IRS's definition of charitable activity,¹⁶ which includes major humanitarian aid organizations, human rights groups and funds, friendship societies, faith-based organizations, environmental groups, museums, hospitals and universities. These organizations provide direct services (such as Save the Children or Doctors Without Borders) and conduct advocacy (such as the ACLU or Amnesty International). Foundations, including public grantmaking organizations (such as community foundations or Global Fund for Women) and private grantmaking organizations (such as the Ford Foundation), are also included in the scope of NPOs. The broad charity and foundation community is therefore included under the term NPOs. It should be noted that "NPOs" and "charities" are used interchangeably throughout this report.

Finally, the information and data presented in this report are intended to help facilitate an informed dialogue with regulators, policymakers, the financial community and the broader public. The report does not purport to be definitive in its assessments, but rather provides the first empirical information upon which informed discussion of solutions, as well as additional research, can be based. While further analysis will be useful in understanding the issues with finer granularity, the evidence presented in this report underscores the immediacy of the problem and the need to address these issues now. For the first time, we now know the scope and nature of the difficulties American nonprofits are experiencing with financial access, as well as some of the consequences of these problems. The work of nonprofits benefits broad foreign policy and security objectives, and this report should be read as a call to action for all stakeholders to reassess policies and work together to more effectively promote the multiplicity of U.S. interests.

¹⁶ A 501(c)(3) organization, also colloquially known as a 501c3, is a United States nonprofit organization that has been approved by the Internal Revenue Service to be tax-exempt if its activities have the following purposes: charitable, religious, educational, scientific, literary, testing for public safety, fostering amateur sports competition, or preventing cruelty to children or animals. See IRS, Exempt Purposes - Internal Revenue Code Section 501(c)(3), <https://www.irs.gov/charities-non-profits/charitable-organizations/exempt-purposes-internal-revenue-code-section-501c3>.

Chapter 1 METHODOLOGY

This study was undertaken as an investigation aimed at assessing the scope and nature of financial problems experienced by nonprofit organizations that work in foreign countries. Rather than test a hypothesis, the research was designed to discover the basic information necessary for stakeholders in the government, financial and nonprofit sectors to engage in constructive future dialogue and action. This approach required the production of empirically sound data as well as information from focus groups, stakeholder interviews and desk research. This chapter describes the methodology used.

Systematic Random Sample of Defined U.S. NPOs

The Charity & Security Network commissioned the Schar School of Policy and Government at George Mason University (GMU) to design a survey of U.S.-based NPOs that conduct work in foreign countries in order to produce reliable and valid data to be combined with more qualitative information. Professors Delton T. Daigle and Stefan Toepler led the survey team.¹⁷

The study defined “nonprofit organizations” by utilizing the IRS definition for organizations claiming tax-exempt status as public charities under Section 501(c)(3) of the Internal Revenue Code. According to the IRS, exempt purposes are:

“Charitable, religious, educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and preventing cruelty to children or animals. The term *charitable* is used in its generally accepted legal sense and includes relief of the poor, the distressed, or the underprivileged; advancement of religion; advancement of education or science; erecting or maintaining public buildings, monuments, or works; lessening the burdens of government; lessening neighborhood tensions; eliminating prejudice and discrimination; defending human and civil rights secured by law; and combating community deterioration and juvenile delinquency.”¹⁸

¹⁷ The data used in this report will be made publicly available in the coming months. Contact the Charity & Security Network to obtain the data.

¹⁸ IRS, Exempt Purposes - Internal Revenue Code Section 501(c)(3), www.irs.gov/charities-non-profits/charitable-organizations/exempt-purposes-internal-revenue-code-section-501c3.

Most NPOs that claim tax-exempt status must annually file IRS Form 990, which includes information on governance, finances and activities. NPOs that perform services or conduct any form of financial transaction outside the U.S. must also complete Schedule F, “Statement of Activities Outside the United States.”¹⁹ Religious organizations or their associations or auxiliaries, private foundations, governmental units, pension funds, organizations organized by Congress or charities with revenue of \$50,000 or less are exempt from these requirements.²⁰

For this study, the universe of NPOs from which the random sample was drawn was determined by the availability of an organization’s most recent Form 990 Schedule F filing. These were obtained through Guidestar,²¹ a nonprofit that collects, organizes and maintains a database of information on nonprofit organizations. In most cases, organizations’ 2014 filings were available, but in some cases, NPOs did not submit their forms in a timely manner, so their most recent filing is for 2013. In order to have as accurate a total universe as possible, forms from 2013 were used for the NPOs for which the more recent forms were not yet available. This was done to prevent any duplication of forms for any organization. Therefore, the universe of NPOs was defined as: *IRS Form 990 Schedule F filers with at least one unique tax filing in the fiscal years of 2013 or 2014.*

With the universe so defined, the target population was determined to be 8,665 unique organizations.

From this population of 8,665 organizations, GMU drew a random sample of 1,010 organizations. To obtain this sample, employee identification numbers (EINs) were randomized through the statistical analysis software program STATA using a randomly selected seed number and then sampling the 1,010 EINs. The EINs were then matched to these organizations’ Form 990 filings, including Schedule F. A number of variables or fields, such as organization characteristics (including assets, revenues, number of employees and activities, as well as organization contact information), were purchased from Guidestar by C&SN for the purpose of this research.²²

C&SN then commissioned GMU’s Center for Social Science Research to conduct telephone interviews with a random sample of U.S.-based NPOs pulled from the Guidestar database. Telephone interviews were conducted with financial officers or other high-level organization representatives from late July through September 2016. The survey data in this report were obtained from the 305 NPOs that completed the phone interview (see survey questions in Appendix B). The survey’s response rate of 38.2% meets the standards of the American Association of Public Opinion Research (AAPOR) for statistically reliable findings.

Because the Form 990 Schedule F filings were available for the total population of 8,665 charities with international activities, a rich comparison could be made between the total population and

19 IRS, Schedule F (Form 990), Statement of Activities Outside the United States, 2016, www.irs.gov/pub/irs-pdf/f990sf.pdf.

20 IRS, *Annual Exempt Organization Return: Who Must File*, www.irs.gov/charities-non-profits/annual-exempt-organization-return-who-must-file.

21 Guidestar collects information on all organizations filing an IRS Form 990. These IRS forms represent the most complete source of information on the universe of U.S.-based nonprofits. *Guidestar, About Us: Guidestar’s Mission*, <https://learn.guidestar.org/about-us/>.

22 Guidestar provided the Form 990, including Schedule F, and processed the sampling as proscribed by C&SN.

the sample of 1,010 to determine the degree to which the responding NPOs (305) represented the entire sample. It was determined that the sample was representative with two qualifications. First, smaller organizations were more likely to complete the interviews than larger organizations. Second, a very small number of hospitals, university foundations and similar organizations (“outliers”) account for 75% of the total revenues of all organizations. For most of the data presentation, the differences were not statistically significant; only marginal differences (<2 percentage points) were observed. Where the difference was statistically significant (e.g., revenues and assets), the “traditional charities” were displayed separately from the “outliers.” *Most importantly*, the findings from this study can be generalized to the total population from which this sample was drawn.

The response rate of 38.2% is relatively high for a standard telephone survey. The Schar School calculated that within a 95% confidence level, the data in Chapter 4 can be considered valid and representative of the NPOs that filed an IRS Form 990 and Schedule F for the year 2014 or 2013. The maximum margin of error for this survey is conservatively estimated at 5.4%.

Focus Groups

While empirical data are crucial to understanding what is happening in an effort to determine future policies, qualitative data are equally important. To collect this qualitative data, C&SN conducted five formal focus group sessions with various stakeholders: grantmakers, NPO treasurers, directors or executives of Muslim or Syrian-focused charities, university treasurers and bankers. The numbers of attendees at these sessions ranged from 4 to approximately 35.

The focus group discussions were conducted under the *Chatham House Rule*: no statements would be attributed to any organization or individual (all were anonymous). As expected, the comments and discussion greatly enriched the analysis and recommendations in this report. Most of the comments and quotes throughout this report are from these meetings.

Stakeholder Meetings

To ensure that the research addressed the questions and concerns of major stakeholders, interviews were conducted early in the research process with experts in government, experts in the financial sector, former regulators and nonprofit leaders. Trade associations and umbrella groups were also contacted. These interviews were also conducted under the Chatham House rule. Interviews with government agencies included multiple bureaus of the State and Treasury Departments, the National Security Council, the Office of Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and United States Agency for International Development (USAID).

Chapter 2

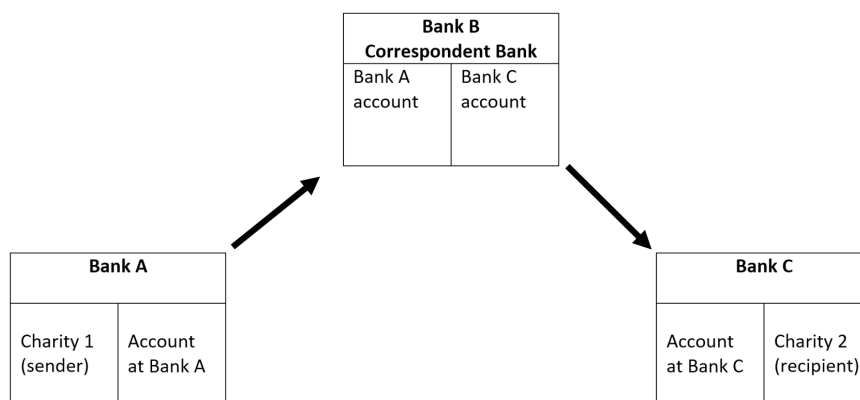
THE CONTEXT FOR NPO FINANCIAL ACCESS PROBLEMS

A variety of forces shape the complex environment in which financial institutions operate, affecting how they deal with the needs of their NPO customers whose work requires transferring funds to staff, partner NPOs and vendors in other countries. These forces include the regulatory structure for both FIs and NPOs, U.S. AML/CFT policies, and enforcement actions. The way FIs respond to these forces has contributed to narrowing access to financial services for NPOs.

Overview of International Financial Transactions: Correspondent Banking and SWIFT²³

To comprehend the reasons NPOs are having difficulties with financial services, a basic understanding of how the international financial system works is necessary. International financial transactions rely on a system of “correspondent” banking relationships. A correspondent bank serves as the intermediary between the bank sending a transfer on behalf of a client (retail bank) and the bank issuing payment to the recipient (respondent bank). Both the retail and correspondent bank hold an account at the correspondent bank, which is used for fund transfers, cash management and other purposes. It is the bedrock of international finance and trade.

Figure 1: Basic Process for Cross-Border Financial Transfers



Written agreements between the retail bank and correspondent bank establish the process for payments among the retail bank and its customers. During an international transfer, retail FIs forward payment instructions to the correspondent bank to sort and process. To provide for secure and consistent communication among banks, the Society for Worldwide Interbank Financial Telecommunication (SWIFT) network enables financial institutions to send and receive information and instructions through a standardized system of codes.

²³ Based on Bank for International Settlements, Committee on Payments and Market Infrastructures, “Correspondent Banking,” July 2016, <http://www.bis.org/cpmi/publ/d147.pdf>.

SWIFT is the largest messaging network, used by more than 11,000 financial institutions in more than 200 countries and territories.²⁴ SWIFT does not hold funds or manage accounts on behalf of customers, but rather enables users to communicate securely, exchanging standardized financial messages in a reliable way, thereby facilitating global financial flows. SWIFT sends payment orders that are settled through correspondent accounts that institutions maintain with each other.

In the past several years, the number of correspondent banking relationships has declined, especially for respondent banks that are located in higher-risk jurisdictions (those subject to sanctions), for customers perceived as higher risk (such as NPOs), or for customers who generate revenues insufficient to recover compliance costs. Increased regulatory compliance costs and penalties, especially concerning AML/CFT requirements, and reduced risk appetite by FIs have been attributed as the drivers for the reduction in correspondent banking.²⁵

The ability to make and receive international payments via correspondent banking is vital for businesses, NPOs and individuals, as well as global economic growth. A decline in the number of correspondent banking relationships affects the ability to send and receive international payments and could drive some payment flows underground, with potential consequences on growth, financial inclusion, and the stability and integrity of the financial system.²⁶ In recognition of these concerns, analytical work has been undertaken by several intergovernmental agencies, including the FSB and International Monetary Fund (IMF), and some governments, notably the UK,²⁷ to understand the withdrawal of correspondent banking and remittances.

Legal Authorities

The U.S. maintains an extensive system of sanctions on various countries and non-state armed groups in an effort to counter terrorism, narcotics trafficking and human rights abuses, among other reasons. When a group or country is sanctioned, their assets subject to U.S. jurisdiction are frozen. All transactions with them are prohibited, including transactions by FIs or NPOs.²⁸ The Treasury Department administers sanctions programs, and its Office of Foreign Assets Control (OFAC) can issue licenses that permit otherwise-banned transactions. Sanctions add to the compliance burdens on banks and NPOs and can have a compounding effect to AML/CFT requirements. In addition, the criminal prohibition against providing material support to Foreign Terrorist Organizations has been incorporated into the sanctions regime through Executive Order (EO) 13224. Although this report discusses some problems associated with U.S. sanctions, the primary focus is on AML/CFT regulatory requirements as a primary driver of derisking.

24 In 2015, SWIFT facilitated the exchange of an average of over 15 million messages per day, compared to an average of 2.4 million daily messages in 1995.

25 Bank for International Settlements, Committee on Payments and Market Infrastructures, “Correspondent Banking,” July 2016, <http://www.bis.org/cpmi/publ/d147.pdf>.

26 Financial Stability Board, “FSB publishes progress report to G20 on action plan to assess and address the decline in correspondent banking,” August 25, 2016, <http://www.fsb.org/2016/08/fsb-publishes-progress-report-to-g20-on-actions-to-address-correspondent-banking-declines/>.

27 David Artingstall, Nick Dove, John Howell, and Michael Levi, *Drivers & Impacts of Derisking: A Study of Representative Views and Data in the UK*, by John Howell & Co. Ltd. For the Financial Conduct Authority, February 2016, <https://www.fca.org.uk/publication/research/drivers-impacts-of-derisking.pdf>.

28 Limited exemptions apply. 50 U.S.C. § 1702(b).

The Risk-Based Approach

Although the letter of sanctions law imposes “strict liability” for violations,²⁹ international standards have been moving toward a more flexible RBA for nearly a decade. The FATF, the inter-governmental body that sets global standards to combat money laundering and terrorist financing, is the primary driver of this trend. Originally established in 1989 to address money laundering, FATF added terrorist financing to its agenda after 9/11 by adopting nine Special Recommendations, including Special Recommendation VIII on Nonprofit Organizations.³⁰ In the 2012 revisions of the FATF Recommendations, Special Recommendation VIII became Recommendation 8 (R8), and Recommendation 1, a new recommendation calling for a risk-based approach to implementation, was added. FATF evaluates and rates countries’ implementation of all 40 of its standards.

FATF first introduced the RBA in 2007 to help ensure that measures to prevent money laundering and terrorist financing threats are commensurate to the risks identified. Previous approaches resulted in a “check the box” method of paper compliance rather than focusing on effective means to combat ML/TF. The intention of the RBA was clear: to create a more pragmatic, flexible and rational approach in which the focus shifted to address actual risks through controls based on customers and the precise risks they posed. A series of guidance documents described how various sectors, including FIs and governments, could implement the RBA.³¹

Overall, the RBA moved the international standard away from an emphasis on technical compliance in favor of regulation that is effective.³² However, implementation of the RBA is an evolving process, as all stakeholders, including governments, NPOs and FIs, find ways of adjusting to these new methods. In the U.S., the legal framework governing sanctions and AML/CFT has changed little since 9/11 (see below) and does not adequately reflect the RBA set forth by FATF.³³ Although U.S. officials have articulated support for the RBA as policy, it is not a legal standard.³⁴

29 50 U.S.C. § 1705; Financial Action Task Force & Asia/Pacific Group on Money Laundering, “United States Mutual Evaluation: Anti-Money Laundering and Counter-Terrorist Financing Measures,” at 88, December 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-United-States-2016.pdf>.

30 Financial Action Task Force, “FATF IX Special Recommendations 3,” October 2001, <http://www.fatf-gafi.org/media/fatf/documents/reports/FATF%20Standards%20-%20IX%20Special%20Recommendations%20and%20IN%20rc.pdf>.

31 See Financial Access Task Force, “Guidance for a Risk-Based Approach: Effective Supervision and Enforcement by AML/CFT Supervisors of the Financial Sector and Law Enforcement,” October 2015, <http://www.fatf-gafi.org/media/fatf/documents/reports/RBA-Effective-supervision-and-enforcement.pdf>; Financial Access Task Force, “Guidance for a Risk-Based Approach: The Banking Sector,” October 2014, <http://www.fatf-gafi.org/media/fatf/documents/reports/Risk-Based-Approach-Banking-Sector.pdf>.

32 Neil Jeans, “Risk-Based Approach to KYC: Sound Concept, Complex Reality,” <https://risk.thomsonreuters.com/content/dam/openweb/documents/pdf/risk/white-paper/risk-based-approach-kyc-white-paper.pdf>.

33 The FATF Mutual Evaluation Report of the U.S. notes that, “The obligation of FIs to implement T[errorist] F[inancing]-related S[anctions] is an absolute strict liability one.” United States Mutual Evaluation at 105.

34 Anti-Terrorism and Effective Death Penalty Act of 1996, Pub. L. No. 104-132, 110 Stat. 1214. See material support provision at “Providing Material Support to Terrorists,” 18 U.S.C. § 2339B and the International Emergency Economic Powers Act Title II of Pub.L. 95-223, 91 Stat. 1626 See 50 USC 1701 et. seq.

Under the RBA, each FI undertakes its own internal risk assessment, tailoring its ML/TF threat-management program to its clients in order to manage risk effectively. This is a complicated and resource-intensive task because more work is required at the front end: FIs are expected to understand and assess specific risks and adopt policies to address them. This resulted in varying interpretations by FIs, leading to confusion within the industry.

In theory, the more flexible RBA approach would find that if FIs undertake appropriate processes to identify risk and adopt policies to mitigate them, they would be in compliance with regulatory requirements. In practice, however, banks have struggled to implement the RBA and have experienced significant variation and subjective determinations from federal regulators. According to a report by the British Bankers Association (BBA) and other organizations, “As regulatory views may differ from examiner to examiner, regulator to regulator and country to country, the avoidance of regulatory risk requires a broad ‘safety buffer’ to stay within expectations. With an increasing number of international banks under regulatory and legal actions (e.g. Deferred Prosecution Agreements, or Cease and Desist Orders etc.), the senior management of banks are developing a near zero tolerance for such regulatory risk.”³⁵

This complexity of the RBA was noted by the Comptroller of the Currency in 2016 when he said, “Banks must choose whether to enter into or maintain business relationships based on their unique business objectives, careful evaluation of the risks associated with particular products or services, evaluation of customers’ expected and actual activity, and an assessment of banks’ ability to manage those risks effectively. That’s no easy task, given the complex environment in which banks operate. Multiple financial regulatory, law enforcement, and other agencies are involved in almost every situation.”³⁶

When FATF first established Special Recommendation VIII in 2001, it incorporated the notion that NPOs are “particularly vulnerable” to terrorist abuse (see Box). Over time, this view was considered to be inconsistent with the RBA and findings on the main sources of terrorist financing.³⁷ In June 2016, FATF removed the “particularly vulnerable” language, putting in its place a recommendation for a risk-based approach that is proportionate and avoids disrupting the activities of legitimate NPOs.

38

35 FATF Plenary and associated working groups, “De-risking: Global Impact and Unintended Consequences for Exclusion and Stability,” at 7, October 2014, https://classic.regonline.com/custImages/340000/341739/G24%20AFI/G24_2015/De-risking_Report.pdf.

36 Remarks by Thomas J. Curry, Comptroller of the Currency, Before the Association of Certified Anti-Money Laundering Specialists 15th Annual Anti-Money Laundering and Financial Crime Conference, September 28, 2016, <https://www.occ.treas.gov/news-issuances/speeches/2016/pub-speech-2016-117.pdf>.

37 Emile van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing: A Proportionate Response,” 2010, <https://openknowledge.worldbank.org/handle/10986/5926>.

FATF TREATMENT OF NPOs ³⁸

In October 2001, FATF made protection of the NPO sector from terrorist abuse a critical component of the global fight against terrorism and a necessary step to preserve the integrity of NPOs. In approving Special Recommendation VIII (SRVIII): Nonprofit Organizations, FATF stated that NPOs were “particularly vulnerable” to terrorist financing abuse. It said countries “should ensure that they [NPOs] cannot be misused: by terrorist organizations 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.”

FATF’s Interpretative Note to SRVIII encouraged countries to focus on supervision and monitoring of the NPO sector and information-gathering and investigation. It cited vulnerabilities to abuse by terrorists as stemming from NPOs enjoying the public trust, having access to considerable sources of funds, being cash-intensive, having a global presence, and often being subject to minimal governmental oversight or background checks (e.g., registration, reporting, monitoring).

Over time, and with the introduction of the revised FATF 40 Recommendations in 2012 (SRVIII became R8), the FATF refined its guidance, acknowledging that “in the 12 years since the text of Recommendation 8 was first drafted, the threat environment and the NPO sector itself have continued to evolve.” Recognizing that the NPO community had responded by developing standards and initiatives to help individual organizations ensure accountability and transparency in their operations, FATF moved toward targeted intervention, in part responding to NPO concerns about disproportionate impact of TF measures on legitimate activities.

In its 2014 Typologies Report and the 2015 Best Practices Paper on Combatting the Abuse of the NPOs, FATF explicitly noted that legitimate charitable activities should not be disrupted or discouraged and clarified the subset of NPOs that should be subject to greater attention: NPOs “engaged in ‘service’ activities” and operating “in a close proximity to an active terrorist threat.” Additionally, emphasis was placed on having a flexible national terrorist financing approach and on “the application of effective, proportionate and dissuasive sanctions.”

Reflecting changed realities concerning NPOs, FATF in June 2016 revised R8 and its Interpretive Note, directing countries to undertake a risk-based approach when considering counter-terrorism financing measures. Incorporating input from NPOs and the private sector through a stakeholder process, FATF recognized that not all NPOs should be subject to the same measures, especially “where humanitarian needs are acute and where charitable work contributes positively to the fight against regional and global terrorism.”

38 Based on FATF reports and documents, including: FATF IX Special Recommendations (October 2001), International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations (February 2012), Risk of Terrorist Abuse in Non-Profit Organisations (2014), Best Practices: Combating the Abuse of Non-Profit Organizations (Recommendation 8) (June 2015), and Outcomes of the Plenary meeting of the FATF, Busan Korea, 22–24 (June 2016). [http://www.fatf-gafi.org/publications/?hf=10&b=0&q=NPOs&s=desc\(fatf_releasedate\)](http://www.fatf-gafi.org/publications/?hf=10&b=0&q=NPOs&s=desc(fatf_releasedate)).

The AML/CFT Regulatory Environment

The legal and regulatory environment changed for both FIs and NPOs after 9/11. This section describes the legal, supervisory and enforcement context within which financial access problems have emerged.

For Financial Institutions

For more than 45 years, the Bank Secrecy Act has been a cornerstone of U.S. AML policies, anchoring the broad initiative to curb abuse of FIs. In October 2001, Congress passed the USA PATRIOT Act amending the BSA to, among other things, protect the U.S. and international financial system against the threat of terrorism through powerful new authorities to counter the financing of terrorism. To better protect the gateway to the financial system—correspondent accounts—Title III of the Patriot Act imposed new requirements on U.S. FIs to restrict certain types of foreign accounts, implement minimum due diligence and record keeping procedures, verify customer identification and beneficial ownership and adhere to U.S. sanctions.³⁹ The purpose was to deter the use of financial institutions by terrorist financiers and money launderers and to assist law enforcement efforts through the creation of an audit trail to identify and track terrorist suspects through financial transactions.

Working through FATF, the U.S. government led a global initiative that shifted FATF's focus from identifying and reporting suspicious activity to a much broader mandate of protecting the international financial system from the threat of financial crime through prevention. The language of financial crime prevention addresses both money laundering and terrorist financing, which includes identifying and reporting the proceeds arising from criminal behavior, preventing criminal and corrupt proceeds from entering the financial system and applying economic sanctions to prohibited countries or persons.⁴⁰ These new policies became essential elements of the Bush Administration's strategy to use American economic power to promote U.S. security through private sector action.⁴¹ FIs became part of the long arm of American law enforcement as they began playing a new role as the first line of defense against terrorism financing. New agencies were created within the Treasury Department (such as the Office of Terrorism and Financial Intelligence), and significant new resources were allocated to fight illicit finance.

For international financial institutions, these developments marked a seismic shift, with financial crime management becoming a key priority. The results of this shift were new comprehensive management and reporting systems, transaction monitoring and AML/CFT/sanctions screening, enhanced procedures and controls for high-risk situations and a significant investment of resources

³⁹ For background, see Sue E. Eckert, "The US Regulatory Approach to Terrorist Financing," in *Countering the Financing of Terrorism* (Thomas J. Biersteker and Sue E. Eckert, ed., 2008). The U.S. Patriot Act, enacted on October 26, 2001, is an acronym for the "United and Strengthening America by Providing Appropriate Tools Required to Interrupt and Obstruct Terrorism," PL 107-56.

⁴⁰ British Bankers Association et al., "De-risking: Global Impact and Unintended Consequences for Exclusion and Stability, Balancing public policy objectives," October 2014, https://classic.regonline.com/custImages/340000/341739/G24%20AFI/G24_2015/De-risking_Report.pdf.

⁴¹ See Juan Zarate, *Treasury's War: The Unleashing of a New Era of Financial Warfare*, September 2013.

in compliance activities. Extensive new regulatory requirements changed the compliance and risk management landscape. While some observers raised questions at the time concerning the appropriate balance between preventing financial crime and safeguarding other foreign policy objectives (such as financial inclusion and economic development), for the most part, these sweeping regulatory measures were adopted with little debate and without consideration of potentially unintended consequences.⁴²

As they have developed, AML/CFT measures constitute a complex system of regulatory requirements for FIs⁴³ that include: freezing transactions and assets, maintaining records and reporting high-risk transactions and suspicious activities; self-disclosures of cross-border movement of certain products (e.g., currency, monetary instruments) and financial accounts held in foreign jurisdictions; collection and verification of information on customers and beneficial owners and sharing of information with other financial institutions, regulatory authorities and law enforcement.⁴⁴ In the wake of the 2008 financial crisis, the Dodd-Frank Act in 2010 further amended the BSA with increased regulatory obligations for FIs and other regulated entities.⁴⁵

For FIs operating internationally, complying with differing legal and regulatory frameworks across national borders presents significant challenges. While the FATF as the global standard-setter has helped to somewhat harmonize AML/CFT requirements at the international level, within the U.S. alone there is a broad array of regulatory and policy agencies involved in AML/CFT issues.⁴⁶

For Nonprofit Organizations

After the 9/11 attacks, the Bush Administration adopted a narrative of charities as “significant source of funds” for terrorist financing.⁴⁷ In the following years, greater information on terrorist financing threats and a more nuanced and evidence-based view emerged. Most examples of terrorist’s abuse of charities involved non-U.S. organizations. The 9/11 Commission’s Staff Monograph⁴⁸ found that extensive investigation “revealed no substantial source of domestic financial support” for the 9/11 attacks. A 2009 report from the UN Counter-Terrorism Implementation Task Force (CTITF) and the World Bank recognized growing concern for the

42 British Bankers Association et al., “De-risking.”

43 The Patriot Act also expanded the range of institutions subject to BSA requirements to encompass all financial institutions, including money transmitters, security brokers/dealers, insurance companies and currency exchangers.

44 For an overview of the U.S. AML/CFT regime, see Protiviti, “Guide to U.S. Anti-Money Laundering Requirements: Frequently Asked Questions,” November 2014, https://www.protiviti.com/sites/default/files/united_states/insights/guide-to-us-aml-requirements-6thedition-protiviti_0.pdf.

45 The Wall Street Reform and Consumer Protection Act (Dodd-Frank Act, P.L. 111-203).

46 See Edward V. Murphy, “Who Regulates Whom and How? An Overview of U.S. Financial Regulatory Policy for Banking and Securities Markets,” Congressional Research Service, January 30, 2015, <https://fas.org/sgp/crs/misc/R43087.pdf>.

47 *The Role of Charities and NGO’s in the Financing of Terrorist Activities: Hearing Before the Subcommittee on International Trade & Finance of the Senate Committee on Banking, Housing, and Urban Affairs*, 107th Cong. (2002) (statement of Kenneth W. Dam, Deputy Secretary, U.S. Department of Treasury), <https://www.gpo.gov/fdsys/pkg/CHRG-107shrg89957/html/CHRG-107shrg89957.htm>.

48 John Roth, Douglas Greenberg, and Serena Wille, Staff Report to the Commission, “National Commission on Terrorist Attacks upon the United States: Monograph on Terrorist Financing” at 3, 2004, http://govinfo.library.unt.edu/911/staff_statements/911_Terr-Fin_Monograph.pdf.

overemphasis on NPOs, cautioning, “States should avoid rhetoric that ties NPOs to terrorism financing in general terms because it overstates the threat and unduly damages the NPO sector as a whole.”⁴⁹

FATF Evaluation of U.S. – Recommendation on NPOs

In its 2016 Mutual Evaluation of the U.S., FATF noted that, “Striking the right balance and avoiding the disruption of legitimate NPOs activities can be challenging, particularly in high-risk conflict zones. As violations of T[errorist] F[inancing]-related S[anctions] are strict liability offenses, the authorities should continue to work with the NPO community to understand and mitigate the real TF risks that exist, while engaging stakeholders on banking challenges that some NPOs face while working in conflict zones.”⁵³

In 2015, the Department of Treasury issued a National Terrorist Financing Risk Assessment,⁵⁰ which discussed criminal enterprise and kidnapping for ransom as major sources of terrorist financing. While noting that “some charitable organizations, particularly those based or operating in high-risk jurisdictions, continue to be vulnerable to abuse for TF,” the National Terrorist Financing Risk Assessment references sham or front organizations as the greatest threat to the nonprofit sector, rather than legitimate NPOs. The report stated, “there has been a shift in recent years towards individuals with no connections to a charitable organization recognized by the U.S. government soliciting funds under the auspices of charity for a variety of terrorist groups...”⁵¹

Many features of U.S. legal and regulatory policy, however, continue to reflect the outdated view of

terrorist financing risks associated with the nonprofit sector. The original Special Recommendation VIII became embedded in various policies in the U.S. and around the world, and, as a result, the misperception that NPOs are “particularly vulnerable” still lingers today, resulting in constraints on the activities of legitimate NPOs.⁵²

U.S. Regulatory Agencies

FIs and NPOs are both subject to complex regulatory systems that supervise them and enforce legal standards. This section describes the agencies involved in regulating FIs and NPOs and the scope of their oversight.

49 Counter-Terrorism Implementation Task Force, “Tackling the Financing of Terrorism,” at 17, October 2009, http://www.un.org/en/terrorism/ctitf/pdfs/ctitf_financing_eng_final.pdf.

50 Department of Treasury, “National Terrorist Financing Risk Assessment 2015,” at 11, 2015, <https://www.treasury.gov/resource-center/terrorist-illicit-finance/Documents/National%20Terrorist%20Financing%20Risk%20Assessment%20%E2%80%932006-12-2015.pdf>.

51 Ibid., at 43.

52 See Ben Hayes, Transnational Institute/Statewatch, “Counterterrorism, ‘Policy Laundering’ and the FATF: Legalising Surveillance, Regulating Civil Society,” February 2012, <https://www.tni.org/en/publication/counter-terrorism-policy-laundering-and-the-fatf>.

53 U.S Mutual Evaluation, December 2016.

Regulatory Authorities for Financial Institutions

The U.S. regulatory and supervisory structure for FIs is complex, and FIs must deal with multiple government agencies. Generally, the government entity that grants the charter establishing an FI will be its primary regulator. A state bank is a bank chartered by the state in which it is located, and it usually offers only retail and commercial services. A national bank is a bank chartered and supervised by the OCC, pursuant to the National Bank Act. For the purposes of this report, the supervisory and examination functions of the agencies are most relevant (see Table 1).⁵⁴

Table 1: Primary Regulators for U.S. Financial Institutions

Primary Regulators Based on Chartering Authority		
For State Banks		For National Banks
Member of Federal Reserve	Non-member of Federal Reserve	Office of the Comptroller of the Currency
State and Federal Reserve	State and FDIC	
FinCEN	FinCEN	FinCEN

The Office of the Comptroller of the Currency (OCC) regulates and supervises all national banks, in addition to monitoring federally chartered thrift institutions and the federal branches and agencies of foreign banks. The OCC conducts periodic examinations of national banks.

The Federal Deposit Insurance Corporation (FDIC) has broad statutory responsibilities that extend from insured depository institutions to bank holding companies (with more than \$50 billion in assets). The FDIC further insures state-chartered banks that are not members of the Federal Reserve system. It conducts supervisory activities to determine an FI's compliance management system through three channels: compliance examinations, site visits and investigations.

The Federal Reserve is the U.S. central bank. It sets monetary policy, supervises and regulates financial institutions, promotes financial stability and consumer protection and works to promote a safe system for U.S. dollar transactions. It regulates state banks that are within its membership. The Financial Crimes Enforcement Network (FinCEN) is the primary AML/CFT regulator. It also supports law enforcement functions, provides financial intelligence to interagency and international efforts, issues and enforces regulations and collects and analyzes data that FIs are required to submit under the BSA filings, such as Suspicious Activity Reports (SARs).⁵⁵

⁵⁴ Regulators generally promote safety and soundness of banking operations, as well as other areas subject to state or federal regulation, including compliance with fair lending, consumer protection and other applicable statutes and regulations. While federal regulators encourage a risk-based approach, it is not enforced.

⁵⁵ Federal Financial Institutions Examination Council Bank Secrecy Act/Anti-Money Laundering InfoBase, *Suspicious Activity Reporting – Overview*, https://www.ffiec.gov/bsa_aml_infobase/pages_manual/OLM_015.htm.

In addition to federal regulators, state governments have their own agencies that administer state banking laws, further adding to the complexity FIs face in dealing with regulatory requirements. Some, such as the New York Department of Financial Services, have been particularly active on AML/CFT issues, proposing regulations that extend personal liability for violations to individual compliance officers and senior managers within banks.⁵⁶

Regulation of U.S. Nonprofit Organizations

The U.S. system for regulating nonprofit organizations is split among federal, state and local governments. Most NPOs are incorporated and registered under state law, and state/local laws often regulate fundraising practices to protect the public from fraud. At the federal level, regulation is focused on tax-exempt status and is administered by the IRS. Public charities and private foundations, exempt under IRS Section 501(c)(3), make up the largest of over two dozen categories of nonprofit organizations recognized by the IRS.⁵⁷ These are the only categories that can provide donors with tax deductions for their contributions.

Public charities are required to file annual informational reports with the IRS, and most states require some form of reporting as well. IRS Form 990 includes information on governance, finances and activities that must be available to the public. (Some organizations, such as houses of worship, are not required to apply for exempt status with the IRS or file annual information reports, but they may be required to register and make annual filings with state authorities to comply with state and/or local fundraising requirements.)

NPOs must also comply with laws directed at national security and sanctions that apply to all U.S. persons and entities. The exemptions for humanitarian assistance are limited. The material support prohibition only exempts medicine and religious materials.⁵⁸ The sanctions statute bars the U.S. President from blocking donations of “food, clothing and medicine intended to be used to relieve human suffering,” unless he/she determines that such aid would “seriously impair his ability to deal with any national emergency.”⁵⁹ This authority was invoked in EO 13224 on September 24, 2001. It has become routine practice for EOs to annually invoke this revocation of the humanitarian exemption and then grant case-specific licenses in each sanctions program.⁶⁰

56 There has been increasing focus on personal liability of bank officers for compliance violations, with the Haider Moneygram case being a good example, among others. While previously possible, it was often easier for regulators to pursue firms, but regulators themselves have been criticized for failing to discipline senior individuals for failings that contributed to the financial crisis. Greater personal liability is becoming a reality in many jurisdictions, and a Thomson Reuters survey reports that 60% of respondents expect the personal liability of compliance officers to increase in the next 12 months, with 16% expecting a significant increase. Todd Ehret, Thomson Reuters Regulatory Intelligence, “Top Ten Concerns for U.S. Compliance Officers in 2016,” 2016, <http://info.accelus.thomsonreuters.com/Top10ConcernsUSComplianceOfficers>.

57 Urban Institute, *The Nonprofit Sector in Brief 2015*, October 2015, <http://www.urban.org/sites/default/files/alfresco/publication-pdfs/2000497-The-Nonprofit-Sector-in-Brief-2015-Public-Charities-Giving-and-Volunteering.pdf>; IRS, Types of Tax-Exempt Organizations, <https://www.irs.gov/charities-non-profits/types-of-tax-exempt-organizations>.

58 18 U.S.C. § 2339A(b)(1).

59 50 U.S.C. § 1702(b)(2).

60 Charity & Security Network, “Safeguarding Humanitarianism in Armed Conflict,” June 2012, <http://www.charityandsecurity.org/sites/default/files/Safeguarding%20Humanitarianism%20Final.pdf>.

NPOs AND DUE DILIGENCE

Robust due-diligence procedures by NPOs serve to protect the organization, its donors, programs, partners and recipients, as well as to prevent abuse from terrorists and criminals. The IRS and state regulators oversee public charities and private foundations, requiring financial, governance and activity reporting to assure appropriate stewardship of donor funds. In addition, the nonprofit sector provides a host of resources to help NPOs with governance and transparency, financial and program management, program implementation and more.

Because of the diversity of the nonprofit sector, there is no one-size-fits-all approach to due diligence, and most employ a variety of methods to implement measures appropriate to the range of activities in which they engage. Risk assessment by legitimate NPOs takes a variety of forms, depending on many variables. These include geographic location, type of activity and the history of engagement in the area. The NPO sector has undertaken significant efforts to develop more robust due-diligence procedures since 9/11. The FATF has said, “The NPO sector has responded considerably to these demands by developing several different standards and initiatives to help individual organisations ensure accountability and transparency in their operations.”⁶¹

Examples of NPO due-diligence resources and programs include the following.

1. The 2005 “**Principles of International Charity**”⁶² includes measures for fiscal responsibility on the part of organizations providing resources to international programs:
 - a. in advance of payment, determining that the potential recipient of monetary or in-kind contributions has the ability to both accomplish the charitable purpose of the grant and protect the resources from diversion to non-charitable purposes;
 - b. reducing the terms of the grant to a written agreement signed by both the charitable resource provider and the recipient;
 - c. engaging in ongoing monitoring of the recipient and of activities under the grant; and
 - d. seeking correction of any misuse of resources on the part of the recipient.
2. MercyCorps⁶³ has developed a **Due Diligence Assessment Tool** to manage possible risks that includes questions to evaluate potential clients, review existing relationships before committing to additional projects/assistance, understand existing risks and incorporate corresponding mitigation activities, and discover emerging risks.
3. At a global level, the **Sphere Project**, composed of representatives of various humanitarian agencies, introduced common principles and “universal minimum standards in life-saving areas of humanitarian response.”⁶⁴
(See *Table 9: Transparency Standards and Initiatives Developed by NPO Sector*, Chapter 7)

61 *Financial Action Task Force Risk of Terrorist Abuse of Nonprofit Organizations*, at 22, <http://www.fatf-gafi.org/media/fatf/documents/reports/Risk-of-terrorist-abuse-in-non-profit-organisations.pdf>.

62 Council on Foundations and Treasury Guidelines Working Group of Charitable Sector Organizations and Advisors, “Principles of International Charity,” March 2005, at <http://www.foreffectivegov.org/sites/default/files/npa/Treasury%20Principles%20Final%20Document%20.pdf>.

63 “Due Diligence Assessment Tool,” Mercy Corps, <https://d2zyf8ayvg1369.cloudfront.net/sites/default/files/Tool%204%20Due%20Diligence%20Assessment.pdf>

64 <http://www.sphereproject.org/about>.

Enforcement

The Bank Examination Process

Since 9/11, U.S. agencies have intensified financial supervision and compliance examinations to ensure that the U.S. financial system is protected from ML/TF risks. Federal bank examinations are intended to set the terms for FIs' behavior regarding legal and enforcement compliance.

Because enforcers of the BSA have the ability to recommend civil fines,⁶⁵ bank examiners have significant influence on FI behavior. They participate in the assessment of financial institutions to determine the existence of unsafe and unsound practices, violations of law and regulation, the adequacy of internal controls/procedures and the general character of management.⁶⁶ Examinations are detail-intensive, covering a broad range of procedures and practices, from staff knowledge of emerging risks to management information systems. In particular, examination procedures assess whether bank controls offer reasonable protection from ML/FT risks, determine whether high-risk accounts are identified and monitored, and evaluate the adequacy of procedures to monitor and report suspicious activities.

Examiners' work is governed by the BSA/AML Examination Manual, which is produced by an interagency body.⁶⁷ It provides specific guidance for bank examiners to review FI compliance, including management of higher-risk customers. The Manual, last updated in 2014 and not due to be revised until 2018, includes a section on NPOs that does not reflect the June 2016 changes in FATF's R8. As such, it describes the entire sector as risky, stating, "the flow of funds both into and out of the NGO can be complex, making them susceptible to abuse by money launderers and terrorists."⁶⁸ It goes on to require FIs to conduct extensive background investigations of NPO customers, including details on their governance, financial procedures, volunteer and donor base, program operations and associations. For nonprofits that work outside the U.S., it adds the following steps:

- Evaluating the principals
- Obtaining and reviewing the financial statements and audits
- Verifying the source and use of funds
- Evaluating large contributors or grantors of the NGO
- Conducting reference checks

65 Federal Deposit Insurance Corporation Regulations, Risk Management Manual of Examination Policies, Sec. 14.1-3, <https://www.fdic.gov/regulations/safety/manual/section14-1.pdf>; Office of the Comptroller of the Currency, Examinations: Overview, <https://www.occ.gov/topics/examinations/examinations-overview/index-examinations-overview.html>.

66 Federal Deposit Insurance Corporation, *What We Do: Supervise Banks and Ensure Compliance with Fair Credit and Community Reinvestment Statutes*, <https://www.fdic.gov/about/jobs/do.html#be>.

67 The FFIEC, an interagency body promoting uniformity in the examination and supervision of financial institutions, is comprised of the Board of Governors of the Federal Reserve System, FDIC, NCUA, OCC, CFPB, and OTS.

68 FFIEC, "Bank Secrecy Act Anti-Money Laundering Examination Manual Bank," at 311-312, https://www.ffiec.gov/bsa_aml_infobase/documents/bsa_aml_man_2014.pdf.

As was previously mentioned, obtaining and evaluating this information is a resource-intensive process. The vagueness of some of the steps, such as how far an FI must investigate the volunteers and donors of an NPO, opens the door to inconsistent implementation. Moreover, extensive questioning by examiners of charity accounts signals to FIs that these accounts are problematic. Given the potential high cost of conducting this due diligence on NPO customers, it is not surprising that some FIs determine that it is not cost-effective to serve them.

Adopting practices to acquire concrete client information (known as “know your customer” [KYC] processes) can provide FIs with legitimate data, promoting informed and fair decisions when offering financial services. Indeed, data, rather than examiners’ opinions, are supposed to drive a specific FI’s risk-based approach to conducting business. However, “second-guessing” by examiners of individual transactions and differing interpretations of risk have sent confusing and mixed signals and have resulted in regulatory actions for “wrong” assessments of risk.⁶⁹

Enforcement Trends for FIs

In recent years, regulators have cracked down on AML/CFT violations, imposing unprecedented fines, in part as a reaction to Congressional criticism of regulators for “showing too much deference to the banks” in the aftermath of the 2008 financial crises and investigation of HSBC money laundering activities.⁷⁰ The CGD report noted that over the last 15 years, both the number and value of AML-related fines have increased in both the U.S. and the UK.⁷¹

The large number of enforcement actions, the unparalleled monetary fines and settlements and the severity of the terms have had a chilling effect throughout the financial sector.

For example, in 2012, several U.S. regulatory agencies cooperated in a settlement that resulted in a \$1.9 billion fine on HSBC for violating sanctions and laundering hundreds of millions of dollars related to Mexican drug trafficking. The same year, Standard

Chartered Bank paid almost \$1 billion to settle actions brought by the federal government and the New York State Department of Financial Services for moving millions of dollars through the financial system on behalf of sanctioned Iranian, Sudanese and Libyan entities.⁷² In 2015, BNP Paribas received a sentence of 5 years’ probation from a U.S. judge in connection with “a record \$8.9 billion settlement resolving claims that it violated sanctions against Sudan, Cuba and Iran.”⁷³ While announcing the settlement, then-U.S. Attorney General Eric Holder noted that he hoped the settlement would serve as a warning to other firms that did business with the U.S. that “illegal

69 Staci Warden, “Framing the Issues: De-Risking and Its consequences for Global Commerce and the Financial System,” *Center for Financial Markets*, at 4, July 2015, <http://www.milkeninstitute.org/publications/view/727>.

70 Nathaniel Popper, “Regulators and HSBC Faulted in Report on Money Laundering,” *New York Times Deal Book*, July 16, 2012, http://dealbook.nytimes.com/2012/07/16/scathing-report-details-money-laundering-problems-at-hsbc/?_r=0.

71 *Unintended Consequences of Anti-Money Laundering Policies for Poor Countries*, Center for Global Development (“CGD Study”), at 11, November 9, 2015, <http://www.cgdev.org/publication/unintended-consequences-anti-money-laundering-policies-poor-countries>.

72 Gavin Finch and Edward Robinson, “Why Banks Like HSBC Won’t Send Money to War-Zone Charities,” *Bloomberg*, May 11, 2016, <https://www.bloomberg.com/news/articles/2016-05-11/banks-cutting-money-flow-for-charities-squeezes-relief-in-syria>

73 Nate Raymond, “BNP Paribas sentenced in \$8.9 billion accord over sanctions violations,” *Reuters*, May 1, 2015, <http://www.reuters.com/article/us-bnp-paribas-settlement-sentencing-idUSKBN0NM41K20150501>.

conduct will simply not be tolerated.”⁷⁴ The large number of enforcement actions, the unparalleled monetary fines and settlements and the severity of the terms have had a chilling effect throughout the financial sector. It should be noted that most criminal investigations do not end with fines on FIs, but having to defend such an investigation can be extraordinarily expensive.

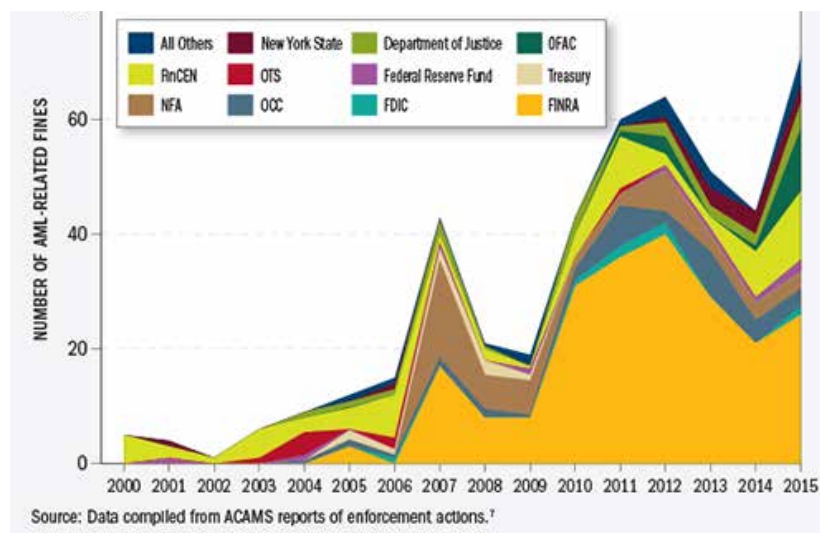
Enforcement Trends for NPOs

Between late 2001 and early 2009, the Treasury Department designated nine U.S. charities as supporters of terrorism, using the expanded powers derived from the Patriot Act. Seven of these NPOs were Muslim charities. These designations effectively prohibited any transactions with these organizations and froze their funds.

In the ensuing years, litigation on the constitutionality of the Treasury Department’s administrative appeal process has produced mixed results. The most recent court decisions found the process to be unconstitutional in that it denied due process by not giving the NPOs a meaningful opportunity to contest their designation and seized (froze) their funds without a warrant.⁷⁵

Since 2009, the focus of enforcement has shifted to criminal prosecutions of “individuals supporting various terrorist groups seeking to raise funds in the U.S. under the auspices of charitable giving, but outside of any charitable organization recognized as tax-exempt by the U.S. government.”⁷⁶ When asked in a 2016 Congressional hearing why no U.S. charities have been shut down since 2009, then-Assistant Secretary for Terrorist Financing Daniel Glaser noted that the Treasury’s engagement with NPOs has “reduced the opportunity for [charities] to be abused” by terrorist organizations. He also noted the trend of fraudulent fundraising by sham organizations.⁷⁷

Figure 2: Number of AML-Related Fines by U.S. Regulators 2000-2015*



*Source: Unintended Consequences of AML Policies (Data compiled from ACAMS reports of enforcement actions) <https://www.theclearinghouse.org/publications/2016/2016-q3-banking-perspectives/aml-unintended-consequences>

74 Nathaniel Popper, “Regulators and HSBC Faulted in Report on Money Laundering,” New York Times Deal Book, July 16, 2012, http://dealbook.nytimes.com/2012/07/16/scathing-report-details-money-laundering-problems-at-hsbc/?_r=0.

75 Kay Guinane and Cherie L. Evans, “Gap Between Tax and Sanctions Law Blocks Lifesaving Aid,” Tax Notes, October 10, 2016; *Al Haramain Islamic Foundation Inc. v. Treasury*, 686 F.3d 965 (9th Cir. 2012) and *KindHearts for Charitable and Humanitarian Development, Inc. v. Geithner*, 710 F. Supp. 2d 637 (N.D. Ohio 2010).

76 U.S. Mutual Evaluation, December 2016.

77 “Stopping the Money Flow: War on Terror Finance, Joint Hearing Before Subcommittees of House Committees on Foreign Affairs and Armed Services,” Questions for the Record for Assistant Secretary Daniel Glaser, June 9, 2016.

Chapter 3

DERISKING: COMPLICATIONS AND CONSEQUENCES

Decisions by financial institutions to terminate or limit relationships due to concerns about risk (derisking) can have significant consequences for a range of clients and countries served. Those most frequently affected include sectors characterized by FATF as vulnerable to terrorist abuse: money service businesses or nonprofits and specific high-risk countries or regions. Correspondent banks are also impacted when one bank closes the accounts or curtails business with another. The following section addresses the regulatory drivers of derisking and its consequences on several sectors and regions, for U.S. and international security, and the implications of derisking for financial inclusion. It also describes the response of the U.S government and NPOs' financial access problems.

Regulatory Drivers of Bank Derisking⁷⁸

The upward trend in enforcement actions and fines against banks, along with the existing regulatory complexity in the AML/CFT/sanctions field, means that banks are facing a significant increase in compliance costs. FIs are reluctant to discuss specific spending on compliance, but some reports place the additional costs at upward of \$4 billion annually. One bank reportedly employed 4,000 additional compliance staff in one year, at an additional cost of \$1 billion.⁷⁹ According to a survey by ACAMS, enhanced regulatory expectations continue to represent the greatest AML compliance challenge, as cited by 60% of respondents (see Figure 3).⁸⁰ The trend toward personal liability of compliance officers for regulatory violations further contributes to escalating costs and challenges.

In its 2016 annual survey on the cost of compliance and the challenges firms expect to face in the year ahead, Thomson Reuters reports that compliance officers are experiencing regulatory fatigue and overload in the face of ever-changing and growing regulations, with 69% of firms (70% in 2015) expecting more regulatory burdens in the coming year.⁸¹

78 While other drivers of derisking have been noted, for example Basel III reforms to strengthen bank capital requirements by increasing bank liquidity, this report focuses only on the AML/CFT/sanctions regulatory compliance issues that have been identified as the primary reasons for derisking.

79 Laura Noonan, "Banks Face Pushback over Surging Compliance and Regulatory Costs," Financial Times, May 28, 2015, <https://www.ft.com/content/e1323e18-0478-11e5-95ad-00144feabdc0>.

80 Dow Jones & ACAMS, "Global Anti-Money Laundering Survey Results 2016," at 4, http://files.acams.org/pdfs/2016/Dow_Jones_and_ACAMS_Global_Anti-Money_Laundering_Survey_Results_2016.pdf.

81 Stacey English & Susannah Hammond, "Cost of Compliance 2016," Thomson Reuters, at 3, <https://risk.thomsonreuters.com/content/dam/openweb/documents/pdf/risk/report/cost-compliance-2016.pdf>.

Enhanced regulatory pressures, rising compliance costs and the chilling effect of enforcement actions and fines have resulted in financial institutions that increasingly withdraw from doing business with customers or regions perceived to carry higher risks. Fueled by concerns that “wrong” compliance decisions could result in reputational and regulatory costs, FIs have grown more risk-averse over the past several years. As documented by numerous policy reports and acknowledged by the FATF in October 2015, “de-risking is having a significant impact in certain regions and sectors.”⁸²

FATF attributes derisking to a complex set of drivers: profitability, reputational risk, the cost of implementing AML/CFT measures, sanctions and other regulatory requirements. To address the problem, FATF issued a statement in 2015 reiterating that regulators and supervisors should use a risk-based approach in supervising financial institutions’ compliance with AML/CFT measures. It notes that when failures are detected, governments should take appropriate and proportionate action, stating that the RBA is not a “zero tolerance” approach. Emphasizing that FIs should manage (not avoid) risks, FATF urged banks to prevent the “wholesale cutting loose of entire countries and classes of customer, without taking into account, seriously and comprehensively, their level of money laundering and terrorist financing risk and applicable risk mitigation measures for those countries and for customers within a particular sector.”⁸³

Figure 3: AML Compliance Challenges*

AML COMPLIANCE CHALLENGES FACED BY ORGANIZATIONS

60% of respondents cite increased regulatory expectations as the greater AML compliance challenge, followed by concerns regarding having enough properly trained staff. Formal regulatory criticism increases by 4% from 2015.

	2013	2015	2016	MAIN CHALLENGE
Increased regulatory expectations & enforcement of current regulations	53%	62%	60%	28%
Having enough properly trained AML staff	36%	49%	50%	19%
Insufficient/outdated technology	31%	38%	41%	15%
Too many false positive screening results	31%	32%	36%	7%
Budget constraints & increased scrutiny of third-party reviews			27%	5%
Additional regulations	25%	26%	22%	3%
Understanding regulations outside home country	22%	23%	25%	4%
Sanctions compliance			24%	3%
Formal regulatory criticism	12%	15%	19% ↑	5%
Fear of personal civil & criminal liability			15%	2%
Lack of senior management/BoD AML engagement	13%	17%	14%	5%
Understanding regulations in home country	10%	9%	9%	1%

*Source: Dow Jones & ACAMS, "Global Anti-Money Laundering Survey Results 2016"

82 See, for example, Unintended Consequences of Anti-Money Laundering Policies for Poor Countries, Center for Global Development, November 9, 2015, <http://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf>; Tracey Durner and Liat Shetret, Understanding Bank De-risking and Its Effects on Financial Inclusion, Oxfam and Global Center on Cooperative Security, November 2015, <http://www.globalcenter.org/wp-content/uploads/2015/11/rr-bank-de-risking-181115-en.pdf> (“Oxfam/GCCS Study”); Withdrawal from Correspondent Banking: Where, Why, and What to Do About It, World Bank, November 2015, <http://documents.worldbank.org/curated/en/113021467990964789/pdf/101098-revised-PUBLIC-CBR-Report-November-2015.pdf>; Report on the G-20 Survey on De-risking Activities in the Remittance Market, World Bank, October 2015, <http://documents.worldbank.org/curated/en/679881467993185572/pdf/101071-WP-PUBLIC-GPFI-DWG-Remittances-De-risking-Report-2015-Final-2.pdf>; Report to the G20 on actions taken to assess and address the decline in correspondent banking, Financial Stability Board, November 6, 2015, www.fsb.org/wp-content/uploads/Correspondent-banking-report-to-G20-Summit.pdf; FATF, “FATF takes action to tackle de-risking,” October 23, 2015, <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/fatf-action-to-tackle-de-risking.html>.

83 “FATF takes action to tackle de-risking,” October 2015.

While FIs do not discuss issues related to individual accounts and are reluctant to engage on the issue of derisking generally, they readily admit that it frequently happens. According to the 2016 ACAMS survey of FIs, 40% of respondents report that their companies have exited a full business line or segment in the past 12 months due to regulatory risk (see Figure 4). One-third of respondents are planning and/or investigating exiting a business line/segment in the next 12 months.⁸⁴

Figure 4: Financial Institutions Exiting Business*



*Source: Numbers derived from figures presented in the *Dow Jones & ACAMS Global Anti-Money Laundering Survey Results 2016* http://files.acams.org/pdfs/2016/Dow_Jones_and_ACAMS_Global_Anti-Money_Laundering_Survey_Results_2016.pdf

It stands to reason, from a cost-benefit and risk-assessment viewpoint, that given these conditions, FIs would decide to terminate relationships perceived as higher risk. One of the architects of the post-9/11 AML/CFT regime, Stuart Levey (former Treasury Under Secretary for Terrorism and Financial Intelligence before he joined HSBC) said that by pushing banks to tighten up on financial crime compliance, regulators had ended up driving them to derisk by cutting off high-risk categories of customers.⁸⁵ As explained in greater detail in Chapter 6, financial institutions are increasingly concerned about “regulatory risk.”

Derisking Impacts Diverse Stakeholders

The impacts of derisking have been felt by specific sectors such as NPOs, MSBs and foreign embassies, as well as specific regions. While the remainder of this report addresses the consequences of derisking on NPOs, other examples are summarized below.

Remittances by Diaspora Populations

Money service businesses, including money transmitters, offer critical services widely utilized by diaspora communities in transferring remittances back home. They are popular because they charge much lower fees than most FIs and do not require customers to maintain formal accounts.

⁸⁴ Dow Jones & ACAMS, “Global Anti-Money Laundering Survey Results 2016.”

⁸⁵ Martin Arnold, “HSBC’s Levey calls for overhaul of anti-financial crime measures,” *Financial Times*, September 26, 2016, <https://www.ft.com/content/408f4022-4171-3d28-a773-805f332bd71e>.

For less-developed countries without well-established financial systems or countries suffering from prolonged conflict, MSBs and informal value transfer systems such as hawala are a primary means of moving funds internationally. As U.S. NPOs' difficulties with banking have increased, many have turned to MSBs as an alternative method to transfer funds abroad.

MSBs AND DESRISKING

Since 9/11, MSBs and remittance services have come under greater scrutiny, falling into the category of higher-risk customers for FIs, along with NPOs. MSBs serve large portions of populations in less-developed countries; Dahabshil, for example, an indigenous African-based money transfer business, has operations in 126 countries across the world, 40 of which are in Africa.

Somalia has been particularly affected by remittance derisking.⁸⁶ Without a functioning central bank, Somalia relies on remittances from Somalis abroad. The World Bank estimates total Somali remittances to be \$1.4 billion, supporting “23% of the [Somali] GDP” in 2015, exceeding the amount it receives in humanitarian aid, development aid and foreign direct investment combined. In 2001, the U.S. government closed down al-Barakaat (the largest MSB serving the Somali community) over suspicions it helped to fund al-Qaida.⁸⁷ (It was removed from the list in 2012.) Since then, U.S. and international financial institutions have been reluctant to process payments to Somalia, with sizeable Somali communities in Minnesota and Ohio left without viable means to remit funds home.⁸⁸

In 2011, Minnesota's Sunrise Community Banks, serving a large diaspora community, closed its Somali remittance accounts after two high-profile prosecutions of Somali-Americans for raising money for al-Shabaab. California's Merchants Bank then became the largest bank specializing in Somali accounts, but it announced plans to close its Somali business in 2014. After negotiating a compromise with U.S. regulators, it reversed its decision, but by February 2015, Merchant Bank ceased its Somali remittance business altogether. It was the last remaining FI handling transfers to Somalia, with 80% of remittances from the U.S. to Somalia. The perception of MSBs as inherently risky persists, and some banks have terminated all MSB accounts or refused to open new ones due to regulatory cost and risk concerns. The World Bank confirmed that money transmitters are experienced increased closures of and/or restrictions on accounts between 2010 and 2014.⁸⁹ While both the FATF and U.S. have reiterated that FIs should apply a risk-based approach to MSBs since they do not present a uniform and unacceptably high risk of money laundering, it has not reassured FIs. Reports of long-established MSBs losing bank accounts in the U.K., Australia and Canada, as well as the U.S., are increasing,⁹⁰ and the lack of access to financial services for MSBs is reaching crisis proportions.

86 Manuel Orozco and Julia Yansura, “Keeping the Lifeline Open: Remittances and Markets in Somalia, 2014, <https://www.oxfam-america.org/static/media/files/somalia-remittance-report-web.pdf>.

87 The 9/11 Commission subsequently found no evidence of misuse of MSBs, including al-Barakaat. See John Roth, Douglas Greenberg, and Serena Wille, Staff Report to the Commission, “National Commission on Terrorist Attacks Upon the United States: Monograph on Terrorist Financing,” 2004, http://govinfo.library.unt.edu/911/staff_statements/911_TerrFin_Monograph.pdf.

88 See Martin Weiss, “Remittances: Background and Issues for Congress,” Congressional Research Service, at 12, May 9, 2016, <https://www.fas.org/sfp/crs/misc/R43217.pdf>.

89 *Report on the G-20 Survey on De-risking Activities in the Remittance Market*.

90 Faisal Khan, “Can't find MSB Friendly Banks? Go ahead, scream. No one is listening.” July 6, 2015. <https://www.linkedin.com/pulse/cant-find-msb-friendly-banks-go-ahead-scream-no-one-is-listening-khan?forceNoSplash=true>

Geographic Derisking

Derisking also impacts parts of the world that are not under direct sanctions but that are subject to perceptions of risk due to other factors. For example, the Caribbean has been particularly hit by this trend. Because of their small sizes and export-driven economies, Caribbean countries depend on correspondent accounts for revenues generated from abroad.⁹¹ As noted in the 2015 World Bank reports, derisking in the Caribbean poses a serious threat to development in the region.⁹²

Similarly, a study by the Arab Monetary Fund, in cooperation with the International Monetary Fund and the World Bank, surveyed 216 banks operating in 17 Arab countries. It found that 39% of banks had seen a significant decline in the scale and breadth of their correspondent banking relationships between 2012 and 2015. The decline in correspondent banking relationships is increasing: the survey found that 63% of banks reported the closure of such accounts in 2015, compared to 33% in 2012. Forty percent of Arab banks said U.S. lenders were most prone to withdraw from correspondent banking relationships, followed by British and German banks.⁹³

Even within the U.S., there is evidence of regional derisking along the southwestern U.S. border. Members of Congress have weighed in on the impact of local populations attempting to use credit unions and money remitters. Beyond letters to the Administration expressing concern for the negative consequences of derisking, Congress has called for Inspector General reports and investigations by the Government Accountability Office of the situation.⁹⁴

FIs also refer to “jurisdictional derisking,” whereby certain countries pose such high levels of risk that some banks have decided not to do any business associated with such destinations. Often, these countries are subject to U.S. or UN sanctions (e.g., Iraq, Iran, Syria, Sudan, Somalia, North Korea, Myanmar) and frequently are the very same countries where many humanitarian assistance, peacebuilding and development NPOs seek to provide services to alleviate suffering resulting from ongoing conflict and terrorism. Many FIs noted that jurisdictional risk outweighs all other concerns; lower-risk NPOs that otherwise would be attractive customers will have significant problems if funds are intended for higher-risk destinations.

91 Naki B. Mendoza, “How banks de-risking can undermine development,” Devex Impact, May 31, 2016, <https://www.devex.com/news/how-banks-de-risking-can-undermine-development-88227>.

92 Ibid.

93 “Arab banks’ ties to foreign banks under pressure, survey finds,” Reuters, September 5, 2016, <http://www.reuters.com/article/us-mideast-banks-idUSKCN11B22R>.

94 See letter and statements at website of Senator Jeff Flake, “Flake, McCain Urge Agencies to Address Bank Closures on U.S.-Mexico Border,” Press Release, March 10, 2016, <http://www.flake.senate.gov/public/index.cfm?p=press-releases&id=-2F767A64-5510-4364-A5BC-360EAC069D42>

EMBASSY DEBANKING

In May 2004, FinCEN and the OCC levied a \$25 million fine (the largest civil money penalty against a U.S. bank at the time for BSA violations) against Riggs Bank for failing to maintain an adequate AML system and willful violations of suspicious activity and currency transaction reporting.⁹⁵ Having served diplomatic and foreign embassies' banking needs for years, Riggs's reputation was devastated. Riggs closed its embassy bank accounts and ultimately was acquired by PNC Bank in 2005.

The ensuing "Embassy Debanking" predicament left many embassies hard-pressed to find new banks as most major American financial institutions exited or scaled back their operations with foreign missions. AML/CFT regulations, rising reputational risks and severe penalties made banks reluctant to take on embassies as clients. Countries significantly affected included Saudi Arabia, Angola, Equatorial Guinea and Sudan. The State Department reported that nearly 40 countries had been affected by embassy debanking, including 16 African nations.⁹⁶

The embassy debanking crisis escalated to the level of heads of state raising financial access problems in bilateral meetings. As a result of the diplomatic fallout, the U.S. Secretaries of Treasury and State urged banks to resume business with foreign embassies, all while noting that embassy debanking was "a commercial decision" but with "ramifications for diplomatic relations."⁹⁷ The American Bankers Association (ABA) responded that the regulatory regime "can make providing routine banking to foreign diplomats almost an impossible task," noting that the Bank Examination Manual required "greater scrutiny and monitoring of all embassy and foreign consulate account relationships."⁹⁸

Ultimately, FinCEN updated its guidance, confirming that financial institutions had the "flexibility to provide banking services to foreign missions while also remaining in compliance with the BSA, and over time banks began to reopen accounts with foreign embassies, but at a premium."⁹⁹ However, without the significant political pressure to find a solution, it is unlikely that this situation would have been resolved. Other groups that do not have comparable political support but are experiencing debanking are unlikely to see similar results.

95 U.S. Department of Treasury, Financial Crimes Enforcement Network, In the Matter of RIGGS BANK, N.A., No. 2004-01, https://www.fincen.gov/sites/default/files/enforcement_action/riggssassessment3.pdf.

96 Matthias Rieker, Joseph Palazzolo, Victoria McGrane, "Banks Exit from Embassy Business: Moves by Largest Lenders Could Strain Relations Between U.S. government and Other Countries," Wall Street Journal, November 20, 2010, <http://www.wsj.com/articles/SB10001424052748703531504575625060985983720>.

97 Josh Rogin, "37 Embassies in Washington Face Banking Crisis," Foreign Policy, November 19, 2010, <http://foreignpolicy.com/2010/11/19/37-embassies-in-washington-face-banking-crisis/>.

98 Frank Keating Letter to Hillary Clinton, January 18, 2011, <https://www.aba.com/aba/documents/news/ClintonGeithnerLetter11811.pdf>.

99 FinCEN, "Guidance on Accepting Accounts from Foreign Embassies, Consulates, and Missions," March 24, 2011, https://www.fincen.gov/sites/default/files/guidance/FFIEC_FinCEN_24_march.pdf; and Juan Zarate, "Treasury's War: The Unleashing of a New Era of Financial Warfare." New York: Public Affairs, 2013.

Security Consequences of Derisking

Derisking can pose significant consequences for U.S. and international security objectives. Experts fear that derisking of correspondent banking, MSBs and NPOs will create a vacuum filled by less-transparent and -accountable financial institutions, which ultimately undermines the integrity of the international financial system as money is driven into riskier channels. Underground banking that is unmonitored or unregulated, and where legitimate money may freely mix with illicit funds before making its way back into the regulated financial system, is not only contrary to AML/CFT objectives but is also actually harmful.¹⁰⁰

Financial and regulatory policymakers have begun to recognize the potential consequences of reduced access to banking services for illicit finance objectives. David Lewis, executive secretary of the FATF, in discussing derisking noted that, “It’s a concern to us, as it undermines transparency within the financial sector and law enforcement’s ability to follow the money.... We are concerned about that as it reduces transparency in financial transactions, it increases the ML/TF risks we are trying to address.”¹⁰¹ Comptroller of the Currency Thomas Curry acknowledged the potential danger, commenting that, “Transactions that would have taken place legally and transparently may be driven underground.”¹⁰² Former Treasury Secretary Jack Lew echoed these concerns when he noted that, “Financial institutions around the world have to adhere to high standards to stop the flow of illicit funds. That means anti-money laundering rules really matter. On the other hand, if the burden is so high ... that people withdraw from the financial system or are excluded from it, it ultimately raises the risk of illicit transactions.”¹⁰³

According to James Richards, an executive vice president and a top Bank Secrecy Act officer at Wells Fargo, “As banks become more cautious about who they can safely bank, bad actors will migrate to institutions that are not as well equipped to detect them.” Richards goes on to say that, “The ironic result of de-risking is re-risking [...] you are just spreading it ... you are sending them to banks that probably can’t handle it.”¹⁰⁴

In addition, derisking can contribute to drivers of violent extremism, undermining the very objectives that AML/CFT measures are intended to support. Key aspects of international strategies to prevent terrorism/counter violent extremism are programs to support local populations where terrorism takes root—initiatives in which NPOs play a vital role. To avoid working at cross-purposes, AML/CFT measures must be consistent and broadly coordinate with national security, foreign policy and economic objectives.¹⁰⁵ In places like Somalia, shuttering legitimate banks and

100 Rob Barry and Rachel Louise Ensign, “Losing Count: U.S. Terror Rules Drive Money Underground,” Wall Street Journal, March 30, 2016.

101 Mark Taylor, “FATF chief talks de-risking dangers and correspondent banking,” March 29, 2016, <https://www.linkedin.com/pulse/fatf-chief-talks-de-risking-dangers-correspondent-banking-mark-taylor>

102 Barry and Ensign, “Losing Count: U.S. Terror Rules Drive Money Underground.”

103 Lalita Clozel, “Lew on DeRisking: Banks Should Not Be Penalized for Engaging Abroad,” American Banker, October 7, 2016.

104 Ian McKendry, “Banks Face No-Win Scenario on AML ‘De-Risking,’” American Banker, November 17, 2014, <http://www.americanbanker.com/news/law-regulation/banks-face-no-win-scenario-on-aml-de-risking-1071271-1.html>.

105 Counter-Terrorism Implementation Task Force, “Tackling the Financing of Terrorism,” at 17, October 2009, http://www.un.org/en/terrorism/ctitf/pdfs/ctitf_financing_eng_final.pdf.

money remitters poses a very real impediment, not only to U.S. counterterrorism and illicit finance goals but also for economic growth and development. Indeed, this development is needed to counter terrorist groups like al-Shabab.¹⁰⁶

Derisking poses complicated policy dilemmas that involve competing interests, and policymakers attempt to navigate between them. An article in *American Banker* noted, “Those responsible for disrupting illicit activity—such as terrorism, drug trafficking and evading sanctions—hold that banks should exit certain markets where they cannot effectively manage the customer, business line and jurisdictional risks. However, policymakers responsible for promoting global development, trade and investment are alarmed by the prospect of walking back decades of economic progress attributable to financial inclusion and global finance.”¹⁰⁷

Robert Kimmitt, former Deputy Treasury Secretary, Under Secretary of State for Political Affairs and National Security Council Executive Secretary, warned of the unintended consequences of aggressive implementation of AML/CFT standards. He stated, “[A]s we work with U.S. and overseas financial institutions, let us not forget the laws of unintended consequences. If we so harshly regulate banks that they withdraw services from post-conflict and other developing countries that are ideal breeding grounds for terrorists and their financiers, we will drive the work of these financiers into the shadows.... We must expect banks to be held to high standards in this area, but not set the bar so impossibly high that the only rational business decision is to withdraw.”¹⁰⁸

Implications of Derisking for Financial Inclusion

Some observers consider derisking to be the “single biggest threat to financial inclusion around the world.”

In recent years, the U.S. and international development agencies have emphasized the importance of extending financial access globally as a way of reducing poverty and boosting

prosperity. “Financial inclusion” is defined as individuals and businesses having access to useful and affordable financial products and services that meet their needs—transactions, payments, savings, credit and insurance—delivered in a responsible and sustainable way.¹⁰⁹ Around 2 billion people, or 40% of the world’s adults, lack access to basic financial services necessary to protect themselves from hardship. Financial exclusion is greatest among poor people and in emerging and developing countries, including the rural households that account for more than 70% of global poverty.¹¹⁰ The World Bank has called for universal financial access (access to a transaction

¹⁰⁶ Alex Zerden, “Four Pressing Issues in Combating Terrorism Financing,” *American Banker*, August 20, 2015, <http://www.americanbanker.com/bankthink/four-pressing-issues-in-combatting-terrorism-financing-1076102-1.html>.

¹⁰⁷ Matthew Epstein and Howard Mendelsohn, “Here’s How to Solve the De-Risking Riddle,” *American Banker*, May 3, 2016, <http://www.americanbanker.com/bankthink/heres-how-to-solve-the-de-risking-riddle-1080805-1.html>.

¹⁰⁸ Statement of Robert M. Kimmitt, Stopping Terror Finance: Securing the U.S. Financial Sector,” Report of the Task Force to Investigate Terrorism Financing, Committee on Financial Services, U.S. House of Representatives, at 30, December 20, 2016, http://financialservices.house.gov/uploadedfiles/terror_financing_report_12-20-2016.pdf.

¹⁰⁹ See Alliance for Financial Inclusion, <http://www.afi-global.org>.

¹¹⁰ “The Imperative of Financial Inclusion,” Website of the UN Secretary-General’s Special Advocate for Inclusive Finance for Development (UNSGSA), <https://www.unsgsa.org>.

account or electronic instrument to store money and send and receive payments) by 2020, and the UN has identified financial inclusion as an enabler for 7 of the 17 Sustainable Development Goals.¹¹¹

The trend of derisking, however, constitutes a significant challenge to financial inclusion. With FIs terminating or restricting business with remittance companies and smaller local banks in certain regions of the world, money transfers for migrant workers and NPOs have become more difficult. Some observers consider derisking to be the “single biggest threat to financial inclusion around the world.”¹¹²

MSBs and remittances have been severely affected by derisking. People working abroad send about \$450 billion a year back to their native countries, representing a major source of income for many developing countries. According to World Bank President Jim Kim, the key to continuing progress toward universal financial access will be to find a way to “mitigate the risks without slowing down financial inclusion.”¹¹³ For Mark Carney, Governor of the Bank of England and Chairman of the Financial Stability Board, derisking is akin to “financial abandonment.” Federal Reserve Chair Janet Yellen told the U.S. Congress that the trend was causing “a great deal of hardship.”¹¹⁴

Recognizing the importance of economic progress attributable to financial inclusion and global finance, then U.N. Secretary-General Ban Ki Moon appointed Her Majesty Queen Máxima of the Netherlands as Special Advocate for Inclusive Finance for Development (UNSGSA). In November 2015, she noted:

“We have recently witnessed some setbacks in the quest for greater financial inclusion. The Financial Action Task Force and the standard-setting bodies housed here at the BIS [Bank for International Settlements] have called for banks to engage in careful risk assessments. But, as many of you are already aware, some banks are engaging in what they call “de-risking” – simply ceasing to engage in lines of business that are seen as potentially high risk relative to their profitability. The term “de-risking” is problematic because, by cutting off certain clients and thereby increasing financial exclusion, de-risking can actually increase the risk of money-laundering and terrorist financing, as FATF has acknowledged. The problem is of particular concern because of its potential impact on cross-border remittances from migrants to family members—sums that in many countries dwarf official aid flows. De-risking, if not addressed in a nuanced fashion, could also negatively impact the ability of small firms to obtain export finance, or other entities to carry out development activities.... The right balance calls for a proportionate, risk-based approach advocated in the standards and guidance of the bodies housed here at the BIS.”¹¹⁵

111 World Bank, “Overview of Financial Inclusion, <http://www.worldbank.org/en/topic/financialinclusion/overview#1>.

112 Center for Financial Inclusion Blog, “Does Global De-Risking Create “Financial Abandonment”? The Background You Need to Know,” October 5, 2016, <https://cfi-blog.org/2016/10/05/does-global-de-risking-create-financial-abandonment-the-background-you-need-to-know/>

113 World Bank, “Powerful panel weighs progress on financial inclusion,” October 7, 2016, <https://blogs.worldbank.org/voices/powerful-panel-weighs-progress-financial-inclusion>

114 CFI, October 6, 2016.

115 Speech by Her Majesty Queen Máxima of the Netherlands, United Nations Secretary-General’s Special Advocate for Inclusive Finance for Development (UNSGSA), at the All Governors’ Meeting, Bank for International Settlements, Basel, November 9, 2015, <http://www.bis.org/review/r151113c.htm>.

U.S. Policy/Regulatory Response to Derisking

September 2016 marked 15 years since the 9/11 terrorist attacks, what the Treasury Deputy Assistant Secretary for Terrorist Financing called the “watershed event that fundamentally changed AML/CFT policy in America.”¹¹⁶ Reflecting on the accomplishments over this period, an official noted the essential role that combating illicit finance plays in promoting U.S. security. She went on to say: “Our terrorist financing risk assessment concluded that our efforts over the past 15 years have pushed terrorist financing out of the banking sector and into other methods, such as cash smuggling.... In the last five years, law enforcement has successfully disrupted more than 100 potential terrorist attacks, in no small part due to critical financial intelligence provided by the private sector and analyzed and disseminated by government agencies.”

Notwithstanding the critical role financial intelligence (FININT)¹¹⁷ plays, recognition of the unintended consequences of AML/CFT regulatory policies by U.S. officials has been measured. It was not until late 2015 that Treasury officials responsible for illicit finance began to acknowledge that certain sectors—correspondent banking and MSBs—are indeed experiencing difficulties in accessing financial services, even while reiterating the appropriateness of current policy: “We believe our risk-based AML/CFT standards are the right ones—for correspondent banking, MSBs and really all cross-border financial services.”¹¹⁸ The gradual recognition by U.S. officials of financial access problems has been limited, however, to certain regions of the world, such as the Caribbean, and to the specific sectors of correspondent banking and MSBs. “Treasury has been focused on this issue for some time now, and over the course of our engagement we have come to understand that some sectors and jurisdictions are affected more than others, but overall, there is no evidence to suggest a global systemic impact.”¹¹⁹ Until November 2016, there was no mention of NPOs in public statements or any recognition of the financial access difficulties NPOs have reported.¹²⁰

The debate as to whether and how much derisking poses a serious concern that requires government intervention continues. Officials object to the use of the term “derisking” as pejorative and inappropriate and remain skeptical as to the degree derisking is in fact a problem. In September 2016, Thomas Curry, Controller of the Currency, stated,

116 Remarks by Deputy Assistant Secretary Jennifer Fowler at the SIFMA Anti-Money Laundering & Financial Crimes Conference, April 6, 2016, <https://www.treasury.gov/press-center/press-releases/Pages/jl0409.aspx>.

117 Analogous to SIGINT (signals intelligence) and HUMINT (human intelligence), some analysts have recently come to characterize financial intelligence as FININT. See Clare Ellis and Inês Sofia de Oliveira, “Tackling Money Laundering: Towards a New Model for Information Sharing,” RUSI, September 2015, https://rusi.org/sites/default/files/201509_op_tackling_money_laundering.pdf.

118 Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference, November 16, 2015. <https://www.treasury.gov/press-center/press-releases/Pages/jl0275.aspx>.

119 Remarks by Acting Under Secretary Adam Szubin at the ABA/ ABA Money Laundering Enforcement Conference, November 14, 2016. <https://www.treasury.gov/press-center/press-releases/Pages/jl0608.aspx>.

120 Under Secretary Szubin’s remarks on November 14, 2016 include a reference to NPOs as part of the stakeholders Treasury is engaged with—the first time NPOs have been mentioned—but there has still been no discussion or efforts to address NPOs problems with financial access.

“...it is not surprising that some banks have chosen to reduce their risks and shrink their exposure and international business portfolios. That choice is the result of what has been pejoratively labeled ‘de-risking.’ These withdrawals, particularly in regions subject to terrorism, drug trafficking, and other illicit activity, have been the subject of a good deal of publicity and, in some cases, have caused outcry both here and abroad. The process that has resulted in these decisions is better described as risk reevaluation. It’s the process in which institutions review the risks they face on a continual basis and ensure they have systems in place that can identify and adequately address those risks. The actual process of regularly reevaluating risk is a critical and expected part of the BSA/AML regulatory regime.¹²¹

Treasury Under Secretary Adam Szubin amplified this definitional concern, noting, “The term ‘de-risking’ has come to mean different things to different people, and is not consistently used by various stakeholders. We prefer to focus the term more precisely on what we view as problematic, which are reports of financial institutions *indiscriminately terminating or restricting broad classes of customer relationships without a careful assessment of the risks and the tools available to manage and mitigate those risks.*” (emphasis added)¹²² This narrow definition and continuing lack of recognition of the impact of financial access problems on U.S. nonprofits continues.

NPO Response to Narrowing Financial Access

Reports of NPO problems with access to financial services began surfacing a decade ago. For example, on the eve of Ramadan in September 2006, the Federal Bureau of Investigation (FBI) conducted a raid on Life for Relief and Development, a Michigan-based organization that has been delivering humanitarian assistance around the world since the 1990s. Despite the fact that no criminal charges were filed, the publicity prompted Life’s local bank to withdraw its services, thereby interrupting their humanitarian assistance programs.¹²³ With this event on its record, Life has continued to have problems accessing banking services, and more NPOs began reporting similar problems.¹²⁴ While the problem initially appeared to mainly impact Muslim charities, over time it has spread to include many types of NPOs.

The serious impacts regarding the loss of financial services generated responses in the nonprofit sector, which began tracking and documenting narrowing financial access for NPOs in 2006. Organizations like Oxfam worked to maintain the remittance services that are so vital to people in need in places like Somalia. As more NPOs experienced problems, the C&SN responded by forming a Financial Access Working Group in 2014 to coordinate research, education and advocacy work on the issue, bringing the issue to the attention of U.S. officials and Congressional oversight committees.

121 Remarks by Thomas J. Curry at the ACAMS 15th Annual AML and Financial Crime Conference, September 28, 2016, <http://www.acamstoday.org/remarks-by-thomas-j-curry/>.

122 Szubin remarks, November 14, 2016.

123 Charity & Security Network, “US Muslim Charities and the War on Terror: A Decade in Review,” December 2011, <http://www.charityandsecurity.org/sites/default/files/USMuslimCharitiesAndTheWarOnTerror.pdf>.

124 Charity & Security Network, “Life for Relief & Development v. Bank of America, NA,” August 19, 2016, <http://www.charityandsecurity.org/node/1434>.

Think tanks also began to address the issue, placing it in the larger context of financial inclusion. Tom Keatinge, a UK-based researcher at the Royal United Services Institute and a former investment banker, wrote, “At the heart of this dilemma is the importance of maintaining proportionality. Research undertaken by the World Bank and the Consultative Group to Assist the Poor (CGAP) concludes that the interaction between the provision of financial services to the poor and the establishment of an effective CFT regime are ‘complementary,’ because ‘without a sufficient measure of financial inclusion, a country’s [CFT] system will safeguard the integrity of only [the formal] part of its financial system... leaving the informal and unregistered components vulnerable to abuse.’”¹²⁵

Reports by NPOs of difficulty with financial access have continued to grow; periodic meetings with government representative have been held but not resulted in concrete steps to address the issues. A significant group of NPOs sent a letter in February 2016¹²⁶ to the U.S. Departments of Treasury and State asking them to convene a multi-stakeholder dialogue as part of a broader effort to ensure that registered, law-abiding NPOs are able to access the global financial system and calling for a public statement making clear that charities are not by definition high-risk customers.

The letter noted that:

“It is increasingly difficult for these nonprofit organizations (NPOs) to access financial services that are necessary to keep their operations going. Banks may delay, or refuse to make, transfers between organizations. Sometimes, NPOs are turned away as customers or have their accounts closed. For example, in the spring of 2015, one charity was unable to pay for fuel needed to supply power to a hospital in Syria because of the banks’ lengthy delays in transmitting funds... The banks and the U.S. Treasury Department are blaming each other for the problem and to date have done little to solve it.”¹²⁷

Treasury and State responded in a May 2016 joint letter stating that, “It is important to emphasize the Treasury Department’s view that the charitable sector as a whole does not present a uniform or unacceptably high risk of money laundering, terrorist financing or sanctions violations.” The letter adds that banks should take a risk-based approach to conducting due diligence on nonprofit customers but that, “Treasury expects banks to apply their due diligence obligations reasonably— *not that they be infallible in doing so...*” (emphasis added).¹²⁸ In a July 21, 2016 response, the group of nonprofits asked the Treasury to update the Bank Examiners Manual section on NPOs that refers

125 A War of Proportion: Regulating the Financial Sector in the Name of Counterterrorism, September 18, 2013, http://www.charityandsecurity.org/blog/War_Of_Proportion_Financial_Sector_Counterterrorism. Citing Bester, H., D. Chamberlain, L. De Koker, C. Hougaard, R. Short, A. Smith & R. Walker, Implementing FATF Standards in Developing Countries and Financial Inclusion: Findings and Guidelines, The FIRST Initiative, 2008, (Washington, DC: The World Bank) www.cenfri.org/documents/AML/AML_CFT%20and%20Financial%20Inclusion.pdf.

126 Letter to Jacob Lew, Treasury Secretary, and John Kerry, Secretary of State, February 25, 2016, http://www.charityandsecurity.org/system/files/Sign%20on%20Ltr%20Fin%20Access_1.pdf. The 58 NPO signatories to the letter included umbrella groups with more than 300 member organizations combined and represented more than 8.3 billion annually in humanitarian aid and services to the world’s most needy.

127 Ibid.

128 Letter to Kay Guinane, Charity & Security Network, from Jennifer Fowler, Deputy Assistant Secretary, Department of Treasury, and Andrew Keller, Deputy Assistant Secretary, Department of State, May 13, 2016, <http://www.charityandsecurity.org/system/files/Joint%20Response%20letter%20to%20NPO%20on%20reduced%20access%20to%20financial%20services%20May%202016%20signed.pdf>.

to the entire sector as “high-risk” to comport to the new FATF R8. Plans have not been announced to move up the timetable for revision of the Manual currently slated for 2018. Progress on the overall issue of derisking of NPOs remains elusive, and many NPOs express frustration with their inability to engage government in a results-oriented process.

As noted in the Introduction to this report, the theme that emerged in the discussions with all stakeholders was the need for solid data in order to better understand the issues NPOs face in accessing financial services. Until now, there has been no empirical data collected concerning U.S.-based NPOs' problems with banking services. Previous studies have called for a representative survey to provide an unbiased assessment of the extent and nature of NPOs' financial access difficulties.¹²⁹ Similarly, a number of senior U.S. government officials, some in public statements and others in private interviews, have called for more data "to continue to improve our understanding of the scope, nature, and drivers of the [derisking] problem." This need was echoed by Congressional staff who asked for analytical data going beyond anecdotal examples.

Chapter 4: SURVEY RESULTS AND DATA ANALYSIS

The purpose of this chapter is to present empirical data from the random sample survey undertaken for this study. (The survey methodology is described in Chapter 1.) The survey findings are supplemented with information gathered from relevant stakeholder discussions.

Researchers wanted to understand specifically the types of NPOs having problems, the programs/services they provide, the possible causes of their banking difficulties and the impact of these obstacles on the NPOs, donors, program beneficiaries, national security and integrity of the financial system. The researchers also sought to understand how NPOs are getting money to these programs when traditional banking services become unavailable or transfers are significantly delayed.

The 305 telephone surveys unearthed a trove of data that sheds new light on the scope, extent and types of banking problems that NPOs regularly face. The problem is far greater in magnitude than previously assumed.

Characteristics of U.S. Nonprofits Operating Abroad

To provide an overview of the organizations upon which this study is based, this section describes the employee size, revenues, expenditures and program activities of U.S. NPOs operating abroad.

¹²⁹ *Unintended Consequences of Anti-Money Laundering Policies for Poor Countries*, Center for Global Development ("CGD Study"), November 9, 2015, <http://www.cgdev.org/publication/unintended-consequences-anti-money-laundering-policies-poor-countries>.

There are 8,665 such groups, based on IRS Form 990 Schedule F filings.¹³⁰ They range from small, volunteer organizations to major research universities and large hospitals. They provide medical care, education, emergency assistance and refugee resettlement to populations in need. They conduct research and sponsor cultural and educational exchanges. They promote human rights and the rule of law and work to build peace in places experiencing violent conflicts.

While there is a broad array in the size of nonprofits, most are relatively small, as defined by revenues and expenditures. Total revenue of these NPOs ranges from as little as \$100 to \$2.7 billion, and their expenditures run from zero to \$2.2 billion. However, about half of the groups have yearly expenditures of less than \$1 million and total revenues of less than \$1.5 million, suggesting that volunteer, grassroots organizations account for a large share of the field (see Table 2).

As noted in Chapter 1, the distribution of revenues and expenditures is skewed by a relatively small number of very large institutions, such as colleges, universities and hospitals, which account for 75% of the total revenues. To allow for an assessment of more “traditional charities,” therefore, much of the data were analyzed omitting this subgroup of “outliers” (defined by their National Taxonomy of Exempt Entities [NTEE] cluster code¹³¹). For most queries, the results were not statistically significant; only marginal differences (<2 percentage points) appeared. For this reason, data showing the difference between the entire group of NPOs and the “traditional” charities are presented only when that difference is statistically significant, as in the table below.

While most groups are relatively small, almost half of them (48%) are large enough to operate a branch or field office abroad, and more than a quarter (27%) maintain a foreign bank account. Although there is further discussion of structure and foreign bank accounts in this report, exploration of these issues was beyond the scope of this report but warrants further analysis.

Table 2: Revenues and Expenditures of NPOs

Median Revenues and Expenditures	All NPOs	“Traditional” Charities
Median total revenue (USD)	1,456,700	1,149,600
Median total expenditure (USD)	1,000,700	749,100
Minimums		
Minimum total revenue (USD)	100	100
Minimum total expenditure (USD)	0	0
Maximums		
Maximum total revenue (USD)	2,691,041,000	771,806,000
Maximum total expenditure (USD)	2,200,720,000	427,704,300

¹³⁰ See Methodology, Chapter 1, for a description of IRS Form 990 Schedule F.

¹³¹ The National Taxonomy of Exempt Entities (NTEE) system is used by the IRS and the National Center for Charitable Statistics to classify nonprofit organizations. It divides the universe of nonprofit organizations into 26 major groups under 10 broad categories, such as Education, Health, Human Services and Religion.

Table 3: Program Areas*

Program Areas	Total Organizations (Percent)
Education	77.1
Development/poverty reduction	46.0
Humanitarian relief	45.2
Public health	39.2
Medical services	33.6
Human rights/democracy building	19.7
Peace operations/peacebuilding	14.3
Other	30.7

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

As expected, NPOs work in a variety of program areas (see Table 3), and the vast majority work in more than one area. Seventy-seven percent are engaged in some type of educational work, which can include institutions of higher learning, charities that provide support for childhood education abroad and much more. The high percentage of charities that conduct educational work suggests that charities often undertake educational activities in order to carry out their mission. This crucial activity is frequently overlooked and highlights the need to learn more from NPO leaders about how they characterize their work. As Table 3 shows, almost half of nonprofits (46%) work in programs that

address immediate human need such as development and poverty-reduction projects (46%), as well as humanitarian relief (45%). One-fifth work in human rights and democracy promotion.

Thirty-two percent of nonprofits self-identify as faith-based. Unfortunately, the random sample was not large enough to make distinctions between various faiths. For example, only three groups self-identified as Muslim, so it was not possible to determine whether certain problems disproportionately affect particular faith groups.

Financial Access Problems

Two-Thirds of All NPOs Encounter Financial Access Difficulties

A significant proportion (2/3) of NPOs that conduct international work are experiencing obstacles in accessing financial services. Extrapolating to the total population of NPOs, *at least 5,875 U.S.-based nonprofits doing work in foreign countries encounter some type of banking difficulty in their work.*

Over 15% of NPOs encounter these financial problems constantly or regularly, with another 31% reporting occasional problems (see Table 4).

Figure 5: Scope of NPO Financial Access Problems

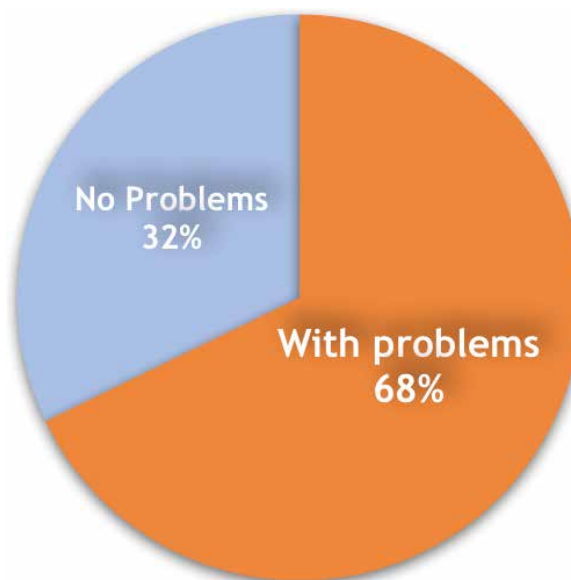


Table 4: Frequency of Financial Access Problems*

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
TOTAL	100.0	8,665

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

Fund Transfers Are the Most Common Banking Problem NPOs Face

The two most common problems encountered by NPOs are delayed wire transfers (affecting almost 37% of all NPOs) and increased fees (affecting approximately 33%). One out of every three NPOs has experienced either or both of these problems in attempting to utilize traditional banking channels to send resources to foreign countries.

Delays in the transfer of funds lasting days, weeks or even months impact time-sensitive programming. “You can’t wait six weeks for a wire transfer,” explained the director of an NPO. Another focus group participant stated that every one of their wires is questioned, even if it is going to a repeat destination or recipient.

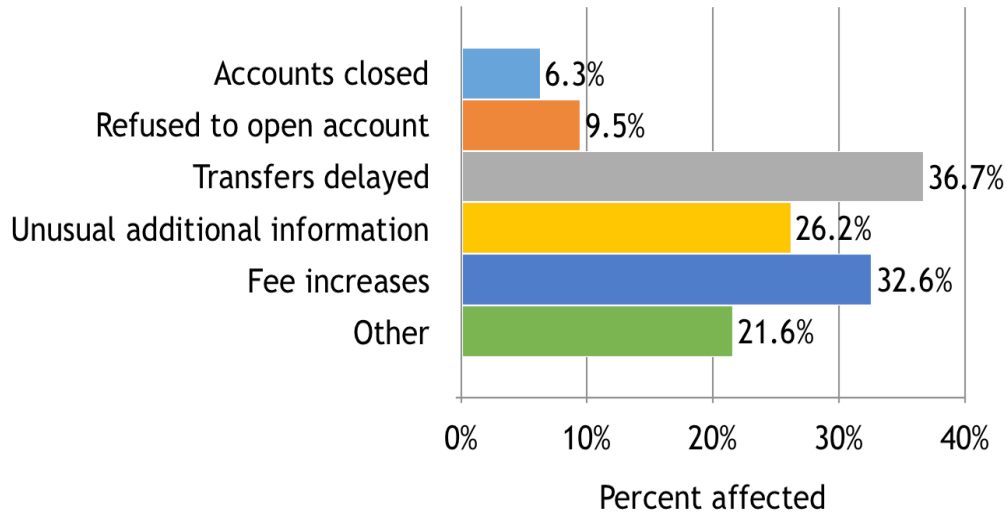
NPOs report that wire requests are sent back with additional questions, but some are returned to the originating bank and denied with no explanation. Wires are sometimes denied because organizations, particularly Muslim charities, are confused with sanctioned persons or groups. “There were two entities with similar names, one of which was on the SDN list” (Specially Designated Nationals list, maintained by the U.S. Treasury Department), explained one charity’s director. “We had maddening conversations trying to prove who we weren’t.”

Many NPOs attribute problems to correspondent banks rather than their own financial institution when wire transfers are held up. One NPO leader noted that intermediate banks do not save the data provided, so they end up asking for the same information with each new transaction. Regulators have suggested that NPOs improve their relationship with their banks in order to facilitate easier transactions, but “a good relationship with a U.S. bank can’t solve problems with intermediaries,” one grantmaker observed.

Problems also occur on the recipient end. Grantees sometimes need to show recipient banks a receipt or other documentation from the originating bank. “Without it, the recipient bank will claim

they haven't received the funds," because they were never sent, a participant explained. In some cases, a foundation employee said, the money will be cleared to the recipient account, but after 3 to 6 months, the recipient bank says that the organization has no right to the money or that the organization needs to open a different kind of account. "They return the funds and the foundation attempts to resend it, but that can take an additional three months."

Figure 6: Prevalence of Financial Access Problems*



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

Additional/Unusual Documentation Requests Create Bottlenecks

Requests for unusual additional documentation can also delay wire transfers as the necessary information is compiled. The excessive nature of some requests means that the needed documents may not be readily available. More than a quarter of NPOs encountered unusual and often duplicative and unexplained documentation requests (see Figure 6), constituting a burden for NPOs. "There's no internal communication within the banks. They request the same information and documentation over and over," explained one charity's director. Others say that lack of clarity about what information is actually required to ensure legal compliance is to blame.

The list of documents requested can be extensive, well beyond information normally supplied. If money is going to a vendor, some FIs will ask for service contracts, receipts, invoices and confirmation that there is no relationship with any sanctioned entity, according to an NPO officer. An NPO treasurer said his organization does not feel like it is dealing with one bank anymore. "Different branches are asking for different information."

NPOs Are Paying Higher Fees for Banking Services

One-third of NPOs report that their costs for financial services are going up. Financial institutions, facing increased compliance expenses, need to recoup these costs and pass them along to the customer. This hinders the ability of NPOs to conduct their work, since most NPOs are small and have limited resources.

Account Closures Are a Smaller Problem with Bigger Impact

Although account closures (reported by 6.3% of NPOs) are less common than transfer delays, they can have an extraordinary impact, affecting approximately 546 nonprofits. Some banks have taken deliberate action to limit business with charities, according to a financial institution manager. The bank indicated its intention to wind down all business with charities due to costs associated with risk management, he explained.

If an NPO has all of its accounts at a single bank, closures can leave a group entirely without banking services. “You have 30 days to move your money” is a daunting message to receive, particularly when no explanation or opportunity to correct perceived problems is offered. “They wouldn’t give a reason,” said one NPO treasurer, adding, “We’d had a relationship with them for more than 20 years. We just got a letter and had to move our money. All of our transactions were with that bank.”

A forced account closure can create shockwaves throughout an organization, regardless of its size, sending personnel frantically searching for new banking services. And once an organization has had an account closed, other banks may be reluctant to accept the NPO as a new customer. “Once you’re flagged, it’s very difficult to find another bank that will be willing to do business with you,” said the director of one charity.

The Prevalence and Types of Problems NPOs Encounter Vary by Program Area

The prevalence of problems encountered by NPOs vary by the types of programs they run. NPOs operating educational programs are by far the most likely to encounter obstacles to financial access (see Table 5). Of all nonprofits experiencing problems, 80% work in education. In addition, approximately half of those with problems are working in development and poverty reduction, humanitarian relief and/or public health.

Table 5: Prevalence of Problems by Program Area*

Program Area	Percent of All Organizations		Percent of “Traditional” Charities	
	Reporting Problems	Not Reporting Problems	Reporting Problems	Not Reporting Problems
Education	80.9	69.5	64.7	35.3
Development/poverty reduction	52.0	31.6	70.8	29.2
Humanitarian relief	49.5	35.1	66.4	33.6
Public health	45.0	27.6	73.8	26.2
Medical services	34.0	33.0	64.6	35.4
Human rights/democracy building	21.5	16.3	68.0	32.0
Peace operations/peacebuilding	16.0	8.6	73.5	26.5
Other	27.9	34.2	56.9	43.1

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

As seen in Table 5, the differences are far more pronounced when looking at “traditional” charities (larger groups or “outliers” omitted). Those NPOs working in peace operations/peacebuilding, public health, development/poverty reduction, human rights/democracy building and humanitarian relief report the greatest percentage of financial access problems. As indicated earlier and seen in Table 6 below, wire transfers are the most common banking issue, along with fee increases, regardless of program area. Some differences in the type of financial access problems encountered are discernable by program area. Peacebuilding organizations are the most likely to incur account closures, new account refusals and wire transfer delays. Groups working in human rights and democracy building are most likely to encounter increased fees.

Table 6: Problem Type by Program Area*

Program Area	Accounts Closed	Refused to Open Account	Transfers Delayed	Unusual Documentation Requests	Fee Increases	Other
Education	7.8	11.3	37.5	28.9	33.2	23.3
Development/poverty reduction	6.5	12.2	41.7	27.3	40.7	26.9
Humanitarian relief	8.8	11.1	46.3	23.5	36.6	22.1
Public health	8.5	11.1	46.6	28.0	39.3	28.3
Medical services	8.9	9.9	38.6	17.8	33.3	17.4
Human rights/democracy building	6.8	11.9	52.5	22.0	43.1	26.8
Peace operations/peacebuilding	11.6	16.3	55.8	25.6	35.7	35.0
Other	7.9	11.8	34.2	31.6	32.0	32.9

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

Wire Transfers Destined for All Parts of the World Encounter Problems

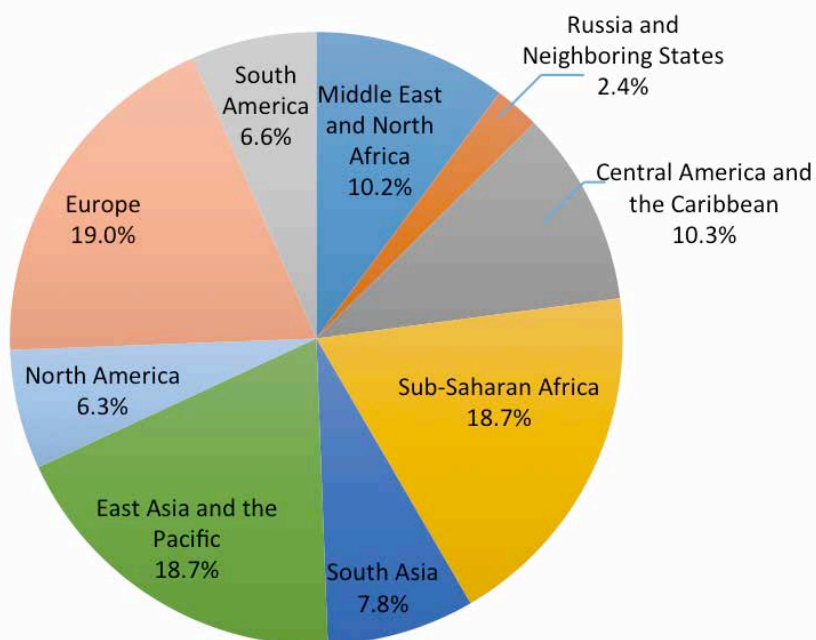
It might be assumed that NPOs face the greatest difficulties with transfers destined for geographic locations subject to violent conflict. However, focus group participants began to paint a different picture. They noted problems not only in Burma, Egypt, Yemen, Iran and Sudan, for example, but also with wires to Europe. “Problems exist in more countries than not,” said one participant. Another explained, “Certain words in the name of the recipient account holder, such as Crimea or Iran, will trigger a problem, even if the wire recipient is based in Europe.” A Syrian-focused charity explained that the word “Syria” in its name has raised red flags at financial institutions. Even groups providing assistance to Syrian refugees in Turkey or Lebanon have experienced serious delays and questions about their financial transfers.

The survey data underscores the broad geographic impact and reinforces the point that difficulties with wire transfers are global (see Figure 7). Rather than being confined to conflict zones or geopolitical hotspots, the problem affects transactions to South Asia, Middle East & North Africa (MENA), Sub-Saharan Africa, South America and beyond.

Survey respondents were asked to identify to which countries their delayed financial transfers were headed. Exhibit 7 shows the distribution of the countries mentioned, by world regions, based on IRS categories of countries. For example, Turkey is listed as part of Europe.¹³²

The Americas collectively account for almost one in four countries mentioned (23%). Surprisingly, regions that might be expected to be particularly affected for geopolitical reasons do not dominate the regional breakdown: the Middle East and North Africa account for 10% of all country mentions; South Asia (including Afghanistan and Pakistan among others) for 8%; and Russia and other former members of the Soviet Union (outside of the Baltics) for a mere 2%.

Figure 7:
Affected Fund Transfer Destinations by Region



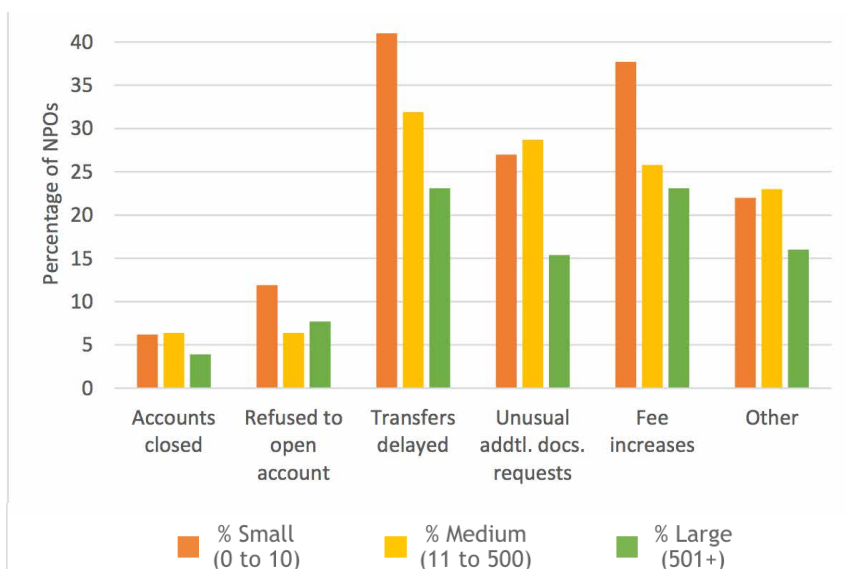
¹³² Using the regional breakdowns in IRS Form 990 Schedule F, see Appendix C.

Small NPOs Are More Likely to Face Banking Obstacles

When dealing with financial access problems, size matters. This is true whether organizations are characterized by the number of employees, by revenue or by expenditures. In general, organizations with more than 500 employees and those with higher revenues and expenditures are less likely to suffer from all types of banking problems than those organizations with fewer than 500 employees or lower revenues and expenditures (see Figure 8).

In this context, it is important to remember that most charities are small—half of them operate with less than \$1.5 million in revenues and less than \$1 million in expenditures. NPOs with 500 or fewer staff members are more likely to encounter delayed wire transfers, fee increases, account closures and unusual documentation requests. Most significantly, smaller organizations are almost twice as likely to receive unusual additional documentation requests. The smallest NPOs (those with 10 or fewer employees) are having the most trouble opening accounts. Size matters not only because banks might respond more positively to larger organizations but also because small NPOs have fewer resources and staff to deal with these issues. Representatives of large NPOs likewise have characterized the obstacles they face as significant; the larger NPOs that experience problems are similarly hamstrung as smaller charities.

Figure 8: Prevalence of Problem by NPO Size*

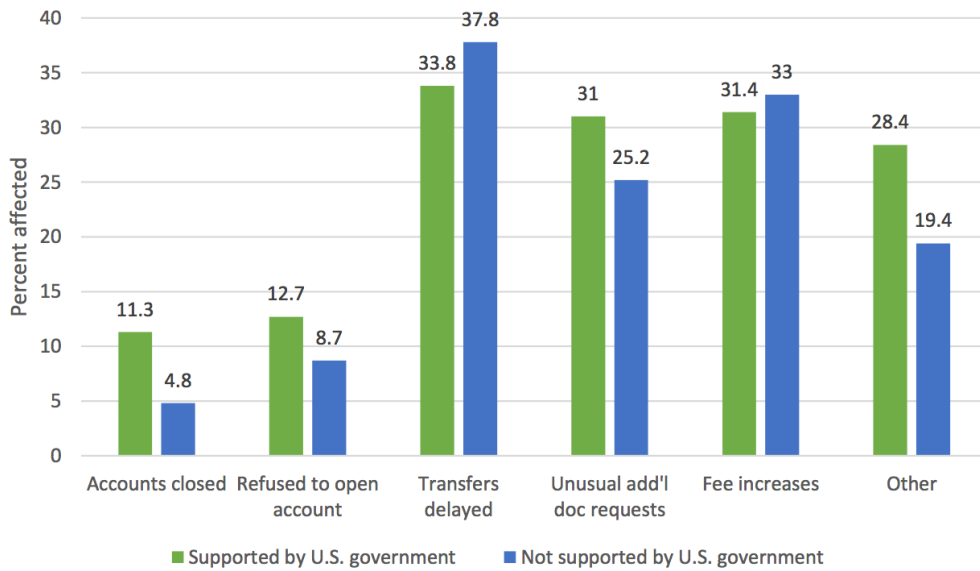


*Percentages do not total 100% because survey respondents were allowed to give more than one response.

NPOs with Government Funding Are More Likely to Encounter Banking Problems

A significant portion of U.S. international assistance is administered and delivered through NPOs. While some might assume that NPOs administering U.S. government-funded projects internationally would have less difficulty with financial transfers since they undergo extensive due-diligence checks, this is not the case. In fact, the data illustrate that these nonprofits actually have greater difficulty with account closures and refusals to open accounts, as well as documentation requests, than those without such support (see Figure 9). One NPO representative informed his FI that they receive USAID money, but the bank responded, “I don’t care. I worry about the regulators.” He added, “One wing of U.S. government is giving us money and another wing says, ‘You might be funding terrorism.’”

Figure 9: U.S. Government Funding by Problem Type *



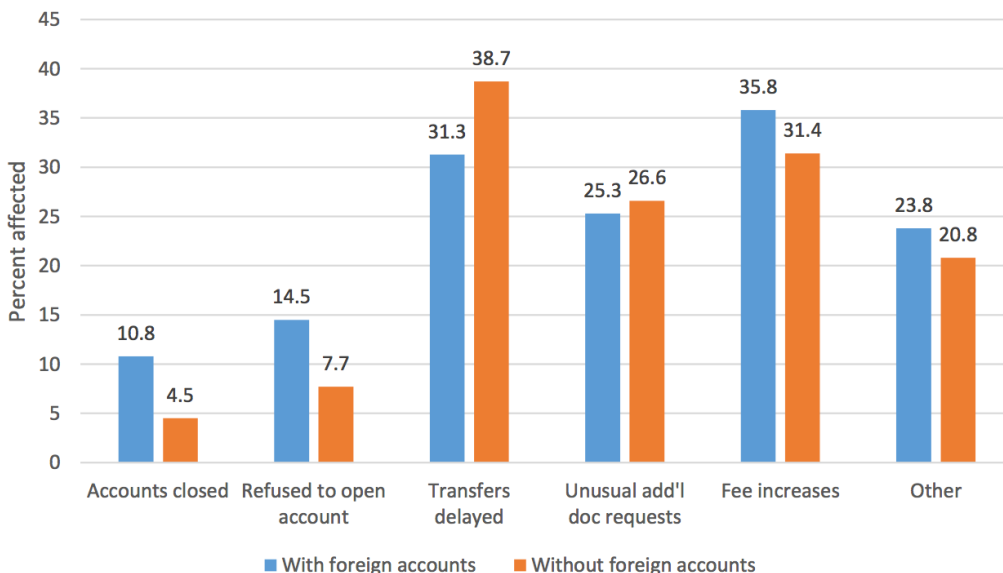
*Percentages do not total 100% because survey respondents were allowed to give more than one response.

These numbers should be of concern to U.S. government agencies funding NPOs to carry out government projects in foreign countries. U.S. assistance funds are having difficulty reaching the intended recipients, and, as discussed later in this chapter, some are slipping out of traditional banking channels. How government funding is related to financial access issues for NPOs is important to explore further.

NPOs with Foreign Bank Accounts Are More Likely to Encounter Banking Challenges

Maintaining a foreign bank account is related to the financial problems that NPOs experience (see Figure 10).

Figure 10: Percent with Foreign Account by Problem Type*



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

Having a foreign bank account seems to be related to greater difficulty with opening and maintaining bank accounts in the U.S. Such NPOs report account closures and refusals to open new accounts domestically at twice the rate of NPOs without foreign accounts. They also report fee increases at a higher rate (36% versus 31%). On the other hand, their wire transfers are less frequently delayed. While almost one-third (31%) of NPOs with foreign accounts report difficulties wiring money internationally, 39% of NPOs without such accounts report the same problem.

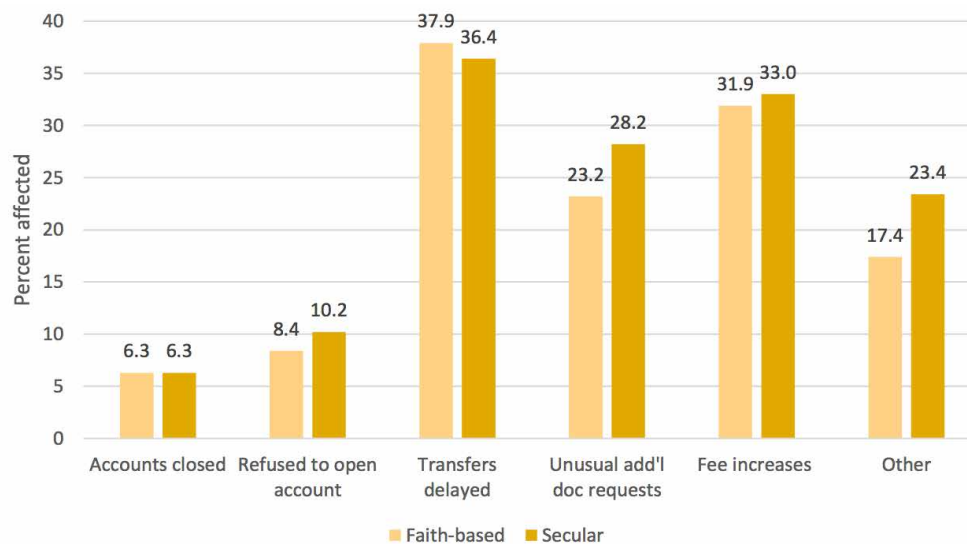
The survey also examined whether banking problems are related to NPOs sending money to their own or another organization’s field office, a local community organization or a government office or agency. The data do not show a clear pattern as to whether the intended recipient or beneficiary of the foreign financial transaction triggers particular banking problems. Account closures, new account refusals and unusual documentation requests are equally likely to occur, regardless of the intended recipient. Groups sending money to their own field offices abroad experience problems at rates slightly higher than the average for all destinations, despite the fact that the recipient is a known entity. At the same time, groups transferring money to field offices of other charities see a slightly higher incidence of delayed transfers (45% versus 38%). Transfers are most commonly delayed when the intended recipient is a local community organization (49.6% of transfers to these groups are delayed).

Faith-Based and Secular Organizations Are Equally Impacted

While certain characteristics of NPOs, such as the organization’s size, do impact a group’s ability to access banking services, other characteristics do not. One of the questions at the outset of this study was whether faith-based organizations, particularly those that self-identify as Muslim, face greater obstacles than secular groups.

Overall, the data show that the likelihood of financial access difficulties is roughly the same between faith-based and secular NPOs (see Figure 11). Where there are differences, it was noted that faith-based organizations have relatively fewer requests for additional documentation than secular groups (23% versus 28%), as well as fewer other demands imposed by financial institutions (17% versus 23%).

Figure 11: Faith-Based or Secular by Problem Type*



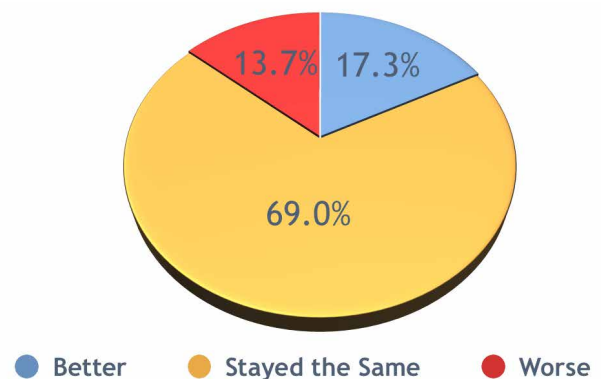
*Percentages do not total 100% because survey respondents were allowed to give more than one response.

An insufficient number of survey respondents self-identified as Muslim charities to analyze them separately. However, anecdotal evidence that Muslim groups are having a particularly difficult time with banking continues to surface. Problems with account closures and refusals to open accounts came up in discussions with Muslim- and Syrian-focused charities more frequently than with other charities. One participant characterized the financial access crisis as “the worst existential threat to Muslim organizations since 9/11.” Given the severe impact that account closures can have on an organization and beneficiaries, even anecdotal indications that Muslim charities are disproportionately impacted is a cause for concern and requires further study.

Financial Access for NPOs Is Not Improving

Although media reports on derisking are more frequent, only recently have they underscored the plight of NPOs in this global phenomenon or the impact it has on the various stakeholders. In reality, NPOs have faced these challenges for some time, and the situation is not improving. When asked about their perception of the change over time of the banking problem for nonprofits, 69% report that the problem has stayed the same, while approximately 14% say it is worse. Only about 17% believe the problem to be improving (see Figure 12).

Figure 12: Perception of Change in Severity



Some say the problem is due to the pervasive view of charities as being “particularly vulnerable” to terrorist abuse, which, despite evidence to the contrary, lingers. “You can’t shake the perception,” explained one financial institution representative.

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

Table 7: Strategies Used to Address Problems*

Strategies	Percent of NPOs Utilizing
Carry cash	41.7
Cancel the program	3.4
Find another financial institution	36.5
Use money remitter (Western Union or similar)	29.4
Perform 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.

Organizations operating in crises cannot simply hit the pause button on programs to address famine-induced starvation or the mass migration of refugees. For the vast majority of NPOs, canceling a program is not an option (see Table 7), and the survey confirmed that: only 3.4% of NPOs do so. Instead, when traditional means of moving money become unavailable, NPOs find workarounds, and the data show that they are utilizing a variety of strategies.

Of significant concern is the data indicating that 42% of NPOs resort to carrying or sending cash when traditional banking channels become unavailable. This tactic entails significant risk for all parties, especially for those operating in conflict zones. There is the physical risk to NPO staff and beneficiaries and the associated liabilities of cash. NPOs are aware of the risks and prefer not to use cash. “We hate it, but the problems made it necessary,” said the director of one NPO. Importantly, this method is contrary to the transparency and traceability objectives of CFT policies.¹³³

Most often, NPOs are able to successfully perform a transaction later. While delays may create a ripple effect throughout programs, in these cases the money remains in traditional banking channels. Other NPOs seek out alternative financial institutions (37%) or ways to move money such as MSBs (29%). However, NPO participants indicate that this latter alternative is becoming increasingly difficult as well. “Unless you’re sending smaller amounts, it’s just like any other wire because it goes through SWIFT (Society for Worldwide Interbank Financial Telecommunication) and OFAC (U.S. Treasury’s Office of Foreign Assets Control) reviews,” explained one NPO treasurer.

Some nonprofits are concerned about the potential risks of using MSBs. One NPO representative said, “I’m not comfortable with compliance around MSBs. I have more confidence in the banking system, but we [if they are not available, we] need to work around them.” “This is very risky because it adds an extra layer of vetting, and there’s also the possibility that the individuals will run with the money,” noted an NPO leader.

In most cases, funds ultimately make their way to intended recipients, but delays can cause dire humanitarian consequences. In addition, finding workarounds to banking problems is time-consuming and resource-intensive. It squanders limited NPO resources and diverts money away from programming and its beneficiaries. As one NPO director put it, “The side solutions help in an emergency but cannot be normal routine.”

Impact of Problems

The Impact of Financial Access Problems for NPOs Is Real and Significant

As the data clearly indicate, NPOs are experiencing significant problems in accessing financial services. While the data provide statistical information, it is important to keep in mind that these difficulties have real and harmful effects.

The biggest impact is felt by the program beneficiaries: people suffering from starvation, disease and conflict.

Forty-five percent of all NPOs engage in humanitarian relief work. The problems caused by any type of financial access problem, from delayed wire transfers to account closures, have serious consequences for many program

beneficiaries. Among NPOs doing humanitarian aid work, 50% have problems accessing financial services. Their problems occur frequently, with 17% having regular or constant difficulties and 34% having occasional problems.

¹³³ See, e.g., Rob Barry and Rachel Louis Ensign, “Losing Count: U.S. Terror Rules Drive Money Underground,” Wall Street Journal, March 30, 2016, <http://www.wsj.com/articles/losing-count-u-s-terror-rules-drive-money-underground-1459349211>.

Turn the proportions of NPOs serving populations of various sizes into total numbers of people, and even the smallest estimates of impact (a program serving less than 100 people) are meaningful. For example, when the total population of NPOs (8,665) is considered, all of the humanitarian aid organizations that serve fewer than 100 people each could impact as many as 19,500 total people¹³⁴ in need.

However, the impacts are likely much larger. About 2/3 of all nonprofits serve sizeable populations, numbering in the thousands and up. In the area of humanitarian relief, for example, approximately 75% of organizations serve between 1,000 and 10,000 program beneficiaries each (see Table 8).

Table 8: Size of Populations Served, Per Organization, by Program Area

Program Area	Size of Populations Served, Per Organization (Percent)				
	Less than 100	100 to 1,000	1,000 to 10K	More than 10K	Total
Education	8.3	29.0	31.6	31.1	100.0
Development/poverty reduction	4.2	18.3	37.5	40.0	100.0
Humanitarian relief	5.0	20.2	36.1	38.7	100.0
Public health	3.0	16.2	39.4	41.4	100.0
Medical services	7.6	18.5	34.8	39.1	100.0
Human rights/democracy building	8.0	16.0	34.0	42.0	100.0
Peace operations/peacebuilding	11.8	23.5	26.5	38.2	100.0
Other	21.1	22.8	26.3	29.8	100.0

The biggest impact is felt by program beneficiaries, people suffering from starvation, disease and conflict. The impact of financial access problems affects numerous programs, from international collegiate sports tournaments to humanitarian aid in Syria, with the severity of these impacts varying significantly.

Humanitarian relief efforts, by definition, provide life-saving aid in areas of conflict and natural disaster. They operate under strict principles of humanity, impartiality, neutrality and independence. In conflict zones, international humanitarian law is meant to protect access to civilians in need of aid. “We work with refugees, gender-based violence, psycho-social care to deal with trauma, nutrition programs, maternal health care, all the things we take for granted here,” explained an NPO treasurer.

¹³⁴ Forty-five percent of U.S.-based nonprofits working abroad are involved in humanitarian aid work (45% of 8,665 total organizations = 3,899 organizations). Five percent of groups working in humanitarian aid (5% of 3,899 = 195) serve fewer than 100 beneficiaries. The maximum number of beneficiaries these organizations could serve is 19,500).

One NPO was prevented from sending immediate relief to the persecuted Rohingya minority in Myanmar in the midst of a dire humanitarian crisis. Timely transmittal of those funds might have saved lives, the charity’s director explained. Another NPO representative said, “We are interested in working with banks to alleviate whatever fears they may have. They need to have an understanding that at the end of the day, this money helps beneficiaries facing real hardships on the ground.” As another said, “We are in the business of charity.”

Conclusion

This chapter presents a range of data that has not previously been available. While there have been abundant anecdotes concerning financial access obstacles in the past, the data indicate that the problem is far more pervasive than previously anticipated. The fact that 2/3 of U.S.-based NPOs experience delays and denials of wire transfers, additional documentation requests, and other problems with international banking constitutes a serious challenge for the continued delivery of vital humanitarian and development assistance—a core component of American foreign and security policies. Moreover, the coping strategies NPOs are forced to pursue to continue their programs, especially resorting to increased use of cash, is contrary to AML/CFT objectives of promoting transparency and traceability to combat illicit finance.

"It is useful to recognize that all parties—policymakers, regulators, banks, and bank customers—are acting rationally, given the distinct pressures and responsibilities they face."¹³⁵

To understand the complexity of the issues surrounding financial access for NPOs, it is critical to appreciate the differing perspectives of the relevant stakeholders: U.S. regulators and policy officials, financial institutions and the nonprofit sector. Over the course of 9 months, a series of meetings, interviews, roundtables and focus groups were organized by C&SN to understand unique viewpoints of each group. Only one of these meetings, organized by the World Bank/ACAMS¹³⁶ in the spring of 2016, involved multiple stakeholders present at the same time.

As problems with financial access for NPOs have come to light over the past several years, there have been limited opportunities for stakeholders to meet and discuss these complicated issues. U.S. government officials have had periodic meetings with NPOs and more regular engagement with FIs in which derisking is discussed, but they have been characterized by multiple participants as sessions in which stakeholders “talk past each other.”

This absence of real dialogue around financial access issues has resulted in an environment of misunderstanding the respective perspectives, as well as reinforced stereotypes. The lack of an overarching process to facilitate collective discussion and responsibility for solutions has contributed to strained relations among stakeholders.

Two overriding impressions resulting from stakeholder meetings are particularly noteworthy. First, there is a sense of frustration among all stakeholders: frustration among NPOs that their problems are not taken seriously and that they are perpetually seen as too risky to bank; frustration among policymakers and regulators that their statements and efforts are not sufficient to address derisking concerns; and frustration within the financial sector for being blamed by both NPOs and government, caught in the middle. The second preponderant view is apprehension: fear to speak out and openly criticize the shortcomings of the current system, given risks of enhanced regulatory scrutiny and potential backlash.

¹³⁵ Matthew Epstein and Howard Mendelsohn, “Here’s How to Solve the De-Risking Riddle,” *American Banker*, May 3, 2016, <http://www.americanbanker.com/bankthink/heres-how-to-solve-the-de-risking-riddle-1080805-1.html>.

¹³⁶ The Stakeholder Dialogue on De-risking, a workshop organized by the World Bank and ACAMS (Association of Certified Anti-Money Laundering Specialists) May 31–June 1, 2016 was the first time that representatives of governments (policy, regulatory and law enforcement authorities), NPOs, academics and think tanks, international organizations and financial institutions had the opportunity to meet and discuss derisking issues. The summary of the meeting is available online. “Stakeholder Dialogue on De-Risking: Findings and Recommendations,” *ACAMS TODAY*, October 11, 2016, <http://www.acamstoday.org/stakeholder-dialogue-on-derisking/>.

The following chapters describe the perspectives and experiences of these three communities, as much as possible, in their own words and through examples of actual occurrences, without commentary.

Chapter 5

REGULATORS AND POLICYMAKERS

The most fundamental task of government is to provide for the security of its citizens. In the aftermath of 9/11, the priorities of the U.S. government shifted to focus on denying terrorist groups (initially al-Qaeda and the Taliban, and now Islamic State/ISIL/ISIS) essential resources to carry out their activities.

Protection of the global financial system from abuse by criminal and terrorist organizations has been and will continue to be an essential element of U.S. national security policy.¹³⁷ Strengthening the international financial system to combat illicit finance, anchored in the FATF, is a key component of multilateral efforts to deter and defeat terrorist threats. In the aftermath of the 2015 Islamic State of Iraq and the Levant (ISIL)/Da'esh bombings in Paris and elsewhere, the international community recommitted to bolstering such efforts through the *G-7 Action Plan on Combatting the Financing of Terrorism*.¹³⁸ Such counterterrorism and CFT initiatives continue to receive widespread political support both in the U.S. and among its allies.

Skeptical View of Derisking

Complaints that AML/CFT regulatory requirements contribute to derisking were initially met with skepticism by policymakers. The then-head of the FATF, Roger Wilkins, told the Financial Times in 2014 that derisking was likely related to rising regulatory capital requirements such as Basel III, and “not so much a function of our standards as a fig leaf for the banks doing what they need to do and are going to do anyway by taking people off their balance sheets.... There is nothing in our standards that requires this ‘blunderbuss’ approach to de-risking.”¹³⁹ In a separate statement, Wilkins noted that, “It is sort of understandable that people working in banks find it easier to say ‘no’ rather than go through a process of understanding the intent and rules involved in a transaction. That of course is unless the customer is wealthy and the transaction is significant.”¹⁴⁰

¹³⁷ See U.S. National Security Strategy, The White House, February 2015, https://www.whitehouse.gov/sites/default/files/docs/2015_national_security_strategy.pdf.

¹³⁸ See G-7 Action Plan on Combatting the Financing of Terrorism, May 20-21, 2016, http://www.g7sendai2016.mof.go.jp/summary/pdf/g7_action_plan_on_cft_en.pdf.

¹³⁹ Martin Arnold, “Financial task force warns on banks’ approach to de-risking,” Financial Times, November 13, 2014, <https://www.ft.com/content/087afe70-66bc-11e4-91ab-00144feabdc0>.

¹⁴⁰ *Remarks of FATF President Roger Wilkins delivered at the 6th Annual International Conference on Financial Crime and Terrorism Financing*, “The danger of driving both illicit markets and financial exclusion,” Kuala Lumpur, October 8, 2014, <http://www.fatf-gafi.org/publications/fatfgeneral/documents/danger-illicit-markets-financial-exclusion.html>.

The undertone of skepticism as to whether derisking is a serious problem, and if so, how relevant it is for U.S. policy, has characterized U.S. government statements since the issue first emerged. In 2015, Treasury Under Secretary David Cohen stated,

“I have put ‘de-risking’ in quotes because there does not appear to be either a uniform understanding about what the term means or a consensus that a serious ‘de-risking’ trend is underway [...] It is not the closing or restricting of an account because a financial institution, applying an appropriately designed risk-based analysis, determines that it cannot manage the risk of illicit activity associated with a particular client. When that happens, a financial institution is doing precisely what the BSA and the FATF standards demand—applying a risk-based approach to its decision-making and saying “no” to some customers. A financial institution that refuses to do business with customers that present a risk profile that the institution cannot manage is doing the right thing. That is not “de-risking.” And it is not a problem. In fact, we have seen the termination of some customer relationships—as well as the threat of termination—spur jurisdictions and institutions to step up their AML/CFT practices... So, is ‘de-risking’ actually occurring? The evidence is decidedly mixed.”¹⁴¹

Acting Treasury Under Secretary Adam Szubin amplified this definitional concern most recently stating, “The term ‘de-risking’ has come to mean different things to different people, and is not consistently used by various stakeholders. We prefer to focus the term more precisely on what we view as problematic, which are reports of financial institutions indiscriminately terminating or restricting broad classes of customer relationships without a careful assessment of the risks and the tools available to manage and mitigate those risks” (emphasis added).¹⁴²

This view among policymakers and regulators—that FIs’ reviews and account closures are appropriate reassessments of risk—persists. In September 2016, Thomas Curry, Controller of the Currency, stated,

“...it is not surprising that some banks have chosen to reduce their risks and shrink their exposure and international business portfolios. That choice is the result of what has been pejoratively labeled ‘de-risking.’ These withdrawals, particularly in regions subject to terrorism, drug trafficking, and other illicit activity, have been the subject of a good deal of publicity and, in some cases, have caused outcry both here and abroad. The process that has resulted in these decisions is better described as risk reevaluation. It’s the process in which institutions review the risks they face on a continual basis and ensure they have systems in place that can identify and adequately address those risks. The actual process of regularly reevaluating risk is a critical and expected part of the BSA/AML regulatory regime.”¹⁴³

¹⁴¹ *Remarks by Under Secretary David Cohen at the ABA/ABA Money Laundering Enforcement Conference*, November 10, 2014, <https://www.treasury.gov/press-center/press-releases/Pages/jl2692.aspx>.

¹⁴² *Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference*, November 14, 2016, <https://www.treasury.gov/press-center/press-releases/Pages/jl0608.aspx>. U.S. policymakers generally characterize derisking in narrow terms, affecting entire categories of customers, products or business lines, or threatening the stability of the global financial system overall.

¹⁴³ *Remarks by Thomas J. Curry at the ACAMS 15th Annual AML and Financial Crime Conference*, September 28, 2016, <http://>

In conversations with U.S. officials, several specifically mentioned the low profitability of higher-risk accounts as a likely reason why many FIs may have chosen and continue to choose to exit business relationships.

Another point emphasized among some officials is a clear aversion to the use of the term “derisking.” In addition to being used in a pejorative way, interviewees noted misunderstandings as to what derisking is and is not. “It is not derisking if a financial institution cannot assure itself that they can effectively manage risks associated with specific clients. Certain clients, such as service NPOs operating in geographical areas of higher risk, require greater scrutiny and may therefore fall out of FI’s risk appetite, which is appropriate,” said one government representative.

Government officials also noted the difficulty of drawing conclusions from individual cases, as each case is unique. Some expressed doubt as to whether problems with financial access constitute a trend or are just reports of a series of individual cases.

Need for More Information/Data

In repeated discussions with government policymakers, Congressional staff and others, there was widespread realization of the need for data. Specifically referring to correspondent banking, Acting Under Secretary Adam Szubin noted that, “...even after these initial surveys, we don’t have a complete picture quite yet. We still need more and better data to help us measure changes in the correspondent banking environment, and to better understand the extent to which de-risking is happening and why.... We need sound, comprehensive data before deciding broad financial and regulatory policy.”¹⁴⁴

In interviews, there was tacit agreement on the need for more information regarding the nature of NPOs’ problems with financial access. Cautionary comments were also offered regarding “the difficulty of feeling comfortable with data on such complicated issues.” All agreed that the integrity of and confidence in the unbiased nature of the data is important.

Reaffirmation of the U.S. AML/CFT Approach

In both public statements and interviews, government officials reiterated the importance of the risk-based approach for effective AML/CFT implementation. In fact, officials claimed that the RBA was the cornerstone of U.S. policy for combatting illicit finance because it enables the government and FIs to focus efforts on those entities most at risk of terrorist abuse: “Our risk-based approach is a road map for financial institutions seeking to evaluate and manage risk, not an off-ramp for financial institutions seeking to avoid it. The key, at this point, is to help financial institutions navigate that road map.”¹⁴⁵

www.acamstoday.org/remarks-by-thomas-j-curry/.

144 *Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference*, November 16, 2015, <https://www.treasury.gov/press-center/press-releases/Pages/jl0275.aspx>.

145 *Ibid.*

Moreover, U.S. government officials have been clear that it is critical to “stay the course,” even if derisking may be the result of the current approach:

“We believe that we cannot address this complex issue by relaxing the prudential requirements that have made our financial system more stable or the AML/CFT rules that have made it safer. Rather, we must ensure that the global standards in place are well understood and implemented consistently and effectively, and in doing so we will enhance financial transparency and subsequently improve financial access.”¹⁴⁶

While reassuring Persian Gulf nations concerned about losing their banking relationships with the U.S., Treasury Assistant Secretary Daniel Glaser indicated in 2015 that despite “quiet calls in some circles for scaling back regulations and tamping down enforcement, we are not going to loosen laws or lower global standards, and we are not going to walk away from supervising our financial institutions or enforcing our laws.”¹⁴⁷

Furthermore, some regulators are sensitized to actions that could be perceived as “going easy” on banks. Through Senator Levin’s investigation into money laundering activities of HSBC, the OCC in particular came under harsh condemnation for showing too much deference to the financial institutions it regulates.¹⁴⁸ In general, government policymakers are concerned about potential criticism from Congress and the public for not being “tough enough” on banks in the aftermath of the 2008 financial crises.

Financial Access Is a Commercial, Not Policy, Decision

When asked about financial access problems, government officials have consistently indicated that closing customer accounts is a business decision of financial firms and that it is not the government’s place to interfere with banks’ assessment of risk. “Treasury cannot direct any bank to open or maintain a particular account or relationship—such decisions must be made by banks themselves,” according to U.S. Treasury’s Jennifer Fowler.¹⁴⁹ Acting Under Secretary Szubin reiterated this point recently by saying, “While the U.S. government cannot instruct the private sector on who to bank, we encourage you to continue to take the time and effort to assess your controls and the risks presented by individual clients and, where you cannot manage effectively that risk, make conscientious decisions.”¹⁵⁰

146 Szubin remarks, November 14, 2016.

147 Ian McKendry, “Treasury to Banks: Derisking Is Your Problem to Solve,” *American Banker*, November 13, 2015, <http://www.americanbanker.com/news/law-regulation/treasury-to-banks-de-risking-is-your-problem-to-solve-1077844-1.html>.

148 Report of the U.S. Senate Permanent Subcommittee on Investigations, of the Homeland Security and Governmental Affairs Committee, “U.S. Vulnerabilities to Money Laundering, Drugs, and Terrorist Financing: HSBC Case History,” released July 17, 2012, <http://www.hsgac.senate.gov/subcommittees/investigations/hearings/us-vulnerabilities-to-money-laundering-drugs-and-terrorist-financing-hsbc-case-history>.

149 Jennifer Fowler, “Treasury Efforts to Protect and Support the Charitable Sector,” Treasury Notes Blog, April 28, 2016, <https://www.treasury.gov/connect/blog/Pages/Treasury-Efforts-to-Protect-and-Support-the-Charitable-Sector.aspx>.

150 Szubin, remarks, November 14, 2016.

Exaggerated Concerns for Enforcement Actions

As previously mentioned, the significant and increasing penalties levied against FIs in recent years have been cited as reasons for their reduced risk appetite. U.S. regulators and policy officials have repeatedly emphasized that FIs should not be concerned with fines, since most enforcement actions are the result of willful and systematic failure to apply the rules:

“...about 95 percent of AML/CFT and sanctions compliance deficiencies identified by Federal Banking Agencies are resolved through cautionary letters or other guidance by the regulators to the institution’s management without the need for a public enforcement action or penalty. In addition, over 95 percent of OFAC sanctions investigations are closed with administrative actions that do not rise to the level of a monetary penalty or other public enforcement response. The rare cases of large monetary penalties or settlements for AML/CFT and sanctions violations have generally involved a sustained pattern of reckless or willful behavior over a period of multiple years and a failure by the banks’ senior management to respond to warning signs that their actions were illegal.”¹⁵¹

Strengthening Global AML-CFT

One of the oft-cited goals of U.S. policy is to encourage other countries to enhance their implementation of AML-CFT measures. American FIs’ reassessments of risks and decisions to terminate certain banking relationships, therefore, have had the positive impact of motivating some countries to enhance their own systems. In doing so, countries and financial institutions address deficiencies in their AML/CFT compliance and enforcement regimes, thereby strengthening the implementation of global system.

“There are often very real concerns about the risks presented by anti-money laundering and countering the financing of terrorism (AML/CFT) compliance. While ‘regulatory risk’ and fear of fines has been cited by some, the core issue here relates to poor and uneven implementation of global AML/CFT standards—either by individual foreign banks or by jurisdictions as a whole. The fact is that some countries lag in the effective implementation of global AML/CFT standards and have not taken the necessary steps to implement the proper legal, regulatory, and supervisory frameworks to adequately counter illicit finance.”¹⁵²

151 Ibid.

152 Ibid.

Acknowledgement of Derisking and Response¹⁵³

Over the past several years, there has been a growing recognition of the problems with financial access, especially in the correspondent banking sector. Several former U.S. government officials noted the seriousness of the derisking dilemma and the need to address it. Former Chairman of FDIC Bill Isaac blogged:

“This situation is creating extreme hardship for countries, organizations and people least able to cope with it.... We have moved from a system that was designed to track the movement of money to a system that is forcing money out of the legitimate banking system and into the shadows, where it is almost impossible to track.... It’s long past time for leading banks and government officials to stop blaming each other and sit down to work out common sense solutions. The solutions won’t be perfect—some funds may well escape the net—but there is no doubt we can do much better than we are doing today.”¹⁵⁴

Michael J. Bresnick, former executive director of President Obama’s Financial Fraud Enforcement Task Force, wrote, “Only when the government truly understands the consequences of its actions (especially the unintended consequences), acknowledges those concerns to those directly affected, and works closely with them to address the challenges they face, can we expect that the multitude of good actors who desperately want to avoid the last resort of de-risking will be able to do so with relative comfort.”¹⁵⁵

Beginning in late 2015, Treasury officials responsible for illicit finance began to acknowledge that certain sectors—correspondent banking and MSBs—are indeed experiencing difficulties in accessing financial services, even while reiterating the appropriateness of the RBA in addressing illicit finance risk on a client-by-client basis. Officials also noted that FIs are not infallible and that “none of this means zero tolerance, zero failure, or zero risk.”¹⁵⁶

In a September 2016 speech, Comptroller of the Currency Thomas Curry discussed the increase in derisking of foreign correspondent banks. After noting that stopping the financing of terrorists is important, he observed, “It cannot be our only goal. A banking system that’s truly safe and sound is also one that meets the legitimate needs of its customers and communities. Ensuring fair access to financial services while also combating threats to the system’s integrity is surely one of the great challenges that regulators and financial institutions face today.”¹⁵⁷

153 Recognition of the derisking problem has been limited to the correspondent banking and MSBs sectors; there have been no public statements addressing financial access problems of NPOs.

154 Bill Isaac, former chairman of the FDIC, comment post in response to Andrea Hall, “Bank De-Risking Hurts Charities and Increases Risk of Laundering,” *American Banker*, November 5, 2015, <https://www.americanbanker.com/opinion/bank-de-risking-hurts-charities-and-increases-risk-of-laundering>.

155 Michael J. Bresnick, “How Regulators Can Fight De-Risking,” *American Banker*, April 7, 2016, <http://www.americanbanker.com/bankthink/how-regulators-can-fight-de-risking-1080297-1.html>.

156 Szubin remarks, November 16, 2015.

157 *Remarks by Thomas J. Curry, Comptroller of the Currency, Before the Institute of International Bankers*, March 7, 2016, <https://www.occ.gov/news-issuances/speeches/2016/pub-speech-2016-25.pdf>.

Efforts to Clarify Regulatory Expectations

U.S. efforts to clarify regulatory expectations have taken place through the Financial Stability Board and the FATF.¹⁵⁸

In August 2016, several U.S. banking regulators issued a “Joint Fact Sheet on Foreign Correspondent Banking,” intended to dispel myths about U.S. supervisory expectations, including the belief that banks should conduct due diligence on the individual customers of foreign financial institutions (a practice referred to as “know your customer’s customer,” or KYCC).¹⁵⁹ For the first time, Treasury officials also penned an accompanying blog, *Complementary Goals – Protecting the Financial System from Abuse and Expanding Access to the Financial System*, providing additional guidance.¹⁶⁰

In October 2016, the OCC also issued guidance concerning expectations for banks to reevaluate risk in their foreign correspondent banking relationships but did not create any new supervisory expectations. Rather, it reiterates current expectations that banks assess these risks as part of their ongoing risk management and due-diligence practices and provides “best practices” for banks to consider when conducting their reevaluations.¹⁶¹

In addition to further regulatory guidance, U.S. officials’ statements have emphasized that the U.S. government “has never advocated a standard of perfection” since “it would promote neither efficiency nor transparency.”¹⁶² Moreover, Treasury officials have expressed a desire and willingness to work with the financial sector to address concerns, as “...we have a shared responsibility to expand access to the financial system while protecting it from illicit activity, and to ensure that our collective efforts result in a well-functioning, transparent, resilient, safe, and sound financial system.”¹⁶³

158 See FATF, *Guidance on Correspondent Banking*, October 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Correspondent-Banking-Services.pdf>; FATF, *Guidance for a Risk-Based Approach: Money or Value Transfer Systems*, February 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-RBA-money-value-transfer-services.pdf> and Financial Stability Board, “Report to the G20 on actions taken to assess and address the decline in correspondent banking,” November 6, 2015. www.fsb.org/wp-content/uploads/Correspondent-banking-report-to-G20-Summit.pdf.

159 See August 30, 2016, “Joint Fact Sheet on Foreign Correspondent Banking” by Treasury and regulators clarifying U.S. government’s approach to supervision and enforcement and describing expectations of U.S. regulators, the supervisory examination process, and the use of enforcement actions. U.S. Department of Treasury & Federal Banking Agencies, “Joint Fact Sheet on Foreign Correspondent Banking,” August 30, 2016, <https://www.treasury.gov/press-center/press-releases/Documents/Foreign%20Correspondent%20Banking%20Fact%20Sheet.pdf>. While characterized by the government as “clarifying” regulatory expectations, many FIs consulted viewed it as restatement of existing standards without providing any new guidance.

160 Nathan Sheets, Adam Szubin, and Amias Gerety, “Complementary Goals - Protecting the Financial System from Abuse and Expanding Access to the Financial System,” Treasury Blog, August 30, 2016, <https://www.treasury.gov/connect/blog/Pages/Complementary-Goals---Protecting-the-Financial-System-from-Abuse-and-Expanding-Access-to-the-Financial-System.aspx>.

161 See OCC BULLETIN 2016-32, *Risk Management Guidance on Periodic Risk Reevaluation of Foreign Correspondent Banking*, October 5, 2016, <https://www.occ.gov/news-issuances/bulletins/2016/bulletin-2016-32.html>.

162 Szubin remarks, November 16, 2015.

163 Szubin remarks, November 14, 2016.

Engagement with NPO Sector

As NPOs' problems have grown and they approached the U.S. government for help, officials' statements have emphasized recognition and support for the critical role charities play globally, especially in conflict regions. Treasury's Jennifer Fowler said, "We take seriously recent concerns from the charitable sector about delayed transactions to intended recipients and claims of indiscriminate bank account closures, the former of which seem to be more prevalent. We are committed to ongoing dialogue with relevant stakeholders on these issues."¹⁶⁴

As noted previously, the Treasury has conducted outreach to the nonprofit sector and organized meetings to facilitate a dialogue on banks' expectations. These sessions brought together representatives from charities, banks, financial supervisors and government to discuss issues that banks face regarding NPO accounts, including delays in financial transactions and banking access challenges.

In general, however, relations with the NPO sector have been challenging. "It hasn't been an easy relationship" is how one policymaker characterized the situation. Recognizing the frustration of many NPOs in not knowing why accounts have been closed or transfers denied, U.S. officials unfortunately are not in a position to be able to provide such information or remedy the situation. As they have repeatedly stated, the government cannot "tell banks what to do." NPOs have pushed back but have left dissatisfied and critical of informational sessions unable to move the dialogue forward. This has led to a general sense of frustration among all participants, including policymakers.

Importantly, the Treasury Department has emphasized that it "does not view the charitable sector as a whole as presenting a uniform or unacceptably high risk of money laundering, terrorist financing, or sanctions violations. However, charities delivering critical assistance in high-risk conflict zones have been, in some cases, exploited by terrorist organizations and their support networks. Protecting the charitable sector from terrorist abuse using a risk-based approach and promoting access to financial services are complementary goals that we all share."¹⁶⁵

Comments on NPO Issues

While recognizing the NPOs' frustrations when FIs give no reason or information related to account closures or transfer problems, government representatives expressed the view that most problems occur with smaller NPOs that are less sophisticated in dealing with regulatory and compliance requirements. They also noted that there are often conflicting accounts of financial access problems when NPOs and FIs are questioned. "When transactions are dissected, there are often differing stories, making it hard to get a straight answer," said one government representative. Government officials indicated that in querying FIs about NPO problems, banks' decisions seem to be thoughtful and specific to the relationship.

¹⁶⁴ Jennifer Fowler, "Treasury Efforts to Protect and Support the Charitable Sector," Treasury Notes Blog, April 28, 2016, <https://www.treasury.gov/connect/blog/Pages/Treasury-Efforts-to-Protect-and-Support-the-Charitable-Sector.aspx>.

¹⁶⁵ Ibid.

Based on discussions with FIs, officials also noted that most problems appear to be related to delays rather than account closures. They noted that delays usually get resolved and that a new account is often opened. Officials also expressed the view that most delays relate to questions or concerns from correspondent banks, not the originating U.S. institution.

When asked what NPOs need to do to address financial access problems, the response was that they needed to provide more information to FIs and be more transparent. “NPOs need to understand that they are no different than other customers—banks’ expectations and requests are the same as for any other customer,” government representatives said. U.S. government representatives also said that NPOs need to understand that they are not being singled out but that they do need to do more to demonstrate steps being taken to mitigate risk and implement compliance measures.

Other government officials remarked on the similarities of current financial access difficulties with the debanking of foreign missions in the aftermath of the Riggs Bank controversy. They noted the extreme difficulties many countries faced in losing banking services for routine payments of rents, salaries, etc. Only when the issue reached the highest levels of governments and became a crisis in bilateral relations were the matters addressed, and even then, not entirely satisfactorily or definitively.

Foreign Policy and Security Implications of Financial Access Problems

“NPOs are critical in reducing the appeal of terrorism, by building social structures and increasing intercommunity dialogue and understanding. These endeavors can prevent the causes of radical ideology from taking root.”

-U.N Counter-Terrorism Implementation Task Force

While the Treasury Department is the leading agency addressing FIs’ efforts to effectively manage customers, business lines and jurisdictional risks, agencies responsible for national security and counterterrorism are additionally affected by derisking. Foreign policy concerns in promoting global development, humanitarian assistance, financial inclusion and global finance, as well

as managing bilateral relations, are important aspects of the financial access dilemma. However, agencies representing these interests are generally not included in these discussions.

A number of interviewees commented on the implications of NPOs’ difficulties for foreign policy and security interests beyond AML/CFT. Several expressed concern for specific U.S. goals, such as supporting civil society and promoting international development. With the 2014 Presidential Memorandum on Civil Society, the Obama Administration committed to instituting a whole government approach to support civil society abroad, with NPOs playing an important role. Recognition of the significant constraints faced by civil society groups operating in increasingly restrictive environments have made it all the more important to support NPOs’ international engagement. Some governments have even used FATF R8 as a justification to crack down on civil society. Financial constraints on NPOs limit their ability to support American foreign policy objectives, including humanitarian assistance.

Some interviewees commented that the foreign policy aspects of financial access are underappreciated and underrepresented in U.S. government deliberations on the issue. Representatives of the State Department and the U.S. Agency for International Development expressed a desire for greater participation through a coordinating body such as the National Security Council, explaining that there are few opportunities to address financial access on a cross-cutting interagency basis. When it does occur, discussions are often country-specific, such as with transfers to Somalia or correspondent banking problems with Belize.

Representatives of security and counterterrorism agencies expressed concern that narrowing financial access for NPOs is an ineffective way to address AML/CFT concerns, potentially creating more problems than it would solve. Echoing views of the UN CTITF, interviewees noted that NPOs play a crucial part in fighting conditions conducive to terrorism. As stated in a 2009 report from the UN CTITF, “NPOs are critical in reducing the appeal of terrorism, by building social structures and increasing intercommunity dialogue and understanding. These endeavors can prevent the causes of radical ideology from taking root.”¹⁶⁶ Others noted the important role of some NPOs in helping to develop counter-narratives and providing positive alternatives for young people in countries where terrorists operate who might otherwise be drawn to violent extremist propaganda.

Even financial and regulatory policymakers have recognized the potential consequences of reduced financial access and its dangers for AML/CFT objectives. Discussing derisking, David Lewis, executive secretary of the FATF, noted that, “It’s a concern to us, as it undermines transparency within the financial sector and law enforcement’s ability to follow the money.... We are concerned about that, as it reduces transparency in financial transactions. It increases the ML/TF risks we are trying to address.”¹⁶⁷ Comptroller of the Currency Thomas Curry acknowledged the potential danger by noting that, “Transactions that would have taken place legally and transparently may be driven underground.”¹⁶⁸

166 UN Counter-Terrorism Implementation Task Force, “Tackling the Financing of Terrorism,” at 16, October 2009, http://www.un.org/en/terrorism/ctitf/pdfs/ctitf_financing_eng_final.pdf.

167 Mark Taylor, “FATF chief talks de-risking dangers and correspondent banking,” March 29, 2016, <https://www.linkedin.com/pulse/fatf-chief-talks-de-risking-dangers-correspondent-banking-mark-taylor>.

168 Rob Barry and Rachel Louise Ensign, “Losing Count: U.S. Terror Rules Drive Money Underground,” Wall Street Journal, March 30, 2016, <http://www.wsj.com/articles/losing-count-u-s-terror-rules-drive-money-underground-1459349211>.

Chapter 6

FINANCIAL INSTITUTIONS

*We are kind of in a Ping-Pong match between financial inclusion and avoiding regulatory scrutiny, and we are the ball.*¹⁶⁹

American financial institutions are largely privately owned, for-profit entities. While FI representatives interviewed for this report emphasized that they want to “do good,” they ultimately are bound by fiduciary responsibilities to maximize profits for shareholders.

In the 15 years since 9/11 and the maturation of the U.S. AML/CFT regime, there has been widespread recognition of the central role banks and financial institutions play in the fight to combat illicit finance. At times the relationship between FIs and the government has been contentious, as regulators propose new requirements that FIs view as unrealistic, excessive or too costly. But a fundamental element of the AML/CFT framework is the essential partnership and cooperation between these two groups.

Regulatory attention to and pressure on FIs increased significantly in the aftermath of the 2008 financial crisis. Negative media coverage and heightened attention by Congress and regulators created an environment in which compliance shortcomings contributed to perceptions of systemic problems in the financial sector, thereby eroding public trust. FIs acted to reduce their risk exposure and improve capital and liquidity positions. Regulatory oversight, criticized as lax prior to the meltdown, was significantly enhanced, and with it came unprecedented penalties and enforcement actions, as well as a negative attitude toward customer types viewed as high risk, such as NPOs.

At the same time, increased costs and record low interest rates coupled with severe penalties, fears of regulatory criticism and personal liability for compliance officers, have resulted in a “perfect storm” whereby FIs have reduced their risk appetite.¹⁷⁰ In the context of managing such risks, FIs increasingly must address whether it is more cost effective and less troublesome to step back from doing business in certain jurisdictions and sectors or with perceived high-risk customers— which includes NPOs.¹⁷¹ As former Treasury officials have characterized the current situation, “What

¹⁶⁹ Pamela Dearden, Managing Director for Financial Crimes Compliance at JP Morgan Chase, as cited in Ian McKendry, “Banks Face No-Win Scenario on AML De-risking,” *American Banker*, November 17, 2014, <http://www.americanbanker.com/news/law-regulation/banks-face-no-win-scenario-on-aml-de-risking-1071271-1.html>.

¹⁷⁰ David Artingstall, Nick Dove, John Howell, and Michael Levi, *Drivers & Impacts of Derisking: A Study of Representative Views and Data in the UK*, by John Howell & Co. Ltd. For the Financial Conduct Authority, February 2016, <https://www.fca.org.uk/publication/research/drivers-impacts-of-derisking.pdf>.

¹⁷¹ Sam Eastwood and Ian Michael Pegram, “The Risks of De-Risking: Conflicting Pressures on Financial Institutions,” Norton Rose Fulbright, May 2015, <http://www.nortonrosefulbright.com/knowledge/publications/129032/the-risks-of-de-risking-conflicting-pressures-on-financial-institutions>.

was designed as a regime to help law enforcement ‘follow the money’ has expanded to include a preventative web of sanctions and regulations used to deny rogue actors access to commercial and financial facilities. This evolution has placed enormous stress on the financial community to meet the expanding definitions of financial crime, complexities of sanctions regimes, and the heightened expectations of compliance. Billions of dollars in fines have been collectively levied against banks.... Institutions faced with expanding policy expectations are left with no choice but to de-risk or expend enormous resources to invest in the tools and personnel needed for compliance [...] These factors haven’t necessarily led to a more effective AML/CFT system.”¹⁷²

Generally, FIs are frustrated with being “caught in the middle,” trying to comply with regulatory expectations that vary, depending on the examiner, and being criticized for closing down accounts of well-meaning charities. As one representative said, “We can manage the risk and do a good job of it; we need not to be second-guessed and criticized for not knowing everything about every account.” FIs’ apprehension at being seen as too critical of regulators, as well as a fear of speaking out given the potential backlash of enhanced regulatory scrutiny, was also evident in numerous discussions.

Risk Management

Assessing and managing risk are key components of the banking industry. Traditional views of risk management hold that “risk is either accepted (as a possibility), or a probability that can be managed and mitigated. Total risk avoidance took the backseat.”¹⁷³ Regulatory attention and enforcement actions since 2008, however, have given rise to a “paradigm shift in the hierarchy of risk perception within banks.”¹⁷⁴

FIs face different kinds of risk: legal,¹⁷⁵ regulatory and jurisdictional¹⁷⁶ risk associated with AML/CFT sanctions compliance; financial risks entailing profitability and ensuring commercial viability; and reputational risk, especially important because loss of confidence and adverse publicity can destroy an institution. For many FIs, it is primarily the regulatory, compliance and reputational risks that have led to decisions to withdraw services or decline to provide financial services to certain customers and jurisdictions. At the same time, many FIs expressed the view that jurisdictional risk is preeminent; however sound an institution, or however low risk the customer base, the jurisdiction risk trumps everything else.

172 Juan C. Zarate and Chip Poncy, “Designing a New AML System,” Banking Perspectives, The Clearing House, <https://www.theclearinghouse.org/research/banking-perspectives/2016/2016-q3-banking-perspectives/a-new-aml-system>.

173 “British Bankers Association Roundtable on Financial Exclusion/Stability arising from financial crime related de-risking,” at 4, March 17, 2014, <http://www.caribbeanderisking.com/sites/default/files/BBA%20Report%20Roundtable%20on%20Derisking%20March%202014.pdf>.

174 Ibid.

175 Another complication for FIs doing business in sanctioned countries is fear of legal challenges, such as civil suits in the case of Arab Bank. One FI recited the months of effort to get money into Sudan blessed under OFAC licenses and exemptions to facilitate UN funds into the country. Ultimately the effort to set up a correspondent account with local bank was unsuccessful, in large part because of the fear of litigation by victims of terrorism under the Terrorism Risk Insurance Act (check). The threat of lawsuits from families of victims of terrorism and attempts to attach funds from terrorist countries (Syria, Sudan, Iran) have undercut policy decisions promoting financial access for NPOs providing humanitarian services.

176 The business will always be considered high risk if it is located in a higher-risk jurisdiction, such as countries subject to sanctions. See Chapter 3 for more detail.

As noted in Chapter 2 of this report, penalties and enforcement actions have increased significantly in recent years and have contributed to enhanced compliance risks for FIs and personnel. Government officials contend that large monetary penalties are the exception (only given for reckless or willful behavior), with 95% of AML/CFT sanctions compliance deficiencies resolved through cautionary letters or other guidance by regulators, short of a public enforcement penalty. However, FIs emphasize that these figures do not take into account the range of regulatory criticism and actions¹⁷⁷ for perceived programmatic weaknesses, even if there is no pattern of criminal activity. This has added substantially to regulatory risk and costs.¹⁷⁸

Inconsistent Examination Process

Regulators play a crucial role in examining, monitoring and enforcing FIs' compliance with a range of financial laws and policies. The risk-based approach adopted by FATF calls for each bank to establish its own system to assess and deal with AML/CFT risk. In practice, however, FIs indicate that regulators routinely second-guess their decisions and treat certain categories of clients as high risk, requiring financial institutions to undertake extensive (and expensive) steps to mitigate those risks.¹⁷⁹ As one FI characterized it, "The risk is more that we might not be able to answer all the questions a regulator might have about a particular client relationship.... That's more of what's driving derisking in many cases, more than the inherent riskiness of the client."¹⁸⁰ The result is increased due-diligence costs, which tips the risk/reward equation to the point where "it's just better for us to cut the account than to be second-guessed by a regulator."¹⁸¹

"Examiners have definitive opinions about what needs to be done, far beyond the Bank Examiners Manual, and they substitute their judgment for the judgment of FIs."

Difficulties associated with the examination process are common complaints from FIs. Surveys of compliance officials indicate that in the past 3 years, concerns of formal examination criticism by regulators increased by 50%.¹⁸² Regulators increasingly want

individual transaction analysis. One banker said, "Examiners will look at your activities and ask specific questions around control functions in place, challenging the amount of controls, significance of controls, and onward, beginning the downward spiral.... They scrutinize every transaction to understand the source/beneficiary of funds, purpose of transactions, and everything associated with the account. It's impossible to know all accounts in that level of detail and maintain a viable business." Another bank official noted that examiners have routinely asked for internal controls and written procedures for all high-risk accounts, including NPOs. "Examiners have definitive opinions about what needs to be done, far beyond the Bank Examiners Manual, and they

177 Such as MRA (matters requiring attention) and MRIA (matters requiring immediate action).

178 Paul Lee and Teresa Pesce, "Regulators Foster De-Risking More than They Admit," American Banker, February 10, 2016, <http://www.americanbanker.com/bankthink/regulators-foster-de-risking-more-than-they-admit-1079271-1.html>.

179 Dow Jones & ACAMS, "Global Anti-Money Laundering Survey Results 2016," http://files.acams.org/pdfs/2016/Dow_Jones_and_ACAMS_Global_Anti-Money_Laundering_Survey_Results_2016.pdf.

180 Staci Warden, "Framing the Issues: De-Risking and Its consequences for Global Commerce and the Financial System," Center for Financial Markets, at 4, July 2015, <http://www.milkeninstitute.org/publications/view/727>.

181 Ibid.

182 Dow Jones & ACAMS, "Global Anti-Money Laundering Survey Results 2016."

Numerous FIs emphasized that, “There is a clear disconnect between what policy officials say and what happens at the individual bank examination level, which is where we get hit.”

substitute their judgment for the judgment of FIs.” Banks feel that they are “at mercy of individual examiners” and complain about inconsistency between bank examiners. “[It] is hit and miss at best. It would be so nice to have one ‘opinion’ of the regulations rather than 5 or 6 differing opinions.”¹⁸³ As another FI

said, “We need balance and reasonableness, not suspicion [...] Contrary to the regulators, bankers are not redlining or deceiving their customers. One bad apple does not mean all bankers should get hit with the same broad brush.”¹⁸⁴

Numerous FIs emphasized that, “There is a clear disconnect between what policy officials say and what happens at the individual bank examination level, which is where we get hit.” Some participants expressed their belief that guidance from government agencies is not helpful because bank examiners have wide latitude. “Guidance is not doing anything for anyone. Even when views at the top change, it’s not applied by examiners in the field, it’s not trickling down.”

FIs are increasingly concerned that examiners are able to say and do whatever they want without repercussions in DC. Indeed, there seems to be little to no accountability at the examiner level, and in a risk-adverse system, there is little incentive for individual examiners to take a balanced approach. Some FIs expressed the view that they would prefer to have clear detailed guidance (a rules-based approach) with a predictable examination/assessment framework that would make it clear with whom they can and cannot bank.

Technology Tools

To lower the cost of compliance, the financial sector is increasingly looking to new technological services, utilities and information-sharing tools that can be used to screen transactions (see box, next page).

¹⁸³ Comment submitted by username “Common Sense” to article on American Banker’s Bank Think blog, “The Time Has (Finally) Come for a Single Regulator” by Robert Heller, December 7, 2016.

¹⁸⁴ Ibid., from username “TooManyRegs.”

TECHNOLOGY TOOLS FOR COMPLIANCE CHALLENGES

With ever-increasing expectations from regulators to comply with the range of federal and state banking requirements, FIs have turned to technology to assist in managing compliance functions. Increasingly common are know-your-customer (KYC) utilities: third-party services intended to reduce costs and administrative burdens associated with KYC rules. A spectrum of KYC utilities now exists to help FIs in onboarding clients while adhering to AML/CFT requirements. KYC utilities generally take client information from FIs, including ownership structure, legal entities, management and board members, and enhance this with data from public/private sources to construct a detailed client profile. On the plus side, utilities can save money, improve the review process and make it more efficient.¹⁸⁵ Popular KYC utilities include Depository Trust & Clearing Corp.'s Clariant Global, Markit/Genpact's kyc.com, Thomson Reuters' World-Check and Org ID, and SWIFT's KYC Registry.¹⁸⁶ However, many of the private utilities have come under increased scrutiny for including unreliable information, which leads to more derisking.

Further reflecting FIs' needs for compliance-related technological solutions, in September 2016, SWIFT launched a "name screening" service for FIs to screen clients, suppliers or employees against sanctions, politically exposed persons (PEPs) and private lists. It is an online search engine-style directory of individual names, as well as an automated batch screening of entire databases to bolster (especially small to midsize FIs') compliance in higher-risk areas. SWIFT offers other compliance services such as "sanctions testing" that allows banks to test, tune and certify the efficiency and performance of their transactions, name screening filters and lists.

It is not uncommon for negative anecdotal information to turn up as part of electronic screening. These databases often compile press accounts or unconfirmed information from the Internet, such as mentions on blogs, for inclusion in their lists. This means that innocent people and organizations might find themselves in these databases.¹⁸⁷ For example, more than one FI reported receiving an adverse publicity flag related to old information or solely because the name of an organization is mentioned in the same location as a sanctioned party (such as both attending the same conference). In one instance, information posted on the Internet when an individual was very young resulted not only in the transaction being denied but in a Suspicious Activity Report being filed. Even though compliance officers may recognize that information is unsubstantiated and likely incorrect, once it comes up, it cannot be ignored without significant complication. An FI must explain, if asked by an examiner, why it proceeded in the face of adverse information indicating risk.

¹⁸⁵ Paige Long, "Banks say take-up of KYC utilities needs to improve," Risk.net, December 11, 2015, <http://www.risk.net/operational-risk-and-regulation/news/2438944/banks-say-take-up-of-kyc-utilities-needs-to-improve>.

¹⁸⁶ Chris Kentouris, "KYC Utilities: How Many Is Too Many?" FinOps Report, April 16, 2015, <http://finops.co/regulations/kyc-utilities-how-many-is-too-many/>.

¹⁸⁷ Namir Shabibi and Ben Bryant, "VICE News Reveals the Terrorism Blacklist Secretly Wielding Power over the Lives of Millions," VICE News, February 4, 2016, <https://news.vice.com/article/vice-news-reveals-the-terrorism-blacklist-secretly-wielding-power-over-the-lives-of-millions>.

Response to U.S. Government Efforts to Clarify Policies

For more than a decade, FIs have consistently been told to reduce their exposure to risk. When dealing with higher-risk categories of customers, stronger risk management and controls are required to exercise effective due diligence. Around 2014, when the effects of derisking had become more evident, however, policymakers began arguing that exiting certain sectors of business, such as NPOs, MSBs, or higher-risk countries, are inconsistent with a risk-based approach. FIs are keenly aware of these conflicting signals and inconsistent messages.

“Bankers are finding themselves trapped between the proverbial rock and a hard place when it comes to complying with anti-money laundering rules. On the one hand, they are facing enhanced scrutiny from bank examiners, causing them to sever ties with businesses they view as high-risk, including online lenders and money services businesses. On the other, top officials at those same regulators are urging banks not to close those accounts, fearing that doing so will cut off vulnerable consumers from much-needed access to credit.”¹⁸⁸

Some of the same pronouncements by Administration officials contain contradictory statements and express skepticism that derisking is in fact taking place. It is therefore not surprising that while banks have heard these messages, there is little clarity or guidance that banks feel they can rely upon in making decisions.

In discussions with FIs, they expressed the need for clear and specific expectations (as opposed to a restatement of existing policies). Policymakers and supervisors need to enact specific reforms, FIs said.

FIs expressed frustration that policymakers and regulators appear to couch FI actions to exit certain customer relationships in terms of the FIs’ concern for their bottom line rather than enhanced regulation and enforcement. Some financial representatives

feel “left in the lurch” to deal with the financial access problems, which they believe were created by government policies.

Attempts to clarify AML/CFT requirements and provide assurances to FIs (in guidance issued in August and October 2016 regarding supervisory and enforcement expectations) have been insufficient to address the financial sector’s concerns. The most recent guidance and various statements by the Treasury claiming that they do not expect perfection have not provided the assurances necessary to tip the balance in favor of banking higher-risk customers or countries.

In discussions with FIs, they expressed the need for clear and specific expectations (as opposed to a restatement of existing policies). Policymakers and supervisors need to enact specific reforms, FIs said.

Officials from the Treasury Department and other agencies have expressed concern about derisking, recognizing that it can hurt economically disadvantaged consumers, but when asked

¹⁸⁸ Ian McKendry, “Banks Face No-Win Scenario on AML ‘De-Risking.’”

about solutions, they generally put the onus on FIs to address derisking, rather than discuss the heightened fear of enforcement penalties that banks say is the reason behind the problem. According to former Treasury Under Secretary Nathan Sheets, “Fear of such penalties should not color the decision-making approach of banks that are carrying out good-faith efforts to abide by the law, maintain strong [anti-money-laundering] standards, and invest in the personnel and technology necessary to implement these standards.”¹⁸⁹

Moreover, U.S. government proposals for FIs to solve the derisking problems alone are viewed as counterproductive. John Byrne, executive vice president at ACAMS, warned, “If policy leaders in the government continue to talk about derisking as solely an obligation of the financial sector to improve processes [...] it will never get solved [...] There has to be a concerted effort with regulators, law enforcement, and the financial sector to candidly discuss risk issues, because it is all about risk appetite, risk management, risk assessment.”¹⁹⁰

Potential Measures to Address Uncertainty

When asked what can be done to address the decline in financial services for certain sectors and jurisdictions, FIs emphasized that the problem is a shared responsibility, not just one confronting banks.

“Efforts to address the so-called ‘de-risking’ phenomenon and the attendant risks to the safe and efficient functioning of the correspondent banking system should reflect the mutual and joint responsibility of the public and private sectors to mitigate the risk that bad actors will access the financial system.... We believe it is crucial that governments and supervisors enact concrete reforms...”¹⁹¹

Moreover, FIs state that measures need to be realistic about the risks inherent in banking and need to afford flexibility to FIs.

“To the extent that such de-risking conflicts with other public policy incentives, such as humanitarian aid, financial inclusion or keeping financial flows in regulated systems, policy makers need to acknowledge that continuing certain relationships to meet these other objectives will necessarily expose banks to certain risks and [need to] provide banks (i) flexibility to manage those risks within the current regulatory architecture and (ii) comfort that their risk management efforts will be evaluated by supervisors according to the principles of the risk-based framework.”¹⁹²

189 Ian McKendry, “Treasury to Banks: Derisking Is Your Problem to Solve,” *American Banker*, November 13, 2015, <http://www.americanbanker.com/news/law-regulation/treasury-to-banks-de-risking-is-your-problem-to-solve-1077844-1.html>

190 Ibid.

191 Letter to Robert Lindley, CPMI Secretariat, from The Clearing House, “Comments in Response to Consultative Report—Correspondent Banking,” at 2, December 7, 2015, <https://www.theclearinghouse.org/-/media/action%20line/documents/volume%20vi/20151207%20tch%20bis%20correspondent%20banking%20comment%20letter.pdf>.

192 Ibid.

Several FIs shared their suggestions on how to address derisking problems, including information-sharing tools and utilities, incentives to encourage FIs to bank higher-risk sectors and jurisdictions, penalties for derisking, safe haven provisions and changes in the management of the examination process to ensure a more consistent approach to supervision. Some representatives suggested the creation of a centralized utility containing all relevant data that could be responsible for monitoring all transactions, removing the liability burden from individual banks. These are explored further in Chapter 9.

FIs also expressed the need for greater and more consistent guidance from governments and regulators. In a 2014 KPMG survey,¹⁹³ 63% of FIs said that regulators should provide additional guidance and 43% indicated that a stronger relationship with regulators would be a welcomed change. Regulators should discuss and clarify the roles and responsibilities of various stakeholders in exercising AML/CFT due diligence and ensure that changes in the framework (such as the revised FATF R8) are translated into guidance for FIs.

FIs' Relationship with NPO Sector

As noted in Chapter 4, half of NPOs are small, operating with less than \$1.5 million in revenues and less than \$1 million in expenditures, making many NPO accounts relatively small compared to corporate and other clients. Given, therefore, that charities' accounts are generally not hugely profitable but do require additional compliance costs, many FIs find them to be "more trouble than they are worth."¹⁹⁴ Indeed, as this report has shown, even with the change of FATF R8, FIs still consider NPOs to be high risk, especially because they often operate in higher-risk jurisdictions (such as countries that are subject to sanctions). The specific activities or due-diligence procedures of NPOs are often not even considered; rather, FIs anticipated the reactions of regulators to NPO accounts.

Several FIs noted unfamiliarity generally regarding how the NPO sector operates and the specific nature of NPO work. The degree to which there is little awareness of what and how NPOs function is not surprising, as there is not widespread understanding of the unique circumstances of delivering humanitarian relief, something most FIs have no expertise with.

¹⁹³ KPMG, Global Anti-Money Laundering Survey 2014, <https://assets.kpmg.com/content/dam/kpmg/pdf/2014/02/global-anti-money-laundering-survey-v5.pdf>.

¹⁹⁴ Ironically, some NPOs have divided their funds over multiple accounts because of the fear of being debanked, making their accounts less profitable for FIs.

ARE NPOs “AUTOMATICALLY HIGH RISK?”

One FI relayed the experience of an examiner telling the bank it needed to exit areas of higher risk, followed by extremely detailed questions concerning an NPO customer. This left the bank officials with the unmistakable message that the NPO was high risk and to be avoided.

Another bank noted that charities were automatically placed in the high-risk category, even though it was known that FATF was proposing a revision of Recommendation 8 to downgrade the risk associated with NPOs generally. The representative stated that until there was guidance from regulators changing the long-standing characterization of NPOs as high risk, the FI would continue to view all NPOs as such.¹⁹⁵

Multiple interviewees also mentioned an implicit attitude by policymakers and regulators of NPOs as “uncertain,” risky, and whose problems are not generally regarded as a priority concern in the same way correspondent banks and MSBs have been acknowledged publicly. A general sense of cautiousness and skepticism seemed to pervade officials’ characterizations of NPOs.

According to some NPOs, “The bankers told us that you never get punished for derisking, but you potentially can suffer significant penalties for keeping charitable organizations around. On the policy level, Treasury representatives indicated that there is no pressure to debank charitable organizations. But something seems to get lost in translation between bank regulators and instructions to banks themselves. Banks will tell us that they’re maintaining charitable accounts, but that they’re being punished for it. Financial institutions are being sanctioned by regulators (letters indicating noncompliance) for working with charitable groups.”

¹⁹⁵ This interview took place prior to the June 2016 decision by the FATF to revise Rec 8; no guidance to implement the change has been issued by the U.S. government.

NPOs also consistently complain about the lack of information and transparency surrounding account closures or cancelled wire transfers. From the FI’s perspective, however, there are concerns about running afoul of prohibitions on “tipping off” the client if adverse information is revealed in KYC checks. Other times, NPOs’ attempts to ward off derisking lead to the very same problem they are trying to avoid. One interviewee told of a situation in which a bank exited an NPO relationship because law enforcement served a subpoena on a specific account (noting patterns of cash deposits that were not viewed as commensurate with expected charity accounts). The reason for the irregular activity stemmed from the fact the NPO had multiple accounts in different banks—an effort to guard against debanking. Because the AML staff did not have any contact with the charity, standing policy dictated that the FI close the account.

What FIs Need from NPOs

For FIs to carry out their due-diligence obligations, certain information is necessary to assess the client’s level of sophistication in managing terrorist financing/financial crime risks. While each bank has unique criteria it requires in deciding whether to accept or retain customers, there are general categories of information FIs need to make determinations and to process payments to higher-risk jurisdictions.¹⁹⁶

In interviews with FIs, the question was repeatedly asked, what do banks need from NPOs in order to confidently provide financial services? The most frequent response from FIs was that NPOs need to be more transparent and help banks understand internal due diligence and audit processes to demonstrate where funds are going.

The High Cost of One Successful FI-NPO Relationship

One bank representative recounted the specific challenges experienced in onboarding a charity client. The organization’s principal source of income was sizable cash donations from worship services. The FI worked with the NPO to design a program to understand its unique operational circumstances, established good lines of communication, conducted site visits and assisted the NPO with extensive due-diligence procedures on the ground so the bank was comfortable that the risk associated with cash could be managed. The monthly process of monitoring deposits at multiple sites, accounting for where cash was coming from, making annual site visits and maintaining a continued dialogue to inform the NPO what it could/could not do and why was “ridiculously labor intensive.” Everyone had to understand all aspects of the business, including the ultimate use of the funds. It was a success story, but not replicable unless the relationship is significant enough to support the cost of compliance. “If the business was tiny, it would not be derisking, but rather common sense,” the FI explained.

¹⁹⁶ Definitions of higher-risk or “hotspot” jurisdictions vary, but usually include, at a minimum, countries to which sanctions apply.

INFORMATION FIs SAY THEY NEED TO BANK NPOs

In assessing risk associated with NPOs, FIs consider a variety of factors. The following are broad areas of information that most banks want to understand in order to support client activities, especially in higher-risk jurisdictions:

- 1) General information on the nonprofit organization – size, types of activities/services provided, jurisdictions in which NPO operates, background of trustees/directors.
- 2) Financial controls – internal NPO policies and procedures to manage TF/financial crime risk, including responsibility for review and approval, transparency regarding sources of donations and disbursement of funds to beneficiaries, procedures to prevent diversion and misuse, reporting and auditing.¹⁹⁷
- 3) Due diligence – procedures used to select beneficiaries, in-country partners and agents (employees, suppliers and other service providers), and to monitor and manage downstream risks.
- 4) Compliance – appropriate steps taken to ensure compliance with AML/CFT and sanctions regulations. Additional measures taken to comply with U.S., UN, EU and other sanctions and export control requirements in higher-risk jurisdictions.
- 5) Humanitarian aid – detailed descriptions of projects (especially in conflict zones), funding for projects and, if government-funded, how projects are subject to auditing and evaluation requirements.

This information is used by the FI to assess the overall relationship of specific NPO projects, enabling a more detailed understanding of the anticipated payment flows and where the NPO controls may need to be strengthened. FIs emphasized that more information made available at the early phases of the relationship enables more expeditious review and provision of financial services.

¹⁹⁷ Some FIs limit use of MSBs to those that are regulated, and restrict cash disbursements.

Chapter 7

NONPROFIT ORGANIZATIONS

*"Our inability to transfer funds in support of our programs is a growing crisis among American NPOs, threatening the lives of beneficiaries and our continued ability to function as humanitarian organizations."*¹⁹⁸

NPOs¹⁹⁹ are "...organization[s] that primarily engage 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.'"²⁰⁰ As mission-oriented entities dedicated to particular social benefit projects, NPOs utilize revenues to further their missions (as distinct from for-profit entities, which maximize and distribute income to shareholders) and often work in challenging, conflict-ridden environments. For all NPOs with a presence in foreign countries, the ability to transfer funds via the formal financial system is crucial to carrying out their operations.

The following section, drawn heavily from focus groups and interviews conducted for this study, addresses general views of the NPO sector, misperceptions and misunderstandings NPOs find that other stakeholders have about them, specific problems NPOs have experienced in accessing the financial sector and responses to address obstacles to financial access.

Overview of the U.S. Charitable Sector and Global Need

There are approximately 1.4 million public charities recognized by the IRS, along with an additional 300,000 small charities or houses of worship that are not required to file for recognition of their tax-exempt status with the IRS.²⁰¹ The number of charities that include international activities in their annual reports to the IRS is small but growing. In 2006, the Center on Nonprofits and Philanthropy found that nearly 5,600 organizations work in the international arena.²⁰² The research for this report identified 8,665 such organizations (see Chapter 4).

¹⁹⁸ Stakeholder interviewee, a representative of a U.S.-based NPO.

¹⁹⁹ As noted previously, charities and NPOs are often used interchangeably, but the NPO sector is larger and more diverse, including human rights groups and funds, foundations, faith-based and secular organizations, hospital and health providers, colleges and universities and cultural and professional associations, among other organizations.

²⁰⁰ FATF definition of NPO. FATF, Best Practices: Combatting the Abuse of Non-Profit Organisations (Recommendation 8), at 7, June 2015, <http://www.fatf-gafi.org/media/fatf/documents/reports/BPP-combating-abuse-non-profit-organisations.pdf>.

²⁰¹ Financial Action Task Force & Asia/Pacific Group on Money Laundering, "United States Mutual Evaluation: Anti-Money Laundering and Counter-Terrorist Financing Measures," at 103, December 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-United-States-2016.pdf>.

²⁰² Elizabeth J. Reid and Janelle A. Kerlin, "The International Charitable Nonprofit Subsector in the United States: International Understanding, International Development and Assistance, and International Affairs," The Urban Institute Center on Nonprofits and Philanthropy, at 7, January 2006, <http://www.urban.org/sites/default/files/alfresco/publication-pdfs/411276-The-International-Charitable-Nonprofit-Subsector-in-the-United-States.PDF>.

U.S. public charities working in foreign countries include major international non-governmental organizations, human rights groups and funds, friendship societies, foundations, faith-based and secular organizations, environmental groups, museums, hospital and health providers, colleges and universities, cultural and professional associations and a variety of other organizations and charities. These groups carry out their work through staff based in field offices outside the U.S. or through financial support to partner organizations or grantees that implement programs.

In 2015, total U.S. charitable giving reached an estimated \$373.25 billion, achieving an all-time high for the second consecutive year.²⁰³ Donations for the international subsector made up about 4% of all donations in 2015, an increase from the previous year. Online giving is an important element of this funding stream, particularly in times of urgent need. In the 2016 “Luminate Online Benchmark Report” from Blackbaud, a nonprofit consulting firm, they found that disaster relief donations averaged \$121.01, an increase from the previous year.²⁰⁴ The international subsector of U.S. nonprofits is likely to continue to grow, making it increasingly important that access to regulated financial channels be protected.²⁰⁵

Escalating humanitarian crises around the world increase the urgent need for NPOs’ international work, particularly humanitarian relief. The scale of humanitarian need is staggering. According to the incoming UN Secretary-General, “When I started as High Commissioner 10 years ago, there were 38 million people in the world displaced by conflict and persecution.... Today, there are more than 60 million refugees, asylum-seekers and internally displaced persons worldwide as a result of conflict and persecution.”²⁰⁶

Beyond these escalating humanitarian crises, NPOs face enormous practical difficulties operating in conflict zones that put employees at risk. InterAction, the largest association of U.S. international NGOs,²⁰⁷ argues that, “Over the past 20 years, the operational environment of NGOs has become increasingly dangerous. Serious incidents—killings, kidnappings, or attacks that cause serious injuries—are on the rise, as are politically-motivated attacks against NGO staff.”²⁰⁸

203 Giving USA, New Giving Record Is More Than a Number, June 14, 2016, <https://trust.guidestar.org/new-giving-record-is-more-than-a-number>.

204 Blackbaud, Luminate Online Benchmark Report 2015, at 42, <http://luminatebenchmarkreport.com/LuminateBenchmarkReport2015-R.pdf>.

205 On September 15, 2015, the UN General Assembly ratified the 2030 Agenda for Sustainable Development, adopting 17 Sustainable Development Goals (SDGs) and 169 targets toward a “plan of action for people, planet, and prosperity.” These benchmarks are meant to focus on and drive the international development agenda for the next 15 years. SDGs include a greater role for philanthropy and nonprofit organizations, highlighting the importance of both the funding capacity and expertise of philanthropic institutions.

206 Opening remarks at the 66th session of the Executive Committee of the High Commissioner’s Programme by António Guterres, United Nations High Commissioner for Refugees: Geneva, October 5, 2015, <http://www.unhcr.org/56122bd76.html>.

207 “Nongovernmental organizations” are generally considered to be a subset of organizations within the nonprofit sector that provide human services.

208 Interaction, NGO Security: Overview, <https://www.interaction.org/project/ngo-security/overview>.

NPOs Support AML/CFT Policies but Are Frustrated with Lack of Action to Address Narrowing Financial Access

Throughout the study's engagement with numerous NPOs, conversations consistently began with the same point: an understanding of the important security concerns that the U.S. government and financial institutions are promoting. At no time did interviewees express anything less than full support for the objectives underlying U.S. AML/CFT or sanction policies that have resulted in enhanced scrutiny by FIs. In fact, NPOs underscored that when operating in conflict zones, they are directly at risk of terrorist activities and want to do everything possible to protect their employees, beneficiaries and programs. While trying to ensure that both they and their partners fully comply with U.S. law, NPOs noted that working toward legal compliance creates tensions with the principles that underlie their stated missions.²⁰⁹ NPOs are frustrated by the increasing difficulties they have encountered in trying to access financial services to support their programs abroad.

“Nonprofit groups repeatedly underscored their willingness to work together with FIs to ensure that compliance requirements are addressed.”

Many NPOs expressed the view, however, that banks seem increasingly reluctant to work with them. Because of the pervasive view that the nonprofit sector is high risk and low profit, FIs tend to require additional,

labor-intensive due diligence and seem less than desirous of taking on NPOs as clients. There was also a feeling that FIs are “trigger-happy” in terms of looking for opportunities or excuses to end relationships with NPOs rather than finding ways to make them work. By the time NPOs are informed of questions or issues, FIs have often already made decisions to deny transfers or close accounts. This results in delays and complications for achieving the NPOs' missions. Rarely are NPOs given any information concerning the reasons accounts are terminated or not opened or wire transfers are delayed. Many NPOs expressed concern that their business was not valued, likely because it is not large or lucrative enough.

NPOs Are Not Valued Customers

In one case, as part of an NPO's annual KYC review with its bank, the FI asked for an extraordinary amount of invasive information for all 30 members of the large international NPO's board, in large part because the account was auto-flagged as high risk. The demand departed from previous practices in which data was only requested for certain foreign nationals. In the process of discussing the request, however, the FI indicated that there was no flexibility because the branch was being audited, and abruptly notified the long-standing customer that its account would be closed in 30 days. NPO staff appealed to their relationship manager, asking what could be done to make the relationship more lucrative for the FI, but the response was that the compliance department's decision to terminate the relationship was final.

²⁰⁹ International humanitarian law is based on the basic principles of humanity, impartiality, neutrality and independence. International Committee of the Red Cross, What is International Humanitarian Law? July 2004, https://www.icrc.org/eng/assets/files/other/what_is_ihl.pdf.

A significant frustration of NPOs is the absence of sustained meaningful engagement and solution-oriented responses to the financial access issues raised. NPOs reported that officials seemed to lack an appreciation or understanding of the essential humanitarian and development benefits that the charitable sector provides and seemed to have a general lack of interest in addressing problems raised.

Finally, there was a palpable sense of apprehension among many NPOs interviewed. Most organizations preferred to discuss experiences on a non-attribution basis, fearing reputational damage if they were “on the record” talking about the difficulties they have encountered. Hesitation to disclose problems that might encourage government scrutiny and have a chilling effect on donors was also evident. Some even feared for potential reprisal they might incur for appearing to criticize U.S. policies and officials. These qualms were most disconcerting to the research team.

(Mis)perceptions and Misunderstanding of NPOs

Discussions with other stakeholders confirmed that there are numerous mistaken impressions surrounding the nonprofit sector. The following perceptions and attitudes are among the most prevalent that NPOs routinely face and strive to overcome.

Perception of NPOs as Inherently Risky

In the immediate aftermath of 9/11, NPOs came under intense scrutiny as potential sources of terrorist financing, beginning what has been a difficult, and at times overtly contentious, relationship with the U.S. government. NPOs contend that the less-than-complete information regarding NPOs’ risk of terrorist financing helped to create an overall perception of NPOs as especially risky. This was exacerbated by FATF’s original recommendation enshrining the notion of nonprofits as “particularly vulnerable” to abuse. This notion has persisted and has been reinforced over time, leaving NPOs struggling to overcome the associated stigma.²¹⁰

NPOs consider this depiction to be unwarranted and inaccurate, tainting an entire sector with suspicion and failing to acknowledge the important and positive humanitarian, social, educational and medical activities that provide vital assistance to millions of people in need. The characterization of NPOs as “high-risk” organizations, regardless of the good work charitable groups provide, continues even after it has become clear that NPOs are not a significant source of terrorist financing.²¹¹ Although FATF removed the “particularly vulnerable” language in June 2016, there has been no subsequent guidance from the U.S. government to encourage FIs to update their risk assessments of NPOs.

210 See OMB Watch and Grantmakers Without Borders, *Collateral Damage: How the War on Terror Hurts Charities, Foundations, and the People They Serve*, July 2008, <http://www.ombwatch.org/sites/default/files/npadv/PDF/collateraldamage.pdf>.

211 Emile van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing: A Proportionate Response,” 2010, <https://openknowledge.worldbank.org/handle/10986/5926>; FATF, *International Standards on Combatting Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations*, updated October 2016, http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf.

Unfamiliarity with NPO Business Model

NPOs report that FIs reviewing financial transactions come back to NPOs frequently, asking basic questions such as “What is humanitarian relief?” This indicates a general lack of understanding on the part of banks as to the nature of NPO work. This low level of awareness is not surprising—nonprofit work uses an entirely different business model than commercial accounts. Nonprofits work where the market systems fail: when other entities cannot make a profit while meeting a community’s needs. Whether it is providing development assistance, access to education or food and medical care in the aftermath of disasters and war, most NPOs rely on donations to support core operations that would not prove profitable in a market context. NPOs exist to sustain those activities.²¹²

The unique mission-driven norms that govern NPOs’ work, especially those providing humanitarian and emergency relief, are also not widely appreciated by either the government or FIs. Established principles governing humanitarian assistance—*independence, impartiality and neutrality*—are not commonplace in a private-sector business model. Coupled with this is the fact that many groups routinely operate in areas of conflict, entailing significant risk to staff, beneficiaries and operations. As a result, many international humanitarian NPOs have developed comprehensive risk management frameworks to enable effective programming while protecting their staff, operations and reputations. Even so, NPOs understand and accept that risk cannot be completely eliminated. There will always be residual risk that must be managed and mitigated to avoid negative consequences. This residual risk is acceptable in light of the benefit that NPOs provide.²¹³ It is also consistent with the risk-based approach. However, the risk calculations used by NPOs may not easily translate into financial risk analysis approaches, because NPOs include the cost of inaction in their analysis and may choose to accept risk to their staff and operations if it can address risks faced by civilians in need of humanitarian aid.

Unique Operational Challenges

NPOs that work in foreign countries face many challenges, from operating in war or disaster zones to being targets of repressive regimes. International NPOs routinely function amid heightened risk, especially in countries such as Afghanistan, Central African Republic, Iraq, Syria, Somalia, South Sudan and Yemen. These conflict-driven emergencies, with highly politicized dimensions, tend to involve multiple risks, including the potential for violence against personnel, accidents, corruption, diversion, program failure and other negative outcomes.²¹⁴ Challenges are greatest for NPOs working in areas in which terrorist organizations such as ISIL, al-Qaeda, Boko Harm and Hezbollah operate. These are often the areas where humanitarian need is greatest.²¹⁵

212 Allen J. Proctor, “Linking Mission to Money: A “Dual-Business” Model for Nonprofit Sustainability,” Georgia Center for Nonprofits, <http://www.gcn.org/articles/Linking-Mission-to-Money-A-%E2%80%9CDual-Business%E2%80%9D-Model-for-Nonprofit-Sustainability>.

213 Humanitarian Outcomes for Interaction, “Residual Risk Acceptance: An Advocacy Guidance Note,” September 2016, https://www.humanitarianoutcomes.org/sites/default/files/residual_risk_advocacy_guidance_note.pdf.

214 Ibid.; Humanitarian Outcomes and Interaction, “NGOs and Risk: How international humanitarian actors manage uncertainty,” February 2016, https://www.humanitarianoutcomes.org/sites/default/files/ngo-risk_report.pdf.

215 See Listed Terrorist Groups and Humanitarian Crises, Charity & Security Network website interactive map, <http://www.chari->

NPOs themselves have the most to lose if problems arise, with significant ramifications in terms of donor funding, access to financial services and the risk of civil or criminal penalties.

Moreover, sending money into conflict zones presents particular challenges, as in most cases there will be a minimal banking system to receive funds. The inability for direct line payments poses significant complications for compliance systems based on

transparency and a risk-based approach. FIs often feel they are left with no option but to decline transactions, given the absence of shared views on appropriate risk management. The lack of direct bank-to-bank channels, and therefore increased reliance on unregulated informal channels, raises specific challenges that require greater analysis and guidance.

In these environments, the armed groups exercising territorial control may impose registration fees or taxation on NPOs or dictate the conditions on which NPOs might gain access to civilian populations. In such cases, humanitarian actors may need to engage in customary, necessary and incidental transactions with listed entities as the governing power. Complex situations need to be recognized and managed, even when there may be unintended or incidental contributions to sanctioned groups.

Due Diligence and Effective Controls

NPOs generally undertake considerable efforts to protect themselves from potential terrorist abuse, instituting internal controls and due-diligence procedures. Before interviewing potential partners, some NPOs undertake compliance checks at multiple levels, which often are shared with their banks. Recipients of NPO funds, including vendors, are screened against sanction lists. Humanitarian organizations have developed internal policies and practices in line with humanitarian principles to help ensure that aid and assistance reaches the intended beneficiaries. NPOs receiving USAID funds engage in a formal vetting program. Donors are increasingly requiring NPOs to sign clauses in grant and partnership agreements requiring implementation of specific anti-bribery, anti-fraud and anti-terrorism-financing policies.²¹⁶ NPOs themselves have the most to lose if problems arise, with significant ramifications in terms of donor funding, access to financial services and the risk of civil or criminal penalties.

tyandsecurity.org/node/1437.

216 “An Analysis of Contemporary Anti-Diversion Policies and Practices of Humanitarian Organizations,” Harvard Law School, Project on Law and Security, May 2014, http://blogs.harvard.edu/cheproject/files/2013/10/CHE_Project_-_Anti-Diversion_Policies_of_Humanitarian_Organizations_May_2014.pdf.

Table 9: Transparency Standards and Initiatives Developed by NPO Sector*

Standard or Initiative	Developing Organization(s)
Principles of Conduct in Disaster Response Programmes	International Red Cross and Red Crescent Movement
The Do No Harm Handbook: The Framework for Analysing the Impact of Assistance on Conflict	Collaborative for Development Action, Inc.; CDA Collaborative Learning Projects
Private Voluntary Organization (PVO) Standards	InterAction
Humanitarian Accountability Partnership Standard	Humanitarian Accountability Partnership
Preventing Corruption in Humanitarian Operations Handbook of Good Practices	Transparency International
Humanitarian Charter and Minimum Standards in Humanitarian Response	The Sphere Project
Evaluation and Learning Activities	Active Learning Network for Accountability and Performance in Humanitarian Action

*Source: Risk of Terrorist Abuse of Nonprofit Organizations Financial Action Task Force, June 2014, at 22.

Financial Access Problems Experienced by NPOs

Sending funds through FIs has become more problematic as each transaction is scrutinized and more detailed information about recipients, beneficiaries and partnering organizations is required. In most cases cited, transfers have been delayed or blocked pending further information. Other examples include payments declined or funds frozen, accounts closed or applications to open new accounts refused.

The following examples are from interviews, focus group discussions or public sources. To encourage openness, names and identifying details have been withheld in order to ensure confidentiality.

Account Closures

As noted from the survey results, even though account closures represent 6.3% of NPOs' experiences, the effects can be devastating. After maintaining its business account at a U.S. bank for many years, one charity applied for a new account at the suggestion of the bank, citing security reasons. The bank declined to open the new account (encountered about 10% of the time for NPOs surveyed) and then refused to reopen the old account, freezing the charity's funds and

forcing delays in the payment of employees' salaries. The bank gave the charity 2–3 days to transfer its funds to another FI. The charity was ultimately able to find a small local bank to take its business, but that institution did not provide services for making overseas payments (see Chapter 4 for more information on account closures).

In another case, upon receiving notice that their accounts were about to be closed, one NPO met with its relationship officer and then asked to meet with risk management staff at the bank. The NPO proactively addressed the activities they assumed to be of concern (no information was provided by the bank officials as to the reason for closure). These involved transactions in support of programs in Syria and Yemen, as well as international partners. After presenting information, documentation and rationale for their activities, the NPO was thanked for coming. Ultimately, however, their efforts did not have a positive impact and the FI terminated the accounts.

Yet another charity providing essential financial support to a hospital in Aleppo had two different financial institutions close their accounts. As a result, hospital staff experienced 4-month delays in receiving salaries.

Denial of Wire Transfers

When FIs reject wire transfers, there can be significant impacts on program beneficiaries. An NPO operating an orphan sponsorship program for hundreds of children in Lebanon was forced to end the program because its FI would not process wire transfers. Two clinics for Syrian refugees, one in Saida and another Akkar, were also forced to close because they could not get funds to the clinics. Some banks have stopped processing vendor payments altogether in certain countries. As a result, an NPO was sued in Sierra Leone by vendors it was unable to pay.

Although education is free in Afghanistan, many students from poor communities cannot take advantage of the opportunity because they cannot afford the additional costs for room and board, food, supplies, transportation and other necessities. One American charity funded a dormitory for 400 underprivileged students so that they could attend university. Fundraising efforts focused on providing students with standard-sized beds, instead of cushioned mats on the ground, and other items that would permit them to comfortably focus on their studies. Information on individual students, their background of need and programs of study were made available to donors to encourage support.

Wire transfers destined to the program began to experience delays and were eventually denied entirely. No reason was provided. Unable to transfer funds and ashamed by their inability to fulfill their commitment, the NPO apologized to the local partner and was forced to abandon the students, some of whom were likely unable to continue their studies.

Foundation and grantmaker NPOs likewise have experienced banking problems in supporting international programs. Problems with wires to numerous countries, including Myanmar, Crimea, Yemen and Iran, have been increasing since late 2013/early 2014. In Afghanistan, there was a backup in the summer of 2014 during which all payments were rejected (evidently as a result of small banks not being in line with AML/CFT rules).

Delays in Fund Transfers

Some NPOs reported that each and every wire takes a minimum of 2 weeks, often longer, to reach their final destinations.

In every meeting with NPOs, the most commonly cited problem concerned delays in wire transfers. Results from the random sample survey (Chapter 4) confirmed that these delays are the most frequent ongoing problem for NPOs, occurring 37% of the time. In some cases, the transfers were destined to the accounts of employees

or other charities in the U.S. While some may assume that delays are less harmful than account closures for NPO operations, interviewees underscored that delays are critical and have severe consequences.

Some NPOs reported that each and every wire takes a minimum of 2 weeks, often longer, to reach their final destinations. For many NPOs supported by grants with specific timelines by which funds must be expended, such delays damage program operations and the reputation of the NPO. When they are uncertain as to their ability to transfer funds in support of grants, some NPOs actually reported forgoing grant opportunities.

Country partners may also add finance charges and late fees when there are delays in paying for services abroad. This strains relationships and causes problems for local employees dependent on regular salaries. Some universities reported that students studying abroad were denied access to their educational institute as a result of delays in payments being received.

According to another interviewee, efforts to ensure that payments are actually processed have become a full-time job:

“Every single wire generates questions, requiring two [to] three rounds of inquiries... with 15 wires per month, it’s a full-time job just to ensure our transfers are processed. Even repeat wires for the same destination encounter the same questions, taking up to a month, or five [to] six weeks, for wires to reach their destinations.”

One NPO operating in Jordan cited government requirements that each program have its own application and approval process. Money must be wired separately for each project to the same Jordanian entity, necessitating many wires each month. Yet the FIs asked for the same information each time, delaying the transfer, which in turn delays salaries, purchases of medicine and other items.

Delays in financial transfers can mean life or death for some of the most vulnerable populations. In spring 2015, one charity was unable to pay for the fuel needed to supply power to a hospital in Syria because of the banks’ lengthy delays in transmitting funds. The FI questioned the transfer and held the funds. The result was that the hospital ran out of fuel. “Delays have real human costs.”

One international NPO supported a “winterization program in Afghanistan that we generally fund annually, providing tents, blankets, and other non-food items. With delays in transferring funds, by the time we were able to send the money, the winter was over and the aid was never delivered.

Frequently working in dangerous and uniquely challenging environments, NPOs' staff and contractors can face real physical jeopardy when funds are not available. One recounted a situation in the field where people expecting to be paid showed up with guns.

This caused a significant number of beneficiaries to suffer severe health complications and, we expect, some deaths due to winter weather.”

Other charities talked about the consequences for international employees and vendors of not being

able to make payroll or pay bills and employees unable to receive pension distributions, some waiting for years. Frequently working in dangerous and uniquely challenging environments, NPOs' staff and contractors can face real physical jeopardy when funds are not available. One recounted a situation in the field where people expecting to be paid showed up with guns.

Because of the delays in wire transfers, some charities have turned to third parties to ensure that payroll for employees abroad is not delayed. This requires 2–3 months of advance payments to be held by the third party, which imposes penalties when transfers are delayed. Wages paid to the U.S. bank accounts of aid workers living abroad have also been delayed, even when it is a transfer within the U.S.

FINANCIAL ACCESS PROBLEMS OF HIGHER EDUCATION

Previously, there was little appreciation of the banking problems experienced by universities and colleges. These institutions were among the NPOs that expressed significant problems in transferring funds internationally. The nature of their work abroad primarily consists of supporting faculty/staff in field research, organizing and managing students' study abroad programs (including housing, food and travel), sponsoring visits such as sports teams' tours and paying honoraria for international speakers.

Due to the limited duration of faculty and student programs abroad and the difficulty involved with opening bank accounts in foreign countries, universities have increasingly shifted to utilizing MSBs for financial transfers. While expressing a strong preference for and comfort with using FIs, representatives nonetheless have to explore these workarounds “when we can't get banks accounts in country or wire funds.” Brazil, Mexico and Chile were among the countries in which educational NPOs encountered frequent problems.

NPOs expressed an aversion to relying on cash because it puts their employees at risk when they carry large sums, but in some countries where electricity is not reliable (and therefore credit cards are not an option) researchers have been forced to carry cash to conduct field work. Dangers exist, however, that staff could get held up in at the border or mugged, creating personal and reputational risks for researchers and institutions. As a result, some higher-education institutions have begun using MSBs to transfer funds for researchers and study abroad programs.

Excessive Information Requests

Information requests by FIs are standard procedures for exercising customer due diligence; however, 26% of NPOs surveyed reported unusual and excessive requests that were unreasonably invasive, impractical or resulted in undue delays. NPOs recounted a wide range of information requests by FIs, especially related to wire transfers, including a variety of requests from branches of the same institution. At times, it was reported, there is even a lack of clarity as to what information is required to ensure legal compliance on the part of both banks and NPOs.²¹⁷

Of particular concern were requests for personal information of those initiating transactions, such as home addresses, driver licenses, passports and copies of utility bills. One bank requested information on every working director of the NPO, as well as every board member, including passport information of those individuals and of their parents. Another NPO indicated that the FI wanted the maiden names of mothers of the individuals undertaking the transactions.

Other NPOs reported having to present IDs and a utility bill in order to open a bank account. FIs also required that each trustee of the charity go personally to the bank and present due-diligence documents. Some NPO employees felt they were profiled: if they sent employees with Western names/appearances, they did not experience the same degree of questions and identification requests as when they sent employees who had Arab or Middle Eastern-sounding names or appearances.

NPOs frequently send recurring payments to the same recipients (such as employees or partners abroad) yet experience repeated requests for the same information/documentation each time a payment is sent; NPOs complained that FIs generally do not appear to have systems for retaining information provided. Moreover, banks indicate that information is required to be provided within 1–2 days, although FIs are never held to such deadlines.

When money is sent to vendors, banks frequently ask for extensive documentation, including copies of service contracts, receipts, invoices and confirmation that the vendors do not have a relationship with any sanctioned entities. In the case of an NPO office in the UK (registered as a UK entity), the New York-based FI requested information every other month regarding vendors and invoices for recurring payments such as rent. Not only do such requests result in delayed payments (for which several NPOs reported being sued), but they can also be difficult to obtain in cultural environments that operate with less formality.

Another charity reported problems with processing travel expenses for employees in India. While it is not uncommon for NPOs to experience foreign banks holding funds and not crediting to accounts in a timely way, this NPO was asked by its U.S. bank to see copies of expense reports (never more than a few hundred dollars) before processing the funds. The bank refused to credit the employees' accounts and returned the money, even though it was the same bank with offices in India with which the NPO had a long relationship.

²¹⁷ FATF Rec 16 suggests standard requirements for cross-border wire transfers via correspondent banks—originator and beneficiary information—intended to minimize denials of transactions for destinations perceived to be high risk.

Even *de minimus* dollar amounts are subject to the same high level of information requests and scrutiny, reflecting strict liability in governing law.

Reluctance to Provide Information: Protection of Recipients

NPOs may not always be as transparent or proactive about who is being served, with their hesitancy to provide names of beneficiaries in wire transfers stemming from security or ethical concerns. In certain countries with repressive governments, NPOs and those who work for them are targeted or surveilled. Providing identifying information can link individuals with foreign funding and endanger NPO staff and beneficiaries. Many NPOs expressed the need to keep confidential information on staff in these difficult operating environments; while there is no concern with providing names, addresses, etc. to the U.S. bank, the possibility that information in the wire transfer may pass on to intermediary banks in such countries can be problematic. “We don’t like to give the name and address of beneficiaries for security reasons. Even seemingly innocuous information, such as purpose of funds, can present a security risk in certain countries; in such cases, we use generic characterizations, like ‘charitable grants,’ because of security concerns.” The fear of sharing too much information on recipients causes groups to be hesitant in sending information (such as invoices for grant payments) than should be necessary.

Others note concerns about violating the humanitarian principle that assistance be provided on the basis of need alone. Such information goes beyond KYC due diligence to “know your customer’s customer” (KYCC), which both the Treasury Department and FATF have emphasized is not expected (see Background, Chapter 2).

Most of the time, NPOs are totally in the dark as to where the questions are coming from or the status of their transfers. Intimidating information requests such as the following have been received, even for wire transfers from one U.S. account to another (from an NPO to its employee).

The following information is requested in order for their Bank to process this wire.

1. Detailed purpose of wire payment
2. All entities and organizations involved
3. Nature of goods or services rendered and to where services were rendered and to whom services are being provided
4. Include all countries directly and indirectly involved.

The intermediary bank has given your bank three days to return the requested information to them. In the event we are unable to meet the deadline, the following results could be encountered:

1. The funds could be returned back to your bank.
2. An OFAC investigation could be initiated against your bank, which could result in fines to our bank.
3. Funds could be seized pending an OFAC investigation (funds are held permanently or not released for several weeks or months).

Please understand that compliance with Due Diligence processes is a serious issue for all banks.

One NPO received a request for additional information concerning a wire to reimburse a physician for travel expenses associated with a medical mission, six weeks after initiating the wire.

Problems Opening Foreign Accounts

While opening an account in the country where programs are operating may at first look like a solution to some financial access problems, many NPOs expressed frustration at the amount of time and effort it took to open bank accounts abroad, even with branches of major international banks. There is no consistency in the information required, even within the same bank, and U.S. account representatives indicated that issues and problems must be dealt with by the NPOs' local bank. India was cited as an example of routinely requiring 1 year of background checks, extensive paperwork, certified identification, etc. for foreigners to open accounts. In China, NPOs reported that it took from between 11 months to 2 years to open an account, and in Kenya, 8 months. In some countries (Egypt was cited), political problems made it difficult to open or hold accounts, and in Mexico, routine requests such as changing the authorized signers took nearly 18 months.

Banking conventions in developed countries require that wire transfers are instantaneous, or at most, next day. However, in many of the third-world countries where NPOs operate, transfers can take days (3–5) or even weeks.

NPOs also complained of the excessive amount of information requested in opening accounts at foreign banks. In addition to corporate documents (by-laws, board, officers and directors, etc.), banks have asked for home addresses, not only of the person opening the account but of the NPOs' trustees as well. For corporate accounts, many local banks require personal information, including utility bills, drivers' licenses, and passports. Because of the difficulties in opening accounts, some NPOs reported employees opening personal accounts rather than business accounts. Numerous interviewees also reported extensive questioning of NPOs concerning the tax-exempt status of nonprofits. Many non-U.S. banks seemed unable to understand the notion of U.S. not-for-profit entities when establishing accounts.

Humanitarian Licensing

There is confusion among some NPOs and FIs over the OFAC licensing process. For example, some FIs request a Specific License, which is redundant in situations where a General License is available. In other cases, FIs ask for licenses when the activity supported by the NPO does not require one. One NPO, with appropriate OFAC licenses for humanitarian assistance to North Korea, was told by several banks that they do not process any payments associated with the country.

A number of countries are seemingly “off-limits” for many FIs due to concerns regarding sanctions. These include Syria, Iran, Myanmar, North Korea, Sudan and Yemen. Notwithstanding the availability of some General Licenses, several

Licensing Delays Shut Down Orphan Program in Sudan

Many multi-year development projects have been constrained by license delays, with some charities reportedly taking as long as 11 months to get an OFAC license, which is valid for 2 years. In the case of one NPO, the license expired before the orphan sponsorship program in Sudan was completed and funds expended. OFAC required that NPO operations be suspended while the license was under review. Representatives of the charity asked, “What are the kids supposed to do? Starve?” Applying for licenses for the orphan program, medical treatment, food and shelter took a huge amount of time, which severely affected recipients. The application for the charity's license renewal was not acted upon for more than 5 years.

NPOs noted that there is little appetite among banks to process transactions directed at these countries. Any financial transactions involving these “red flag” countries trigger excessive delays and additional questions, with most ultimately leading to transaction denials.

Cost/Time of Routine Equipment to Sanctioned Countries

For NPOs working in conflict zones, which are also often countries subject to sanctions, it can be complicated and time consuming to send even basic office equipment to support field operations. Understanding when Specific Licenses are required or General Licenses may apply can be challenging, often requiring legal assistance. One charity wanted to export laptops to their office in Syria and were advised that this required an OFAC license. They applied, and the license was approved after several months but contained strict conditions regarding end use and disposal. The costs of legal assistance to obtain the license exceeded the value of computers. “Even in instances where ‘no’ license is required, the fear that goods or finances could be diverted to designated individuals or entities has created a ‘chilling effect.’” For this reason, FIs and exporters will often go well beyond what is actually required, in essence implementing a “compliance buffer zone.”²¹⁸

For countries subject to comprehensive sanctions, such as Syria, available licenses are often not broad enough to cover the range of humanitarian activities, and therefore the banks are unable to process payments. There is also no mutual recognition of licenses approved among like-minded governments, which creates hurdles for humanitarian projects. Moreover, in conflict areas often subject to significant sanctions, there is no viable payment gateway or corridor to get humanitarian funds safely into the country. It is not an issue of risk appetite by FIs, but rather a more fundamental structural problem regarding lack of available banking channels into conflict zones.²¹⁹

Alternative Methods NPOs Use to Address Financial Access Difficulties

Accustomed to working in difficult environments and committed to their missions, NPOs have developed practical

“Red Flag” Countries

One NPO experienced significant delays due to intense scrutiny of each and every wire because the project supported Syrian refugees in Turkey: “Anything with ‘Syria’ in the name is being flagged and stopped as high-risk.” Even salary payments from an NPO account in the U.S. to its employee’s account in the U.S. took 1 month and prompted many questions, ostensibly because the NPO’s name contained “Syria.”

Another American charity had agreement for support from a Canadian group, but their bank refused a wire to any “Syrian-related accounts in the U.S.,” indicating that the Canadian government does not allow transfers to any organization “related to Syria” except UN organizations. Yet another NPO sent repeated payments to the same pharmacy for the same partner organization. Each transfer was delayed, and in fact, the delays increased and the same questions were asked each time. Some charities actually changed their names to avoid problems and delays associated with anything related to Syria.

²¹⁸ Justine Walker, Study on Humanitarian Impact of Syria-Related Unilateral Restrictive Measures: National Agenda for the Future of Syria, May 16, 2016, <https://assets.documentcloud.org/documents/3115191/Hum-Impact-of-Syria-Related-Res-Eco-Measures-26.pdf>.

²¹⁹ Ibid.

workarounds to problems of access to the formal financial system. The primary means NPOs cited to move funds in the face of problems with FIs include using MSBs and carrying cash; 41.7% of NPOs report doing this. While some were forced to cancel programs (3.4% of NPOs), many spoke of their reluctant acceptance of alternative ways of moving funds, which tend to involve less-transparent channels. All interviewees clearly preferred using established international financial institutions, but when such options are not available, other ways are found.

Money transmitters/MSBs have become frequent alternatives for NPOs to move money; 29.4% of NPOs use these services. While some NPOs expressed concerns that MSBs might not be as reliable as FIs and stated that they would prefer using banks, they felt forced to use these channels. In certain circumstances, however, even these options may be limited. Some NPOs mentioned wiring money to an individual rather than an organization. Transfer to and from individuals can be risky, however, because it adds an additional layer of vetting and puts the organization at risk if individuals abscond with the money. Some NPOs have employees use personal credit cards for travel-related expenses, with the expectation that they are easier to reimburse.

Some NPOs also reported an increase in the use of informal value transfer systems based on trust and personal ties—known as hawala²²⁰—because it is often the only way of getting cash into areas of conflict such as Syria.

Many NPOs have resorted to the greater use of cash despite increased vulnerabilities to theft and loss and the heightened physical risk to employees. Interviewees understood the value of audit trails, preferring not to use cash unless no other option was available (see Chapter 4). “Recently we had to send cash by hand (to Greece and Lebanon), which we hate but the problems made it necessary. Obviously that can’t be done with large amounts; it can help in an emergency but cannot be the normal routine.”

To hedge against potential account closures, NPOs reported that sometimes they open and maintain multiple bank accounts. The irony, however, is that multiple accounts can be a liability, making banks suspicious and increasing the likelihood of account closures. In addition, spreading assets among multiple accounts also makes each one less profitable for FIs, also potentially leading to terminations.

To manage increased risks of alternate methods, some charities have taken out crime insurance policies for possible thefts related to cash or bank transactions. However, carriers have begun dropping NPOs from coverage due to increased risks. In disaster situations, there is often no electronic banking, and even if there are banks, they aren’t always considered safe.

²²⁰ Hawala, an Arabic word meaning transfer or trust, is a popular and informal value transfer system based on the performance and honor of a huge network of money brokers, primarily located in the Middle East, North Africa, the Horn of Africa and the Indian subcontinent.

Effects of Financial Access Problems

Chilling Effect on Donors and Fundraising

A potentially significant cost to NPOs that are experiencing difficulties moving money is how this might affect donors who want to ensure that their support makes a difference. Delays in funding to programs or delivery of services have an unsettling effect on donors. Moreover, with competition for scarce resources (especially in places like Syria), an NPO's inability to consistently operate within expectations can be harmful to future fundraising.

With the perception that Muslim charities can be subject to increased scrutiny, some donors have stopped donations for fear of bank accounts being flagged. Reportedly, one donor had personal accounts closed due to contributions to Muslim charities. "The scariest thing is the chilling effect on large donors to Muslim organizations."

In some cases, NPOs have been hesitant to speak out about the problems they experience with sending funds abroad for fear it would dissuade donors: "We were suffering privately because we were worried donors would switch-up if this became public." The uncertainty regarding sending funds has hurt fundraising efforts, as NPOs are not sure they will be able to transfer funds to pay for programs (see Chapter 4).

Increasing Compliance Costs and Challenges

A number of NPOs indicated that financial access problems have driven up costs of compliance to the point that they have been forced to either abandon certain programs or forgo pursuing grants: "Some donors require no overhead, or a zero indirect rate, but with compliance costs rising, it's impossible to carry out responsibilities without our increasing rates.... This is money that's not going to help at-risk populations." Donors, including government donors, generally have not increased funding to account for this additional overhead in their grants.

When NPOs cannot maintain bank accounts in the U.S., or when wire transfers are delayed or canceled, it affects their operations. NPOs must devote scarce resources to handle questions and additional documentation requests. One grantmaker whose organization sends 20 to 40 wires per day said that 10%–20% of them are kicked back. "We have to increase staff to work out these details," she explained.

Afghan Literacy Program

"If we're not in there, the Taliban will be."

A major children's charity was informed by their financial institution that operating in Afghanistan raised their risk profile and would lead to difficulties with their other accounts globally. Rather than risk being debanked in more than two dozen other countries in which the charity operated, they reluctantly closed down the Afghan literacy program for nomadic children and returned funds to the UK. In Afghanistan's north (where children rarely attend school and the literacy rate among men is less than 7%, and among women less than 2%) the project provided flexible community-based classes and study groups to support girls' education. It was supported by a £1.7 million grant from the UK's Department for International Development, and it facilitated literacy efforts for 2,000 children, including 1,200 girls, in Afghanistan.

The Thomson Reuters Foundation conducted a survey of 21 NGOs and found that government donors and banks were also demanding more in-depth audits for programs in Syria, thus increasing costs. Seven NGOs, whose Syria aid budgets ranged from \$500,000 to \$75 million, reported that additional audit costs had risen substantially to a total of \$7.5 million. One charity said the cost of compliance reporting had doubled since March 2014.²²¹

Some NPOs reported relocating assistance programs to other areas in Syria “because of difficulties dealing with armed groups and fears of running afoul of anti-terrorism laws.” According to one study, bureaucratic workload for projects in Syria has risen by an average of 7,000 extra man-hours per charity in the 2 years since ISIS had taken root, the equivalent of three full-time staff members.²²²

Some NPOs Are Limiting Programs

NPOs frequently mention the hard choices they have faced in shutting down programs or halting specific assistance due to banking problems, which 3% of NPOs reported doing. “Because of the possibility of serious delays or cancellation, we have to pick programs that will do least damage if operations are suspended. This excludes some of the most important programs related to development and assistance.” One NPO reluctantly decided it would no longer be able to support Sudanese orphans because of financial access-related issues: “In trying to prevent money laundering and terrorism finance, restrictions on sending money are resulting in the death of persons, particularly the victims of terrorism.”

Tom Esslemont, “Syrians suffer as anti-terror laws squeeze charities – survey,” Thomson Reuters Foundation, February 24, 2016, <http://news.trust.org/item/20160224000357-rtjoh>.

²²² Ibid.

SYRIA: MICROCOSM OF FINANCIAL ACCESS CHALLENGES

The crisis in Syria represents unprecedented challenges on multiple fronts:²²³ more than 13 million people, including 6 million children, are in dire need of humanitarian assistance. Reports set the toll at more than 470,000 Syrians dead as a result of the war. With 6.5 million internally displaced people, Syria has become the largest displacement crisis globally.²²⁴ The magnitude of need has helped to propel the growth of Syrian-American civil society organizations with the establishment of numerous humanitarian and development NGOs. Among the many dilemmas they face, sending money transfers to Syria has become extremely difficult. Problems stem in part from sanctions directed at the Syrian regime, as well as the fact that any reference to “Syria” in the name, destination, etc. is intensely scrutinized by FIs and frequently denied (which has led many organizations to change their names and remove “Syria” from their titles).²²⁵

Nearly all of the obstacles NPOs have encountered in accessing financial services over the past several years play out in the case of Syria. Humanitarian organizations have reported FIs closing bank accounts, delaying and denying transfers, asking for unprecedented amounts of detailed information regarding partners, purposes of funds and anyone associated with operations, and outright denial of any transactions involving Syria. This includes transactions directed to Syrian refugees in Turkey and elsewhere. Syria represents one of the world’s worst humanitarian crises while simultaneously posing extreme challenges in terms of NPOs’ ability to access vulnerable populations, to ensure they do not support ISIL and exercise due diligence to protect employees and to transfer funds into the region to provide effective assistance.

Many NPOs working in the northern part of Syria operate programs from Turkey, where tens of thousands of people have sought sanctuary from an intensifying offensive by Russian and Syrian government forces. Because moving money into Syria is so difficult, NGOs have taken to withdrawing cash from Turkish banks and transferring it across the border using hawala. Supplies are procured outside and transported in to Syria, with hawala providing the most effective means of settling accounts. Syrian drivers, doctors and logistical staff often require that salaries be paid through MSBs or hawala in Turkey, but even these have been delayed or blocked for those living close to the Syrian border. Syrians who work for Western charities report salary payments being blocked from the Turkish side of the Syrian border. Fadi Hakim of the Syrian NGO Alliance said there was little that aid groups could do to deal with the system: “The regulations are not ours to change. They are out of our hands, so in the end you just deal with things the way they are.”²²⁶ As one NPO representative stated, “We need to untie the hands of people trying to help Syrian people; excessive risk aversion of banks is making a tragedy even worse.”

223 Ibid.

224 “Syria: UN says aid convoys unable to reach besieged areas despite US-Russia deal on ceasefire” U.N. News Centre, September 15, 2016, <http://www.un.org/apps/news/story.asp?NewsID=54927#.WIGZ8PkrLyR>.

225 Zedoun Alzoubi, “Syrian Medical NGOs in the Crisis: Realities, Perspectives, and Challenges,” Norwegian Peacebuilding Resource Center, October 1, 2015, <http://noref.no/Regions/Middle-East-and-North-Africa/Syria/Publications/Syrian-medical-NGOs-in-the-crisis-realities-perspectives-and-challenges>.

226 Tom Esslemont, “Syrians suffer as anti-terror laws squeeze charities – survey.”

SECTION FOUR OBSERVATIONS & RECOMMENDATIONS

Chapter 8 OBSERVATIONS

This situation is creating extreme hardship for countries, organizations and people least able to cope with it. It's long past time for leading banks and government officials to stop blaming each other and sit down to work out common sense solutions. The solutions won't be perfect—some funds may well escape the net—but there is no doubt we can do much better than we are doing today.²²⁷

Previous chapters endeavored to present the results of this investigation without significant editorializing or commentary; Section Two described the results of the random sample survey, and Section Three portrays the views of various stakeholders as reflected in focus groups, interviews and public statements. This chapter offers observations and findings that form the basis for the recommendations to address problems of financial access for NPOs found in the final chapter.

There Is a Problem

Until now, there have been no data indicating the scope and type of difficulties U.S. NPOs might be experiencing. In the absence of information, a hesitancy to act is understandable. This research initiative was undertaken to inform policy discussions with solid empirical data.

With this report, the question as to whether financial access is a problem for NPOs has now been answered: it definitively is. Years of anecdotal evidence reported by NPOs regarding difficulties with financial services are now confirmed through the random sample survey that is discussed in this report.

The scope of financial access difficulties, affecting 2/3 of U.S.-based NPOs and programs in all parts of the world, constitutes a serious and systemic challenge. As a result, financial access for NPOs must be recognized as a problem that needs to be addressed, on par with correspondent banking and MSB issues. It is time to move beyond discussions of whether there is a problem,

²²⁷ Bill Isaac, former chairman of the FDIC, comment post in response to Andrea Hall, “Bank De-Risking Hurts Charities and Increases Risk of Laundering,” American Banker, November 6, 2015, at: <https://www.americanbanker.com/opinion/bank-de-risking-hurts-charities-and-increases-risk-of-laundering>.

arguments over definitions and the finger-pointing that have characterized the issue to date. Now is the time to seek solutions.

The primary difficulties NPOs face include delays in funds transfers (experienced by 36.7% of NPOs), excessive requests for information (26.2%) and increased fees (32.6%), rather than account closures (6.3%) or refusals (9.5%). As such, it is more appropriate to characterize the issue as NPOs' difficulties accessing financial services rather than an issue of "derisking." The problem is less "NPOs having access to bank accounts" and more "being unable to transfer funds to high-risk jurisdictions."

NPOs are routinely treated as high risk, which results in delayed wire transfers and requests for additional documentation. This forces them to move money through less-transparent, traceable and safe channels. In the face of these difficulties, charities must find ways to deliver vital assistance to war-torn regions suffering humanitarian crises. According to the survey, the most common way of dealing with financial access problems is by carrying cash (41.7% of NPOs report doing this). This increases risk for NPOs and their beneficiaries. Moreover, increased use of cash and unregulated MSBs push funds into opaque channels, undermining the AML/CFT objectives of keeping money out of the hands of terrorists and criminals. Humanitarian relief and development initiatives are impacted when program money cannot make its way to its intended recipients.

As NPOs' ability to access the financial system has been hampered, the level of humanitarian need worldwide has reached all-time highs. Refugees fleeing war, climate disasters or political repression make up the largest number of displaced persons since World War II, making the programs U.S. NPOs operate in other countries even more important in saving lives and preventing the further erosion of democracy and human rights.

The Drivers of Narrowing Financial Access for NPOs Are Complex

There is no simple or singular reason why NPOs are having financial access problems, and this study does not contend that all decisions by FIs to terminate NPO accounts or delay wire transfers are attributable exclusively to AML/CFT concerns. However, interviews for this report, as well as regular surveying of the financial industry, consistently demonstrate that FIs' compliance-related concerns are among the primary reasons for derisking. A multiplicity of factors has resulted in serious unintended consequences that limit financial access for NPOs.

As discussed throughout this report, increased compliance costs, record penalties, fear of regulatory criticism and personal liability for compliance officers have resulted in a "perfect storm," causing FIs to reduce their risk appetite. For many FIs, decisions to withdraw or decline the request for financial services are based on the perceived notion that some customers, such as NPOs, are higher risk, and that certain countries (often where humanitarian assistance and development NPOs work) are higher-risk jurisdictions. The routine second-guessing of FIs' decisions and treatment of certain clients as categorically high risk by bank examiners require FIs to undertake extensive and expensive steps to mitigate those risks, tipping the risk-reward scale toward exiting such relationships. Despite reassuring statements from government officials, FIs perceive a clear disconnect between what policy officials say and what happens at the individual bank examination level, resulting in inconsistency among examiners.

Implementation of the Risk-Based Approach Remains Problematic

Government attempts to mitigate FIs' concerns by clarifying that regulators do not expect perfection have failed to provide the assurances necessary to tip the balance in favor of banking customers and countries perceived to be higher risk. The perception remains that regulators have zero tolerance for ML/TF risks. Without concrete action to provide greater certainty, the situation will continue unabated.

To overcome these concerns, FIs expressed the need for clear and specific guidance, flexibility to manage their risk-based programs without second-guessing and assurances that inadvertent mistakes will not result in significant enforcement actions. A safe harbor (protection from enforcement liability for FIs that meet certain conditions) has been advanced as the type of assurance and incentive to maintain such relationships. Guidance should support the risk-based approach, as well as reflect current realities by acknowledging that despite robust due diligence, there may be residual risk.

Barriers to Action Must Be Acknowledged and Dismantled

There has been little recognition by U.S. officials that financial access is a problem for NPOs, in contrast to the public acknowledgement of derisking in the context of correspondent banking and MSBs. U.S. policymakers and regulators appear reluctant to take NPOs' concerns seriously or to address these issues. Skepticism, along with long-held attitudes that the sector is high risk, pervades many discussions, from the policy levels down to individual examiners. FIs are likewise reluctant to devote resources to address the issues that regulators do not treat as a priority.

Overall, the absence of genuine engagement around financial access issues has resulted in the misunderstanding of the respective stakeholders' perspectives. The lack of a process to facilitate collective discussion and responsibility for solutions has contributed to strained relations among all parties.

This has led to frustration and a sense of apprehension among all stakeholders. NPOs are discouraged that their problems are not taken seriously and that they are seen as too risky to bank. At the same time, they are fearful of speaking out on the issue. Policymakers and regulators feel that their attempts to reassure banks that there is no zero-tolerance policy for inadvertent AML/CFT violations should be sufficient, yet they are also concerned about potential criticism from legislators for "going easy" on FIs or appearing to retreat from strict CFT policies. Banks do not want to be viewed as abandoning charitable organizations, yet they feel abandoned themselves by the lack of adequate guidance or the ability to manage risk without being second-guessed. Many FIs are also fearful of openly criticizing the shortcomings of the current system, given risks of enhanced regulatory scrutiny and potential backlash.

Action Is Needed

To effectively address the problems of derisking/financial access, all stakeholders must work together in a concerted effort. Solutions will only be found if the problem is approached as a shared responsibility. Characterization of these issues as solely “commercial decisions” by policymakers ignores reality and is a recipe for continued derisking and all of its consequences.

Currently, there is a clear lack of leadership and accountability on derisking issues, as noted in previous reports.²²⁸ Government points to the private sector, banks point at regulators, and NPOs are left frustrated and without adequate financial services. The most promising avenue for action is the dialogue sponsored by the World Bank and ACAMS.

All parties would benefit from solutions to these financial access issues, but the associated cost makes it unlikely that any individual group can or will undertake it alone. Therefore, the ideal solution is collective action so that the cost is shared. This collective action requires leadership from policymakers and regulators, starting with an acknowledgment of the seriousness of the issue and moving to action to clarify regulatory expectations and articulate a coherent policy.

Importantly, the human costs of NPOs’ financial access difficulties and continued inaction must be recognized. When programs are delayed or canceled because of the inability to transfer funds, peace is not brokered, children are not schooled, staff is not paid, hospitals lose power, the needs of refugees are not met and, in the worst cases, people die. Maintaining the current policies in the face of overwhelming evidence of the negative humanitarian consequences of such policies is not only harmful, it is inconsistent with American values.

Inaction Is Costly to Security

As noted previously, there are multiple interests at stake in the derisking crisis. In this context, broader foreign policy and security concerns appear to be underappreciated. The goals of financial inclusion and financial integrity have been characterized as incompatible, but both can be achieved. Ironically, current policy has created unintended consequences that increase the risk of illicit finance. Because these problems are not being effectively managed, U.S. policy objectives of development, humanitarian assistance and even countering terrorism and violent extremism are negatively impacted. Pursuit of multiple goals requires greater openness, a willingness to let go of entrenched positions to work together and the recognition that U.S. policy goals are equally valuable and compelling.

Protection of the global financial system from abuse by criminal and terrorist organizations has been and will continue to be an essential element of U.S. national security policy. But a key component of P/CVE initiatives is the ability of civil society organizations to engage and support local populations where terrorism takes root. NPOs play a vital role in this effort. However, according to recent assessments, the international AML/CFT regime continues to have a “chilling effect on the ability of civil society organizations to support P/CVE work.”²²⁹

²²⁸ Tracey Durner and Liat Shetret, Understanding Bank De-risking and Its Effects on Financial Inclusion, Oxfam and Global Center on Cooperative Security, November 2015, <http://www.globalcenter.org/wp-content/uploads/2015/11/rr-bank-de-risking-181115-en.pdf>.

²²⁹ Royal United Services Institute and The Prevention Project, “CVE Practitioner Workshop: Opportunities and Challenges for

The U.S. government process to address financial access issues, however, remains heavily weighted to illicit finance concerns, with the range of other agencies and interests not playing a commensurate role. Failure to involve all relevant agencies, coordinated by the National Security Council, means that broader security, foreign policy and humanitarian assistance perspectives are not adequately represented.

Ultimately, even AML/CFT objectives are not promoted when financial access to NPOs is restricted. Excessive regulatory requirements and enforcement push money into opaque channels, where it is more likely to fall into the wrong hands. Fear of compliance failures results in a vacuum that is likely to be filled by less transparent and accountable financial institutions, undermining the integrity of the global financial system and U.S. security. Recent Congressional inquiries noted that, “Implementation of federal anti-money laundering efforts must be pursued with an eye towards avoiding unnecessary and unintended impacts to law-abiding citizens and businesses. It is important to recognize that the loss of financial access can actually subvert anti-money laundering efforts by driving certain financial activities into untraceable banking alternatives.”²³⁰

There is an urgent need for all stakeholders to collaboratively reassess the existing policies to prevent illicit finance and address the serious and systemic problems hindering financial access for U.S. nonprofits.

Civil Society in Pushing Back Against Violent Extremism,” July 26-27, 2016, <http://www.organizingagainstvse.org/wp-content/uploads/2016/08/Formatted-CVE-Practitioner-Conference.pdf>.

230 Congressional letter to the Comptroller of the Currency on de-risking (lead signatories Senators Jeff Flake and John McCain), May 26, 2016, http://www.flake.senate.gov/public/_cache/files/647cddc2-d848-4a65-a2a1-03a128d6f859/signed-may-26-derisking-letter-to-occ.pdf.

Chapter 9

OPTIONS AND RECOMMENDATIONS

There appears to be no “silver bullet” for the derisking issue.²³¹

Regardless of what it is called—derisking or financial access—the problems that NPOs are experiencing in obtaining banking services to fund international programs will not be resolved without concerted action by all stakeholders. If financial institutions continue to consider banking NPOs as too risky or costly, the problem will only worsen. If government agencies fail to intervene, the human costs—denial of vital assistance to populations in crisis—will escalate, with potentially devastating results. Fundamental U.S. foreign policy interests, including inviolable humanitarian principles and long-term security imperatives, demand action now.

While the financial and nonprofit sectors play essential roles in helping to develop and implement solutions to financial access problems, the U.S. government bears responsibility for leadership in addressing this “collective action problem.” Furthermore, it is in government agencies’ interest to stop the movement of funds into unregulated or opaque channels; ensuring that NPOs have access to traditional banking services is the most effective way to address these challenges. While there is no “silver bullet” to solve the complex problem of derisking all at once, there are specific actions that can and should be taken to help remove the impediments to nonprofits’ critical humanitarian, development, education and peacebuilding work abroad.

This chapter will review proposed solutions that have been put forward by various stakeholders and experts, assessing their feasibility and potential for successfully addressing the problems raised in this report. It will also explain why some proposals are not practical solutions.

These recommendations and options should be viewed as the starting point in a process among stakeholders that moves toward solutions; the list is not exhaustive, nor is it intended to preclude additional ideas that emerge from further consideration of the problem. However, in order to be effective, solutions must meet some basic criteria:

- Address the drivers of narrowing financial access for NPOs
- Adapt to all sizes of NPOs and FIs
- Improve the implementation of the risk-based approach to AML/CFT programs
- Avoid anything that would make compliance unduly complex and burdensome

²³¹ David Artingstall, Nick Dove, John Howell, and Michael Levi, *Drivers & Impacts of Derisking: A Study of Representative Views and Data in the UK*, by John Howell & Co. Ltd. For the Financial Conduct Authority, February 2016, <https://www.fca.org.uk/publication/research/drivers-impacts-of-derisking.pdf>.

RECOMMENDATIONS

Launch a Solutions-Oriented Multi-Stakeholder Dialogue

The systemic nature of the problems indicates that changes implemented by only one group will not necessarily bring about the overall desired results: access for NPOs to regulated, transparent financial channels. All stakeholders must work together to find effective solutions for the multiple problems identified in this report, and in order for this dialogue to take place, new modes of engagement between regulatory officials, NPOs and FIs must be created.

A multi-stakeholder process should work toward ensuring that the financial system is responsive to NPOs, streamlining regulatory requirements on FIs, and protecting the system from abuse by terrorists or other bad actors. Such a process can encourage mutual cooperation to reduce apparent misunderstandings and fear and assist in better understanding the unique situations NPOs face. A high-level, sustained, multi-stakeholder process should craft practical solutions that benefit all parties, ensuring that they do not exacerbate the very problems they seek to eliminate.

Participants should include:

- U.S. agencies whose interests are impacted by the financial access problem, including those engaged in financial regulation, foreign policy, foreign assistance and national security
- A diverse range of NPOs, along with sector umbrella groups
- Financial institutions involved in international fund transfers, and key trade associations
- Multilateral organizations, such as the World Bank, UN and FATF

The World Bank/ACAMS meetings in June 2016²³² and January 2017 were successful gatherings of relevant stakeholders focused on practical solutions and represent a process to build on. Work streams and engagement of NPOs and FIs resulting from the January meeting should be sustained to promote greater understanding and dialogue.

Update the Bank Examination Manual and Bank Examiner Training

As enforcers of the Bank Secrecy Act with the ability to impose civil fines,²³³ Federal Bank Examiners are key to regulatory oversight and significantly influence FI behavior. As this report reveals, their work is often intrusive, second-guessing FIs' due-diligence procedures and applying pressure that increases compliance costs and discourages FIs from serving their NPO customers. In addition, regulatory oversight often varies by examiner, and the inconsistency adds further uncertainty for FIs. Banks reported examples in which examiners were not aware of policy guidance that banks are not required to know their customers' customers. A training program

²³² The Stakeholder Dialogue on De-risking, a workshop organized by the World Bank and ACAMS (Association of Certified Anti-Money Laundering Specialists) May 31-June 1, 2016, <http://www.acamstoday.org/stakeholder-dialogue-on-derisking/>.

²³³ Federal Deposit Insurance Corporation Regulations, Risk Management Manual of Examination Policies, Sec. 14.1-3, <https://www.fdic.gov/regulations/safety/manual/section14-1.pdf>; Office of the Comptroller of the Currency, Examinations: Overview, <https://www.occ.gov/topics/examinations/examinations-overview/index-examinations-overview.html>.

addressing appropriate examination techniques, policy objectives (including supporting financial inclusion when dealing with NPOs, MSBs and correspondent banks), guidance on the risk-based and proportional framework and greater understanding of NPOs, and that they are not by definition high-risk customers, is necessary and would help bridge the knowledge gap between examiners and FIs and examiners and NPOs.

The NPO section of the Bank Examination Manual has not been updated to reflect the June 2016 changes in FATF R8 (and is not scheduled to be revised until 2018). A collaborative effort between FIs, NPOs and the FFIEC²³⁴ is needed to revise the outdated language concerning risk assessment of NPOs and to implement it immediately. The resulting revision should guide FIs through a proportionate risk-based approach.

Create an NPO Repository/Utility to Streamline FI Customer Due Diligence

Technology-based solutions to enable effective and proportionate FI compliance, often referred to as “utilities,” can eliminate much of the paperwork and documentation requests that result in rising compliance costs and, hence, restricted financial access for NPOs. A repository created specifically for NPO financial access purposes could set out customized criteria that allow all types of organizations—large and small, established and new, secular and religious—to be included. FIs could then use the repository for their customer due diligence, obtaining the necessary information quickly and inexpensively. Using existing models as a guide, a team of lawyers and financial industry experts would evaluate the information submitted by NPOs.

Such a database would be a “green list”—one that is operated by an independent entity, such as an NPO or consortium of stakeholders—in order to avoid making the government a gatekeeper to NPO financial access (“white list”). However, one or more government agencies would need to give FIs assurance that they can rely on the information in conducting their due diligence. NGO Source, a repository used by international grantmakers, provides a useful precedent for such a regulatory greenlight (see box below).

The primary challenge in establishing a repository will be determining what screening criteria are appropriate for facilitating NPO financial access. The criteria should be limited to what are necessary and relevant for FIs’ risk management purposes in order to avoid unnecessary compliance costs. For example, “know your customer’s customer” questions, such as specific information on program beneficiaries or donors, go beyond the scope of what is required by regulators, according to both the U.S. Treasury and multilateral organizations such as FATF.²³⁵ And criteria used by existing repositories intended to help donor decision-making are not useful to facilitate international financial transactions, as they exclude some organizations on the basis of budget size, age or religious affiliation.²³⁶

²³⁴ Federal Financial Institutions Examination Council, <https://www.ffiec.gov/>.

²³⁵ FATF, Guidance on Correspondent Banking, October 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Correspondent-Banking-Services.pdf>.

²³⁶ Charity Navigator excludes groups not recognized by the IRS under 501(c)(3) or that do not file annual reports to the IRS (Form 990). Typically, these are religious organizations and their affiliates. This database also requires an NPO to have “at least \$1 million in revenue for two consecutive years and been in existence for at least seven years,” thus excluding both small and new organizations. See <http://www.charitynavigator.org/> and <http://www.give.org>.

NGO SOURCE: A MODEL THAT COULD BE ADAPTED FOR FINANCIAL ACCESS PURPOSES

In 2012, the nonprofit TechSoup Global and the Council on Foundations launched a project to build a repository of information on foreign NPOs that U.S. donors could use to streamline and simplify the process for international grantmaking. Supported by the expertise of top technology companies and leaders in U.S. philanthropy, the project launched the first custom-built database that is used by grantmakers needing an “equivalency determination” that a foreign grantee meets the IRS requirements for public charities under Section 501(c)(3) of the tax code before making a grant.

The database, known as NGO Source, avoids the duplication and unnecessary expense of separate equivalency determinations by individual grantmakers by using a standardized process developed by legal experts that is designed to comply with IRS regulations. In 2015, the IRS finalized a rule on equivalency determinations designed to lower the costs and administrative burdens of cross-border grants, giving grantmakers confidence that they can rely on equivalency determinations from a program such as NGO Source.

The process is straightforward. Grantmakers pay an annual membership fee to register with NGO Source, giving them access to the Grantmaker Portal, where they can search to see if the proposed grantee is already listed. If so, they can get an Equivalency Determination Certificate and accompanying documentation. If the proposed grantee is not listed, the grantmaker can request that an Equivalency Determination be made. The grantee is then sent a questionnaire that includes all the information required by IRS rules. NGO Source is available to help the grantee complete the questionnaire, a process that can take up to 4 weeks. Costs, paid by donors and foundations seeking these determinations, range from \$250 for organizations already in the database up to \$1,760 for a new determination.

Next, the NGO Source team of tax law experts evaluates the information submitted. If the proposed grantee meets the criteria, it is added to the repository and the grantmaker receives an Equivalency Determination Certificate. If the proposed grantee does not meet the criteria, NGO Source notifies the grantmaker and provides an explanation. Once the NPO is in the database, the information is available to other grantmakers.

NGO Source is similar to SWIFT’s Know Your Customer database in that both are fee-based services that allow users to conduct due-diligence procedures quickly and cost-effectively by relying on the services’ expertise and work product. The difference is that NGO Source is custom-built to deal with the unique features of NPOs and has the virtual blessing of the sector’s regulator. Its technology could be adapted to the financial services context by establishing criteria for NPO eligibility that fit the risk management needs of financial institutions.

Create a Special Banking Channel for Humanitarian Crises

When the international financial system is not able to meet the needs of NPO customers doing humanitarian work, new and special procedures to facilitate the transfer of funds overseas may be needed. Given the dire humanitarian need in places like Syria, it is even more important that fund transfers are timely. Although special procedures would not address the systemic problem revealed by this study, it could alleviate some of the most dangerous and serious impacts.

Working with foreign governments and multilateral organizations, the U.S. should create a viable banking channel into specific conflict areas where humanitarian need is greatest to better facilitate NPO aid delivery without creating repercussions for banks. For NPOs that have lost their accounts, a public entity, such as a government body, regional development bank or the UN, could establish a means of facilitating the movement of funds, even on an emergency basis, and put risk management procedures in place.

As part of this process, it is important to recognize that in some humanitarian crises, reliable documentation and ordinary due diligence required of NPOs are likely to be unrealistic, given unique local conditions. To acknowledge this reality, alternative ways to avoid inadvertent support to designated groups should be explored.

Institute Safe-Harbor Protections

The World Bank/ACAMs dialogue suggested the creation of safe-harbor provisions, whereby FIs that bank NPOs in good faith and meet certain criteria would be held harmless if funds inadvertently ended up in the wrong hands. Adopting a safe harbor would give U.S. banks confidence that they can do business with higher-risk customers and regions, provided they maintain rigorous risk-mitigation controls that are recognized by regulators; investment in consistent and effective due-diligence procedures would lessen the threat of prosecution or regulatory enforcement or, at a minimum, cap penalties at nominal amounts. This approach could be highly effective in expanding financial access for NPOs.

U.S. policymakers have been reluctant to establish safe harbors in the sanctions/national security context, fearing abuse by bad actors and the perception that such measures might imply a less-rigorous commitment to combatting illicit finance. Various formulations could be developed on a trial basis, however, such as temporary waivers of sanctions enforcement or limited safe harbor from regulatory actions for all but egregious violations. The USG could also require that FIs utilizing the safe harbor protection agree to additional, regular information sharing with law enforcement and regulators.

U.S. government funding of an NPO also could be considered adequate customer due diligence, since the extensive governance and reporting requirements that government grantees must meet make FI customer due diligence duplicative and unnecessary. Such a provision would have to be carefully crafted to ensure that it does not become de facto “white list” (see discussion of “white list” below).

Improve Implementation of the Risk-Based Approach

FATF has updated its risk-based approach to make it proportionate and ensure that it does not negatively impact the work of legitimate NPOs. This framework, focused on effectiveness, is relatively new, and the notion of residual risk acceptance,²³⁷ inherent in the risk-based approach, is not always reflected in current rules or enforcement policies. As the FATF noted in its 2016 mutual evaluation of the U.S., terrorist financing and sanctions violations “are strict liability offenses.”²³⁸ There is an inherent tension between strict liability and a risk-based approach that appears to contribute to narrowing financial access for NPOs.

Policy statements in speeches and blogs, attempting to clarify that regulators do not expect perfection and that charitable sector as a whole is not by definition high risk, have proven insufficient to provide the assurances necessary to tip the balance in favor of banking customers and countries perceived to be higher risk. Government agencies must be more explicit about the level of oversight they do and do not expect of FIs, including for NPO accounts.

The following steps should be taken:

Counter the Outdated Portrayal of NPOs as “Particularly Vulnerable” to Terrorist Abuse

The obsolete view of the terrorist financing risks associated with the NPO sector persists, notwithstanding changes to FATF R8, which removed the “particularly vulnerable” language and called for a proportionate risk-based approach. To bring U.S. policy up to date, officials should review all laws, regulations and guidance that impact NPO financial access to ensure that they reflect the revised FATF R8. Furthermore, the government should clearly state that NPOs are not by definition high-risk bank customers and avoid overstating the risk of NPOs. The Bank Examination Manual is just one such document in need of revision. FIs should also examine their policies and procedures with the goal of removing all outdated language.

Develop Clear Guidance and Standards to Reduce Guesswork and Compliance Costs

Guidance and standards must be consistent, practical, relevant to today’s financial services market and proportionate to any actual risk identified. They should clearly outline what information is required to ensure legal compliance by both banks and NPOs while remaining flexible enough to adapt to various types of FIs and NPO customers. When all parties know what is expected, guesswork and conflicting requests are avoided. This can lower compliance costs, differentiate between different levels of risk and focus scarce resources on reducing real risks.

237 Humanitarian Outcomes for InterAction, “Residual Risk Acceptance: An Advocacy Guidance,” September 2016, https://www.humanitarianoutcomes.org/sites/default/files/residual_risk_advocacy_guidance_note.pdf.

238 Financial Action Task Force & Asia/Pacific Group on Money Laundering, “United States Mutual Evaluation: Anti-Money Laundering and Counter-Terrorist Financing Measures,” December 2016, <http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-United-States-2016.pdf>. It is important also to note that FATF did not cite the unintended consequences of the U.S. application of the risk-based approach as a problem (or even as a concern) in the U.S. evaluation. This sends an ambiguous signal concerning over-compliance with AML/CFT requirements resulting in derisking.

A standardized list of information and documents FIs need from NPO clients to establish new accounts, monitor transactions and conduct annual reviews should be developed jointly by FIs and NPOs. Greater clarity of expectations will promote transparency and information sharing, enhance communications at the outset of a banking relationship and reduce time and costs. Similarly, standard information requirements for cross-border wire transfers via correspondent banks, as suggested by FATF Recommendation 16, could minimize delays or denials.

Promote Transparency, Information Sharing and Proportionality to Recalibrate Risk Perception

Clear standards must be combined with proportionate and transparent enforcement policies. Fear of harsh, expensive enforcement actions weighs FIs' risk-benefit calculation in favor of derisking NPOs.²³⁹ To reassure banks that they will not face severe penalties for inadvertent violations and to operationalize official statements rejecting zero tolerance, the government should formalize the standards for and mechanics of the enforcement process to reflect the risk-based approach. In particular, it should clearly differentiate between actions taken in good faith and those that are negligent or intentional. Intermediate sanctions, such as those used by the IRS for tax-exempt organizations, could make the process much more proportionate and ease FI fears of taking on clients perceived to be riskier.

Create Incentives to Encourage Appropriate Risk Management

Stakeholders should develop a menu of measures, beyond creation of a safe harbor, to incentivize FIs to bank NPOs and encourage greater efforts to engage with and better understand NPOs' operations and needs. Monetary incentives, such as tax credits, or reputational incentives, such as recognizing FIs who engage in—rather than avoid—effective risk management of NPOs and other customers perceived as high risk, should be explored. A structure for NPOs to pool accounts may provide an incentive for FIs by streamlining administration and lowering costs.

At the level of the FATF, statements should clearly articulate that FIs are responsible for commercial decisions on whom to bank but that widespread account closures within national jurisdictions are not consistent with implementation of the risk-based approach. FATF mutual evaluations should take into account such systematic closures and explore why they happen. Greater FATF attention to financial access could encourage regulatory officials to communicate guidance and expectations on the national level to correspondent banks, MSBs and NPOs. FATF (or other international financial bodies, such as FSB) should expand technical assistance in the area of financial governance and regulation to higher-risk jurisdictions.

239 Unintended Consequences of Anti-Money Laundering Policies for Poor Countries, Center for Global Development, at 10, November 9, 2015, <http://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf>.

Other Options

In cases in which formal financial transfers remain problematic, U.S. and international organizations could identify appropriate alternatives to the formal banking system—informal payment channels that NPOs can utilize to help lessen reliance on carrying cash. Alternative methods of moving funds, such as Bitcoin and other virtual currencies, mobile money and new electronic payment systems, should all be explored. Another option concerns creating de minimus exemptions for transactions below a certain dollar threshold; if being sent by an NPO for humanitarian purposes, ordinary FI due-diligence procedures would not be necessary.

Impractical Options

The findings in this report are likely to generate many ideas for increasing financial access for nonprofits that merit further consideration. At the same time, however, many ideas have been proposed that, upon examination, were found to be unworkable for a variety of reasons. Others have been attempted without success. These suggestions either are unlikely to effectively address the NPOs' financial access difficulties or have the potential to create additional problems.

The Problems with “White Lists”

A “white list” generally refers to a list of “approved” NPOs that have been vetted by the government. Proposals for white lists have been discussed since the U.S. Treasury published its *Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities*²⁴⁰ but have generally not been supported by either NPOs or the government. White lists are not inherently a bad idea. Rather, the context defines when they are appropriate.²⁴¹

There are several problems associated with a white list for financial access purposes. First, all groups not on the white list are presumed to be essentially on a black list, which would make it more difficult for those organizations to get financial services. Second, NPOs are cautious about the degree of government control, and government is concerned that publishing a list of “approved” charities could make them targets for terrorist financiers. Third, such a system is prone to discrimination practices that could, for example, disfavor Muslim charities or groups that are critical of government policies. Fourth, a government-run white list might also erect barriers for small NPOs, which, as this report shows, make up a significant proportion of NPOs that do international work.

240 Treasury *Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities*, Department of Treasury, 2010, https://www.treasury.gov/resource-center/terrorist-illicit-finance/Documents/guidelines_charities.pdf.

241 Examples of “good” white lists include the IRS list of tax-exempt organizations and USAID’s PVO list. However, these lists are not workable models for financial access purposes. The IRS list excludes organizations that are not required to obtain tax-exempt status, such as religious congregations and associations of religious groups, both of which conduct essential services in foreign countries. The PVO list maintained by USAID is based on criteria set forth in federal regulations and requires at least 18 months of operations and an audited financial statement for the prior fiscal year. This effectively precludes new organizations from joining the list. USAID’s criteria also exclude “church, synagogue, mosque or other similar entity organized primarily for religious purposes.”

Social Responsibility Initiatives at Financial Institutions

Corporate social responsibility initiatives to promote NPO access to financial services could be helpful. However, given FIs' perception of regulatory risk and increasing compliance costs, appeals to FI social responsibility without changes in the regulatory environment are unlikely to achieve the goal of financial inclusion for NPOs.

Building Relationships with Local Bank Managers

Some NPOs have tried to solve their financial access problems by establishing and maintaining regular contact with the bank's branch managers, where they provide detailed information on their operations and finances. However, in several cases when accounts have been closed, local bank managers have said that decisions are made at a higher level and that the local branch cannot change them. In addition, local branches have no influence over correspondent banks, which are often the source of delayed and canceled wire transfers and additional documentation requests.

Recommendations to Strengthen the Knowledge Base: Future Research

This report provides important new information on the impact the global trend of bank "derisking" has on the nonprofit sector, but, as with many reports, it also raises questions that require further information and analysis. Areas for future research include:

- The present study found little significant difference between faith-based and secular NPOs in their bank problems. However, the sample was not large enough to examine specific religious-based organizations. It is important to, at the very least, obtain information about all U.S.-based Muslim nonprofit organizations working in foreign countries. This could help determine whether discrimination contributes to their banking problems.
- In some areas, the only way to determine potential solutions is to collect data on the ground where programs are actually implemented. This is where both intended and unintended consequences really can be observed; indeed, such observations would indicate what happens when fund transfers are significantly delayed or canceled. This information can inform functional policy and solutions.
- There is agreement that increased compliance costs are a major problem; this point was made by study participants from financial institutions, stakeholders and survey respondents (32.6% referred to fees as a problem) and is reiterated in news reports. All groups acknowledge that it is a driver of derisking. Cost-effectiveness analyses can be applied throughout—from the government's role in financial institutions as middle processors to NPOs.
- In order to understand the impact of American NPOs, there needs to be more precise information than is currently available, such as their specific program areas or their primary missions. This is exemplified by the fact that 77% of NPOs list education as one of their missions. However, to develop and implement new strategies targeted to the greatest need, it is important to know what is meant by a primary mission.

- Further research should examine the FI perspective on financial access and derisking; what information financial institutions collect from NPOs; how they decide to maintain or drop NPO customers; when they request more information; and, within the institution, who makes these decisions. In essence, there is a dearth of information from and about financial institutions regarding the important role they have in this process.
- Following on previous studies regarding correspondent banking and MSBs, the World Bank is in a good position to gather further data and should be commissioned to provide a deeper analytical base regarding challenges confronting NPOs. It could explore new options, such as indemnification and insurance for firms and NPOs engaged in higher-risk jurisdictions, and propose next steps.
- It is always crucial to understand the things that work. Additional research on the 32% of NPOs without financial access problems could offer valuable insight into how financial access difficulties can be avoided. Do these NPOs work only in certain geographic areas? Do they know how to “work the system?” Knowing ways in which they differ from those NPOs that have difficulties in financial transfers will clarify some of these issues.

CONCLUDING THOUGHTS

This report presents new data concerning the scope, severity and effects of narrowing financial access for U.S. NPOs. The fact that 2/3 of NPOs face difficulties with international financial transactions, that more than 6% experience account closures, and that 37% experience delays of wire transfers is a cause for alarm. The fact that these problems affect many different types of programs in all parts of the world points to the systemic nature of the problem. These data mean that people suffering from starvation, disease, terrorism and conflict are being harmed.

The underlying AML/CFT and sanctions policies resulting in the phenomena of derisking are based on valid and critical security objectives in the aftermath of 9/11. But the damaging unintended consequences of these policies threaten to undermine vital U.S. security and foreign policy interests.

A new way of looking at financial access is necessary to confront this growing crisis. It is not a choice between financial integrity and financial inclusion; indeed, they are complementary, not contradictory, goals. As former U.S. Treasury Secretary Jack Lew noted, these efforts should not be antithetical: “This is not a conflict of interest, it is a need to bring together two parallel interests.”²⁴²

The convergence of interests of all stakeholders—U.S. policymakers and regulators, financial institutions and nonprofits—in finding solutions to the financial access problems NPOs are encountering provides the basis for a win-win proposition. All have a stake in preventing diversion of charitable assets to terrorist organizations. With broader foreign policy and security interests, the U.S. government supports activities of U.S. charities in meeting vital humanitarian and development imperatives, including addressing underlying conditions conducive to terrorism. Financial institutions want to lower compliance costs, reduce enforcement risks and work within reasonable risk management parameters. NPOs require timely and reasonably priced financial services to facilitate international operations, frequently to regions in conflict.

The ideas proposed and analyzed in this report warrant serious consideration, as do other options that stakeholders may develop through collaborative engagement and dialogue. It does not address the entirety of the complex financial access issue, nor purport to offer definitive solutions to the NPO aspect of the problem. The report has generated many questions and identified areas that should be explored further. It is but a first step in focusing attention on a critical problem and constructive approaches to the challenges.

Most importantly, however, leadership is needed from U.S. policymakers, as the serious and systemic problems will not be solved otherwise. Without acknowledging the deleterious humanitarian consequences of restricted financial access for NPOs, as well as concerted action to address it, the situation will continue unabated, undermining U.S. foreign and security policies. The opportunities for new approaches to these challenging issues represented by the changes in the U.S. government and Congress makes this a propitious time. The growing crisis demands action now.

²⁴² Lalita Clozel, “Lew on DeRisking: Banks Should Not Be Penalized for Engaging Abroad,” *American Banker*, October 7, 2016, <https://www.americanbanker.com/news/lew-on-de-risking-banks-should-not-be-penalized-for-engaging-abroad>

APPENDIX A

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APPENDIX B

SURVEY QUESTIONS

Some NGOs have experienced problems accessing banking services for international transactions in recent years. I am going to list a number of problems that can be experienced when conducting an international transaction. Please answer yes or no if your organization has experienced any of the following problems that may occur with banking services:

1. Accounts closed
(1) No (1) Yes
2. Refused to open account
(1) No (1) Yes
3. Transfers delayed
(1) No (1) Yes
4. Unusual additional documentation requests
(1) No (1) Yes
5. Fee increases
(1) No (1) Yes
6. Have you experienced other problems in addition or beyond these?
(1) No (1) Yes

[If no to Q1 through Q6, skip to Q17]

7. Can you please specify?
[Verbatim]
8. For any of the previously mentioned problems, did the financial institution mention any particular reason?
[Verbatim]
9. How frequently have you experienced problems of the type or types you mentioned? Would you describe it (them) as:
 - (1) Rare
 - (2) Occasional – maybe once a year
 - (3) Regular – every few months
 - (4) Constant – ongoing, few breaks between incidents

Given the difficulty [your organization] experienced with international transactions, which of the following remedies to these problems have you sought? Please answer yes or no to each of the following:

10. Find another financial institution
(0) No (1) Yes
11. Use money remitter, such as Western Union or something similar
(0) No (1) Yes
12. Carry cash
(0) No (1) Yes
13. Cancel the program
(0) No (1) Yes
14. Tried transaction successfully again later
(0) No (1) Yes
15. Was there any other option that you used??
(0) No (1) Yes

[If no to Q10 through Q15, skip to Q17]

16. Can you please specify?
[Verbatim]

Now I am going to list a series of possible program areas that your international transfers may have been designed to support. As I go through the list, please answer “yes” or “no” to the areas your program was intended to support.

17. Public Health
(0) No (1) Yes
18. Humanitarian Relief
(0) No (1) Yes
19. Medical Services
(0) No (1) Yes
20. Education
(0) No (1) Yes

- 21. Development/Poverty Reduction
(0) No (1) Yes
- 22. Human Rights
(0) No (1) Yes
- 23. Democracy Building
(0) No (1) Yes
- 24. Peace operations or peace building
(0) No (1) Yes
- 25. Something else?
(0) No (1) Yes
- 26. Can you please specify?
[Verbatim]
- 27. Can you tell me which countries the transfers were intended for? [Verbatim]

Now to get a better sense as to whom charities operating abroad are interacting with, I am going to read you a list of possible intended money or fund recipients. Please just respond yes or no if any of the following are typically your intended recipient(s):

- 28. Your own field office
(0) No (1) Yes
- 29. The field office or program of another international NGO
(0) No (1) Yes
- 30. A local community organization
(0) No (1) Yes
- 31. A government office or agency in the target country
(0) No (1) Yes
- 32. Another group or individual?
(0) No (1) Yes

[If no to Q28 through Q31, skip to Q34]

- 33. Can you please tell us whom the intended recipient was? Please, don't tell us the person's name, just the organization type or the individual's title is all we are looking for.
[Verbatim]

34. Can you estimate for us the number of people that are served by your international programs annually?
[Enter numerical value as quoted, probe numeric estimate, or verbatim if not numeric]
35. And can you estimate the number of people who may be impacted by the difficulties you experienced with international financial transactions?

[Enter numerical value as quoted, probe numeric estimate, or verbatim if not numeric]
36. Generally speaking, have your organization's banking problems gotten better, worse, or stayed about the same over the last few years?
(1) Worse
(2) Stayed the same
(3) Better
37. Does your organization have support from the U.S. government, such as grants or contracts with agencies such as with USAID or the State Department?
(0) No (1) Yes
38. Does your group self-identify as a Muslim charity?
(0) No (1) Yes
39. Does your organization self-identify as a faith-based charity?
(0) No (1) Yes
40. And with which faith community does your organization identify? [Verbatim]
41. Finally, have I missed anything about banking services that you could tell me?
(0) No (1) Yes
42. Can you please specify?
[Verbatim]
43. Would you be willing to receive a callback to discuss on a confidential basis problems experienced with international financial processing in greater depth?
(0) No (1) Yes

Thank you very much for taking the time from your busy schedule. This has been very helpful.

APPENDIX C

IRS GEOGRAPHICAL REGIONS, FORM 990 SCHEDULE F INSTRUCTIONS

Available online at <https://www.irs.gov/pub/irs-pdf/i990sf.pdf>

Antarctica

Central America and the Caribbean

Antigua & Barbuda, Aruba, Bahamas, Barbados, Belize, Cayman Islands, Costa Rica, Cuba, Dominica, Dominican Republic, El Salvador, Grenada, Guadeloupe, Guatemala, Haiti, Honduras, Jamaica, Martinique, Nicaragua, Panama, St. Kitts & Nevis, St. Lucia, St. Vincent & the Grenadines, Trinidad & Tobago, Turks & Caicos Islands, and British Virgin Islands.

East Asia and the Pacific

Australia, Brunei, Burma, Cambodia, China (including Hong Kong), East Timor, Fiji, Indonesia, Japan, Kiribati, Korea, Laos, Malaysia, Marshall Islands, Micronesia, Mongolia, Nauru, New Zealand, North Korea, Palau, Papua New Guinea, Philippines, Samoa, Singapore, Solomon Islands, South Korea, Taiwan, Thailand, Timor-Leste, Tonga, Tuvalu, Vanuatu, and Vietnam.

Europe (Including Iceland and Greenland)

Albania, Andorra, Austria, Belgium, Bosnia & Herzegovina, Bulgaria, Croatia, Czech Republic, Denmark, Estonia, Finland, France, FYR Macedonia, Germany, Greece, Greenland, Holy See, Hungary, Iceland, Ireland, Italy, Kosovo, Latvia, Liechtenstein, Lithuania, Luxembourg, Monaco, Montenegro, the Netherlands, Norway, Poland, Portugal, Romania, San Marino, Serbia, Slovakia, Slovenia, Spain, Sweden, Switzerland, Turkey, and the United Kingdom (England, Northern Ireland, Scotland, and Wales).

Middle East and North Africa

Algeria, Bahrain, Djibouti, Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Libya, Malta, Morocco, Oman, Qatar, Saudi Arabia, Syria, Tunisia, United Arab Emirates, West Bank and Gaza, and Yemen.

North America

Canada and Mexico, but not the United States.

Russia and Neighboring States

Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.

South America

Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, French Guiana, Guyana, Paraguay, Peru, Suriname, Uruguay, and Venezuela.

South Asia

Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka.

Sub-Saharan Africa

Angola, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Democratic Republic of the Congo, Republic of the Congo, Cote D'Ivoire, Equatorial Guinea, Eritrea, Ethiopia, Gabon, Gambia, Ghana, Guinea, Guinea Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Nigeria, Rwanda, Sao Tome & Principe, Senegal, Seychelles, Sierra Leone, Somalia, South Africa, Sudan, Swaziland, Tanzania, Togo, Uganda, Zambia, and Zimbabwe.