

Report

International Stakeholder Dialogue: **Ensuring Financial Services for Non-Profit Organizations**

Thursday, 15 February 2018 | The Hague, the Netherlands

1. Introduction

In recent years, many financial institutions have left or limited business relationships with different categories of clients and countries, because of business considerations or fear of reputational and liability risk. Often, banks also cite the cost of implementing international sanctions, anti-money laundering and countering the financing of terrorism (AML/CFT) measures, and exposure to penalties by supervisory and law enforcement authorities as reasons for their decisions to pull back their services. Consequently, some non-profit organizations (NPOs) have been denied bank accounts or seen them being shut down. More often, however, banks – or their correspondent banks – increase their due diligence threshold and ask NPOs for more information about their activities, donors and beneficiaries. This has led to delays in transactions, particularly for international wire transfers, which, in some cases, have been reported to last up to nine months. This is especially worrisome for critical humanitarian assistance to countries such as Syria, Somalia and other conflict areas.

On 15 February, 2018, the Ministry of Finance of the Netherlands and the Human Security Collective, organized an international stakeholder meeting to discuss the financial access difficulties of non-profit organizations with the support of the World Bank, and the Association of Certified Anti-Money Laundering Specialists (ACAMS). During the meeting, new research on the impact of derisking on non-profit organizations (NPOs) was presented and seventy-five representatives from NPOs, governments, international organizations, financial institutions and academia shared their knowledge and insights during three roundtable sessions, which took place under Chatham House Rules. This report aims to reflect the main themes of the meeting and the subjects that participants recommended for further work. The views expressed during the discussions do not necessarily reflect or represent those of the organizers.

2. Discussions

A. Impact of financial access challenges on NPOs

Participants agreed that there is pressure on NPOs' access to financial services, particularly of those NPOs that work in higher risk environments or finance such work. The most vulnerable and marginalized communities in conflict contexts with diminished rule of law and absence of government assistance rely on NPOs with activities on the ground. Small NPOs and faith-based charities are reporting that financial access problems are worsening and that they are forced to modify their activities. Derisking has a significant impact on the programming of NPOs and influences where humanitarian assistance can and cannot be provided. In a recent study by the London School of Economics, NPOs identified areas where they will cease to provide assistance because banks are refusing to take on the risk.

How to balance banks' due diligence obligations and the confidentiality requirements of NPOs

Banks are legally bound to apply due diligence measures and monitor transactions. When it comes to counter-terrorist financing obligations, there is strict criminal liability – even though this has never been enforced in practice. In executing financial transactions for NPOs, banks run a higher risk of being liable for indirectly providing funds to terrorists, with the result that they request that NPOs provide them with information regarding the recipients of these funds. In cases of international wire transfers, correspondent banks that facilitate transactions in foreign currencies often ask for follow-up information, leading to more delays in the transfer of funds.

Some of the information asked for, such as detailed lists of beneficiaries, is particularly sensitive in conflict areas and may put local contacts at risk. This is particularly problematic when state-owned banks are asked to perform a monitoring function for a government or when banks expect an immediate response. Generally, larger NPOs designated as SWEs (Significant Well-Established Entities) have the personnel and knowledge to navigate such requirements. Small NPOs often lack a comprehensive compliance policy, resources on the ground to enforce that policy and the operational framework to support it. They also have more difficulties in responding to frequent and varying due diligence requests. The lack of common due diligence requirements among financial institutions is generally considered to be unhelpful. Clearer procedures and tailored questions from banks, such as a Wolfsberg-type questionnaire (recently reworked for correspondent banks), were suggested. Such a questionnaire for NPOs could be developed together with NPOs, making sure that it is balanced and workable.

Each of the stakeholders could play a facilitating role in the coordination and dissemination of knowledge and resources. Charity commissions could help direct information, National Banking Associations could share guidance on banking requirements with NPOs and governments could use their convening powers to bring partners together.

Suggestions: Information requests to NPOs

- NPOs could seek early dialogue with their banks about their activities, beneficiaries and information requests
- Banks could work to harmonize CDD and follow up questions for NPOs

NPOs often lack knowledge regarding AML/CFT compliance

Considering the challenges that smaller NPOs face, it was asked if it would be helpful to consolidate them, incorporate them under an umbrella organization or forge partnerships with larger NPOs. It was pointed out that this would increase bureaucracy, but also harm their autonomous position in gaining trust and legitimacy on the ground, working as small NPOs often do in accessing or representing minority groups who otherwise would not be represented. Furthermore, it would not solve the due diligence requirements needed for each individual project or transaction.

Many NPOs have little knowledge on AML/CFT requirements for banks, and even though they have encountered financial access problems they are largely unaware of the systemic drivers behind banks' decisions. A need for awareness-raising among NPOs was signalled, with more engagement and training and the provision of tools to facilitate banking relationships for smaller NPOs. Roundtable



initiatives such as those taking place in the Netherlands or the UK can help in raising mutual awareness of each other's positions and drivers.

The initiative of the Estonian Presidency of the Council and the European Commission on developing an interactive EU sanctions map was highlighted as a good example. This map would help sectors, including NPOs, who might encounter the effect of sanctions in their work, easily navigate the field through a consolidated list (<https://www.sanctionsmap.eu/#/main>). Participants did however flag that not many NPOs seek advice on exemptions and licenses, perhaps out of fear of branding themselves as 'high-risk'. The EU has created an FAQ on humanitarian assistance to Syria and is looking to create more of those for other sanction regimes. Such guidance may also be useful elsewhere and could include information on red-flag triggers for banks. In the UK, the Office for Sanctions Implementation (OFSI) has created an FAQ for NPOs.

There might also be information developed at NPO-level that could be shared with the broader sector. Many NPOs have a risk-management system in which terrorism risks are central. This is especially so for the big INGOs that manage a large diversity of incoming funds and transfer money to conflict areas. For example, a Norwegian NPO has a counter terrorism risk-management toolkit on due diligence procedures, including a code of conduct. Larger and smaller charities could work together in sharing good practices around due diligence and compliance. Pooling resources could prove useful.

Suggestions: Increasing the AML/CFT knowledge of NPOs

- Sharing best practice on counter terrorism and AML/CFT compliance between NPOs
- Developing government guidance for NPOs on AML/CFT compliance and international sanctions
- Considering greater use of blanket or general licenses, development of new project licenses, or recognition of licenses granted by other countries
- Adopting a standing exemption for humanitarian activities could be something that the UN Security Council considers, paving the way for changes to promote greater use of humanitarian exemptions in EU sanctions

B. Banks' concern about regulatory actions and costs of compliance

Banks fear regulatory action, even though strict liability has never been applied

Legally, the UN Sanctions regimes lead to strict criminal liability: anyone who provides funds to potential terrorists or makes funds available to them commits a criminal offence. There are only limited options for exemptions. Currently only the sanctions regime for Somalia contains an exemption for humanitarian assistance. In the EU Counter Terrorism Directive, a sanction safeguard for humanitarian actions has been included. Future sanctions regimes would benefit from such safeguards. As a way of structuring the safeguards, the UK Bribery Act provides an interesting example of a possible solution: according to that Act a company found to be connected to an act of bribery is not guilty if it can show it had adequate procedures in place to prevent persons associated with it from undertaking the act. It was discussed whether a similar framing might work for sanctions legislation as well.



That said, there has never been a case where strict liability has been applied in a case where Customer Due Diligence (CDD) and other internal controls were in place and an inadvertent diversion of funds occurred. This raises the question of whether any policy can resolve derisking. Regulatory action resulting in large fines have come from major, sustained and long-term fraudulent behaviour; not small lapses in due diligence. Even though there are no such precedents for inadvertent breaches, banks still report fears over exposure to such risks. Even if regulators would not impose sanctions, banks point out that any negative publicity on this issue would cause them reputational damage.

Cost of compliance and knowledge of NPOs for banks

The burden of compliance for banks has increased, due also to intensified prudential requirements. Often, banks have difficulties profiling the risks of NPOs, leading to high compliance costs against already low profit margins. Most banks have limited knowledge of the NPO sector and frequently treat NPOs as SMEs when assessing risks, conducting CDD and determining the level of customer service. Specific guidance from regulators on NPOs might help banks in this field. There are banks with industry-specific teams, including for charity and public-sector clients, but these are exceptions that frequently rely on individual commitment and leadership. Nonetheless, such practices might serve as lessons for other banks and could be discussed in horizontal dialogues between banks. It was noted that some banks are unwilling to cultivate relationships with smaller- or medium-sized NPOs, though this may also depend on individual compliance officers and relationship managers. Relationship managers of smaller banks have no incentives to invest in higher intensity customer services for smaller clients. Banks could be encouraged to consider changes to these incentives.

Participants discussed whether banks could access other avenues to meet their compliance requirements. For example, a system where outcomes of due diligence processes performed by donors (including government donors) feed into the due diligence performed by banks. It was felt by the participants that these solutions for improved efficiency are worthy of further research and discussion.

The possibilities for technological solutions to lower compliance costs were discussed. Financial technology, such as KYC utilities, machine learning, blockchain, legal entity identifier (LEI) were mentioned, and so too were biometrics and big data, all of which could potentially help improve the efficiency and accuracy of CDD and improve transaction monitoring, including help passing information along from one bank to the other in the correspondent banking chain. Knowledge of these technological solutions among most participants was basic, but it was agreed that further exploration of these type of solutions could be promising. It was pointed out that obstacles on information sharing due to national legislation (e.g., privacy) could inhibit the potential use of technological solutions, including information sharing within financial groups.

Participants also wondered whether there could be economic incentives for banks providing services to smaller NPOs, such as tax credits (e.g., Community Reinvestment Act in the US).

Suggestions: Improving bank knowledge on NPOs and lowering the costs of compliance

- Regulators could provide NPO-specific guidance to banks
- Banks could cultivate NPO knowledge among their staff through dedicated teams or persons

- Options for technological solutions, which could help lower the costs of compliance, could be explored
- Banks could explore the option of using the information already gathered by donors when conducting their due diligence processes on NPOs
- The possibilities for creating economic incentives in banks to provide services to (smaller) NPOs could be tested

C. Policy implementation and coordination

International standards were revised to emphasize that only a small percentage of service NPOs might be exposed to a higher TF risk, but this is not yet being implemented

Despite the recent rewording of FATF Recommendation 8 (R8) and the publication of a guidance paper clearly stating that only a small percentage of service delivery NPOs present an elevated risk, countries and banks have not yet reflected this amendment in their implementation, with human rights and advocacy organizations also being viewed as presenting a high TF risk. In addition, there are reports that R8 is being used as an excuse to justify a crackdown on civil society in some countries. Likewise, concerns were raised about banks in some countries reviewing the mandate and objectives of advocacy and human rights NPOs against government objectives during the onboarding process and, in some cases, refusing to onboard NPOs whose activities challenge government agendas.

Given that the old R8 wording and policy was in place for 15 years, it may take a long time to change perspectives and the prevalent discourse on the NPO sector. Participants considered that more engagement by the FATF on these issues is needed. Focus on this issue may be useful at the FATF Private Sector Consultative Forum, where NPOs have a seat, but also at the G20, the G7 and the EU, particularly in relation to financial inclusion.

Risk-based approach results in zero tolerance for risk

Central to the discussion was the risk-based approach. Participants expressed the view that compliance is being applied in a rule-based manner. There was found to be a big discrepancy between the policy statements of regulators versus day-to-day supervision. Banks have insufficient comfort regarding the extent of reasonable due diligence. As a result, banks fear sanctions for inadvertent breaches. Some participants expressed their observation that both banks and regulators are going far beyond legal requirements and international standards, e.g., when it comes to requirements such as Know Your Customer's Customer. Without sufficient guidance, it is hard for banks, NPOs and even supervisors to make an appropriate risk assessment and determine who to apply restrictions to. While the suggestion of an NPO whitelist was firmly rejected (i.e., NPOs that are not on a whitelist become blacklisted by default), it must be acknowledged that all stakeholders are overcompensating, creating more risk aversion. Participants suggested that supervisors need more training and guidance on the application of the risk-based approach.

Different governments are now undertaking TF risk assessments, which also cover the NPO sector. It was seen to be crucial that NPOs participate in these discussions to ensure that risk assessment at a policy level is correctly informed. It is crucial to ask which part of the sector represents the risk, and how dynamic the sector is as a whole in mitigating it. This could be of particular importance when governments conduct their national ML/TF risk assessments.

Exploring alternatives to correspondent banking, including dedicated charity banking

There may be instances where the terrorist financing risks are too high for a private commercial party to bear, but where the services of NPOs are critical for humanitarian aid. For such cases, it may be necessary to look into more far-reaching alternatives to international wire transfers that require correspondent banking. Ideas suggested included public entities, such as central banks, or international development banks establishing a means of facilitating the movement of funds into high-risk areas, even on an emergency basis, and putting risk-management procedures in place. The modalities of such arrangements would need to be discussed further. Another option that was raised was the idea of a charity-specific bank that could cater to small and medium NPOs, though this would still require the correspondent banking chain. There are also commercial parties that are seeking other payment chains that do not require correspondent banking for cross-border payments, particularly in business-to-business payments.

Government policy on counter terrorism and international development needs to be aligned

Derisking may result in a preference for the use of cash and informal payment channels, which increases the risk of opaque financial flows, making it harder to tackle corruption, money laundering or even terrorist financing. International standard-setting bodies and governments have a responsibility to focus on aligning underlying policies to tackle these threats.

Participants suggested that governments (Departments of Defence, National Security, Finance, Justice and International Development) need closer coordination and cooperation on their counter-terrorism objectives. International sanctions, national security, counter-terrorist financing policy and stabilization policies serve many of the same objectives. There is a need for government champions on this topic. Increased engagement between Ministries of Finance and Justice, and NPOs could be useful as well.

Financial services as part of aid programming

Further, participants suggested that donors need to take greater responsibility for ensuring NPO access to financial services, particularly when the government itself is the donor. Programming should be more flexible, to allow for extensions in case of money transfer delays. It is worthwhile to further look into the role a government donor could play in providing banks delivering such services with greater assurance, taking the burden away from banks having to make such political decisions.

Participants wondered whether the costs of audits on NPO activities, which banks could use in their due diligence process, could be factored into institutional grants along with training and other resources. In this way governments would share the burden of the cost of compliance. Administrative costs should be recognized when funding projects, which could defray some of the compliance costs.

Ongoing multi-stakeholder dialogue

Participants emphasized the need for transparency and ongoing multi-stakeholder dialogue, such as those ongoing in the UK, US and the Netherlands. The UK has built such dialogue around four pillars: 1) guidance and best practice; 2) legislation; 3) innovation; and 4) information sharing. And while the body of research is growing, a need to capture the effects, both qualitative and quantitative, of NPO



derisking on aid and development was raised – particularly with a focus on small organizations on the ground receiving money rather than only on organizations sending the money.

Suggestions: Policy implementation and coordination

- Include NPO risk assessments and the risk of financial exclusion in national money-laundering and terrorist-financing risk assessments
- Adopt supervisor and bank guidance and practices to further implement the changes to FATF R8 and the risk-based approach
- Explore safe payment alternatives to correspondent banking, including through central banks or dedicated charity banks
- Ensure closer coordination between all government stakeholders on international aid, counter terrorism and terrorist financing to guard against unintentional conflicting policy outcomes
- Push for greater discussion of the interrelated issues of sanctions, AML/CFT and derisking in international fora (e.g., G-20, G-7, FATF, UN, EU)
- Integrate, as a government donor, access to financial services as part of aid programming and provide banks with due diligence assurance
- Organize or contribute to ongoing multi-stakeholder dialogue

The organizers are grateful to all participants for their contributions and suggestions made during this meeting, as well as to the organizations they represent. Together, we aim to explore the possibilities for collaboration on financial access for humanitarian organizations and charities.

D. Interested in learning more about this work?

The organizers are interested in and open to cooperating with stakeholders on practical ways to address challenges facing NPOs in accessing financial services.

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