Input from Global NPO Coalition on FATF to public consultation on R.1

Part 1: Good practice example from The Netherlands on applying the risk-based approach to enhance sectoral financial inclusion and prevent derisking

In 2022, the Dutch Central Bank DNB (De Nederlandsche Bank) published a report titled 'From Recovery to Balance' after realisation that their AML/CFT supervisory approach was not risk-based enough, was leading to the derisking of certain classes of customer, and was not the most effective in keeping the financial sector free from financial crime.

A roundtable process was set up in response. This was supported by the Central Bank and the Ministry of Finance, but was coordinated by the Dutch Banking Association. Human Security Collective (HSC), the co-chair of the Global NPO Coalition on FATF, was part of this roundtable engagement, the result of which were twofold:

- Risk-Based Industry Baselines published in May 2023 for banks and customers. These provide banks with clear principles for risk-based CDD.
- Sector Baselines: more detailed sector baselines for those sectors most impacted by derisking such as NPOs, sex workers, etc. The NPO baseline, for example, lays out both risk enhancing and risk mitigating factors for NPO transactions. Banks are initially meant to see NPOs as neutral (as opposed to before, when the entire sector was seen as high-risk for TF) and would then apply a risk lens to do 'more if necessary, less if possible' in terms of due diligence. We anticipate that these risk-based standards will reduce civil society organisations' difficulties accessing banking services for their legitimate activities. The standard is designed to eliminate unnecessary and burdensome due diligence customer checks on civil society organisations, making it easier for them to access essential banking services. The Dutch Banking Association is monitoring the operationalisation of this sector standard, while NPOs involved in developing the baseline are monitoring whether NPOs still experience problems accessing banking services post the introduction of the standard. These two data points will provide the information required to gauge whether banks have incorporated the baseline in their protocols and procedures. **Initial reports have been encouraging: at one of the international banks, Rabobank, as of June 2024 the number of NPOs immediately given the high-risk label went down from 34,000 to 14,000 through the application of the NPO baseline or risk-based standard.**
- The above is consistent with HSC's research findings, which indicated that the risk-based approach was inappropriate for smaller regulated institutions for not only being too resource-intensive but also for the underlying assumption made that industry as a whole (the market, i.e. the regulated) would be better at identifying and managing risk than the regulators/supervisors. A rule-based approach, such as the Dutch example above, would not be without risk consideration, but the identification and calibration of that would lie with the regulator. **Only such nuanced calibration at the supervisory level will translate to appropriate SDD/EDD calibration at the financial-institution level.**

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Part 2: Supervision and monitoring of risk

Supervision must be more holistic than it is now. To that end, INR 1, para 9 needs to be amended. Supervisors should not just be looking at institutional risk profiles but also at the risk mitigation measures that financial institutions have put in place (so not just the 'inherent' risk but the 'residual' risk, as in a normal Risk Assessment procedure). Moreover**, supervision needs to also consider other risks such as those of financial exclusion in the overall risk calculus**. Supervision of risk is currently too siloed, and does not take into account either mitigating factors or other policy imperatives such as financial inclusion and human rights frameworks.

Part 3: Change in methodology and procedures

The FATF methodology and procedures must subsequently be amended **to allow assessors to mark countries down if their financial institutions are not using simplified due diligence in low risk scenarios**. The issue of **financial exclusion/derisking (individuals/sectors) needs to become an integral part of National Risk Assessments**: if entities are not or at limited risk for terrorism financing then simplified due diligence guidance from banks and banks' supervisors should be in place. If a country with limited or no evidence for terrorism financing abuse of NPOs, for example, still disproportionally derisks NPOs, then the FATF evaluation team needs to be able to mark the country down.