

Terrorism and NPOs— What Could FATF Do?

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I. Introduction

The issue of government controls being imposed on civil society organizations has been receiving a lot of attention lately and drawing responses from a wide variety of different actors. Last year, at a special round table for civil society during the UN General Assembly meeting, US President Obama observed that

...a growing number of countries are passing laws designed specifically to stifle civil society. They're forcing groups to register with governments, eroding human rights protections, restricting NGOs from accessing foreign funding, cracking down on communications technologies that connect civil society groups around the globe. (...) We're also seeing new and fragile democracies cracking down on civil society, which I believe sets them back and sends a dangerous signal to other countries.¹

Similarly, a recent report from the Carnegie Endowment for Peace noted that

Governments are erecting legal and logistical barriers to externally sponsored democracy and rights programs they deem too politically intrusive, publicly vilifying international aid groups (...) harassing or expelling [them](...). Of particular concern (...) is the viral like spread of new laws restricting foreign funding (...).²

Countries from almost every region in the world are enacting and enforcing legislation requiring civil society organisations to obtain government approval for funding from abroad, to funnel their funds only through certain approved channels, or to spend their funds only on certain activities.

¹ See Remarks by President Obama at Civil Society Roundtable available at <http://www.whitehouse.gov/photos-and-video/video/2013/09/23/president-obama-holds-civil-society-roundtable#transcript>. All internet links cited in this article were accessed October 6, 2014.

² See "Closing Space: democracy and human rights support under fire" Thomas Carothers and Saskia Brechenmacher, p1, Carnegie Endowment for International Peace, available at <http://carnegieendowment.org/2014/02/20/closing-space-democracy-and-human-rights-support-under-fire/h1by>.

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There is more than one driver of this development. The paper goes on to say that they lie in “several interrelated and major changes in international politics. Identifying these underlying causal factors is vital to understanding the overall trend (...).”³

Partly they are the instinctive response of (semi-)authoritarian rulers, intent on preventing the spread of dangerous ideas about freedom and democracy and remaining in power. Another driver of civil society’s “closing space” that commentators point to when discussing this phenomenon, are the post-9/11 policies on counter terrorism. Robust language about the need for security above all else has allowed governments to cut corners on established human rights and freedoms, so the argument goes. Action taken to curb terrorism-financing (TF) is often mentioned in this context. The measures promulgated by the international standard setter on anti-money laundering and combating terrorist financing (AML/CFT), the Financial Action Task Force (FATF) and the way in which those standards are evaluated come in for particular criticism. Perhaps the most critical of the articles on the link between AML/CFT and the restrictions imposed upon civil society is Ben Hayes’ “Counter-terrorism, ‘policy laundering’ and the FATF: legalising surveillance, regulating civil society.”⁴ The international AML/CFT standards have spun

a global web of international law and policy transposed into national rules and regulations and endless bureaucracy. As the web has been expanded, the powers of state officials, prosecutors and investigators have been harmonised at a particularly high (as in highly coercive) level. At the same time, guarantees for suspects, defendants and ‘suspect communities’ have been largely disregarded. Caught in this global web are charities, development organisations, NGOs, human rights defenders, community organisers, conflict mediators and others who find their work hampered or paralysed by onerous regulations or politically-motivated legal manoeuvres.⁵

The evaluation system of FATF is described in similarly bleak terms as having endorsed some of the most restrictive NPO regulatory regimes in the world, and strongly encouraged some already repressive governments to introduce new rules likely to restrict the

³ Ibid at p 21.

⁴ Available at <http://www.hscollective.org/wp-content/uploads/2013/09/fatf-report.pdf>.

⁵ Ibid at p 10-11.

political space in which NGOs and civil society actors operate.⁶

This paper aims to examine more closely this possible nexus between counter terrorism measures and the restrictions imposed on civil society organisations' access to financial resources. To what extent can CFT standards as promulgated by FATF and endorsed by the UN⁷ be held responsible for this development and what, if anything, can FATF or its members do to address it. Before doing so however, it may be helpful to examine what countries concretely are doing in law or regulation to restrict CSO's use of and access to funding and also to review in more detail who this standard-setter really is, and what it does, and what these standards have to say about NPOs and how they might affect them.

II. Governments Imposing Restrictive Measures on CSOs

Though each country is unique, and the rules imposed vary from jurisdiction to jurisdiction, the rules imposed on CSOs restricting their operations and funding often exhibit one or more of the following characteristics:

- *Burdensome Registration Requirements*
- *Prior Government Permission for Funding*
- *Prescribed Channels for Foreign Funding*
- *Prohibitive Tax Burdens*

The following country examples can serve to illustrate some of these points: In **Tunisia** first aid and charity organizations may only accept contributions approved by the Minister of Interior, and other associations may only receive subscriptions paid by members or funds extracted from the members. Although the law does not explicitly require prior approval for foreign funding, some groups report that foreign funding has been

⁶ Ibid at p 11. He does not further discuss the dilemma in which assessors find themselves when confronted with such restrictive legislation: Give the country a good rating- and one is endorsing repression, give them a bad rating and one risks the country taking even further restrictive measures in response.

⁷ In UN Security Council Resolution 1617, the UN Security Council strongly urged UN member states to

monitored through the central government bank, and the government has frozen or confiscated NGO funds for no clear reason. As a result, organizations have limited ability to obtain funds with which to sustain themselves.⁸

Indonesia requires social organisations that seek to receive or provide donations from or to foreign entities to engage in an exhaustive approval and reporting process. According to a 2008 regulation foreign funds cannot be used for activities that “disrupt national unity or harmony” or “cause social anxiety and disorder of national and regional economy.” The regulation requires social organisations to register with the government and to seek approval from the Ministry of Home affairs or from local government for any foreign funding, pay tax on those funds and communicate to the community through the media on implementation on foreign funded activities.⁹

The key legal barrier to CSO resources in **Bangladesh** also relates to foreign funding. The government established the NGO Affairs Bureau (NGOAB) within the Ministry of Establishment to coordinate and regulate the activities of CSOs operating with foreign funding. A CSO seeking to receive or use foreign donations must obtain approval, known as the *FD Registration*, from the NGOAB. Separate approval for all projects is required from the NGOAB, irrespective of prior registration by any other authority. The NGOAB is now located in the Prime Minister’s Office and is responsible for all contact with CSOs under the Foreign Donations Regulation Rules, 1978. The NGOAB, released the Foreign Donations (Voluntary Activities) Regulation Act 2011 in January 2012. The Cabinet of Ministers approved the draft Act in June 2014. It is now pending review by Parliament.

If enacted, the draft Act, would:

- Prohibit individuals and organizations from receiving foreign dona-

implement the FATF recommendations.

⁸ International Center for Not for Profit Law, Global Trends in NGO Law, a quarterly review of NGO legal trends around the world, Volume 3, Issue 1: Arab Spring: An Opportunity for Greater Freedom of Association and Assembly in Tunisia and Egypt? Available at <http://www.icnl.org/research/trends/trends3-1.html>.

⁹ Regulation of Minister of Home Affairs no 38 of 2008 on the Receipt and Giving of Social Organization Aid to and from foreign parties available at <http://ccingoregnet.solutionsclient.co.uk/Library/Home%20Affairs%20Decree%2038%202008.pdf>.

tions/contributions for the purpose of carrying out any voluntary activity without prior government approval.

- Require all organizations wishing to receive and use foreign donations/contributions to register with the NGOAB.
- Require all organizations seeking to carry out activities with foreign donations to secure advance project approval.
- Penalize NGOs if the Director General of the NGOAB believes that NGOs are engaged in activities which are “illegal or harmful for the country.”¹⁰

“If we fail to regulate the unethical activities of the NGOs and micro- credit organisations, the country might be downgraded from the current ‘grey list’ to ‘dark grey list’ of FATF,” an official said.¹¹

In February 2013 the **Azerbaijan** Parliament introduced and passed amendments to the Code of Administrative Offenses, the Law on Grants, the Law on Freedom of Religion, and the Law on Non-Governmental Organizations. The amendments put in place hefty fines on NPOs that fail to register grants with authorities in a timely manner and other restrictions on funding, such as penalties on accepting most cash donations. In an official justification to the proposed amendments, the drafters stated:

The main purpose of the draft is to ensure transparency in the reception and usage of voluntary donations by NPOs and religious organizations, as well to enforce international obligations of the Republic of Azerbaijan in the area of combating money-laundering.

Effects of the new measures:

- Increased penalties for NPOs that fail to register a grant;
- Introduction of a penalty for failure to include donation information in financial reports;

¹⁰ ICNL, NGO Law Monitor, Bangladesh available <http://www.icnl.org/research/monitor/bangladesh.html>.

¹¹ See http://www.thefinancialexpress-bd.com/old/more.php?news_id=128048&date=2012-04-2. Concerning the listing, see further below.

- Introduction of a penalty for donors giving cash donations;
- Requirement that donations to be paid by bank transfer; and
- Introduction of confiscation and a penalty for implementation of projects without a grant contract.¹²

On December 21, 2010, **Venezuela's** National Assembly passed the Law for Protection of Political Liberty and National Self-determination, which targets NPOs dedicated to the “defense of political rights” or other “political objectives.” Specifically, it precludes these organizations from possessing assets, or receiving any income from foreign sources. Noncompliance could lead to a fine of double the amount received from the foreign source.¹³

In **Ethiopia** NGOs that receive more than 10% of funding from foreign sources are restricted from participating in essentially all human rights and advocacy activities thus severely affecting their right to expression. CSP Article 14j-n restricts participation in activities that include the advancement of human and democratic rights, the promotion of equality of nations and nationalities and peoples and that of gender and religion, the promotion of the rights of disabled and children’s rights, the promotion of conflict resolution or reconciliation and the promotion of the efficiency of the justice and law enforcement services to Ethiopian Charities and Societies.¹⁴

In January 2006, **Russia** enacted the Russian Federation Law on Introducing Amendments to Certain Legislative Acts of the Russian Federation (the 2006 Russian Non Commercial Organisations (NCO) Law). The 2006 Russian NCO Law introduced burdensome registration and reporting requirements for NCOs, accompanied by severe penalties for non-compliance. In July 2012 a bill *Introducing Amendments to Certain*

¹² See “How the FATF Is Used to Justify Laws That Harm Civil Society, Freedom of Association and Expression” available on the Charity and Security website at http://www.charityandsecurity.org/analysis/Restrictive_Laws_How_FATF_Used_to_Justify_Laws_That_Harm_Civil_Society#Bahrain.

¹³ ICNL, NGO Law Monitor, Venezuela available at <http://www.icnl.org/research/monitor/venezuela.html>.

¹⁴ ICNL, NGO Law Monitor, Ethiopia available <http://www.icnl.org/research/monitor/ethiopia.html>.

Legislative Acts of the Russian Federation Regarding the Regulation of Activities of Non-commercial Organizations Performing the Function of Foreign Agents was signed into law. The law requires all NCOs to register in the registry of NCOs, which is maintained by the Ministry of Justice, prior to receipt of funding from any foreign sources if they intend to conduct political activities. Such NCOs are called “NCOs carrying functions of a foreign agent.” NCOs are required to report on their use of funds and other assets received from both foreign and local sources. Foreign or international organizations wishing to make tax-exempt grants to Russian citizens or NCOs must be on a list of organizations approved by the Russian Government; access to this list is severely limited. Public associations (PAs) are required to submit information about the funding and property they receive from foreign and international organizations and foreign persons to the registration authority. Repeated failure on the part of a PA or an NCO to provide the information required in a timely fashion is grounds for the registration authority to bring a claim in court requesting a ruling that the organization terminate its activities as a legal entity, which then leads to its exclusion from the Unified State Register of Legal Entities.¹⁵

The **British Virgin Islands’** (BVI) proposed Non-Profit Organizations Bill seeks to register and monitor the operations of all non-profit organizations in the BVI. Proponents of the bill explicitly linked passage of the bill to meeting the recommended standards of the FATF. In October 2012, the Minister of Health and Social Development told members of the BVI’s House of Assembly that adopting the bill would make the country more likely to be compliant with FATF standards in future assessments. The preliminary language to the Bill also states makes that point.

Sections of the proposed bill of concern for non-profit organizations include:

- the annual registration of all nonprofit organizations. The definition of a “nonprofit organization” includes a “body of persons” promoting “social purposes.” Under Section 11(2), the penalty for failing to register is “a fine not exceeding fifty thou-

¹⁵ ICNL, NGO Law Monitor, Russia, <http://www.icnl.org/research/monitor/russia.html>.

sand dollars or imprisonment for a term not exceeding three years, or both.”

- the obligation to appoint a Money Laundering Reporting Officer (MLRO) for all NPOs with a staff of three or more people. In addition nonprofits with less than three employees are required to “perform the Money Laundering Reporting Officer functions” though they need not appoint a MLRO. Under Schedule 3 of the bill, fines range from \$3,000-\$30,000 (including a \$5000 for “failure to maintain any records required to be maintained.”) This issue was a particular concern to smaller non-profits, including those with all-volunteer staff.¹⁶

The above, by no means exhaustive, list of examples provides a flavour of the type of legislation that is being passed in different regions around the world and that affect the financing and expenditures of NPOs. Particularly the pre-approval of foreign funding is very widespread. It is important to emphasize that these are not separate incidents as it were coincidentally occurring together— they are part of a larger development pushing back against civil society.

III. FATF and Recommendation 8 on NPOs

The question here is to what extent this development is due to counter terrorism financing legislation. What are the international standards on AML/CFT, who sets them and what do they have to say about civil society (Non-Profit Organisations as they are referred to by FATF)?

The Recommendations

The FATF is an inter-governmental body established in 1989. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.

It issued its first version of “the 40 recommendation against money laundering”

¹⁶ As reported in issue brief #7, May 2013, of the Charity and Security Network, p 5, available at

in 1990— which has since been revised several times. In October 2001, shortly after the 9/11 attacks, FATF issued the Special Recommendations (SR) against Terrorism Financing eight, supplemented two years later by a ninth recommendation). Those two sets of recommendation have become the global standard against money laundering and terrorism financing. In February 2012, after three years of negotiation, the FATF adopted a latest version of the “Recommendations against Money Laundering and Terrorism Financing.”

As standards, the Recommendations are the outcome of negotiations between ministries, regulatory agencies and financial intelligence units of FATF member countries. They form the basis for national action on AML/CFT and are endorsed by almost all countries in the world.¹⁷ To be clear: the Recommendations are not a treaty and do not require legislative approval. However, through a process of evaluation by fellow members, national legislative and regulatory action is monitored closely, and countries that fall short may be subjected to being publicly listed for having “strategic AML/CFT deficiencies” or not having sufficient political commitment to AML/CFT.¹⁸ Being named publicly may in turn affect a country’s ability to receive payments from abroad (or at least the time within which such payments are received).¹⁹ Being listed or the threat of

<http://www.charityandsecurity.org/system/files/Bad%20Laws%20Issue%20Brief.pdf>.

¹⁷ FATF itself consists of 34 members-32 countries (mostly members of the OECD and important regional economies) and two regional organisations (the EU and the Gulf Cooperation Council). In addition there are so called FATF Style Regional Bodies (FSRBs) covering the Caribbean (CFATF), Latin and Central America (GAFISUD), Central and Eastern Europe (Moneyval), the Middle East and North Africa (MENAFATF), Western Africa (GIABA), Eastern and Southern Africa (ESAAMLG), Central Asia (the Eurasian Group), and the Asia Pacific (APG). An FSRB for Central Africa (GABAC) is in the process of obtaining recognition as an FSRB, leaving at present only Cuba, Iran, North Korea and Somalia as not subscribing to the FATF recommendations.

¹⁸ Concretely what happens is that countries with a low rating on certain “key or core” recommendations end up being reviewed by the “International Cooperation Review Group” which may in the end decide to name the country publicly for having strategic AML/CFT deficiencies. It should be emphasized here that the recommendation on Non-Profit Organisations, currently Recommendation 8, is not part of the “key and core”, and thus is not relevant for this process. See also the comment by the Bangladeshi official cited earlier.

¹⁹ This is based on the theory that a country listed publicly by FATF will move to the “high risk” category in any financial institution, and as a consequence the financial institution will conduct more due diligence before any payment to that country is executed, which in turn would cause a delay. Though indeed financial institutions do tend to categorize a country to a “high” or “higher” risk following a public statement by FATF- I am not aware of any research or systemic review that confirms that delay in payments. One country claimed to me that its listing by FATF under the previous process had caused the interest rate on its bonds to rise- but again I am not aware of any objective confirmation of this claim. Only to say: it is possible that the

being listed, will generally spark considerable national legislative and regulatory action to come off the list or avoid being listed. Thus, while the recommendations can in no way be said to constitute international law, they are a remarkably effective form of “soft-law”—effective that is, from the point of view of the national legislative activity they generate.

The 2012 version consolidated the previous two sets of ML and TF specific recommendations into one and revised certain substantive rules. The most significant shift in the recommendations as a whole is the extent to which the concepts of risk and, in its wake, effectiveness, now permeate the new standards and inform all government action on AML/CFT.

Remarkably the substance of the special recommendations against TF, including on NPOs, was left untouched. New Recommendation 8 (previously SR VIII) obliges countries to review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism and ensure that NPOs cannot be misused by terrorist organizations posing as legitimate entities, conduits for terrorist financing, or to conceal the clandestine diversion of funds intended for legitimate purposes to terrorist organizations. In the Best Practice Paper (BPP) that followed shortly after the Special Recommendations were issued, FATF underlined the need to

safeguard and maintain the practice of charitable giving and the strong and diversified community of institutions through which it operates whilst advocating a number of measures focusing on financial transparency, programmatic verification, and the administration of NPOs.²⁰

Because the broad and general language of the Recommendation leaves a lot of room for interpretation without stipulating what precise measures countries are to be taken an Interpretive Note (IN) was adopted in 2006 to define what constitutes an NPO

effects of being listed or named are exaggerated.

²⁰ FATF, International Best Practices Combating the Abuse of Non-Profit Organisations, 11 October 2002, par 5, accessible at <http://www.fatf-gafi.org/media/fatf/documents/recommendations/11%20FATF%20SRIX%20BPP%20SRVIII%20October%202003%20-%20COVER%202012.pdf>.

and what exactly is required under this Recommendation (and again, the content of the IN was not affected by the recent revision of the standards).

NPOs and Supervision

The IN defines an NPO as

a legal entity or organisation that primarily engages 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.’²¹

Countries should be able to demonstrate that for NPOs that account for a) a significant portion of the financial resources under the control of the sector and b) a substantial share of its international activities certain supervisory measures are in place. This echoes the BPP, which states that

small organisations that do not raise significant amounts of money from public sources and locally based organisations or organisations whose primary function is to redistribute resources among members may not necessarily require enhanced government oversight.²²

In limiting the scope in this way, FATF is applying a risk-based approach, focusing its efforts only on those institutions that are presumed to pose a potential risk. Whether it is thus targeting the right group is a matter for debate— there may be a different range of risk factors that is relevant.

The specific supervisory measures focus on the transparency and accountability of an NPO. Relevant information on the identity of the NPO’s management and owners, and on its objectives should be publicly available. NPOs should have internal controls ensuring their spending is in accordance with the purpose and objective of the NPO and maintain records of domestic and international transactions. They should also make a best-efforts attempt to confirm the identity, credentials, and good standing of their beneficiaries and associate NPOs. Finally, they should be registered or licensed, subject to

²¹ See Interpretive Note to Recommendation 8 (Non-Profit Organisations) available at http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf.

²² See Best Practices Paper, par 5.

monitoring by appropriate authorities (which may include self-regulatory organizations), and subject to sanction for non-compliance.

Underlying the recommended action appears to be the idea that ensuring transparency of financial flows and, to the widest extent possible, the *bona fides* of all those in any way associated with the NPOs will allow for early detection by competent authorities of possible instances of TF by NPOs. In addition, it may provide useful information to those investigating NPOs once they are under suspicion.

Narrow Focus

It is important to repeat the point about the restricted scope of the supervisory measures. FATF defines the NPO as a **legal entity or organization** (i.e., excluding the many informal organizations that under many definitions would qualify as an NPO) that **primarily engages in raising or disbursing funds** (i.e., excluding advocacy organizations and many others active in the expressive field) for charitable purposes. Having thus excluded a substantial part of what is commonly considered to constitute the nonprofit sector, the supervisory measures are then further limited to those organizations accounting for a **significant portion of the financial resources** and a **substantial share of the sector's international activities**. In other words the supervisory measures apply to a subset of a subset of what most countries would regard as their nonprofit sector. As shown elsewhere, for England and Wales one could convincingly argue that the supervisory measures apply to only 6.3% of the total number of registered charities.²³

IV. Is “Philanthropic Protectionism” Due To FATF?

It will be clear from the examples cited and the overview of the standard, that much of what countries have been doing to impose limitations on their civil society sector, is not contemplated in Recommendation 8 or the IN. Recommendation 8 does not tell countries to put in place measures to approve all foreign funding, or not accept cash or to appoint money laundering reporting officers. Thus it could be argued, as some do,

²³ See my earlier paper on this topic “Nonprofit Organization and the Combatting of Terrorism Financing-A

that this is really none of FATF's concern, and that if countries want to clamp down on their civil society sector, they will do so, regardless of what FATF says or does. Not their problem— or is it?

Provide Clarity Give Guidance

For one, as was shown in the example, some countries adopt the legislation while explicitly citing FATF, Recommendation 8 or the need to counter the financing of terrorism. To what extent those references are only used for cover— to feign an international obligation while concealing an underlying authoritarian objective— and to what extent they are genuine misunderstandings, cannot always be determined. Certainly in the case of a country like the BVI, not exactly known for its dictatorial tendencies, the legislation is more likely based on confusion as to what the standard actually requires (possibly coupled with a lack of care about the non-profit sector) rather than an intention to stifle non-profit organisations. From personal experience I have found that frequently officials responsible for AML/CFT in a country are not clear about what is required and more or less automatically assume that NPOs are basically to be dealt with in the same way as banks and other financial and non-financial institutions— i.e. that they need to identify suspicious transactions and report to the national financial intelligence unit (hence the appointment of money laundering reporting officers in the BVI). So, genuine misunderstanding about the content of the standard certainly seems to have at least led some countries to approach this topic in the way they have. It is important that FATF or the regional FATF-style body, give those countries guidance on what R8 actually says.

But even in cases where countries cynically use the FATF language as a way to legitimize their own more authoritarian ends, would it not be incumbent upon FATF to speak up— if only as it were to protect its brand?²⁴ It may not dissuade those intent on

Proportionate Response” p 9, available at issuu.com/world.bank.publications/docs/9780821385470/4.

²⁴ There was an acknowledgement of the problem at the FATF plenary meeting in October 2012, which resulted in a rather tepid comment in the Outcomes of the Plenary meeting that “It will be important that regulations and actions in this area [of Recommendation 8] do not harm the legitimate activities of such organizations [NPOs],” see <http://www.fatf->

clamping down on their civil society to change course, but at least it would take away their veil of legitimacy. In addition it would make it clear to the outside world where FATF stands on this issue. Some clarity is needed— also considering the emphasis that is often placed on the standards being “minimum” standards— meaning countries can go further (i.e. put more controls in place). That, and the fact that the language of the interpretive note leaves a lot of scope for countries to determine how to address possible vulnerabilities, mean that it is all the more important that FATF state clearly what the standard says— and what it does not say. A simple one pager on its website stating what measures are *not* contemplated by Rec 8 could be a practical way to deal with the issue.

Clarity is also sorely needed on the topic of what qualifies as an NPO that is subject to the recommendations. As pointed out, the standard is supposed to apply to grant makers and service oriented (i.e. humanitarian and aid) organisations, not to democracy promoting and advocacy organizations. That focus was further underscored by a recent typology study²⁵ on the use of NPOs for terrorist purposes which found that out of 102 cases that it reviewed in which an NPO had (allegedly) been used for TF purposes, the NPO in question was a service oriented NPO. No instances were found of the involvement of an “expressive” (i.e. one focused on advocacy or democracy building) NPO. Similarly the Transnational NPO Working Group on FATF, a coalition of NGOs, noted that Humanitarian and Development NGO’s reported abuse²⁶ more often than human rights defenders or peace builders.²⁷ But, as *The Economist* recently noted “NGOs focused on democracy building or human right are most affected (...)”²⁸ by the recent clamp down on civil society— which stands to reason if the proposition that much of

gafi.org/topics/fatfgeneral/documents/outcomesofthepenarymeetingofthefatfparis17-19october2012.html.

²⁵ FATF undertakes regular studies of money laundering or terrorist financing trends that typically focus on certain ways in which money is laundered or terrorist groups are financed, referred to as typology studies. For this recent report see “Risk of Terrorist Abuse in Non-Profit Organisations,” available at <http://www.fatf-gafi.org/media/fatf/documents/reports/Risk-of-terrorist-abuse-in-non-profit-organisations.pdf>.

²⁶ It should be pointed out that abuse in that paper is more widely defined as attacks on personnel, theft, robbery or unauthorized actions by employees- i.e. not necessarily linked to terrorism.

²⁷ See Annex III- NPO Sector Risk and Risk Mitigation Survey Analysis of the Transnational NPO Working Group on FATF Recommendations: Financial Action Task Force Typology Review, p14, available at <http://www.hscollective.org/wp-content/uploads/2014/08/NPO-Sector-Typology-Position-Paper-FATF-1.pdf>.

²⁸ Economist magazine, September 13th, “Foreign funding of NGO’s, Donors: keep out.”

that government action is motivated by the desire to stay in power, is correct. Why try and hamper the operations of foreign aid organisations, if one is worried about the spread of dangerous ideas about freedom?

Now, that mismatch between those organizations that are the target of many of the restrictive measures imposed and the NPOs that are the subject of the FATF recommendations, is in itself possibly an indication that again, the FATF Recommendations are not the root cause of the “closing space,” but it would be helpful if that point, hidden under a lot of legal language and hard for any outsider to follow, could be made more succinctly. Not only outsiders find this point difficult, even the insiders tasked with evaluating countries on compliance with Recommendation 8, do not typically discuss this issue in a country evaluation, or fault countries for applying the measures too widely. There is, however, a possibility that that might change in future evaluations.

Focus On Risk

As noted earlier, the biggest change between the earlier set of FATF recommendations and the latest version is the current focus on country risk as the starting point for the design of any AML/CFT measures. Although the recommendation on non-profits itself has not changed, the overarching importance of country risk puts each individual recommendation in a new perspective. The merit of a country’s rules and regulations to control money laundering and terrorism financing is determined by the extent to which a rule addresses an identified risk. In fact, without wanting to go into too much technical detail, there is now one whole part of the country assessment that deals only with *effectiveness*, which is directly related to risk.²⁹ A rule is effective to the ex-

²⁹ Under the previous methodology for assessing compliance with the 40 plus 9 recommendations, assessors were required to evaluate the formal compliance with the recommendation being evaluated and at the end would add some wording on the “effectiveness” of that recommendation- e.g. one might first review to what extent a country’s legislation criminalized money laundering in the correct way and review all the elements of the offence, and then end with a brief paragraph that indicated how many cases of money laundering a country had brought, and how many convictions, and then conclude, based on those numbers, to what extent a country had been “effective” on money laundering. The problem with that approach was that there wasn’t really a benchmark to assess against- what do the numbers really mean? Are they addressing their biggest risks when they’re prosecuting money laundering? So, to provide that framework and start evaluating effectiveness in a more structured way, the evaluation procedure has now been divided into two- the first

tent that it mitigates a certain risk and thus achieves a certain predetermined outcome. The relevant outcome for NPOs (outcome 10) says that “Terrorists, terrorist organisations and terrorist financiers are prevented from raising, moving and using funds and from abusing the NPO sector.”

In the criteria to assess whether this outcome is being achieved, assessors are to consider “to what extent, without disrupting legitimate NPO activities, has the country implemented a targeted approach, conducted outreach and exercised oversight in dealing with NPOs that are at risk from the threat of terrorist abuse.”³⁰ Thus assessors now have a way to take into account any rule that is imposed to ostensibly further AML/CFT objectives that may adversely affect NPOs operations. Previously, this was not possible. The Best Practice Paper recognizes the valuable work that the charitable sector does and says that “it is important that regulations and actions in this area do not harm the legitimate activities of non-profit organisations” but does not go any further in articulating the harm or providing guidance to assessors. It could be useful if guidance on this topic were provided to assessors— both on the way in which AML legislation may negatively affect NPOs and on the manner in which the consequences can be avoided. This is particularly relevant considering that many who evaluate this recommendation tend to be AML/CFT specialists- not necessarily experts on the charitable sector. That guidance could be part of the training of assessors that is conducted by FATF and FATF-Style Regional Bodies and should be developed in close cooperation with the civil society sector.

Equally importantly though, assessors will need to evaluate whether a country has implemented a “targeted approach”— which means that a determination of risk

part purely formal technical compliance- to what extent do a country’s laws and regulations reflect the content of the 40 recommendations- and the second part an effectiveness assessment which assesses to what extent a country is in practice effectively fighting money laundering and terrorism financing. 11 different building blocks are deemed to make up an effective regime, and for each of these building blocks - referred to as “immediate outcomes”- a separate assessment is made. For the FATF Methodology for assessing technical compliance with the FATF recommendation and the effectiveness of AML/CFT systems, see <http://www.fatf-gafi.org/topics/fatfrecommendations/documents/fatfissuesnewmechanismstostrengthenmoneylaunderingandterroristfinancingcompliance.html>.

³⁰ Immediate Outcome criterion 10.2 in the FATF Methodology for assessing technical compliance with the

needs to precede any measures that affect the NPO sector. Whereas the Best Practice Paper adopted in 2002 already recognized that “Government oversight should be flexible, effective, and proportional to the risk of abuse,”³¹ the proportionality of legislation, whether the measures in effect address the risk, was never assessed. That is different now. Risk cannot be assumed—it must be demonstrated. This means that it is up to countries to conduct a fully-fledged risk assessment of their non-profit sector— as also prescribed in Recommendation 8. Given the dearth of cases in most countries of NPO involvement in terrorist financing cases this is a difficult undertaking. The temptation to generalize based upon one or two available cases and have done with it is strong. That urge should be resisted, however. What is needed is a nationwide discussion between law enforcement, charities regulators, the sector itself, possibly tax- authorities and financial and other intelligence bodies to discuss where the vulnerabilities are, what channels are being exploited and where, in terms of geography and area of operations, potential risks are materializing. That discussion tends to be difficult, and very time-consuming but it’s only in having that discussion that a country can truly be said to have demonstrated that it is serious about AML/CFT.

This really gets to the heart of the debate on this and many other AML/CFT related topics: are countries imposing rules on their private and non-profit sector because an international organization is telling them to, which to some degree absolves those drafting the rules of the obligation to reflect too deeply upon the intent behind those rules, or are they doing it because they have examined their environment closely and come to the well informed conclusion that certain threats are not being addressed?

To some extent that same attitude of proper reflection is required from the assessor evaluating the country, at least when evaluating effectiveness: not a simple review of whether a law has been passed or a rule is in place, but a considered judgment on whether a country’s rules make sense given the risk profile.

As noted earlier, that risk profile has been predetermined in the interpretive

FATF recommendation and the effectiveness of AML/CFT systems.

note where FATF says that the supervisory measures outlined should cover “NPOs that account for a significant portion of the financial resources under control of the sector and a substantial share of the sector’s international activities.” Whether those NPOs are indeed most likely to be involved in terrorism financing is a matter for debate. Is it really likely that those types of NGOs with large scale international operations such as World Vision and the Bill and Melinda Gates foundation are most at risk for terrorism financing? Is it not rather the small informally organized outfits, with little public visibility in donor countries, that are more at risk? One should be careful with untested assumptions of course, but to predetermine the category that requires supervision for all countries, would appear to fly in the face of the risk based approach which is being advocated. Possibly a targeted approach would lead a country to conclude that that part of the sector does not require oversight. It would be an unfortunate result if strict adherence to the standard as written were to preclude such a conclusion— and ultimately it would render the system less effective. Although the FATF is unlikely to re-open discussion on the content of the standard any time soon, the practice of country evaluations tends to generate its own form of “case-law.” A systematic focus on the type of NPOs that are being made subject to national AML/CFT regulations, and a discussion of the rationale for doing so under the effectiveness assessment, should help in highlighting this point. And here one should bear in mind that FATF is not a monolith— it is made up of different member states and observers, represented by persons who, at times, because of their specific expertise or authority, can table points for discussion and exert influence. It is in that way that progress is made and new precedents are set. In addition, while FATF is the standard setter, the regional bodies in all parts of the world conduct their own evaluations— again offering a platform for shaping this debate.

Financial Exclusion

Quite apart from what can be done in the context of a country assessment, it is important that FATF communicate to the outside world in a measured way on this is-

³¹ See Best Practices Paper p 2.

sue. It is the type of general statement that “terrorists and terrorist organisations exploit the NPO sector” that has recently led financial institutions to terminate their relationship with charities (or at least provided partial cover for doing so). The phenomenon, referred to by the euphemistic term “de-risking,” is widespread and deserves serious consideration. In the earlier mentioned letter of the NPO sector to FATF in relation with the typologies exercise, the NPOs note that more than half of the respondents to their questionnaire had experienced problems with access to banking services. Over half had international fund transfers delayed and/or denied and 34% of grant makers that responded had had accounts frozen by a bank. While the statement that terrorists exploit the NPO sector is accurate in the sense that there are instances of terrorists using non-profit organisations, it is precisely the use of the turn of phrase “exploit the NPO sector” that triggers the type of response from the financial sector. In the wake of the recent spate of hefty fines imposed for breaches of sanctions and AML/CFT legislation, it can come as no surprise that any relationship with a party which according to the international standard setter is particularly vulnerable to terrorist financing abuse (and a not very profitable relationship at that) is the first to be “de-risked.” That not only creates a further impediment for the NPO in question to carrying on its legitimate activities— it also increases the use of *informal* financial channels.

As FATF recognized in the guidance on financial inclusion published last year, together with the Asia Pacific Group on Money Laundering and the World Bank:

The promotion of formal financial systems and services is central to any effective and comprehensive AML/CFT regime. However, applying an overly cautious approach to AML/CFT safeguards can have the unintended consequence of excluding legitimate businesses and consumers from the formal financial system.³²

It is in its interests then, as well as that of the NPO sector, to make sure that NPOs remain able to use the formal financial system and are not excluded.

³² See FATF GUIDANCE, Anti-Money Laundering and Terrorist Financing Measures and Financial Inclusion, p5 available at http://www.fatf-gafi.org/media/fatf/documents/reports/AML_CFT_Measures_and_Financial_Inclusion_2013.pdf.

In the context of country assessments, the financial exclusion argument could also give assessors a way of discussing legislation that does not have AML/CFT as its objective but that does affect the NPO sector (such as some of the country examples cited at the beginning). Where overly stringent legislation ends up affecting NPOs' access to financial services, that can in itself (regardless of the objective of the legislation) be a reason for criticising a country.

Quite apart from the necessity to be specific in communicating about NPOs involvement in terrorism financing, it may be good to balance that language with more positive messages- about the role that NPOs play in addressing the so called "conditions conducive to terrorism." As is recognized in the Best Practices Paper: "NPOs can also play an important role in preventing the causes of radical ideology from taking root and are, therefore, potential allies in the fight against terrorism." It would stand to reason then, that something could be made out of this potential alliance and that any dialogue between FATF and the NPO sector be not only focused on potential risks in the NPO sector but also include a discussion on how NPOs and FATF could work together in the fight against terrorism. That is already happening to some extent in the anti-corruption field, where CSOs are invited to participate in FATF's private sector forum and put forward ideas on how to achieve greater transparency in financial flows possibly related to corruption and organized crime. There may be merit in exploring to what extent NPOs could actually play a role as a partner and provider of ideas, rather than merely as being a potential risk. A start was made in forging that type of discussion with a meeting in March 2013 between FATF and a coalition of different civil society organisations. That debate deserves to be continued and institutionalized, in the interests of both parties.

V. Beyond ATF

All these are valuable ideas- and worth exploring further- but there is only so much that can be done within the framework of FATF, or the wider "FATF family" (its members, observers and regional bodies) itself. The more fundamental issues transcend

its specific and technical framework. They are political in nature and need to be resolved at that level.

Freezing of Terrorist Assets

One of the terrorist financing related requirements that has possibly affected NPOs more than others, is the obligation on countries to freeze the assets of individuals or organisations that are determined by the UN Security Council’s Sanction Committee to be “associated with” Al Qaida or the Taliban. Though this is also a FATF Recommendation (Recommendation 6), it is in fact no more than a restatement of a UN Security Council resolution (UNSCR 1267 and following resolutions) and as such it can be said to properly constitute international law-binding upon UN member states pursuant to Chapter VII of the UN Charter. In addition, UN Security Council Resolution 1373, adopted shortly after 9/11, obliges countries to freeze terrorist assets (again this requirement is further reinforced by FATF Recommendation 6). That obligation has been interpreted as constituting an obligation to put in place a system to administratively designate persons or entities as “terrorists” or “terrorist organisations,” and upon such determination freeze all their assets.

The legitimacy of the UN designation system has long been called into question by commentators and legal scholars— and since 2008 they have been joined by the European Court of Justice, the court of the European Union, based in Luxembourg. In a landmark ruling,³³ while ostensibly faulting another EU body (the Council), the ECJ in fact delivers a blistering verdict on of the way in which the UN Security Council has listed persons without regard to due process— notably the right to effective judicial protection and the right to be informed of the evidence as well as the fundamental right to respect for property— and declares the designation invalid. It is a very symbolic step- a regional court telling off the world’s highest body responsible for peace and security. A

³³ Joined Cases C-402/05 P and C-415/05 P Yassin Abdullah Kadi and Al Barakaat International Foundation v Council of the European Union and Commission of the European Communities, Judgment of the Court (Grand Chamber), 3 September 2008, available at http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?ELX_SESSIONID=v1J8Jz1JyG2qGypPBydnpXHXzGk1BGYCVqhpvXHtnp952hsQwJK2!1996567712?isOIdUri=true&uri=CELEX:62005CJ0402.

more recent ruling from the ECJ, while acknowledging some of the improvements to the designation system, substantively confirms the 2008 decision.³⁴ The debate is about much more than technicalities about the exact extent of permissible limitations on certain human rights: it is about the fundamental question of whether we allow safety and security to become the ultimate goal/objective to which all other goals must be made subservient. It is, in a way, a restatement of the earlier point made about proportionality: as a (Western, free) society are we rationally justified in allowing safety to become the measure of all things, in the face of the real possibility of a terrorist attack? Or are we overreacting?

“Safety Is a Fine Thing, but As an Obsession It Rots the Soul”³⁵

In his dissenting opinion on the compatibility of section 23 of the UK’s Anti-terrorism, Crime and Security Act 2001 (indefinite detention of foreign prisoners without a trial), with the European Convention on Human Rights, Lord Hoffman famously stated:

Terrorist violence, serious as it is, does not threaten our institutions of government or our existence as a civil community. (...) The real threat to the life of the nation, in the sense of a people living in accordance with its traditional laws and political values, comes not from terrorism but from laws such as these. That is the true measure of what terrorism may achieve. It is for Parliament to decide whether to give the terrorists such a victory.³⁶

His was a dissenting opinion however, and the majority of the Court disagreed on this

³⁴ Joined Cases C-584/10 P, C-593/10 P and C-595/10 P, Judgment of the Court (Grand Chamber) 18 July 2013, available at <http://curia.europa.eu/juris/document/document.jsf?text=&docid=139745&pageIndex=0&doclang=en&mode=req&dir=&occ=first&part=1&cid=1914364>. Even if it did overturn part of the Grand Chamber’s reasoning, it affirmed that the ECJ will continue to review EU listings implementing strict Security Council obligations in the face of lack of equivalent control at UN level, and insisted on a rather strict standard of review of such listings, and undertook—for the first time—substantive review of the reasons for listing offered by the EU (which were in fact merely those offered in the ‘narrative summary of reasons for listing’ that the Security Council released). See Blog of the European Journal of International Law available at <http://www.ejiltalk.org/kadi-showdown/>.

³⁵ Jack Gordon, *Milksop Nation*, winner of the Economist/Shell Writing Prize 2002, available at <https://www.scribd.com/doc/33754/Milksop-Nation-Jack-Gordon>.

³⁶ See the Dissenting opinion of Lord Hoffmann, in *A and others v Secretary of State for the Home Department* [2004] UKHL 56, par 96-97 available at <http://www.bailii.org/uk/cases/UKHL/2004/56.html>.

point.³⁷

In the US, the Supreme Court ruled in 2010 that it was constitutional to prohibit a group of humanitarian legal professionals (including a retired U.S. judge) from engaging in training members of a designated terrorist organization to use international law to resolve disputes peacefully or teaching those members to petition the United Nations and other representative bodies for relief because such activities constitute “material support to a terrorist organization.”³⁸ It is hard to square that with the overarching aim of sanctions legislation which is to effect a change on the part of the sanctioned individual, organization or state³⁹— but that is another matter. The point here is to show how the concept of supporting terrorism has been steadily expanding and the concomitant limitations on people actions.⁴⁰ Three Justices dissented.

Though the cases are different of course and taken at different times and one should be cautious drawing conclusions on the basis of only two instances, it would appear (based on what one hears and reads in media and on-line) that the rulings in the US and UK cases are still an accurate reflection of the populations’ (in those and indeed most countries) acceptance of the logic of security and safety as subordinating all other public goods. Intellectuals and civil society organisations may disagree and a few judges may dissent— they are a minority. The ECJ’s rulings are the odd one out. Considering the recent actions of ISIS and the Al-Nusra front in Syria and Iraq, Boko Haram in Ni-

³⁷ But struck the relevant part of the law down nonetheless on the basis that is discriminated between foreigners and UK citizens- as long as UK citizens could also be held indefinitely all was well.

³⁸ See Holder, Attorney General, et al. v. Humanitarian Law Project et al. no. 08–1498. available at <http://www.supremecourt.gov/opinions/09pdf/08-1498.pdf>.

³⁹ Indeed in the UN context, the Al-Qaida and Taliban Monitoring Team which supports the work of the UN Security Council in the designation of individuals and entities as being “associated with” Al-Qaida or the Taliban, explicitly recognizes the logic of de-listing for those who have renounced terrorism or otherwise demonstrated that they no longer deserve to be listed (Second report of the Analytical Support and Sanctions Monitoring Team appointed pursuant to resolution 1526 (2004) concerning Al-Qaida and the Taliban and associated individuals and entities. The sanctions (designations) are not punitive in nature, but intended to bring about a change in behavior of art 39 and 41 of the UN Charter. Once that change has been effected, the sanction can be lifted.

⁴⁰ For a more detailed discussion of this development see OMB Watch, Grantmakers without Borders “Collateral Damage, How the War on Terror Hurts Charities, Foundations and the People they Serve”, chapter 2 “The Continuously Expanding Interpretation of What is Prohibited” available at http://www.charityandsecurity.org/studies/Collateral_Damage.

geria and Cameroon and Al Shabaab in Kenya and Somalia, and the extent to which these actions have dominated the media and driven public debate, it is unlikely that that logic is going to change any time soon— or rather that governments are going to re-evaluate their priorities. For the foreseeable future we will continue to be cautioned to ask our fellow travellers on public transport “Is that your bag?” for fear that it contain an explosive. It may seem trivial— but it reveals a lot about the place we have allowed safety to occupy in our daily lives: a bag is no longer just a bag, it is a potential threat. Until such time as a recalibration of the place of security in our hierarchy of values becomes possible, NPOs room for manoeuvre will be constrained within the confines of this logic. To be clear: this is not to disparage the problem posed by terrorism or to imply that we should not try and make sure that terrorists do not have access to funds or material support. It is about calling into question the nature of our response and the prominence we attach to it.

In a report from the Fourth Freedom Forum and Kroc Institute for International Peace Studies at the University of Notre Dame, the authors note in reviewing the UN’s Global Counter Terrorism Strategy that

While [it] is an improvement over approaches that are focused narrowly on security, it can be interpreted as subordinating development and human rights imperatives to the logic of security.

Development and human rights are critically important in their own right (...) and should be supported fully without reference to other priorities.⁴¹

Ultimately then, what may be more important in the long run, is to have that debate about that logic itself and the limits and trade-offs it imposes to be able to return safety and security to their proper place.

⁴¹ Friend not Foe, *Opening Spaces for Civil Society Engagement to Prevent Violent Extremism*, 2nd Edition, May 2011, David Cortright, with Alistair Millar, Linda Gerber- Stellingwerf, George A. Lopez, Eliot Fackler and Joshua Weaver available at <http://www.hscollective.org/wp-content/uploads/2013/09/Friend-not-Foe-2.pdf>.

Nonprofit Organizations and the Combatting of Terrorism Financing

A Proportionate Response

Emile van der Does de Willebois



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Executive Summary

One of the ways that terrorist organizations raise and transfer funds is by using the fundraising power, and the aura of charitable activity, of nonprofit organizations (NPOs). Ever since the adoption of the Special Recommendation VIII on the abuse of NPOs Terrorism Financing purposes by the FATF in October 2001, countries have struggled to find a proper way to address the potential terrorism financing risk posed by NPOs. The issue at stake is to strike a balance between addressing a potential threat and ensuring NPOs have the freedom to operate. In many important ways, the work of NPOs deal with the conditions conducive to the spread of terrorism; therefore, it is essential that in trying to address one aspect of the terrorist threat—terrorism financing—we do not inadvertently diminish the impact of other ways of tackling the issue.

This article argues that, when discussing the threat and how to address it, policy-makers need to be specific and not paint the whole sector with the same brush. Virtually all governments already interact with the NPO sector in one way or another. These preexisting avenues should be used for dealing with this issue; it is inefficient and ultimately counterproductive to devise an entirely new regulatory framework. The ultimate objective is to enhance the transparency of the sector—to ensure information is available on the people in charge of NPOs, their sources of funds, and, particularly, the way those funds are spent. This aim serves a much wider purpose than just terrorism financing and touches on many aspects of good governance of civil society that the sector itself and others have been debating for a long time. When devising public policy on how to deal with possible terrorism financing through the nonprofit sector, the contribution of the NPO sector to fighting terrorism should be recognized and used to its full advantage. Moreover, the NPO sector's own stake in being "clean," and being regarded as such by others, should be acknowledged. NPOs are an indispensable partner in drawing up such policies. For the same reason, self-regulation should be considered.

List of Abbreviations

AML	Anti Money Laundering
BPP	Best Practice Paper
CFT	Combatting Financing Terrorism
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
IN	Interpretive Note
NPO	Nonprofit Organization
PVS	Partner Vetting System
SRO	Self-Regulatory Organization
SR VIII	Special Recommendation VIII
TF	Terrorism Financing
UN	United Nations

Foreword

Terrorism causes untold material, physical, social, and psychological damage. As individuals and as a society, people must stand up to the terrorist threat. People must not, however, allow it to change the way they live and make them give up freedoms they enjoy. Resilience and prudence are of the essence. This applies equally when society is confronted with instances of nonprofit organizations being used for terrorist purposes. People need to address this problem without allowing it to fundamentally alter their way of life. The development and growth of civil society, and its contribution to many aspects of daily life, is one of the great accomplishments of our age. As a voice for the oppressed; a provider of medicine, education, and humanitarian aid; an advocate for worker's rights; a promoter of the arts, cultural understanding, and, more generally, an awareness of "the other," civil society has been an enormous force for good. While crucial in many ways to daily life in the developed world, civil society is simply indispensable in the developing world where it provides services elsewhere provided by government, whether medical care or education. Without nonprofit organizations, large segments of the populations in developing societies would not go to school or receive medical treatment.

In some instances, the global networks of nonprofit organizations have been used as a channel to raise and divert funds towards terrorist causes. Of course, such abuse needs to be tackled head-on, and NPOs and governments must do all they can to ensure that the funds are used as intended. Care should be taken, however, that action to counter such abuse is targeted and does not harm the healthy functioning of the NPO sector.

As recommended in the report of the United Nations (UN) Counter-Terrorism Implementation Task Force on Tackling Terrorism Financing, published in 2009, "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." The World Bank recognizes the vital role of civil society in fostering development, but also realizes that safety and security are a prerequisite to development. As an international organization dedicated to the cause of development, the World Bank wishes to ensure that both objectives are fulfilled. The World Bank hopes this paper will provide a useful starting point for further discussion.

Consulate Rusagara
Director, FPDFS
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Introduction

The business of terrorism is fear and, in order to generate that fear, terrorism, like any other business, requires money. Money is required to buy safe-houses, to fund travel, to run training camps, to recruit new terrorists, to pay off officials, to procure weapons, to obtain false documentation and covers for sleeper cells, to promote the cause, and for many other ends. Those financial needs are met in different ways, drawing on both legal and non-legal sources. According to those at the forefront in combating terrorism financing (CFT), in particular the Financial Action Task Force against money laundering (FATF), one of the ways that terrorists obtain funds is through nonprofit organizations (NPOs). They draw upon examples of NPOs being used to raise, transfer, and divert funds for terrorist purposes.

The international community has taken various remedial measures in response. This paper aims to explain what lies behind the international action targeting NPOs and to clarify what the recognized international standard actually recommends in this respect—there is a lot of misunderstanding as to what is really required. This paper also discusses the issues involved in implementing or advising on CFT policy. It is important in taking action that countries do not overestimate the threat and that they are aware of all the possible consequences, even unintended ones. In many ways, the nonprofit sector of a country is a force for good and needs to be protected, rather than unnecessarily curtailed. Similarly, those who offer technical assistance to countries on this issue should advise and make recommendations that take into account possible adverse side effects of government action against NPO abuse. Applied in the wrong way, government measures can end up harming the NPO-sector and, ultimately, damage the wider counterterrorism effort.

After describing the types of cases mentioned in justification of remedial action and the rationale for specific measures recommended, this paper will attempt to highlight key issues surrounding regulation of NPOs for terrorism financing (TF) purposes and make some recommendations on how countries could sensibly deal with this question.

Examples of Abuse

The instances of abuse of NPOs for purposes of financing terrorism (TF) mentioned in FATF, government, media, academic articles, and documents cover NPOs raising, transferring, and disbursing funds for terrorist purposes. Below is a cross section of examples mentioned in justification of taking action.

NPOs Raising Funds for Terrorist Organizations

1. A number of religious groups in the countries A and B classified as charities and, therefore, entitled to tax-exempt status, raise funds for ostensibly apolitical projects in country C. In fact, significant sums go to causes controlled by members of a quasi-paramilitary body that is at the center of a protean network of front organizations. This structure facilitates arm's-length money-raising. Its arm in country A is a charity registered for nearly 30 years. Their appeal for earthquake victims raised more than 6 million USD.
2. In most countries with a significant diaspora population, members of an ethnic group established charitable organizations to raise funds for their causes. Although the charities solicited funds to assist civilians affected by the war, numerous inquiries, including investigations by intelligence services in country D, have found that a significant amount of the funds raised by charities were channeled to a designated terrorist organization for its military operations. The intelligence services of country D concluded that at least eight nonprofit organizations and five companies were operating in country D as fronts for the terrorist organization.

NPOs Transferring Funds for Terrorist Organizations

3. One of the most unlikely sources of Al Qaeda funding coming into the region was through the Foundation E based in the capital of country F. The foundation—which has offices in countries G,H, and I—was ostensibly established to address the needs of a small ethnic minority population in country F. Foundation E ran a school for grades 7–10 [...] Al Qaeda used the foundation for “significant money transfers” for both itself and for Jemaah Islamiyah. The foundation was believed to have laundered several million dollars for Al Qaeda; the school was receiving \$10,000 wire transfers each month in its account at a bank in country F.
4. An NPO with an office in country J came to the attention of the authorities through the submission of STRs by credit institutions on an apparent discrepancy between the stated objectives of the NPO and its actual expenditure. The NPO was also known to have a poor history of reporting to the authorities on tax issues. An investigation revealed that funds were being transferred from the NPO to apparently fictitious or shell entities and then being withdrawn in cash for onward transmission to illegal armed militants.

Diversion of Funds by Individuals or Branch Offices

5. Individuals, such as person K, are suspected of using NPO L and M, of which K is chairman, as vehicles to transfer large amounts of money to small radical groups. There is no evidence to suggest that person K is a member of Al Qaeda, but there is evidence that he has channeled funds to groups and organizations that have ties with Al Qaeda.”
6. “The office director for a nonprofit organisation in a beneficiary region defrauded donors from a donor region to fund terrorism. In order to obtain additional funds from the headquarters, the branch office padded the number of orphans it claimed to care for by providing names of orphans that did not exist or who had died. Funds sent for the purpose of caring for the non-existent or dead orphans were instead diverted to al-Qaida terrorists. In addition, the branch office in a beneficiary region of another nonprofit organisation based in a donor region provided a means of funnelling money to a known local terrorist organisation by disguising funds as intended for orphanage projects or the construction of schools and houses of worship. The office also employed members of the terrorist organisations and facilitated their travel.”¹

Complicit and Exploited NPOs

It may be analytically useful to draw a distinction between NPOs that act as a front for terrorist organizations and those that are being abused by others for nefarious purposes. This is, however, not the place to discuss the finer details of corporate liability and at what stage an act can be attributed to an organization. Suffice it at this stage to point out the difference between a “complicit NPO” (i.e., where it is acting as a front and the organization can be said to be involved in TF) and an “exploited NPO” (i.e., where it is abused by others). Of course, the line between the two will not always be clear, but it is important in determining remedial action. Within the category of exploited NPOs, one may be able to make a further distinction between those abused by outsiders and those abused by insiders. Stopping legitimate NPOs from being exploited by insiders may require a focus on their internal governance or financial controls. Abuse by outsiders may require improving access to information on partner organizations or beneficiaries. In the case of complicit NPOs, however, such action would not appear to address the problem.

It is unclear whether the majority of cases of the use of NPOs for TF purposes involve complicit or exploited NPOs. However, in its Best Practices paper, FATF states that: “*In certain cases* [author’s italics] the organisation itself was a mere sham that existed simply to funnel money to terrorists. However, *often* [author’s italics] the abuse of nonprofit organisations occurred without the knowledge of donors, or even of members of the management and staff of the organisation itself. . . .” This suggests that in FATF’s view, at least, the majority of cases involve exploited NPOs. This is in contrast to some of those in the sector who appear to hold that the issue relates predominantly to complicit NPOs (see footnote 29).

There are many examples similar to those given above, but it is important to put them into perspective. As a percentage of terrorist revenues or funding, funds collected or transferred by NPOs might be significant—since there are no reliable figures either on the scale of terrorism funding or on NPO contributions, this is obviously impossible to determine. Nevertheless, as a percentage of total NPO turnovers, the sums involved are surely not. By any reckoning, the NPO sector worldwide is vast, encompassing millions of entities with annual expenditures of over \$1.3 trillion²—even the highest estimates for annual terrorism income amount to only a fraction of that.³ In the United States alone in 2006, NPOs received \$1 trillion in revenue, and private giving (by individuals, foundations, and corporations) reached \$295 billion.⁴ Whatever sum of that is diverted towards terrorist

purposes, it is only going to amount to a fraction of a percentage of total NPO funds. As was also recognized by the government of the United Kingdom in its charitable sector review “the scale of terrorist links to the charitable sector is extremely small in comparison to the size of the charitable sector.”⁵

Notes

¹ Combating the Abuse of Non-profit Organisations, International Best Practices, Financial Action Task Force on Money Laundering, 11 October 2002, p 8, available online at <http://www.fatf-gafi.org/dataoecd/39/19/34033761.pdf>.

² Lester M. Salomon, S. Wociec and Associates, *Global Civil Society: Dimensions of the Nonprofit Sector*, vol. 2 (Bloomfield, CT: Kumarian Press, 2004), 15–16. This study, sponsored by Johns Hopkins University, only covers 36 countries; the real size of the global sector is larger.

³ The 9-11 Commission monograph on terrorism financing, still one of the most concise reports on the issue (not at the high end of the estimates), estimated annual Al Qaida funding at approximately 30 million USD per year (see National Commission on Terrorist Attacks upon the United States, Monograph on Terrorist Financing, p. 4, available online at http://www.9-11commission.gov/staff_statements/911_TerrFin_Monograph.pdf page 4).

⁴ See the press release on the *Nonprofit Almanac 2008*, “New Edition on Nonprofit Almanac Offers Detailed Portrait of an Expanding Sector,” The Urban Institute, available online at <http://www.urban.org/url.cfm?ID=901164>.

⁵ Review of Safeguards to protect the charitable sector (England and Wales) from Terrorist Abuse, Home Office and HM Treasury, December 2007, p16 online at http://www.homeoffice.gov.uk/documents/cons-2007-protecting-charities/Charities_consultation.pdf?view=Binary.

International Action

Special Recommendation VIII, the Best Practice Paper, and the Interpretive Note

Although many of the actual examples given above postdate the adoption of Special Recommendation VIII (SR VIII) on nonprofit organizations, it was with these types of cases in mind that FATF adopted it in October 2001 shortly after the attacks of September 11. The Special Recommendation states that countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism and ensure that NPOs cannot be misused by terrorist organizations posing as legitimate entities, conduits for terrorist financing, or to conceal the clandestine diversion of funds intended for legitimate purposes to terrorist organizations. In the Best Practice paper that followed, FATF underlined the need to “safeguard and maintain the practice of charitable giving and the strong and diversified community of institutions through which it operates whilst advocating a number of measures focusing on financial transparency, programmatic verification, and the administration of NPOs.”¹ The broad and general language leaves a lot of room for interpretation and does not stipulate what precise measures countries are to take. Consequently, in an attempt to provide clarification and after a long debate between its members, FATF issued an Interpretive Note (IN) in February 2006 to define what constitutes an NPO and what exactly is required under SR VIII. Both the text of the special recommendation, the Best Practice Paper and the Interpretive Note are included as an appendix to this paper.

The IN lists those characteristics that may render NPOs vulnerable to abuse:

- They enjoy the trust of the general public—implying that donors and government authorities may not be sufficiently vigilant in their dealings with NPOs.
- They have access to considerable sources of funds and they are often cash-intensive—implying that, as a matter of course, they move large amounts of money, and, when they deal in cash, do not leave a financial trace.
- They may have a global presence that provides a useful framework for national and international operations and financial transactions, often within or near those areas most exposed to terrorist activity—not by accident, these are often areas of humanitarian need.
- Depending on the legal form of the NPO and the country, NPOs may be subject to little or no governmental oversight, or few formalities may be required for their creation.²

An NPO is defined as “a legal entity or organisation that primarily engages 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.’”³

Taken together, the Special Recommendation, the IN, and the BPP recognize the vital role played by the NPO sector and that any measure taken to address the financing of

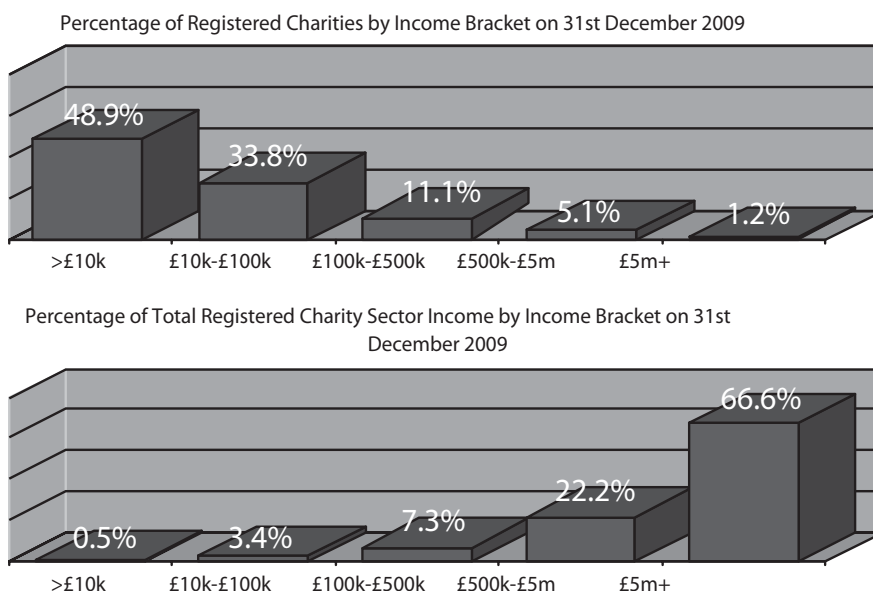
terrorism should not disrupt or discourage legitimate charitable giving. This is an important point that should be borne in mind by all those who deal with the issue—effectiveness of any measures adopted in implementation of SR VIII should also take into account whether measures taken have discouraged or disrupted legitimate charitable giving. The measures are as much about protecting the NPO sector against abuse as they are about identifying and targeting possible culprits. It recognizes possible tension that may exist between taking such action and charitable giving: “Action taken [to address terrorism financing] should to the extent reasonably possible avoid any negative impact on innocent and legitimate beneficiaries.” Government oversight should be “flexible, effective and proportionate to the risk of abuse. Mechanisms that reduce the compliance burden without creating loopholes should be given due consideration” (BPP). On the measures to be taken to prevent or detect such abuse, the IN says in general terms that they should promote transparency and engender greater confidence that charitable funds and services reach intended legitimate beneficiaries, both across the donor community and the general public. Specifically, this means: a) outreach to the sector, b) supervision or monitoring of the sector, c) effective investigation and information gathering, and d) effective mechanisms for international co-operation.

Of these four components, the second, supervision or monitoring, has proved to be most contentious and open to debate. Collectively, the measures proposed under this heading will be referred to as “supervisory measures.” The IN stipulates that countries should be able to demonstrate that a list of more specific standards apply to NPOs that account for a significant portion of the financial resources under the control of the sector and a substantial share of its international activities. This echoes the BPP, which states that “small organisations that do not raise significant amounts of money from public sources and locally based organisations or organisations whose primary function is to redistribute resources among members may not necessarily require enhanced government oversight.” In limiting the scope in this way, FATF is attempting to apply a risk-based approach, focusing its efforts only on those institutions that might pose a potential risk, thus minimizing any compliance burden. Whether it is thus targeting the right group is a matter for debate (see below); there may be a broader range of risk factors that is relevant.

The specific measures proposed as supervisory measures focus on the transparency and accountability of the NPO. Relevant information on the identity and background of the NPO’s management and owners, and on its objectives and financial statement, should be maintained and made available to appropriate authorities. NPOs should have internal controls ensuring their spending is in accordance with the purpose and objective of the NPO. They should also make a best-efforts attempt to confirm the identity, credentials, and good standing of their beneficiaries and associate NPOs. Finally, they should be registered or licensed, subject to monitoring by appropriate authorities (which may include self-regulatory organizations), and subject to sanction for non-compliance.⁴ Underlying the recommended action appears to be the idea that ensuring transparency of financial flows and, to the widest extent possible, the bona fides of all those in any way associated with the NPOs will allow for early detection by competent authorities of possible instances of TF by NPOs. In addition, it will provide useful information to those investigating NPOs once they are under suspicion, and it may prevent those planning to use NPOs for TF purposes from putting their ideas into action.

Before proceeding to discuss the arguments put forward by those who have criticized taking action against NPOs, it is important to repeat the point about the restricted scope of the supervisory measures. An example will illustrate this point.

FATF defines the NPO as a *legal* entity or organization (i.e., excluding the many informal organizations that under many definitions would qualify as an NPO) that *primarily engages in raising or disbursing funds* (i.e., excluding advocacy organizations and many others active in the expressive field⁵) for charitable purposes. Having thus excluded a substantial part of



Source: See Facts and Figures on the UK Charity Sector available online at http://www.charity-commission.gov.uk/About_us/About_charities/factfigures.aspx.

Note: The figures are based on the Annual Gross Income reported by charities in their Annual Returns. 7% of registered charities have not provided this information and are excluded from the figures. At an aggregate level the total income figures for all registered charities inevitably includes an element of double counting. Double counting arises when resources are transferred between charities and counted in both.

what is commonly considered to constitute the nonprofit sector the supervisory measures are then further limited to those organizations accounting for a significant portion of the financial resources *and* a substantial share of the sector's international activities. In other words the supervisory measures apply to a subset of a subset of what most countries would regard as their nonprofit sector. To show how much of a subset we are talking about, the following figures on the financial size of registered charities in 2009 in England and Wales may be illustrative.

As is clear from the above diagrams, 6.3 percent of the total number of registered charities (i.e., the total percentage from £500,000 upwards) accounts for almost 90 percent of the total revenue. When one takes into account the fact that there are a substantial number of non-registered charities at the low end of the scale⁶ (i.e., < £5,000) and that there are some charities at the high end of the scale that do not engage in international charity, the total percentage of interest to FATF for supervisory measures is even lower than 6.3 percent—obviously assuming that 90 percent of total revenues qualifies as “significant” for the purposes of FATF's IN.⁷ It is important to emphasize this point, since many who criticize the FATF action on this point appear unaware of it.⁸

Notes

¹ See the Financial Action Task Force on Money Laundering, “*Combating the Abuse of Non-Profit Organizations, International Best Practices*” available online at <http://www.fatf-gafi.org/dataoecd/53/53/34260889.pdf>.

² The U.K. Charity Commission adds to this that “charities are often engines for social change that attract people committed to making change happen and are powerful vehicles for bringing people together for a common purpose and collective action, and may inadvertently provide a ready-made

social network and platform of legitimacy for terrorists or terrorist sentiments.” See “Charity Commission, Counter Terrorism strategy” (July 2008), 5, <http://www.charitycommission.gov.uk/Library/investigations/pdfs/ctstext.pdf>.

³ A political party or a terrorist organization not being established for carrying out “good works” would not be covered by this definition.

⁴ A noteworthy omission is the absence of rules on the hiring of employees by NPOs. For exploited NPOs wishing to make sure they are protected against abuse, this is surely one of the most important issues.

⁵ The term “expressive” is derived from the distinction (see Salomon et al., *op. cit.*, 24) between nonprofit organizations that have a “service” function and those that serve an “expressive” function. It is used here to denote organizations that provide avenues for the expression of cultural, spiritual, professional, or policy values and beliefs.

⁶ All charities with an income over 5,000 GBP are obliged to register with the Charity Commission, whereas it is voluntary for those with a figure below this number.

⁷ Comparative data for other countries could not be found. Although the exact percentages for other countries will obviously be different, it is assumed that for the majority of developed countries—and thus of the FATF member countries—the ratios are similar, i.e., a small percentage earn the vast majority of total income.

⁸ As indeed many who evaluate application of SR VIII appear to be as well. A cursory review of evaluations undertaken by FATF and regional bodies demonstrates that many assessors who evaluate SR VIII do not take into account the fact that the recommendation addresses only a particular (limited) class of NPOs and rather evaluate the application of the measures proposed under SR VIII to the entire NPO sector rather than to the subset described above.

Criticism of International Action

The discussion will now proceed to objections to the type of measures discussed above and the assumptions underlying them. While not covering each and every criticism, it does represent a relevant cross section of the critique most frequently raised. Again, the arguments below are merely a reiteration of opinions as expressed in a wide variety of online journals and media, not necessarily an endorsement.

Harming the Sector and the Cause

In discussing the quality of the available literature on NPO abuse, a recent report commissioned by the European Commission noted that “the current concern about terrorism has not helped improve the quality of available information. Instead, it has tended to exacerbate the problem of journalistic and sensational media accounts of particular cases leading to a plethora of unwarranted inferences and inductions in the press.”¹ “Sensational media accounts” may affect more than only the quality of information.

Donor caution

Highlighting the possible links between charities and terrorism has not only affected NPOs themselves but also had an impact on the donor community. Since the criminalization of the financing of terrorism renders all those who knowingly contribute towards terrorist causes, directly or indirectly, liable to criminal charges, many donors have become more cautious about donating to those NPOs that operate in environments or countries associated with terrorist activity, fearing that they (i.e., the donors) might themselves be held liable of terrorism financing. Certainly, in the immediate aftermath of September 11, this resulted in a drop in donor funds. As testified by a U.S. official before a Senate Committee: “The larger balance [of the success of counterterrorism measures] is found in the wariness, caution, and apprehension of donors; in the renunciation of any immunity for fiduciaries and financial intermediaries who seek refuge in notions of benign neglect and discretion, rather than vigilance.”² Although it is difficult to estimate the drop in donor contributions since September 11, there is a belief that such a drop did occur. Muslim Charities in particular appear to have suffered a decline in funding.³

Use of FT rhetoric for other ends

In recent years, countries all around the world have introduced laws and regulations restricting operations of the NPO sector.⁴ Citing terrorism concerns, a number of governments have imposed restrictive legislation upon the NPO sector—not simply attempting to establish transparency, but seeking in effect to control the activities and the funding of NPOs. In some instances, prior government approval is required before international funding may be received.⁵ Indeed, in one instance, a government official explicitly cited provisions in domestic legislation, ostensibly intended to establish some form of transparency in the NPO sector for TF purposes, as an effective means of ensuring that grass roots political opposition was denied funding.⁶ In a report examining the possible

contradiction of counterterrorism measures that can hinder the work of countering terrorism by the Dutch development agency Cordaid, the Fourth Freedom Forum, the Kroc Institute for International Peace Studies at the University of Notre Dame and civil society partners in Europe, Asia, Latin America and Africa, the authors observe that “Organizations and movements that challenge the abusive policies of unaccountable governments inevitably arouse the ire of those in power, but in recent years such pressures have mounted as policy makers have appropriated the language of counterterrorism to intensify their attacks against civil society-based critics.⁷ Needless to say, such measures, the real target of which often appears to be the political opposition⁸ are not envisaged or recommended by FATF.

Alienating NPOs in the fight against terrorism

A further objection to associating NPOs with terrorism in a generalized manner is that it alienates what should be a valuable partner in the fight against terrorism and extremism. Far from being considered primarily as possible risks for TF, NPOs should rather be regarded as important allies. In the UN Global Counterterrorism Strategy adopted on September 8, 2006, the General Assembly resolves to undertake measures aimed at addressing the conditions conducive to the spread of terrorism, in order, amongst other things, “to promote dialogue, tolerance and understanding among civilizations, cultures, peoples and religions.”⁹ In this regard, it welcomes the initiative on the Alliance of Civilizations by the Secretary General, which is “to recommend a practicable programme of action for States, international organizations and civil society aimed at promoting harmony among societies.”¹⁰ Clearly civil society organizations—NPOs—have a valuable role to play in helping to curb extremism and “contributing to strengthening institutions of democratic governance including (...) the protection of human and civil rights and mechanisms for peacefully resolving conflicts.”¹¹ A crucial part of the fight against terrorism is to build social structures and to establish or maintain dialogue between communities to counter radicalization and feelings of exclusion. Many charities carry out these activities by delivering aid and by other means. CFT measures that do not take this into account may cause net harm. The abovementioned report on possible contradiction of counterterrorism measures notes that: “Many of the organisations that work against extremism by promoting development and human rights are themselves being labeled extremist and are facing constraints in their ability to operate.”¹² The question then arises of whether this role can still be fulfilled if the sector itself is treated with caution and suspicion. It may appear a moot point, but it becomes real when one considers the vital role played by Islamic charities in many Muslim countries and communities. Some banks, given their global reach and the possible legal, regulatory, and reputational repercussions if implicated in terrorism financing, have stated that they will not accept a client’s instruction to transfer money to an Islamic charity, whether or not that charity appears on a list of terrorist organizations.¹³

Preventing humanitarian assistance

NPOs often operate in highly vulnerable areas or conflict zones in which terrorist organizations operate as well. Sometimes the territory is actually controlled by terrorist organizations, making it all but impossible not to, at least, be in contact with such organizations if one wishes to work there. What, for instance, is an NPO to do in the event of a humanitarian disaster occurring in a zone controlled by a terrorist organization? Would interaction with a terrorist organization under those circumstances imply that the NPO is itself supporting terrorism? The question came up in the case of the tsunami which struck in South and East Asia in December 2004. One of the devastated countries was Sri Lanka. Part of the affected area was, at that time, controlled by the Liberation Tigers of Tamil Elam (LTTE), an organization designated as terrorist in many countries, including the United States. The LTTE was the de facto government of the area and controlled all traffic. Are humanitarian organizations prohibited from taking action because it would entail

cooperation—or at least interaction—with such an organization, whereby, in this case, some of the 40,000 people affected would have been deprived of aid? Such a consequence would appear undesirable. Some accommodation will have to be found to ensure that aid can be provided under such circumstances, even though it may mean implementing further controls to protect this aid from abuse.¹⁴ Ensuring aid is only delivered in kind—as opposed to being financial—and controlling the delivery thereof, for instance, already limits the possibility for abuse.

In addition, what happens when legitimate NPOs do not act or are prevented from doing so? A U.S. Treasury report on the 2005 Kashmir earthquake¹⁵ said that terrorist organizations were sometimes the first on the scene, remained prominent throughout the emergency and seem to have been effective in their delivery of aid. It reports a survivor saying that, if the terrorist organization had not helped her, she would have died. Focusing on CFT—rather than creating a larger, stronger sector—could leave a vacuum for terrorist organizations to fill and a lingering resentment by survivors against the government, either for failing to help them or directing its attention to counterterrorism rather than humanitarian relief.¹⁶

Government Regulation Is Inappropriate

A second strand of argument against the type of action proposed above questions whether government regulation is the appropriate response to what, from the NPO sector perspective, is a very exceptional phenomenon. Surely, so the reasoning goes, it is the role of law enforcement (or possibly intelligence services) to investigate and prosecute.

Regulation not effective

The case is particularly relevant for complicit NPOs. How can government regulation be a useful tool against an extremist organization posing as a legitimate NPO? Do they not simply disappear from sight when regulation is introduced and carry on their activity “underground”—i.e., unregulated and invisible on the government’s radar? Regulatory measures can be seen as only imposing extra burdens on many bona fide organizations while not affecting those organizations intent on doing harm. As the executive director of an international foundation put it: “why do we have these rules if there are no apparent cases of *inadvertent* support for terrorism?”¹⁷

For the category of exploited NPOs, although one may be able to make a case for regulatory measures that seek to enhance transparency,¹⁸ one may still question how much enhanced scrutiny would achieve. In reviewing all cases of alleged diversion of funds for terrorist purposes, a U.S. report in 2004 found that there were “none that involve a diversion of funds granted by a U.S. grant maker to a foreign recipient organization, where the diversion would have been uncovered but for the lack of appropriate due diligence and oversight procedures.”¹⁹ Quite apart from that, one can still debate whether the imposition of government regulation is really necessary to achieve this aim. As one observer noted “Charitable organizations are already vigilant, already taking steps; many are already going beyond the law. Many are taking extra steps just to be sure their charitable assets are not being diverted.”²⁰

We are, as of yet, unaware of any criminal cases in which instances of terrorism financing were detected as a result of the type of supervisory measures discussed above.²¹ Anecdotal information suggests, rather, that it is financial intelligence that is essential. As one former employee from a Financial Intelligence Unit (FIU) said: “We at the FIU identified a number of NPOs that are involved in terrorist financing, but we discovered them not through any intensified NPO scrutiny or regulation, but rather by trawling through the wire transfer data that was routinely reported to the FIU by all financial institutions, and by comparing and contrasting reports from a wide range of institutions. Without the benefit of the wire

transfer data it is very doubtful that we would have been able to identify instances of TF whether carried out by NPOs or any other body.”²² Of course, the preventive effect of the types of measures envisaged will always be impossible to ascertain. One can hardly expect to prove that certain individuals did not engage in certain activities because of an existing regulation.

The argument made by those in favor of regulating NPOs for TF purposes is that the introduction of regulation usually entails the introduction of concomitant regulatory powers to enforce the regulation. In the case of NPOs, the IN explicitly recommends such powers, giving public authorities a tool for taking early action before any possible terrorist abuse can take place. In cases where, originally, no public action was possible until a crime had been committed, a regulator can now act to disrupt by taking supervisory enforcement action. So, where an NPO has not kept its financial records in order or authorities find worrisome information about associates of the NPOs, the regulator can now engage them earlier rather than later: “effective regulation involves putting a strong emphasis on giving support and guidance to charities to prevent problems and abuse occurring in the first place.”²³ The argument then is that the introduction of regulation is not so much about the apprehension of perpetrators as it is about widening the possible tools available for government action in order to disrupt activity to prevent any possible terrorist abuse taking place.

However, the other argument against the imposition of regulation, namely that it drives the targeted group or the targeted activity “underground,” is not affected by the above consideration.²⁴ If, indeed, the effect of regulation is to drive the groups or activities out of the public eye, it will require extra law enforcement efforts to detect them and take action.²⁵

Regulation not justified

An argument closely linked to the one discussed above is that a very small percentage of cases, proportionally, does not justify government regulation, because—unlike, for instance, the regulation of other parts of society like the financial sector—it infringes upon a basic human right.

The right at issue here is the freedom of association that underpins the existence and activities of many NPOs. In this view, the argument is that government regulation of NPOs restricts this right by imposing obligations on the NPO sector. According to article 22 of the International Convention on Civil and Political Rights,²⁶ to which 165 states are now party,²⁷ restrictions on this right are justified only under limited, defined conditions, among others, in the interest of national security or public safety. They cannot be invoked as a reason for imposing limitations to prevent relatively isolated threats to law and order.²⁸ In case law on article 11 of the European convention,²⁹ the European Court on Human Rights stipulates that exceptions must be “construed strictly,” that only “convincing and compelling reasons” can justify restrictions that must be “proportionate to the aim pursued and that there must be relevant and sufficient evidence for decisions based on an acceptable assessment of the relevant facts before a restriction can be justified.”³⁰ For the critics who believe that some of the measures taken by certain governments, purportedly to address CFT concerns, indeed do limit the right to the freedom of association, the argument for their justification becomes more problematic the more isolated the instances of financing of terrorism through NPOs are.

How Useful Are the Specific Measures Proposed?

The above arguments discuss in a general way what the effects of the imposition of regulation are or might be. The following directly addresses the implications of the financial transparency and due diligence measures proposed in the IN.

Apart from seeking to ensure that pathways of information are established between government authorities and the NPO sector—whether by way of registration or licensing—the IN imposes obligations on NPOs to ensure transparency in their funding, their operations, and the information that is made available on all those associated with the organization, donors, beneficiaries, and partner organizations. It is a “best-efforts,” not a “results,” obligation—meaning that NPOs should make the best attempt, reasonable under the circumstances, to establish the identity of the relevant persons and cannot be held in breach of this obligation merely because they have not established the identity. As far as the financing is concerned, the NPO is to put controls in place to ensure that all funds are accounted for in accordance with the NPO’s objectives.

Approach to risk

As noted, FATF’s definition of NPOs differs from the way in which many countries have defined NPOs for the purposes of their CFT legislation. The total number of organizations upon which many countries impose their CFT obligations is often wider than the definition given by FATF. FATF’s definition considerably limits the circle of organizations to which measures should be applied. As was shown above, in the United Kingdom, 6.3 percent of registered charities account for approximately 90 percent of the income of the charity sector. The question is whether or not, in deciding to focus the supervisory measures on this numerically small group, FATF is targeting the relevant organizations. It would, for instance, most certainly include those international organizations well known around the world for their charitable activity. Are they indeed most likely to be at risk for terrorist abuse? Does their diversity of operations and global presence imply a higher risk or are they, precisely because they are bigger and tend to be more professionally organized, more likely to have taken internal risk mitigation measures that would prevent such abuse? A survey of charities in England and Wales found that smaller charities, with a turnover of less than £1 million per year were less likely to have fraud policies, risk assessments, and control assessments in place than bigger charities,³¹ possibly rendering them more vulnerable to abuse. In addition, it should be noted that none of the examples above and none of the many other examples reviewed included any of the bigger, well-known charity organizations involved in instances of (inadvertently) supporting terrorist financing.

In so limiting the scope of its supervisory measures, FATF’s approach is also slightly at odds with its own recommendation to countries that they should undertake a domestic review of the sector in order to identify features and types of NPOs that, by virtue of their activities or characteristics, are at risk of being misused for terrorist financing. Surely, the whole point of such an exercise is to allow countries to decide for themselves where the risks are (and presumably impose the recommended supervisory measures upon that part of the sector) without having to limit themselves to a predefined sub-category. Applying a risk-based approach implies that countries themselves identify their own risks and apply their measures accordingly. Such an analysis may well show that the real risks are at the fringes of the sector with NPOs operating on a marginal budget.

A “best-efforts” approach

Although no one will argue with the basic idea that an NPO should know how its funds are spent—if only to justify the donor’s trust—and whom it is working with, the real question is how far those obligations should go. Do the controls demand that an NPO has to verify, on site, how funds are spent? What would that imply for an NPO in a donor country working with NPOs overseas? Can it rely on a statement from the overseas NPO? Or would it be required to enlist the services of an outsider to check on how the funds are spent?

As a high-level document,³² the IN cannot be expected to address those questions. Exactly where the line is drawn, however, has significant financial consequences for the NPO

sector. A duty on an NPO providing funds to a project abroad run by a partner organization to verify how funds were spent and who exactly all the decision makers within the partner NPO are and whether they have criminal records or not, may prove very costly and divert funds to activities that are not essential to the fulfillment of the NPO's legal mandate. The reality is that much of the required information is not readily available in a large part of the developing world.³³ Furthermore, "even if a charity could amass facts (which will be hard in many humanitarian settings, cash economies, and poor societies) there are no objective standards against which to test them."³⁴ Quite apart from the availability and reliability of the information, the resources needed to conduct the required due diligence should also be considered; grant-making organizations with small budgets may be especially affected because they lack the personnel or resources to engage in these procedures.³⁵

Breach of trust

Resources are, however, only part of the issue. To a large extent, international grant-making has to rely on cooperation between different NPOs—very few can afford to have a completely global network. In furthering the common good, organizations join forces—donor organizations in the richer parts of the world often rely on local organizations in the developing world to carry out projects. The cement that holds that cooperation together is trust. A thorough examination of your counterparty's credentials (particularly where disparities of power and influence exist) can severely damage that trust and the goodwill that underlies strong and spontaneous cooperation. The earlier-mentioned report on the possibly counter-effective effects of certain measures aimed at combatting terrorism notes that "Requiring nonprofit groups to collect personal information on their partners puts them at risk of being perceived as law enforcement or intelligence agents."³⁶ Cordaid, a big Dutch development organization with an international network of almost a thousand partner organizations in 36 countries in Africa, Asia, and Latin America, recently refused a USAID co-financing grant for a partner group in North Kivu in the Democratic Republic of Congo because of the rigid conditions attached, including participation in a partner vetting system³⁷ and declined a financing opportunity in Pakistan because of a refusal to compromise relationships of trust with local partners.³⁸ In sensitive countries, "some grant-makers are already beginning to experience hostility and suspicion from prospective grantees—particularly non-profit organizations that advocate for political and economic reform."³⁹ In addition, charities operating abroad and foundations funding foreign organizations. In the U.S. context one observer argued that imposing the PVS [Partner Vetting System] is "using a flame thrower to kill an ant. And more than ants may be killed if the PVS is implemented" may be perceived as agents of the government because of counterterrorism measures.⁴⁰ And it is claimed, here again, that the results of such measures may prove counterproductive.

Notes

¹ Matrix Insight, "Study to Assess the Extent of Abuse of Non-Profit Organisations for Financial Criminal Purposes at EU level" (3 April 2008), commissioned by the European Commission, Directorate-General Justice, Freedom and Security, available online at http://ec.europa.eu/homeaffairs/doc_centre/terrorism/docs/study_abuse_non_profit_orgs_for_financial_criminal_purposes_avril09.pdf.

² Written Testimony of David D. Aufhauser, General Counsel, Department of the Treasury before the Senate Judiciary Committee Subcommittee on Terrorism, Technology and Homeland Security June 26, 2003 2:00 p.m. The United States Senate, p11, available online at <http://www.ustreas.gov/press/releases/reports/js5071.pdf>.

³ See, for instance, "Muslim Charities Say Fear Is Damming Flow of Money," *Washington Post*, August 9, 2006. According to the U.K. Charity Commission, there is no evidence to support this fact for the United Kingdom.

⁴ Doug Rutzen and Cathy Shea, "The associational Counter Revolution" *Alliance* 11, no. 3 (September 2006), p. 27, available online at <http://www.icnl.org/knowledge/pubs/AssocCounterRevol.pdf>. See

also, "Defending Civil Society, A report of the World Movement for Democracy" (February 2008), co-authored by the International Center for Not-for-Profit Law (ICNL) and World Movement for Democracy Secretariat at the National Endowment for Democracy available online at <http://www.wmd.org/documents/Defending%20Civil%20Society%20%20English.pdf>.

⁵ See *Global Trends in NGO law, a quarterly review of NGO legal trends around the world 1, no. 1* (March 2009), available online at <http://www.icnl.org/knowledge/globaltrends/GloTrends1-1.htm>.

⁶ Author's conversation with government official, March, 2005.

⁷ David Cortright with George A. Lopez, Alistair Millar and Linda Gerber-Stellingwerf, "Friend not Foe: Civil Society and the Struggle against Violent Extremism," a report to Cordaid from the Fourth Freedom Forum and Kroc Institute for International Peace Studies at the University of Notre Dame, p. 3, available on line at http://www.fourthfreedom.org/pdf/08_10_Friend_Not_Foe.pdf

⁸ See, for example, J. Howell, "The Global War on Terror, Development and Civil Society", *Journal of International Development* 18 (2006): 128.

⁹ See "Resolution: The United Nations Global Counter Terrorism Strategy" adopted by the General Assembly on September 8 2006 UN Doc A/Res/60/288, available online at <http://www.un.org/terrorism/strategy-counter-terrorism.shtml>.

¹⁰ See "Secretary General Announces composition of High Level Group for Alliance of Civilizations" 2 September 2005, UN Doc SG/SM/10073/Rev.1* , available online at <http://www.un.org/News/Press/docs/2005/sgsm10073.doc.htm>.

¹¹ F. Barnett Barron, "Deterring donors: Anti Terrorist financing rules and American Philanthropy," *The International Journal for Not-for-profit Law* 6, no. 2, (January 2004), http://www.icnl.org/knowledge/ijnl/vol6iss2/special_5.htm.

¹² Cortright et al., op.cit. p. 1.

¹³ James Shaw Hamilton, 2007 "Recognizing the Umma in Humanitarianism: International Regulation of Islamic Charities," in *Understanding Islamic Charities*, ed. Jon Alterman and Karin von Hippel, p. 15–31, Washington, D. C., CSIS Press.

¹⁴ For a wider discussion of this particular, point see "Testimony at an Oversight Hearing on Amendments to the Material Support for Terrorism Laws, before the Subcommittee on Crime, Terrorism and Homeland Security of the House Judiciary Committee" (10 May 2005), available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_house_hearings&doid=f:21139.wais. For a discussion on the legal aspects of this issue under U.K. law, see "The U.K.'s "Anti-Terrorist" Finance Regime and Its Implications for the Non-Profit Sector," Legal opinion by Edward Fitzgerald QC and Caoilfhionn Gallagher (7 December 2006) in appendix to Nolan Quigley and Belinda Pratten, "Security and Civil Society, The impact of counter-terrorism measures on civil society organizations," Report of Advisory Council set up by National Council for Voluntary Organisations (11 January 2007), available on line at http://www.ncvo-vol.org.uk/uploadedFiles/NCVO/Policy/Civil_Society_and_Participation/2007%2001%2024%20Security%20and%20Civil%20Society-A%20report%20from%20NCVO.pdf.

¹⁵ Typologies and Open Source Reporting on Terrorist Abuse of Charitable Operations in Post-earthquake Pakistan and India, published online by the US Department of Treasury, available at http://treas.gov/offices/enforcement/key-issues/protecting/docs/charities_post-earthquake.pdf

¹⁶ The point also came up in the context of the floods in Pakistan in August 2010. At a special meeting of the UN General Assembly, Pakistan's foreign minister, Shah Mahmood Qureshi said that the international community must help address the upheaval created by the floods. "If we fail, it could undermine the hard-won gains made by the government in our difficult and painful war against terrorism. We cannot allow this catastrophe to become an opportunity for the terrorists." See *In Pakistan, Militants Use Flood Aid to Seek Support*, Corey Flintoff, August 23, 2010, available online at <http://www.npr.org/templates/story/story.php?storyId=129379169&ft=1&f=1004>.

¹⁷ Nancy Billica, "Philanthropy Counter Terrorism and Global Civil Society Activism", prepared for the London School of Economics Workshop on Aid, Security, and Civil Society in the Post-911 Context, 28-29 June 2007, p10, available on line at <http://www.lse.ac.uk/collections/CCS/events/conference/Billica.pdf>, 10. The discussion is, of course, by no means exclusive to NPOs and terrorism financing. Lawyers are objecting to the introduction of AML measures in their profession because, they say, while there are undoubtedly cases of money laundering involving lawyers, there are no cases of unwitting involvement in money laundering by lawyers, and only those cases can usefully be dealt with by regulation.

¹⁸ The argument being that, if the NPO itself is legitimate, one can reasonably assume that those in charge will do everything possible to stop being exploited by others for terrorist purposes. The measures proposed might lead to the discovery of incidents or malpractices that would otherwise be

overlooked. Due diligence of a beneficiary might reveal that there is reason for caution and lead to the imposition of extra safeguards to guarantee that money is being spent correctly.

¹⁹ Victoria B. Bjorklund, "Terrorism and Money Laundering: Illegal Purposes and Activities" (paper delivered for the National Center on Philanthropy and the Law, October 28, 2004), available at http://www3.law.nyu.edu/ncpl/library/publications/Conf2004_Bjorklund_DRAFT.pdf.

²⁰ Billica *op. cit.*

²¹ Of course, that is not to say such cases do not exist. There may be very valid reasons for law enforcement and intelligence agencies not wishing to disclose how an instance of abuse was detected.

²² E-mail to author, August 18, 2008.

²³ U.K. Charity Commission Counter Terrorism Strategy, page 4, online at <http://www.charity-commission.gov.uk/Library/investigations/pdfs/ctstext.pdf>

²⁴ See, for example, Mark Sidel, "Counter-terrorism and the enabling Legal and Political environment for Civil Society" in *The International Journal of Not-for-Profit Law* volume 10, issue 3, June 2008, available online at http://www.icnl.org/knowledge/ijnl/vol10iss3/special_2.htm, who in discussing the Guidelines issued by the U.S. Treasury Department to U.S.-based charities states: "And the Guidelines carried the risk that legitimate and well meaning charities would struggle to comply with standards while less professional or less well meaning groups might just ignore them." Similarly, see Mohammed R. Kroessin, "Islamic charities and the "War on Terror": dispelling the myths," *Humanitarian Exchange Magazine*, Issue 38, June 2007 available online at <http://www.odihpn.org/report.asp?id=2890>: "this switch away from established charities may have further weakened the transparency and accountability of charitable donations."

²⁵ Ironically, attempts to close down or control formal charities may have had precisely the opposite effect by forcing charitable giving into less regulated channels. Charity Commission, *op. cit.* (p.8), where it states: "We must also be alert to the unintended risk that a higher burden of regulation may encourage money to be donated to unregistered organisations or to others overseas and therefore beyond the regulatory scope of the Commission." See also, Ibrahim Warde, *The Price of Fear, The Truth behind the Financial War on Terror*: p. 130, Berkeley, University of California Press, 2007 "post-September 11 policies proved mostly counterproductive; they weakened mainstream controllable charities, while building up informal, unchecked and potentially dangerous charitable and donor networks."

²⁶ See also article 11 of the European Convention for the Protection of Human Rights and Fundamental Freedoms and article 16 of the American Convention on human rights.

²⁷ As at November 6, 2009, see http://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsq_no=IV-4&chapter=4&lang=en

²⁸ OSCE/ODIHR Key guiding principles of freedom of association with an emphasis on Non Governmental Organisations, page 5 as quoted in *Defending Civil Society, A report of the World Movement for Democracy*, *op. cit.*, p. 24.

²⁹ Although legally speaking, this case law is relevant only to parties to the European Convention, the virtual identical language of this article and art 22 ICCPR and the standing of the ECHR render it of more than merely European significance.

³⁰ See *Sidiropoulos and others v. Greece*, 10 July 1998, (57/1997/841/1047) and *United Communist Party of Turkey and other v Turkey*, 30 January 1998(133/1996/752/951).

³¹ *Matrix Insight*, *op. cit.*, p. 28.

³² Given the decision-making process within FATF and the number of members, FATF recommendations tend to address principles and objectives rather than be technically prescriptive in how those are to be achieved.

³³ Barnett F. Baron, *op. cit.*

³⁴ James Shaw-Hamilton, *op. cit.*

³⁵ Nancy Billica, "Philanthropy & Post-9/11 Policy Five Years Out: Assessing the international impacts of counter terrorism measures", p.15. (December 2006), available online at http://www.urgentactionfund.org/assets/files/philanthropy_at_risk/Philanthropy-Post%209-11_final.pdf. To put the issue of NPO resources into some more perspective, only about 20 percent of the 800,000 associations in France have one employee or more.

³⁶ David Cortright, et al, *op. cit.*, p. 14.

³⁷ *Ibid.*

³⁸ Cortright, et al. *op. cit.*

³⁹ Barnett Barron, *op. cit.*

⁴⁰ OMB Watch and Grantmakers without borders, "Collateral Damage, How the War on Terror Hurts Charities, Foundations and the People they serve," (July 2008), 6, <http://www.ombwatch.org/npadv/PDF/collateraldamage.pdf>.

Conclusions and Recommendations

The international and national reaction to instances of terrorism financing by NPOs has been considerable. Despite the energy put into this effort, we are not aware of examples in which measures proposed by individual countries in implementing SR VIII and the IN, or similar national legislation, have resulted in detecting or deterring cases of terrorism financing. Part of the explanation for this may be that the measures are too recent to have become fully effective, that such instances have not been made public, or that the measures are, in essence, meant to be preventive in nature (the effect of which is, inherently, impossible to measure).¹

Regulation: Use Existing Frameworks

The rarity of instances of terrorism financing by NPOs, when contrasted against the enormous scope of the sector, does raise the question of whether, *in and of itself*, government regulation is the most appropriate response. To be clear, this is not to belittle the significance of the issue; rather, it is to question the nature of the response.

This does not mean, however, that regulation—whether by government or through the non-profit sector itself—has no role to play. So far, the debate about terrorism financing and NPOs has dealt with the issue in isolation, as if it were a wholly new type of problem, not connected to other NPO-related problems and, requiring a radically different approach to NPOs. This is not the case. Concern over use of funds by NPOs is well known and has already led to widespread regulatory and self-regulatory action aimed at enhancing the transparency and integrity of the NPO sector in many countries. To a very large degree, these measures address terrorist financing concerns as well. A report on the European Union’s efforts in the fight against terrorist financing noted that strengthening anti-fraud measures, and other measures to increase financial oversight and reporting, was considered by many to be the more effective approach to addressing TF concerns.²

In advocating any action to address TF concerns, it is very important to be aware of the regulatory frameworks already in existence. This point deserves extra emphasis, since many of those involved in Anti Money Laundering (AML) and CFT do not appear to be aware of these frameworks and of the sources already available to government to obtain information on NPOs. In virtually all countries, NPOs already engage with the governments in various ways: when they need or want to register with the government, when they seek tax privileges, or when raising money from the citizens of a given jurisdiction. Each jurisdiction is different in how one of these circumstances creates a relationship between the NPO and the authorities, but one or more of these moments exists in almost every system.³

None of these forms of government engagement or oversight were specifically set up to address issues of terrorist financing. Each of them raises different issues, opportunities, and challenges. The key question is the extent to which a particular form of engagement helps the authorities to gain relevant information about NPOs—concerning finances (especially expenditures), activities, and its management and personnel.⁴

In addition to these forms of government supervision, NPO oversight can take place through self-regulatory organizations (SROs). Although SROs may not have the force of law, they can have the force of contract and the power to sanction their members where there is violation of an agreed code of conduct.⁵ NPO SROs have often been in the front lines of the non-profit sector's fight against fraud, so their forms of oversight may turn out to be more directly relevant for CFT than existing government controls. Governments should recognize the need felt in the sector to demonstrate its good governance and care and its standing as a responsible actor and use that aspiration to also address terrorism financing concerns, allowing it to take ownership of its own problems. Peer pressure and moral suasion can be effective tools to promote a culture of transparency.

Regulation designed to tackle terrorism financing by and through NPOs should be seen as part of a much wider effort to enhance the transparency of the NPO sector—encompassing the governance, finances, and partner organizations—and to strengthen the sector as a whole. Those involved in advising on counter-terrorism financing policy should seek to understand the NPO sector in a country and know what self-regulatory mechanism and government licensing and registration is already in place and make full use of the information already available through those channels. Understanding and knowing the domestic NPO sector and the existing regulations is indispensable before any action is undertaken. Such knowledge and understanding cannot be obtained without the involvement of the sector.

Of course, the above is first and foremost relevant to what we have termed exploited NPOs. Regulation as such is not likely to cause complicit NPOs to change their behavior, although it does provide for the necessary tools to allow early government intervention. The primary agencies responsible for dealing with such organizations however, are the law enforcement or intelligence authorities and not regulatory bodies.

Apply a Risk-Based Approach

When requiring NPOs to take measures specifically to address terrorism financing concerns, governments should recognize the limitations of such obligations. Lack of resources, reliable information, and time may render the fulfillment of those obligations impossible. Depending on how it is done, gathering information on a prospective partner can destroy trust and harm a relationship and the cost, both in terms of time and money, can be considerable. Given their duty towards their donors, it is vital to ensure that those costs are only made when really necessary and in such a way as to promote equality between prospective partners (e.g., by recommending there be an *exchange* of similar information between partners, rather than a one way supply of information from one organization in a developing country to a donor organization in the developed world). To assist NPOs in ensuring their efforts are well directed, governments should conduct risk assessments that clarify what situations are higher risk and when extra efforts may be required. Governments should involve the sector in this effort—only they can provide the information needed to make such an exercise useful.⁶

Be Specific When Discussing NPOs and TF

In order to allow the NPOs to play their vital role, it is important to emphasize that only a very small fraction of the sector has been abused for terrorism financing purposes. Rhetoric associating NPOs and TF in general terms overstates the threat and is not helpful. It risks alienating a vital ally in the struggle against extremism and it renders potential donors reticent to contribute. Rather than making statements about the vulnerability of the NPO sector as such, it would be more productive to concentrate on specific charitable activity that is at risk, erasing the cloud of suspicion hanging over the entire sector and focusing instead

on certain operations. The international community and FATF should remain vigilant and speak out against governments that use the purported connection to justify restricting the space within which civil society can operate.

The Humanitarian Imperative Is Paramount

The civilian population should not be prevented from receiving humanitarian assistance as a result of counterterrorism standards. After all, the ultimate aim of counterterrorism measures is precisely the protection of the civilian population from organized harm; thus, allowing civilians to suffer would constitute an odd confusion between means and ends. Everything should be done to ensure that suffering of victims can be alleviated no matter whose territory they are in.⁷ Indeed, not allowing bona fide NPOs to operate in certain geographical areas would likely expose those in need to terrorist and extremist organizations to a far greater degree. To prevent financial resources from falling into the hands of terrorist related organizations, consideration should be given to aid in kind, and ensuring control up until the final point of distribution.

Notes

¹ Moreover, it is recognized that an important component of any counter-terrorism strategy is gathering intelligence—which is obviously outside the FATF remit—and that the imposition of regulation might yield a useful source of intelligence.

² “The EU’s efforts in the fight against terrorist financing in the context of the Financial Action Task Force’s Nine Special Recommendations and the EU counter terrorist financing strategy, Final Report” (John Howell & Company, February 1, 2007), 33, http://ec.europa.eu/justice_home/doc_centre/terrorism/docs/report_01_02_07_with_appendix_en.pdf. Another EU report on recent measures to improve accountability in the NPO sector found that little evidence FATF or counter-terrorism was a primary factor for reforms in the 140 initiatives identified, See Study on Recent Public and Self-Regulatory Initiatives Improving Transparency and Accountability of Non-Profit Organisations in the European Union, Commissioned by the European Commission Directorate-General of Justice, Freedom and Security Submitted by the European Center for Not-for-Profit Law, April 2009 available online at http://ec.europa.eu/home-affairs/doc_centre/terrorism/docs/initiatives_improving_transparency_accountability_npos_avr09.pdf.

³ It should be clear, however, that there may be NPOs that do not interact with government in any way at all. In the vast majority of cases, this will be because the NPO in question is an informal group of people whose aim is the benefit of the members of the group, or limited in time or whose funds are so insignificant as to make the fulfillment of any formalities not worthwhile. This group is specifically recognized by FATF as of lesser interest in its Best Practice Paper where it states that “Small organisations that do not raise significant amounts of money from public sources, and locally based associations or organisations whose primary function is to redistribute resources among members may not necessarily require enhanced government oversight.”

⁴ In fact, this is recognized by the FATF IN which states: “Specific licensing or registration requirements for counter terrorist financing purposes are not necessary. For example, in some countries, NPOs are already registered with tax authorities and monitored in the context of qualifying for favorable tax treatment (such as tax credits or tax exemptions).”

⁵ For further discussion on the role of self-regulation and the different models of SRO, see Robert Lloyd, “The Role of NGO Self-Regulation in Increasing Stakeholder Accountability” (July 2005), <http://www.oneworldtrust.org/documents/NGO%20Self-Regulation%20July%202005.pdf>. Lloyd discusses under what conditions self-regulation initiatives can increase NGO’s accountability to their beneficiaries.

⁶ For the United States, the American Bar Association has proposed a continuum of risk factors that could be helpful in deciding when to take action, see “Comments in response to Internal Revenue Service Announcement 2—3-29, 2003-20 I.R.B. 928 regarding international grant-making and international activities by domestic 501(c)(3) organizations,” online at <http://www.abanet.org/tax/pubpolicy/2003/030714exo.pdf>.

⁷ See also, Charities Commission, op. cit. p. 7: “It would be profoundly undesirable if an unintended consequence of a counter-terrorist strategy were to make it impossible for legitimate overseas aid charities to be involved in providing aid, or make it impossible for any charity to provide aid in particular parts of the world.”

FATF Special Recommendation VIII

Countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Nonprofit organizations are particularly vulnerable, and countries should ensure that they cannot be misused:

1. by terrorist organizations posing as legitimate entities
2. to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset-freezing measures
3. to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organizations

Interpretative Note to Special Recommendation VIII: Nonprofit Organizations

Introduction

1. Nonprofit organizations (NPOs) play a vital role in the world economy and in many national economies and social systems. Their efforts complement the activity of the governmental and business sectors in providing essential services, comfort, and hope to those in need around the world. The ongoing international campaign against terrorist financing has, unfortunately, demonstrated that terrorists and terrorist organizations exploit the NPO sector to raise and move funds, provide logistical support, encourage terrorist recruitment, or otherwise support terrorist organizations and operations. This misuse not only facilitates terrorist activity but also undermines donor confidence and jeopardizes the very integrity of NPOs. Therefore, protecting the NPO sector from terrorist abuse is both a critical component of the global fight against terrorism and a necessary step to preserve the integrity of NPOs.
2. NPOs may be vulnerable to abuse by terrorists for a variety of reasons. NPOs enjoy the public trust, have access to considerable sources of funds, and are often cash-intensive. Furthermore, some NPOs have a global presence that provides a framework for national and international operations and financial transactions, often within or near those areas that are most exposed to terrorist activity. Depending on the legal form of the NPO and the country, NPOs may often be subject to little or no governmental oversight (e.g., registration, record keeping, reporting, and monitoring), or few formalities may be required for their creation (e.g., there may be no skills or starting capital required and no background checks necessary for employees). Terrorist organizations have taken advantage of these characteristics of NPOs to infiltrate the sector and misuse NPO funds and operations to cover for or support terrorist activity.

Objectives and General Principles

3. The objective of Special Recommendation VIII (SR VIII) is to ensure that NPOs are not misused by terrorist organizations: (i) to pose as legitimate entities; (ii) to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; or (iii) to conceal or obscure the

clandestine diversion of funds intended for legitimate purposes but diverted for terrorist purposes. In this Interpretative Note, the approach taken to achieve this objective is based on the following general principles:

- a. Past and ongoing abuse of the NPO sector by terrorists and terrorist organizations requires countries to adopt measures both:
 - (i) protect the sector against such abuse and identify and,
 - (ii) take effective action against those NPOs that either are exploited by or actively support terrorists or terrorist organizations.
- b. Measures adopted by countries to protect the NPO sector from terrorist abuse should not disrupt or discourage legitimate charitable activities. Rather, such measures should promote transparency and engender greater confidence in the sector, across the donor community and with the general public, that charitable funds and services reach intended legitimate beneficiaries. Systems that promote achieving a high degree of transparency, integrity, and public confidence in the management and functioning of all NPOs are integral to ensuring the sector cannot be misused for terrorist financing.
- c. Measures adopted by countries to identify and take effective action against NPOs that either are exploited by or actively support terrorists or terrorist organizations should aim to prevent and prosecute, as appropriate, terrorist financing and other forms of terrorist support. Where NPOs suspected of or implicated in terrorist financing or other forms of terrorist support are identified, the first priority of countries must be to investigate and halt such terrorist financing or support. Actions taken for this purpose should, to the extent reasonably possible, avoid any negative impact on innocent and legitimate beneficiaries of charitable activity. However, this interest cannot excuse the need to undertake immediate and effective actions to advance the immediate interest of halting terrorist financing or other forms of terrorist support provided by NPOs.
- d. Developing cooperative relationships among the public, private, and NPO sector is critical to raising awareness and fostering capabilities to combat terrorist abuse within the sector. Countries should encourage the development of academic research on, and information sharing in, the NPO sector to address terrorist financing related issues.
- e. A targeted approach in dealing with the terrorist threat to the NPO sector is essential given the diversity within individual national sectors, the differing degrees to which parts of each sector may be vulnerable to misuse by terrorists, the need to ensure that legitimate charitable activity continues to flourish, and the limited resources and authorities available to combat terrorist financing in each jurisdiction.
- f. Flexibility in developing a national response to terrorist financing in the NPO sector is also essential in order to allow it to evolve over time as it faces the changing nature of the terrorist financing threat.

Definitions

4. For the purposes of SR VIII and this Interpretative Note, the following definitions apply:
 - a. The term *nonprofit organization*, or *NPO*, refers to a legal entity or organization that primarily engages 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.”

- b. The terms *FIU*, *legal arrangement*, and *legal person* are as defined by the FATF Forty Recommendations (2003) (the FATF Recommendations).
- c. The term *funds* is as defined by the Interpretative Note to FATF Special Recommendation II.
- d. The terms *freezing*, *terrorist*, and *terrorist organization* are as defined by the Interpretative Note to FATF Special Recommendation III.
- e. The term *appropriate authorities* refers to competent authorities, self-regulatory bodies, accrediting institutions, and other administrative authorities.
- f. The term *beneficiaries* refers to those natural persons, or groups of natural persons who receive charitable, humanitarian or other types of assistance through the services of the NPO.

Measures

- 5. Countries should undertake domestic reviews of their NPO sector or have the capacity to obtain timely information on its activities, size, and other relevant features. In undertaking these assessments, countries should use all available sources of information in order to identify features and types of NPOs, which, by virtue of their activities or characteristics, are at risk of being misused for terrorist financing.¹ Countries should also periodically reassess the sector by reviewing new information on the sector's potential vulnerabilities to terrorist activities.
- 6. There is a diverse range of approaches in identifying, preventing, and combating terrorist misuse of NPOs. An effective approach, however, is one that involves all four of the following elements: (a) outreach to the sector, (b) supervision or monitoring, (c) effective investigation and information gathering, and (d) effective mechanisms for international co-operation. The following measures represent specific actions that countries should take with respect to each of these elements in order to protect their NPO sector from terrorist financing abuse.
 - a. Outreach to the NPO sector concerning terrorist financing issues
 - (i) Countries should have clear policies to promote transparency, integrity, and public confidence in the administration and management of all NPOs.
 - (ii) Countries should encourage or undertake outreach program to raise awareness in the NPO sector about the vulnerabilities of NPOs to terrorist abuse and terrorist financing risks, and the measures that NPOs can take to protect themselves against such abuse.
 - (iii) Countries should work with the NPO sector to develop and refine the best practices to address terrorist financing risks and vulnerabilities and, thus, protect the sector from terrorist abuse.²
 - (iv) Countries should encourage NPOs to conduct transactions via regulated financial channels, wherever feasible, keeping in mind the varying capacities of financial sectors in different countries and in different areas of urgent charitable and humanitarian concerns.
 - b. Supervision or monitoring of the NPO sector

Countries should take steps to promote effective supervision or monitoring of their NPO sector. In practice, countries should be able to demonstrate that the following standards apply to NPOs that account for (1) a significant portion of the financial resources under control of the sector; and (2) a substantial share of the sector's international activities.

 - (i) NPOs should maintain information on: (1) the purpose and objectives of their stated activities; and (2) the identity of the person(s) who own, control, or direct their activities, including senior officers, board

- members, and trustees. This information should be publicly available, either directly from the NPO or through appropriate authorities.
- (ii) NPOs should issue annual financial statements that provide detailed breakdowns of incomes and expenditures.
 - (iii) NPOs should be licensed or registered. This information should be available to competent authorities.³
 - (iv) NPOs should have appropriate controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose and objectives of the NPO's stated activities.
 - (v) NPOs should follow a "know your beneficiaries and associate NPOs" rule,⁴ which means that the NPO should make best efforts to confirm the identity, credentials, and good standing of their beneficiaries and associate NPOs. NPOs should also undertake best efforts to document the identity of their significant donors and to respect donor confidentiality.
 - (vi) NPOs should maintain, for a period of at least five years, and make available to appropriate authorities, records of domestic and international transactions that are sufficiently detailed to verify that funds have been spent in a manner consistent with the purpose and objectives of the organization. This also applies to information mentioned in paragraphs (i) and (ii) above.
 - (vii) Appropriate authorities should monitor the compliance of NPOs with applicable rules and regulations.⁵ Appropriate authorities should be able to properly sanction relevant violations by NPOs or persons acting on behalf of those NPOs.⁶
- c. Effective information gathering and investigation
- (i) Countries should ensure effective cooperation, coordination, and information sharing to the extent possible among all levels of appropriate authorities or organizations that hold relevant information on NPOs.
 - (ii) Countries should have investigative expertise and capability to examine those NPOs suspected of either being exploited by or actively supporting terrorist activity or terrorist organizations.
 - (iii) Countries should ensure that full access to information on the administration and management of a particular NPO (including financial and programmatic information) may be obtained during the course of an investigation.
 - (iv) Countries should establish appropriate mechanisms to ensure information is promptly shared with all relevant competent authorities in order to take preventative or investigative action when there is suspicion or reasonable grounds to suspect that a particular NPO: (1) is a front for fundraising by a terrorist organization; (2) is being exploited as a conduit for terrorist financing, including for the purpose of escaping asset freezing measures; or (3) is concealing or obscuring the clandestine diversion of funds intended for legitimate purposes, but redirected for the benefit of terrorists or terrorist organizations.
- d. Effective capacity to respond to international requests for information about an NPO of concern
- Consistent with Special Recommendation V, countries should identify appropriate points of contact and procedures to respond to international requests for information regarding particular NPOs suspected of terrorist financing or other forms of terrorist support.

Notes

¹ For example, such information could be provided by regulators, tax authorities, FIUs, donor organizations, or law enforcement and intelligence authorities.

² The FATF's *Combating the Abuse of Non-Profit Organisations: International Best Practices* provides a useful reference document for such exercises.

³ Specific licensing or registration requirements for counterterrorist financing purposes are not necessary. For example, in some countries, NPOs are already registered with tax authorities and monitored in the context of qualifying for favorable tax treatment (such as tax credits or tax exemptions).

⁴ The term "associate NPOs" includes foreign branches of international NPOs.

⁵ In this context, rules and regulations may include rules and standards applied by self-regulatory bodies and accrediting institutions.

⁶ The range of such sanctions might include freezing of accounts, removal of trustees, fines, de-certification, de-licensing, and de-registration. This should not preclude parallel civil, administrative, or criminal proceedings with respect to NPOs or persons acting on their behalf when appropriate.

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One of the ways in which terrorist organizations raise and transfer funds is by using nonprofit organizations (NPOs); however NPOs are also an important way to deal with the conditions conducive to the spread of terrorism. In trying to address one problem—terrorism financing—it is important not to diminish the important work of NPOs. This paper discusses the threat and how to address it without tainting the entire NPO sector and concludes that it is inefficient and counterproductive to devise an entirely new regulatory framework. The ultimate objective is to enhance the transparency of the NPO sector—the people in charge of NPOs, NPO funding sources, and how funds are spent. The NPO sector has a stake in being clean and being regarded as such by others, thus NPOs are indispensable partners in drawing up regulatory policies, including self-regulatory policies.

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