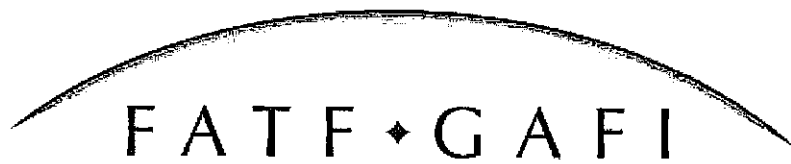


**Appendix B**

FATF International Best Practices on  
Combating the Abuse of non-Profit  
Organisations



**Financial Action Task Force  
on Money Laundering**

*Financial Action Task Force  
on Money Laundering*

**COMBATING THE ABUSE OF  
NON-PROFIT ORGANISATIONS**

**International Best Practices**

11 October 2002

## COMBATING THE ABUSE OF NON-PROFIT ORGANISATIONS

### *International Best Practices*

#### **Introduction and definition**

1. The misuse of non-profit organisations for the financing of terrorism is coming to be recognised as a crucial weak point in the global struggle to stop such funding at its source. This issue has captured the attention of the Financial Action Task Force (FATF), the G7, and the United Nations, as well as national authorities in many regions. Within the FATF, this has rightly become the priority focus of work to implement Special Recommendation VIII (Non-profit organisations).

2. Non-profit organisations can take on a variety of forms, depending on the jurisdiction and legal system. Within FATF members, law and practice recognise associations, foundations, fundraising committees, community service organisations, corporations of public interest, limited companies, Public Benevolent Institutions, all as legitimate forms of non-profit organisation, just to name a few.

3. This variety of legal forms, as well as the adoption of a risk-based approach to the problem, militates in favour of a functional, rather than a legalistic definition. Accordingly, the FATF has developed suggested practices that would best aid authorities to protect non-profit organisations that engage in raising or disbursing funds for charitable, religious, cultural, educational, social or fraternal purposes, or for the carrying out of other types of "good works" from being misused or exploited by the financiers of terrorism.

#### **Statement of the Problem**

4. Unfortunately, numerous instances have come to light in which the mechanism of charitable fundraising – i.e., the collection of resources from donors and its redistribution for charitable purposes – has been used to provide a cover for the financing of terror. In certain cases, the organisation itself was a mere sham that existed simply to funnel money to terrorists. However, often the abuse of non-profit organisations occurred without the knowledge of donors, or even of members of the management and staff of the organisation itself, due to malfeasance by employees and/or managers diverting funding on their own. Besides financial support, some non-profit organisations have also provided cover and logistical support for the movement of terrorists and illicit arms. Some examples of these kinds of activities were presented in the 2001-2002 FATF Report on Money Laundering Typologies<sup>1</sup>; others are presented in the annex to this paper.

#### **Principles**

5. The following principles guide the establishment of these best practices:

- The charitable sector is a vital component of the world economy and of many national economies and social systems that complements the activity of the governmental and business sectors in supplying a broad spectrum of public services and improving quality of life. We wish to safeguard and maintain the practice of charitable giving and the strong and diversified community of institutions through which it operates.
- Oversight of non-profit organisations is a co-operative undertaking among government, the charitable community, persons who support charity, and those whom it serves. Robust oversight

<sup>1</sup> Published 1 February 2002 and available at [http://www.fatf-gafr.org/FATFDocs\\_en.htm#Trends](http://www.fatf-gafr.org/FATFDocs_en.htm#Trends).

mechanisms and a degree of institutional tension between non-profit organisations and government entities charged with their oversight do not preclude shared goals and complementary functions – both seek to promote transparency and accountability and, more broadly, common social welfare and security goals.

- Government oversight should be flexible, effective, and proportional to the risk of abuse. Mechanisms that reduce the compliance burden without creating loopholes for terrorist financiers should be given due consideration. 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.
- Different jurisdictions approach the regulation of non-profit organisations from different constitutional, legal, regulatory, and institutional frameworks, and any international standards or range of models must allow for such differences, while adhering to the goals of establishing transparency and accountability in the ways in which non-profit organisations collect and transmit funds. It is understood as well that jurisdictions may be restricted in their ability to regulate religious activity.
- Jurisdictions may differ on the scope of purposes and activities that are within the definition of "charity," but all should agree that it does not include activities that directly or indirectly support terrorism, including actions that could serve to induce or compensate for participation in terrorist acts.
- The non-profit sector in many jurisdictions has representational, self-regulatory, watchdog, and accreditation organisations that can and should play a role in the protection of the sector against abuse, in the context of a public-private partnership. Measures to strengthen self-regulation should be encouraged as a significant method of decreasing the risk of misuse by terrorist groups.

#### **Areas of focus**

6. Preliminary analysis of the investigations, blocking actions, and law-enforcement activities of various jurisdictions indicate several ways in which non-profit organisations have been misused by terrorists and suggests areas in which preventive measures should be considered.

##### *(i) Financial transparency*

7. Non-profit organisations collect hundreds of billions of dollars annually from donors and distribute those monies – after paying for their own administrative costs – to beneficiaries. Transparency is in the interest of the donors, organisations, and authorities. However, the sheer volume of transactions conducted by non-profit organisations combined with the desire not to unduly burden legitimate organisations generally underscore the importance of risk and size-based proportionality in setting the appropriate level of rules and oversight in this area.

##### *a. Financial accounting*

- Non-profit organisations should maintain and be able to present full program budgets that account for all programme expenses. These budgets should indicate the identity of recipients and how the money is to be used. The administrative budget should also be protected from diversion through similar oversight, reporting, and safeguards.
- Independent auditing is a widely recognised method of ensuring that accounts of an organisation accurately reflect the reality of its finances and should be considered a best practice. Many major non-profit organisations undergo audits to retain donor confidence, and regulatory

authorities in some jurisdictions require them for non-profit organisations. Where practical, such audits should be conducted to ensure that such organisations are not being abused by terrorist groups. It should be noted that such financial auditing is not a guarantee that program funds are actually reaching the intended beneficiaries.

*b. Bank accounts:*

- It is considered a best practice for non-profit organisations that handle funds to maintain registered bank accounts, keep its funds in them, and utilise formal or registered financial channels for transferring funds, especially overseas. Where feasible, therefore, non-profit organisations that handle large amounts of money should use formal financial systems to conduct their financial transactions. Adoption of this best practice would bring the accounts of non-profit organisations, by and large, within the formal banking system and under the relevant controls or regulations of that system.

*(ii) Programmatic verification*

8. The need to verify adequately the activities of a non-profit organisation is critical. In several instances, programmes that were reported to the home office were not being implemented as represented. The funds were in fact being diverted to terrorist organisations. Non-profit organisations should be in a position to know and to verify that funds have been spent as advertised and planned.

*a. Solicitations*

9. Solicitations for donations should accurately and transparently tell donors the purpose(s) for which donations are being collected. The non-profit organisation should then ensure that such funds are used for the purpose stated.

*b. Oversight*

10. To help ensure that funds are reaching the intended beneficiary, non-profit organisations should ask following general questions:

- Have projects actually been carried out?
- Are the beneficiaries real?
- Have the intended beneficiaries received the funds that were sent for them?
- Are all funds, assets, and premises accounted for?

*c. Field examinations*

11. In several instances, financial accounting and auditing might be insufficient protection against the abuse of non-profit organisations. Direct field audits of programmes may be, in some instances, the only method for detecting misdirection of funds. Examination of field operations is clearly a superior mechanism for discovering malfeasance of all kinds, including diversion of funds to terrorists. Given considerations of risk-based proportionality, across-the-board examination of all programmes would not be required. However, non-profit organisations should track programme accomplishments as well as finances. Where warranted, examinations to verify reports should be conducted.

*d. Foreign operations*

12. When the home office of the non-profit organisation is in one country and the beneficent operations take place in another, the competent authorities of both jurisdictions should strive to exchange information and co-ordinate oversight or investigative work, in accordance with their

comparative advantages. Where possible, a non-profit organisation should take appropriate measures to account for funds and services delivered in locations other than in its home jurisdiction.

*(iii) Administration*

13. Non-profit organisations should be able to document their administrative, managerial, and policy control over their operations. The role of the Board of Directors, or its equivalent, is key.

14. Much has been written about the responsibilities of Boards of Directors in the corporate world and recent years have seen an increased focus and scrutiny of the important role of the Directors in the healthy and ethical functioning of the corporation. Directors of non-profit organisations, or those with equivalent responsibility for the direction and control of an organisation's management, likewise have a responsibility to act with due diligence and a concern that the organisation operates ethically. The directors or those exercising ultimate control over a non-profit organisation need to know who is acting in the organisation's name – in particular, responsible parties such as office directors, plenipotentiaries, those with signing authority and fiduciaries. Directors should exercise care, taking proactive verification measures whenever feasible, to ensure their partner organisations and those to which they provide funding, services, or material support, are not being penetrated or manipulated by terrorists.

15. Directors should act with diligence and probity in carrying out their duties. Lack of knowledge or passive involvement in the organisation's affairs does not absolve a director – or one who controls the activities or budget of a non-profit organisation – of responsibility. To this end, directors have responsibilities to:

- The organisation and its members to ensure the financial health of the organisation and that it focuses on its stated mandate.
- Those with whom the organisation interacts, like donors, clients, suppliers.
- All levels of government that in any way regulate the organisation.

16. These responsibilities take on new meaning in light of the potential abuse of non-for-profit organisations for terrorist financing. If a non-profit organisation has a board of directors, the board of directors should:

- Be able to identify positively each board and executive member;
- Meet on a regular basis, keep records of the decisions taken at these meetings and through these meetings;
- Formalise the manner in which elections to the board are conducted as well as the manner in which a director can be removed;
- Ensure that there is an annual independent review of the finances and accounts of the organisation;
- Ensure that there are appropriate financial controls over program spending, including programs undertaken through agreements with other organisations;
- Ensure an appropriate balance between spending on direct programme delivery and administration;
- Ensure that procedures are put in place to prevent the use of the organisation's facilities or assets to support or condone terrorist activities.

**Oversight bodies**

17. Various bodies in different jurisdictions interact with the charitable community. In general, preventing misuse of non-profit organisations or fundraising organisations by terrorists has not been a historical focus of their work. Rather, the thrust of oversight, regulation, and accreditation to date has been maintaining donor confidence through combating waste and fraud, as well as ensuring that

government tax relief benefits, where applicable, go to appropriate organisations. While much of this oversight focus is fairly easily transferable to the fight against terrorist finance, this will also require a broadening of focus.

18. There is not a single correct approach to ensuring appropriate transparency within non-profit organisations, and different jurisdictions use different methods to achieve this end. In some, independent charity commissions have an oversight role, in other jurisdictions government ministries are directly involved, just to take two examples. Tax authorities play a role in some jurisdictions, but not in others. Other authorities that have roles to play in the fight against terrorist finance include law enforcement agencies and bank regulators. Far from all the bodies are governmental – private sector watchdog or accreditation organisations play an important role in many jurisdictions.

*(i) Government Law Enforcement and Security officials*

19. Non-profit organisations funding terrorism are operating illegally, just like any other illicit financier; therefore, much of the fight against the abuse of non-profit organisations will continue to rely heavily on law enforcement and security officials. Non-profit organisations are not exempt from the criminal laws that apply to individuals or business enterprises.

- Law enforcement and security officials should continue to play a key role in the combat against the abuse of non-profit organisations by terrorist groups, including by continuing their ongoing activities with regard to non-profit organisations.

*(ii) Specialised Government Regulatory Bodies*

20. A brief overview of the pattern of specialised government regulation of non-profit organisations shows a great variety of practice. In England and Wales, such regulation is housed in a special Charities Commission. In the United States, any specialised government regulation occurs at the sub-national (state) level. GCC member countries oversee non-profit organisations with a variety of regulatory bodies, including government ministerial and intergovernmental agencies.

- In all cases, there should be interagency outreach and discussion within governments on the issue of terrorist financing – especially between those agencies that have traditionally dealt with terrorism and regulatory bodies that may not be aware of the terrorist financing risk to non-profit organisations. Specifically, terrorist financing experts should work with non-profit organisation oversight authorities to raise awareness of the problem, and they should alert these authorities to the specific characteristics of terrorist financing.

*(iii) Government Bank, Tax, and Financial Regulatory Authorities*

21. While bank regulators are not usually engaged in the oversight of non-profit organisations, the earlier discussion of the importance of requiring charitable fund-raising and transfer of funds to go through formal or registered channels underscores the benefit of enlisting the established powers of the bank regulatory system – suspicious activity reporting, know-your-customer (KYC) rules, etc – in the fight against terrorist abuse or exploitation of non-profit organisations.

22. In those jurisdictions that provide tax benefits to charities, tax authorities have a high level of interaction with the charitable community. This expertise is of special importance to the fight against terrorist finance, since it tends to focus on the financial workings of charities.

- Jurisdictions which collect financial information on charities for the purposes of tax deductions should encourage the sharing of such information with government bodies involved in the combating of terrorism (including FIUs) to the maximum extent possible. Though such tax-

related information may be sensitive, authorities should ensure that information relevant to the misuse of non-profit organisations by terrorist groups or supporters is shared as appropriate.

*(iv) Private Sector Watchdog Organisations*

23. In the countries and jurisdictions where they exist, the private sector watchdog or accreditation organisations are a unique resource that should be a focal point of international efforts to combat the abuse of non-profit organisations by terrorists. Not only do they contain observers knowledgeable of fundraising organisations, they are also very directly interested in preserving the legitimacy and reputation of the non-profit organisations. More than any other class of participants, they have long been engaged in the development and promulgation of "best practices" for these organisations in a wide array of functions.

24. Jurisdictions should make every effort to reach out and engage such watchdog and accreditation organisations in their attempt to put best practices into place for combating the misuse of non-profit organisations. Such engagement could include a dialogue on how to improve such practices.

**Sanctions**

25. Countries should use existing laws and regulations or establish any such new laws or regulations to establish effective and proportionate administrative, civil, or criminal penalties for those who misuse charities for terrorist financing.