

“COMBATING THE ABUSE OF NON-PROFIT ORGANIZATIONS”
Summary and Commentary of a Document Issued by the
Financial Action Task Force on Money Laundering on October 11, 2002

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A. INTRODUCTION

The Financial Action Task Force on Money Laundering (hereinafter referred to as the ‘FATF’), like so many other supra-national policy-making institutions, maintains an ambiguous, yet substantial law-shaping role with respect to the Canadian legal system and those operating under its umbrella. This independent inter-governmental body was originally convened at the 1989 Paris G-7 Summit with a mandate of combating the laundering of drug money through the establishment and promotion of anti-money laundering policies. Since September 11, 2001, the FATF has expanded this mandate to include the development of financial policy in order to prevent and obstruct those who would use the international financial system for purposes of advancing terrorist objectives.

Non-Profit Organizations (hereinafter referred to as NPOs), defined as “organizations 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’,” (See, “Combating the Abuse of Non-Profit Organizations”. http://www.fatf-gafi.org/pdf/SR8-NPO_en.pdf pg. 1) have been identified by the FATF as, “a crucial weak point in the global struggle to stop such funding at its source.”(Ibid, pg. 1) This categorization derives from both their potential and occasional actual use as conduits for the financing of terrorist purposes. A series of recommended ‘best practices’ have consequently been crafted to counter the perceived deficiencies presently existent with respect to these organizations.

Having first identified NPOs as an area of concern (Eighth Special Recommendation on Terrorist Financing – October 31, 2001 available at <http://www.antiterrorism.ca/intterr.htm#FATF> and http://www1.oecd.org/fatf/SRecsTF_en.htm), the FATF subsequently issued a report, entitled “Combating the Abuse of Non-Profit Organizations, October 11, 2002 (“Report”),” outlining those measures, which in their view would best serve to inhibit the financial misuse of NPOs by terrorist organizations. This Alert reviews these measures - or “recommendations” - contained in the said Report with the purpose of providing NPOs here in Canada with information about the new expectations and legislative developments that may become the operating norm in the future. A brief summary of the specific recommendations and a commentary of the possible implications for NPOs are set out below in order to provide a broader understanding of the nature these new norms may take. In its structure, this Alert parallels that of the Report and consists of two parts: those recommendations applicable to NPOs and those recommendations applicable to regulatory authorities in charge of the oversight of NPOs.

B. RECOMMENDATIONS APPLYING TO NON-PROFIT ORGANIZATIONS

The FATF’s recommendations effectively establish new international standards. NPOs are now expected to act and manage their affairs in a manner that is above reproach. They must take a pro-active role in facilitating greater “transparency” and “accountability”, two themes that recur throughout the Report. Insofar as they directly apply to NPOs, the FATF has highlighted and concentrated its recommendations to three particular areas: financial transparency; program verification; and administration; the highlights of which are outlined below:

1. Financial Transparency

a) Financial Accounting

- That NPOs maintain and remain ready to present full program budgets that account for all program expenses. This also applies to administrative budgets.
- That the identities of all recipients and the manner in which the monies were spent are duly recorded.
- That independent auditing is utilized to better discover abuses.

b) Bank Accounts

- That NPOs maintain registered bank accounts and keep funds in them.
- That registered financial channels are utilized for the transferring of funds, especially internationally, which will serve to bring NPOs into the formal banking system and subject to its various controls and regulations.

2. Programmatic Verification

a) Solicitations

- That solicitations for donations accurately and transparently inform would-be donors precisely what their donations will be used for.
- That NPOs ensure these funds are duly applied.

b) Oversight

- That the following criteria are met:
 - ◆ Projects are actually carried out.
 - ◆ The beneficiaries are real.
 - ◆ The intended beneficiaries receive the funds that were sent for them.
 - ◆ All funds, assets, and premises are accounted for.

c) Field Examinations

- That direct field audits of programs be conducted if the nature of the charitable activity requires it. However, the potential for actual abuse should be considered before embarking on this type of examination.
- That program accomplishments as well as finances be tracked and that all reports be scrutinized for verification.

d) Foreign Operations

- That when the home office and location of operations differ in respect to political jurisdiction, authorities in both endeavour to exchange information and co-ordinate oversight as befits their comparative advantages.
- That NPOs take appropriate measures to account for funds and services rendered in locations other than its home jurisdiction.

3. Administration

a) Control

- That NPOs be able to document their administrative, managerial, and policy control over their operations.
- That in this regard the role of the board of directors is crucial.

b) Responsibilities

- That the board of directors, or whomever is in possession of executive authority, act with due diligence and concern to ensure the organization operates in an ethical manner.
- That the board knows who is acting in the organization's behalf, especially office directors, plenipotentiaries (defined as those possessing full discretionary authority), individuals with signing authority, as well as fiduciaries.
- That the board exercises care and takes proactive verification measures whenever possible to ensure the organization is not being abused for terrorist purposes.
- That the board ensures partner organizations and those receiving funding, services, or material support, are not being penetrated or manipulated by terrorists.

c) Liability

- That directors act with diligence and integrity. Ignorance or passive involvement does not absolve a director of responsibility.
- That directors recognize that they have responsibilities to:
 - ◆ The organization and its members to ensure its continued financial health and focus on its stated mandate.
 - ◆ Those with whom the organization interacts; like donors, clients, and suppliers.
 - ◆ All levels of government possessing regulatory jurisdiction over the organization.

d) Board of Directors Protocol

- That every board member be able to positively identify each other and all executive members.
- That the Board meet on a regular basis and keep records of all decisions made.
- That the Board formalise the manner of director election and removal.
- That the Board conducts an annual independent review of the finances and accounts.
- That appropriate financial controls over program spending are implemented, including programs undertaken through agreements with other organizations.
- That an appropriate balance be maintained between spending on direct program delivery and administration.
- That procedures be established to prevent the use of the organization's facilities or assets to support or condone terrorist activities.

C. RECOMMENDATIONS APPLYING TO REGULATORY AUTHORITIES

As the FATF recounts in its Report, the oversight, regulation, and accreditation powers of regulatory authorities over NPOs have in the past been relatively limited, only as extensive as has been necessary to maintain donor confidence with the minimum amount of oversight and control. That is to say, as extensive as was needed to combat waste and fraud, as well as to ensure that tax-relief benefits went to deserving organizations. However, with the spectre of terrorism perceived by many to be on the rise, the FATF and other governing authorities have felt that a broader scope of oversight is now required to effectively counter the terrorist threat. While acknowledging the differences among countries in respect to the types of agencies in charge of NPO oversight - whether governmental, non-governmental, or both - the FATF has identified and developed five key areas of policy that it would have universally implemented. These include policies regarding government law enforcement and security officials; specialized government regulatory bodies; government bank, tax, and financial authorities; private-sector watchdog organizations; and sanctions; the highlights of which are outlined below:

1. Government Law Enforcement and Security Officials

- ◆ That law enforcement and security officials continue to play a fundamental role in combating the abuse of NPOs by terrorists.
- ◆ That these officials should by extension be given the means to achieve this end.

2. Specialized Government Regulatory Bodies

- ◆ That interagency outreach and discussion within governments on the topic of terrorist financing be carried out – especially between those agencies acquainted with terrorist financing and those that are not.
- ◆ That terrorist financing experts work in cooperation with Non-Profit Organization regulatory authorities to spread awareness of the problem and inform these authorities concerning the specific characteristics of such financing.

3. Government Bank, Tax, and Financial Regulatory Authorities

- ◆ That bank regulators report any suspicious activity and utilize “Know-your-Customer” (KYC) rules, etc, - in order to supplement the controls already existent within the bank regulatory system.

- ◆ That those agencies in charge of collecting financial information on NPOs for the purpose of tax-deductions, share this information with the relevant governmental bodies involved with the “war on terrorism” to the maximum extent possible.

4. Private-Sector Watchdog Organizations

- ◆ That private-sector watchdog and/or accreditation organizations be utilized for their expertise and knowledge of fundraising organizations.
- ◆ That regulatory authorities approach and engage these agencies in developing and putting into place those practices that will best combat the abuse of NPOs.

5. Sanctions

- ◆ That countries make use of already existing laws and regulations or create new laws and regulations to establish effective and proportionate administrative, civil, or criminal penalties for those who misuse NPOs for terrorist purposes.

D. COMMENTARY ON RECOMMENDATIONS

Though labeled recommendations, the policies fashioned by the FATF not only create a de facto binding obligation upon domestic legislators of member countries made up of the 31 countries, territories and two regional organizations of the FATF’s membership, but may even do so upon non-members as well. An example of the indirect binding nature of these recommendations can be found in the existence of the ‘Non-Cooperative Countries and Territories’ (NCCT) index. One of the tasks of the FATF is to monitor whether domestic legislation is being harmonized with the standards it draws up. When a Government is found wanting, it is placed on the NCCT index, which essentially constitutes a last warning before punitive countermeasures are levied, either orchestrated directly by the FATF, or indirectly via national governments acting independently of FATF directives. To date, nine countries are listed on the NCCT index. In this regard, the FATF is much more than a mere policy-making institution, for it does in effect possess international enforcement mechanisms.

By extension, the domestic policies of member countries – and non-members - can be shaped a great deal by FATF recommendations. For NPOs here in Canada, this means that the recommendations contained in the Report may impact legislation or governmental policy in some form or another, as Canadian lawmakers seek

to generally harmonize existing legislation or policy in accordance with FATF guidelines. Such harmonization has already occurred, as evidenced in amendments to the Proceeds of Crime Act implemented by Bill C-36, the Anti-terrorism Act (For a summary of the potential implications of these amendments for NPOs, please see, “Compliance with Anti-terrorism Legislation – Section D,” found at <http://www.carters.ca/pub/article/terrorism/2002/TSC-1120.pdf>). Moreover, even if Canadian legislators were to refrain from such harmonization, it is likely that NPOs operating outside of Canada would nevertheless be impacted by FATF regulations, as implemented in the domestic legal system under which they carry on operations.

E. CONCLUSION

The FATF’s recommendations contained in the Report as summarized in this Alert are likely to impact NPOs, irrespective of jurisdiction, particularly those that operate internationally. It is important, therefore, for Canadian NPOs to be aware of the nature of these recommendations, especially in light of their having recently been identified as a “crucial weak point” in the fight against terrorism. If recent legislation is any indication, they will likely continue to play a significant role in the day-to-day activities of NPOs, operating both nationally and internationally. Whether these recommendations are actually enforced is a matter that will vary according to jurisdiction. However, so long as terrorism is considered a serious threat and the political will exists to compel the alignment of domestic policy and practice in accordance with FATF initiatives, Canadian NPOs should expect a relative consistency in their dealings with other regulatory authorities, both domestic and foreign, and should, therefore, reflect these new international standards in their own operating policies and procedures.