

UNPRECEDENTED ANTI-TERRORISM DUE DILIGENCE STANDARDS EMERGE FOR CHARITIES INTERNATIONALLY

By Terrance S. Carter, B.A., LL.B., Trade-mark Agent and Sean S. Carter, B.A., J.D. Candidate

A. INTRODUCTION

One of the greatest challenges facing charities both in Canada and abroad is the prospect of complying with an ever-expanding body of domestic and international anti-terrorism law. An international campaign, led primarily by the United States, has been in progress to institute a series of “best practices” with regards to anti-terrorism due diligence procedures for charities. These “best practices” were purportedly created in part to assist charities in complying with complex and over-burdensome legislation. The level of information collection and due diligence set out in these “best practices” is not only unprecedented, but exceeds the current operational capability of most charities. Additionally, because of recent developments on the international stage, these “best practices” are perhaps better now understood as expected operating procedures.

There has even been a significant opposition to these “best practices” worldwide, including a call for complete withdrawal of the United States Department of the Treasury’s “best practices” for charities from the Taxation and Criminal Justice Section of the American Bar Association (“ABA”) in April 2006. Recent policies adopted by the Financial Action Task Force (“FATF”) are clearly based on the Treasury Department’s standards and FATF member countries, including Canada, are now responsible for implementing similar requirements for charities in their home jurisdiction. Understanding U.S. policy,

particularly including its campaign for “global oversight” of charities and institution of international due diligence standards is crucial for Canadian charities. Proactive development of anti-terrorism due diligence procedures for charities worldwide, especially those that operate internationally or are engaged in any cross-border transfer of aid or funds, are now a clear necessity. This *Anti-terrorism and Charity Law Alert* will examine the “best practices” and examine its implications for charities.

B. U.S. TREASURY DEPARTMENT AND ITS “BEST PRACTICE” GUIDELINES

In 2001, the United States Department of the Treasury (“Treasury Department”) was directed to work with other U.S. federal agencies and the international community to develop a “sustained and comprehensive” campaign against sources and conduits of terrorist financing.¹ Shortly after, charitable organizations were identified as a “weak link” in the global campaign against terrorism, and in November 2002 the Treasury released its first *Anti-terrorist Financing Guidelines: Voluntary Best Practices for U.S. Based Charities* (“Guidelines”).² These initial guidelines came under substantial criticism, as the resulting general confusion was widespread among affected organizations as to *how* and even *if* these sweeping guidelines may be met.

In November 2005, the Treasury Department issued a revised version of the Guidelines. However, the concerns of the public and private sector about the substantial impact on charities has not abated. Because of these substantial concerns with the revised Guidelines, the Taxation and Criminal Justice Section of the ABA called for a complete withdrawal of the Guidelines in April 2006.³ The Treasury Department’s Guidelines should be of particular note not only to U.S. based charities but charities world-wide because they have become the foundation for the international regime of “best practice” standards.

C. “INTERNATIONAL ENGAGEMENT” AND “GLOBAL OVERSIGHT”

The Treasury Department has made it clear in the past few years that it understands international engagement to be a key focus of its energies. The Treasury Department’s website indicates its central means of combating terrorist financing to be bilateral engagement and involvement with multilateral bodies, such as the Financial Action Task Force (“FATF”). Through this international engagement, the Treasury Department aims to

¹United States Department of State, “Executive Order 13224 Fact Sheet”, available at <http://www.state.gov/s/ct/rls/fs/2002/16181.htm>.

²Financial Action Task Force on Money Laundering, “Combating the Abuse of Non-profit Organizations: International Best Practices” 11 October 2002.

³Taxation Section, American Bar Association. “Comments on the U.S. Department of the Treasury Anti-terrorist Financing Guidelines: Voluntary Best Practices for U.S. Based Charities” April 5, 2006, available at <http://www.abanet.org/tax/groups/eo/040406antiterroristfincomment.pdf>.

heighten “global oversight of the international charitable sector” and establish “international standards” to combat terrorist financing that uses charitable organizations as conduits or fundraisers.⁴

The Treasury Department is aggressively seeking out charities that are perceived or suspected by members of the public to be violating U.S. standards and law. This campaign has been made particularly efficient with the launch of the Treasury Department’s Online “Counter-Terrorist Referral Form for Charities.”⁵ Visitors to the site are encouraged to fill out the online form if they have any information concerning a tax-exempt organization, or anyone receiving funds from a charitable organization, that may be involved in “suspicious financial activity” possibly related to supporting terrorism.

D. THE EMERGING STANDARDS FOR ANTI-TERRORISM DUE DILIGENCE

The Treasury Department’s Guidelines set the level of due diligence expected of charitable organizations in the U.S. and serve as a global benchmark in the area. The procedures in the Guidelines include oversight and monitoring of a variety of individuals and entities including: directors, “key employees,” affiliates, and recipient organizations. The Guidelines also lay out standards for governance and financial practice for charities. As will be discussed in more detail later, these Guidelines have been the basis for recent additions to FATF policy, which countries like Canada are obliged to implement as member countries.

1. Information Collection

One of the key thrusts of the Guidelines is for charities to develop their own collection and analysis of information concerning certain individuals within its own organization, of affiliate or subsidiary organizations, and recipient organizations. The Guidelines identify those individuals about which this information must be retained, including: “key employees” of the organization; key, non-U.S. employees working abroad; key employees of any subsidiaries or affiliates receiving funds from the organization; and board members of any subsidiaries or affiliates receiving funds from the organization.

The contentious due diligence standards in the Guidelines concerning information collection seem to have actually expanded from the original Guidelines. The ABA report recognized that the information collection in the original guidelines were already “well beyond the capacity of most charitable

⁴ United States Department of the Treasury, “Protecting Charitable Organizations” available at <http://www.ustreas.gov/offices/enforcement/key-issues/protecting/index.shtml>.

⁵ See <http://www.ustreas.gov/offices/enforcement/feedback.html>.

organizations.”⁶ In the face of these emerging standards, charities need to consider significant proactive additions and changes to their operating procedures.

2. Ongoing Database Searches and Basic Vetting

The Guidelines stipulate that information collected should be maintained and checked against various databases of “designated” individuals and entities. This procedure represents a substantial due diligence requirement considering that the list maintained by the Treasury Department’s Office of Foreign Assets Control (“OFAC) alone recently exceeded 325,000 names.⁷ In addition, the Guidelines recommend a “basic vetting” of the personal and organizational data, a potentially Herculean process involving intensive on-line searches to discover whether the individual or organization has ever been even suspected of being linked to terrorist activities. This involves searching a variety of information, including: websites of affiliates, donors and recipient organizations; news organizations and their archives; and government agencies and their archived press releases and reports.

3. Recipient Organizations

The Guidelines identifies recipient organizations as a particular focus for anti-terrorism due diligence standards. Information must be maintained concerning current and historical jurisdictional information of the recipient organization; information on individuals and entities the recipient plans to support; and information on operating history and founding members of the recipient organization. Additionally, charities are directed to require recipients to “certify” that they do not employ, transact with, provide services to, or otherwise deal with any individuals, entities, or groups connected with terrorist activities or with any persons known to the recipient to support terrorism. The Guidelines also direct charities to perform routine, on-site audits of recipients to ensure that the recipient has taken adequate measures to protect its charitable resources from diversion to, or abuse by, terrorists or their support networks. All of these due diligence procedures, including those regarding recipient organizations are not a one time exercise, rather the Guidelines direct that there be an ongoing system of a monitoring and due diligence.

⁶ Taxation Section, American Bar Association. “Comments on the U.S. Department of the Treasury Anti-terrorist Financing Guidelines: Voluntary Best Practices for U.S. Based Charities” (5 April 2006), available at <http://www.abanet.org/tax/groups/eo/040406antiterroristfincomment.pdf>.

⁷ Walter Pincus and Dan Eggen, “325,000 Names on Terrorism List”, *The Washington Post* (15 February 2006), A01.

4. Becoming More Than “Voluntary”

With respect to the Guideline’s application to U.S. charities, the ABA report states that they “believe that the title, ‘U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices For U.S.-Based Charities’ misstates both the content and the purpose of the Guidelines.” The ABA notes that various U.S. federal agencies are already directing charitable organizations to comply with the Guidelines, suggesting that compliance is more than “voluntary.” The ABA report also indicates that the failure of an organization to adhere to a “best practice” promulgated by the federal government, when the operative regulatory standard is that of “reasonable” or “prudent” behaviour, suggests that the Guidelines may have real, immediate legal import and may not be “voluntary” in all circumstances absent a specific disclaimer that the Guidelines have no relationship to reasonable or prudent behavior as the concept is incorporated into U.S. federal tax law. The Treasury Department seems to be, as the ABA report recognizes, in a steady process of developing more detailed and stringent standards and may be incorporated as regulation or introduced as legislation the once the Guidelines are believed to be of sufficient strength and purpose.

E. THE FATF AND THE RECENT “INTERPRETATIVE NOTE”

One of the key recent developments that has solidified the need for Canadian and other international charities to take careful note of the Treasury Department’s Guideline’s is the FATF’s recent publication of “Interpretative Note to Special Recommendation VIII: Non-Profit Organizations” (“Interpretative Note”) in February 2006.⁸ Together, the Interpretive Note and the FATF’s 2002 publication of its own “International Best Practices” are an integral step in ensuring that these “best practices” become enforceable by law as regulation, legislation or some other method in jurisdictions worldwide.⁹ The FATF is the global money laundering supervisory body of which Canada is a member country and to which Canada has specific obligations to domestically implement these policy documents.¹⁰

⁸ Financial Action Task Force, “Interpretative Note to Special Recommendation VIII: Non-Profit Organizations,” available at <http://www.fatf-gafi.org/dataoecd/16/6/36174688.pdf>

⁹ Financial Action Task Force, “Combating the Abuse of Non-Profit Organizations: International Best Practices,” available at <http://www.fatf-gafi.org/dataoecd/39/19/34033761.pdf>

¹⁰ For more information concerning the FATF, its structure, organizations and Canada’s responsibilities as a member please refer to Anti-Terrorism and Charity Law Alert No. 3 “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” available at <http://www.carters.ca/pub/alert/ATCLA/atcla03.pdf>.

The Interpretive Note mirrors the Treasury Department's "best practices" in key ways, including stipulating that non-profit organizations ("NPOs") should maintain information on their key employees, senior officers, board members and trustees. The same type of oversight and information collection and due diligence is set with regards to beneficiaries and associate NPOs. This information is to be vetted and checked against relevant international lists of designated individuals and entities. In addition, the Interpretive Note directs countries to ensure effective cooperation and information at all levels of appropriate authorities that hold information on NPOs, measures consistent with the program of "global oversight" of the non-profit organizations as originally put forward by the Treasury Department.

Canada's role in the FATF and the international community is becoming more and more prominent, further heightening the potential pressure to publicly hold itself out as a model of implementation of FATF and other international institutional policy. Canada's public role in this area will be heightened when Canada assumes the one-year rotating presidency of the FATF in the coming months. In addition, the Egmont Group recently announced that it would make Toronto, Ontario its permanent home and base of global operations. While the Egmont Group does not set global scrutiny standards like the FATF, it does promote co-operation and information sharing among national anti-laundering agencies.¹¹

F. IMPACT FOR CANADIAN CHARITIES

Though these standards are described with words like "voluntary" and "best practices," the unfolding reality is that these standards will be the expected norm of operation for charities in Canada and beyond. The standards of the U.S. Treasury Department are global benchmarks for operation and procedure, and any charity wanting to protect itself, its employees and those that may depend on its operations, need to consider due diligence and proactive action that reflects these standards. It is important to note that the Treasury Department's Guidelines and other U.S. Policy regarding NGOs and charities impacts Canadian charities in and of themselves, regardless of being incorporated into "Interpretive Notes" of FATF policy.¹² For example, the information sharing and data collection alone carried out by Canada and the U.S. means that assessments and suspicions made on the basis of U.S. policy by U.S. officials becomes the foundation or impetus to the

¹¹ Chase, Steve. "Top sleuths to set up home base in Toronto" *The Globe and Mail* (8 July 2006), A1.

¹² For further discussion, see Terrance S. Carter and Sean S. Carter, "Worldwide Implications of America's Emerging Policies Concerning NGOs, Non-Profits and Charities" in *Anti-terrorism and Charity Law Alert* No. 5 (30 November 2004), available at www.antiterrorismlaw.ca.

investigation of charities in Canada. This, at the very least, could involve the freezing of charitable assets and a shut-down of operations during the course of the investigation by Canadian authorities.

International “best practice” standards for charities have been recognized in Canada for several years now. Canada Revenue Agency (“CRA”) has directed Canadian charities working internationally to the Treasury Department’s Guidelines since their original publication in 2002. CRA recently revised its publication “Charities in the International Context” to make special note of not only the revised Guidelines but also recent FATF’s recent Interpretative Note.¹³ Particularly in the absence of “made in Canada” due diligence standards, what CRA has essentially done is incorporate the Treasury Department Guidelines and FATF Interpretative Notes into *de facto* Canadian law.

Even now, before these standards are formally instituted in Canada as regulation, legislation or in some other form, this due diligence and proactive action on behalf of charities is already a necessity in response to Canada’s existing anti-terrorism legislation. In the face of broad, sweeping legislation that is practically impossible to ensure complete and ongoing compliance with, directors, officers and charities have little choice other than institute their own anti-terrorism due diligence procedures in order to minimize the risk of contravention of the legislation and fulfill their duty to protect the charity and its assets. The promulgation of these “best practice” standards is a strong signal that this type of due diligence response, despite its onerous nature, is an expected response on behalf of charities. Charities should consult with legal counsel who is familiar with this specific area of law and regulation, and work towards developing a comprehensive plan to implement anti-terrorism procedures in its operations.

¹³ Canada Revenue Agency, “Charities in the International Context” available at <http://www.cra-arc.gc.ca/tax/charities/international-e.html>

G. CONCLUSION

What anti-terrorism policy implicitly requires, and what is confirmed by the spread of these “best practices,” is that compliance necessarily involves a significant, proactive review and possible overhaul of the operations of charities. Anti-terrorism procedures touch nearly all areas of operations, including the hiring of directors, officers, key employees, transferring aid internationally, and establishing the ability to conduct ongoing searches and continuous monitoring. Even though these standards are innocuously referred to as “voluntary” and purported to be “best practices,” it has become apparent that they are quickly becoming the accepted operational norm for charities, especially those involved in any international transactions, programs or activities.

Understanding the U.S. Treasury Department’s policies will assist Canadian charities not only because the Guidelines have implications in and of themselves, but also because they serve as the global benchmark and foundation for policies that will soon be a reality here in Canada. Canadian charities, with the assistance of legal counsel familiar with this field, need to aggressively and proactively assess their current operating structure and develop a specific plan for instituting anti-terrorism due diligence procedures that will help minimize the risk of contravention and bring the charity in line with international standards.



CARTERS PROFESSIONAL CORPORATION
Société professionnelle Carters
Barristers, Solicitors & Trade-mark Agents
Affiliated with **Fasken Martineau DuMoulin LLP**
Avocats et agents de marques de commerce
Affilié avec Fasken Martineau DuMoulin S.E.N.C.R.L., s.r.l.

Offices / Bureaux
Ottawa (613) 235-4774
Mississauga (416) 675-3766
Orangeville (519) 942-0001
Toll Free: 1-877-942-0001

By Appointment / Par rendez-vous
Toronto (416) 675-3766
London (519) 937-2333
Vancouver (877) 942-0001

www.charitylaw.ca

DISCLAIMER: This is a summary of current legal issues provided as an information service by Carters Professional Corporation. It is current only as of the date of the summary and does not reflect subsequent changes in the law. The summary is distributed with the understanding that it does not constitute legal advice or establish the solicitor/client relationship by way of any information contained herein. The contents are intended for general information purposes only and under no circumstances can be relied upon for legal decision-making. Readers are advised to consult with a qualified lawyer and obtain a written opinion concerning the specifics of their particular situation.

© 2006 Carters Professional Corporation