



**Asia/Pacific Group
on Money Laundering**

ASIA/PACIFIC GROUP ON MONEY
LAUNDERING

Typologies Report

NPO SECTOR VULNERABILITIES

Adopted by APG Members at the 14th Annual Meeting

India, 22 July 2011



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EXECUTIVE SUMMARY

Despite continued efforts to counter the financing of terrorism (CFT), non-profit organizations (NPOs) around the world continue to be abused by terrorists. This report aims to assist Asia/Pacific Group on Money Laundering (APG) members with the with the implementation and enforcement of the Financial Action Task Force's (FATF) Special Recommendation VIII, which calls on FATF members to review the adequacy of their laws and regulations relating to NPOs as part of their larger CFT strategy.

Overall, this report is a resource for policy formation and encourages APG members to mitigate the risk of terrorist abuse and enhance transparency and accountability within their respective NPO sectors by improving domestic NPO regulation. More specifically, this report promotes the adoption of a risk-based approach – that is, tailoring existing regulatory mechanisms to the vulnerabilities unique to the NPO sector in question. NPO sectors across APG member jurisdictions vary significantly, thus making a “one-size-fits-all” regulatory system ineffective. Instead, this report provides a flexible structural framework to help members adapt domestic NPO regulation to the needs of their sector. This requires ongoing detailed review of the sector itself and ongoing risk assessments to identify changing vulnerabilities within the sector, followed by ongoing evaluations of gaps within current laws and regulations.

Chapter 1, *The NPO “Sector”*, briefly explores the growing, positive global role of NPOs and the subsequent need to protect them from terrorist abuse. It also highlights that the term NPO “sector” is misleading because the characteristics of NPOs differ substantially, both across APG members as well as within them.

Chapter 2, *Scope of the Problem*, explains that although terrorist groups have abused NPOs to finance their operations, NPOs have also been abused for other purposes, such as weapons smuggling or recruitment. Accordingly, the term “terrorist resourcing” provides a more comprehensive characterization of the abuse than the term “terrorist financing.” In addition, a distinction must be made between “complicit” and “exploited” NPOs. Chapter 2 also discusses the prevalence of terrorist abuse of NPOs and demonstrates that the threat continues to exist due to several vulnerabilities unique to the sector, most notably, lack of oversight.

Chapter 3, *The Merits of Effective Regulation: CFT is an Intrinsic By-Product*, argues that regulatory oversight of the NPO sector improves transparency and accountability among NPOs, and thus consequently deters, detects, and disrupts related terrorist activity. CFT is thus an intrinsic by-product of regulation. Effective NPO regulation can also serve to complement other CFT efforts, such as law enforcement. Despite the benefits of regulation, however, most APG members do not have effective regulatory systems. This can be explained by numerous challenges faced by APG members, in particular lack of information regarding domestic NPO sectors and their vulnerabilities.

Chapter 4, “Step 1” - *Knowing the Risks*, emphasizes that, in accordance with Special Recommendation VIII, a “one-size-fits-all” approach to regulation is not

effective. Rather, a risk-based approach is necessary in order to tailor regulations to the risks inherent to a jurisdiction's NPO sector. The first step in adopting a risk-based approach is the collection of information regarding one's NPO sector, following by a risk-assessment of vulnerabilities. Given that only some APG members have conducted detailed reviews of their NPO sectors and fewer still have performed risk assessments, a comprehensive study of specific typologies, vulnerabilities, risk indicators, and regulatory systems applicable across all jurisdictions is not possible at this time.

Chapter 5, *A Structural Framework for Enhancing Regulation*, provides a structural framework to assist APG members with designing risk-based regulations. Although regulatory structures differ substantially between APG members, the framework is sufficiently broad to account for these differences. Specifically, the framework identifies nine strategic gaps in NPO sector regulation, and nine corresponding phases of action to address these gaps, beginning with assessments of the NPO sector itself, its vulnerabilities, and current laws and regulations.

Chapter 6, *Caveats for Regulation*, presents APG members with numerous caveats regarding NPO regulatory mechanisms. For example, regulation should not be pursued purely for CFT purposes. Use of CFT-focused regulatory measures to constrain the sector would be both counter-productive and would risk alienating NPOs. Further, measures should be proportional to the risk and flexible enough to accommodate particular types of NPOs or situations. Chapter 6 also explores the benefits of NPO self-regulation.

Chapter 7, *Risk Indicators and Case Studies*, recommends that jurisdictions develop their own set of indicators of possible risk of terrorist abuse specific to their NPO sectors. Case studies of terrorist abuse of the NPO sector and corresponding risk indicators are provided for APG members as a guide for the development of risk indicators relevant to their own NPO sectors. This section is followed by a more elaborate sample of a Canadian risk indicator.

Lastly, **Chapter 8, *Policy Implications***, presents policy implications stemming from the recommended adoption of a risk-based domestic regulatory system for NPOs. They include:

- prioritizing NPO regulation and ensuring the necessary resources are available;
- conducting a detailed review of one's NPO sector and subsequent detailed risk assessment of vulnerabilities;
- including the NPO sector in all stages of regulation and CFT planning that may affect them;
- striking a balance between seemingly opposing aims, such as transparency and privacy, accountability and flexibility, and enforcement and self-regulation;

- the need to continue to share best practices between governments, international organizations, NPOs, and other stakeholders as a means of regularly improving the regulatory system.

INTRODUCTION

1. Following the attacks of September 11, 2001 in the United States and the growing need for a truly global counter-terrorism strategy, the Financial Action Task Force (FATF) issued a list of nine special recommendations to combat terrorist financing (TF).¹ This report focuses specifically on Special Recommendation VIII (SR VIII), which calls on FATF members to review the adequacy of their laws and regulations relating to non-profit organizations (NPOs).

2. According to the FATF, “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.”² Numerous cases from around the world have demonstrated how terrorists have successfully abused this weak point to finance or support their operations. Well-known cases include the International Islamic Relief Organization (IIRO) Philippine Branch, as well as the Holy Land Foundation for Relief and Development (HLF) in the United States.

3. Given that members and observers of the Asia/Pacific Group on Money Laundering (APG) are committed to the effective implementation and enforcement of internationally accepted standards for countering the financing of terrorism (CFT),³ it is critical that APG members pursue the steps outlined in SR VIII to mitigate the risk of abuse of NPOs. To help achieve this, experts within the APG’s members, and its observers, have undertaken the following examination of vulnerabilities in the NPO sector to terrorist abuse. Specifically, this report aims to:

- draw lessons from literature published to date with regard to terrorist abuse of NPOs;
- encourage more effective domestic risk-based regulation of the NPO sector;
- assist APG members in meeting the standards established by the FATF by encouraging a sector-specific risk indicator development process; and,
- highlight potential policy implications for effective implementation of regulation of the NPO sector.

¹ Financial Action Task Force on Money Laundering (FATF). “FATF IX Special Recommendations,” FATF Standards, October 2001, <http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf> (accessed February 2, 2011).

² Financial Action Task Force on Money Laundering (FATF). “Combating the Abuse of Non-profit Organisations: International Best Practices,” October 11, 2002, <http://www.fatf-gafi.org/dataoecd/53/53/34260889.pdf> (accessed February 2, 2011).

³ “About APGML: History and Background,” *APGML web site*, <http://www.apgml.org/about/history.aspx> (accessed November 30, 2010).

METHODOLOGY

3. This paper draws on multiple publications relating to NPO vulnerabilities to terrorist abuse. The FATF has drafted much of the literature on this topic, including the 2002 Best Practices paper and the 2006 Interpretive Note to SR VIII, which outlines general principles, definitions, and measures to mitigate abuse.⁴ Since 2002, the FATF has also included a section on NPOs in their annual money laundering typologies reports, as has the APG. The World Bank and the European Commission have also published reports on this subject.

4. Publications, however, are not limited to multilateral organizations. The Center on Global Counterterrorism Cooperation (CGCC) recently issued a discussion paper in preparation for a United Nations Counter-Terrorism Committee Executive Directorate (UN CTED) experts meeting in London and a regional meeting in Bangkok. In addition, several national agencies, such as the Charity Commission for England and Wales, have also contributed to the literature on this topic. Information published by the NPO sector itself has also provided invaluable insight.

5. Much of the data presented in this report was further derived from APG member's NPO sector reviews, and APG typology workshops in both Siem Reap, Cambodia (2009) and Dhaka, Bangladesh (2010) in which NPO vulnerabilities were addressed.

6. The sample risk indicator provided in Chapter 7 is based on extensive research undertaken by the Canada Revenue Agency (CRA). A detailed literature review of academic articles, media stories, NPO sector publications, as well as government, international organization, and research institution publications have informed the indicator presented here, as have file observations of confirmed and suspected cases of terrorist abuse of Canadian NPOs

⁴ FATF, "FATF IX Special Recommendations."

CHAPTER 1 - THE NPO “SECTOR”

INCREASING IMPORTANCE OF NPOs

7. The role of NPOs in the world’s international system grew considerably in the latter half of the 20th Century and continues to grow today. NPOs have become prominent actors in the global aid architecture and strongly influence domestic government policy as well as international standards, many of which pertain to human rights, health, education, and other critical social needs.

8. Much of this growing role is due to the unprecedented size of the sector, now numbering in the millions worldwide. NPOs also contribute more financially than ever before. According to a Johns Hopkins University study, the annual operating expenditure of the NPO sector in 36 jurisdictions is an estimated \$1.3 trillion USD,⁵ compared to \$119.6 billion USD in net Official Development Assistance provided by members of the Organization for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC).⁶ According to the same study, the global NPO sector also employs over 40 million people and transfers approximately \$20 billion to developing jurisdictions annually.⁷

9. The importance and influence of the NPO sector cannot be overstated. NPOs often provide crucial social services that cannot or will not be provided by governments. Similarly, NPOs often provide a voice for the most marginalized populations. These activities may play a vital role in mitigating some of the root causes of terrorism, such as poverty and discrimination, that likely motivate at least some terrorist groups and individuals.⁸

10. As noted by the CGCC, the NPO sector is “a central mechanism in the global voluntary redistribution of wealth and provision of assistance to those most in need, and fulfils a range of positive cultural, religious, education and other social purposes.”⁹ Given that the value-added and number of NPOs worldwide only appear to be increasing, it is more urgent than ever to protect them from abuse, particularly from terrorists.

⁵ Lester M. Salamon et al., *Global Civil Society: Dimensions of the Nonprofit Sector* (Baltimore, MD: Johns Hopkins Center for Civil Society Studies, 2004).

⁶ Based on 2009 figures. “Development aid rose in 2009 and most donors will meet 2010 aid targets,” *Organization for Economic Co-operation and Development (OECD) – Development Co-operation Directorate web site*, http://www.oecd.org/document/0,3746,en_2649_34447_44981579_1_1_1_1,00.html (accessed February 21, 2011).

⁷ Salamon, *Global Civil Society*.

⁸ Paul K. Davis and Kim Cragin, eds., “Social Science for Counterterrorism: Putting the Pieces Together,” *RAND National Defense Research Institute*, 2009.

⁹ Center on Global Counterterrorism Cooperation (CGCC). “Expert working group meeting on preventing abuse of the non-profit sector for the purposes of terrorist financing,” *Discussion Paper*, January 18-20, 2011.

THE NPO “SECTOR” AND THE ASIA/PACIFIC REGION

11. As highlighted in a recent publication by the CGCC, the term NPO “sector” is misleading due to its implication that all NPOs are alike.¹⁰ In fact, NPOs around the world vary enormously in terms of their aims and activities, size, and revenue. The diversity among NPOs throughout the Asia/Pacific region is no different, whether comparing NPOs across jurisdictions, or within a given jurisdiction. In the United States of America, for example, there are over 1.35 million charities, foundations, and religious organizations.¹¹ Nauru, on the other hand, has approximately 25 NPOs.¹² NPOs also often range from small organizations run entirely by a single volunteer, to large federation-styled organizations with 40,000 employees such as World Vision International, which raised over \$2.575 billion USD in 2009.¹³

12. The geographical areas of operation of NPOs further vary substantially. In APG members where social welfare infrastructure is relatively advanced, such as Canada, Australia, and the United States, thousands of NPOs carry out programs and projects primarily overseas where social infrastructure is often less advanced. NPOs based in richer jurisdictions also generally have large donor bases (and often large diaspora populations) eager to send money to help those living in developing jurisdictions. In other APG members, however, the situation likely differs. NPOs in developing jurisdictions, whether local or foreign, ostensibly prefer to focus their efforts on domestic projects where the need is greatest.

13. Clearly, the characteristics of NPOs in APG members vary significantly. As we will see in Chapter 4, these differences have important ramifications for risk assessments and CFT strategies.

BOX 1. CLOSER LOOK AT CANADA

Canada’s non-profit sector is composed of a variety of charities and not-for profit organizations that range in size and represent many different causes.

Canadian charities are organizations registered with the Charities Directorate of the Canada Revenue Agency (CRA). They can be registered under either the relief of poverty, the advancement of education, the advancement of religion, or for other purposes beneficial to the public. Registered charities are able to issue tax receipts to donors and are tax-exempted. Continued registration is, among other things, dependent upon the submission of annual information returns to the CRA.

¹⁰ CGCC, “Expert working group meeting on preventing abuse of the non-profit sector...”

¹¹ United States of America. *NPO sector review submitted to the Asia/Pacific Group*, 2006.

¹² Nauru. *Status report submitted to the Asia/Pacific Group prior to typologies workshop*, Cambodia, October 2009.

¹³ 2009 Annual Review, *World Vision International web site*, [http://www.wvi.org/wvi/WVIAR2009.nsf/0D0BC6D2A56F63AF882576DC00252534/\\$file/wvi_ext_ar_A4_2009_0210_d07.pdf](http://www.wvi.org/wvi/WVIAR2009.nsf/0D0BC6D2A56F63AF882576DC00252534/$file/wvi_ext_ar_A4_2009_0210_d07.pdf) (accessed 2011-05-20).

Not-for profit organizations are able to operate within Canada for any purpose other than to gain profit. While there is no formal registration process, they are required to file an information return each year with the Agency.

Over 85,000 registered charities in Canada are regulated by the CRA.¹⁴ Each charity is subject to the terms and conditions set forth in the *Income Tax Act* and is held accountable to the *Anti-terrorism Act*. The *Charities Registration (Security Information) Act* has been developed as a mechanism to more efficiently use intelligence to help combat the potential threat of terrorism in the registration system for charities.

The CRA uses a risk-based approach to identify potential terrorist threats. Regular intergovernmental coordination between the CRA, the police, and other intelligence-based government organizations are used to monitor and protect the sector. This risk-based approach has led to the refusal to register many charities years before they were listed as supporters of terrorist groups in Canada and elsewhere.

BOX 2. CLOSER LOOK AT MALAYSIA

Malaysia's non-profit sector is composed of organizations that generally take the form of either a charitable corporation or a society. A charitable corporation, identified as a company limited by guarantee, must register with the Companies Commission of Malaysia (CCM) and is held accountable by the *Companies Act* of 1965. The CCM is responsible for registering, supervising, and controlling the activities of these charitable corporations. These charitable corporations are formed to provide recreation, promote commerce, industry, art, science, religion, charity, or any other objects useful to the community.

Societies are registered, monitored, and controlled by the Registry of Societies Malaysia (ROS), within the Ministry of Home Affairs, and are held accountable by the *Societies Act* of 1966. All registered charities under the *Companies Act* or *Societies Act* may apply for tax exemption under the *Income Tax Act* 1967. The Inland Revenue Board stipulates certain conditions that registered institutions must comply with in order to qualify for tax exemption.

Societies are further identified as organizations (not companies, trade unions, or cooperatives) with seven or more members. They are categorized under any of the following causes: religion, welfare, social and recreational, women's issues, cultural issues, sports, youth, education, politics, or a general category. There are also mutual-benefit societies, trade associations, and employment associations.

The Enforcement Office within the CCM and ROS is used to monitor, supervise, and investigate registrants using a risk-based approach. CCM monitors them through routine site visits and inspections. All registered Malaysian NPOs are subject to the

¹⁴ "Charities Listings," *Charities and Giving* section of the Canada Revenue Agency (CRA) web site. <http://www.cra-arc.gc.ca/ebci/haip/srch/basicsearchresult-eng.action?s=registered&k=&p=1&b=true> (accessed 2011-03-03).

Anti-Money Laundering Act of 2001 and are scrutinized by an array of institutions, including financial and banking institutions.

CHAPTER 2 - SCOPE OF THE PROBLEM

FINANCING VS. RESOURCING

14. Although SR VIII specifically refers to the threat of “terrorism financing,” it is important to emphasize that terrorist abuse of NPOs extends beyond the diversion of monetary funds. Several known cases demonstrate that terrorists have abused NPOs in a variety of ways. The following are some examples of types of abuse, and do not represent a comprehensive list.

15. Terrorists have abused NPOs by:

- diverting finances;
- diverting materials (such as gifts-in-kind);
- using them as an intermediary to local partners that divert financing/materials;
- using them to facilitate travel and/or board travellers;
- using them as a front or cover for illicit activities, such as the transfer of arms;
- openly using them to provide social services as a means to solicit public support;
- using them as a platform to distribute messaging as a means to gain political/ideological support;
- using them to radicalize and/or enlist individuals;
- taxing them for access to certain impoverished areas;
- kidnapping and ransoming employees;
- impersonating employees to obtain access to particular areas/people; and/or
- using an NPO’s name to raise funds, without the NPO’s knowledge.

16. These examples illustrate that many other facets of NPOs can be abused for terrorist purposes and that finances are not the only vulnerability. As such, the term “terrorist resourcing” provides a far more accurate picture of the abuse than the term “terrorist financing.” Terrorist resourcing encompasses the use of funds, materials, personnel and other associated individuals, beneficiaries, as well as property to further a terrorist cause.

COMPLICIT VS. EXPLOITED NPOs

17. Regardless of the means by which an NPO can be abused by terrorists, one must differentiate between “complicit” NPOs and “exploited” NPOs.¹⁵ “Complicit” NPOs are essentially front organizations, while “exploited” NPOs are organizations in which insiders or outsiders abuse a legitimate NPO without the knowledge of most of its members. In both cases, it is possible to have “witting” or “unwitting” donors.¹⁶ It is unknown whether the majority of terrorist resourcing cases consist of complicit or exploited NPOs,¹⁷ and data may differ according to jurisdiction.

PREVALENCE OF ABUSE

18. It is currently impossible to determine the extent to which terrorist abuse of NPOs occurs worldwide, including among APG members. NPO sector reviews and typology reports submitted by APG members indicate that the vast majority of members have received minimal numbers of Suspicious Transaction Reports (STRs) involving NPOs,¹⁸ and fewer still have pursued prosecutions or successfully convicted NPO board members or staff. Similarly, only 0.0000554% of American NPOs have allegedly been implicated in terrorism.¹⁹

19. Many governmental authorities have, however, reported that NPOs consistently appear in investigations pertaining to terrorist activities. For example, Canada’s financial intelligence unit (FIU), the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), reported in 2006 that approximately one third of all disclosures to intelligence partners relating to TF or other national security threats to Canada involved NPOs.²⁰ In 2007, this figure was one fifth.²¹ Similarly, the United Kingdom’s HM Treasury has reported that “‘a significant portion’ of terror

¹⁵ Emile van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing: A Proportionate Response,” *World Bank Working Paper No. 208*, 2010, <http://issuu.com/world.bank.publications/docs/9780821385470> (accessed December 20, 2010).

¹⁶ Emery Kobor, “NPOs Used for Financing Terrorism: The U.S. Experience” (presentation on behalf of the U.S. Department of the Treasury, Asia/Pacific Group Typologies Workshop, Dhaka, October 25-28, 2010).

¹⁷ van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing.”

¹⁸ Exceptions in which APG members have reported large numbers of STRs involving NPOs include Australia and Indonesia, among others.

¹⁹ Doug Rutzen (presentation on behalf of the International Center for Not-for-Profit Law (ICNL) at the United Nations Counter-Terrorism Committee Executive Directorate (UN CTED) experts meeting, London, January 18-20, 2011).

²⁰ Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). “FINTRAC Annual Report 2006,” 2006, <http://www.fintrac-canafe.gc.ca/publications/ar/2006/AR-eng.pdf> (accessed February 2, 2011).

²¹ Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). “FINTRAC Annual Report 2007,” 2007, <http://www.fintrac-canafe.gc.ca/publications/ar/2007/ar-eng.pdf> (accessed February 2, 2011).

finance investigations included analysis of links to charities.”²² In addition, 43 NPOs and 29 associated individuals were designated terrorist supporters by the US Treasury Department by 2006, accounting for fifteen percent of all designated supporters or financiers at the time.²³

20. These figures clearly demonstrate that NPOs continue to be abused by terrorists. Although statistics on terrorist abuse of NPOs may appear insignificant relative to the volume of NPOs worldwide, low incidence rates are likely attributable, at least in part, to poor detection. In all probability, the incidence of terrorist resourcing involving NPOs is higher than the figures presented above, particularly in jurisdictions in which NPO regulation is ineffective and the sector is theoretically more exploitable. Thus, the impact of terrorist abuse of NPOs may in fact be more serious than currently thought.

VULNERABILITIES IN THE NPO SECTOR

21. NPOs clearly continue to be perceived as attractive conduits for terrorists. Ironically, many of the vulnerabilities unique to NPOs that make them attractive sources of funds and/or resources to terrorists also double as some of the sector’s greatest strengths. These vulnerabilities are outlined below and demonstrate why efforts to mitigate threats to the integrity of the NPO sector must be prioritized.

22. First, **NPOs “enjoy the public trust.”**²⁴ NPOs are generally considered to be reputable, typically because they help the needy and advocate on behalf of marginalized populations. As a result, NPOs historically have not been expected to strongly demonstrate qualities such as transparency and accountability. Although this is slowly changing, lax expectations have provided terrorists with ample opportunity to take advantage of NPOs and conceal their activities.

23. Second, **NPOs have access to considerable sources of funds (ranging from hundreds to millions of dollars) which are often cash-intensive.**²⁵ Although terrorist activities do not necessarily require extensive funding, large, structured terrorist organizations that do require significant resources have diverted substantial sums of money from NPOs in the past to support and conceal recruitment, training, housing, travel, and the procurement of supplies.

24. Third, **NPOs sometimes “have a global presence that provides a framework for national and international operations and financial transactions,**

²² CGCC, “Expert working group meeting on preventing abuse of the non-profit sector...” 2. Unable to access HM Treasury, “Financial Challenge to Crime and Terrorism” (February 28, 2007).

²³ United States Department of Treasury. “U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities,” revised 2006, http://www.treasury.gov/resource-center/terrorist-illicit-finance/Documents/guidelines_charities.pdf (accessed March 3, 2011) 14-15.

²⁴ FATF, “FATF IX Special Recommendations.”

²⁵ Ibid.

often within or near areas that are most exposed to terrorist activity.”²⁶ This is particularly true among NPOs focused on humanitarian, development, and human rights objectives. Many of the world’s poorest and neediest areas are also home to terrorist groups, making it difficult to distinguish between legitimate and illegitimate organizations.

25. Fourth, NPOs **“frequently have exposure to a large number of beneficiaries, some of whom may be vulnerable to radicalization...”**²⁷ Some NPOs, for example, run large educational institutions or orphanages in which impressionable children may be vulnerable to radicalization. Similarly, NPOs abused by terrorists (whether complicit or exploited) that work with marginalized populations may solicit support from their beneficiaries for a terrorist group fighting a perceived common enemy.

26. Fifth, NPOs **“may often be subject to little or no governmental oversight, or few formalities may be required for their creation.”**²⁸ This point is arguably the only vulnerability listed here that can be mitigated without undermining the work and reputation of NPOs, and is further explored in Chapter 3.

²⁶ Ibid.

²⁷ CGCC, “Expert working group meeting on preventing abuse of the non-profit sector...” 2.

²⁸ FATF, “FATF IX Special Recommendations.”

CHAPTER 3 - THE MERITS OF EFFECTIVE REGULATION: CFT IS AN INTRINSIC BY-PRODUCT

27. Many jurisdictions around the world, including those belonging to the APG, do not currently have sufficiently effective oversight of their NPO sector. As a result, NPOs in many jurisdictions can be established by just about anyone and can operate with few checks and balances with regard to their finances, activities, and partners. These conditions serve to provide criminals, and in particular, terrorists, with plenty of opportunity to abuse NPOs.

28. A recommended course of action, therefore, is to improve oversight of NPOs through regulation, whether governmental, NPO self-regulation, or otherwise. The principal aim of effective regulation is to enhance transparency and accountability among NPOs, making it more difficult for associated criminals to hide abuse (such as fraud for personal gain) and consequently, to maintain donor confidence. Effective regulation can enhance transparency and accountability, for example, by requiring registration and the submission of annual returns, and consequently instilling a “culture of compliance.”²⁹ Such requirements can provide regulators, government bodies, and the public with crucial information regarding an NPO’s board members and other affiliated individuals, finances, and activities.

29. Thus, in addition to a regulator’s chief purpose, that is, protecting the integrity of NPOs by enhancing transparency and accountability, regulation intrinsically serves a secondary CFT purpose by deterring, detecting, and disrupting terrorist abuse of NPOs as well as traditional criminal abuse. Terrorists and criminals alike are less likely to use an NPO as a conduit if they expect the organization to be scrutinized. Effective regulation thus serves as both an active prevention tool, as well as a reactive compliance tool. This supports recent United Nations discussions on NPOs and TF in which it was agreed that “the primary policy objective in this area should be to strengthen and secure the sector [and] to build its capacity and protect it from abuse...,”³⁰ rather than regulating NPOs strictly to meet CFT purposes.

NPO REGULATION – ONE OF MANY CFT TOOLS

30. There is some debate, however, over the merits of NPO sector regulation as a tool for CFT, and more specifically, whether regulation has in fact ever instigated criminal cases of terrorist financing. A recent World Bank publication states: “Anecdotal information suggests, rather, that it is financial intelligence that is

²⁹ Ibid, 4.

³⁰ Center on Global Counterterrorism Cooperation (CGCC). “Key Observations of the Organizers,” Expert working group meeting on preventing abuse of the non-profit sector for the purposes of terrorist financing (Lancaster House, London, January 18-20, 2011), February 3, 2011 (draft), 1.

essential.”³¹ Although the value of financial intelligence cannot be overstated, there have been many instances in which NPO regulators have worked in conjunction with, or parallel to, law enforcement and intelligence authorities to combat terrorist abuse of NPOs. A regulator might, for example, “tip off” a partner law enforcement agency regarding concerns surrounding a particular NPO. The two bodies may then work in parallel to pursue criminal measures to prosecute offenders as well as civil measures to impede operations or discontinue tax benefits. Canada’s Charities Directorate as well as the Charity Commission for England and Wales operate in tandem with law enforcement agencies in this way, as does the United States, in which criminal investigators from the Internal Revenue Service (IRS) collaborate regularly with the National Joint Terrorism Task Force and other joint terrorism-related task forces.

31. Clearly, regulation is not meant to be a “stand-alone” measure to mitigate terrorist abuse of NPOs. Rather, regulation complements CFT efforts of law enforcement and intelligence agencies, financial intelligence units, other regulators, and private sector watchdogs domestically and internationally – cooperation recommended in the FATF’s International Best Practices guidelines.

THE STATUS IN APG MEMBERS

32. Despite the apparent benefits of NPO regulation and repeated international calls for improved supervision and monitoring of NPOs as a means to combat terrorist resourcing (such as the FATF’s Interpretive Note to SR VIII), only a few APG members worldwide have effective regulatory mechanisms in place, and efforts to create or improve mechanisms in remaining APG members have largely been hampered.

33. A number of evaluations demonstrate widespread regulatory deficiencies across jurisdictions. According to the 2008 Global Survey on the Implementation of Security Council Resolution 1373,³² which calls for the prevention and suppression of TF, as well as the criminalization of wilful provision or collection of funds for such acts,³³ only three jurisdictions were fully compliant with respect to the protection of NPOs from terrorist financing, all of which are listed under the “Western Europe and other States” category.³⁴ Most other jurisdictions were found to be only partially compliant, while a small number of other jurisdictions “were assessed as having no

³¹ van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing.”

³² This survey was conducted by the United Nations Counter-Terrorism Committee Executive Directorate (CTED). The information was collected until October 2007, and was published in June 2008.

³³ United Nations Security Council. “Security Council Unanimously Adopts Wide-ranging Anti-terrorism Resolution: Calls for Suppressing Financing, Improving International Cooperation,” press release, September 28, 2001, <http://www.un.org/News/Press/docs/2001/sc7158.doc.htm> (accessed March 2, 2011).

³⁴ United Nations Security Council. “Global Survey of the Implementation of Security Council Resolution 1373 (2001),” June 10, 2008, <http://www.un.org/en/sc/ctc/docs/GIS2008.pdf> (accessed February 10, 2011).

legal framework or capacity to protect, regulate, and monitor their NPO sectors.”³⁵ An updated survey in 2009 showed little progress beyond improved information collection.³⁶ The status of regulation in APG members mirrors the global picture above. Most APG members do not have the necessary measures in place to effectively regulate NPOs, and are therefore at greater risk of terrorist abuse.

CHALLENGES OF REGULATION

34. Jurisdictions face numerous challenges that explain why the development and implementation of effective NPO regulatory systems to date have largely been inadequate.

35. **First, NPO regulation is often considered “low-priority.”** Many jurisdictions have yet to incorporate the mitigation of NPO abuse into their counter-terrorism strategies.³⁷ Likely, this is partially due to the fact that the majority of terrorist financing cases do not include NPOs. Other, more aggressive counter-terrorism initiatives, such as freezing assets, may also appear as more immediate and visible measures in the eyes of both government officials and the public, and thus may constitute a preferred tactic.

36. **Second, an efficient comprehensive regulatory mechanism also requires substantial financial and human resources.** The FATF has further remarked that “low-capacity countries” are additionally burdened by a severe lack of resources and skilled workforce, overall weakness in legal institutions, dominant informal sectors and cash-based economies, poor documentation and data retention systems, and very small financial sectors.³⁸

37. **Third, regulation can itself be very difficult, particularly with respect to monitoring the activities of humanitarian NPOs operating in foreign conflict zones.** Such monitoring would present challenges in terms of jurisdictional authority as well as reviewing accurate and complete records.

38. **Fourth, many NPOs have resisted government oversight and regulation.** They argue that regulation will incur added costs on organizations that are often already struggling to survive, and that there are substantial concerns surrounding the potential for government authorities to abuse the regulation of NPOs for political purposes.³⁹

³⁵ “Global Survey of States’ Implementation of Resolution 1373: focus on the obligations to protect the non-profit sector” (presentation on behalf of the United Nations Counter-Terrorism Committee Executive Directorate (CTED) at the experts meeting, London, January 18-20, 2011).

³⁶ Ibid.

³⁷ “Global Survey of States’ Implementation of Resolution 1373...”

³⁸ Financial Action Task Force on Money Laundering (FATF). “Guidance on Capacity Building for Mutual Evaluations and Implementation of the FATF Standards within Low Capacity Countries,” February 29, 2008, <http://www.fatf-gafi.org/dataoecd/61/28/40248726.pdf> (accessed March 2, 2011).

³⁹ BOND. “A BOND Approach to Quality in Non-Governmental Organisations: Putting Beneficiaries First,” A Report by Keystone and AccountAbility for the British Overseas NGOs for

39. Fifth, **many jurisdictions have complicated, overlapping, and/or contradictory laws and regulations for historical or cultural reasons.** NPO regulatory systems vary widely across APG members. The vast majority of members do not have a centralized national body responsible for regulating NPOs. Instead, responsibility is often divided between several governmental departments, depending on the nature of the NPO, making a concerted effort to identify NPOs at risk of abuse extremely difficult. For example, an NPO focused on the promotion of sport may fall under the Ministry of Sport and Recreation, while an NPO focused on the promotion of religion may fall under a separate religious ministry. Some governments further require NPO registration, while for others, registration is voluntary, and in others still, regulation is partially carried out by the private sector. As a result, developing and implementing an effective NPO regulatory system may require legal changes affecting numerous government departments and other actors.

40. Sixth, and most importantly, **effective regulation requires an in-depth knowledge of one's NPO sector, its vulnerabilities, and the current laws and regulations affecting it,** which many APG members currently lack. This theme is further explored in the following chapters.

CHAPTER 4 - “STEP 1” – KNOWING THE RISKS

THE NEED FOR A *SECTOR-SPECIFIC RISK-BASED* APPROACH

41. Despite the many challenges involved, many APG members recognize the merits of NPO regulation and are eager to begin improvements. The first step in achieving effective regulation, however, is to determine where the risks are within the sector. Risks to NPOs vary in different jurisdictions, thus a transnational “one-size-fits-all” approach to regulation is unlikely to benefit all APG members equally. Instead, domestic regulatory measures must be nuanced and adapted to the risks inherent to the NPO sector in question. This risk-based approach, strongly encouraged by the FATF, provides for a targeted and proportionate approach in which NPOs that are generally considered low-risk are not heavily monitored, freeing up resources for authorities to focus the majority of regulatory and CFT efforts on those that are considered high-risk.

42. Determining which NPOs are most at risk, however, can be difficult. The following FATF functional definition⁴⁰ of an NPO and subsequent examples⁴¹ are clearly very broad, and were adopted to encompass the diversity of NPOs around the world.

BOX 3. “NPO” AS DEFINED BY THE FATF

“The term *non-profit organisation* or *NPO* refers to 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’.”

The FATF further provides several examples of NPOs in its Best Practices paper, including “associations, foundations, fundraising companies, committees, community service organisations, corporations of public interest, limited companies, [and] Public Benevolent Institutions.”

43. As noted by the World Bank, the Interpretive Note to SR VIII further defines an NPO as a *legal* entity or organization. It also states that supervision and monitoring should be applied to “NPOs which 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.”⁴²

44. It is the responsibility of domestic regulators, however, to narrow the functional definition and directives provided by the FATF in order to identify high-risk and low-risk NPOs unique to their sector during the development and implementation of their CFT measures. Not all NPOs are equally at risk of terrorist

⁴⁰ FATF, “FATF IX Special Recommendations.”

⁴¹ FATF, “Combating the Abuse of Non-profit Organisations: International Best Practices.”

⁴² FATF, “FATF IX Special Recommendations,” 22.

abuse. Legal entities may not necessarily be the most vulnerable in certain jurisdictions, particularly because it is possible that terrorists would avoid these organizations to evade formal requirements such as submitting names of board members. In addition, the wealthiest, most high-profile NPOs may not be most at risk of terrorist abuse in other jurisdictions. As noted by the World Bank, “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, possibly rendering them more vulnerable to abuse.”⁴³ Similarly, heightened supervision and monitoring of NPOs operating internationally may not make sense in developing jurisdictions in which the majority of organizations operate locally.

45. Moreover, identifying vulnerabilities specific to one’s NPO sector is critical to reducing the likelihood that governments will abuse regulations by targeting NPOs for political reasons. Many (if not the majority of) known TF cases involving NPOs have comprised organizations whose objectives have been primarily apolitical, such as promoting religion, humanitarianism, and development. These NPOs frequently receive large amounts of funding, materials, and equipment, which are then transferred to the poorest regions of the world, often where terrorists operate. Few known TF cases involving NPOs comprise other types of organizations, such as political or advocacy organizations.

THE NEED FOR SECTOR-SPECIFIC *INFORMATION AND RISK ASSESSMENTS*

46. Determining where the risks are within the NPO sector requires two sub-steps. **The first is completing a detailed analysis of the sector itself.** How many NPOs are there? What activities do they pursue, and where? How much money do they collect, and how do they spend it? To what extent do they range in size? What is normal, and what is not?

47. Once such questions are answered and baseline data is collected, **the second sub-step is to begin a risk assessment of the sector.** In order to effectively regulate NPOs, one must establish what the sector’s specific vulnerabilities are. What types of NPOs have been abused the most by terrorists and suspected terrorists in the past? Do they work in particular regions? Do they carry out particular activities? What other characteristics do they share?

48. While the technical components of conducting a risk assessment are not discussed in this report, a wide range of factors within the NPO sector should be considered. These include:

- types of NPOs (e.g. humanitarian, religious, etc.)

⁴³ Matrix Insight. “Study to Assess the Extent of Abuse of Non-Profit Organisations for Financial Crime Purposes at EU Level,” study commissioned by the European Commission, Directorate-General Justice, Freedom & Security, April 3, 2008, http://ec.europa.eu/home-affairs/doc_centre/terrorism/docs/study_abuse_non_profit_orgs_for_financial_criminal_purposes_avril09.pdf (accessed March 2, 2011).

- revenue;
- sources of revenue;
- means of distributing funds and materials;
- whether they are primarily donors or recipients;
- partners;
- geographical areas of operations;
- types of activities;
- personnel and other associated individuals (such as directors and volunteers); and,
- beneficiaries.

THE STATUS IN APG MEMBERS AND ITS IMPACT ON TYPOLOGIES

49. To date, many APG members have only rudimentary pictures of their NPO sectors. Following submissions of NPO sector reviews in 2006, an APG report found that only 32% of members had fully completed them.⁴⁴ Although a few members have since concluded reviews, the vast majority of APG members still do not appear to have conducted threat or risk assessments.

50. The lack of information on NPO sectors in the Asia/Pacific region makes a comprehensive discussion of specific typologies, vulnerabilities, risk indicators, and regulatory systems applicable across all NPO sectors in APG members premature. Canada's experience in these matters differs significantly from other members, and NPO vulnerabilities will not be identical in every jurisdiction. As an example, hospitals in Canada do not appear to be subjects of terrorist abuse, while hospitals in other APG members may in fact be at risk. Similarly, few foreign NPOs operate in Canada, unlike other APG members in which foreign NPOs have been implicated in several cases of terrorist abuse.

51. Finally, the need for information regarding one's NPOs sector presents a paradox for some APG members attempting to design more effective regulatory mechanisms, particularly for those lacking baseline data. Much like the "chicken and the egg" scenario, effective regulation requires information about the sector, and collecting the most accurate information about the sector likely requires regulation. However, effective regulation requires years of development. Given that threats to the NPO sector are dynamic, revisions to legislation, policies, and practice must occur constantly even in members with advanced regulatory mechanisms.

⁴⁴ Asia/Pacific Group on Money Laundering (APG). "APG Program for NPO Domestic Sector Reviews Summary Report," July 2007.

CHAPTER 5 - A STRUCTURAL FRAMEWORK FOR ENHANCING REGULATION

52. Once a jurisdiction has obtained detailed knowledge of its NPO sector and has identified vulnerabilities, regulatory mechanisms can begin to be enhanced by implementing a risk-based approach. That is, regulatory mechanisms can be tailored specifically to the risks unique to the sector rather than to risks that are irrelevant.

53. In order to assist APG members in adopting a risk-based regulatory system, this chapter provides a structural framework based on recommendations provided by the FATF that can be applied in any APG member. The starting point of the framework requires domestic reviews of the NPO sector and its vulnerabilities. The remaining steps in the framework rely almost entirely on this starting point, ensuring that the resultant regulatory system is tailored to risks inherent to the sector in question.

54. Given that there is no “one-size-fits-all” or “correct” form of regulation, the framework is meant to be a guide, and has been designed to be sufficiently broad so as to account for differences between jurisdictions. Furthermore, this section does not advocate “starting from scratch.” Rather, most APG members will be able to use the framework presented here to build on or complement existing regulations.

55. Jurisdictions wishing to improve regulatory mechanisms may also want to consult the “NGO Sector and Regulation Review Tool” (RRT) offered by the Charity Commission for England and Wales. The RRT allows authorities to obtain information on the NGO sector, its size, activities and diversity, to map the regulatory mechanisms in place, to identify any gaps or weaknesses in the regulatory coverage, to assess the effectiveness of regulatory systems, and, to identify strategic priorities.⁴⁵ Its greatest strength, however, is that it also requires input from the NPO sector itself. To date, the RRT has been successfully implemented in the Philippines and Indonesia.

THE 9 STRATEGIC GAPS IN NPO SECTOR REGULATION

56. The following 9 strategic gaps in NPO sector regulation represent conceptual weak points that each member must consider in their efforts to enhance regulation. The vast majority of APG members will find that at least some of these gaps are present within their current regulatory system. Once these flaws are identified, jurisdictions can begin to correct them. It should be noted that the following gaps are not mutually exclusive, and often challenges in one area will exacerbate problems in another.

Strategic Gap	Description
Information Gap	A lack of knowledge concerning the characteristics and

⁴⁵ “NGO Sector and Regulation Review Tool,” *United Kingdom Charity Commission, International Programme*, http://www.ngoregnet.org/whats_new/NGO_Sector_and_Regulation_Review_Tool.asp (accessed 2011-02-20).

	vulnerabilities of one's NPO sector (as discussed in Chapter 4).
Effectiveness Gap	A lack of knowledge regarding the effectiveness of current laws and regulations (i.e. their capacity to address actual risks to the NPO sector).
Framework Gap	A lack of consensus as to what strategic framework of regulation would be best suited to your sector (e.g. tax regulation, internal security, law enforcement, self-regulation, etc.). Without a clear consensus, legislation/regulations cannot clearly identify the appropriate lead regulatory authority.
Legal Gap	The absence of appropriate legislation relating to the regulation of NPOs, or the ineffectiveness of present statutory measures in relation to actual risks. As per SR VIII, the legislation must allow for supervision or monitoring of the NPO sector, as well as the ability to effectively gather information and carry out investigations.
Structural Gap	The failure to designate a lead organization with sufficient legal authority and resources to regulate the NPO sector, which is necessary in order to centralize the information. Also, the failure to define the mandates or extent of authority of other stakeholders.
Resource Gap	Although a lead organization is designated, it does not have the necessary funding, personnel, data/records systems, or analytic systems in place to perform essential tasks. These tasks include sectoral analysis, risk identification, and secure data management.
Cooperation Gap	<p>The cooperation gap is divided into two sub-sections:</p> <p>Internal: Where there are insufficient measures in place for cooperation. The body responsible for NPO regulation is unable to maintain liaison and cooperation with other stakeholders, including (but not limited to) financial intelligence units, law enforcement, security services, and immigration authorities.</p> <p>External: Where there are insufficient measures in place for cooperation with other governments, multilateral bodies, or self-regulatory bodies.</p>
Outreach Gap	Efforts to educate NPOs regarding risks posed to the sector by terrorists and the need to conduct due diligence are insufficient.
Participation Gap	The failure to include the NPO sector throughout all stages of enhancing regulation.

TURNING THE 9 STRATEGIC GAPS INTO 9 PHASES OF ACTION

57. By turning the 9 strategic gaps in regulation into phases of action that specifically address these gaps, a standardized strategic framework for regulation begins to form. Within each phase, jurisdictions can tailor the operational and tactical aspects of regulation to the nuances present in their own NPO sectors.

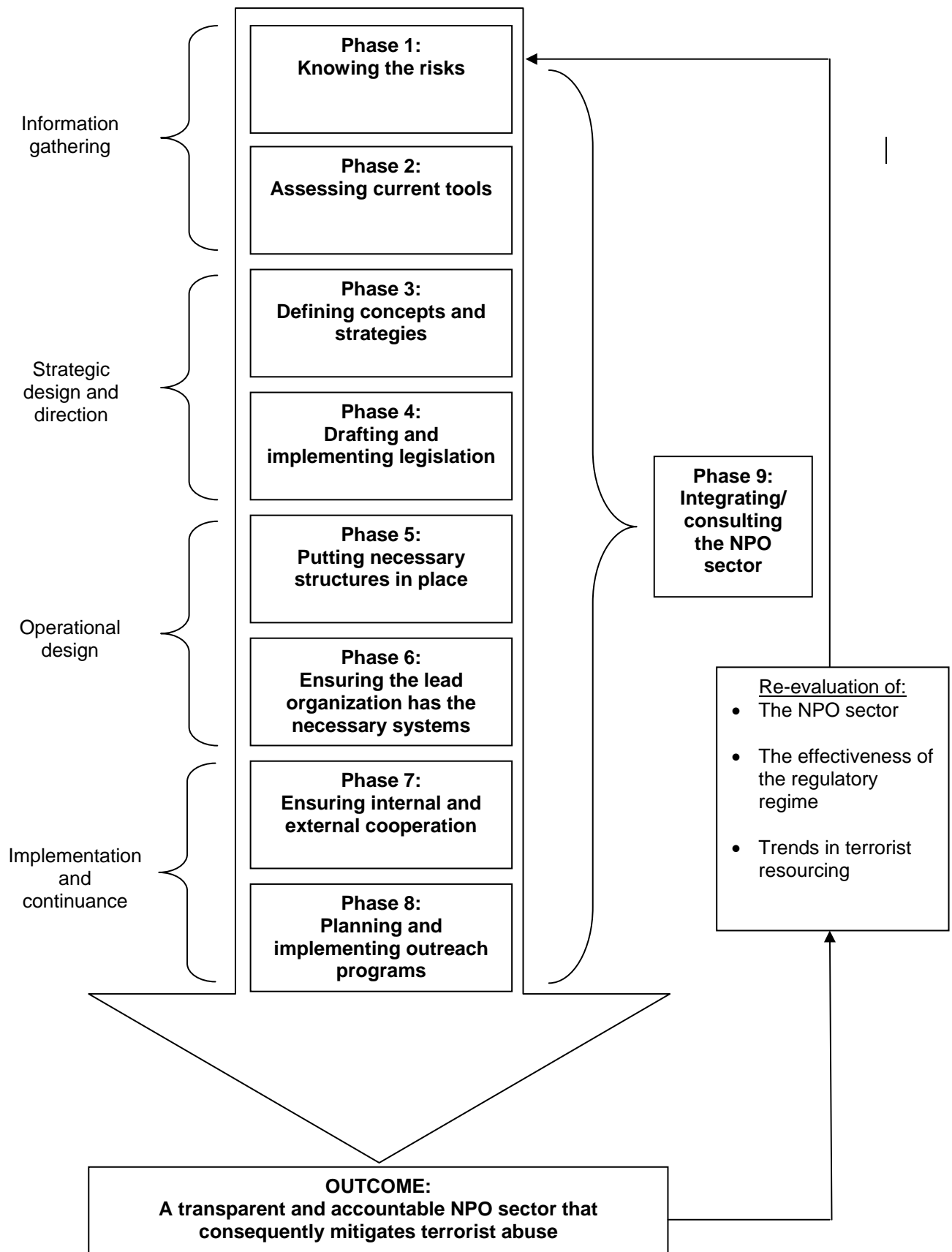
Strategic Gap	Corresponding Phase of Action
Information Gap	Knowing the risks <ul style="list-style-type: none"> • Conduct an NPO sector review and subsequent risk analysis to determine where the vulnerabilities are. The most accurate information may require consulting and coordinating with all stakeholders.
Effectiveness Gap	Assessing current tools <ul style="list-style-type: none"> • Once a risk assessment of the NPO sector is completed, conduct a review of existing laws and regulations to determine inconsistencies with actual risks. This phase is required by SR VIII, and should ensure that classes of NPOs previously overlooked will be incorporated under the new regulatory system.
Framework Gap	Defining concepts and strategies <ul style="list-style-type: none"> • Determine the strategic framework best suited to regulate your sector (tax regulation, internal security, law enforcement, etc.).
Legal Gap	Drafting and implementing legislation <ul style="list-style-type: none"> • Design legislation around the primary method of regulation, ensuring it addresses actual risks and gives adequate authority to the body involved • Being mindful of the directives provided by SR VIII with regard to supervision, monitoring, and investigation, will the method of regulation be passive (a registration and reporting regime), active (intelligence and auditing), or a mixture of both?
Structural Gap	Putting necessary structures in place <ul style="list-style-type: none"> • Designate a lead organization that fits the initial chosen method of regulation. For example, if regulation is to be tackled through tax enforcement, the lead agency should be a taxation body. • Begin to define mandates or the extent of authority of other stakeholders. • Plan for the operational implementation of regulation.
Resource Gap	Ensuring the lead organization has the necessary people and systems <ul style="list-style-type: none"> • If possible, systems for automated analysis, databases, reporting, etc. • Training for staff in analysis, the use of systems, etc. • Implement the operational aspects of regulation.
Cooperation Gap	Ensuring internal and external cooperation <ul style="list-style-type: none"> • Put in place mechanisms to ensure cooperation between the lead organization and other government stakeholders (e.g. information-sharing laws, memoranda of

	<p>understanding, invitations to working groups/inter-agency committees etc.).</p> <ul style="list-style-type: none"> • Ensure bilateral and multilateral engagement with lead organizations in other jurisdictions on information-sharing, strategic planning, risk management, etc.
Outreach Gap	<p>Planning and implementing outreach programs in consultation with the NPO sector</p> <ul style="list-style-type: none"> • Inform the NPO sector about the risks of abuse from terrorists. • Maintain donor confidence in the NPO sector through outreach programs. • Ensure due diligence procedures form part of outreach programs.
Participation Gap	<p>Integrating/consulting the NPO sector</p> <ul style="list-style-type: none"> • Ensure the NPO sector is included in discussions/decision-making during each phase of this framework. Experience has shown that best results are achieved when the NPO sector is continually involved and consulted.

58. The phases of action listed above are not mutually exclusive, and therefore cannot be treated as separate steps in which one step does not begin before the previous step has been completed. Additionally, this strategic framework should not merely be used once. Fine-tuning one's regulatory system will require constant re-evaluation of its effectiveness and a need to return to this framework regularly to ensure gaps are being adequately addressed. That is, the framework is essentially cyclical, as illustrated in Figure 1.

59. It is also imperative that discussions surrounding enhancements to one's regulatory framework include all relevant government departments, enforcement and intelligence agencies, and most importantly, the NPO sector itself. This will ensure the achievement of an effective and balanced regulatory system.

FIGURE 1 - A STRATEGIC FRAMEWORK FOR NPO REGULATION



CHAPTER 6 - CAVEATS FOR REGULATION

60. A number of caveats regarding NPO sector regulation must be kept in mind by all jurisdictions.

61. As previously stated, CFT is a by-product of effective regulation. Regulation should not be pursued simply for CFT purposes. Instead, it should be pursued to foster transparency and accountability among NPOs, and to thereby protect the integrity of the NPO sector. By focusing efforts solely on CFT, jurisdictions run the risk of actually aiding terrorists by shutting down or discouraging legitimate NPO work in areas of risk. Such action may then provide terrorists in these areas with opportunities to fill the void and provide much-needed humanitarian assistance, which will likely increase support for them from the local population.⁴⁶

62. This also touches on the need for proportionality. The design of any regulatory mechanism must be weighed against the potential costs to society. As observed at a recent United Nations meeting in London, these impacts include the “economic, human, reputational, and democratic consequences of regulatory action.”⁴⁷ A disproportionate response to the risk of terrorist abuse may affect the assistance provided by NPOs, and may in fact hurt more people than it helps.

63. Flexibility within a regulatory system is further essential. As an example, it may not be feasible to expect NPOs that respond to sudden humanitarian crises to maintain clear lines of accountability. According to the UN Counter-Terrorism Implementation Task Force (CTITF), “Under some circumstances, including humanitarian crises, unavailability of reliable documentation, lack of existing registration requirements and lack of NPO resources, certain due diligence requirements can be unrealistic. There exist cases in which counter-terrorism financing controls precluded aid from being delivered to those in need.”⁴⁸ In these instances, certain exceptions may be necessary. As a possible alternative to mitigate the risk of terrorist abuse, a World Bank publication has suggested that only goods-in-kind be made available rather than cash.⁴⁹

64. All of these factors inform one of the FATF’s most important general principles, which states that “Measures adopted by countries to protect the NPO sector

⁴⁶ van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing.”

⁴⁷ CGCC, “Key Observations of the Organizers.”

⁴⁸ United Nations Counter-Terrorism Implementation Task Force (CTITF). “Tackling the Financing of Terrorism,” Working Group Report, October 2009, http://www.un.org/terrorism/pdfs/CTITF_financing_ENG_final.pdf (accessed March 3, 2011) 17-18.

⁴⁹ van der Does de Willebois, “Nonprofit Organizations and the Combatting of Terrorism Financing.”

from terrorist abuse should not disrupt or discourage legitimate charitable activities.”⁵⁰

65. Finally, although governmental regulation appears to be the most common manifestation of oversight of the NPO sector, NPO self-regulation can also play a role. Over the past twenty years, self-regulation in the NPO sector has become increasingly popular.^{51, 52} NPOs often sign up to codes of ethics or join umbrella associations in which they are monitored to improve good practice and governance, ensure common principles are met, and to gain the public’s trust. These objectives are shared by governments seeking to improve CFT. Although accountability standards initiated by the NPO sector itself are generally voluntary and have few compliance measures, they can strongly complement governmental regulation and may save significant public resources, and should therefore be encouraged by authorities.

⁵⁰ FATF, “FATF IX Special Recommendations,” 20.

⁵¹ Robert Lloyd, “The Role of NGO Self-Regulation in Increasing Stakeholder Accountability,” *One World Trust* (July 2005): 1-15.
http://www.oneworldtrust.org/csoproject/images/documents/2005_The_Role_of_NGO_Self-Regulation_in_Increasing_Stakeholder_Accountability.pdf (accessed March 7, 2011).

⁵² Global Effectiveness Framework for NGOs – Open Forum for CSO Development Effectiveness, *One World Trust* database of civil society self-regulatory initiatives, http://www.oneworldtrust.org/csoproject/cso/initiatives/345/global_effectiveness_framework_for_ngos_-_open_forum_for_cso_development_effectiveness (accessed March 7, 2011).

CHAPTER 7 - RISK INDICATORS AND CASE STUDIES

66. Although a risk-based approach to regulation encompasses many different tools, identifying indicators of possible risk of terrorist abuse of NPOs is extremely helpful. Risk indicators provide a relatively objective tool for regulatory authorities that help to determine which NPOs are low-risk, and which are high-risk and should thus be closely monitored.

67. While risk indicators of terrorist resourcing involving NPOs should incorporate information from a literature review of relevant studies, reports, and media stories,⁵³ they should also be based on cases and vulnerabilities specific to the NPO sector in question (hence the need for sector reviews and risk assessments). For example, in some jurisdictions, NPOs advertising for donations on television networks owned and operated by terrorist groups may be an indicator of terrorist resourcing. In other jurisdictions, however, terrorist-affiliated television networks may not exist, making such a risk indicator irrelevant. This chapter provides numerous cases studies from around the world and suggests corresponding extrapolated risk indicators that may indicate possible risk of terrorist abuse among other NPOs. In the last section, a risk indicator derived from an extensive literature review and cases of suspected and confirmed terrorist abuse of Canadian NPOs is presented in conjunction with a Canadian case study to demonstrate how risk indicators may be applied.

68. In addition, the presence of one or more indicators does not signify that terrorist abuse of an NPO or its assets is occurring. There could be many innocent and/or non-terrorist-related explanations for the presence of indicators, just as the absence of any/all of the indicators is not evidence that there is no such abuse. Risk indicators therefore need to be used in conjunction with other analytical tools to fully assess the vulnerability of a particular NPO.

GENERAL INDICATORS

69. As previously stated, a comprehensive study of risk indicators applicable to all APG members is premature given the current information gaps in these members. However, a series of case studies from around the world are presented here, and risk indicators that could potentially be derived from these cases are presented directly below them.⁵⁴ These risk indicators may or may not be applicable to each jurisdiction, and are thus presented only as examples to help guide members. It should also be noted that these case studies comprise both proven and strongly suspected instances of terrorism resourcing.

CASE STUDY 1

⁵³ See Methodology, page 9.

⁵⁴ It should be noted, however, that risk indicators should be derived from as many different cases as possible.

A domestic NPO was found to have several directors who openly espoused a radical ideology.

The organization's religious leader had published writings calling for revolution in jurisdictions that do not adhere to the same ideology. The religious leader and other representatives of the organization had also participated in conferences that glorified political violence.

Additionally, the NPO had itself hosted a number of guest speakers who espoused a similar view to the organization's leadership. For example, one guest speaker had attacked those who do not adhere to the same ideology. Another guest speaker called for militant action to address perceived injustices, and argued that militant action was obligatory for those adhering to the same faith.

In all of these cases, the rhetoric used further adhered to the ideology espoused by a foreign government.

Collaboration with other government departments established a connection between one of the NPO's founders, and another organization believed to be a front for covert activity by the foreign government mentioned above. Partner information also indicated that the NPO was being used as a coordinating body for the activities of a terrorist group operating as a proxy for the foreign government in question.

Possible risk indicators include:

Providing a forum for ideologues or others to disseminate extremist rhetoric.

Distributing, publishing extremist materials.

CASE STUDY 2

An NPO operating in an area controlled by a terrorist group ostensibly worked to rehabilitate people affected by war. The NPO had seventeen fundraising offices worldwide and maintained approximately 200 bank accounts at six major banks. Investigations revealed that funds received by the NPO from various international organizations had been routed through a number of different accounts to disguise the exact use of the funds, which were eventually largely withdrawn in cash. Investigations also revealed that withdrawn funds had been deposited with an illegally operating bank run by the terrorist group. The NPO had prepared various progress reports to domestic and international agencies detailing the fund receipts in support of projects which were later found to be fraudulent. Funds received by the NPO from 2003 to 2006 amounted to approximately \$44.5 million USD. In addition, most of the NPO's employees were found to be members of the terrorist group. Machinery and equipment such as vehicles, boats, engines, generators, and tents belonging to the NPO had also been used by the terrorist group to transport explosives.

Possible risk indicators include:

Material/financial support for terror suspects and/or their families, the social infrastructure of terrorist groups, or other support.

CASE STUDY 3

A domestic NPO came to the attention of a regulatory body for a variety of reasons, including operating in areas of concern/conflict. Over the past 15 years, the NPO had operations in jurisdictions that had experienced significant violence relating to terrorism, including Afghanistan, Algeria, Bosnia-Herzegovina, Chechnya, Iraq, Iran, Kashmir, Kosovo, Lebanon, Palestine, Somalia, Sudan, Tunisia, and Yemen. A review of the information that the NPO was obligated to file annually with the regulatory body indicated instances of sudden and large disbursements of funds over a short period of time.

The lack of control of disbursed funds had been a problem in the past with the NPO. In the early 1980s, the organization was unable to produce sufficient financial statements to substantiate how its funds were being used when disbursed to third party organizations. Recently, the NPO had entered into agreements for joint operations with two organizations known to be connected to terrorist groups.

The NPO also experienced similar problems demonstrating control and direction of funds disbursed to its branch offices abroad. An audit of the NPO revealed that there were few safeguards put in place to account for funds disbursed to its international branch offices. In addition, the NPO maintained no copies of books and records for its branch offices at its headquarters. Thus, there was no way for the regulator to confirm how the funds were used once the branch office received them. This was especially problematic in light of the fact that one of the NPO's branch offices, a separate legal entity over which the domestic regulator had no jurisdiction, was found to have redirected funds for the purposes of financing terrorist activity.

Possible risk indicators include:

Lack of direction, control, or transparency in fundraising, expenditure, finances, or resourcing.

CASE STUDY 4⁵⁵

An NPO ostensibly involved in child welfare programs used video tapes depicting religious "freedom fighters" in action in various jurisdictions together with graphic images of atrocities perpetrated against members of that religion. The tapes contained an appeal to send donations to a post office box number to help in the "struggle." These tapes were apparently widely distributed to religious establishments throughout

⁵⁵ Financial Action Task Force (FATF). "Report on Money Laundering Typologies 2003-2004," February 26, 2004, <http://www.fatf-gafi.org/dataoecd/19/11/33624379.PDF> (accessed January 4, 2011), 8-9.

the region. The same post office box number was associated with a further appeal in magazines which published articles by well-known extremists.

Possible risk indicators include:

Sympathy for political movements.

CASE STUDY 5

A domestic NPO was listed as a “Specially Designated Global Terrorist” in two foreign jurisdictions for supporting a Foreign Terrorist Organization (FTO) also designated in the two foreign jurisdictions. The NPO lacked direction and control over funds sent to its overseas partners. Additionally, materials related to the FTO were found in the offices of these overseas partners. Members of the management committees of some of these overseas partners had also been convicted of militant activity. Further, the NPO was a founding member of a larger umbrella NPO designated abroad, and the two NPOs shared a director. Additionally, a member of the committee of the umbrella NPO was designated domestically as a terrorist person, and other member organizations under the umbrella NPO had been also been designated domestically.

Possible risk indicators include:

Association through activities, staff, directors or other relationships to organizations or individuals of interest.

CASE STUDY 6

A national regulatory body received allegations that the directors of a charity had lost control to the charity’s religious leader and his supporters. This loss of control had led to misuse of the charity. Investigating officers found that individuals had been living at the charity’s premises, and that the directors, who had been effectively denied access to the premises and other properties, had been unable to carry out necessary repairs, thus putting the property at risk. The religious leader was also found to be providing sermons of an extreme and political nature. The religious leader was later jailed for soliciting murder and inciting racial hatred, and is alleged to have aided terrorist activities overseas.

Possible risk indicators include:

Internal structure or control problems.

CASE STUDY 7

Law enforcement commenced an investigation into alleged fundraising and procurement activities of individuals of concern. The investigation established that the individuals were sending a number of large international funds transfers to businesses in another jurisdiction believed to be front organizations used to control funds for a terrorist organization in Southeast Asia.

Law enforcement ascertained that the majority of the funds originated from cash raised under the guise of charitable activities. Funds obtained were transferred via direct debit into a central account. Third parties also ‘rolled’ funds from another account into this central account, to be repaid later.

The primary targets used wire transfers to international bank accounts, and bank transfers to accounts held domestically. The individuals frequently conducted these transactions via internet banking, and funded their activities via cash cheques and credit cards which were linked to the central account. Legitimate businesses, such as grocers, restaurants, and hospitality venues were also used to raise funds. The funds would be disbursed by various techniques, including person-to-person, bank account deposits, asset purchases (e.g. real estate), and funds transfers from a central bank account into individuals’ accounts for alleged “expenses” relating to the administration of the charitable organization.

Domestic FIU information identified numerous structured wire transfers of values just under the reporting threshold. A central account was not used for the wire transfers. Instead, the wire transfers were organized through several different banks.

The majority of the transactions were in the suspects’ own names, but third parties were used to create the central bank account. Third parties were also used to send wire transfers and conduct purchases using funds withdrawn from the central account. Several arrests were made. Those arrested were charged with being members of a terrorist organization, providing support or resources to a terrorist organization, and making funds available to a terrorist organization.

Possible risk indicators include:

Connection to a business or charitable front.

Lack of direction, control, or transparency in fundraising, expenditure, finances, or resourcing.

RISK INDICATOR APPLIED: A CANADIAN EXAMPLE

70. The following section demonstrates the application of a risk indicator of terrorist resourcing involving NPOs derived from Canadian cases and experience, as well as a literature review of relevant studies, reports, and media stories.⁵⁶ First, the indicator itself is presented and describes how a history of criminal activity may

⁵⁶ See Methodology, page 9.

indicate possible risk of terrorist abuse. Second, a list of factors that influence the level of risk is provided. This is followed by a corresponding Canadian case study in which the risk indicator was observed and flagged. Lastly, an analysis of the indicator's presence in the case study is provided to demonstrate how a risk level is determined and assigned.

71. It should be noted that this indicator will not necessarily apply to all APG member jurisdictions, and is presented here purely as an example within the Canadian context.

RISK INDICATOR: THE NPO, ITS DIRECTORS, STAFF, ETC. ARE CURRENTLY SUSPECTED OF HAVING OR HAVE A HISTORY OF CRIMINAL ACTIVITY

Description:

Our research demonstrates that NPOs/individuals associated to NPOs known to have been implicated in terrorist resourcing have used their charitable cover as a means to conduct criminal activity (such as weapons smuggling) for the benefit of a terrorist group. As a result, current or previous criminal activity within an NPO or by individuals associated with an NPO represents some level of risk of additional criminal activity possibly tied to terrorism.

Factors to consider:

The following factors should be considered in determining the level of risk (high, medium, low) that can be attributed to criminal activity:

- **Nature of the (alleged) crime.** How serious is the crime? Is it related (or have the potential of being related) to terrorist resourcing or activity?
- **Status of the crime/investigation.** Is the investigation ongoing? Have arrests been made? Have there been any convictions?
- **Relationship of the individual(s) to the NPO.** Who has been implicated in the criminal activity and what is their position within NPO? To what extent do the individual(s) exert influence within the governance structure of the NPO? Is there opportunity for them to covertly divert resources?
- **Knowledge of the (alleged) criminal activity.** Did other individuals associated with the NPO have knowledge of the criminal activity? Is it reasonable to expect that other individuals associated with the NPO would have an awareness of the criminal activity? How extensively are other individuals associated to the NPO implicated?
- **Reliability and credibility of the source.** How reputable is the source of information? Have they been accurate in the past? Do they have any potential motivations/biases that might affect the reliability and/or credibility of the

information? Can this source's information be corroborated in whole or in part by other sources?

- **When did the (alleged) crime take place?** How recently was the crime committed? Is it ongoing? Did it take place while the individual was associated to the NPO? If so, did it involve the use of the NPO's resources?

Case study:

A domestic NPO with operations abroad was involved with small disaster relief projects, among other activities. Most of these disaster relief activities were not, however, reported in the information that the organization was obligated to provide annually to the national regulatory body. Rather, they were discreetly included in the organization's *Zakat* disbursement and were revealed only through an audit of the organization's finances by the national regulatory body.

Examples of these *Zakat* disbursements included several thousand dollars to three organizations for earthquake relief, relief of poverty, and religious education. An audit done on the NPO found that it exercised no control or accountability over the use of these funds once they were transferred. Some of the recipient organizations had been implicated in supporting terrorism and terrorist activities.

The NPO was also under suspicion for using its *Zakat* and one other account for money laundering. The second account was used for collecting interest-free loans that the NPO received from its members. During an audit performed by the national regulatory body, irregularities were noted with the loans which suggested that the NPO was misusing the two accounts. A review of the information that the NPO was obligated to file annually revealed that for several years the amount of loans received by the organization was very close to the amount of loan repayments disbursed by the organization for the same fiscal period.

In addition to these issues, open source information from a think tank showed that a convicted money launderer was first the Vice-President, and then the President, of the NPO during this period. Additionally, the NPO's accountant and past President were implicated in the same money laundering scheme.

Analysis of level of risk attributable to this particular indicator:

Based on the information provided in the above case study, the level of risk that can be attributed to criminal activity is rated HIGH for the following reasons:

- **Nature of the (alleged) crime.** Money laundering is a serious crime and has been used by terrorists to fund activities in the past.
- **Status of the crime/investigation.** Although only one individual appears to have been convicted, two other individuals associated with the NPO were also implicated. It is unknown whether there is another ongoing investigation.

- **Relationship of the individual(s) to the NPO.** The individuals involved in the money laundering scheme hold executive positions within the NPO. Consequently, they exert influence within the governance structure and there is opportunity for them to covertly divert resources.
- **Knowledge of the (alleged) criminal activity.** It is unknown whether other individuals associated to the NPO are aware of the criminal histories of their counterparts.
- **Reliability and credibility of the source.** The information pertaining to the criminal histories of these individuals originated from a reputable Canadian think tank known to be both reliable and credible. Additionally, information has been corroborated by police.
- **When did the (alleged) crime take place?** The date of the crime is unknown.

Given the totality of factors described above, the criminal activity associated to this NPO indicates that the risk of terrorist abuse is HIGH.⁵⁷

⁵⁷ It is important to note here that risk indicators cannot be evaluated in isolation. Each risk indicator must be weighed against the presence and strength of other risk indicators in order to provide an overall risk assessment of the NPO.

Chapter 8 - Policy Implications

72. Designing and implementing a risk-based regulatory system for NPOs has numerous policy implications for APG members.

73. First and foremost, **enhancing one's NPO regulation must become a priority for APG members wishing to adhere to SR VIII and mitigate domestic terrorist activities.** This requires ensuring the necessary funds, personnel, systems, and cooperation will be put in place and maintained.

74. Second, **a detailed review of one's NPO sector and a subsequent detailed risk assessment of vulnerabilities are crucial.** Enhancing regulation cannot be properly achieved without tailoring mechanisms to actual risks.

75. Third, **it is imperative that APG members include and consult with their respective NPO sectors during all stages of regulation and CFT planning.** Experience has shown that involvement of NPOs produces more effective regulatory systems. This approach is also likely to mitigate the risk of abuse of regulations for political purposes. Governments and the NPO sector must “meet halfway” and actively cooperate to ensure regulatory measures will be fair, effective, and allow freedom of association.

76. Fourth, **effective regulation requires striking a balance between seemingly opposing aims:** transparency and privacy, accountability and flexibility, enforcement and self-regulation.⁵⁸ This task is very difficult, and will likely require years before a balance is reached.

77. Fifth, given the complexity of enhancing regulation and the transnational nature of terrorist resourcing, **the continued sharing of best practices between governments, regulators, international organizations, NPOs, and other stakeholders is strongly recommended.**

⁵⁸ CGCC, “Expert working group meeting on preventing abuse of the non-profit sector...;” “NPO’s and terrorist financing vulnerabilities” (presentation on behalf of the United Nations Counter-Terrorism Committee Executive Directorate (UN CTED), APG Typologies Workshop, Dhaka, October 25-28, 2010).

CONCLUSION

78. Despite efforts over recent years to protect NPOs from the risk of terrorist abuse, the threat continues to evolve and it is likely that numerous cases have not yet been detected.

79. As a result, it is strongly recommended that the best way for APG members to reduce the likelihood of terrorist abuse is to enhance regulation of the NPO sector using a risk-based approach. Not all NPOs face equal risk of terrorist abuse, thus a targeted approach is necessary to ensure resources are not wasted on low-risk NPOs, and more importantly, to ensure that legitimate NPOs are not obstructed from playing a positive role in society. Effective regulatory measures also allow APG members to meet twin objectives: improving transparency and accountability among NPOs, and as a by-product, deterring, detecting, and disrupting affiliated terrorist activity.

80. Given the many benefits that NPOs provide to society at large and the trust conferred upon them by the public, governments and NPOs alike have a responsibility to prioritize protection of the sector while simultaneously allowing it to operate freely and shape its own future, as recommended by the FATF.

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