



HM TREASURY



Home Office

Review of Safeguards to Protect the Charitable Sector (England and Wales) from Terrorist Abuse

A Consultation Document

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Preface

In February 2006, the Government initiated a review of the safeguards in place to protect charities from the threat of being abused by terrorists.

This consultation document marks the end of the first phase of that process, and has been issued to allow all relevant stakeholders to comment on the findings and recommendations of the review.

It sets out the key questions to be addressed when deciding how best to enhance and develop existing safeguards in order to ensure the continuing protection of the sector from terrorist exploitation in line with the increased threat of abuse.

The Government welcomes views on this paper's assessment of the current regime and the proposals for change by 2 August 2007. Please see the section entitled 'How to respond' in Chapter 4 for instructions on how to respond to this consultation document.

Executive summary

England and Wales are fortunate to benefit from a long and rich history of charitable activity. The charity sector is incredibly diverse and makes an important contribution to the social and economic vibrancy of the country.

An important part of the sector's success is the world-class regulatory framework that exists for charities in this country, a framework that demands a high degree of integrity and transparency from the sector thereby protecting charitable funds from being stolen or misused. However, just as with other business models, the activities and processes of a charity can be used to provide a veil of legitimacy to the financing of terrorist networks. As controls on this kind of abuse tighten in other areas such as the financial services sector, it is important to ensure that there is no displacement of such financing to the charity sector.

The risk of charitable activity being seen as a soft option for terrorist finance (particularly in countries with little or no existing regulatory framework) has been recognised by the Financial Action Task Force (FATF).¹ The FATF response to this challenge, Special Recommendation VIII, requires that all countries should review the adequacy of laws and regulations that relate to charitable entities which can be abused for the financing of terrorism. It takes as its starting point the concept that charities are particularly vulnerable, and proposes that countries should ensure that they cannot be misused:

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

The FATF standard recognises the potential of charities to be exploited as a means of raising and moving terrorist-linked funds. It also reflects the role that some organisations can play in sustaining a terrorist infrastructure, often in highly distressed parts of the world, by providing cover for such activities and acting as a vehicle for recruitment and propaganda. But above all, it reflects the need to encourage a flexible and vibrant charity sector that is sufficiently protected from terrorist abuse to prevent exploitation and protect donor confidence.

In February 2006, the Treasury and the Home Office initiated an assessment of existing safeguards for the charitable sector in order to identify the key requirements of an effective, proportionate response to the evolving terrorist threat.

The Government's assessment is that while the current scale of terrorist links to charitable activity is extremely small in comparison to the size of the charitable sector, the scope for exploitation of charities by terrorists could become a significant aspect of the terrorist finance threat without appropriate and co-ordinated action now by the sector, regulator and government. The review acknowledges that there are examples of good practice that the charitable sector already has in place, or is developing to guard against links with terrorism. Similarly, the review recognises that the Charity Commission has considerable experience of using its protective powers, and an existing policy regarding allegations of terrorist exploitation of charities, which it can build upon. In order to ensure that the Charity Commission has the tools it needs to respond to the threat, extra resources will be made available to increase its capacity in this area.

1 The Financial Action Task Force is an inter-governmental body set up in 1989 for the development and promotion of national and international policies to combat money laundering and terrorist financing. See www.fatf-gafi.org

Key recommendations

The recommendations of the review that are set out below are for the charity sector together with the Charity Commission, other relevant government departments and law enforcement agencies in order to enhance current work to reduce the risk of terrorist exploitation of the sector. The recommendations are designed in particular to:

- stimulate further efforts by the sector to raise awareness of the threat and encourage further dissemination of best practice to mitigate the risk of abuse;
- support the work of the sector in building stronger communities, promoting democracy and overseas development;
- reinforce Charity Commission work to protect the sector from all kinds of abuse, including that by terrorists; and
- strengthen the working relationships and co-ordination between relevant government departments and law enforcement agencies and the Charity Commission to combat the risk of terrorist exploitation of charities.

The Government seeks to consult the sector and the public on the proposals of this review in order to establish the strongest possible policy framework going forward.

Commitment and responsibility

All those involved in the charitable sector should commit themselves to ensuring that charities do not provide a transmission belt for funds to terrorist networks. Both the Charity Commission and the sector have an important role to play in delivering effective preventative safeguards. This responsibility should include preventing the transmission of funds ostensibly for humanitarian relief that directly or indirectly support terrorist activity.

Strategy and objectives

The Charity Commission should publish its strategic and operational objective to identify and minimise the risk of terrorist exploitation of charities. It should have a business strategy that directs activities and resources to deliver this objective. It should have benchmark indicators of success, on which it reports regularly.

In partnership with other relevant bodies, this strategy should include provisions to encourage the following outcomes:

(i) Risk-based diligence and assurance

Charities should assess their exposure to the risk of terrorist exploitation and, in response, take proportionate steps accordingly to ensure that funds are not passed, directly or indirectly, to partner organisations with terrorist connections.

A 'know your beneficiary' principle should extend to identifying and forestalling any funding connections either to designated terrorist organisations (such as those on the Bank of England's asset freeze list) or to recipients whose activities may give support to terrorism.

This risk-based approach should be supported by the Government and the Charity Commission through:

- practical guidance on evaluating risk and forestalling abuse;
- ongoing and informed feedback to the sector on charity-linked terrorist finance threats worldwide; and
- risk-based assurance work (including, where appropriate, on-site visits) to verify the proper end use of funds.

(ii) Proactive investigation and disruption

The Charity Commission should develop its investigative capacity and the appropriate co-ordination with counter-terrorist agencies to help ensure that possible instances of terrorist finance in the sector are identified and investigated proactively, in line with the Commission's independent risk-assessment procedures.

Both the Commission and the counter-terrorist agencies are operationally independent. Effective working relationships between them are therefore essential. Protocols to encourage this co-ordination, and their success, should be kept under review.

The Charity Commission and other relevant bodies should deploy the independent powers available to them proactively, as an integral part of efforts in the UK to choke off funds to terrorists. The Commission and other relevant bodies should co-ordinate activity to ensure maximum disruptive effect against terrorist finance threats.

Introduction

“Wise governments respect the crucial independence of the sector. But government has an important role to play in providing support.”

Prime Minister Tony Blair, on publication of the Strategy Unit's 2002 review of the charity sector, Private Action, Public Benefit.

1. England and Wales² are fortunate to be home to one of the most energetic and diverse charitable sectors in the world. This sector is a vital part of the social and economic vibrancy of the country. In the context of combating terrorism, the sector's work to promote community cohesion and inter-faith harmony is also particularly important.
2. The Government has repeatedly demonstrated its commitment to a healthy and robust charitable sector. Since 2001, charities have been able to avail themselves of Gift Aid tax relief on donations from UK taxpayers. The comprehensive review of the sector by the Prime Minister's Strategy Unit in 2002 culminated in the passage of the Charities Act 2006, which overhauled and strengthened the legislative framework for charitable activity in England and Wales. The Treasury and the Office of the Third Sector will report later in 2007 on their joint review of the future role of the third sector in social and economic regeneration. This review is designed to underpin the relationship between charitable activity and the CSR settlement 2008–11.³ As part of this exercise, the Chancellor has already announced that government departments that fund charitable work should contribute to sector sustainability through the establishment of three-year minimums on funding agreements as standard.
3. Public and donor confidence in the charitable sector is high, not least because of the existing standards for governance and probity that are set out in law and enforced by the statutory regulator, the Charity Commission. This regulatory regime demands a high degree of openness from the charitable sector, and is far in advance of the requirements imposed on charities in most of the rest of the world – indeed, the Charity Commission helps to develop stronger regulatory systems in overseas jurisdictions through its own International Programme. Although it is clear that the great majority of charities in this country comply with the existing regulatory requirements, it is right that the Government should take steps to ensure that the sector continues to be adequately protected in the face of relevant emerging threats.
4. The Charity Commission has broad experience of identifying and investigating financial abuse in the charity sector and of taking protective and remedial action to deal with such abuse, including in relation to cases of terrorist exploitation.
5. In February 2006, the Chancellor announced that the Government would review how best to strengthen the safeguards to protect the charitable sector from terrorist abuse and protect donor confidence in so doing. This decision was taken in the context of two relevant issues:
 - international obligations, including the development by the Financial Action Task Force of an international best practice standard on the prevention of terrorist abuse of charities; and
 - law enforcement operational experience of an increased threat in this area.

2 The review applies to England and Wales. Regulation of the charitable sector is a devolved issue in Scotland and Northern Ireland but the Home Office and the devolved administrations recognise the need for a joined-up approach on this issue so the review will be copied to the Scottish Executive and the Northern Ireland Office.

3 See www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr06/other_docs/prebud_pbr06_odthirdsector.cfm

6. Recognising that England and Wales are home to one of the most diverse and effective charity sectors in the world, and recognising also that the Charity Commission already applies a sophisticated model of regulation that is admired and emulated by other countries around the world, the goal for this review was to look at the regulatory environment for charities through the lens of terrorist finance risk in order to seek out strengths, gaps and vulnerabilities, and to report accordingly. The issues raised in this review are clearly of interest and relevance to all parts of the United Kingdom although the focus of the review was limited to England and Wales in line with the remit of the Charity Commission.

The UK context

7. The regulation of charities in Scotland and Northern Ireland is a devolved matter. This review focused on the safeguards in place in England and Wales, although the key findings and recommendations clearly have relevance to the charity sector across the UK, and to the different jurisdictions. There are more than 21,000 charities in Scotland, and approximately 9000 in Northern Ireland, both with significant annual income. It is important therefore that safeguards to protect the sector from terrorist abuse are equally robust across the UK. The Home Office will share the findings from this consultation exercise with the Scottish Executive and the Northern Ireland Office.

Charity regulation in Scotland

8. Charities in Scotland are regulated by the Office of the Scottish Charity Regulator (OSCR). The Charities and Trustee Investment (Scotland) Act 2005 provides a modern, proportionate regulatory framework designed to support and encourage charitable activity in Scotland. The Act introduces a Scottish definition of charity, and includes a 'charity test' which all bodies

must pass to be entered on the Scottish Charity Register. The Act also establishes OSCR as an independent regulator, provides OSCR with a range of supervisory powers, regulates fundraising and sets up an appeals system for charities to appeal OSCR decisions.

Charity regulation in Northern Ireland

9. Charity policy and legislation in Northern Ireland is administered by the Department for Social Development though currently there is no register of charities nor a regulator in the manner of Scotland or England and Wales. New draft legislation has recently been laid at Westminster; this, however, may refer back to the Northern Ireland Assembly if devolution is restored. Once passed, this will create a Charity Commission for Northern Ireland with similar powers and responsibilities to its counterparts in Scotland and England and Wales. Registration of charities in Northern Ireland with the new regulator will be introduced in stages over the next three years.

Review team and related issues

10. Responsibility for leading the review was taken by the Home Office, drawing on both Home Office and Treasury resources for the project team. A full list of organisations interviewed is included at Annex A.
11. In parallel with this review process, sector umbrella groups have conducted their own analysis of the interplay between measures to counteract terrorism and the role of the charity sector. This has resulted in the publication of a report by the National Council for Voluntary Organisations entitled *Security and Civil Society: the impact of counter-terrorism measures on civil society organisations*.⁴ Key messages from that exercise will be considered alongside the responses to this consultation document.

4 Available at www.ncvo-vol.org.uk/policy/index.asp?id=3906

Chapter 1: Combating terrorist finance

“...all states shall...prevent and suppress the financing of terrorist acts.”

United Nations Security Council Resolution 1373 (2001).

The need to combat terrorist financing

- 1.1 The current terrorist threat⁵ facing the country is genuinely international in nature. Terrorists with similar ideologies have carried out or attempted attacks in numerous countries, including the UK. Sometimes the attacks are carried out by individuals from the country concerned, and sometimes by non-residents. The domestic and international dimensions of the threat are therefore closely linked, and this is facilitated by the ease with which information and money flows across the globe.
- 1.2 The Government’s current threat level is assessed as severe (as of April 2007).⁶ This means that an attack is highly likely and indicates a continuing high level of threat to the UK. International terrorism is one of the most serious national security threats that we face today. As the London terrorist attacks in July 2005 showed, an attack or multiple attacks may be mounted without warning.
- 1.3 The intelligence picture on the methods employed by terrorists to raise, move, store and deploy funds is constantly evolving. Although it is widely accepted that the costs of staging attacks have in many cases been minimal, terrorist networks need significant funding to support the rest of their activities, such as recruitment and training. Experience has demonstrated that action to identify, track and interdict such funds is a vital part of broader efforts to combat terrorism.

- 1.4 The nature of the threat is such that the Government’s approach to countering terrorist finance must be sufficient to tackle both:

- the funding for direct attacks against the UK; and
- the abuse of the UK’s financial services sector for the transmission of funds – raised here or elsewhere – to facilitate terrorism overseas.

Summary of current controls

- 1.5 The UK has in place a robust framework of terrorist finance controls, closely aligned with its anti-money laundering architecture. These controls are derived from obligations under UNSCR 1373 and the international best practice standards agreed by the Financial Action Task Force.⁷
- 1.6 The main legislative provisions are found within the Terrorism Act 2000 as amended by the Anti-Terrorism Crime and Security Act 2001. Sections 15–18 of that Act make it an offence to:
 - raise funds for the purposes of terrorism;
 - hold or use funds for the purposes of terrorism;
 - become involved in an arrangement to make funds available for the purposes of terrorism; or
 - facilitate the laundering of terrorist money.
- 1.7 Section 19 of the Act imposes an obligation to disclose information to the authorities where a person:
 - ‘(a) believes or suspects that another person has committed an offence under any of sections 15 to 18; and

5 As described in the UK Government’s strategy on countering international terrorism.

See www.intelligence.gov.uk/publications/documents/countering.pdf

6 MI5, *Threat to the UK from International Terrorism*, www.mi5.gov.uk/output/Page269.html

7 www.fatf-gafi.org

- (b) bases his belief or suspicion on information which comes to his attention in the course of a trade, profession, business or employment.’

Failure to comply with this duty constitutes an offence. Section 21 sets out the circumstances in which a person can explicitly seek the consent of a constable to proceed with a transaction or arrangement that might otherwise be an offence under Sections 15–18.

1.8 This broad obligation is further refined for several business sectors by the Money Laundering Regulations 2003, which require such businesses to implement internal systems and controls to prevent money laundering. As part of these controls, the regulations explicitly require that relevant employees are made aware of their responsibilities under the Terrorism Act 2000.

1.9 Business sectors covered by the Money Laundering Regulations 2003 are:

- credit institutions;
- financial institutions (including for example banks, bureaux de change and money transmission agents);
- auditors, external accountants and tax advisers;
- estate agents;
- legal professionals;
- dealers in high-value goods whenever payment is made in cash, in an amount of €15,000 or more;
- trust or company service providers; and
- casinos.

1.10 As part of their compliance and enforcement programmes, the statutory regulators and supervisors for the sectors listed above also specifically check that businesses operating in these sectors have the required systems in place and that these systems are working effectively to counter the terrorist finance threat. In accordance with Hampton principles,⁸ such checks by regulators are risk-based and proportionate, ensuring that the compliance burden is minimised for those businesses considered least at risk of abuse.

1.11 This framework appears to work well. Over the course of 2005, these business sectors submitted a total of 2,091 reports to the authorities on suspected terrorist financing. Over the same period, data collected by businesses subject to the Money Laundering Regulations 2003 has been repeatedly found to be an important source of information for police investigations into terrorism.

8 Hampton review into regulatory inspection and enforcement, see www.hm-treasury.gov.uk/independent_reviews/hamptonreview/hampton_index.cfm

The charity sector in England and Wales

2.1 Charities are the most well-known, high-profile form of not-for-profit or ‘third sector’ entity active in England and Wales.⁹ With a few exceptions, all charities with an annual income of over £1,000¹⁰ must by law register with the Charity Commission, which acts as registrar as well as regulator. ‘Charity’ is a legal status defined through a combination of statute and case law going back over 400 years. The recently passed Charities Act 2006 reinforces and updates the definition of a charity. Charitable status confers a number of benefits on organisations in addition to the kudos that it attracts, such as a number of tax exemptions that are available only to charities. In return for these benefits, and to protect high levels of public confidence, charities are subject to a specific regulatory regime, which is examined in more detail later in this chapter.

2.2 Registered charities make up the largest single component of the third sector, numbering almost 200,000 organisations, with a combined annual income of around £40 billion and assets of a further £90 billion.¹¹ The majority of sector income is accounted for by a small number of very large charities. The net growth in registered charities stands at about 1,800 per annum. Charities benefit from time contributed by volunteers which is equivalent to the work of 1.1 million full-time paid staff (this includes those persons responsible for managing and directing the charity),¹² and across the UK charities have paid staff accounting for approximately 2 per cent of the workforce.¹³

2.3 The full importance of public recognition of and confidence in charitable status is hard to quantify, although public donations remain an important source of sector income.¹⁴ Certainly the fact that charities must register with the Charity Commission seems to communicate a sense of probity, integrity and legitimacy to the public.¹⁵ The Charity Commission’s view is that registration is certainly seen as desirable by bona fide organisations for this reason. Registration is not dependent on self-selection: if an organisation meets the legal definition of charitable status and has an annual income above £1,000 it has a legal obligation to register. Most organisations in England and Wales that raise and distribute funds for social or humanitarian purposes have charitable status.

2.4 It is accepted that the charitable sector makes an important contribution to national life,¹⁶ by:

- providing vital services;
- strengthening communities;
- identifying new needs;
- representing important interests that otherwise risk being marginalised;
- contributing to public goods like the environment; and
- innovating ways of tackling social problems.

2.5 The values and independence of charities allow them to develop and deploy bespoke solutions to particular problems with unparalleled rapidity, placing the needs of their beneficiaries first. An important element in this is the vital

9 The ‘charitable and wider not-for-profit sector’ was defined in *Private Action, Public Benefit* (Prime Minister’s Strategy Unit, 2002) as including: charities, self-help groups, community groups, social enterprises and community-based mutual organisations with social objectives.

10 This will increase to £5,000 when the relevant provisions of the Charities Act 2006 come into force.

11 Charity Commission, 2005–06 statistics.

12 NCVO (2006) *Voluntary Sector Almanac*, www.ncvo-vol.org.uk/uploadedFiles/NCVO/Research/AlmanacSummary2006.pdf

13 *Ibid.*

14 *Ibid.*

15 Prime Minister’s Strategy Unit (2002) *Private Action, Public Benefit*.

16 *Ibid.*

role of volunteers at all levels of charitable activity, including on the governing bodies of charities – opening up considerable scope for those with most knowledge or experience of a problem to drive the solution.

- 2.6 A good example of this is in the field of international disaster relief, where charities have repeatedly demonstrated their ability to transform public concern about a given disaster into on-the-ground aid solutions within hours of the news breaking. Although this is a particularly high-profile element of charity work, the philosophy displayed is a recurrent theme throughout the sector, even down to the smallest community-focused groups.
- 2.7 It is important to recognise the significant contribution that third sector organisations make in addressing some of the underlying causes of disaffection often quoted as a reason why people turn to extremism or even terrorist activities. By promoting social inclusion and building stronger communities, organisations active in minority or marginalised communities in particular can offer a constructive, legitimate channel for disaffection. Charities operating overseas can also present a positive impression of British civil society and values, helping to build goodwill and furthering international relations.

Charity model and inherent risk

- 2.8 Just as with any other mechanism for collecting, moving and distributing funds (for example, businesses subject to the Money Laundering Regulations 2003), the basic model of a charity is exposed to the risk of terrorist exploitation through either the creation of an entirely bogus entity or the abuse of a legitimate organisation. The existing safeguards to prevent this are examined in more detail later in this chapter. The risk of such exploitation taking place is rendered more significant by the high levels of public trust that exist in relation to the sector, which could make exploitation more difficult to spot when safeguards have failed and which

could be seriously eroded by any sense that the sector is rife with abuse.

- 2.9 Expanding the model further to take in the enormous diversity in size, income and activity present within the sector, it becomes clear that the inherent risk does not apply equally across the sector. Again, putting to one side the safeguards that already exist and concentrating only on the activities of the sector, there is a graduation of risk which increases not only with size but also, separately, with objective and function. For example, a charity that transfers funds across the globe to provide aid in areas of conflict may be at equal risk of abuse, for different reasons, as a domestic charity that has limited assets but close links with groups that promote an extremist ideology.
- 2.10 Based on law enforcement agencies' experience and intelligence regarding the extremely rare cases where the sector has been abused by terrorists, either here or overseas, the risk (either of a charity being set up as a sham or of a legitimate entity being exploited) is greater for those groups which:
- are closely aligned to particular religious or cultural movements;
 - frequently move funds or other resources to areas of conflict or unrest around the world;
 - pass funds to other organisations based overseas rather than deliver services directly;
 - deal exclusively in cash or alternative remittance systems where no formal banking infrastructure exists; or
 - have extremely complicated financial records in which suspicious transactions are less easy to identify.

It must be stressed that what is being described here is a risk model. There is no suggestion that a charity displaying one or more of these characteristics should be considered to be funding terrorism – indeed the vast majority of such entities are doing valuable work – merely that the exposure to risk of abuse is

relatively greater for such an entity when compared to a charity that displays none of these characteristics. The list is not exhaustive: there may be other risk factors weighing on individual charities that the sector and the regulator are better placed to identify.

- 2.11 Central to this review is the principle that charities should assess their level of exposure to the risk of terrorist exploitation and, where risks are identified, put in place proportionate measures to reduce their exposure to these risks.¹⁷ There is also an acceptance that for many parts of the sector, the exposure to risk will be very low, and therefore a ‘one size fits all’ approach would not only represent an inappropriate and disproportionate response, but could also be counter-productive and damaging to the sector.
- 2.12 The model described above has implications for the way the sector analyses risk. Just as all charities are potentially at risk of fraud or theft, so there is a latent risk of abuse for the purpose of terrorist financing, making it important that no part of the sector is complacent. That said, the risk model above suggests that, for the majority of the sector, an analysis of terrorist finance risk is likely to be a very simple exercise. The model is not the whole story however, as many safeguards already exist within the sector.

Existing safeguards: counter-terrorist legislation

Terrorism Act 2000

- 2.13 The key piece of primary legislation on terrorism which affects the work of charities – and indeed all relevant sectors – is the Terrorism Act 2000.

- 2.14 Section 1 of the Act provides a definition of terrorism. Section 1(5) makes it clear that in the Act references to action taken for the purposes of terrorism include action taken for the benefit of a proscribed organisation. Under Part II of the Act, an organisation is proscribed in the UK if it is (a) listed in Schedule 2 of the Act, or (b) operates under the same name as an organisation listed in that Schedule. Organisations can be added and removed from Schedule 2 by order. In certain circumstances, the Secretary of State may also make an order that a name of an organisation that is not listed in Schedule 2 is to be treated as another name for an organisation that is listed in Schedule 2. Offences that flow specifically from an organisation being proscribed include membership (Section 11), support (Section 12) and uniform (Section 13). The list of proscribed organisations currently runs to 58 entities. The list is of particular relevance to internationally active charities, as some of the proscribed organisations – for example the Liberation Tigers of Tamil Eelam (LTTE) – have an ostensibly social or humanitarian function in their home states with which charities may come into contact.
- 2.15 Part III of the Act covers terrorist property. Offences include fundraising (Section 15), use and possession (Section 16), funding arrangements (Section 17) and money laundering (Section 18). A person can commit an offence under those sections not only if they know, or as the case may be intend, that their actions are for the purposes of terrorism, but also if they have reasonable grounds to suspect that is the purpose.
- 2.16 Section 19 provides that a person who receives information in the course of a trade, profession, business or employment which leads them to *believe or suspect* that another person has committed an offence under Sections 15–18 is guilty of an offence if they do not disclose (a)

17 For an example of current sector practice, see the Charity case study in Annex C.

their belief or suspicion and (b) the information on which it is based to a constable as soon as is reasonably practicable. For legitimate charities this is perhaps the most significant obligation of the Act, as it effectively demands a high degree of vigilance above and beyond the financial prudence required by the Charity Commission's regulatory model and explicitly in relation to terrorist finance.

2.17 Finally, Section 39 of the Act creates the offence of 'tipping off' the subject of an investigation under the Act, or tampering with any relevant material.

The Terrorism (United Nations Measures) Order 2006 and The Al-Qaida and Taliban (United Nations Measures) Order 2006

The Terrorism (United Nations Measures) Order 2006

2.18 This secondary legislation implements the 'asset freezing' requirements of United Nations Security Council Resolution (UNSCR) 1373 and its successor resolutions in the UK. This legislation performs two main functions in that:

- it enforces financial restrictions in the UK against individuals who have been designated as terrorists under EC Regulation 2580/2001; and
- it gives the UK a power to impose financial restrictions against persons who the UK has reasonable grounds to suspect are terrorists (i.e. persons who commit, attempt to commit, facilitate or participate in the commission of acts of terrorism); persons acting on behalf of or at the direction of terrorists; or persons directly or indirectly controlled or owned by terrorists.

The Al-Qaida and Taliban (United Nations Measures) Order 2006

2.19 This secondary legislation implements UNSCR 1267 and successor resolutions in the UK. This

legislation performs three main functions in that:

- it implements financial restrictions in the UK against persons who have been designated under the relevant UNSCRs;
- it enforces in the UK financial restrictions against persons who have been designated under the relevant UNSCRs where those restrictions are implemented by the European Union (EU) under EC Regulation 881/2002; and
- it gives the UK a power to impose financial restrictions against a person who the UK has reasonable grounds to suspect is or may be designated under the relevant Security Council Resolutions; a person acting on behalf or at the direction of a designated person; or a person directly or indirectly owned or controlled by a designated person.

2.20 An asset freeze under either of these Orders prohibits the acts of:

- dealing with funds (including financial assets) and economic resources (i.e. other assets of every kind) that belong to or are owned or held by a designated person; and/or
- making funds and economic resources available to a designated person.

2.21 Failure to abide by an asset freeze under these Orders is a criminal offence with a maximum penalty on conviction of seven years' imprisonment and an unlimited fine.

2.22 The full list of persons designated under these Orders is published on the Bank of England's website (financial sanctions page).¹⁸ The list is substantial, and covers a range of individuals and organisations based in the UK and overseas. This makes it an important resource for both domestic and internationally active charities – particularly grant-givers – not only for the purposes of ensuring that their funding (or any

18 See www.bankofengland.co.uk/publications/financialsanctions/index.htm

relief falling under the definition of an 'economic resource') is not going to designated persons, but also for the purpose of vetting any person wishing to join the charity who would exercise any control over the charity's funds.

Existing safeguards: charity law and Charity Commission regulation

2.23 The Charity Commission is established by law¹⁹ as the independent regulator and registrar for charities in England and Wales.

2.24 It is a non-ministerial government department staffed by civil servants under the direction of a non-executive board appointed through open competition by the Minister for the Cabinet Office.²⁰ As a non-ministerial government department it is not subject to direction or control by ministers, and so makes decisions about its day-to-day work independently from government. The Charities Act 2006 modernised the Charity Commission's constitution and preserves its independence. As in the case of other departments, the Commission's funding comes directly from the Treasury on a three-yearly basis and is reviewed within the framework of the Comprehensive Spending Review cycle. It is accountable directly to Parliament for its use of this funding.²¹ The charitable sector exercises no authority over the Commission, nor is it liable to pay any kind of fee to support the registration or regulatory functions of the Commission.

2.25 The Commission describes its regulatory role as:

- to ensure that charities meet the legal requirements for being a charity and are equipped to operate properly and within the law;
- to check that charities are run for public benefit and not for private advantage;

- to ensure that charities are independent and that their trustees take their decisions free of control or undue influence from outside; and
- to detect and remedy serious mismanagement or deliberate abuse by or within charities.

2.26 Day-to-day work to fulfil this role can be broken down into the following areas.

Information and advice on (i) what the law requires of charities and (ii) good practice

2.27 This is chiefly achieved through the publication, on paper and online, of a vast library of guidance, reports and miscellaneous other documents. This resource appears to be well known to the sector and is routinely accessed.

Charity services

2.28 This is essentially the bulk of the Commission's work, and consists of:

- the registration process;
- bespoke advice and guidance formally provided to 24,000 charities each year, with a further 250,000 calls handled by its contact centre;
- several hundred visits to charities each year to review their activities, constitutions and administration, identifying good and bad practice;
- legal schemes or orders modernising the constitutions of existing charities; and
- collation and monitoring of data routinely collected from the sector.

Compliance, intervention and enforcement

2.29 The Commission has an arsenal of remedial powers that it can apply where the evidence points to misconduct or mismanagement within a charity, or to any other action that puts charitable assets at risk of loss, damage or misuse. Such powers are normally deployed by

19 The Charities Act 1993 and the Charities Act 2006.

20 Previously the Home Secretary.

21 See www.parliament.uk/parliamentary_committees/committee_of_public_accounts.cfm

the Commission's investigative unit, which is tasked with obtaining the requisite evidence to underpin such usage.

Regulatory engagement: the lifecycle of a charity

2.30 The main points of contact between the Commission and a charity during its lifetime are as follows.

Registration

2.31 The registration process is a largely paper-based exercise during which the Commission asks for a range of information from the charity in order to satisfy itself that the organisation is charitable in law. It also requires some demonstration that the organisation is more than just a concept (such as some evidence that the organisation has been established) and that it has a governing document that is correctly applied.

2.32 A list of members of the governing body ('trustees') and figures for projected annual income are also fundamental inputs from the charity at this stage, without which registration is not carried forward.

2.33 The Charities Act 1993 makes it illegal for certain categories of person to act as trustees, namely those who:

- have an unspent conviction for an offence involving dishonesty or deception;
- are undischarged bankrupts;
- have previously been disqualified from acting as a company director; or
- have previously been removed from control of a charity by order of the Commission.

2.34 As part of the registration process, the Commission has the option to conduct checks on the members of the governing body to determine whether they are acting while disqualified.

2.35 Once registration is complete, the charity is assigned a registration number and entered into the Commission's database. A summary of information about the charity is published on the Commission's website.

Annual monitoring

2.36 All charities on the register are required to furnish the Commission with a minimal level of information on income, expenditure and changes to its trustee body. All charities have 10 months beyond the end of their financial year to provide this information to the Commission before they are considered to be in default.

2.37 The amount of information supplied is proportionate to income and increases in stages as a charity's annual income increases, so that larger charities (with an income over £1 million) are required to submit a substantial amount of information on their activities, funding, projects or services and governance.

2.38 The financial data supplied are run through automated risk-analysis systems to detect potential compliance problems such as the use of funds to pay wages to trustees or to pay for outputs that are incompatible with the charity's objectives. Any 'hits' at this stage are followed up by a caseworker.

2.39 A summary of income and expenditure information is added to the charity's entry on the Commission's website. Commission records are updated with any reported changes to the charity's governing body.

2.40 Charities that default on their obligation to submit annual information are chased up by the Commission's investigative unit. Defaulters are prioritised according to their annual income, ensuring that potential risks to charitable funds are dealt with in order of magnitude.

2.41 The names of persistent defaulters are published by the Commission, a useful sanction as it causes the charity concerned significant reputational damage. A charity is normally considered to be 'dormant' or inactive when it has been out of contact with the Commission for a total of three years. Through tracing work, these charities are either brought back into the regulatory regime or removed from the register if the Commission is satisfied that they are no longer operating.

Review visits

2.42 The Commission operates a visits programme that delivers a 'health check' on compliance with charity law and governance arrangements to approximately 300 charities per year. Several risk factors are considered as part of the selection process. The programme is mainly based on themes or topics of relevance to the charity sector (such as risk management or international work), with the aim of disseminating advice on best practice. Where necessary, the programme provides bespoke guidance on preventing or responding to the misapplication of funds or mismanagement.

The Charity Commission and compliance

2.43 The Commission has created a specific intelligence function within the organisation in order to:

- ensure close and continuous engagement with other departments and law enforcement agencies on relevant operational issues; and
- inform risk-based prioritisation of casework, drawing on relevant corporate knowledge, external intelligence and complaints or allegations received from the public.

2.44 The Charity Commission has the power to institute 'formal inquiries' into charities where serious instances or allegations of abuse are detected and where it decides that this is a proportionate response to the concerns raised. In circumstances where trustees can and are

willing to co-operate with the Commission to resolve concerns, a formal inquiry is not normally opened.

2.45 To assist in the gathering of information under these inquiries, the Commission has the power to demand documents from or interviews with relevant individuals, and under the Charities Act 2006 has the power both to enter premises to inspect and take documents and to direct the charity to take specific action. All the Commission's powers are devolved from the High Court, so (with the exception of entry, search and seizure) it can bring them to bear without seeking a court order.

2.46 The management of such inquiries is conducted with a view to:

- protecting charity assets from misuse; and
- re-establishing good governance and stable administration in the charity.

Under the terms of a formal inquiry, the Commission can bring a number of powers to bear, including in particular the following:

Temporary and protective powers

2.47 These include:

- the freezing of a charity's bank accounts and restricting transactions;
- the suspension of trustees or others;
- the appointment of new trustees; and
- the appointment of a receiver manager to take control of a charity for a specified period.

Permanent and remedial powers

2.48 These include:

- removing and appointing trustees; and
- remedial schemes (to replace or amend the charity's governing document).

Existing safeguards: internal controls and sector best practice

2.49 The regulatory framework that exists for charities requires them to take steps to ensure their compliance. For example, a governing body of a charity that could not demonstrate to the Charity Commission that it had applied its resources according to its stated goals, nor that it had set up procedures for handling funds commensurate with the risk of fraud, theft or other abuse, would be subject to intervention by the Commission.

2.50 Many charities have therefore already taken steps explicitly to minimise the risk of abuse by terrorists. For example, the recent National Council for Voluntary Organisations report entitled *Security and Civil Society: the impact of counter-terrorism measures on civil society organisations* notes that:

‘there is a growing recognition within the international development sector that organisations need to be more vigilant in the way that they work, for example, reviewing financial controls and undertaking checks on partner organisations on the ground to ensure that they are not on a proscribed list.’

The Disasters Emergency Committee and British Overseas NGOs for Development, both important umbrella bodies for charities involved in international aid, are working with their members to mitigate the risk of terrorist abuse. Similar work is under way in other parts of the sector as well, for example in relation to fundraising activities.

2.51 The existence of a growing body of good practice in the sector provides an important resource for the regulator and the rest of the sector to adapt and propagate.

Chapter 3: Effectiveness of current safeguards

Charities and counter-terrorism legislation

- 3.1 Charity Commission guidance paper OG96, *Charities and Terrorism*, published in 2003, gave charities the option of complying with the reporting obligation under Section 19 of the Terrorism Act 2000 by allowing them to report suspicions of terrorist financing to the Charity Commission. In the time that has elapsed since the publication of that guidance, very few charities have made any such report. Over the same period, the UK's Financial Intelligence Unit (previously part of the National Criminal Intelligence Service and now housed within the Serious Organised Crime Agency (SOCA)), which acts as the central repository for all reports of suspected money laundering or terrorist financing, has received very few reports from charities.
- 3.2 Law enforcement and intelligence agency experience suggests that charities displaying one or more of the high-risk characteristics set out in Chapter 2 are often likely to be in close proximity to situations or activities that could give grounds for suspicion.
- 3.3 During the course of 2006, the UK's Financial Intelligence Unit received 48 'suspicious activity reports' from the financial services sector regarding suspected links between charities (or individuals connected to charities) and terrorist financing. Of these, 34 were considered substantive enough to warrant further investigation.
- 3.4 Over the same period, law enforcement inquiries into terrorist networks found that 'a significant proportion' of their investigations were extending to include the consideration of a charity in some context. Actual instances of abuse have proven very rare; it is more common in these cases for a charity to be found on the periphery of a given network either by virtue of its membership, employees or beneficiaries.
- 3.5 Major incident investigations have shown similar results: the financial trail followed by the National Terrorist Financial Investigation Unit (NTFIU) in relation to the 7 July 2005 attacks in London included direct or indirect links to eight different charities. A further six charities have been linked to the networks suspected of being behind two subsequent foiled attacks.
- 3.6 Given such causes for concern, the small number of reported suspicions under the Terrorism Act 2000 by the charity sector is hard to explain, although it may derive from a lack of awareness about the scope and relevance of the legislation.
- 3.7 More could be done by government to raise awareness of the Terrorism Act 2000 and financial sanctions legislation within the charitable sector. At present, the only specific guidance is that provided by the Charity Commission (OG96), and this is in some respects out of date and not as comprehensive as it could be. A thorough review and overhaul of the document, and the cross references from other relevant Charity Commission guidance, would be beneficial.
- 3.8 Furthermore, there appears to be no routine sharing of information on emerging terrorist finance risks between government and the charity sector. By comparison, the financial services sector frequently receives both written and oral updates from SOCA and in some cases the Financial Services Authority on such issues. Business sectors subject to the Money Laundering Regulations 2003 are served by standing arrangements with SOCA for dialogue about emerging threats and other relevant issues. Although dialogue between the Charity Commission and the charity sector is excellent, there is limited explicit focus on terrorist finance threats and their relevance to the sector.

Charity Commission regulation and combating terrorism

- 3.9 The confidence that exists in the charitable sector is in large part due to the success of the Charity Commission in regulating the sector. The Charity Commission's regulatory model is frequently studied by other countries seeking to implement similar measures. The Commission's approach to regulation is predicated on the themes of risk and proportionality, and relies upon a detailed knowledge of the sector that it regulates.
- 3.10 Some aspects of the Commission's work are hard to quantify, others are much more straightforward. For example, during the financial year 2005/06 the Commission utilised its remedial powers more than 1,000 times, resulting in the safeguarding of an estimated £2.3 million of charitable assets. The Commission has built up a considerable body of experience on the best and most effective use of such powers.
- 3.11 In respect of terrorist exploitation of the charity sector, the Commission's experience is that actual cases of sham charities or the abuse of legitimate charities are rare. Investigation reports on closed cases are publicly available in relation to 16 charities; in several of these cases the suspicion of terrorist abuse has been refuted through Charity Commission investigation. Details about additional fact-finding work in relation to suspicions of terrorist abuse and live cases are not in the public domain.
- 3.12 It is the case, however, that as terrorist finance controls in other sectors tighten, so terrorists increasingly seek to find ways to circumvent them. The recent passage of the EC Wire Transfers Regulation 2006²² and the imminent implementation of the European Third Money Laundering Directive 2005²³ will make it even more difficult for terrorists to channel funds

through money remitters, banks and other sectors currently subject to the Money Laundering Regulations 2003. The Charity Commission's regulatory model, though robust, was originally designed to combat more mundane abuses such as fraud or theft; it is important that the Commission's approach continues to evolve in line with the increased threat.

A strategy for the Charity Commission and the charity sector on combating terrorist exploitation of charities

- 3.13 The Charity Commission publicises its policy regarding allegations of terrorist exploitation of charities on its website. This policy has been in place for some time and has informed Charity Commission decision making on particular cases on several occasions. The policy revolves around three key assumptions:
- The Commission would not register an organisation that had support of terrorism explicitly or implicitly as an objective.
 - The use of an existing charity's assets for support of terrorist activity is not a proper use of those assets.
 - Links – or alleged links – between a charity and terrorism corrode public confidence in the integrity of charity.
- 3.14 This policy is an important and welcome statement of intent, although at present it is not complemented by a published strategy for delivering on the underlying objective, which runs the risk that the Commission's approach may not be sufficiently proactive. A strategy is required that:
- ties together all the elements of the Commission's remit under the policy objective of combating terrorist exploitation of the sector;

22 EC Regulation 1781/2006.

23 Directive 2005/60/EC.

- puts the Commission onto a more proactive footing in terms of its intention to deter, detect and disrupt terrorist abuse in the charity sector; and
- involves the sector in the development and implementation of that strategy, particularly in raising awareness and identifying and disseminating existing best practice.

3.15 The development of such a strategy should take into account best practice already operating effectively within the sector in order for the Commission to reach a view on what risk assessment, due diligence and proportionate preventive measures could be deployed by the sector in order to identify risk and counter the terrorist finance threat.

Relationship between the Charity Commission and the counter-terrorist community

3.16 The Charity Commission, although part of government, is an independent regulator, with discretion to set its own internal procedures for information sharing with other parts of government and for initiating action against charities according to its own risk-assessment procedures. This independence was confirmed and preserved by the Government with the passage of the Charities Act 2006. When working with other government departments and law enforcement and intelligence agencies, therefore, it is important that this independence is not compromised. The existence of an intelligence function within the Commission is to be welcomed as an essential prerequisite of operating a successful risk-based and proportionate regulatory model. There may be scope for the Commission to review its approach further with a view to building clearer intelligence links into its casework.

3.17 One part of the intelligence function's role is to provide a standing network of liaison relationships or 'single points of contact' with other relevant agencies in government and law enforcement. This network appears to be

thriving in respect of interaction on more straightforward problems such as allegations of fraud in charities or theft of assets. There is scope for improvement in the Commission's relationships with the spectrum of government departments and agencies involved in counter-terrorist work to improve. With the exception of a long-standing link to NTFIU, direct relationships with government intelligence agencies and the Whitehall counter-terrorist committee structure are characterised as somewhat ad hoc. Working procedures and protocols should be reviewed and refreshed in order to ensure that these relationships become more effective in countering the terrorist threat. This should include more systematic access to and use of classified intelligence material on the terrorist threat by the Charity Commission.

3.18 The Government's strategy on countering terrorist finance explicitly recognises the value of disruption alongside deterrence and detection, reflecting the importance of being able to interdict funds before they are applied for terrorist purposes. Closer working relationships between the Commission and other government departments, intelligence agencies and law enforcement bodies should also ensure that where the Commission utilises its powers in cases of suspected or potential terrorist abuse, this is done in the most co-ordinated way possible, recognising the roles of other parts of government and the nature of the particular threat.

3.19 Within this context, the role of the Commission's investigative function in respect of cases with suspected or potential terrorist links should also be reviewed and where possible enhanced.

3.20 The Commission is an independent civil regulator, not a prosecuting authority. Where criminality is detected, the Commission refers the matter to the police. Since it is not collecting information for use in court, Commission investigations are not run

according to the rules of evidence in the Police and Criminal Evidence Act 1984. Investigators are normally generalist caseworkers with a high level of expertise in charity law and the regulatory environment, and historically the investigation work of the Commission has been desk-based, relying heavily on correspondence rather than interviews, visits or surveillance. This can sometimes make it difficult for law enforcement agencies to pick up where the Commission leaves off.

- 3.21 To improve the referral of such cases, some consideration should be given to training caseworkers to achieve formal accreditation as financial investigators²⁴ and to providing bespoke training and guidance to all caseworkers on terrorist finance issues.
- 3.22 There is also scope for the Commission to consider how it can better satisfy itself in respect of the proper end use of funds by charities fitting a high-risk profile, including a review of the appropriateness of deploying on-site visits in foreign jurisdictions. At present the Commission relies heavily on scrutiny of accounting records to form judgements about the proper use of funds overseas, with additional information gathering or analysis left to the discretion of the caseworker concerned.

Charities' internal controls

- 3.23 The limited number of cases of identified abuse of legitimate charities to date suggests that best practice within the sector is already having a positive impact where it is being applied. However, the findings of the review suggest that more could be done to raise awareness within the sector of both the threat and the current safeguards. An analysis of existing best practice within the sector in terms of its risk assessment and due diligence procedures to mitigate terrorist finance risk was beyond the scope of this review; however, the consultation process does provide a mechanism

for identifying what best practice does exist, both in terms of risk assessment and proportionate measures to counter risk which could be disseminated more widely.

- 3.24 Ongoing development of best practice in the sector may wish to address any new vulnerabilities identified by this review. There have been a small number of instances where internationally active charities have suffered failures of their financial controls which have exposed them to a high risk of having their funds misappropriated and potentially exploited for terrorist activity. The case study below synthesises elements from more than one such case to provide an illustrative example.

A charity was working with an existing partner to deliver a health programme in Afghanistan. It used an intermediary organisation based in Pakistan with business interests in Afghanistan to transfer funds to its partner organisation.

The charity made a large payment to the intermediary organisation. The intermediary then failed to transfer these funds to the charity's partner. This was not picked up by the charity's audit systems until the end of the financial year.

In response to this incident, the charity carried out a full review of its financial controls and governance. The review identified a number of weaknesses in the charity's systems which contributed to the loss of funds. This included a failure to ensure that the transfer arrangements were subject to a partnership agreement, which made recovering the lost funds more difficult.

The charity implemented new procedures to prevent similar losses occurring in the future. These included new risk assessment and audit systems, the introduction of new anti-money laundering and international operations policies and the compulsory use of partnership agreements.

24 Accreditation as conferred by the Assets Recovery Agency under the Proceeds of Crime Act 2002.

- 3.25 This sort of failure is very much the exception rather than the norm, but it serves to illustrate that the types of risk encountered by the sector are varied, and also highlights the importance of a proportionate response to situations where safeguards have failed. It also reinforces the message that all charities working internationally should ensure that their controls take into account not only the potential for loss but also the risk that partners overseas might seek to exploit opportunities to use the charity's money directly or indirectly for terrorist purposes.
- 3.26 Significant benefit could be derived from a joint piece of work by the sector and the Charity Commission on standardising the approach to situations involving the use of foreign partner organisations, particularly in states where the lines of demarcation between ostensibly humanitarian groups and terrorist groups are murky or obscure. More strenuous and targeted risk assessment work by those parts of the sector that are particularly susceptible to these risks would also be extremely valuable in this context.

Chapter 4: Recommendations and consultation

“...we need not only to deny a safe haven to terrorists, but ensure there is no hiding place for those who finance terrorism.”

Chancellor of the Exchequer Gordon Brown, speech to the Royal United Services Institute, 13 February 2006.

“... however much we rely on our intelligence and security agencies, as we should, we ought to remember... that defeating terrorism is not simply a job for the Government, the security agencies or the police. Just as the intelligence and security agencies work on behalf of the whole community, the whole community must be involved in defeating terrorism.”

Home Secretary John Reid, Intelligence and Security Committee, Annual Report, 11 July 2006.

4.1 During the course of the review, the review team was impressed by the understanding shown by sector representatives in respect of the need to act decisively against terrorist risks, and the conviction of public sector representatives that an independent charity sector is vital to the social fabric of the country. This is a delicate balance, but one which it is vital to maintain if both sectors are to work together effectively to combat terrorism in the future.

4.2 Key findings of the review are that:

- to date, identified instances of terrorist exploitation of charities are rare;
- the latent risk of terrorist exploitation inherent in some parts of the sector is significant, and continued vigilance is required from all stakeholders to ensure that this risk is not realised;
- the legislative framework for controlling the terrorist abuse of charities can only be effective if the sector is fully aware of and compliant with its provisions;
- the Charity Commission is a world-leader in the regulation of charities, and it is essential that it implements appropriate and proportionate measures to deal with the evolving threat of terrorist finance.

4.3 Recommendations on a response to these findings are set out below.

Key recommendations

4.4 The recommendations of the review that are set out below are for the charity sector together with the Charity Commission, other relevant government departments and law enforcement agencies in order to enhance current work to reduce the risk of terrorist exploitation of the sector. The recommendations are designed in particular to:

- stimulate further efforts by the sector to raise awareness of the threat and encourage further dissemination of best practice to mitigate the risk of abuse;
- support the work of the sector in building stronger communities, promoting democracy and overseas development;
- reinforce Charity Commission work to protect the sector from all kinds of abuse, including that by terrorists; and
- strengthen the working relationships and co-ordination between relevant government departments and law enforcement agencies and the Charity Commission to combat the risk of terrorist exploitation of charities.

4.5 The Government seeks to consult the sector and the public on the proposals of this review in order to establish the strongest possible policy framework going forward.

Commitment and responsibility

4.6 All those involved in the charitable sector should commit themselves to ensuring that charities do not provide a transmission belt for funds to terrorist networks. Both the Charity Commission and the sector have an important role to play in delivering effective preventative safeguards. This responsibility should include preventing the transmission of funds ostensibly for humanitarian relief that directly or indirectly support terrorist activity.

Strategy and objectives

4.7 The Charity Commission should publish its strategic and operational objective to identify and minimise the risk of terrorist exploitation of charities. It should have a business strategy that directs activities and resources to deliver this objective. It should have benchmark indicators of success, on which it reports regularly.

4.8 In partnership with other relevant bodies, this strategy should include provisions to encourage the following outcomes.

(i) Risk-based diligence and assurance

4.9 Charities should assess their exposure to the risk of terrorist exploitation and, in response, take proportionate steps accordingly to ensure that funds are not passed, directly or indirectly, to partner organisations with terrorist connections.

4.10 A 'know your beneficiary' principle should extend to identifying and forestalling any funding connections either to designated terrorist organisations (such as those on the Bank of England's asset freeze list) or to recipients whose activities may give support to terrorism.

4.11 This risk-based approach should be supported by the Government and the Charity Commission through:

- practical guidance on evaluating risk and forestalling abuse;
- ongoing and informed feedback to the sector on charity-linked terrorist finance threats worldwide; and
- risk-based assurance work (including, where appropriate, on-site visits) to verify the proper end use of funds.

(ii) Proactive investigation and disruption

4.12 The Charity Commission should develop its investigative capacity and the appropriate co-ordination with counter-terrorism agencies to help ensure that possible instances of terrorist finance in the sector are identified

and investigated proactively, in line with the Commission's independent risk-assessment procedures.

4.13 Both the Commission and the counter-terrorist agencies are operationally independent. Effective working relationships between them are therefore essential. Protocols to encourage this co-ordination, and their success, should be kept under review.

4.14 The Charity Commission and other relevant bodies should deploy the independent powers available to them proactively, as an integral part of efforts in the UK to choke off funds to terrorists. The Commission and other relevant bodies should co-ordinate activity to ensure maximum disruptive effect against terrorist finance threats.

Consultation

4.15 This document gives all interested parties the opportunity to engage with the Government on how the UK can best implement the recommendations of the review in order to ensure continued future effectiveness in safeguarding the sector from terrorist abuse.

4.16 The Home Office invites comments on the policy framework created by the recommendations from this review. Specific questions are listed below, but respondents are of course free to frame their responses as they see fit.

4.17 This consultation document represents part of a wider process of discussion and engagement with representatives of the charitable sector and other stakeholders; a list of organisations consulted is attached at Annex A.

4.18 This is a consultation on policy issues only. If it becomes desirable to update the law in order to introduce any additional specific regulations, this will be conducted and if necessary consulted on in accordance with the procedures set out by the Better Regulation Executive (see www.cabinetoffice.gov.uk/regulation).

4.19 The Government's strategy on countering international terrorism is relevant to this document, and can be found at www.intelligence.gov.uk/publications/documents/countering.pdf

Consultation questions

Overall policy

- Do you agree that a risk-based and proportionate approach involving all stakeholders is the best way to counter the threat of terrorist abuse of charities?
- Are there measures that the Government could take in addition to the recommendations presented here that would help to safeguard public and donor confidence in the integrity of the sector?

Policy recommendations

- How should charities assess their exposure to the risk of terrorist exploitation?
- What information and tools would assist charities to do this?
- Is there a need for a more explicit 'due diligence' obligation on the charity sector requiring appropriate controls to be put in place by charities for the purposes of detecting and forestalling abuse by terrorists? If so, what is the best mechanism for delivering this change?
- What form should 'know your beneficiary' checks take?
- Should the proposals for 'know your beneficiary' checks be turned into a standardised requirement across the sector? If so, what is the best way to do this?
- Given the diversity of the sector, what is the best way to raise awareness of its obligations under the Terrorism Act 2000 and financial sanctions legislation?
- How can existing best practice in the sector be identified and promulgated in terms of a) risk assessment, and b) proportionate controls,

systems and processes to reduce exposure to particular risks?

- What form should feedback to the sector on relevant terrorist threats take?

How to respond

4.20 The Government welcomes the views of all stakeholders on the issues raised in this document. The consultation period begins with the publication of this document, and will run for 12 weeks. Please ensure that your responses reach us by 2 August 2007.

Comments should be sent to:

Charities and Terrorist Finance Consultation
Home Office
CRCSG
2 Marsham Street
London
SW1P 4DF

E-mail:

CharitiesReview2007@homeoffice.gsi.gov.uk

4.21 This document can also be found on the websites of the Home Office, the Treasury and Cabinet Office. Hard copies are available on request from the above address.

4.22 When responding, please state whether you are responding as an individual or representing the views of an organisation. If responding on behalf of a larger organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.

Confidentiality of responses

4.23 All written responses will be made public on the Home Office's website unless the author specifically requests otherwise. In the case of electronic responses, general confidentiality disclaimers that often appear at the bottom of e-mails will be disregarded for the purpose of publishing responses unless an explicit request for confidentiality is made in the body of the

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response. If you wish part, but not all, of your response to remain confidential, please supply two versions – one for publication on the website with the confidential information deleted, and another confidential version for the consultation team at the Home Office only.

4.24 Even where confidentiality is requested, if a request for a disclosure of the consultation response is made in accordance with the freedom of information legislation, and the response is not covered by one of the exemptions in the legislation, the Government may have to disclose the response in whole or in part.

4.25 Any Freedom of Information Act queries should be directed to:

Freedom of Information
Jane Sigley
Information and Record Management Services
2 Marsham Street
London
SW1P 4DF

Annex A:

Organisations consulted by the review team

Public sector input

- Cabinet Office
- Charity Commission
- Department for International Development (DFID)
- Department for Social Development Northern Ireland
- Foreign and Commonwealth Office
- Financial Services Authority (FSA)
- Joint Terrorism Analysis Centre (JTAC)
- Metropolitan Police Service (NTFIU)
- Office of the Scottish Charity Regulator
- Serious Organised Crime Agency (SOCA)
- Security and Intelligence Agencies

Charity sector and business input

- Association of Chief Executives of Voluntary Organisations (ACEVO)
- BDO Stoy Hayward
- British Bankers' Association (BBA)
- British Overseas NGOs for Development (BOND)
- Charity Law Association
- Charity Finance Directors' Group (CFDG)
- Council of Ethnic Minority Voluntary Sector Organisations (CEMVO)
- Disasters Emergency Committee (DEC)
- Institute of Fundraising
- National Council for Voluntary Organisations (NCVO)

Interpretative Note to Special Recommendation VIII: Non-Profit Organisations

Introduction

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

Objectives and general principles

3. The objective of Special Recommendation VIII (SR VIII) is to ensure that NPOs are not misused by terrorist organisations:
 - to pose as legitimate entities;
 - to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; or
 - to conceal or obscure the clandestine diversion of funds intended for legitimate purposes but diverted for terrorist purposes.
4. In this Interpretative Note, the approach taken to achieve this objective is based on the following general principles:
 - Past and ongoing abuse of the NPO sector by terrorists and terrorist organisations requires countries to adopt measures both:
 - to protect the sector against such abuse; and
 - to identify and take effective action against those NPOs that either are exploited by or actively support terrorists or terrorist organizations.
 - Measures adopted by countries to protect the NPO sector from terrorist abuse should not disrupt or discourage legitimate charitable activities. Rather, such measures should promote transparency and engender greater confidence in the sector, across the donor community and with the general public that charitable funds and services reach intended legitimate beneficiaries. Systems that promote achieving a high degree of transparency, integrity and public confidence in the management and functioning of all NPOs are integral to ensuring the sector cannot be misused for terrorist financing.
 - Measures adopted by countries to identify and take effective action against NPOs that either are exploited by or actively support terrorists or terrorist organisations should aim to prevent and prosecute as appropriate terrorist financing and other forms of terrorist support. Where NPOs suspected of

or implicated in terrorist financing or other forms of terrorist support are identified, the first priority of countries must be to investigate and halt such terrorist financing or support. Actions taken for this purpose should to the extent reasonably possible avoid any negative impact on innocent and legitimate beneficiaries of charitable activity. However, this interest cannot excuse the need to undertake immediate and effective actions to advance the immediate interest of halting terrorist financing or other forms of terrorist support provided by NPOs.

- Developing co-operative relationships among the public, private and NPO sector is critical to raising awareness and fostering capabilities to combat terrorist abuse within the sector. Countries should encourage the development of academic research on and information sharing in the NPO sector to address terrorist financing related issues.
- A targeted approach in dealing with the terrorist threat to the NPO sector is essential given the diversity within individual national sectors, the differing degrees to which parts of each sector may be vulnerable to misuse by terrorists, the need to ensure that legitimate charitable activity continues to flourish and the limited resources and authorities available to combat terrorist financing in each jurisdiction.
- Flexibility in developing a national response to terrorist financing in the NPO sector is also essential in order to allow it to evolve over time as it faces the changing nature of the terrorist financing threat.

Definitions

5. For the purposes of SR VIII and this Interpretative Note, the following definitions apply:
 - 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 terms *FIU*, *legal arrangement* and *legal person* are as defined by the FATF Forty Recommendations (2003) (the FATF Recommendations).
 - The term *funds* is as defined by the Interpretative Note to FATF Special Recommendation II.
 - The terms *freezing*, *terrorist* and *terrorist organisation* are as defined by the Interpretative Note to FATF Special Recommendation III.
 - The term *appropriate authorities* refers to competent authorities, self-regulatory bodies, accrediting institutions and other administrative authorities.
 - The term *beneficiaries* refers to those natural persons, or groups of natural persons who receive charitable, humanitarian or other types of assistance through the services of the NPO.

Measures

6. Countries should undertake domestic reviews of their NPO sector or have the capacity to obtain timely information on its activities, size and other relevant features. In undertaking these assessments, countries should use all available sources of information in order to identify features and types of NPOs, which by virtue of their activities or characteristics, are at risk of being misused for terrorist financing.¹ Countries

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

should also periodically reassess the sector by reviewing new information on the sector's potential vulnerabilities to terrorist activities.

7. There is a diverse range of approaches in identifying, preventing and combating terrorist misuse of NPOs. An effective approach, however, is one that involves all four of the following elements:
 - outreach to the sector;
 - supervision or monitoring;
 - effective investigation and information gathering; and
 - effective mechanisms for international co-operation.
8. The following measures represent specific actions that countries should take with respect to each of these elements in order to protect their NPO sector from terrorist financing abuse.

Outreach to the NPO sector concerning terrorist financing issues

9.
 - Countries should have clear policies to promote transparency, integrity and public confidence in the administration and management of all NPOs.
 - Countries should encourage or undertake outreach programmes to raise awareness in the NPO sector about the vulnerabilities of NPOs to terrorist abuse and terrorist financing risks, and the measures that NPOs can take to protect themselves against such abuse.
 - Countries should work with the NPO sector to develop and refine best practices to address terrorist financing risks and vulnerabilities

and thus protect the sector from terrorist abuse.²

- Countries should encourage NPOs to conduct transactions via regulated financial channels, wherever feasible, keeping in mind the varying capacities of financial sectors in different countries and in different areas of urgent charitable and humanitarian concerns.

Supervision or monitoring of the NPO sector

10. Countries should take steps to promote effective supervision or monitoring of their NPO sector. In practice, countries should be able to demonstrate that the following standards apply to NPOs 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.
 - (i) NPOs should maintain information on: (1) the purpose and objectives of their stated activities; and (2) the identity of the person(s) who own, control or direct their activities, including senior officers, board members and trustees. This information should be publicly available either directly from the NPO or through appropriate authorities.
 - (ii) NPOs should issue annual financial statements that provide detailed breakdowns of incomes and expenditures.
 - (iii) NPOs should be licensed or registered. This information should be available to competent authorities.³
 - (iv) NPOs should have appropriate controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose and objectives of the NPO's stated activities.

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

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

- (v) NPOs should follow a ‘know your beneficiaries and associate NPOs’⁴ rule, which means that the NPO should make best efforts to confirm the identity, credentials and good standing of their beneficiaries and associate NPOs. NPOs should also undertake best efforts to document the identity of their significant donors and to respect donor confidentiality.
- (vi) NPOs should maintain, for a period of at least five years, and make available to appropriate authorities, records of domestic and international transactions that are sufficiently detailed to verify that funds have been spent in a manner consistent with the purpose and objectives of the organisation. This also applies to information mentioned in paragraphs (i) and (ii) above.
- (vii) Appropriate authorities should monitor the compliance of NPOs with applicable rules and regulations.⁵ Appropriate authorities should be able to properly sanction relevant violations by NPOs or persons acting on behalf of these NPOs.⁶

Effective information gathering and investigation

11.
 - Countries should ensure effective co-operation, co-ordination and information sharing to the extent possible among all levels of appropriate authorities or organisations that hold relevant information on NPOs.
 - Countries should have investigative expertise and capability to examine those NPOs suspected of either being exploited by or

actively supporting terrorist activity or terrorist organisations.

- Countries should ensure that full access to information on the administration and management of a particular NPO (including financial and programmatic information) may be obtained during the course of an investigation.
- Countries should establish appropriate mechanisms to ensure that when there is suspicion or reasonable grounds to suspect that a particular NPO: (1) is a front for fundraising by a terrorist organisation; (2) is being exploited as a conduit for terrorist financing, including for the purpose of escaping asset freezing measures; or (3) is concealing or obscuring the clandestine diversion of funds intended for legitimate purposes, but redirected for the benefit of terrorists or terrorist organisations, this information is promptly shared with all relevant competent authorities in order to take preventative or investigative action.

Effective capacity to respond to international requests for information about an NPO of concern

12. Consistent with Special Recommendation V, countries should identify appropriate points of contact and procedures to respond to international requests for information regarding particular NPOs suspected of terrorist financing or other forms of terrorist support.

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

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

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

Annex C: Case studies

Proven instances of charities registered in England and Wales being exploited by terrorists remain rare. Even allowing for unreported and undetected abuses, it is clear that the vast majority of charities in this country are applying their resources towards legitimate charitable objectives, and in doing so make an extremely positive contribution to the social fabric of our society.

The following case studies are presented to illustrate situations where the existing safeguards to protect the sector have failed or have been seriously tested by terrorist abuse, as this material – alongside other information – has been important in shaping the findings of the review. This is followed by a case study in which an internationally active charity has adopted good practices to safeguard it from terrorist exploitation. Where the sector has been exploited, the information suggests that one of the three following methods has been used:

- deployment of a ‘charity’ to serve as a front organisation to raise funds in support of terrorist organisations;
- abuse of a legitimate charity to provide a transmission belt to move funds and other resources, and operatives, overseas; and
- abuse of a legitimate charity to deploy funds, resources and services being used to recruit members and foster grassroots support for a terrorist organisation’s militant ideology.

Case study 1: Tamils Rehabilitation Organisation

In 2000 the Charity Commission received allegations that the Tamils Rehabilitation Organisation (TRO) had links with the Liberation Tigers of Tamil Eelam (LTTE) – a proscribed organisation under the Terrorism Act 2000. The Commission subsequently opened an inquiry and, as a precautionary step, froze the charity’s bank accounts. It then issued an order requesting the submission of financial statements and records. During the course of the investigation it became apparent that the charity trustees had little, if any, control over money that was sent to Sri Lanka. The Commission therefore determined that an Interim

Manager be appointed to take over the administration of the charity. Continuing investigative work by the Charity Commission concluded that the charity’s representatives had indeed liaised with the LTTE to make decisions about where funds should be applied. The Interim Manager determined that a new organisation, the ‘Tamil Support Foundation’ should be established. Suitable trustees were identified and appointed and the assets of the TRO were transferred to the newly created Tamil Support Foundation and other charities conducting relief work in Sri Lanka. The inquiry was subsequently closed.

Case study 2: North London Central Mosque

The Charity Commission became aware of internal difficulties within the North London Central Mosque in 1998. Working with the trustees to resolve these difficulties, increasing concerns were identified about the conduct of extremist Abu Hamza. By 2001 it was clear that Abu Hamza was using the charity inappropriately for personal and political rather than charitable purposes. Abu Hamza abused his position at the Mosque to engender support for Islamic terrorist acts. As a result, the Commission suspended and later removed him as trustee of the charity. During its investigation, the Commission found that Abu Hamza and his supporters had set up a new separate bank account for the charity, which was frozen and later shut down. Following Abu Hamza’s removal the Commission has assisted the governing body to return the Mosque to a secure footing.

Case study 3: Islamic Foundation

The Charity Commission’s routine monitoring work uncovered the fact that two trustees of the Islamic Foundation appeared to be individuals named on the Bank of England’s asset freeze list. The Commission opened an inquiry and immediately suspended the named trustees. During the course of the investigation it materialised that the two individuals did not reside in the UK and had taken no real part in

the administration of the charity for some years.
The two trustees subsequently resigned.

The cases listed below by the National Terrorist Financial Investigation Unit relate to counter-terrorist investigations that remain current.

The detail from the cases listed has been removed to protect sensitive intelligence sources. However, the nature of the activity clearly demonstrates the extent to which the charitable sector is vulnerable to abuse by terrorists.

Case A

A UK-based charity raises funds from local charitable donations and by receiving funds from other reputable charitable organisations and businesses. It is believed that this charity also raises funds from wealthy individuals in the Middle East. These funds are then transferred to country A through multiple jurisdictions. The funds are transferred through the banking system, hawala and using cash couriers. These funds are destined to support attacks on UK or US interests in country A.

Case B

A UK-based charity raises funds from local donations, business interests and through fraud. These funds are then transferred to entities controlled by the trustees or withdrawn in cash and sent to country B where they are destined for a proscribed terrorist organisation.

Case C

Over a number of years a UK-based charity collected funds through local collections. These funds were then transferred through the banking system to an individual working in another charity in country C. These funds are then distributed by that individual to a proscribed terrorist organisation in country C.

Case D

A UK-based charity raises funds from local donations and business interests. The funds are then transferred to country D for the benefit of members of a proscribed terrorist organisation.

Charity case study

An internationally active charity, based in the UK and a member of British Overseas NGOs for Development (BOND), has developed the following risk management strategy based on its experiences:

- risk assessments of partners before they are accepted;
- risk assessments of projects before they are funded;
- funding agreements for each partner, with conditions for the continued funding of projects; and
- partner and project assessment visits to ensure that these conditions are being delivered on.

