

KCO BLOGS 2020

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COMBATING MONEY LAUNDERING AND COUNTERING FINANCING OF TERRORISM

Guidance for Non-Profit Organizations

The pertinence of the topic to our beloved country has become much more significant in last couple of years. Appearance of Pakistan on the “Grey List” of Financial Action Task Force (FATF) is certainly not a thing to ignore or to cheer about. To be removed from the not so good guys list, the concerned authorities of Pakistan are working hard to implement the FATF’s recommendations, the deadline of which is going to expire in October 2020.

The FATF is an inter-governmental body established in 1989. The mandate of FATF is to set standards and to promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and financing of proliferation and related threats to the integrity of the international financial system.

As each country has different legal, administrative and operational framework and different financial system and countries cannot take all identical measures to counter the threats. Therefore, the FATF recommendations set an international standard, which country should implement through measures adapted to their particular circumstances. The [recommendations](#) list out the essential measures that countries should have in place to:

- identify the risks, and develop policies and domestic coordination;
- pursue money laundering, terrorist financing and the financing of proliferation;
- apply preventive measures for the financial sector and other designated sectors;
- establish powers and responsibilities for the competent authorities (e.g., investigative, law enforcement and supervisory authorities) and other institutional measures;
- enhance the transparency and availability of beneficial ownership information of legal persons and arrangements;
- and facilitate international cooperation.

Generally, speaking the FATF standards recommends that Countries should first *identify, assess* and *understand* the risks of money laundering and terrorist finance that they face, and then adopt appropriate measures to mitigate the risk. This risk-based approach allows countries to adopt a more flexible set of measures in order to consume their resources and energies more effectively and apply preventive measures that are commensurate to the nature of risks.

In June 2018, as part of its ongoing review of compliance with the AML/CFT standards, the FATF identified Pakistan to have strategic AML/CFT deficiencies and out us in the List called “Grey List”. Other countries in the list were Ethiopia, Serbia, Sri Lanka, Syria, Trinidad and Tobago, Tunisia and Yemen. Pakistan made a high-level political commitment to work with the FATF to strengthen its AML/CFT regime and to address its strategic counter-terrorist financing-related deficiencies.

Pakistan has [committed](#) to work to implement its action plan to accomplish these objectives, including by:

- 1) demonstrating that TF risks are properly identified, assessed, and that supervision is applied on a risk-sensitive basis;
- 2) demonstrating that remedial actions and sanctions are applied in cases of AML/CFT violations, and that these actions have an effect on AML/CFT compliance by financial institutions;
- 3) demonstrating that competent authorities are cooperating and taking action to identify and take enforcement action against illegal money or value transfer services (MVTs);
- 4) demonstrating that authorities are identifying cash couriers and enforcing controls on illicit movement of currency and understanding the risk of cash couriers being used for TF;
- 5) improving inter-agency coordination including between provincial and federal authorities on combating TF risks;
- 6) demonstrating that law enforcement agencies (LEAs) are identifying and investigating the widest range of TF activity and that TF investigations and prosecutions target designated persons and entities, and persons and entities acting on behalf or at the direction of the designated persons or entities;
- 7) demonstrating that TF prosecutions result in effective, proportionate and dissuasive sanctions and enhancing the capacity and support for prosecutors and the judiciary;
- 8) demonstrating effective implementation of targeted financial sanctions (supported by a comprehensive legal obligation) against all 1267 and 1373 designated terrorists and those acting for or on their behalf, including preventing the raising and moving of funds, identifying and freezing assets (movable and immovable), and prohibiting access to funds and financial services;
- 9) demonstrating enforcement against TFS violations including administrative and criminal penalties and provincial and federal authorities cooperating on enforcement cases; and
- 10) demonstrating that facilities and services owned or controlled by designated persons are deprived of their resources and the usage of the resources.

If we closely watch the above list, we can conclude that most of the above measures that are committed related to countering terrorism and related activities. This is easily comprehensible keeping in view the condition and extent of terrorism and related activities in the country during last 10-15 years. Limiting/countering and stopping the financing of terrorism is utmost important for reducing if not eliminating it completely? Therefore, all organizations vulnerable to threats of financing of terrorism and related activities are required to cooperate with the government and other authorities in order to implement the strategies and fulfill the above commitments made to FATF.

Non-profit organizations (NPOs) sector is one of vulnerable sector to threats of financing of terrorism due to following reasons;

- NPOs enjoy high public trust and confidence;
- Have large outreach, and global presence including operating in conflict zones, resulting in interaction with large number of people;
- Are easy to be formed under most of the laws in vogue;
- By and large, are single person driven, without collective thought process, especially in small NPOs;
- Exhibit complex financial operations arising from multiple currencies, multiple donors, etc.
- Income and expenditure streams unpredictable, Suspected Transaction Report (STRs) harder to identify; and
- Have varying level of regulations in different parts of the world

FATF requires that countries should review the adequacy of laws and regulations that relate to NPOs which the country has identified as being vulnerable to terrorist financing abuse. Countries should apply focused and proportionate measures, in line with the risk based approach, to such NPOs to protect them from terrorist financing abuse, including:

- a) by terrorist organizations posing as legitimate entities;
- b) by exploiting legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset-freezing measures; and
- c) by concealing or obscuring the clandestine diversion of funds intended for legitimate purposes to terrorist organizations.

It is under this background that Securities and Exchange Commission of Pakistan (SECP) on 7th June 2018 issued “***Associations with Charitable and Not for Profit Objects Regulations, 2018***” to specify the requirements of licensing, registration and governance of associations not for profit under section 42 of the Companies Act, 2017. The Regulations introduced various measures to mitigate the risks of money laundering and terrorist financing by Non-Profit Organizations (NPOs) licensed under section 42 of the Companies Act, 2017. Existing associations were required to immediately comply with all the requirements of the Regulations.

The Regulations, inter-alia, specifies procedures for;

- ***grant of license*** to associations with charitable and not for profit objectives,
- ***incorporation*** of association as a public limited company;
- ***conditions applicable*** to such companies with regard to their business operations;
- ***fit and proper criteria*** for the promoters, members, directors & CEO; and
- ***enhanced due diligence*** of such companies and their members/directors in respect of money laundering/terrorist financing (ML/TF) risks,

The license granted under section 42 of the Companies Act, 2017 may be revoked by the Commission by an order in writing. Among other grounds for revocation, clause (g) (iii) of Section 42 provides as under: “the company is run and managed by persons who are involved in ***terrorist financing*** or ***money laundering***; “

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Various measures are required to be undertaken by NPOs to mitigate the ML/TF risks, in line with the FATF Recommendation and the international best practices, including the following;

- **Compliance with the conditions** prescribed in relation to the anti-money laundering and countering the financing of terrorism under the applicable laws;
- Maintenance of a **system of sound internal control** to ensure safeguarding of the company's charitable assets.
- Ensuring that donors, beneficiaries, promoters, members, directors, stakeholders, employees, volunteers or other people associated with the company or its associated company are not listed as a **designated individual or entity** which is subject to targeted financial sanctions;
- Ensuring that the promoters, members, directors and chief executive comply with the **fit and proper criteria** which, inter-alia, requires that:
 - none of such persons shall be associated with any money laundering or terrorist financing activities, illegal banking business, illegal deposit taking or financial dealings, and
 - understand the company's unique risks including the money laundering and terrorism financing risks in the locations where the company operates;
- Maintaining **the register of donors and donations as well as the register of donees and beneficiaries of the funds disbursed**, etc., containing detailed information about the sources and usage of funds, particulars of donors and donees, purpose of donation, mode of payments, etc.
- Utilizing the income and any profits of the company solely to promote the **company's objectives** and no portion thereof would be distributed by way of profit to the members of the company or their close relatives.
- At the time of renewal of license, a **certification from the auditor** confirming that funds/donations have been received through proper banking channels.
- Providing clear **Credit Information Report** in respect of members/directors who shall not have any overdue amount from the banks and financial institutions;
- Providing **separate disclosures of local and foreign funds**, grants, contributions, etc. in the financial statements of such companies;
- Submitting a **monthly report to the Commission** in respect of amount received from local and foreign sources equivalent to or more than five million rupees;
- Specifying requirement of obtaining **security clearance in respect of foreign funding or foreign promoters, directors and CEO**.

Fundamental principles of Good Practices

To meet the above conditions and to comply with laws and regulation, an NPO must adhere to following fundamental principles of Good Practices.

- Implementation of AML/CFT policy duly approved by Board and ensure that policy be made public and reviewed regularly.
- Commitment from the top to establish and enforce the approved policy.
- Undertaking training of employees on AML/CFT issues, challenges, policies & procedures of the NPO and repercussions for acting against the national interest and breach of policies.

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- Establishing a system to regularly monitor list of proscribed individuals and organizations and taking immediate action to end the relationship including freezing up of any assets of that individuals and organizations under the control of NPO and to inform the relevant authorities.
- Refraining itself to indulge in political activities or surveys not related to their mandate.
- Identification of every board member and their screening against the NUSCR lists.
- Considering risk-based approach, may also consider arranging to have independent oversight or review of operational, financial, and AML/CFT risk.
- The purpose of seeking for donation should be clearly stated with the donation request letters or advertisements.
- Strict use of banking channels for receipts and spending of donations. Identity of depositors and withdrawers to be ensured, use of dedicated bank accounts of receipts and separate account of projects, having joint signatories to have better control etc.
- Generation and reporting of Suspicious Transaction Report (STRs) to Financial Monitoring Unit (FMU) if transaction appears unusual/suspicious irrespective of amount involved.
- Utilization of funds strictly in accordance with objects of the entity.
- Foreign funds received on any projects to be utilized strictly in accordance with the terms of MOU with EAD.
- Internal audit function to be established to help identify risk, improve, internal control and governance.

The above list is suggestive and not conclusive, and there may be other steps keeping in view the circumstances and area of operation of NPO. However, to key to all above is

- ❖ **Know Your Donors**
- ❖ **Know Your Beneficiaries/Partners**
- ❖ **Know Your Employees**

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