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U.S. House Committee on Financial Services Subcommittee on Terrorism and Illicit Finance
Hearing on: Managing Terrorism Financing Risk in Remittances and Money Transfers
July 18, 2017

Chairman Pearce, Ranking Member Perlmutter, Members of the Subcommittee:

I greatly appreciate the opportunity to testify before the Subcommittee on the critical and timely issue of managing terrorism risk in remittances and money transfers. I am testifying in my capacity as the Humanitarian Policy Lead for Oxfam America. As part of the global Oxfam confederation, we and our local partners work in more than 90 countries around the world to tackle the root causes of poverty and save lives in humanitarian crises. In order to be independent advocates for effective US foreign assistance and foreign policy, Oxfam America does not accept US government funding.

Oxfam first became concerned about the subject of today's hearing during the 2011-12 humanitarian emergency in Somalia. At the time, a large part of the country was experiencing a catastrophic famine that ultimately claimed the lives of approximately 258,000 people, most of them children under five years of age.[1] Oxfam was working with local partners to help Somalis, particularly women and children, access food, procure clean and safe water, and prevent disease. We also endeavored, as we do in each emergency, to raise the voices of the most vulnerable. In this instance, vulnerable Somalis told us that, more than any other operational or policy issue affecting them, the most important threat to their lives was the possibility of a disruption in remittance flows from the United States to Somalia. Oxfam took their concerns very seriously. With partner agencies, we subsequently published two reports on remittances to Somalia[2] and an additional study on the broader, global phenomenon of banks' exiting or limiting relationships with MTOs among other types of bank customers.[3]

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[1] "Mortality among populations of southern and central Somalia affected by severe food insecurity and famine during 2010-2012." May, 2013; Food and Agriculture Organization and the Famine Early Warning Systems Network (FEWS NET), available online at http://www.fsnau.org/downloads/Somalia_Mortality_Estimates_Final_Report_8May2013_upload.pdf.

[2] See Orozco, Manuel and Yansura, Julia. "Keeping the Lifeline Open: Remittances and Markets in Somalia." July, 2013; Oxfam and Adeso, available at https://www.oxfamamerica.org/static/media/files/somalia-remittance-report-web.pdf; "Hanging By

Both financial exclusion and terrorism stand in the way of achieving Oxfam's vision of a world without poverty where all people are able to enjoy the full range of their human rights. In many places where we work, remittances represent a community's collective effort toward a better life, as well as its only firewall against destitution. We also see terrorist groups trap many of those same communities in poverty, insecurity, and horrific cycles of violence. In my travels through Somalia, Yemen, El Salvador, and Nigeria, I have seen firsthand the dreadful effects of indiscriminate violence and attacks on civilians. Any coherent, principled, prudent, and compassionate approach to the financial sector must aim to both enable *bona fide* remittances and reduce financing for extremist violence.

In my view, a strategy that aims to maximize remittances, keep them within the formal financial system, and curb illicit financial flows will achieve the twin aims of poverty alleviation and combating the financing of terrorism. To do this, remittance services must be accessible, affordable, and accountable – both to law enforcement authorities and to the families sending and receiving money.

Remittances Fight Poverty and Aid Humanitarian Response

In 2016, migrants sent $575 billion in remittances to their countries of origin, including $429 billion to developing countries.[4] In the world's poorest countries, remittances are particularly crucial. At the household level, remittances may be used to put children through school, pay rent, access medical treatments, or as start-up costs for a business. Remittances received by women and in woman-headed households have been shown to increase women's economic empowerment and investment in social capital.[5] At the national level, particularly in low-income countries, remittances are often drivers of the economy. Remittances accounted for more than 10 per cent of GDP in at least 28 countries and more than 20 per cent in at least nine of them.[6]

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a Thread: The Ongoing Threat to Somalia's Remittance Lifeline." February, 2015; Oxfam, Adeso, & Global Center on Cooperative Security, available at https://www.oxfam.org/en/research/somalia-remittances-hanging-by-thread.

[3] Shetret, Liat and Durner, Tracey. "Understanding Bank De-Risking and Its Effects on Financial Inclusion." November, 2015; Oxfam & Global Center on Cooperative Security, available at https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/rr-bank-de-risking-181115-en_0.pdf.

[4] "Migration and Development Brief 27," April, 2017; World Bank, available at http://pubdocs.worldbank.org/en/992371492706371662/MigrationandDevelopmentBrief27.pdf.

[5] "Gender, Migration and Remittances," International Organization for Migration (IOM), available at https://www.iom.int/sites/default/files/about-iom/Gender-migration-remittances-infosheet.pdf.

[6] See "Migration and Remittances Data as of October 2015," World Bank, in "Report to the G20 on Actions Taken to Assess and Address the Decline in Correspondent Banking," note 1;

Remittances play a particularly crucial role in humanitarian emergencies, especially when state institutions and the private sector have collapsed. In Somalia and Yemen – two countries that face the threat of famine in the midst of complex humanitarian emergencies – remittances have been a relatively stable financial inflow. In Yemen, businesses have been decimated by fighting and a *de facto* blockade on the country's Red Sea ports, and public sector salaries on which a quarter of all Yemenis depend have not been paid for nearly a year.[7] In Somalia, government-provided social services are nearly nonexistent, and 26 years of civil war have undermined essentially all domestic industry other than subsistence farming, herding, and fishing, which themselves have been threatened by climate change and illegal, unreported and unregulated (IUU) fishing. In both countries – as well as for the surrounding region – money transfers from migrants abroad have been a stabilizing force. They have been more consistent than aid, investment, or social welfare programs. In Somalia, famine would have been declared long ago if not for money from the diaspora. At every phase of an emergency – the pre-crisis phase, the crisis phase, and the recovery phase – remittances help families and communities survive. They build resilience to crises, help communities weather the storm, and then help them build back better.[8]

Remittances are transmitted in a variety of ways – through banks, fintech enterprises, cash couriers, trust-based networks – known primarily in the United States by their Arabic name, *hawalas* – and non-bank money transfer operators (MTOs). MTOs are often the only remittance option for many poor migrants and their families who have no other point of access to the formal financial sector. MTOs themselves typically rely on banks to provide financial services, such as check collection, deposit services, payroll services, and most critically, wire transfers, as well as for their typically more robust anti-money laundering/combating the financing of terrorism (AML/CFT) information technology infrastructure. MTOs rely on cross-border wires in order to settle its accounts. If an MTO is unable to access this service in a country where it sends or receives money, it will be forced to identify another way to move money in or out of the jurisdiction, and otherwise may shut down its operations there.

Banks are Closing MTO Accounts

November, 2015; Financial Stability Board, available at http://www.fsb.org/wp-content/uploads/Correspondent-banking-report-to-G20-Summit.pdf.

[7] For more information on remittances and Yemen's financial sector in the context of its current humanitarian crisis, see Salisbury, Peter. "Bickering While Yemen Burns: Poverty, War, and Political Indifference." June, 2017; Arab Gulf States Institute in Washington, available at http://www.agsiw.org/wp-content/uploads/2017/06/Salisbury_Yemen_ONLINE.pdf.

[8] Savage, Kevin and Harvey, Paul. "Remittances during crises: implications for humanitarian response." May, 2007; Overseas Development Institute, available at https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/317.pdf.

Unfortunately, MTOs are one of a number of types of customers losing access to banking services, both in the United States and globally. A 2015 World Bank study that interviewed representatives of governments, MTOs, and banks in G20 countries reported that 46 per cent of MTO respondents had experienced bank account closures.[9] 28 per cent reported that they could no longer access banking services, with a staggering 45 per cent reporting that some of their agents were unable to use banks.[10] Neither banks nor MTOs interviewed for the study cited money laundering or terrorist financing-related violations or sanctions as one of the top five reasons for account closures. In short, MTOs are losing their bank accounts despite being viewed as law-abiding customers.

MTOs are not alone. MTOs are just one of a number of segments of the banking customer base losing financial services without regard to their AML/CFT compliance records. Other segments of the customer base include nonprofit organizations, respondent banks, foreign embassies and diplomatic missions, fintech enterprises, payday lenders, and other merchant categories viewed as high-risk.[11] The most widely used term for these practices is "bank de-risking," which former U.S. Under Secretary of the Treasury Adam Szubin defined as, "instances in which a financial institution seeks to avoid perceived regulatory risk by indiscriminately terminating, restricting, or denying services to broad classes of clients, without case-by-case analysis or consideration of mitigation options."[12] I prefer not to use this term, for two reasons. First, the term "de-risking" masks the fact that pushing law abiding customers out of the formal financial system actually increases, rather than decreases, money laundering/terrorist financing (ML/TF) risk. Second, "de-risking," as defined by Mr. Szubin and others, is concerned only with the indiscriminate denial of services to broad classes of clients. We should be equally concerned when any financial flow is forced to the margins of formal banking system, even if it is the result of careful, case-by-case analysis by each bank. Instead, I will discuss these practices as a decline in access to financial services.

All of the customer types experiencing this decline in access have a trait in common: they are all viewed widely in the financial sector as inherently "high-risk." It is important to note in this context that the level of risk associated with a customer does not describe the likelihood that

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[9] "Report on the G20 Survey on De-Risking Activities in the Remittance Market." October, 2015; World Bank, available at http://documents.worldbank.org/curated/en/679881467993185572/pdf/101071-WP-PUBLIC-GPFI-DWG-Remittances-De-risking-Report-2015-Final-2.pdf.

[10] *Ibid*.

[11] Shetret and Durner.

[12] "Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference," November, 2015, available at https://www.treasury.gov/press-center/press-releases/Pages/jl0275.aspx.

the customer will violate the law. Rather, it connotes the likelihood of the customer's being exploited for the purposes of terrorist financing, money laundering, or other financial crimes. Even the most stringent AML/CFT controls may not save a customer from being perceived or rated as high-risk, depending on the nature of its business, the jurisdictions in which it operates, or other factors.

The decline in financial access for customers perceived as high-risk appears to stem from the less tolerant political environment in which banks have operated following the 9/11 terrorist attacks and the 2008 financial crisis. We see this in number of ways, including:

- High fines for Bank Secrecy Act (BSA) noncompliance, particularly related to AML/CFT failings;

- Reputational risk for association with AML/CFT failings;

- Higher capital requirements and liquidity thresholds;

- Compliance costs related to BSA compliance;

- Shift from corporate to individual liability, including criminal liability;

- Risk of private civil litigation related to AML/CFT failings; and

- Pressure from bank examiners related to the maintenance of high-risk accounts, particularly in the wake of the 2008 financial crisis.

These factors have combined to dramatically reduce banks' risk appetites.[13] Consequently, banks are deciding that it is easier and more profitable to avoid any risk associated with customers like MTOs than to manage that risk.

There is little agreement over the relative importance of each of these factors, but from my experience and conversations with bank representatives, banks of different sizes have different rationales. Large banks tend to be more concerned with reputational risk, but at the same time more willing to maintain relationships with large MTOs. The UK legal dispute between Barclays Bank and Dahabshiil, a Somali MTO, provides fascinating insight into the decision-making

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[13] See Shetret and Durner. See also "Unintended Consequences of Anti-Money Laundering Policies for Poor Countries," November, 2015; Center for Global Development, available at https://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf.

process on account retention of one large bank. The judgment publishes the "Minimum Standards" used by Barclays for MTOs customers, which include a minimum revenue requirement and a high net tangible assets requirement.[14] In other words, Barclays had decided that no small MTO could be account-worthy, no matter how strong its AML/CFT compliance program.

On the other hand, small banks appear to withdraw accounts immediately following examinations. On occasion, banks have told me that examiners explicitly discourage banking MTO customers. More commonly, I hear examiners appropriately asking to see details and asking probing questions about MTO accounts at the beginning of examinations, which simply makes examiners nervous about maintaining these accounts. It is possible that many small banks simply do not have the capacity to conduct effective due diligence on complex MTO customers, but the likely alternative – pushing the compliant MTO and its remittance flows out of the banking sector altogether – seems much worse.

Pressures on Correspondent Banking Are Compounding and Globalizing the Challenges to MTO Financial Access

As I mentioned earlier, correspondent banks are one of the types of customers viewed as high-risk that are experiencing rapid account closures.[15] Foreign banks in particular rely on correspondent banking to access the US financial system and currency. For many, losing the ability to conduct transactions in US dollars is a death sentence.

Like MTOs, correspondent banks have been targeted as vulnerable to money laundering and terrorist financing (ML/TF) abuse.[16] And as with MTOs, banks are deciding that the costs and consequences of managing these interbank relationships outweigh the benefits (one representative of a large bank told me that the cost of onboarding a new respondent customer exceeded $60,000). Like MTOs, however, not all correspondent bank accounts are equal when it comes to account maintenance and retention. Large banks with lower risk profiles are viewed as more attractive customers than small banks with higher risk profiles. In 2015, the World Bank

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[14] Dahabshiil Transfer Services Ltd vs. Barclays Bank Plc, judgment of Henderson, J. [2013] EWHC 3379 (Ch), Available at http://www.bailii.org/ew/cases/EWHC/Ch/2013/3379.html.

[15] Correspondent banks provide services for and on behalf of other banks, often to provide access to different jurisdictions. Those services include foreign exchange, wire transfers, business transactions, and settlement of accounts.

[16] See, e.g., "Money Laundering: A Banker's Guide to Avoiding Problems," December, 2002; Office of the Comptroller of the Currency (OCC), available at https://www.occ.gov/topics/bank-operations/financial-crime/money-laundering/money-laundering-2002.pdf.

concluded that roughly half of the emerging market and developing economy jurisdictions surveyed have experienced a decline in correspondent banking systems.[17]

For customers that depend on banking services in both wealthy and developing countries alike – including MTOs and charities such as Oxfam – this decline compounds the financial access problem in two ways. First, fewer interbank connections means more difficulty routing cross-border transactions, particularly to high-risk jurisdictions. Second, banks are desperate to make themselves more attractive customers for larger correspondent banks. This is especially true for foreign banks looking to maintain correspondent relationships with US financial institutions, which are insisting that their respondent banks reduce their risk profiles. Cutting MTO accounts, appears to be an easy way to do that, at least superficially.

The impacts of MTO account closures on remittances are unclear

It is certain that MTOs are experiencing bank account closures at an alarming rate. What is less clear is what effect this is having on actual remittance flows – the extent to which they are declining or moving outside of the formal financial system.

The evidence is mixed. Here's what we do know:

- An investigation into MTO bank account closures in Australia showed that the account closures had forced a number of MTOs to go out of business, but also showed that overall financial outflows from Australia remained constant.[18]

- Global remittances declined in 2016 from an all-time high of 2015, the first decline since the 2008 financial crisis, despite predictions that they would continue to increase.[19]

- In a number of instances, governments have raised concern at the highest levels about the impacts of bank account closures on remittance flows, particularly in the Caribbean region.[20]

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[17] "Report to the G20 on Actions Taken to Assess and Address the Decline in Correspondent Banking."
[18] "Bank De-Risking of Remittances Businesses," November, 2015; AUSTRAC, available at http://www.austrac.gov.au/bank-de-risking-remittance-businesses.
[19] "Migration and Development Brief 27."
[20] Torbati, Yeganeh. "Caribbean Countries Caught in U.S. Crackdown on Illicit Money." 12 July 2016; Reuters, available at http://www.reuters.com/investigates/special-report/usa-banking-caribbean/; The Hon. Audley Shaw CD, MP. Presentation at 2016 IMF/World Bank Annual Meetings, available at

- Even in the absence of more convincing evidence that remittance flows are declining or going underground, the World Bank MTO study shows that MTOs are coping with account closures by employing other MTOs' bank accounts, cash couriers, or personal bank accounts.[21] This means higher costs and less transparency in money flows.

Remittances to Somalia: a case for more aggressive intervention

As I mentioned at the beginning of my testimony, I first became aware of these problems following an outcry from our partners in Somalia during the last famine in 2011-12. Somalia presents a unique case:

- Somalia is one of the most remittance-dependent countries in the world, with money from the diaspora comprising roughly a third of its entire economy. At more than $1.3 billion annually, the flow of remittances to Somalia is greater than the humanitarian aid, development assistance, and foreign direct investment it receives – combined.[22]

- Most of this money helps people meet their most basic needs, such as food, shelter, school fees, and basic medical expenses.[23]

- Most international banks and MTOs that are well-known in the US are almost entirely absent from Somalia. The only realistic channel through which to send money to Somalia are a set of Somali-owned MTOs offering low fees and an impressive ability to deliver throughout the country.[24]

- With the internationally designated terrorist group al-Shabaab present throughout much of South and Central Somalia and only the most nascent oversight of the financial sector, Somalia is viewed as an extremely high-risk destination for cross-border transactions.

One Somali-American I interviewed two years ago told me: "Without the money we're sending them, I don't think the Somali nation would exist." Another confessed to me tearfully that the thought of not being able to send money to his sick mother for food and medicine made him consider going back to face drought and conflict. "I can't even eat thinking about it," he told me.

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http://www.mof.gov.jm/downloads/speeches/presentations/2016_annual_meetings_small_states_form_speech.pdf.

[21] "Report on the G20 Survey on De-Risking Activities in the Remittance Market."

[22] Orozco and Yansura.

[23] *Ibid.*

[24] *Ibid.*

Many people have expressed a concern that they were being targeted by the U.S. government because of their nationality or religion.[25]

Somali MTOs operating in the United States are registered with the Financial Crimes Enforcement Network (FinCEN) and are regularly examined by state authorities and the Internal Revenue Service. I am not aware of any Somali MTO that has been subject to civil or criminal penalties. I am aware of a number of instances in which Somali MTOs have provided information that has been used in the prosecution of individuals accused of sending money to al Shabaab. I should note here that in Somali, these companies are known as *hawalas*, which simply means money transfer. In English, *hawala* is used to designate money value transfer systems as informal and unregulated. For that reason, Somali MTO professionals forcefully reject this label.

No large bank has agreed to a relationship with a Somali MTO in at least six years. In response to community pressure, one large bank publicly announced in 2014 that it was considering opening an account for the largest Somali MTO. This MTO told me that the bank requested two costly audits and then declined to provide an account.

Small banks, for one reason or another, have almost all closed their Somali MTO accounts over the past five years. In official communications, they simply said they had decided to exit the relationships without providing any reasons,[26] but Oxfam and the MTOs opened lines of communication with a number of them following the account closures. One community development bank said it was concerned about criminal liability. A few banks claimed that recent examinations demonstrated to them that they did not have the capacity to conduct due diligence over the accounts. The last bank serving many of the MTOs, a bank that holds itself out as a specialist bank for MTO and other money service business customers, felt unable to maintaining the accounts while operating under a Consent Agreement with the U.S. Office of the Comptroller of the Currency.

The effect of these account closures is difficult to ascertain without better evidence. One survey conducted by the Food Security, Nutrition, and Analysis Unit (FSNAU) of the World Food Programme found that in the period following Somali MTOs' last major bank account closure, 35 per cent of urban Somalis outside the capital of Mogadishu reported receiving less money than before.[27] It is difficult to draw other strong conclusions from the survey due to its methodology

[25] *Ibid.*
[26] *Ibid*.
[27] "Assessment of External Remittances in Selected Urban Areas and Among Displaced Populations Across Somalia," September, 2015; FSNAU, available at http://www.fsnau.org/downloads/FSNAU-Assessment-of-Remittance-Flows-in-Selected-Urban-Areas-of-Somalia-October-2015.pdf.

and coincidental timing with other disruptions, but in my opinion, it indicates a connection between bank account closures and a decline in life-saving income for many Somali households. The consultations I have done with communities in Somalia and in Somali diaspora communities in the United States support that conclusion.

Somalia's banking system, financial oversight, and mobile-based remittance systems are all developing, but it will take years before we know whether these will give rise to a reliable remittance system and a stable economy in Somalia. Today, as parts of Somalia teeter on the verge of famine and al-Shabaab continues to assert itself throughout South-Central Somalia, remittances from the United States to Somalia remain on the precipice of a serious disruption. With many Somali MTOs remaining unbanked, some have resorted to carrying cash abroad to settle accounts – a legal option that has the blessing of the Treasury Department, but one that puts people and funds in great jeopardy.[28] In 2017, I'm convinced we can come up with options preferable to suitcases full of cash when it comes to our national security and the Somali people's lifeline.

Our goal is a fully inclusive and transparent financial system

We're witnessing a market failure in the financial sector today. In a perfectly functioning market, some banks would be providing service to MTOs, correspondent banks, nonprofit organizations, and others that are associated with high risk and low revenue potential. Those banks would be conducting better due diligence and potentially charging higher fees for MTOs and be in regular dialogue with MTOs on improving their AML/CFT controls. The reduced profit margins and additional costs passed on to individuals sending money aren't ideal, but they're preferable to the alternative that we're watching unfold. Market, regulatory, and political incentives are pushing banks to drop MTOs altogether, especially small MTOs specializing in money transfers to high-risk jurisdictions. If these MTOs aren't banked, we're not only likely to see a decline in remittances, but also an increase in the share of remittances being transmitted though informal networks – where law enforcement officials, regulators, and money senders can't trace it. That means less money in the hands of people looking to escape poverty and more opportunity for designated terrorists and other financial criminals to transact business.

A better approach would be to affirmatively encourage access to financial services for all regulated MTOs, including those at the high-risk end of the market. Government should be the first mover. In that regard, I would like to offer a few recommendations to the Committee.

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[28] Trindle, Jamila. "Money Keeps Moving Toward Somalia, Sometimes in Suitcases." 15 May 2015, *Foreign Policy*. Available at http://foreignpolicy.com/2015/05/15/money-keeps-moving-toward-somalia-sometimes-in-suitcases.

Recommendations

1. **Get more and better data**. The GAO is currently undertaking four interrelated studies related to this issue which should make an important contribution to our understanding of the topic. I would encourage the Committee to more regularly request information on remittance outflows from the United States and, to the extent practicable, to follow up on these information requests to determine the causes and consequences of any disruptions.
2. **Urge the Treasury and State Departments to increase technical assistance for improved financial controls in high-risk countries**. Both Treasury and State have initiated this process with the Government of Somalia. Similar processes should be replicated and supported where there is an interested government partner whose weak financial governance contributes to its perception by banks as a high-risk jurisdiction.
3. **Request input from government agencies and offices concerned with financial inclusion**. As concerns terrorist financing, Treasury's Office of Terrorist Financing and Financial Crime (TFFC) and the federal banking agencies tend to play the leading roles in policymaking. Officials in these agencies have done an incredible job in recent years reaching out to and soliciting input from interested parties over the past few years. Still, I believe that officials at the State Department, USAID, and officials at Treasury more focused on financial inclusion should have a stronger role in the policymaking process and informing public debate around these issues.
4. **When there is a strong public interest, support public-private partnerships to maintain money flows at the periphery of the banking system**. These could take many forms. As an example, Section 271 of the Countering Iran's Destabilizing Activities Act, currently under consideration in by the House of Representatives would require a feasibility study to determine whether the Treasury Department could assist private banks or credit unions wishing to facilitate remittances to Somalia. Another approach would be for the Federal Reserve Banks to utilize Fedwire to transmit funds on behalf of certain unbanked customers. I don't advocate these options in all cases, but in circumstances such as Somalia's remittance corridor, or for unbanked organizations delivering life-saving assistance in Syria, these options are worthy of consideration.