To: Office of Terrorist Financing and Financial Crime  
U.S. Department of the Treasury  

From: ABA Section of Taxation and Criminal Justice Section  

Date: April 5, 2006  

Re: Anti-Terrorist Financing Guidelines  

Enclosed are comments under the U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices of U.S.-Based Charities. These comments represent the views of the American Bar Association Section of Taxation and Criminal Justice Section. They have not been approved by the Board of Governors or the House of Delegates of the American Bar Association and should not be construed as representing the policy of the American Bar Association.

Enclosure  

cc: Chip Poncy, Director of Strategic Policy, Terrorist Financing & Financial Crimes  
U.S. Department of the Treasury  
Eric Solomon, Acting Deputy Assistant Secretary (Tax Policy),  
U.S. Department of the Treasury  
Michael J. Desmond, Tax Legislative Counsel, U.S. Department of the Treasury  
Eric San Juan, Attorney Advisor, U.S. Department of the Treasury  
Andrea Keller, Policy Advisor, U.S. Department of the Treasury  
Steve Miller, Commissioner, TE/GE, Internal Revenue Service  
Lois Lerner, Director, Exempt Organizations, Internal Revenue Service  
Donald L. Korb, Chief Counsel, Internal Revenue Service  

COMMENTS ON U.S. DEPARTMENT OF THE TREASURY
ANTI-TERRORIST FINANCING GUIDELINES: VOLUNTARY
BEST PRACTICES FOR U.S.-BASED CHARITIES

These comments (“Comments”) on the U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities (the “revised Guidelines”) are submitted on behalf of the American Bar Association Section of Taxation and Criminal Justice Section and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Betsy Buchalter Adler, Victoria B. Bjorklund, Lisa L. Johnsen, Jennifer I. Reynoso, and LaVerne Woods, Chair of the Section of Taxation’s Committee on Exempt Organizations. The Comments were reviewed on behalf of the Section of Taxation by Carolyn M. Osteen for the Section of Taxation’s Committee on Government Submissions, and by Richard S. Gallagher, Council Director for the Section of Taxation’s Committee on Exempt Organizations.

Although the individuals who participated in preparing these Comments have clients who would be affected by the revised Guidelines or have advised clients on the application of the revised Guidelines, no such participant (or the firm or organization to which such participant belongs) has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

Contact person: LaVerne Woods

Phone: 206.628.7792

Email: lavernewoods@dwt.com

Date: March 8, 2006
EXECUTIVE SUMMARY

This submission responds to the Department of the Treasury’s request for comments to the revised Guidelines. While we commend the Department of the Treasury (“Treasury”) for adopting the risk-based approach that the Section of Taxation (the “Tax Section”) recommended in its prior comments to the Internal Revenue Service (the “IRS”) in response to IRS Announcement 2003-29, 2003-20 I.R.B. 928 (May 19, 2003), we suggest that Treasury withdraw the revised Guidelines and endorse in their place the Principles of International Charity (the “Principles”). Our position is based on three principal concerns: first, that the revised Guidelines contain provisions suggesting that charitable organizations are agents of the government; second, that the revised Guidelines suggest the collection of more information on more individuals and organizations than did the initial Guidelines, and are unduly burdensome; and third, that the revised Guidelines do much more than address their stated purpose, that is, to offer guidance to charities that might be helpful in achieving compliance with sanctions administered by the Office of Foreign Assets Control (“OFAC”). Because we recognize that Treasury may decline to withdraw the revised Guidelines, we also offer suggested changes.

BACKGROUND AND OVERVIEW

In November 2002, the U.S. Department of the Treasury issued its “Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities” (the “initial Guidelines”) addressing how charities could reduce the risk that charitable funds would be diverted to terrorist purposes. Comments on the initial Guidelines were included in comments the Tax Section submitted to the IRS in response to Announcement 2003-29, in which the Service requested comments on how it might clarify requirements that Section 501(c)(3) organizations must meet with respect to international grantmaking and other international activities and on how additional guidance might reduce the possibility of diversion of assets for non-charitable purposes while preserving the important role of charitable organizations worldwide.

In response to various comments, in April 2004, Treasury invited organizations that commented on the initial Guidelines to participate in a charities forum to permit charities and Treasury to discuss the terrorist financing issue. The groups participated in the forum, but declined the offer to work directly with Treasury to develop guidance for the charitable sector because they believed that an independent process would be more consistent with their non-governmental character. As a result, these organizations convened a working group to draft an effective alternative to the initial Guidelines and invited participation by all interested parties. The product of the group’s deliberations, the “Principles of International Charity,” which was released in March 2005, describes the fundamental principles that guide the international

---

1 The revised Guidelines are available on the Treasury Department’s website at http://www.treas.gov/offices/enforcement/key-issues/protecting/charities-intro.shtml.
2 The Section’s prior comments are available on the ABA’s website at http://www.abanet.org/tax/pubpolicy/2003/030714exo.pdf.
charitable work of experienced U.S. organizations as they ensure that charitable assets will be used for their intended purposes and not diverted to terrorist or other non-charitable uses.

The Principles reflect a range of due diligence procedures that have proven effective in minimizing the risk of diversion of charitable assets and mitigating the real security threat facing many of those delivering charitable assistance without discouraging international charitable activities by U.S. organizations. Treasury issued a revised version of the Guidelines on December 2, 2005.

Throughout its communications with concerned charities, Treasury has emphasized that the Guidelines are intended to assist charities attempting to protect themselves from terrorist abuse, a statement that is echoed in the introduction to the revised Guidelines. After reviewing the revised Guidelines, however, we have concluded that the revised Guidelines suggest procedures that are unnecessarily burdensome and potentially harmful to charities. Furthermore, they do so without providing any protection that is not already present under the laws and practices that are currently followed by those organizations for which the Guidelines were drafted, that is—according to the revised Guidelines—those “charities that attempt in good faith to protect themselves from terrorist abuse.” Accordingly, we recommend that Treasury withdraw the Guidelines and endorse the Principles of International Charity in their place. Because we recognize that Treasury may decline to do so, we also offer suggested changes to the revised Guidelines.

We note that on February 1, 2006, the Council on Foundations, on behalf of the Treasury Guidelines Working Group, sent detailed comments on the revised Guidelines to the Department of the Treasury. Portions of these Comments are substantially similar to the comments of the Treasury Guidelines Working Group.

**COMMENTS**

We have three key concerns about the revised Guidelines that prompt our recommendation for withdrawal:

First, the revised Guidelines contain provisions that suggest that charitable organizations are agents of or are closely tied to the U.S. government, thereby potentially compromising the safety of humanitarian workers who may be targeted as a result of their perceived lack of independence from the government.

Second, the revised Guidelines suggest the collection of more information on more individuals and organizations than did the initial Guidelines, notwithstanding that, as we stated in our comments on the initial Guidelines, the information collection suggestions in the initial Guidelines were well beyond the capacity of most charitable organizations.

Third, we are concerned that the revised Guidelines do much more than offer guidance to charities that might be helpful in achieving compliance with sanctions administered by OFAC. While the revised Guidelines include procedures that are clearly related to the credibility of recipients of charitable assets and the ability to trace charitable funds, they also address issues already covered by state or federal laws or highly developed practices widely accepted in the charitable sector. The fact that Treasury opines on those issues in a document
that also explains that violations of related laws involve substantial civil and criminal penalties may afford those opinions more influence than they are appropriately due. Thus, we are concerned that the revised Guidelines could evolve into de facto legal requirements through incorporation into other federal programs, despite the inclusion of the word “voluntary” in the title. Mandatory compliance with the revised Guidelines is inconsistent with the risk-based approach to preventing the diversion of funds advocated in the revised Guidelines themselves.

Recognizing that Treasury may decide not to follow our principal recommendation, we provide the following comments on specific aspects of the Guidelines.

**Title:** U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities

We believe that the title, “U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices For U.S.-Based Charities,” misstates both the content and the purpose of the Guidelines. First, it is not accurate to present the Guidelines as a compilation of the charitable sector’s “best practices.” Given the diversity of the charitable sector, there is simply no one set of “best practices” that applies to all organizations. Second, despite the continued use of the term “voluntary” in the title, the revised Guidelines seem to be more than suggestions, in large part because they have been issued by a federal agency with regulatory authority over tax-exempt organizations. We are concerned that other government agencies will adopt the suggestions included in the Voluntary Guidelines as requirements because Treasury has indicated that these are, in fact, best practices. The Guidelines have already been incorporated into at least one federal program. In commentary accompanying the regulations effective for the 2006 Combined Federal Campaign (the “CFC”), the Office of Personnel Management stated that participants in the CFC "as a minimum, should follow the "Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities." Further, we are aware that IRS agents -- both in the context of audits and applications for exemption -- have asked organizations if they are complying with the Guidelines. Thus, even though no statutory authority prescribes the issuance of the Guidelines, the incorporation of the Guidelines into other federal programs may confer on them de facto legal authority. If the revised Guidelines are not withdrawn, we suggest that the “best practices” phrase should be deleted and the title should be changed to reflect the intended purpose, to a title such as “Suggestions for Complying with Anti-Terrorist Financing Laws.”

**Introduction:** The Introduction to the revised Guidelines states:

Investigations have revealed terrorist abuse of charitable organizations, both in the United States and worldwide, often through the diversion of donations intended for humanitarian purposes but funneled instead to terrorists, their support networks, and their operations. This abuse threatens to undermine donor confidence and jeopardizes the integrity of the charitable sector, whose services are indispensable to both national and world communities.

The Introduction makes broad statements regarding the extent of diversion of charitable assets to terrorist purposes. We recognize that some charitable funds may have been intentionally raised or diverted to support terrorist activities, but we are concerned that sweeping
statements misrepresent the prevalence of terrorist abuse of the U.S. charitable organizations that are the intended audience for the revised Guidelines. We believe that charities acting in good faith to protect their charitable assets from diversion would be better served by the presentation of data on diversion. Consequently, we believe that Treasury should instead describe how many individuals and organizations have been designated terrorist entities or supporters, how much money has been frozen worldwide and how much of that has been in the U.S, and how many U.S. charities have lost their tax exemption as a result of terrorist activities. We believe the substitution of data for broad statements will have two positive effects: (1) it will not undermine donor confidence (which is a possible outcome of the revised Guidelines’ sweeping statements); and (2) it will educate charitable organizations about the threat and realities of terrorist use of charitable assets, particularly as the crux of the concern appears to be the gravity of the terrorist use, rather than the prevalence or dollar amount of such diversions.

We also believe that the Introduction to the Guidelines should include a statement that compliance with the Guidelines is not legally required. The fact that government agencies are directing charitable organizations to comply with the Guidelines demonstrates the real need for such a clear statement. By releasing the revised Guidelines, Treasury may accomplish by the mere power of its suggestion what Congress has not explicitly asked it to do – make rules governing the administration of charitable organizations. This approach is inappropriate and inconsistent with Treasury’s stated intent to protect and assist charities. Based upon our experience, many of the procedures included in the revised Guidelines, while well intentioned, are overly burdensome and the guidance included therein is unrelated to the threat of diversion of assets. Yet, if government agencies continue to incorporate the Guidelines into their operating procedures, they will become mandatory for charitable organizations. Based on the response to the initial Guidelines, which were published only in an attachment to a press release, we believe that the publication of the revised Guidelines in the Federal Register may give government agencies even greater cause to defer to the Guidelines, even though they continue to be labeled “voluntary.” A number of the mandatory statutory and regulatory provisions in federal tax law governing charities incorporate a “reasonable” or “prudent” behavioral standard. Failure of an organization to adhere to a “best practice” promulgated by the federal government when the operative regulatory standard is that of “reasonable” or “prudent” behavior suggests that the Guidelines may have real, immediate legal import and may not be “voluntary” in all circumstances absent a specific disclaimer that the Guidelines have no relationship to reasonable or prudent behavior as the concept is incorporated into federal tax law.

We believe that footnote 1 should explain to both the charitable sector and federal and state agencies that the Guidelines are not enforceable under the law, have no bearing on reasonable or prudent behavior as the concept is incorporated into federal tax law, and -- just as compliance with the Guidelines does not constitute a defense in event of a violation of law -- failure to comply with any particular provision of the Guidelines will not result in legal sanctions.

**Reporting and other provisions:**

The revised Guidelines tend to blur the critical separation between the U.S. government and the charitable sector.
Independence from governments is a basic principle of humanitarian action by the charitable sector. We are concerned that the revised Guidelines add provisions that could be interpreted as linking charitable organizations more closely to the U.S. government, potentially undermining the trust between U.S. charities and foreign recipients. In addition, such perceived links could be exploited by persons hostile to U.S. charities. The press release accompanying the revised Guidelines could lead a reasonable reader to question the independence of U.S. charities by stating that “. . . the Treasury has worked hand-in-hand with the U.S. charitable and donor community . . .” (emphasis added). Moreover, the revised Guidelines include new reporting provisions stating that charities should report findings of individuals “suspected of activity relating to terrorism” to OFAC and/or the FBI. These reporting provisions are coupled with enhanced information collection procedures, including: (1) vetting of the charitable organization’s own key employees, (2) collecting information on each place of business of the organization (rather than just the principal place of business), and (3) identifying branches, in addition to subsidiaries and affiliates, that receive resources and services from the charity.

Reports of attacks on charitable aid workers have become alarmingly commonplace. The president of the International Federation of the Red Cross and Red Crescent Societies, Juan Manuel Suarez del Toro, connects “the growing politicization of humanitarian aid and the erosion of respect for our independent and impartial work, with the corollary of increasingly frequent attacks on our staff”. Based upon the genuine fear that the revised Guidelines will exacerbate the real threat to humanitarian workers, we believe that Treasury should remove provisions that blur the line between charitable organizations and the government.

**Governance, Financial Practice/Accountability, and Disclosure/Transparency in Finances and Governance:**

The revised Guidelines include three separate sections on governance, financial practice/accountability, and disclosure/transparency in finances and governance. The Governance section generally fails to take into account the complexity of its various recommendations because these deceptively complicated issues fall outside the core experience and expertise of Treasury. Section III.B. illustrates this problem. It recommends that the governing body of a charity should consist of at least three members, without making any appropriate exceptions. This recommendation goes well beyond any existing requirements of federal tax law and could present compliance difficulties for trusts and religious entities organized as “corporations sole.” It may also run directly counter to state law governing nonprofit corporations and trusts. By comparison, when the Panel on the Nonprofit Sector made a similar recommendation in June, 2005, it included appropriate exceptions for houses of

---

worship and certain affiliated entities, as well as for existing organizations, such as organizations formed as a corporation sole or as trusts with fewer than three trustees.  

Because the Guidelines carry extraordinary weight, we believe that a provision advocating a three-member board without appropriate exceptions is ill-advised. Keeping in mind that the Guidelines are drafted for charities that in good faith are attempting to prevent diversion of charitable assets, we are confident that any organization that is diligent enough to consult the Guidelines will already have determined its appropriate board size and structure and will have done so by consulting guidance available from organizations and advisors with relevant expertise. 

More importantly, Section III.B.4 makes recommendations that infringe upon existing legal protections by stating that board records should be available for public disclosure and should immediately be made available for inspection by the appropriate regulatory/supervisory and law enforcement authorities. First, making records or all board decisions subject to public inspection represents a level of disclosure beyond that required by the current disclosure requirements in the Internal Revenue Code, the Freedom of Information Act, and state “government in the sunshine” laws. Second, the revised Guidelines added the recommendation that board records should immediately be made available for inspection by the appropriate regulatory/supervisory and law enforcement authorities. We find this suggestion especially troubling as it both treats U.S. charitable organizations as information providers to the government and overlooks the constitutional protections accorded charitable organizations. We doubt that Treasury intended to suggest that regulatory/supervisory and law enforcement authorities are entitled to inspect board records without complying with constitutional or other legal protections by obtaining a warrant or other appropriate authorization for that purpose. 

The remaining provisions in the sections on governance, financial practice/accountability, and disclosure/transparency in finances and governance generally are unnecessary because they describe a number of actions that are required of most grantmakers under applicable provisions of the federal tax laws. The specific provisions set forth in these sections are unnecessarily detailed and restrictive, and are unlikely to be more effective than general good operating practices in preventing the use of funds to support terrorism. Accordingly, we suggest that Treasury delete the provisions included in the governance section from the revised Guidelines entirely. We also suggest that Treasury combine the provisions included in the sections on financial practice/accountability, and disclosure/transparency in finances and governance into a single section entitled “Accountability,” which lists only the principles applicable to financial accountability that would be considered relevant to the Treasury in the event of an investigation concerning the alleged use of funds to support terrorism.

---

5 Panel on the Nonprofit Sector (convened by Independent Sector), *Strengthening Transparency, Governance, and Accountability of Charitable Organizations, a final report to Congress and the Nonprofit Sector*, June 2005, pp. 75-78.
Anti-Terrorist Financing Best Practices:

The “Anti-Terrorist Financing Best Practices” section includes three significant improvements over the corresponding section in the initial Guidelines: first, the list checking recommendation has been simplified and clarified; second, the provision recommending checking bank references has been deleted; and third, the Guidelines incorporate the risk-based approach to due diligence recommend by the Tax Section in its prior comments to the IRS. We commend Treasury for those changes.

However, there are additional changes to this section that will increase the burden on organizations to collect information that they are ill-equipped to pursue or analyze, hinder legitimate and needed service delivery, and inadvertently expose humanitarian workers to greater security risks. The revised Guidelines suggest the collection and retention of an even greater and more detailed quantity of information regarding all recipients of charitable funds and in-kind contributions, domestic and foreign, and even on the charitable organization’s own employees. Further, the revised Guidelines broaden the scope of information recommended for collection to information “reasonably available” (see, VI.A.3.) and “reasonably discoverable” (see, VI.A.6.). Compliance with the revised Guidelines’ recommendations for additional information collection may create the impression that the charity is collecting information on behalf of the U.S. government, which could impact the charity’s effectiveness and safety in many parts of the world. The section, in fact, recommends that the charity report to the OFAC or the FBI suspicious activity or valid or potentially valid matches should the charity engage in list-checking, confirming the doubts of any recipient that may find it problematic or even hazardous to receive charitable assistance from what it deems to be an arm of the U.S. government.

Three years of experience in attempting to follow certain provisions of the initial Guidelines has demonstrated that it is difficult for humanitarian workers in the field to make the inquiries suggested by the initial Guidelines. Moreover, the information collected appears to be of limited value in the effort to apply a risk-based approach to prevent the diversion of assets to terrorist purposes. Based on our clients’ experience collecting identifying information, we more firmly believe that identification of terrorist connections is properly the job of law enforcement, with its greater skill and intelligence resources.

In light of the increased information collection and new reporting recommendations, we do not believe it is appropriate to re-name the section “Anti-Terrorist Financing Best Practices.” In our judgment, this section contains a list of procedures that are difficult to administer, most of which are only remotely likely to produce any information helpful to the charity in determining whether there is a risk of diversion. Accordingly, we recommend that Treasury withdraw this section completely and endorse in its place the Principles of International Charity. Failing that, we urge Treasury to modify this section to balance more appropriately the value of information that could realistically be collected, given the limited investigatory powers of private citizens, against the resource constraints of charitable organizations.