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Investing in rural people

## Anti-Money Laundering and Countering the Financing of Terrorism Policy

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**For: Approval**

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## **Abbreviations and acronyms**

ACD	Accounting and Controller's Division
AML	anti-money laundering
CFT	countering the financing of terrorism
FATF	Financial Action Task Force
IFI	international financial institution
ML	money laundering
TF	terrorist financing

## Recommendation for approval

The Executive Board is invited to approve the IFAD Anti-Money Laundering and Countering the Financing of Terrorism Policy.

### I. Introduction

1. Over the past several years, the international community has become increasingly concerned about the growing problem of money laundering (ML) and terrorist financing (TF).
2. This concern arises from the fear that such activities could seriously jeopardize the integrity of national financial systems and hamper economic development. Combating ML and TF is a problem of global concern, requiring concerted and cooperative action on the part of a broad range of institutions.
3. Under the Agreement Establishing the International Fund for Agricultural Development, IFAD has a fiduciary responsibility to "make arrangements to ensure that the proceeds of any financing are used only for the purposes for which the financing was provided".
4. The Fund recognizes that combating ML and preventing TF are core components of its development mandate and fiduciary responsibility. The Fund is committed to promoting and adhering to the highest standards of probity and accountability in the use of its financing and will not tolerate the diversion of the resources entrusted to it by Member States, non-Member States and other sources through ML and TF.
5. The need for a policy addressing ML and TF was highlighted in a recent independent IFAD Financial Risk Assessment report prepared by Alvarez & Marsal, which states that a robust approach to conduct and financial crime risk – defined and managed for IFAD as a whole – is required to mitigate reputational harm.
6. The IFAD Anti-Money Laundering and Countering the Financing of Terrorism Policy is based on best practices of various development finance institutions (DFIs) and seeks to ensure that integrity risks are identified, assessed and adequately mitigated by taking the nature, scale and complexity of the Fund's activities into account. The benchmarking exercise presented in annex I demonstrates that in the category of screening and assessment, this Policy is significantly aligned with the African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD), the Inter-American Development Bank (IDB) and the European Investment Bank (EIB), and largely aligned with another five DFIs of the benchmarked institutions.
7. The intent of this Policy is to prevent the Fund's exposure to serious reputational risk, financial loss or legal liability that could give rise to challenges from Member States, international contributors, donors, and other key stakeholders. IFAD will endeavour to ensure that its funds and the funds it administers are not used to finance any illegal acts connected with ML and TF.
8. While this Policy does not apply to IFAD staff members ("staff") and other persons hired under a non-staff contract ("non-staff") in the performance of their official duties and in their private conduct, IFAD will enhance screening to include staff and non-staff, in line with the Human Resources Policy and Code of Conduct. Appropriate policies and procedures, including the provisions contained in the IFAD Human Resources Policy and Code of Conduct and its Policy on Preventing Fraud and Corruption in its Activities and Operations, regulate the conduct and behaviour of staff and non-staff and adherence to the highest ethical standards.
9. This Policy takes effect on the date of its approval. Following approval of the Policy, internal due diligence procedures will be developed to meet the Policy objectives.

## II. Policy Context

### **International efforts and global initiatives to combat ML and TF**

10. United Nations Security Council Resolutions have reaffirmed the United Nations call to all states to sign, ratify and implement the relevant international conventions criminalizing terrorism and TF. United Nations General Assembly Resolution 60/288 (2006) also encourages the Member States to implement Financial Action Task Force (FATF) international standards.
11. The FATF is the main international body responsible for developing and setting international standards for anti-money laundering (AML) activities and countering the financing of terrorism (CFT).
12. The FATF issues recommendations that set an international standard for combatting money laundering and the financing of terrorism and proliferation that countries should implement through measures tailored to their particular circumstances. The FATF routinely assesses countries for the effectiveness of the implementation of the recommendations. The FATF recommendations and effectiveness standards – adjusted as necessary for use by an international financial institution (IFI) rather than a country – will be relied upon by IFAD, if applicable, in developing its procedures.

### **Money laundering**

13. At its most general, ML is concealment of the origins of money obtained illegally, typically by passing it through a complex sequence of financial or commercial transactions. ML usually involves three stages: (i) introducing the proceeds of crime into the financial system (placement); (ii) transactions to convert or transfer the funds to other locations or financial institutions (layering); and (iii) reintroducing the funds into the legitimate economy as "clean" money and investing it in various assets or business ventures (reintegration) appearing to have been legally obtained. ML activities can occur in any country but may have a more significant impact on developing countries with relatively small or fragile financial systems or weak economies that are particularly susceptible to disruption from illicit activities. ML activities damage the reputation of financial-sector institutions, may require mitigating measures by IFIs and may scare away foreign investors. This reduces a country's access to both foreign investments and foreign markets. The FATF recommends that ML be criminalized by every country on the basis of article 3(1)(b) and (c) of the Vienna Convention<sup>1</sup> and article 6(1) of the Palermo Convention.<sup>2</sup>

### **Terrorist financing**

14. TF involves the solicitation, collection or provision of funds to support terrorist acts, individual terrorists or terrorist organizations. The funds may come from both legal and illicit sources. Preventing terrorism also involves major challenges. Disconnecting terrorist groups from their sources of financing is one of them. Since 1999, with the adoption of the International Convention for the Suppression of the Financing of Terrorism, there has been a broader-based consensus around the need to interfere with activities related to TF.

## III. Objective

15. The Fund is committed to promoting and adhering to the highest standards of probity and accountability in the use of its financing and will not tolerate the diversion of the resources entrusted to it by Member States, non-member States and other sources through ML and TF. The intent of this Policy is to reduce the risk of the Fund's exposure to serious reputational damage, financial loss or legal liability that could result in a loss of credibility with Member States, international

<sup>1</sup> United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, 1988.

<sup>2</sup> United Nations Convention Against Transnational Organized Crime, 2000.

contributors, donors and other key stakeholders. The objective of the proposed policy is to affirm the Fund's continued commitment to combating ML and TF and strengthening the safeguards and measures in place to ensure the Fund's continued achievement of its objectives.

#### **IV. Scope**

16. This Policy applies to all IFAD-financed and/or IFAD-managed operations and activities and to the following individuals and entities.
  - (i) Individuals and entities holding a commercial contract with the Fund and any of their agents or personnel ("vendors");
  - (ii) Public entities receiving IFAD financing or financing managed by the Fund (e.g., "government recipients") and private entities receiving IFAD financing or financing managed by the Fund ("non-government recipients"), collectively referred to as "recipients"<sup>3</sup>; and
  - (iii) Individuals and entities, other than those referred to above, that receive or apply to receive, provide or may provide transfer or take/influence decisions regarding the use of proceeds from IFAD financing or financing managed by IFAD, including, but not limited to, bidders, investment or potential investment counterparts, issuers or potential issuers of financial instruments.

#### **V. General principles**

17. Like all IFIs,<sup>4</sup> IFAD commits to having and maintaining appropriate AML and CFT procedures and controls to prevent its assets from being used for ML and/or TF.
18. Under the AEI, the Fund has a fiduciary responsibility to "make arrangements to ensure that the proceeds of any financing are used only for the purposes for which the financing was provided."
19. The Fund shall endeavour not to make, fund, support or permit any payment prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations.
20. The Fund therefore has a fiduciary responsibility to protect its assets against potential misuse and ensure that its own financing is not used to enable ML or fund TF. In fulfilling this responsibility, the Fund shall commit to ensuring that its funds and the funds that it administers are not used to support ML and TF; to identify, assess and adequately mitigate the risk related to ML and TF considering the nature, scale and complexity of the Fund activity; and to apply and strengthen existing due diligence processes to prevent and combat ML and TF.
21. As part of the international financing community, IFAD is committed to observing international AML, CFT and Know Your Customer (KYC) best practices and to aligning itself with the FATF recommendations to the greatest extent possible for an IFI.

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<sup>3</sup> The Revised IFAD Policy on Preventing Fraud and Corruption in its Activities and Operations has been amended to strengthen the due diligence obligations of borrowers and grant recipients in relation to downstream partners. In particular, through a "self-certification form", borrowers and grant recipients would be required to include clauses in procurement documents and contracts that would establish an obligation for bidders and contractors to disclose information related to relevant criminal convictions, administrative sanctions and/or temporary suspensions in the course of a procurement process and any time thereafter.

<sup>4</sup> See annex I.

22. This Policy is designed to meet the following integrity principles:
- (i) Leadership, sponsorship and commitment by the Executive Board, President, Vice-President, Associate Vice-Presidents, Directors and Country Directors to promote, encourage and support implementation of this Policy;
  - (ii) Safeguard the Fund's assets and protect the interests of its Member States and borrowers;
  - (iii) Encourage a culture that identifies and mitigates ML and TF risks to support achievement of the Fund's strategic objectives;
  - (iv) Integrate the detection of ML and TF activities into business processes by applying due diligence measures, assessing the risk of ML/TF and implementing procedures to drive effective and accountable decision-making;
  - (v) Implement proper monitoring and internal reporting mechanisms that will assist in the identification of instances of integrity risk and the tracking of remedial actions;
  - (vi) Existence of appropriate competencies and training to discharge responsibilities and provide support for ML and TF management.

## **VI. Governance and responsibilities**

23. Specific roles and responsibilities in implementing the policies in a manner consistent with IFAD's Accountability Framework are:
- (i) The Executive Board is responsible for overseeing proper management of the Fund's integrity risks and for approving this Policy.
  - (ii) The Audit Committee assists the Executive Board in supervising the financial administration and internal oversight of the Fund, which includes ensuring continuous effectiveness of the integrity risk management systems established by the President and Management. The Audit Committee reviews and recommends this Policy to the Executive Board for its approval.
  - (iii) President and Senior Management: The President has overall responsibility, and Senior Management is accountable for the oversight and monitoring of AML and CFT.
  - (iv) The Enterprise Risk Management Committee is responsible for the general oversight of ERM policy and related risk processes, including strategic risks, and coordinating an integrated approach to risk management.
  - (v) The relevant technical Risk Committee is in charge of the Fund's operational risk and compliance governance, which includes the scope of this Policy.
  - (vi) The Office of Audit and Oversight provides reasonable assurance of the Fund's compliance with this Policy, assessing the effectiveness of internal controls that mitigate the risks of ML and TF and validating the robustness of the system in place.
  - (vii) The Ethics Office is responsible for overseeing the ethics and compliance functions related to the Code of Conduct applicable to staff, consultants and other individuals engaged by IFAD under a non-staff contract.
  - (viii) The Accounting and Controller's Division (ACD) is responsible for monitoring the Fund's ML and TF risks by conducting risk assessments, monitoring activities, and advisory work and reporting to Senior Management. ACD is responsible for updating this Policy.
  - (ix) The Office of the General Counsel plays an advisory role with respect to ML and TF and related legal risk matters.

- (x) Other IFAD front-line departments<sup>5</sup> (e.g., Programme Management Department [PMD], Strategy and Knowledge Department, Corporate Services Department, Financial Operations Department [FOD], etc.) have responsibility for compliance with this policy and supporting the enhanced due diligence process to mitigate ML and TF risks.
- (xi) The Treasury Services Division plays a role in ensuring that the disbursement of funds is compliant with IFAD policies and procedures.
- (xii) The Risk Management Unit plays a role in establishing the Capital Adequacy Framework used as the basis for assessing and allocating capital to protect the Fund from financial losses, a process that includes the assessment of operational risk.
- (xiii) IFAD personnel in the various departments and divisions have a responsibility to comply with this policy and support the enhanced due diligence processes to mitigate ML and TF risks.

## VII. Action

- 24. The Fund seeks to strengthen its reputational and fiduciary safeguards, internal procedures, monitoring and assurance mechanisms to ensure that its own financing and the financing that it administers are used for the intended purposes and not subject to ML and TF.
- 25. In order to identify and address specific vulnerabilities that the Fund may still have in this regard, the Executive Board tasks Management with:
  - (i) Reviewing the General Conditions for Agricultural Development Financing, and, if necessary, submitting any amendments to ensure consistency with this Policy to the Executive Board for consideration and approval;
  - (ii) Reviewing the Project Procurement Guidelines, the IFAD Corporate Procurement Guidelines and, if necessary, amending them to ensure consistency with this Policy;
  - (iii) Reviewing the language currently used in financing agreements and, if necessary, reformulating and strengthening the representations and covenants that the Fund typically includes in its legal documentation to focus more specifically on ML and TF to ensure consistency with this Policy. In the case of lending to or through private-sector organization and enterprises, providing language to be used in financing documents or imposing due diligence requirements on these entities. In the case of loans extended to entities responsible for the implementation of projects for onlending, looking at the contractual language to impose a due diligence requirement on these entities;
  - (iv) Developing or amending due diligence procedures to address integrity issues related to ML and TF in IFAD's countries of operation and other related integrity issues consistent with this Policy;
  - (v) Strengthening due diligence practices to safeguard IFAD's funds, including considering the possibility of introducing an enhanced – computerized – ML and TF due diligence system, based on customer identification, checklists and a "red-flag" system. Procedures, systems and tools to further implement these due diligence practices shall be developed;
  - (vi) Facilitating the exercise of due diligence in identifying ML and TF transactions; and

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<sup>5</sup> Divisions having specific roles include the PMD regional divisions, Operational Policy and Results Division, the Administrative Services Division, and FMD.



- (vii) Reviewing relevant frameworks, policies, procedures and guidelines and, if necessary, amending them in consistency with this Policy.

## **VIII. Monitoring and reporting**

- 26. Monitoring will be based on the results of the risk assessment and will assist the relevant operational units in improving procedures and internal controls and provide assurance on how well risks are being managed, including the identification of any new risks.
- 27. Relevant key ML and TF risk indicators will be reported in IFAD's Corporate Risk Dashboard.

## **IX. Training and culture**

- 28. The most effective way of avoiding integrity failures is to instil a culture of high ethical standards.
- 29. IFAD will provide ongoing ML and TF risk-related training to relevant IFAD personnel, with special attention to the business/operational units. The main objective of the training is to improve the understanding, abilities, and analytical capacity of relevant personnel with respect to ML and TF risk and its reputational and other impact on the Fund's operations.
- 30. These training initiatives also serve to enhance and foster a risk culture and capabilities to identify the changing nature of ML and TF activities/risks to enable the Fund to react and respond to them in a timely and appropriate manner.

## **X. Policy effectiveness review**

- 31. A policy effectiveness review will be conducted on a regular basis. FOD/ACD will ensure that all improvements identified and/or changes required are reflected in this Policy. Any relevant changes to this Policy must be reviewed by the Audit Committee and approved by the Executive Board.
- 32. The Policy will be updated, as necessary, to ensure alignment with the revised IFAD Policy on Enterprise Risk Management, which includes internal governance, accountability, risk taxonomy definitions and risk appetite and leading practice.

## Benchmarking<sup>6</sup>: practices of IFIs

Based on the results of the benchmarking, IFAD's policy is significantly aligned in the category of screening and assessment to the following IFIs benchmarked:

<i>Institution</i>	<i>Money laundering and terrorism financing (ML/TF)</i>	<i>Due diligence screening/assessment</i>
Asian Development Bank (AsDB)	Yes	Pre-employment screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Integrity-related (anti-money laundering and know your customer) concerns</b></li> </ul> Customer due diligence according to the non-bank financial institution's customer acceptance policy for: <ul style="list-style-type: none"> <li>- <b>ML/TF risk</b></li> <li>- <b>Criminal/terrorist activities and records</b></li> <li>- <b>Links to corrupt jurisdiction</b></li> </ul>
AfDB	Yes	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Internal corporate procurement issues and operations</b></li> <li>- <b>KYC procedures</b></li> </ul>
EBRD	Yes	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>List of ineligible entities</b></li> <li>- <b>Integrity due diligence and beneficial ownership verification</b></li> <li>- <b>Legal due diligence</b></li> </ul>
EIB	Yes	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Identification and verification of identity of counterparty</b></li> <li>- <b>Identification and verification of identity of beneficial owner(s)</b></li> <li>- <b>Establishment of purpose of business relationship</b></li> </ul>
IDB	Yes	Screening/assessment of clients for: <ul style="list-style-type: none"> <li>- <b>Money laundering and terrorist financing</b></li> </ul>
World Bank	Yes	Screening/assessment due diligence of individuals for: <ul style="list-style-type: none"> <li>- <b>Employment of former public officials</b></li> <li>- <b>Transactions and payments records</b></li> <li>- <b>Sponsorships and charitable donations</b></li> </ul> Screening/assessment due diligence of business partners for: <ul style="list-style-type: none"> <li>- <b>Beneficial owners</b></li> <li>- <b>Other beneficiaries not on record</b></li> </ul>
International Finance Corporation	Yes	Screening/assessment of clients for: <ul style="list-style-type: none"> <li>- <b>Same as World Bank</b></li> </ul>
Asian Infrastructure Investment Bank	No	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Initial project sourcing and identification</b></li> </ul>
Council of Europe Development Bank	Yes	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Serious criminal convictions/investigations</b></li> <li>- <b>Actual ownership of entity</b></li> </ul>
Nordic Investment Bank	Yes	Screening/assessment for: <ul style="list-style-type: none"> <li>- <b>Serious criminal convictions/investigations</b></li> <li>- <b>Actual ownership of entity</b></li> </ul>

<sup>6</sup> Adapted from IFAD's Management of Compliance Risk Paper (authored by the Compliance Task Force established by the IFAD's Executive Management Committee).

## **Response of multilateral development banks to ML and TF**

1. Multilateral development banks are becoming more active in supporting developing countries efforts to prevent ML and TF. They agree on the need for vigorous measures to prevent ML and TF.
2. The World Bank, in particular, has substantially expanded its program in the areas of anticorruption governance, and public financial management. The World Bank's 2001 policy paper on Enhancing Contributions to Combating Money Laundering identified three main ways in which it would contribute to the global efforts to combat financial abuse and ML:
  - (i) Helping countries identify and address structural and institutional weaknesses that may contribute to the lack of market integrity and potential for financial abuses;
  - (ii) Participating in targeted international efforts to combat ML based on its mandate and expertise; and
  - (iii) Ensuring that the World Bank's own financial transactions do not inadvertently undermine international actions to curb illegal practices.
3. The World Bank provides assistance to countries in carrying out financial sector reforms, through financial sector lending and technical assistance activities. Its action plan for AML/CFT includes measures to upgrade and expand staff capacity to respond to client requests for assistance in meeting international AML/CFT standards. It is able to link AML/CFT assistance with country assistance strategies and to offer assistance in building capacity among financial supervisors and other government agencies involved in AML/CFT.
4. In March 2003, the AsDB adopted a policy on Enhancing the Asian Development Bank's Role in Combating Money Laundering and the Financing of Terrorism. The strategy focuses primarily on assisting its developing country members to establish and implement effective legal and institutional systems for AML/CFT, increasing collaboration with other international organizations and intergovernmental and governmental development agencies, strengthening internal controls to safeguard AsDB's funds, and upgrading AsDB staff capacity. It has incorporated AML/CFT into its policy dialogue with Regional Member Countries. In November 2017, AsDB conducted its third review of the implementation of this policy.
5. The EBRD which is mostly active in the private sector and is present in potentially high-risk countries for ML and FT has had to strengthen its own due diligence practices to ensure that its assets were not used for ML and FT or other illegal or fraudulent purposes. The Office of the Chief Compliance Officer (OCCO) was created and new integrity and AML due diligence procedures were set in place. One of OCCO's overall objective is to ensure that the Bank's ethical rules of conduct and internal standards, procedures, and guidelines on AML, CFT, conflicts of interests, prohibited practices, treatment of confidential information, and integrity due diligence are in line with, or reflect, internationally accepted norms.
6. The AfDB has taken some concrete measures in responding to the potential threats of ML. In the context of its institutional support projects, the AfDB has strengthened Auditor-General offices in several African countries to deal with ML.